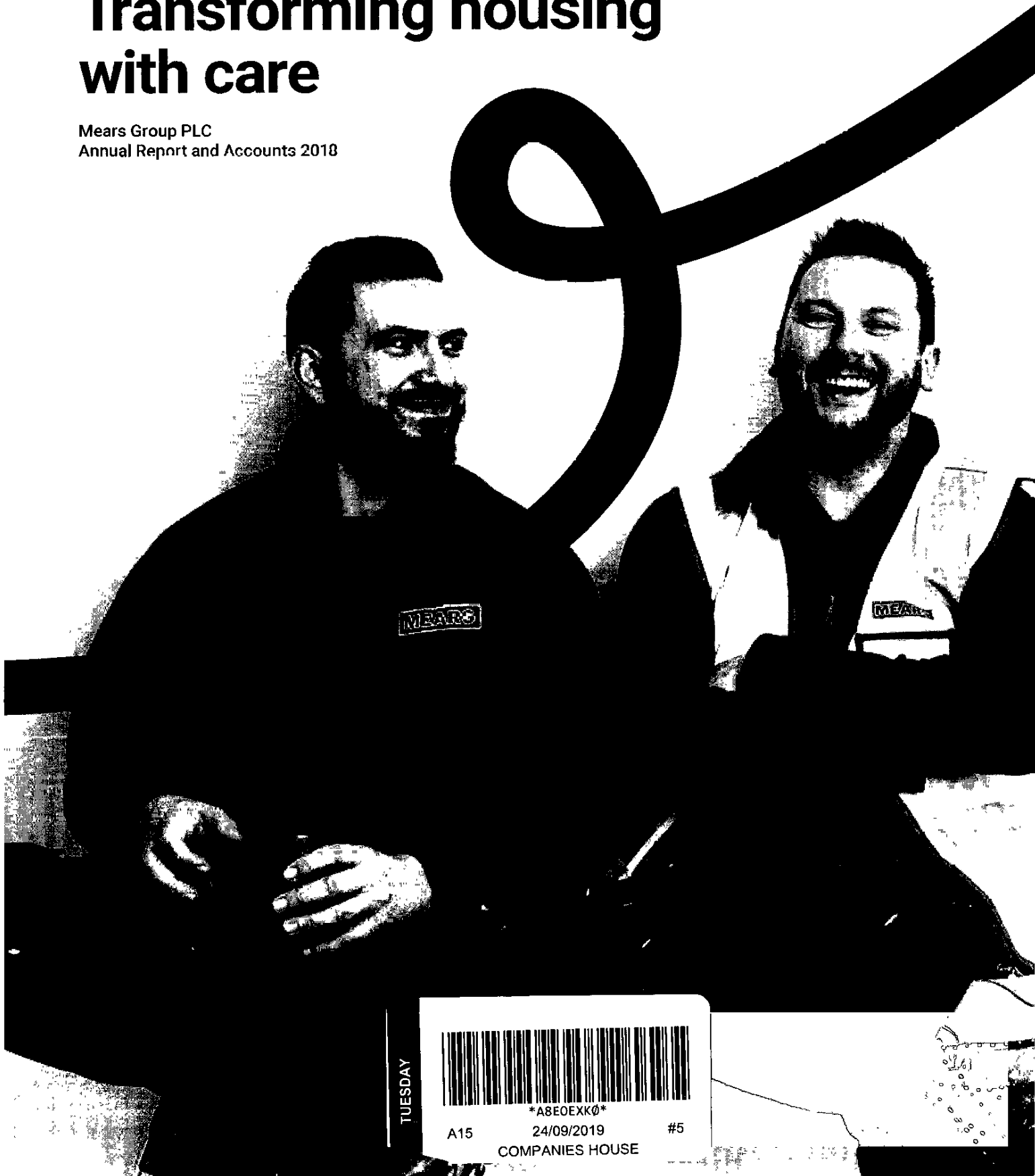




Transforming housing with care

Mears Group PLC
Annual Report and Accounts 2018



TUESDAY



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24/09/2019

COMPANIES HOUSE

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Mears is a leader in the housing and care markets in the UK. Our range of housing services has expanded from maintenance into resident management, creating new affordable homes and running the national Planning Portal. Our domiciliary care services run increasingly in tandem with our housing services, helping create new solutions for the more vulnerable. In 2018, we employed over 11,000 staff.

Our key strengths

Differentiated service delivery

In order for customers to recommend us, we must deliver excellent service. We randomly conduct over 80,000 Housing customer surveys each year.

Strategic relationships

We listen carefully to the needs of our clients and their tenants. As our clients' needs have changed, we have developed a broader service offering which has increased the depth of our client partnerships.

Strong financial management

We operate in a high volume, low value and low margin environment where we have delivered consistent financial results over an extended period of time. This is achieved through works management systems, conservative accounting policies and a culture of giving attention to detail.

Social value

We lead the way with social value in the markets where we operate, delivering meaningful outcomes through positive community engagement projects and effective measurement

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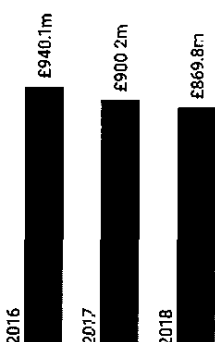
Strategic developments and positive earnings progress

Financial

Group revenue

£869.8m

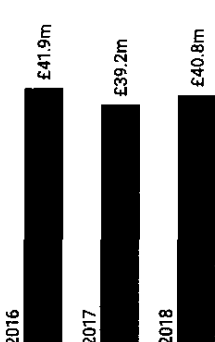
-3.4%



Adjusted Group operating profit

£40.8m

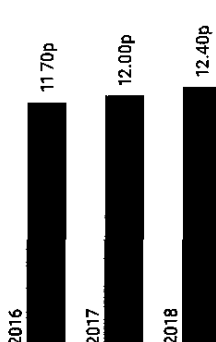
+4.1%



Dividend per share

12.40p

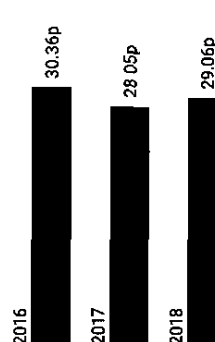
+3.3%



Normalised diluted earnings per share

29.06p

+3.8%



Strategic highlights



Asylum Accommodation and Support Contract win



Continued improvement in profitability and stability in care



Mitie property services Housing acquisition



High levels of customer satisfaction and continued social value leadership



Housing Green Paper post the Grenfell tragedy creates opportunity



Mears well positioned for new Ministry of Defence tender opportunity

Alternative performance measures (APM)

APM	Definition
Adjusted Group operating profit and margin %	Adjusted operating profit and margin is based upon operating profit before the amortisation of acquisition intangibles and exceptional items
Normalised diluted earnings per share (EPS)	Normalised EPS utilises an earnings figure before the amortisation of acquisition intangibles and exceptional items. Earnings are also adjusted to reflect a full tax charge at the headline tax rate. The headline tax adjustment typically reduces EPS but it is felt that this measure better allows for the assessment of operational performance, the analysis of trends over time, the comparison of different businesses and the projection of future performance

We are specialists in providing housing solutions and we understand the needs of our service users, many of whom are vulnerable

Housing...



What we do

Mears has a single minded focus on the housing market and delivering services to the residents of these homes. We operate within the affordable housing sector, which is an area that will see continued investment given the significant housing shortage and the rising number of people who are regarded as statutorily homeless.

Our services

Our core services are in the maintenance and management of homes. Increasingly we operate an intelligent approach to maintenance, using technology and experience to operate preventative maintenance programmes that reduce levels of emergency repairs. As regards management, we collect rent and ensure homes are managed and maintained to a decent standard. Our particular focus is in providing sustainable alternatives to homelessness, helping reduce the rising problems created by the housing shortage in the UK. Through our running of the national Planning Portal, we help enable planning decisions to be made based upon ensuring the right information is available for Councils to make an informed decision.

Our customers

We work predominantly with Central Government and Local Government, in the delivery of housing services. These are through often long-term contracts. We equally recognise that the residents of the homes that we manage and/or maintain, are customers, and we take pride in the high levels of customer satisfaction that we achieve.

...with Care



What we do

Domiciliary care is one of the key services provided to the elderly and disabled residents of social housing properties. The provision of quality housing is recognised as an important driver in lowering the pressures on hospital admissions and social care. While the market has seen under-investment for many years, there are signs that this is starting to change and Mears housing, with care positioning, makes us well positioned for the future.

Our services

We provided regulated personal care services in people's homes, through our teams of care staff. The aim is to help often elderly and frail individuals maintain their dignity and independence. Increasingly we support a growing number of specialist accommodation units, such as extra care facilities, which enable care to be given within a safe and supportive environment. We don't however operate any services within our Care homes.

Our customers

We are commissioned by Local Councils and NHS Trusts to provide domiciliary care services. We only deliver care where we are confident that the charge rates paid are high enough to ensure the quality of service that our customers are right to expect.

Long-term drivers

The shortage of housing in the UK has made investment in housing both a political and an economic priority. More recently, the Social Housing Green Paper and the Grenfell tragedy have put greater focus on tenant engagement and safety. As such, we anticipate rising investment in our markets and a greater attention to the quality of delivery.

Housing revenue



Housing operating profit



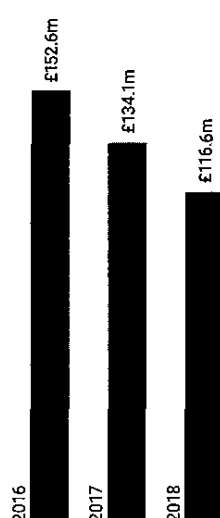
Housing operating margin



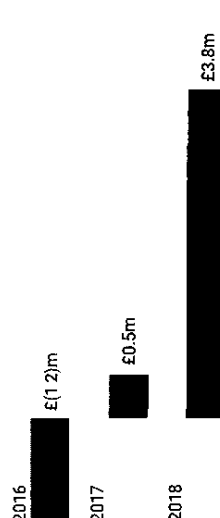
Long-term drivers

Demographic change is the key long-term driver, given the ageing population of the UK. The Government has delayed its decision making on how the rising cost of care will be funded over the long term but has again committed to a Green Paper in 2019.

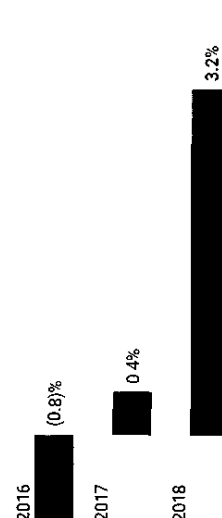
Care revenue




Care operating profit



Care operating margin



 Read more on pages 12–23



6,000

repairs per day across UK



Strategic report

Transforming housing with care

Using our approach to tackle national issues

Asylum housing and support

Our approach to integration of our services was given a boost with the award of three new contracts worth in excess of £1bn under the Asylum Accommodation and Support Services Contract (AASC), delivering estimated revenues of around £100m a year for the next ten years

The contracts are to provide accommodation as well as supporting each service user. Mears has been awarded contracts for Scotland, Northern Ireland and the North East, Yorkshire and the Humber. The contracts are for ten years

The contracts are part of the way in which the UK Government meets its duty to provide asylum for those seeking international protection in the UK. To deliver the contracts, Mears will draw on its outstanding 30-year track record of providing housing, housing maintenance and care services all across the UK, with a strong footprint in Scotland, Northern Ireland, and the North East and Yorkshire

Our commitment

Mears is committed to ensuring that asylum accommodation is safe, habitable and fit for purpose and will meet all contractual and regulatory standards. Moreover, Mears understands the importance of supporting each person whilst living in its accommodation and to ensure that as a company it works with the communities in which it delivers services

During the Mobilisation period, up to 1 April 2019, Mears will work with the Home Office and service users, to make sure that accommodation that is used in the new AASC contract meets the required quality standard. Mears will establish operational teams in each of the areas for which we are responsible so that we are in a position to provide the best possible performance, within the terms of the contract. This will include identifying support needs, managing community cohesion issues, and developing strong partnerships with local authorities and in communities

The Mears approach has been to apply our knowledge of housing management, repairs, and supporting and engaging with our tenants and customers. By extending this approach to asylum housing we have successfully demonstrated that our core model is one which our partners increasingly demand

Congratulations to Mears Employee of the Year 2018 Rob Pearce (shown here), a Multi Skilled Operative from Medway



£2.0m

spent each day by Local
Authorities on temporary
accommodation



9,500

homes in full management
including our Registered
Provider portfolios

Strategic report

Transforming housing with care

Tackling homelessness with Mears

London Borough of Waltham Forest joint venture

Waltham Forest, where more than £3.4m is spent every year on temporary housing, agreed to go into a joint venture with Mears to buy 400 homes to put a roof over the heads of people in housing crisis. Almost 100 households in the borough live in bed and breakfast accommodation, while another 2,326 families are in a form of temporary or hostel accommodation. The scheme will make a real difference to people and follows on from a similar scheme that Mears arranged with Bromley. Mears will manage the housing over a 40-year period.

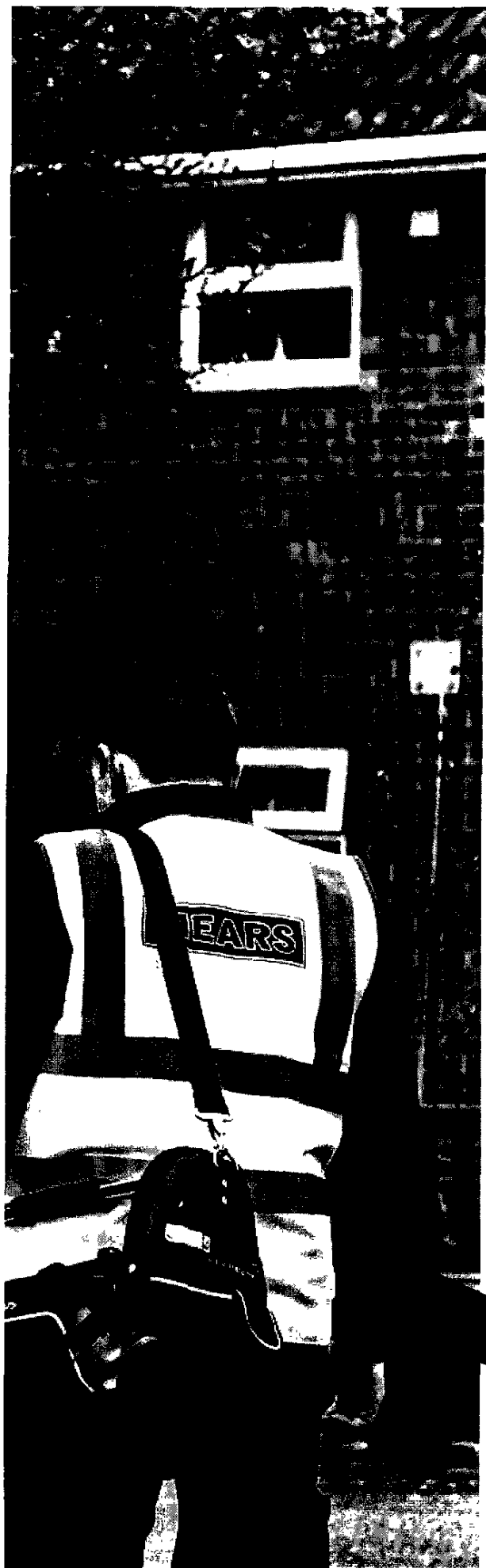
Our aim is to provide Waltham Forest with an alternative, affordable housing supply to replace the significant bed and breakfast accommodation costs currently incurred on homeless local people.

Mears has engaged funding partners to finance the purchase of properties on behalf of our partner, and we carry out refurbishment works and act as managing agent for the portfolio.

Nature of service

- ~ We utilise a Privately Placed Bond to purchase and refurbish 365 homes
- ~ We house homeless families who would otherwise be living in bed and breakfast or expensive temporary accommodation
- ~ We manage the acquisition and improvement works
- ~ Through our Registered Provider, we will also manage and maintain the homes

By working with our partners, Mears is innovating to provide answers to some of our most deep-seated policy issues, which is why we have become the largest supplier of temporary accommodation in the UK.





£62m

Riverside contract
valuation



Mears provides a full
management service for
this insured solution

Strategic report

Transforming housing with care

Building on our relationships to deliver repairs solutions

Riverside repairs

In 2018 Mears won a £62m contract to deliver repairs and maintenance services to Riverside Housing Association. The ten-year contract, with an overall budget of £115m, is for responsive repairs, voids, planned works and providing a domestic gas service. It covers over 10,000 homes in the Central and South regions, including London, East Anglia, Kent, Leicester, Bristol and the M4 corridor.

Before winning the contract Mears provided a maintenance service to Riverside. This played a very important part in ensuring that Riverside saw us as their potential partner for this long-term contract.

What we do

We provide a wide range of services, including

- ~ reactive repairs and maintenance,
- ~ planned works, repairs and maintenance (under the Property MOT programme),
- ~ gas servicing and installation, and
- ~ 24-hour out of hours service.

Our relationships with our partners goes to the core of everything we do. By working closely with clients and understanding their needs Mears has shown it can grow business and strengthen our partnerships.



The Riverside Partnership demonstrates how Mears can support clients, even when there is a preference for insourcing.

We welcome our new Chairman, Kieran Murphy



Kieran Murphy
Chairman

I am delighted to deliver my first Chairman's Statement, having joined the Board at the start of the year. In my short time in the Group, I have taken the opportunity where possible to meet a broad cross section of colleagues, to better understand the culture and values that underpin the Group's success.

Overview

I am delighted to deliver my first Chairman's Statement, having joined the Board on 2 January 2019. Whilst I am only in my third month at Mears, it has been an exciting early period. It was tremendous to see the Group awarded three new long-term contracts by the Home Office to provide accommodation and support for asylum seekers. The contracts are estimated to deliver revenues in excess of £1 billion over their 10 year term. Their scale reflects the progress that Mears has made over a number of years in transforming itself from a small-ticket maintenance contractor towards being a specialist provider of housing-related services to the public sector. Winning and, more importantly, delivering this contract to the standards that Mears sets itself required, and will continue to require, high quality dedicated effort from teams across the Group. I look forward to seeing this dedication resulting in effective delivery.

Another highlight of the past 12 months was the acquisition of certain business assets and contracts from Mitie's property services division ('MPS'). The period since completion has progressed to plan, and the respective senior teams are combining well. The system migrations, which underpin the synergies and improvements to service delivery, are underway. Moreover, it was pleasing that MPS was successful in securing a contract with Home Group within a short time following the acquisition. This contract, valued at £200m over a 10 year term, will see the Group deliver maintenance and planned works to 10,000 homes in the South East. We expect MPS to continue to win new business opportunities as the months unfold.

During the course of the past few weeks, I have held a series of individual meetings with shareholders who between them represent over two-thirds of the Company's equity base by value. I am grateful to each of them for taking the time to meet with me, for their welcome and for the views that they expressed. It was encouraging to hear a number of very positive messages about the Group's core business and the enthusiasm for its continued success. However, the performance of the Company's share price over the past six months has been a source of understandable disappointment. It is also clear that shareholders, and the market collectively, are taking a much more cautious view about indebtedness, again understandably in the light of events elsewhere in the sector. It is appropriate that the Company should take account of this in its plans for the current year and into 2020. Accordingly, the Board will work with management to take a number of active steps to reduce debt progressively over this period.

£869.8m

Group revenue

£40.8m

operating profit
before amortisation
of acquisition
intangibles and
exceptional items

Results

Group revenue for the year ended 31 December 2018 was £869.8m, a small reduction on the previous year (2017: £900.2m). However, operating profit before amortisation of acquisition intangibles, exceptional costs and long-term incentives items rose to £40.8m (2017: £39.2m). Operating margins similarly increased to 4.7% (2017: 4.3%). Normalised diluted earnings per share increased to 29.06p (2017: 28.05p), an increase of 3.6%. The average net debt for the year was narrowly behind our target of £110m at £113.2m.

Dividend

The Board remains confident in the Group's long term potential and in its progressive dividend policy. The Board is therefore recommending a final dividend of 8.85p per share, having paid an interim dividend of 3.55p per share in November 2018, giving 12.40p per share for the year as a whole. This represents a 3.3% increase over the total of 12.00p per share paid in respect of 2017. The final dividend will be payable, subject to shareholder approval, on 4 July 2019 to shareholders on the register on 14 June 2019.

Board developments

In July 2018, as part of the continuing evolution of the Board, the then Chairman, Bob Holt, indicated his intention not to stand for re-election at the 2019 Annual General Meeting. The Board undertook a competitive and structured process for the recruitment of the new Chairman and I was delighted to be offered the position in December 2018. I should place on record the thanks of the entire Group to Bob Holt for his 23 years of service, which was instrumental in taking the Group on its journey from a small privately owned business with annual turnover of £12m, through flotation on AIM and from there to the Main Market, leading to the national player and market leader that it is today.

In June 2018, the Company became one of the first listed companies in the UK to appoint an Employee Director, Amanda Hillerby, underlining the Company's commitment to progressive corporate governance. Mears understands the vital role that our workforce plays in the success of the Group. We intend that this role will help the Board to receive full, open and honest insight and views from its workforce on how strategic initiatives are being implemented. It should also help to provide the wider workforce with a better understanding of how the Board operates. We will keep under review how best to use Amanda's skills to further these objectives.

It is essential to ensure that Mears, in common with all listed companies, is equipped with a Board that can provide a wide range of views, skills and experience to work with and challenge the management team to further the effective development of the Group. I will keep under review the balance of capabilities around the Board table so as to ensure that the Group has what it needs for effective leadership.

Our people

In my short time with the Group, I have taken the opportunity where possible to meet a broad cross section of colleagues to better understand the culture and values that underpin the Group's success. I will continue to undertake a programme of visits throughout the business during the course of the coming year. I attended the Group's annual conference in February 2019, which acknowledges and celebrates those members of staff who have delivered exceptional levels of service to our customers. I have been impressed by the professionalism and commitment of our employees and I thank them for their dedication and hard work.

I was pleased that Mears was recognised recently by the Sunday Times annual survey as one of the best 25 big companies to work for in the UK in 2019. While this reflects well on our investment in culture and people, it speaks volumes about the people who work for us. It was also pleasing that the Group achieved a very high rating from FTSE4Good, which assesses listed company policies and procedures on their social and environmental impact and governance.

Summary

I am very much at the start of my journey at Mears. I sense the strong commitment throughout the Group to do the best for all our stakeholders, be they our shareholders, our public sector customers or our clients who receive our services day in and day out. That commitment to excellence will serve the Group well in the years to come and I look forward to being a part of the team that will continue to deliver it.

We have remained highly focused on a single area, providing services to tenants in and around their homes



David Miles
Chief Executive Officer

“

The Board is clear that it must take action to refocus the Group's main activities to those of a specialist housing provider, with maintenance and management being fundamental to this. Those Group activities that are peripheral to this core activity, especially where they absorb working capital, will be reviewed in terms of how we can deliver the best financial return for shareholders.

Our transformation time-line

The affordable housing market has seen significant change and Mears has adapted its service capability well to this changing market



2010 Traditional contracting Operations:
Maintenance
Regeneration



Mears secures Registered Provider status

2014

Acquisition of Omega – temporary housing expertise

£1.3bn

Orders secured

93%

Excellence rating

Introduction

I am pleased at the progress made by the business in 2018, although the year has not been without its challenges. I am naturally disappointed at our share price performance and this dissatisfaction is mirrored by a number of our major shareholders.

Mears has made significant progress over recent years in evolving its business. My focus has been on a range of stakeholders including clients, service users, employees, communities and shareholders. I believe that much of the Board's strategy has delivered successful outcomes, although the full financial benefits in certain areas have taken longer to come through. The success of our investment into Housing Management is evidenced through the Key Worker and AASC bidding successes while our investment in Housing Development is demonstrated by our success at Milton Keynes. The success of our joint venture in the Planning Portal highlights the investment made in Planning Solutions. Even our investment in Care, which from a return on investment perspective has been very disappointing, played a significant part in securing the recent AASC contract. Finally, it is also pleasing that much of our strategic progress has delivered good outcomes in terms of social value, client confidence and Mears' reputation.

The negativity surrounding outsourcing has been unhelpful, especially when so many of the issues have been specific to other companies in the sector. Unlike other providers in the sector, Mears has remained highly focused on a single area, providing services to tenants in and around their homes. We are specialists in providing housing solutions and we understand the needs of our service users, many of whom are vulnerable.

Notwithstanding the above, the Board is mindful of its responsibilities to shareholders. We recognise shareholders are seeking better financial outcomes, particularly in respect of cash generation, and the Board is clear that it must take action to refocus the Group's main activities to those of a specialist Housing provider with maintenance and management being fundamental to this. Those Group activities that are peripheral to this core activity, especially

where they absorb working capital, will be reviewed in terms of how we can deliver the best financial return for shareholders including cessation, downscaling or disposal if appropriate. Investor appetite for gearing has gone full circle. We must now direct our capital resources to those areas which deliver the best financial returns, whilst always ensuring that we do not lose our long-term approach to how we run the business. Going forward, we will review how Mears can best contribute to the housing development needs of our customers but in ways which do not place undue strain on the Group balance sheet. This is covered in further detail later in this review.

Notable highlights for 2018 include

- ~ Our success in securing three regions under the AASC was a significant achievement for the Group. With a contract value estimated at £1 billion over a ten year term, this is the largest contract ever awarded to Mears and exemplifies the significant progress made by the Group since extending our services into Housing Management in 2014.
- ~ The acquisition of certain business assets and contracts of the property services division of Mitie ('MPS') followed a long period of negotiation and due diligence. Since completion, the integration of MPS has gone according to plan.
- ~ Once again, Mears has delivered high levels of customer service with our customer service excellence rating increasing to 93%. Our dedication to deliver a first class service to our clients is central to our culture and underpins our success.
- ~ The Group restructured its central support structures to reflect the changing nature of the business and differing support requirements. The Group delivered the planned annual savings of approximately £5m with a low disturbance to day-to-day performance.
- ~ The Group has positioned itself well in the MoD bidding opportunities. The MoD is a key client of the Group and the new tender provides Mears the opportunity to deliver management and maintenance services to improve the quality of housing for the UK's Armed Forces and their families.

2015

Joint venture with Ministry of Housing, Communities & Local Government to deliver national Planning Portal



Building relationships with funding partners

**2020 Placemaking
Housing Management:**

Income management
Tenancy management
Allocations

Operations:

Maintenance
Regeneration

Asset Management:

Immediate solutions
Acquisition
Development

£870m

Group revenues

4%

EPS growth

There will always be areas where the Group can improve

- ~ The Housing Maintenance division's new contract win rate has, for the second year running, been below our historical norm. We are confident that there has been no lack of good quality opportunities to bid, the quality of our tender submissions has been high and we continue to demonstrate our value for money proposition. Interestingly some lost opportunities are now representing themselves to us.
- ~ We chose to exit a small number of maintenance contracts, with an annual value approaching £30m, as the balance between risk and reward was not considered favourable to the Group.
- ~ The operational performance in some parts of our Housing Management business was below par owing to the AASC tender requiring considerable resource together with the significant emphasis that the business has placed on enhancing the internal controls and governance required in a fast growing regulated business. While this resulted in some loss of focus in the existing business, this was an important priority and is now behind us.
- ~ Our Housing development activities experienced a challenging final quarter to the year, with a slowdown in sales impacting upon both revenues and working capital.

Financial performance

The Group reported revenues for the year of £869.8m, a reduction of 3% on 2017. However, encouragingly, taking half year by half year, this shows revenues have stabilised since the sharp reduction in the second half of 2017.

The profit for the year before tax, exceptional costs and amortisation of acquisition intangibles of £38.5m (2017: £37.1m) was a small improvement and saw a solid increase in operating margins to 4.4% (2017: 4.1%). Normalised diluted earnings per share of 29.06p (2017: 28.05p) reflected this increase in profits, increasing by 4%.

As reported previously, the Group has carried out a review of its central support structures to ensure they reflect the changing nature of the business and that they are efficient and deliver value. This was particularly relevant given the changing sales mix that brings a differing support requirement. The review identified annualised savings of approximately £5.0m and these have been secured in the year. The Group will continue to keep on top of its central support costs. The Group has a long-term target to maintain central overheads at around 3.0% of revenue. While this may appear a high percentage, the Board views this strong centralisation principle as being crucial to deliver consistency and better control across the Group. Over recent years, the central overhead percentage has edged towards 4.0%, however the additional revenues secured with the MPS acquisition and the AASC contract will lower this level and it is a key Group target to reduce central overheads back to 3.0% and to then maintain them at that level. The Group is also carrying out a review of its regional support functions, a process which is being aligned with the MPS integration.

The Board recognises that the Group's net debt and operating cash performance need to improve. The broader activities delivered by the Group carry significantly different working capital requirements, and a single EBITDA to operating cash conversion measure, which for many years the Group delivered a measure at close to 100%, does not provide an accurate reflection of the Group's cash performance. The Group has consistently reported an average daily net debt, rather than focusing on the balance on a single day at the period end, and further detail is included in the Finance Review. In addition, below we provide analysis in respect of the working capital absorbed against the different Group activities which demonstrates a solid performance other than in Development.

Average daily net debt for the year, excluding the property acquisition facility, was £113.2m, narrowly behind the target set at the start of the year of £110.0m. The level of average debt was broadly comparable to that in 2017 (£96.4m) when allowing for the timing of the cash out flows late in that year of £8.2m relating to discontinued activities and a deferred consideration payment of £11.1m in early 2018.

Acquisition of certain business assets and contracts from the property services division of Mitie

In November 2018, Mears completed the acquisition of certain business assets and contracts from the property maintenance business of Mitie, the acquired business is branded as MPS Housing. The initial consideration was £22.5m together with contingent consideration payable, up to a cap of £12.5m, based upon the future profitability of the business over a 24 month period following completion. The initial consideration was funded through a placing of c. 6.8m new ordinary shares.

The business comprising 14 branches, circa 30 customer relationships and approaching 1,000 employees, is expected to contribute annualised revenue in excess of £100.0m during the current financial year. Mears has a strong track record for driving improvements in previous acquisitions as evidenced by the successful turnaround of the Morrison business following its acquisition in 2012. The MPS business has strong similarities to that business, and Mears is approaching this transformation plan in a similar way.

Whilst it is still only a short period since completion, the Board is encouraged by the progress made. The reaction from MPS customers has been positive and the MPS team have welcomed the change. We are still at a relatively early stage in the integration process, with the key driver being the migration of MPS' three operating systems onto the single Mears Contract Management platform.



Q

A number of companies involved in outsourcing have got into difficulties, with Carillion being a stand out example. What makes Mears different?

A

We are different. We focus solely on housing and housing related care and as such we have a great deal of understanding of risk and sustainable operational management. We are very selective in terms of what we bid and the partnerships that we forge. We manage our cash well and have systems that enable us to manage our cost base effectively at a very detailed level. We take a responsible and transparent approach to governance, which is very important when working with the public sector.

Q

What issues has Brexit created for Mears?

A

Our revenue is all within the UK and to this point the issues we have faced largely relate to some delays in Government decision making and policy development. The long-delayed policy document around the future funding model for social care is a prime example of this. The key thing for us is our workforce and to maintain our focus on making Mears the best place to work in the sector. We are already a long way down this path and this remains a priority for us.

Q

Mears puts Placemaking at the heart of its strategy. What does this mean?

A

High quality, well-managed housing is in our view the most important aspect of any thriving community. We see ourselves as leaders in contributing across the spectrum of planning, building, managing and maintaining high quality but affordable housing solutions. Our Care services work in tandem where needed to support people who are often elderly or disabled. Our combined approach really starts with thinking about the locations in which we operate and how we can use our services to help make better places to live, in conjunction with our partners.

Q

Safety and compliance have become higher profile since the events of Grenfell Tower tragedy. How has Mears responded to this?

A

We are proud of our track record on health and safety. We have reduced Accidents Rates by over 10% and achieved the RoSPA Highly Commended Industry Sector Award (16 consecutive Golds), for our continued commitment to accident and ill-health prevention. Over the year we have carried out over 50,000 hours of health and safety training to ensure we continue our commitment to improving the skills and awareness of all employees.

As well as our own continued focus on ensuring our staff and customers are protected, we have been working with our clients in support of tightening regulatory requirements around housing and helping implement improvements needed, starting with work on high rise properties. We are pleased to see standards being raised here and as the recent Social Housing Green Paper becomes a White paper, we expect further positive developments in this space.

Q

Mears' reputation as a great place to work, seems to be increasing. Why is this and why does Mears regard this as important?

A

We are obviously pleased to be recognised by the Sunday Times as one of the 25 Best Big Companies to Work For in the UK. Also, we hold the Housing Diversity Network accreditation for Excellence in Diversity. These are ultimately just some of the awards that we have won for 25 years of effort in making Mears a place where people want to work and where there is opportunity for personal development. We have championed encouraging more women to work in the trades and to secure better terms and conditions for care staff. We do this because a great workforce is the central building block for everything we do. We recognise that we have to be better than ever today, if we are to continue to perform well in terms of workforce, and we will continue to invest in our people.

Q

The recently won Home Office contract represents a significant development for Mears. Do you see other opportunities of this type and scale in the future?

A

We do see further opportunities with centrally led housing contracts, especially in housing solutions to support service personnel. We also see significant housing opportunity in specialist housing to support demographic change, and indeed 2018 saw us completing our first build and manage properties for the elderly and for younger people with physical and mental support needs.

£753m

Housing revenues

5.0%

Housing margin

Housing

	2018			2017		
	H1	H2	FY	H1	H2	FY
Revenue £m	374.9	378.3	753.2	402.1	364.0	766.1
Operating profit £m	19.0	18.6	37.6	20.8	18.7	39.5
Operating profit margin %	5.1%	4.9%	5.0%	5.2%	5.1%	5.2%

The Housing division reported revenues of £753.2m, a slight reduction against the previous year. Encouragingly the half year on half year progress shows revenues increasing following the sharp reduction in the second half of 2017. As expected, it was a quiet period for new contract mobilisations, following the slow period of new bidding success in 2017. The recently acquired business of MPS contributed revenues of £9.0m in the one month that it was part of the Group.

The division generated an operating margin of 5.0%, with the second half margin (4.9%) reflecting both the initial impact of MPS together with costs expended in respect of the AASC bidding and mobilisation.

The Housing division comprises three core activities: Maintenance, Management and Development. Increasingly there have been opportunities to deliver a combination of these services which we term as 'placemaking'. It is critical to the Group's success that Housing is operated and managed as a single division, with the different specialisms combining to deliver the optimal outcome. However, in broadening our Housing activities, it has become harder to explain the underlying performance, and, importantly, provide stakeholders with a better understanding of the growth expectations and risks attached to each area and, particularly in the current environment, the related working capital requirements.

It must be recognised that, increasingly, opportunities are being secured that require a full asset management service that does not slot easily into a single category. Rather than artificially allocating revenues and profit across each category, all revenues and profit are assigned to the predominant category. Given that the Housing Management activities incorporate an element of maintenance, whilst the maintenance growth in isolation may appear low, at times this will simply reflect a change in allocation more than a change in activity.

The revenue for the full year was slightly lower than our expectations at the start of the year of a firm and probable revenue of £770m. In maintenance, some revenues expected to be delivered in 2018 were re-phased and will be delivered into 2019 in agreement with our partners, Milton Keynes being the most significant example. Our development activities experienced a challenging last quarter – whilst the primary focus has been working in partnership with Housing Associations, and the development of affordable homes, this activity does incorporate an element of private sales, which most Housing Associations require to make the overall scheme viable. The Development business experienced a significant slowdown in private sales in the lead-in to the year end, negatively impacting on both revenues and working capital.

Historically the Group has pursued a strategy focusing on earnings growth whilst keeping within the strict confines of Housing. Whilst good working capital management has been a cornerstone of the Group, equally cash has not been allowed to constrain the Group's evolution. However, as the Group's Housing business has evolved, it should be recognised that the different activities within Housing have significantly different working capital requirements.

~ Maintenance (representing 77% of divisional revenue in 2018) is a high volume and low value activity. Given the requirement to measure, review, inspect and value a large number of works orders, the invoicing cycle cannot be rushed or short cuts taken. Accordingly, it is not unusual for a period of 90 days between completion of work and receipt of income although the average is closer to 70 days. On the positive, the measurement of revenues is very secure and there is minimal bad debt risk. The cost base includes specialist subcontractors and merchant suppliers with varying payment terms averaging 40 days. As a result, typically around 30 days' work is absorbed in working capital.

£117m

Care revenues

3.2%

Care margin

	2018			2017		
	Revenue £m	Operating profit £m	Margin %	Revenue £m	Operating profit £m	Margin %
Maintenance	578.7	28.0	4.8%	606.2	32.6	5.4%
Management	135.4	8.5	6.3%	133.8	5.7	4.3%
Development	39.1	1.1	2.8%	26.1	1.2	4.6%
Total	753.2	37.6	5.0%	766.1	39.5	5.2%

- ~ Management (representing 18% of divisional revenue in 2018) is lower volume with the most significant transactions being linked to collecting and paying property rentals. Typically both rental receipts and payments are paid monthly in arrears such that the business operates on a low working capital requirement.
- ~ Development (representing 5% of divisional revenue in 2018) is based on low volume but high value transactions. Where developments are being built under

a simple contracting relationship, work can be invoiced during the course of construction although typically as projects approach their conclusion, the receipts become slower. Some mixed tenure developments include units that are subject to private sale and Mears funds the build cost of those units until their sale. The direct works are entirely subcontracted, being paid in around 30 days from invoicing and as a result, this area of our Housing activities can absorb high levels of working capital.

The working capital allocation and returns of each activity are set out below

	Operating profit £m	12-month average working capital £m	Return on working capital employed*
Maintenance	28.0	19.0	>100%
Management	8.5	1.7	>100%
Development	1.1	15.6	7%

*Trade receivables less trade payables

Looking ahead into 2019, there will be a change of priorities for Mears. We will refocus our capital allocation on those areas which deliver the best returns whilst being mindful of the strategic impact such changes may have upon the Group's future opportunities. The relatively modest working capital requirements of our core maintenance and management activities, combined with their attractive returns on capital, indicate that these are two core areas where the Group should focus its attention.

The property acquisition facility of £30m was introduced in 2017 to enable the Group to acquire and build portfolios of properties prior to disposal to a long term funding partner. This provided the Group with an ability to accelerate the flow of properties into its Housing Management operations together with an additional profit opportunity at the point of transfer. The funding requirement is high, relative to our resources, and the flow of profits irregular. Whilst the property acquisition facility has been useful, its cancellation over the course of 2019 will have a low strategic impact.

The Group has broadened its service capability in recent years to include the provision of Housing Development, primarily targeting existing clients, as part of the holistic service offering to them. However, the working capital absorbed in this area has been higher than expected, and whilst the financial returns could be considerably higher than their current levels, the working capital currently allocated to this area could be better deployed elsewhere or used to reduce current net debt levels. The Board will keep this area under close review going forwards. The current pipeline of works will unwind over the coming three years although the Group will endeavour to accelerate that process, especially for those contracts which have the highest working capital intensity. The reasons for offering a development capability were compelling and remain so. The Group will continue to explore ways in which it can contribute to its clients' housing development needs, but in a way which creates value for both parties without significant working capital consequences for Mears.

Strategic report
Chief Executive Officer's review continued

84%

Care regulatory compliance

221

Care apprenticeships

Care

	2018			2017		
	H1	H2	FY	H1	H2	FY
Revenue £m	60.3	56.3	116.6	68.7	65.4	134.1
Operating profit £m	1.9	1.9	3.8	(1.0)	1.5	0.5
Operating profit margin %	3.2%	3.4%	3.2%	(1.5%)	2.3%	0.4%

The performance of the Care division over the last 18 months has been pleasing with a return to profitability and margin improvement in line with the challenging target set by the Board. Management remains highly selective in bidding for any new work and regularly revisits its existing activities, focusing on delivering good quality care at a sustainable margin rather than placing emphasis upon top-line growth. In that regard, revenues reduced to £116.6m (2017: £134.1m) while operating margins increased to 3.2% (2017: 0.4%), marginally ahead of expectation.

The Care division secured charge rate increases which broadly allowed us to match the increasing cost base driven

by an increase in the National Living Wage and increase in the pension auto-enrolment contribution rate. The main challenge in Care remains the sourcing and retention of sufficient care workers of good quality and this is an area that continues to receive significant attention. It is achieving success in this area of operations which underpins the Group's target of a 5.0% margin in Care.

The Group is increasingly directing its Care bidding activity towards those clients where there are likely to be opportunities to provide a complete Housing service and, consequently, there is less focus on those opportunities which provide care services in isolation.

In line with the working capital and returns analysis provided in Housing, the Care division delivers a good return on working capital employed as set out below:

	Operating profit £m	12-month average working capital £m	Return on working capital employed*
Care	3.8	13.6	28%

*Trade receivables less trade payables

Contract awards

Mears continues to see existing and target clients demanding a broader Housing offering. The Group is operating very well and our excellent service delivery is putting Mears in a good position to secure new business opportunities, notwithstanding the discussion above as to Group strategy and capital allocation going forward.

Mears was delighted to secure its primary bidding target for 2018, the AASC, being awarded three regions with an estimated contract value of £100m per year over a ten year period. Mears could never previously have been in a position to bid such a large and complex contract and it reflects the significant strategic and operational progress that the Group has made over recent years in extending and developing its capabilities. It also reflects a change in Central Government attitude, with a realisation that such contracts require providers who are specialist at providing Housing services together with a capability for dealing with vulnerable people. The tender itself was very intensive in terms of the time and resource required and at times was a distraction from the day to day business, however we are delighted at the positive result. The new contract will require a similar level of intensive support from across the Group through its mobilisation period, with the soft-start in April 2019 and a full go-live due in September 2019.

The year was also busy in terms of new Housing maintenance contracts with the Group bidding in the region of £1 billion of new opportunities. It was disappointing that our new contract win rate in this area was low with a contract win rate on competitively tendered works of 15%. The Group missed out on a number of key maintenance contract targets, typically scoring well on quality but missing out on price. Whilst this win rate is disappointing, the Group has a long track record of taking a disciplined approach to bidding and will never be tempted to secure work at a price which is sub-optimal. Interestingly a few of those lost opportunities are now representing themselves to us as a result of service levels not being met by the winning parties.

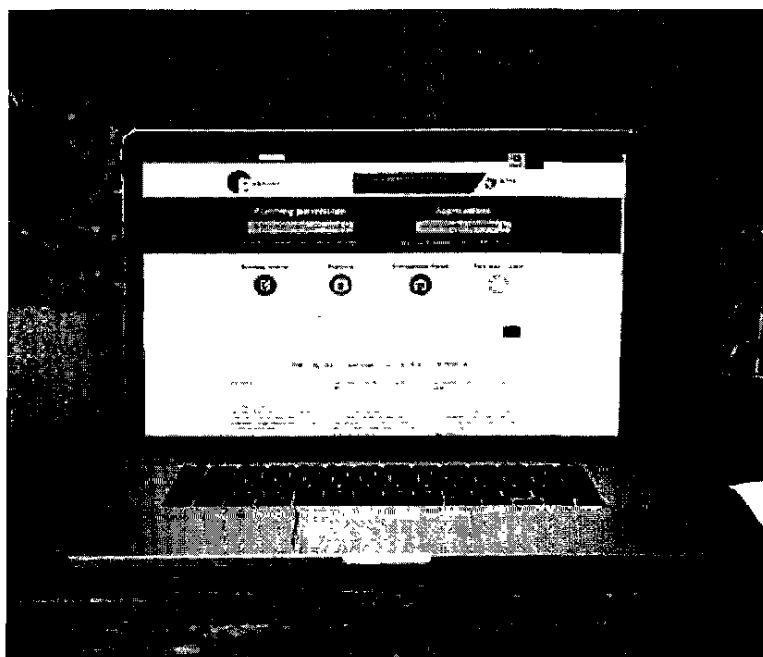
Other notable new contract awards in 2018 include:

- ~ A contract to deliver repairs and maintenance services to Riverside Housing Association for an initial period of five years, valued at £62m. There is an option to extend the contract for a further five years, taking the total opportunity to £125m. The contract covers over 11,500 homes across the Midlands, East Anglia and the South of England. The service requires Mears to work alongside Riverside's own in-house maintenance provider and commenced in July 2018.
- ~ A contract with Octavia Housing valued at £75m over 10 years, will see our existing contract with Octavia double in size. Mears will now be delivering planned works in addition to response and void maintenance services.

- ~ Since the year end, and not reflected within the 15% contract win rate, a contract with Home Group, to deliver maintenance and planned works to 10,000 homes in the South East. The contract, which commences in April 2019, is valued at £200m over a 10 year term. In addition, a contract with London Borough of Hammersmith and Fulham to deliver response and void maintenance services. The contract has been awarded for a twelve month period and is valued at £6m. Whilst unusual for the Group to tender for a contract with such a short duration, the Group sees this as a key client relationship and is delighted to have secured this engagement.

The increasingly innovative nature of our Housing Management solutions means that work can often be secured without the requirement for an extended, competitive and expensive tender process. These opportunities are not valued in the Group's pipeline or in the contract win rate but are increasingly material to the Group. New orders secured during the year through this negotiated route include:

- ~ A partnership with the London Borough of Waltham Forest (LBWF) to arrange the purchase and refurbishment on their behalf of 365 homes currently under private ownership. The key aim is to provide LBWF with an alternative, affordable housing supply to reduce the significant bed and breakfast accommodation cost currently being incurred. Mears has engaged funding partners to finance the purchase of properties on behalf of the client, while it will carry out refurbishment works and act as managing agent for the portfolio. The contract will be operated by LBWF and Mears for 40 years and the arrangement is valued at circa £75m. Whilst the contract did not go live until August 2018, the property acquisition facility enabled the Group to start purchasing properties in March 2018 and by the year end, the Group was ahead of schedule having completed the purchase of 65 properties with a strong acquisition pipeline.
- ~ A partnership with CBRE Global Investors and 'Step Forward', a property company established by former service personnel who are seeking to provide affordable homes for ex-service personnel and enable Local Authorities to meet their duty under the Armed Forces Covenant. The proposal is that, under a nomination agreement, a Local Authority agrees that for each s106 affordable housing unit, priority will be given to former and current service people. CBRE has created an investment fund of around £250m and anticipate acquiring 2,000 properties over the next two years to place into this arrangement. Mears, through its Registered Provider, manages the housing, assuming responsibility for rent collection, occupancy and asset management over a 22 year period, whilst ensuring that the conditions of the s106 planning consent are met. Based on property numbers of 2,000 this would equate to revenues of in excess of £100m over the contract term.



Case study: Planning Portal

Innovating to help our public sector partners

The national Planning Portal is run by Mears Group subsidiary, Terraquest. The Planning Portal has helped to transform the planning process, making information and services simpler and more accessible for those involved in the process, be they applicants, agents or Local Authorities.

In 2018, we made a number of significant service improvements, for which we now make a small charge to each application.

By working in partnership with every Local Authority across England and Wales and focusing on delivering a quality service to our customers, we will continue to be the national home of planning and building regulations information and the national planning application service.



The National Planning Portal, run by Mears, processes the vast majority of planning applications in England and Wales. We work to make planning faster and more efficient.



Case study: Balmoral Place

Building places where Care and Housing work together

We have built on our work to integrate housing and care contracts, at the front line delivery of service but also in the creation of new specialist accommodation, such as supported living housing and extra care property.

Mears combines its skills to build, manage, maintain and provide care to specially adapted homes for elderly and disabled people to help them live independently.

These schemes are not new, but there is renewed interest as Local Authorities look for innovative ways to look after vulnerable people and increase their health and wellbeing. Our extra care scheme – Balmoral Place, opened in 2018, with more opportunities in the pipeline.

Balmoral Place is an extra care housing scheme offering an affordable, positive lifestyle choice for older people in Northampton. The scheme provides a safe, secure and vibrant community for those over 55, who want to live independently with personalised care designed for their needs.

Mears Housing Management is responsible for the day-to-day running and maintenance of the scheme. Mears Care is on site seven days a week to provide a care and support service to our customers. Balmoral Place has an on-site manager, care team and 24-hour emergency alarm response service.

Order book

The order book stands at £3.2bn (2017: £2.6bn). The order book increases as the Group secures new work and reduces as works are delivered. The increase of £600m reflects new orders secured of £1.3bn together with the order book of £200m acquired on the acquisition of MPS before deducting revenues delivered during 2018.

Bid pipeline and contract expiries

Following conclusion on the AAST tender, our bid team have moved their focus towards the Group's other major bidding opportunity with the Ministry of Defence (MoD). The provision of quality, affordable housing for the Armed Forces and their families is integral to the Armed Forces Covenant. With the current contract due for renewal and the procurement methodology being significantly different from past MoD tenders, Mears views this as an exciting opportunity to become a key provider of management, maintenance, repairs and upgrades to the UK Armed Forces' housing in the UK. A total of 5 housing-focused lots are up for tender of which any bidder can win a maximum of three. All lots are being let for an initial 7 year period with an extension option for a further 3 years. The lots include one national housing management lot and 4 regional repairs and upgrade lots. The bidding process will last for much of 2019 and the MoD proposes to announce successful bids in the Spring of 2020 with contracts due to commence in the Autumn of 2020.

Elsewhere across the Group, the pipeline of traditional opportunities continues to flow at a consistent level with around £1 billion of new work expected to be tendered this year. The Group is well placed on a number of these and expects to deliver a contract win rate, by value, in line with historical norms of one in three.

The Group has enjoyed a recent period where few existing contracts having been up for renewal. As announced previously, 2019 will be a very busy period for re-bidding existing contracts with an annual value of £115m up for renewal in each of 2020 and 2021. This represents some risk over the medium term, though a number of these retenders also provide an opportunity to secure increased revenues and better terms.

£1.3bn

Orders secured

£3.2bn

Forward order book

+15%2019 Target
revenue growth**4.5%**2019 Target
operating margin**Guidance and outlook**

As discussed above, the Board expects 2019 to see a change of priorities for Mears. We will reallocate our capital to those areas of the business which deliver the best financial returns or use it to reduce debt levels.

The Group expects to deliver strong growth in revenues for 2019 and may exceed £1bn for the first time ever. Within this, Housing Maintenance revenue will grow, bolstered by the acquisition of MPS, however we will take the opportunity to exit a number of contracts which are not delivering their anticipated margins. We expect to see growth in Housing Management revenue across a number of areas, predominantly through the new AASC contract which will start to make a significant revenue contribution during the second-half. The Group will continue to explore ways in which it can contribute to its clients Housing Development needs but in a manner that creates value for both parties without placing a strain on the Group's balance sheet. The decision to reposition the Development activities will result in some reduction in the rate of revenue growth previously expected from this activity in 2019. The Care division may see a further reduction in revenue as we continue to focus on service delivery and profitability rather than revenue growth.

While noting the expected trends in revenue highlighted above, Mears expects to make satisfactory progress in profitability for 2019. Underlying margins across the Housing Maintenance activity will be broadly unchanged. Similarly, the underlying margin in Housing Management will also be maintained at the level of the previous year. However, while costs relating to the mobilisation of the AASC contract are recoverable, any material profit contribution from this contract may not arise before 2020. The actions being taken in respect of Development activities may result in a small loss in 2019. Meanwhile, the focus in Care will be to continue to deliver the solid margin progression delivered in the previous year.

For 2020, Group revenue is expected to show strong growth as the full year impact of the AASC contract comes through and more than offsets the reduction in activity from Development. The Group expects to deliver growth in Maintenance although the number of contracts to be rebid may provide a headwind in this area. Profit growth will be driven by the full year contribution of the AASC contract which is expected to reach a typical Housing margin during that year. It is expected that this profit growth will be augmented by the continuing improvement in MPS as its integration progresses.

The Board expects the actions being taken to result in a reduction in average net debt in 2019. We will look to continue this downward trajectory through 2020 with a target average net debt for a 12 month period, whose midpoint is no later than December 2020, to be below EBITDA for the same period.

At Mears we are proud to have been awarded and accredited by outside bodies through rigorous testing. Our commitment to safety, our staff and providing social value to the communities we work in all make us stand out from the crowd



Tpas Quality Standard Mark

Mears is proud to have maintained its Tpas Quality Standard Mark, passing the three-yearly assessment every time since 2006. The Tpas accreditation demonstrates Mears' commitment to supporting landlords and encouraging tenant involvement. This Quality Mark for contractors is an assessment of the standard of resident involvement in responsive repairs, maintenance and capital works contracts which ensures best practice for three consecutive years.

Areas of Mears' good practice which were highlighted included tenant conferences and the Mears Change Club, which involved residents in developing Mears policies and procedures.



Customer Service Excellence accreditation

Customer Service Excellence (CSE) aims to bring professional, high level customer service concepts into common currency with every customer service by offering a unique improvement tool to help those delivering services put their customers at the core of what they do.

Care and Housing go through a rigorous assessment on an annual basis and have successfully achieved this accreditation year on year for the past six years. They are assessed on their current service delivery and on how they have made service improvements on the previous year's performance. Care has been awarded accreditation across all of the five CSE standards, with nine Compliance Plus awards. 36 Housing branches have successfully gone through the accreditation and have undertaken three rolling programmes on all five criteria.



Royal Society for the Prevention of Accidents

In 2017, Mears was awarded the Highly Commended Industry Sector Award (making 16 consecutive Golds) in the prestigious annual scheme run by RoSPA.

Health and safety is paramount to our business, and the achievement of both of these awards bears testament to the significant commitment that Directors, managers and staff have to the health and safety activities within the Group. It gives recognition that Mears Group is one of the leading companies in the UK devoted to continually improving safety, health and environment standards.



FTSE4Good

FTSE4Good

Mears Group has been recognised for its outstanding environmental, social and governance practices by gaining a place in the FTSE4Good Index – which places Mears in the top 9% of companies in the index.

FTSE4Good is an initiative run by FTSE to provide an independent measure on the environmental, social and governance (ESG) practices of companies on its global index. It was set up to cater for a growing number of investors who want access to a list of companies recognised for being involved in socially responsible investment (SRI).

Organisations hoping to be included on the list must supply robust and detailed evidence on how they fulfil the index's key indices, which focus on three areas: the environment, human rights and stakeholder relations



Diversity Network

Mears is very proud to have been awarded Diversity Network Accreditation (DNA). DNA is a forward thinking and outcome-based accreditation framework. It is an independent, robust and comprehensive assessment of how an organisation deals with equality and diversity. Achieving DNA is recognition from the Housing Diversity Network, the leading specialist body in the sector, that an organisation has effective leadership and processes in place and that they are achieving positive outcomes for those who work for them and their customers.



Best Companies

In 2019 for the first time, Mears has been accredited by the Sunday Times Best Big Companies, as being one of the top 25 big companies to work for in the UK. For us this is only the beginning. We will work on an action plan in the coming year to build on our work and aim to come even higher in 2020.

The Sunday Times Best Companies aims to create a true measure of workplace engagement to build a happier, healthier workforce

Its lists and accreditations are now recognised as the standard in workplace engagement, with specific categories for small, medium-sized, large and not-for-profit organisations, and one dedicated to Housing Associations.

Stakeholder engagement is central to our strategy. We are focused at delivering positive outcomes for all our stakeholders



Clients

How we engage

Our clients are from Central Government, Local Government, Housing Associations and the NHS. Our model has always been based on establishing long-term partnerships that address the significant challenges and opportunities faced by our clients. Transparency and responsibility are at the heart of our approach and we focus on solutions that establish sustainable solutions, rather than quick fixes.

Stakeholder expectations

The partners we work with expect a trusted partner that can contribute to strategic thinking as well as deliver excellent operational solutions that improve service and lower long-term cost. Increasingly partners are looking for good governance, a strong financial position and high levels of social responsibility.

Relevance to business model and strategy

We operate as trusted long-term partner to the public sector. As partners we have to demonstrate that our values complement their own. We are not like many other outsource organisations, in that both the focused nature of our services and the cultural fit with our clients continue to position us to win major new contracts, such as with the Home Office, and to retain long-standing contracts in the way that we do. We are also careful to not continue with contracts where values are not aligned, as demonstrated by us handing back some Care contracts in recent years.



Tenants and service users

How we engage

We have a long track record of listening to the needs of our end customers and having service solutions that address their needs effectively. Centrally, we have a national Change Club, made up of tenants from across the UK, who look at strategic service issues and support improvement. At a local level, every branch is charged with having a plan to engage with local people. This will be through regular tenant meetings as well as learning from the 80,000+ surveys that we carry out each year. We benchmark our engagement methodologies through Tpas and have long been a leader in this field.

Stakeholder expectations

Our tenants and service users expect to be part of developing solutions rather than to be simply a recipient. In Housing, expectations for engagement are rising, given issues identified post Grenfell and this is likely to lead to greater requirements going forward, which we will fully support. In Care, every service user has a personalised care plan, where each person directly contributes to the nature of their care.

Relevance to business model and strategy

As an organisation with a clear objective to be the leader in terms of customer service, wherever we operate, this cannot be done without good engagement. Our outstanding customer service performance is a testament to our success.



Communities

How we engage

In terms of community commitment, every branch is tasked with developing a social value plan for their area, which demonstrates where we will add value to the community, often over and above any contract commitments. This might be working with local schools to encourage and support young women, thinking of an apprenticeship, or working with local charities to support people who have become socially isolated. The detail of our work is shown in the Social value section of this report.

Stakeholder expectations

Stakeholders expect, given their long-term commitment, that we contribute positively to the communities in which they live. They want us to help local people into work, to upskill people and to work with them to address local issues where we can.

Relevance to business model and strategy

Being a socially responsible organisation with a firm commitment to supporting communities is essential to being a valued partner to our clients. Establishing strong community links also helps us attract the right people into our workforce and to establish links with other community-based organisations, which can contribute to our service offer.



Colleagues

How we engage

We are proud to be on the list of the Sunday Times 25 Best Big Companies to Work For. We have a national Workforce Group that is responsible for setting the approach to staff engagement and each local branch has a People plan, which sets out what it will do in each year. We have an Employee Director who sits on the Mears Group Board, which also helps ensure that the views of the workforce are listened to and actioned.

Stakeholder expectations

Our staff want to work for an organisation that values them and the communities in which they live. They want an organisation that treats people fairly and gives them the opportunity for personal development. Our staff really appreciate the fact that when they do a good job, they do help make a difference to society as a whole, given that better housing and care can make such a difference to the wellbeing of so many people.

Relevance to business model and strategy

Our workforce engagement is built around the Mears 'Red Thread' model, which works to establish the type and culture of workforce that we know will lead to both customer and financial success.



Suppliers

How we engage

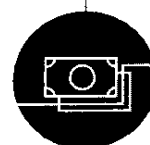
We work in partnership with clients and we reflect this way of working with our suppliers. We focus on keeping our promises to them, be that how we pay them or the commitments we make in terms of helping them grow their business. We challenge them to operate to the same social value approaches that we do and have a clear supplier Charter that sets out our expectations from them. We recognise that all suppliers cannot be at the same level as ourselves but will support them where we can to improve. As you would expect, we set appropriate controls to ensure work quality and compliance standards are delivered to our expectations. We also have an established approach to setting up new supplier arrangements, to ensure that both parties are clear on responsibilities and risks.

Stakeholder expectations

The most important thing for our suppliers is that we keep the promises that we make to them. This means that we set out clearly what is expected in conjunction with our supply partners and that we keep our part of the arrangement in a fair and transparent way.

Relevance to business model and strategy

Our supply chain is fundamental to the success of our business, both in the provision of materials and in the delivery of services under our leadership.



Investors and bankers

How we engage

The Company is committed to maintaining good communications with investors. There is an active programme of communication with existing and potential shareholders. There is increased dialogue with institutional investors following the publication of final and interim results, which is facilitated through a series of formal presentations. The Company has also looked to hold additional investor days during the year to ensure that they are better informed of market and Company developments. The Group regularly receives and responds to questions raised by small private shareholders through the investor enquiry portal within the Group's website. The Group holds regular meetings with its funding partners.

Stakeholder expectations

Our shareholders and bankers expect the Group to maintain a high standard of corporate governance. Mears recently achieved a very high rating from FTSE4Good, which assesses listed company policies and procedures on social impact, environmental impact and governance. Our shareholders require Mears to deliver sustainable profitable growth, with good generation of free cash flow and dividend growth.

Relevance to business model and strategy

Our funders are fundamental to the Group's success. Mears has utilised equity to complete a number of acquisitions, most recently MPS, Il S and Morrison. The Group's organic growth strategy has been funded through both debt and retained earnings, none of which could have been delivered without shareholder and banker support.

Responding to a changing environment

Housing market



Expenditure – by Local Authorities and private Registered Providers in England, Scotland and Wales (based on official estimates):

	2015/16	2016/17	2017/18	2018/19
Housing Management	£71bn	£70bn	£70bn	£70bn
Repairs & Maintenance	£4.5bn	£4.5bn	£4.4bn	£4.4bn
Capital works/major repairs	£1.7bn	£1.5bn	£1.4bn	£1.4bn
Total	£13.4bn	£13.1bn	£12.8bn	£12.8bn

The market for our housing services is stable with potential for growth. Currently £12.8bn is spent on housing management, maintenance and major works. Following the publication of the Social Housing Green Paper with a broad commitment from Government to social housing, we anticipate that demand from Local Government partners and Housing Associations will grow.

Social housing build is seen by Government as an engine to reach ambitious housing build targets. The Green Paper discusses the next stage of the Decent Homes Programme and the Treasury has committed funding to social housing build through the Housing Infrastructure Fund.

The debate around homelessness has been recognised on the political agenda, supported by the Homelessness Reduction Act 2017. But this is an issue which is growing, with 95,792 households in temporary accommodation in the UK. With no commitment for funding of temporary accommodation new build, we must continue to find innovative solutions from current stock alongside our partners.

Care Market



Value of supply of homecare and supported living by sector and age, England and UK estimate 2016/17 (source Laing Buisson).

	All clients aged 18-64	All clients aged 65+	Total clients
Total market value (UK estimate)	£3,926m	£5,182m	£9,109m

The market for our Care services is also growing, with the homecare and supported living market value estimated at £9.1bn. Funding for care has increased in both cash and real terms since 2016 and we expect this trend to continue.

An ageing population means the need to find new solutions for caring for people in older age is pressing. The number of people eligible for social care will increase by 30% by 2022. Forecasts predict there will be a more than 20% increase in people aged over 85 by 2028, by 2039, the average number of households with people over 75 is predicted to double.

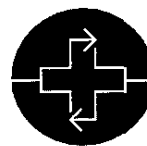
We need legislative change urgently to place social care on a sustainable funding settlement. The Social Housing Green Paper on funding and sustainability has been delayed since summer 2018 and is now expected to be published in the coming months. Legislative certainty on funding will provide our care business with the certainty the whole market needs to continue to grow.

Mears' market position



Best placed to deliver housing growth and repairs

Being a strategic partner to the public sector, we are uniquely placed to meet the challenges of affordable housing and social care in the 21st century. The Government has committed to provide a boost to the number of social homes and a "deepening commitment to those who live in them". The Social Housing Green Paper refers to the next stages of the Decent Homes Programme and the expansion of the housing supply.



Market-leading and sustainable care provider

In Care, we provide a comprehensive range of homecare and complex care services to over 15,000 people a year, enabling older and disabled people to continue living in their own homes. This amounts to over 5.5 million hours of care delivered per year.



Best placed partner for repairs

Mears is the clear leader with a market share of circa 10% and growing, following our acquisition of MPS.



Leading provider of housing with care

We have built on our work to integrate Housing and Care contracts, at the front line delivery of service but also in the creation of new specialist accommodation, such as supported living housing and extra care property.



Largest provider of innovative solutions to tackle homelessness

Almost 79,000 households are currently living in temporary accommodation, including bed and breakfasts, hostels and private rented accommodation. This is an increase of 4,000 since last 2018. Mears is the leading provider of innovative solutions alongside our partners in Local Government.



Largest private Registered Provider in the UK

Mears owns and operates two not-for-profit Registered Providers, Plexus and Omega Housing. Our partnerships allow us, as a Registered Provider, to contract with Councils to provide homelessness prevention, with settled and temporary accommodation solutions.

Critical market factors that influence performance

Drivers



Political and economic landscape

- ~ Social Housing Green Paper published – includes more powerful tenant voice and regulation, lays ground for next stage of Decent Homes Programme and safety, expanding home ownership; and treatment of complaints
- ~ Green Paper on Social Care expected in coming months
- ~ Brexit uncertainty
- ~ Mergers of larger Housing Associations
- ~ Impact of Grenfell tragedy
- ~ End of austerity spending from Government



Rising levels of homelessness due to housing shortage



Demographic change



Rising customer expectations

- ~ Collapse of Carillion
- ~ Rising tenant expectations
- ~ Post-Grenfell focus on social value across the market

Potential opportunities and risks

- ~ Greater commitment to affordable and social housing evident
- ~ Commitment to implement the Hackitt Review of Building Regulations and Fire Safety in full
- ~ Decent Homes Programme next stage likely to create additional workstreams
- ~ Some workforce issues and delays to legislation as a result of the distraction of Brexit

- ~ Innovative and rapid solutions needed given likely continued slow growth on new build provision
- ~ Homelessness still growing – 79,000 in 2019
- ~ Target to build 300,000 homes per year and planning reforms to streamline process
- ~ Brexit creating some funding uncertainty

- ~ More specialist housing needed to limit escalating cost to the NHS and social care sector
- ~ Care spend rising in cash and real terms – Social Care Green Paper is overdue but its eventual publication will provide the opportunity to create a long-term and sustainable funding regime
- ~ The pace of change on care funding is slower than needed

- ~ Customers' quality, communication and speed expectations continue to increase
- ~ Stronger tenant voice demanded by Social Care Green Paper
- ~ Some reluctance to outsource following Carillion
- ~ Opportunity to demonstrate the core strengths of our business model

Mears' response

- | | |
|--|--|
| <ul style="list-style-type: none"> ~ Continuing to deliver market-leading service and not compromising on pricing ~ Fully engaged on Social Housing Green Paper to ensure best outcomes ~ Growing our share of the repairs market with the acquisition of MPS ~ Market-leading approach to workforce engagement shown by Sunday Times Best Companies accreditation | <ul style="list-style-type: none"> ~ Addressing client pressures from growing regulation and compliance ~ Range of outsourcing models to suit varying client requirements ~ All divisions ready to capitalise on Government spend increase |
| <ul style="list-style-type: none"> ~ Increasing the supply of more affordable homes ~ We have become the leading provider of cost-effective homelessness solutions ~ Creating temporary accommodation from current building stock rather than waiting for pipeline | <ul style="list-style-type: none"> ~ Broadened footprint to areas of specific need e.g. MoD, Asylum ~ Improving planning efficiency through the national Planning Portal ~ Our housing providers Plexus and Omega now represent the largest Private Registered Social Landlord in the UK |
| <ul style="list-style-type: none"> ~ Focused involvement with homecare, where Councils are creating a more sustainable model | <ul style="list-style-type: none"> ~ Development of specialist housing solutions such as extra care ~ Championing social care reform |
| <ul style="list-style-type: none"> ~ Mears' single focus on the tenant in their home ~ Benchmarking against the best across all industries ~ Supporting regulatory change that gives service users a bigger voice ~ Proactively demonstrating our approach to outsourcing | <ul style="list-style-type: none"> ~ Working to continuously improve tenant engagement ~ Highlighted by accreditation from Tpas ~ Continuing to support better communities in which service users live ~ Commitment to social value and tenant engagement through Change Club and other partnerships |

We focus on long-term outcomes and positive social, economic and environmental impact

Our key resources and relationships

Outstanding partnerships

We work with Central and Local Government as well as Housing Associations. Our end service users are the recipients of housing services and care in the home.

Exceptional people

We recognise our staff as our greatest asset. Mears employees are skilled in delivering an excellent service whilst showing a strong customer service ethos and an empathy for our service users.

Market-leading technology

Our performance is built on a bedrock of first class IT platforms giving market-leading capability and driving innovation.

Supply chain partners

We choose suppliers who share our values and meet our standards. We work closely with suppliers to develop innovative services and integrate them with our core systems.

Financial stability

We receive funding through shareholder capital, retained profits, debt and cash generation to run our business and fund its activities. We have a long track record of maintaining solid margins even during difficult trading conditions.

Innovation

The challenge of delivering service improvements at lower cost requires innovative thinking and the use of technology. We create and lead best practice in our markets.

- ~ Manage housing stock
- ~ Innovative funding
- ~ Planning support

OUR ROLE

Housing
strategic
development

Creating more
decent homes

Community outcomes



Better place to live



Reduced homelessness



Reduced pressures on the NHS and more efficient public sector spend



Improved life chances for individuals

How we generate revenue

Mears' revenue is generated from payments from Government, Local Authority, Housing Association and NHS Trust clients in respect of its Housing and Care services. Whilst the end service users are at the centre of our business model, they rarely pay for the service directly.

OUR SERVICES

- ~ Regenerate, refurbish and re-purpose stock
- ~ Intelligent maintenance

The value we share



Investors and bankers



Read more on page 25



Suppliers



Read more on pages 24 and 25



Clients



Read more on pages 24 and 25



Communities



Read more on pages 52–61



Colleagues



Read more on pages 52–61



Tenants and service users



Read more on page 24

How profits convert to cash

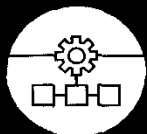
We have a long-standing record of converting profit into cash, utilising strong financial management combined with good relationships with clients and supply chain.

Investing in our strategy

Strategic priorities



Deepening our client relationships
in both Care and Housing



Increasing quality leadership



Developing our people

Performance in 2018

- ~ Winning our biggest ever contract with the Home Office
- ~ Developing the national Planning Portal
- ~ Continued growth of our Housing Management and New Build divisions
- ~ Significantly increased care margins

- ~ 93% rated our service as excellent
- ~ CSE accreditation

- ~ Reached Sunday Times list of 25 Best Big Companies to Work For
- ~ Achieved Housing Diversity Network accreditation
- ~ Recruited an Employee Director

Focus in 2019

- ~ Improve win rates
- ~ Create more housing with care opportunities
- ~ *Continue to grow our Housing Management capability*

Link to KPIs

- ~ Extending services with existing clients
- ~ Retaining contracts at sustainable pricing
- ~ Winning work with new clients that share our values

Link to risks

- ~ A number of existing contracts will be retendered over the next 18 months
- ~ Continued delays in decision making related to Brexit and uncertain political environment

- ~ Ensure we mobilise the Asylum contract well
- ~ Ensure all MPS Housing contracts perform to Mears service standard expectations


- ~ Service user and client feedback


- ~ We continue to demonstrate that quality leads to long-term cost reductions

- ~ Continue to improve staff retention
- ~ Ensure that we recruit effectively to mobilise new contracts
- ~ Continue to increase diversity at all levels in the organisation
- ~ Ensure we successfully integrate MPS staff into the overall Mears Group, achieving efficiencies and enhanced performance

- ~ Staff retention
- ~ Benchmarking v other organisation
- ~ Ability to fill vacancies cost effectively
- ~ Margin improvements

- ~ Uncertainty created around Brexit

 Read more on pages 34–37

 Read more on pages 41–42

Measuring our progress

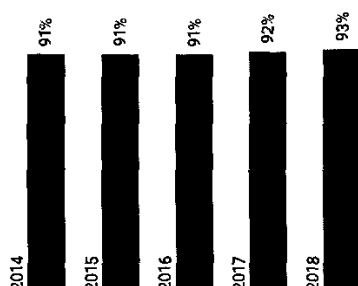
Non-Financial

'Excellent' service rating (Housing)

In order for customers to recommend us, we must deliver excellent service. We randomly conduct around 80,000 customer surveys per year.

Results from the year

93%



We are delighted that our service delivery has remained at a high level. Strong performance will ensure competitiveness as we continue to be ranked above our peers. Our target for 2019 is to do even better.

How we performed

2018 target

92%

↑ Outperformance

2019 target

>93%

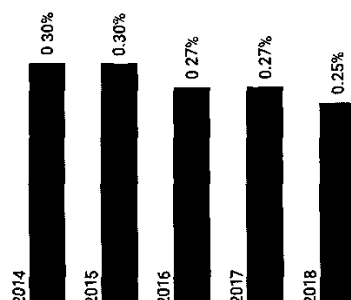
🔗 *Linked to Directors' remuneration
– read more on page 89*

Customer complaints (Housing)

Incidents resulting from poor service result in a complaint. We are committed to dealing with all complaints on an individual basis.

Results from the year

0.25%



We are committed to providing our colleagues with the skills and equipment to deliver great service. We seek to identify trends in order to improve our overall service quality.

How we performed

2018 target

<0.27%

↑ Outperformance

2019 target

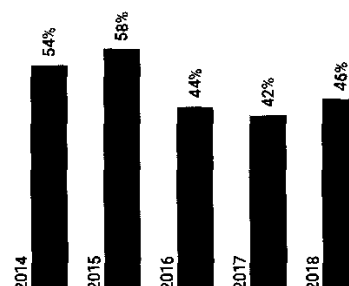
<0.25%

Carer churn (Care)

The carer churn figure is calculated as the total number of leavers during the year as a proportion of the average carer headcount.

Results from the year

46%



The main challenge in Care remains the sourcing and retention of sufficient care workers of good quality and this is an area that continues to receive significant attention. The carer churn measure increasing is very disappointing but we have already put in place actions to improve this.

How we performed

2018 target

30%

↓ Underperformance

2019 target

40%

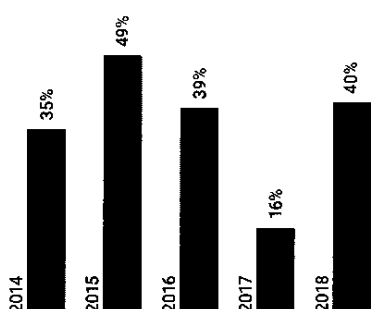
Business development

New contract success (Housing)

Contract success is measured by results of tender by contract value. We typically tender around £1bn of new opportunities each year. The average contract length is around six years. In order to achieve our organic growth forecasts, we monitor the proportion of new contracts secured as a proportion of total tendered works.

Results from the year

40%



The Housing Maintenance division's new bid conversion rate was below historical norms. We are not worried by this. There has been no lack of good quality opportunities to bid and we are pleased with the quality of our tender submissions. Positively, we secured three regions of the new Asylum contract, valued at £1bn over the ten-year term. Given its size, this has skewed the new contract success rate. We are pleased to have delivered against target, but equally realise we must perform better in 2019.

How we performed

2018 target

33%

↑ Outperformance

2019 target

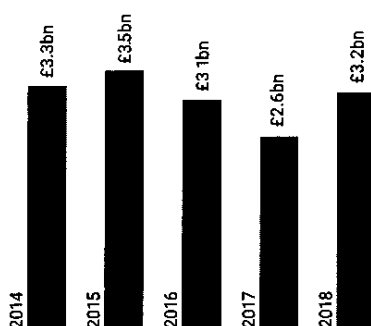
33%

Order book (Group)

Our order book provides us good visibility of those revenues secured for future periods. It is helpful that we have long-term contracts that allow us to plan with confidence, in the knowledge that we have significant revenues already contracted. It is also positive for all our stakeholders, providing stability to our supply chain, funders and, most importantly, for recruiting and motivating our workforce.

Results from the year

£3.2bn



The order book increases as the Group secures new works and reduces as revenues are delivered. It will be challenging to grow the order book in 2019 given the timing of new bids, but we are delighted to have grown the order book so strongly in 2018 and we would also hope to see an increase in 2020 when the MoD tender process reaches its conclusion.

How we performed

2018 target

£2.6bn

↑ Outperformance

2019 target

£2.7bn

Strategic report

Key performance indicators continued

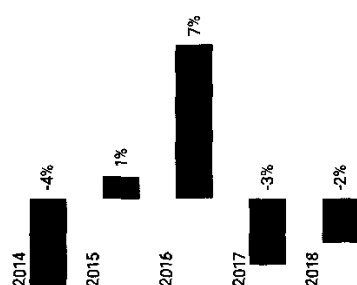
Financial performance

Revenue growth (Housing)

Revenue represents the amounts due for services provided during the year. In order to measure organic growth, we deduct incremental revenue arising from acquisitions. We believe that organic growth gives a better indication of business performance, as it is a purer aggregation of market growth, success in new contract bidding and contract retention.

Results from the year

-2%



The revenue for the year is slightly lower than our expectation. In Maintenance, some revenues expected to be delivered in 2018 were re-phased and will be delivered in 2019. Our Development activities experienced a challenging last quarter, with a significant slowdown in sales activity impacting negatively on both revenues and working capital. With the acquisition of MPS together with the mobilisation of the Asylum contract, growth expectations for 2019 are high.

How we performed

2018 target

0%

↓ Underperformance

2019 target

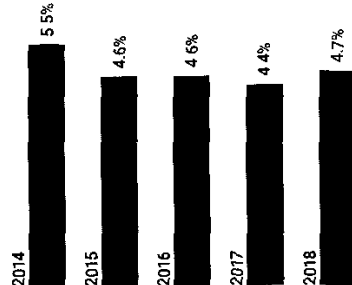
15%

Adjusted operating margin (Group)

Operating margin is the KPI used to measure and understand the profitability of our activities. This KPI is used to continually monitor our costs to ensure services are being delivered efficiently.

Results from the year

4.7%



The Housing division contributed an operating margin of 5.0%, with second half margin reporting a small reduction following the acquisition of MPS and costs expensed in respect of the Asylum mobilisation. However, Care margins increased to 3.3% (2017: 0.4%) reflecting the continued focus on service delivery and sustainable margins rather than revenue growth. The blended margin fell short of target, but did show an increase on the prior year which is pleasing. The 2019 target is set lower reflecting the decision to refocus the Development activities, combined with the new Asylum contract which is expected to break even in 2019.

How we performed

2018 target

>5.2%

↓ Underperformance

2019 target

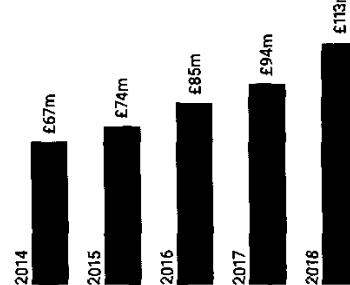
4.5%

Average net debt (Group)

Good working capital management remains a cornerstone of the business. The Group's IT systems are designed to deal with the challenges of high volume and low value activities. This is particularly relevant to the Group's core Maintenance, Management and Care activities. The Group has utilised debt to fund acquisitions over the last five years of circa £60m which is reflected in the increasing average net debt.

Results from the year

£113m



In 2019, we will refocus our capital allocation on those areas with the lowest working capital requirement and the Board will take active steps to reduce debt over 2019 and 2020. The release of cash from the unwinding of Development may be phased over time, so it is prudent to assume that 2020 may show a more significant reduction in net debt than 2019.

How we performed

2018 target

£110m

↓ Underperformance

2019 target

£105m

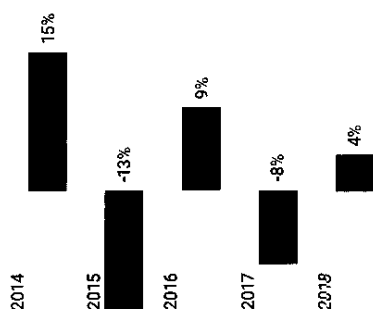
Health and safety

Growth in normalised diluted EPS (Group)

Normalised earnings are stated before exceptional costs and exclude the amortisation of acquisition intangibles together with an adjustment to reflect a full tax charge

Results from the year

4%



Normalised diluted earnings per share of 29.06p (2017: 28.05p) reflected the increase in profits, increasing by 4%. The target for 2019 has been set to maintain earnings at this level to reflect the expected loss in respect of refocusing the Development activities and the break-even forecast for the new Asylum contract.

How we performed

2018 target

>5%



Underperformance

2019 target

+3% (before impact of IFRS 16)



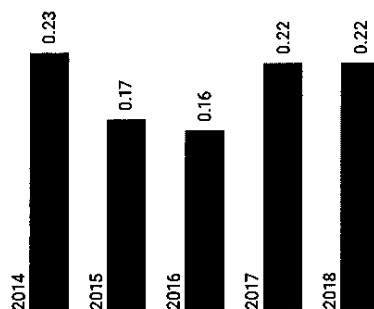
Linked to Directors' remuneration
– read more on page 89

Accident frequency rate (Group)

Providing our employees with a safe working environment remains paramount. Our accident frequency rate (AFR) is calculated as the number of reportable incidents (by both employees, service users and third parties) divided by the number of hours worked, multiplied by 100,000.

Results from the year

0.22



We are proud of our record in this area and we continue to invest in our health and safety training, which is delivered through our in-house registered training provider. We place emphasis upon all accidents and near misses, however trivial, being reported and properly captured, which naturally impacts negatively on this measure. Much of this increase relates to an improved reporting regime. Whilst we have fallen short of our stretch target, our accident rates are already at very low levels for our sector. However we will continue to strive to deliver further improvements to this critical area.

How we performed

2018 target

0.16



Underperformance

2019 target

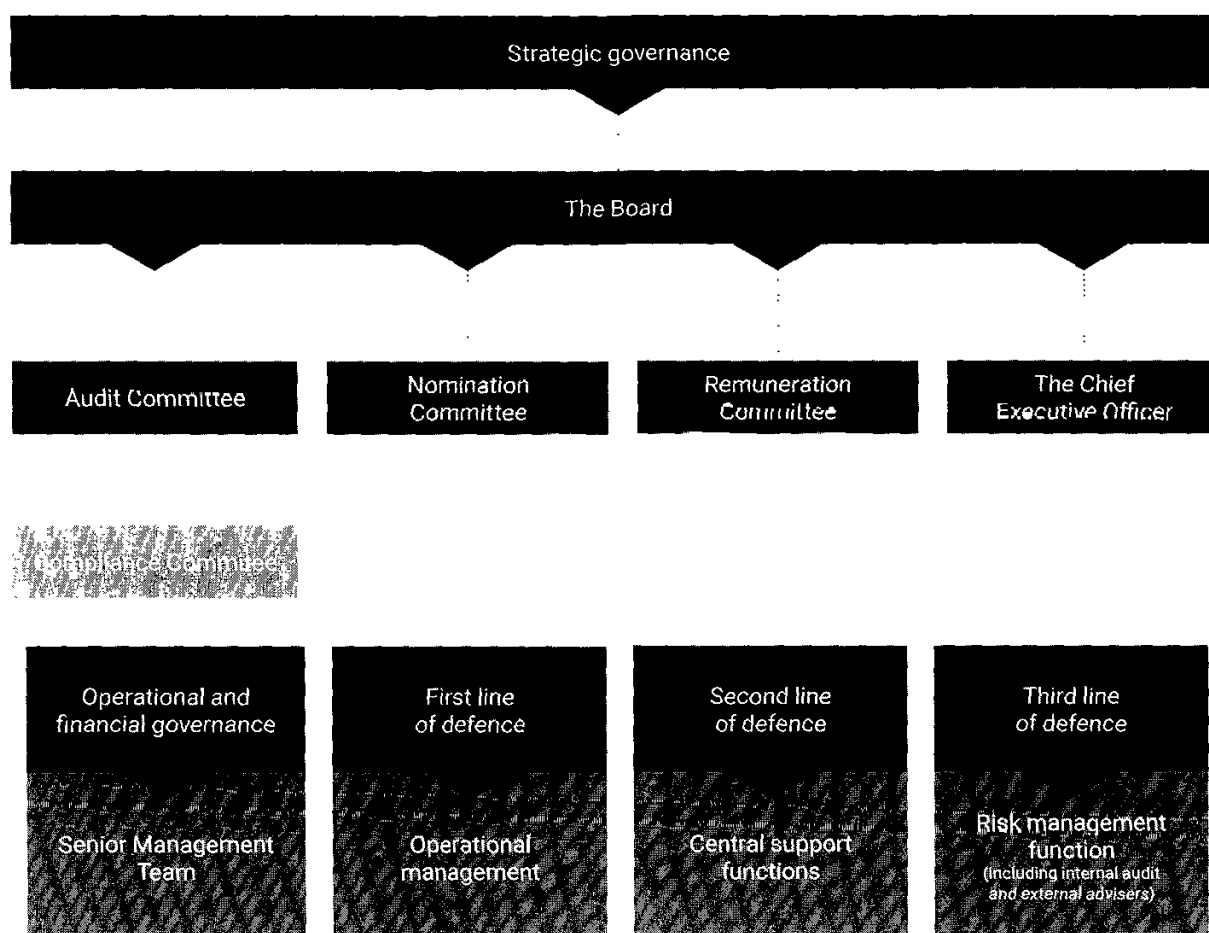
0.21



Linked to Directors' remuneration
– read more on page 89

Effective management of risks and opportunities is essential to the delivery of the Group's strategic objectives, the achievement of sustainable shareholder value and maintaining good standards of corporate governance

Risk management process



The Senior Management Team

The Senior Management Team reviews and identifies the key risks which may impact upon the achievement of the Group's strategic goals and will consider how these risks are developing with changes in the operations, markets and the regulatory environment

The nature of the risk is reviewed, including the possible triggering events and the aggregated impacts, before setting appropriate mitigation strategies directed at the causes and consequences of each risk. The risk is assessed in relation to the likelihood of occurrence and the potential impact of the risk upon the business, and assessed against a matrix scoring system which is then used to escalate risks within the Group as appropriate. The Senior Management Team has responsibility for managing the Group's key risks.

The Board

The Board has overall responsibility for determining the nature and extent of risk it is willing to accept within the agreed strategy, and ensuring that risks are managed effectively across the Group.

Risk is a regular agenda item at Board meetings and is closely aligned to strategy review.

The Board also reviews reports on the effectiveness of the systems and processes of risk management and internal control.

The Audit Committee

The Audit Committee monitors the Group's key risks identified by the risk assessment processes and reports findings to the Board. It also has delegated responsibility for reviewing in detail the effectiveness of the Group's system of internal control policies and procedures for the identification, assessment and reporting of risk.

Compliance Committee

Created in 2017 as a sub-committee of the Audit Committee, its purpose is to continue to increase the Board's focus on health and safety strategy and performance, regulatory compliance and related risk management and provide a closer link between the Board and the operations.

Risk management function

The Group risk function, headed by the Group's Chief Risk Officer, supports the risk management process by providing guidance and support to management. Group risk also acts as the central point for the coordination and initial review of risk assessment and risk monitoring procedures. To ensure our risk management process continues to drive improvement, the Group risk function monitors the ongoing status and progress of mitigation plans on a quarterly basis.

The Group outsources elements of internal audit and cyber-security to external advisers. The control environment is underpinned by a detailed scheme of delegated responsibilities that defines processes and procedures for the approval process in respect of decision making. This ensures that decisions within the organisation are made by the appropriate level of management.

Risk management approach

The Group's approach to risk management is targeted towards early identification of risks and mitigation of those risks to reduce their likelihood and impact.

The Group is committed to protection of its assets through an effective risk management process, supported by insurance where appropriate. Examples of assets within scope include human, intellectual, physical property and financial resources.

Reporting within the Group is structured so that key issues can be escalated rapidly through the management team to the Board where appropriate. Risks are continually monitored, contingency plans are provided and this information is reported through established procedures. There is extensive fieldwork undertaken by risk auditors incorporating systems review, branch visits and cross-business surveillance.

The internal control approach is designed to manage rather than eliminate the risk of failure and thus can only provide a reasonable, rather than absolute, assurance against material misstatement or loss.

Strategic report

Risk management continued

Risk management process

The responsibility for risk identification, analysis, evaluation and mitigation rests with the line management of the businesses. They are also responsible for reporting and monitoring key risks in accordance with established processes under the Group operational policies.

Identified risks are documented in risk registers showing the risks that have been identified, characteristics of the risks, consequences of the risks, the basis for determining the mitigation strategy, and what reviews and monitoring are necessary. The person(s) accountable for assessing and monitoring each risk is noted.

We continue to drive improvements in our risk management process. We also review our business model, core markets and business processes to ensure that we have properly identified all risks. We continually review our mitigating actions to ensure that they are sufficient to minimise our residual risk. Key financial and non-financial risks identified by the business from the risk assessment processes

are collated and reviewed by the Audit Committee.

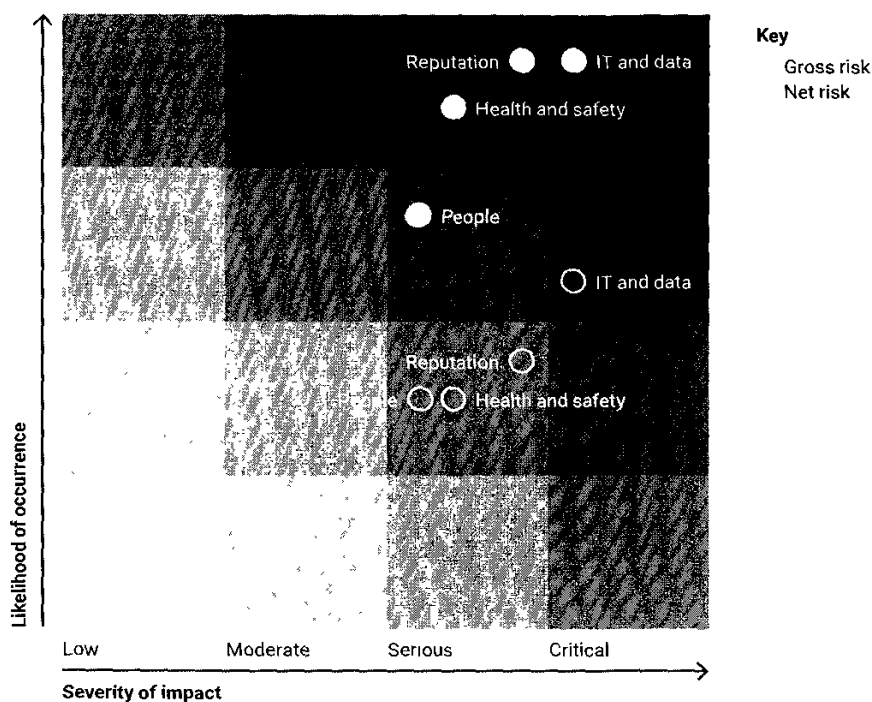
The financial and non-financial risk registers are reviewed to monitor the status and progression of mitigation plans, the key risks are reported to the Board on a regular basis.

Principal risks

The Board has carried out a robust assessment of the principal risks facing the Group, including those that threaten the business model, strategy, future performance, solvency and liquidity. Risks have been identified as 'principal' based on the likelihood of occurrence and the severity of the impact on the Group, and have been identified through the application of policies and processes previously outlined. The Board is keen to simplify the reporting of risks, to ensure the risks disclosed to shareholders are those that are considered as business critical or potentially catastrophic. Therefore no additional risks have been disclosed in this Annual Report. These business-as-usual risks are monitored by divisional management.

Prioritising our risks

The Group's risk register rates risks on a matrix scoring system based on their likelihood and impact, i.e. potential severity. This severity can be measured using life and limb, financial, customer service, growth, regulatory compliance and reputational criteria. Therefore, Mears measures more than simply the financial impact of the risk. These scores are used to escalate risks and to drive the mitigation plans.



Read more in the Corporate governance section on page 69



Read more in the Report of the Audit Committee on page 77

Risks are identified as 'principal' based on the likelihood of occurrence and the potential impact on the Group. The Group's principal risks are identified below, together with how we mitigate those risks.

Key risk movements

Each principal risk is considered in the context of how it relates to the achievement of the Group's strategic objectives. The risk discussion includes assessment of gross risk and net risk. Gross risk reflects the exposure and risk landscape before considering the mitigations in place, with net risk being the residual risk after mitigations. The gross risk movement from the prior year for each principal risk has been assessed and is presented below.

Mitigations in place supporting the management of the risk to a net risk position are also described for each principal risk.

Reputation

Increased gross risk exposure



Definition

We recognise the significant commercial value attributable to the Mears brand. Our success in securing larger and more complex contracts, such as the new Asylum contract, increases the risk of reputational damage in the event of failure.

Poor service delivery would damage our reputation. Both our Housing and Care markets are close-knit communities where examples of poor performance are quickly communicated widely.

In the environment of caring for vulnerable people, there is a risk of isolated incidents of abuse and neglect, which rightly receive significant press coverage with the inevitable reputational damage.

KPIs associated with risk:

- ~ 'Excellent' service rating
- ~ Customer complaints
- ~ Carer churn

Mitigation

- ~ In-house IT system developed to provide operational management with a real-time dashboard of service delivery indicators
- ~ Internal auditing of KPI reporting including 'mystery shoppers'
- ~ Strict process in place for vetting and approval of subcontractors
- ~ We drive a culture of putting our customers first, this is continually reinforced through internal communications

Well-communicated policy for dealing with press enquiries and incident management

- ~ Care risk plans for dealing with vulnerable customers
- ~ Compliance management of bribery and corruption legislation and whistleblowing policy
- ~ We induct and train all new starters. This induction ensures that all employees understand our values and it reinforces the Group's culture
- ~ We ensure that staff are properly trained for their roles. We ensure that we deliver relevant training and implement best practice

Strategic report

Principal risks and uncertainties continued

People		No change
<p>Definition</p> <p>The Group employs over 10,000 people who are critical to the success of our contract performance. Attracting and maintaining good relations with employees and the investment in their training and development are essential to the efficiency and sustainability of the Group's operations. Delivery of strategic objectives increases our ability to attract, motivate and retain talent. In addition, the Care division is facing a challenging environment where the ability to recruit and retain carers is restricting performance.</p> <p>KPIs associated with risk:</p> <ul style="list-style-type: none">~ 'Excellent' service rating~ Customer complaints~ Carer churn	<p>Mitigation</p> <p>We induct and train all new starters. This induction ensures that all new employees understand our strategy, vision and values. All Care staff have access to NVQ training.</p> <ul style="list-style-type: none">~ We regularly review and benchmark our remuneration packages to ensure that they remain competitive. In Care, we are investing in an innovative recruitment process to ensure an increase in the volume and quality of carers. Local Care branches are targeted on a monthly basis in the areas of recruitment and retention.~ At the senior end of the business, we have increased our focus on succession planning and increased our investment in senior management development. Our senior leadership programme has identified a cross-section of the Group's brightest talent that we would envisage will play central roles in our future business.~ Expansion of apprenticeships	<p>An annual appraisal process is completed for all employees to ensure that all people receive feedback in respect of their performance and to identify future training and development requirements. We hold a national accreditation as an Investor in People. We are continually looking to improve our position as an employer of choice by improving the level of engagement with our employees through formal communications, awards to recognise success, local events and family fun days.</p> <ul style="list-style-type: none">~ We are continually monitoring our future skills requirements~ We regularly undertake employee surveys to gauge employee satisfaction and engagement, and any barriers to high level performance
Health and safety		No change
<p>Definition</p> <p>Prevention of injury or loss of life for both employees and customers is of utmost importance. In addition, it is vital to maintain the confidence our customers and clients have in our business.</p> <p>KPIs associated with risk:</p> <ul style="list-style-type: none">~ Accident frequency rates~ Customer complaints~ 'Excellent' service rating	<p>Mitigation</p> <p>Significant investment in the centralised health, safety and environment (HSE) function to maintain consistency and quality.</p> <ul style="list-style-type: none">~ We have comprehensive safe systems of work which are well communicated through a robust and coordinated internal training regime~ We have robust processes for inducting new staff to ensure the importance of health and safety is emphasised together with detailed method statements for working safely~ Creation of a Compliance Committee to monitor and oversee health and safety strategy and performance, regulatory compliance and risk management	<p>Closer review of buildings safety compliance (post Grenfell) in higher risk areas, e.g. Housing Management</p> <ul style="list-style-type: none">~ Regular HSE training and updates are held, predominantly delivered by the in-house training function~ Independent review of health and safety cases by insurers where recommendations of change are implemented~ Internal health and safety auditing takes place using third party validation~ A Group health and safety strategy and plan are produced annually
IT and data		Increased gross risk exposure
<p>Definition</p> <p>A major incident or catastrophic event could impact on the Group's ability to trade. In addition, it is essential that the security of customer, employee and Company confidential data is maintained. A major breach of information security could have a major negative financial and reputational impact on the business. The risk landscape of IT and data is constantly increasing with deliberate acts of cyber-crime becoming more sophisticated and frequent across all markets.</p>	<p>Mitigation</p> <p>The Business Continuity Plan is constantly reviewed and frequently tested to ensure it is fit for purpose.</p> <ul style="list-style-type: none">~ Business continuity and IT disaster recovery management resource is convened at short notice to manage the response and any associated risk to the Group~ General Data Protection Regulation (GDPR) steering group	<p>Information security penetration is externally tested to recommend improvements which are then implemented.</p> <ul style="list-style-type: none">~ Data Security Committee in place to monitor and review both physical data security and IT data security~ GDPR implementation plan and steering group

Business planning and financial viability

In accordance with provision C 2.2 of the UK Corporate Governance Code 2014, the Directors have assessed the viability of the Group over a five-year period. A period of five years has been chosen as it reflects the average contract length, being a blend of an average contract length of six years in Housing and three years in Care. Whilst the Group holds contracts which extend beyond this time horizon, a period of greater than five years is considered too long, given the inherent uncertainties involved.

The Board considered its key risks. The principal risks are set out on pages 41 and 42 and the most relevant of these risks on viability were considered to be:

- ~ a service delivery failure, possibly resulting in the death or harm of a service user, with significant negative publicity and long-term reputation damage,
- ~ a health and safety failure resulting in serious personal injury or death of an employee or service user, leading to significant financial penalties and significant reputational damage, and
- ~ a failure in our IT systems impacting upon our ability to deliver our services. We provide services to vulnerable people and even a short period of downtime could cause severe reputation damage. A serious system failure could have significant impact to invoicing our customers and collecting cash.

A financial model has been built on a contract-by-contract basis for the next 12 months and extended on a business-by-business basis for the following four years. The five-year plan considers cash flows as well as financial covenants. Consideration was given to a number of key assumptions, namely future revenue growth, operating margins and working capital management. The assumptions were set at levels which were broadly in-line with the current run rates. Sensitivity analysis was undertaken to stress-test the resilience of the Group and its business model to the potential impact of the Group's principal risks, or a combination of those risks. The Board overlaid the potential impact of the principal risks which could affect solvency or liquidity in 'severe but plausible' scenarios.

Three scenarios were modelled:

- ~ **Scenario 1** As reported in detail in the Annual Report, the Group has been awarded a contract in respect of Asylum Accommodation and Support Services. The contract is large in size, in excess of £100m per annum. Whilst this award is of significant strategic importance to the Group, in the event of any failure in mobilisation, service delivery or pricing, this contract could impact negatively on both reputation and financial viability. A key assumption underpinning the contract pricing relates to occupancy rates, the tender model assumed the requirement for around 4,500 properties, accommodating 15,000 service users. This scenario assumes a significant deterioration in occupancy rate, resulting in an increase in the number of properties required by circa 30%, at an additional cost of around £19.5m per annum. The additional cost flows directly to operating profit although the model assumes that no steps are taken to either drive operational improvement or take other mitigating steps.
- ~ **Scenario 2** This scenario takes a negative stance in respect of Housing Maintenance contract renewals. As detailed within the Annual Report, 2020 and 2021 will experience a high level of existing contracts coming up for re-bid. The annualised value of these re-bids, over the course of two years, is circa £225m. The Group has a solid track-record of re-securing work on re-bid. For the purposes of considering the viability of the Group, the model has assumed that all material contracts that come up for re-bid over this 24-month period are lost. This loss of revenue results in a reduction in Housing gross margin and an under-recovery in central support overhead, resulting in a reduction in net profit margin from 5.0% to 4.6% in year 5 of the model.
- ~ **Scenario 3** a combination of both scenario 1 and 2. The combination of both significant loss in margin from scenario 1 and reduced revenues and operating leverage triggered in the event of scenario 2, the combined scenario results in a profit margin reduced from 5.0% to 2.6%.

All scenarios showed that the Group would remain viable even in the event of a severe business failure over an extended period. No mitigating actions were included within either scenario, which was considered conservative but not entirely realistic. Whilst the Group's operations are entirely based in the UK, the large network of branches reduces the risk of serious business interruption through a single failure. In addition, the Group has a broad spread of customers – the largest single client is now 10% of Group revenues, being the Asylum contract. All scenarios have provided comfort that, while significant, the loss of a major client would not impact on the Group's wider viability. The Group's existing debt facilities run to November 2022. The future viability review extends narrowly beyond this date and therefore assumes that there will be sufficient appetite from our existing or new funders to provide the required level of funding on similar terms. The Group's average daily net debt in 2018 was circa £113m. In all three cases, it is forecast that the Group would have delivered a reduction in its debt level at renewal compared with the balance today, and it could be in a position to seek a reduction in the facilities required at renewal.

The Board also considered the impact of Brexit on the business and does not envisage any significant negative effect impacting on the Group's viability for the period under review.

The Board is mindful that there has been a significant increase in the fines that can be levied upon companies for non-compliance in areas such as health and safety, and data protection. Fines are discretionary based on the nature, gravity and culpability of the company but fines are applied based upon a percentage of Group revenue. In a low margin business such as Mears, any single fine could have a significant and disproportionate impact on retained profits. The Board took the view, however, that, whilst such an event could be damaging, it would not ultimately impact on the long-term viability of the Group. Both health and safety, and IT and data feature high on the Group's risk register and we continually review our mitigating actions to ensure that we minimise our residual risk.

The Board accepts that uncertainty of results increases as the projections cover a five-year period. However, the Board concluded that there was a reasonable expectation that the Group would continue in operation and would be able to continue to meet liabilities as they fell due over the five-year period of business planning.

The Directors are taking a number of active steps to progressively reduce debt



Andrew C M Smith
Finance Director

This section provides further key information in respect of the financial performance and financial position of the Group to the extent not already covered within the Chief Executive review

Alternative performance measures (APM)

APMs used by the Group are detailed below to provide a reconciliation for each non-IFRS measure to its IFRS equivalent and an explanation as to why management considers the APM to provide a better understanding as to the Group's underlying performance. The APMs are used externally to meet investor requirements and also used when reporting financial performance internally

The Group defines normalised results as excluding the amortisation of acquisition intangibles and exceptional costs and adjusted to reflect a full tax charge and uses these results are used for reporting all profit and EPS measures. This aids consistency when comparing with historical results and enables performance to be evaluated before non-recurring items. Investors typically require results to be reported before the amortisation of acquired intangibles and the Group's adjusted earnings measure reflects this

29.06p

Normalised
diluted EPS

22.91p

Statutory
diluted EPS

	Normalised result for year £'000	Full tax charge £'000	Amortisation of acquired intangibles £'000	Exceptional £'000	Statutory (all activities) £'000
2018					
Sales revenue	869,843	–	–	–	869,843
Cost of sales	(662,825)	–	–	–	(662,825)
Gross profit	207,018	–	–	–	207,018
Total administrative costs	(166,177)	–	(4,434)	(5,657)	(176,268)
Operating profit	40,841	–	(4,434)	(5,657)	30,750
Finance income	1,154	–	–	–	1,154
Finance costs	(3,473)	–	–	–	(3,473)
Profit for the year before tax	38,522	–	(4,434)	(5,657)	28,431
Tax expense	(7,231)	2,310	–	1,315	(3,606)
Profit for the year	31,291	2,310	(4,434)	(4,342)	24,825
Earnings per share					
Basic	29.24p	2.22p	(4.25p)	(4.16p)	23.05p
Diluted	29.06p	2.20p	(4.22p)	(4.13p)	22.91p

Strategic report
Financial review continued

£22.5m

Initial consideration
for MPS acquisition

£11.1m

Final Deferred
consideration
in respect of
Omega acquisition

2017	Normalised result for year £'000	Full tax charge £'000	Amortisation of acquired intangible £'000	Statutory (continuing activities) £'000	Statutory (discontinued activities) £'000	Statutory (all activities) £'000
Sales revenue	900,184	~	~	900,184	~	900,184
Cost of sales	(676,482)	~	~	(676,482)	~	(676,482)
Gross profit	223,702	~	~	223,702	~	223,702
Total administrative costs	(184,551)	~	(10,638)	(195,189)	~	(195,189)
Operating profit	39,151	~	(10,638)	28,513	~	28,513
Finance income	751	~	~	751	~	751
Finance costs	(2,780)	~	~	(2,780)	~	(2,780)
Profit for the year before tax	37,122	~	(10,638)	26,484	~	26,484
Exceptional items	~	~	~	~	(16,500)	(16,500)
Tax expense	(6,682)	2,367	~	(4,315)	3,176	(1,139)
Profit / (loss) for the year	30,440	2,367	(10,638)	22,169	(13,324)	8,845
Earnings per share						
Basic	28.29p	2.31p	(10.32p)	20.28p	(12.93)	7.35p
Diluted	28.05p	2.28p	(10.23p)	20.10p	(12.81)	7.29p

Acquisitions

(i) Certain business assets and contracts from the property services division of Mitie

In November 2018, Mears completed the acquisition of certain business assets and contracts from the property maintenance business of Mitie, with the acquired business branded as MPS Housing ("MPS"), as detailed in the Chief Executive Review. The initial cash consideration was £22.5m and was funded through an issue of approximately 6.8m new ordinary shares. The business was acquired on a cash free, debt free basis, with a target net asset value, based on the sellers' accounting policies, of £12.3m.

Whilst the acquisition was a share transaction, there was a business transfer into a newly incorporated vehicle immediately prior to completion. This transaction structure added a layer of complexity but positively reduced the Group's exposure to risks associated with share capital transactions, such as pensions, taxation and legacy activities.

The fair value of the net assets acquired, based upon Mears accounting policies and reflecting a level of conservatism, is estimated to be £71m and after recognising intangible assets of £17.4m and deferred tax of £3.3m, goodwill of £3.3m was recorded. Given the proximity of the acquisition to the year end, the Directors have not concluded their assessment of the assets and liabilities acquired and this estimate remains provisional and will be finalised during 2019. Inevitably there will be both positive and negative variances as judgements and estimates are revised in light of changing circumstances.

Contingent consideration is payable in 2021, up to a maximum of £12.5m, based upon a multiple of three times applied to the total net profits generated by the acquired business during the 24 months following completion, and after deducting the initial consideration of £22.5m. Based upon the forecasts prepared for the earn-out period, the Directors have estimated that further consideration will be payable of £2.0m and which would become payable in 2021.

(ii) Omega Group of companies

In January 2018, deferred consideration of £11.1m was paid in full and final settlement of all deferred consideration relating to the 2014 acquisition of Omega.

Exceptional items

Exceptional items are items which are considered outside normal operations. They are material to the results of the Group either through their size or nature. These items have been disclosed separately on the face of the Income Statement to provide a better understanding as to the underlying performance of the Group.

	2018 £m	2017 £m
Restructuring costs	3.6	~
Non-trading legal costs	2.1	~
	5.7	~

The Group has carried out a review of its central support structures to ensure they reflect the changing nature of the business and that they are efficient and deliver value. The review identified annualised savings of approximately £5.0m and these have been secured in the year. The costs associated with this restructure of £3.5m have been accounted for within exceptional items.

£4.4mAcquisition
intangible
amortisation**£2.3m**

Net finance charges

The legal costs relate to two matters. Firstly, the Group committed to enter into a lease on a property in the course of construction. The property required completion by September 2018. Mears has incurred litigation costs of £1.8m as the construction of the property was not complete by the contractual date and is not compliant with fire safety regulations leaving the Group no option but to defend its position robustly. The Group will not compromise the safety of tenants for any reason. The Directors are very confident as to a successful outcome to this litigation and a proportion of these fees would be recoverable in such an event. Given the size of this single item, and the unique circumstances of the matter in dispute, the Directors believe it should be accounted for as an exceptional item. Costs of £0.4m relating to the acquisition of MPS are also included as exceptional on the basis they are non-trading.

Amortisation of acquisition intangibles

	2018 £m	2017 £m
Carrying value at 1 January	9.6	19.8
Revisions / disposals	–	0.4
Recognised on acquisitions during the year	18.0	–
Amortisation	(4.4)	(10.6)
Carrying value at 31 December	23.2	9.6

A charge for amortisation of acquisition intangibles of £4.4m (2017: £10.6m) arose in the year. The charge has reduced significantly on the prior year reflecting few acquisitions over the last three-year period and the subsequent reduction in carrying value of acquired intangibles. The acquisition of MPS in late 2018 will result in an increase in amortisation in 2019 to 2021. The remaining unamortised value of £23.2m (2017: £9.6m), predominantly relating to order book and customer relationships, will be written off over their estimated lives.

Net finance charge

	2018 £m	2017 £m
Finance costs	(3.5)	(2.8)
Finance income	0.4	0.3
Pension income	0.8	0.5
	(2.3)	(2.0)

A net finance charge of £2.3m has been recognised in the year (2017: £2.0m). The finance cost in respect of bank borrowings was £3.5m (2017: £2.8m), reflecting a higher level of average debt.

The Group held two interest rate swaps covering 2018. The first, which ran throughout the year, fixed a rate of 0.84% on £40.0m of borrowings and expires in December 2020. The second, which commenced in August 2018, fixed a rate of 0.96% on £30.0m of borrowings. The remaining debt bore a variable LIBOR rate. The Group pays a margin of 120–220bps over and above LIBOR, subject to a ratchet mechanism.

The net finance costs also includes a net credit generated from defined benefit pension accounting of £0.8m (2017: £0.5m).

Tax expense

	2018 £m	2017 £m
Current tax on continuing activities recognised in income statement	(1.2)	5.3
Deferred tax on continuing activities recognised in income statement	4.8	(1.0)
Current tax on discontinued activities recognised in income statement	–	(3.2)
Total tax expenses recognised in income statement	3.6	1.1
Profit before tax and amortisation of acquired intangibles	38.5	37.1
Profit before tax on continuing activities	28.4	26.5
Effective current tax rate on continuing activities	(4.1%)	20.1%
Taxes paid / (received)	(0.7)	3.8

The headline UK corporation tax rate for the year was 19.0% (2017: 19.3%). The total tax charge for the year relating to continuing operations was £3.6m (2017: £4.3m) resulting in an effective total tax rate of 12.7% (2017: 16.3%). The key reconciling items to the headline rate were the utilisation of brought forward losses where the deferred tax impact had not previously been recognised, an annual corporation tax deduction in respect of share options and adjustments in respect of the prior year estimated tax charge. The current tax credit for the year on continuing operations was £1.2m (2017: £5.3m charge), which represents an effective tax rate of (4.1%) (2017: 20.1%). The current tax credit was generated through the impact of IFRS 15, resulting in a large credit in the current year, offset against the unwinding of the deferred tax balance recognised on transition to the new standard.

Strategic report

Financial review continued

£113.2m

Daily average
net debt

£65.9m

Net debt at
31 December 2018

Mears does not engage in inappropriate or aggressive tax planning arrangements. Where appropriate, the Group takes advantage of available statutory tax reliefs. The tax position in any transaction is aligned with the commercial reality and any tax planning undertaken is consistent with the spirit as well as the letter of tax law. In situations where material uncertainty exists around a given tax position, the Group engages with expert advisers and, where appropriate, advance clearance is sought from HMRC in order to establish the most appropriate treatment.

We value our low risk assessment from HMRC and will continue to work to maintain this status through continual review of our controls and processes.

Discontinued activities

The results for the previous year reported a loss from discontinued activities of £16.5m. This was in relation to the Mechanical and Electrical division which was the subject of a disposal in 2013 and included an entity operating in the United Arab Emirates (UAE). As part of that disposal, the Group ultimately retained a beneficial interest in 1% of the share capital of this UAE Company due to the Group still carrying a number of performance guarantees, which unwind as the underlying contracts reach the end of their defects liability period. In 2017, a number of the performance guarantees were called, and the Group made a provision against the outstanding performance guarantees.

A balance is owed by the UAE company to the Group in excess of £14m however this balance is fully provided against. During the year, the Group has incurred cash costs of £1.7m in respect of the costs of litigation associated with the performance guarantees. The Group is carrying a remaining provision of £2.2m in respect of the two outstanding performance guarantees, amounting to £3.9m, resulting in a residual contingent liability of £1.7m. Mears does not believe that there is any justification for the guarantee holders making a call on these guarantees, given that the contracts to which they are attached were concluded several years ago. However Mears is also mindful of the challenges in managing this process in a country that follows very different legal and business practices. Mears believes the current position is sufficiently conservative, however if both bonds were to be called, and in the event that Mears recovered none of the debtor balance owed, this would result in a further loss to be recognised of £1.7m. This provision of £2.2m is reported within other creditors. The £1.7m is disclosed as a contingent liability.

Earnings per share (EPS)

	2018 p	2017 p	Change %
Diluted earnings per share*	22.91	20.10	+14%
Normalised diluted earnings per share*	29.06	28.05	+4%

*Continuing activities

The weighted average number of shares for EPS purposes was 105.1m (2017: 104.0m). The increase is predominantly due to the issue of c. 6.8 million shares in November 2018 in relation to the acquisition of MPS, the effect of which is pro-rated for the part-year following issue.

The statutory diluted EPS measure allows for the potential dilutive impact of outstanding share options and reflects the exceptional loss reported in through discontinued activities. The normalised diluted EPS increased by 4% to 29.06p (2017: 28.05p). Normalised earnings are based upon continuing activities before the amortisation of acquisition intangibles together with an adjustment to reflect a full tax charge of 19.0% (2017: 19.3%). We believe that this normalised diluted EPS measure better allows the assessment of operational performance, the analysis of trends over time, the comparison of different businesses and the projection of future performance.

Cash flow and net debt

As referenced in the Chief Executive Review, the Board recognises that operating cash performance is an area which requires improvement. When the business was simply Housing Maintenance and Care, cash movements were relatively predictable and whilst the focus on the cash balance on any single day was perhaps simplistic, nevertheless the position at the interim and year end date was viewed as a key performance metric.

As the business has evolved, this single day position has become less appropriate and relevant. The Housing Development activities do not generate uniform cash flows and the timing of payments can also have a significant impact upon the period end metric. Accordingly, this is why the Group has consistently ensured that its daily average debt measure is also disclosed. The average daily net debt will be used as the primary performance measure going forwards.

The average daily net debt for the year, excluding the property acquisition facility, was £113.2m, narrowly behind the target of £110.0m set at the start of the year. The net debt at the year end was £65.9m (2017: £25.8m). The property acquisition debt at the year end was £15.0m (2017: £13.9m), with an average balance of £24.0m (2017: £1.2m) in the year.

£210.3m

Net Assets

£0.7mCorporation tax
inflow following
adaption of IFRS15

Mears has always fostered a strong 'cash culture', whereby the Group operations understand that invoicing and cash collection are intrinsically linked and that works are not complete until the sales cycle is completed. While the headline cash metrics in recent periods have not been as good as the business would like, our core activities continue to utilise working capital at relatively low levels. It is pleasing that the average receivables outstanding through 2018 showed a reduction in the three high volume activities of Maintenance, Management and Care.

This demonstrates our operations have good controls and robust disciplines, supported by IT systems. As discussed in the Chief Executive Review, the working capital absorbed within the Development activity has been a challenge in the year with average receivables increasing to £21.2m (2017: £9.5m). The Development receivables balance outstanding at 31 December 2018 was £33.3m which was much of the cause for the average debt being narrowly higher than target and the cash flow generated from operating activities being low.

	2018 – 12-month average			2017 – 12-month average		
	Receivables £m	Payables £m	Net working capital £m	Receivables £m	Payables £m	Net working capital £m
Maintenance	123.2	(104.2)	19.0	125.7	(116.4)	9.3
Management	21.0	(19.3)	1.7	21.6	(21.0)	0.5
Development	21.2	(5.6)	15.6	9.5	(2.7)	6.7
Care	19.0	(5.4)	13.6	21.7	(8.3)	13.5
Total	184.4	(134.5)	49.9	178.5	(148.5)	30.0

A summary of the consolidated cash flow is detailed below together with explanations in respect of the major movements

	2018 £m	2017 £m	Note
Operating profit	30.8	28.5	
Amortisation of acquisition intangibles	4.4	10.6	
Depreciation and amortisation	8.2	8.3	1
EBITDA	43.4	47.4	
Other adjustments	0.6	(0.1)	
Change in inventories	(11.0)	(7.5)	2
Change in operating receivables	(13.9)	(0.1)	
Change in operating payables	(17.5)	(11.0)	3
Cash inflow from operating activities	1.6	28.7	
Taxes paid	0.7	(3.8)	4
Cash outflow from discontinued operations	(1.6)	(9.4)	5
Capital expenditure	(10.8)	(9.2)	6
Purchase of subsidiary undertakings	(37.8)	(5.0)	7
Issue of shares	22.1	1.9	8
Dividends	(13.1)	(12.7)	9
Interest received / (paid)	(3.2)	(2.2)	
Other financing and investing activities	2.0	(1.6)	10
Change in net debt	(40.1)	(13.4)	
Opening net debt	(25.8)	(12.4)	
Closing net debt	(65.9)	(25.8)	

The major movements in the year are:

- 1 Depreciation of £5.8m, amortisation of other intangible assets of £2.4m and share based payments of £0.6m
- 2 The outflow in respect of inventories is entirely due to working capital absorbed in Housing Development activities
- 3 The change in operating payables reflects both the changing sales mix and good payment practices
- 4 Relates to the corporation tax deduction in respect of IFRS 15, resulting in a refund of corporation tax previously paid
- 5 Legal and other professional costs incurred in the year in relation to the discontinued M&E activity based in the UAE. There was no impact to the income statement. Due to release of a provision attached to performance guarantee
- 6 Tangible fixed asset additions of £8.7m (2017: £8.1m) and IT development costs of £3.1m (2017: £3.7m) however the cash flow statement only reports the cash flows attached to this expenditure and therefore differs from the balance sheet additions which are recognised on an accruals basis
- 7 Initial consideration of £22.5m in respect of the acquisition of MPS and deferred consideration of £11.1m in respect of Omega
- 8 Primarily the equity placing associated with the acquisition of MPS, £22.5m was raised less costs and a small number of share options exercised during the period
- 9 The £12.5m paid to Mears shareholders and £0.6m paid in respect of non-controlling interests
- 10 Property assets held for resale, loans to other entities, and discharges of finance lease liabilities

Balance sheet

A summary of the Group Balance Sheet is detailed below together with explanations in respect of the most significant balances and the major movements

	Reported 2018 £m	MPS acquisition £m	Pre-MPS 2018 £m	2017 as restated £m	Adjustments for IFRS 9 & 15 £m	2017 as reported £m	Note
Goodwill and intangible assets	228.6	(21.5)	207.1	210.9	—	210.9	1
Property, plant and equipment	25.0	(0.3)	24.7	22.0	—	22.0	2
Inventories	29.8	—	29.8	18.7	—	18.7	3
Trade receivables	178.2	(37.6)	140.6	122.0	(31.6)	153.6	3
Property assets held for resale	12.4	—	12.4	13.9	—	13.9	5
Trade payables	(180.4)	2.7	(152.7)	(167.8)	—	(167.8)	4
Operating net debt	(65.9)	2.8	(63.1)	(25.8)	—	(25.8)	
Property acquisition facility	(15.0)	—	(15.0)	(13.9)	—	(13.9)	5
Deferred consideration	(2.0)	2.0	0.0	(11.1)	—	(11.1)	6
Other payables	(12.4)	—	(12.4)	(10.6)	—	(10.6)	7
Net pension	13.6	—	13.6	22.3	—	22.3	8
Taxation	(1.6)	3.4	1.8	3.3	6.0	(2.7)	
Net assets	210.3	(23.5)	186.8	183.9	(25.6)	209.6	

The major movements in the year were:

- 1 The carrying value of goodwill of £197.1m (2017: £193.6m) is not amortised but is reviewed for impairment on an annual basis or more frequently where there is an indication of impairment. The headroom between the carrying value of the Care asset and anticipated future value that will be delivered by the Care division has been low over a number of years. The increase in goodwill during the period relates to the acquisition of MPS.
- 2 Group capital expenditure of £8.7m (2017: £8.1m) includes an addition during the year of £3.6m (2017: £nil) relating to the development of 70 modular homes which are currently under construction which, upon completion, will be used to deliver a homelessness solution within our Housing Management activities. The homes are expected to be completed in November 2019 at a total cost of £5.8m. Mears is looking for a long term funder to acquire these properties upon completion. A further £2.0m is expected to be capitalised during 2019. Excluding the investment in modular homes, the remaining expenditure of £5.1m (2017: £8.1m) relates to IT hardware, other office equipment and the refurbishment of new office premises. The level of capital expenditure in respect of property, plant and equipment in any single year has a close correlation to the number of new contracts mobilised in that period. The low level of investment in 2018 reflects a quiet period of new contract mobilisations.

£20.6m

taxes incurred and paid to HMRC

£95.6m

taxes collected and paid to HMRC

In addition, intangible assets includes the capitalisation of expenditure incurred on developing our in-house IT platform. Additions in the year amounted to £3.1m (2017: £3.7m) with a carrying value of £8.4m (2017: £7.7m), which is amortised over five years. Having made significant investment in our IT systems over a number of years, we are starting to see a reduction in our development expenditure moving forward and this is reflected in the 2018 amounts.

The majority of plant utilised by our operational teams is subject to short-term hire arrangements and motor vehicles are subject to operating leases, hence neither are included within capital expenditure or recognised as an asset within the balance sheet. Similarly, the Housing Management business has a large number of short-term property leases which are similarly not carried on the balance sheet. The new accounting standard, IFRS 16 Leases, will impact upon this treatment as discussed below.

- 3 Trade receivables and inventories increased to £208.0m (2017: £172.3m). This predominantly relates to an increase in working capital associated with the Housing Development activities which accounts for an increase of £20.7m. The IFRS15 adjustment resulted in a reduction of £31.4m whilst balances acquired on the acquisition of MPS resulted in an increase of £37.6m.
- 4 Trade payables reported an increase to £180.4m (2017: £167.8m), however the acquisition of MPS brought a balance of £277m. As such, there was an underlying reduction in payables by £16.2m reflecting changing sales mix and good payment practice.
- 5 The Group has secured a property acquisition credit facility of £30m to acquire and build portfolios for resale. At 31 December 2018, assets held for resale utilising this facility amounted to £12.4m (2017: £13.9m). At 31 December 2018, the associated draw-down for these acquisitions was £15.0m (2017: £13.9m), funding both these assets for re-sale together with also part-funding the modular homes included within fixed assets as discussed above.

- 6 In January 2018, deferred consideration of £11.1m was paid in full and final settlement of all deferred consideration relating to the acquisition of Omega in 2014. The balance at 31 December 2018 relates to the contingent consideration in respect of the acquisition of MPS and, subject to performance, would be due for settlement in 2021.
- 7 Other payables predominantly relates to provision for expected losses in relation to the insurance captive which manages the Group's insurance risks. Finance lease liabilities are also included within this category.
- 8 The Group participates in two principal Group pension schemes (2017: two) together with a further 28 (2017: 28) individual defined benefit schemes where the Group has received Admitted Body status in a Local Government Pension Scheme (LGPS).

The Group holds a number of pension arrangements with Local Government Pension Schemes. The accounting treatment for these schemes follows the guidelines set for defined benefit schemes. This does not present the commercial reality for a number of our LGPS arrangements, where the Group holds back-to-back indemnities from its clients in respect of both its exposure to changes in pension contribution rates and to future deficit risk. These have been identified in the table below as 'limited risk'. For the remaining LGPS arrangements where the Group does not benefit from indemnities, the risks attaching to these schemes matches the time horizon of the underlying contract which, whilst not removing all risks, does reduce the period over which a deficit can arise. This second category has been identified in the table below as 'medium term'. The Group schemes are typical defined benefit arrangements where the Group is ultimately responsible for any deficit resulting from movements in discount rates, interest rates, mortality rates and investment performance. This last category has been classified as 'long-term'.

	Group schemes (no indemnity) long-term	LGPS schemes (no indemnity) medium-term	LGPS (indemnified) limited-risk	Total
Number of schemes	2	13	15	30
Assets £m	152.9	62.1	217.5	432.5
Liabilities £m	(136.5)	(64.9)	(217.5)	(418.9)
Net surplus/(deficit) £m	16.4	(2.8)	--	13.6

£13.6m

pension net surplus

£25.6m

opening reserves
adjustment resulting
from adoption of
IFRS 9 and 15

Changes to accounting standards

IFRS 9 'Financial Instruments'

In respect of IFRS 9, Mears does not hold complex financial instruments and the impact of this standard on its hedging instruments is not material. However, included within financial assets are trade and other receivables. From 1 January 2018, Mears is required to recognise a loss allowance for expected credit losses on these financial assets. The new standard states that if the credit risk on a financial instrument has significantly increased since initial recognition, the loss allowance must be measured using the lifetime expected credit loss.

Given the significant majority of our invoicing is to public sector clients, assessed to have a very low credit risk, expected credit losses to this customer type are deemed to be negligible. However, Mears provides regulated services to private individuals in both its Housing and Care businesses and, as such, services cannot immediately be withdrawn when the Group becomes aware of an increased credit risk. Mears has both a moral and legal obligation to continue to provide services whilst alternative arrangements are being made for these service users.

The difference between the previous carrying amount and the carrying amount at the beginning of the reporting period under IFRS 9 is recognised as an adjustment to the opening balance of equity. The impact of this change at 1 January 2018 is a reduction in the opening balance of equity of £2.3m.

IFRS 15 'Revenue from Contracts with Customers'

IFRS 15 changes the timing of recognising revenue and costs in respect of certain long-term contracts. In the case of the large majority of our contracts, the accounting methodology will be unchanged. Mears has typically looked to recognise revenue and cost at the individual works order level, whether that be a singular maintenance order or care visit. This has ensured that the valuation of working capital balances is straightforward and contains fewer areas of significant judgment.

However, there are a small number of arrangements where the Group has accounted for multiple service contracts by treating them as a single supply of a service. This occurs where local contract mechanics were not easily aligned with the commercial framework of the contract. The new accounting standard requires Mears to allocate the total transaction price to each distinct performance obligation. In addition, a number of contracts include variable consideration, where revenue and profit are linked to the achievement of performance targets and milestones. The new standard requires more detailed analysis in determining the appropriate timing of recognising this revenue.

IFRS 15 has been applied using the modified retrospective approach on transition which results in an adjustment to the opening balance of equity at 1 January 2018 and no restatement of the prior period. The impact of this change in 2018 will see a reduction in the opening balance of equity of £23.9m. The change to IFRS 15 has no impact on the lifetime profitability of the contracts and there are no cash flow impacts, although the change will drive better alignment between the timing of profit recognition and its associated cash flow. Moving forward, it is expected to have a positive impact in respect of operating profit from 2018 through to 2027, as performance obligations are satisfied. The impact of adopting IFRS 15 has been to increase the operating result for 2018 by £0.9m.

IFRS 16 'Leases'

The new leasing standard, IFRS 16 Leases, is effective from 1 January 2019 and will have a significant impact on the Group's Balance Sheet, principally due to the use of leased vehicles and residential property for the operational delivery of Housing Maintenance and Housing Management. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is under 12 months or the underlying asset is of a low value.

The Group will use the modified retrospective transition method on adoption. Under this method, the asset is calculated as if IFRS 16 had always been applied, however the liability is calculated as if all leases start on 1 January 2019, which will result in no change to comparative numbers but an adjustment within the reserves of the Group.

Under IFRS 16, a lessee will recognise its right to use a leased asset and a lease liability representing its obligation to make lease payments. The depreciation cost of the newly recognised 'right of use' lease asset will be charged to profit within administrative costs, whilst the interest cost of the newly recognised lease liability will be charged to net finance costs. On the basis that depreciation is required to be charged on a straight-line basis, whilst the interest element is charged on a reducing balance basis, this results in a higher charge being applied to the income statement in the early years of a lease, with this impact reversing over the later years. The profit impact over the life of a lease is neutral and IFRS 16 has no cash impact.

The Group is in the process of finalising its work in applying the new requirements of IFRS 16. As a result, it is possible that there may be changes to estimates and judgement used in applying this new standard. These will be finalised prior to the release of the Group's 2019 interim results later in the year.

The current estimate of the impact of IFRS 16 to the Group, at the point of transition, is detailed below

- 1 From a balance sheet perspective, the transitional adjustment will see a right of use asset recognised of c £118m, and an associated lease liability of c £125m, being the present value of future lease payments. The net liability being recognised on transition results in an adjustment to opening reserves.
- 2 In terms of the income statement, and based on the existing business at the date of transition, the impact will be an increase to EBITDA by in the region of £35.0m per year, as the operating lease charge previously applied is replaced by a depreciation charge applied on a straight line basis to the right of use asset. The impact to PBT is expected to be broadly neutral as leases reach maturity, however the impact is not linear due to increased lease liability interest cost in earlier years of leases, and this will result in a small reduction in profit in 2019 with this impact unwinding in later periods.

The adoption of IFRS 16 is particularly relevant to the Group's new AASC contract which will see the Group enter into around 4,500 residential property leases. It is not possible to estimate the balance sheet impact without an accurate assessment of the mix of lease lengths. However, as detailed above, the impact of IFRS 16 on profits from a contract of this nature is that profit generated in the early years of the contract will be reduced by a higher interest cost. However IFRS 16 should not be considered in isolation. Securing good quality properties, cost effectively over the long-term is a key element of delivering operational outperformance and increasing the financial return.

Delivering social value in practice

Our strategy

For us, social value is not something we simply pay lip service to. It is part of our DNA, completely embedded in everything we do. We work in some of the most socially deprived areas of the country and we feel a strong sense of responsibility towards finding ways to improve the long-term prospects of the people who live in these communities that make a real and positive difference to people's lives.

Highlights

2018: A year of growth

We have been recognised as an organisation which is delivering on the social responsibility agenda, but we are never content to rest. During 2018, we increased the number of social value projects we are engaged in by 10% and continued to develop our strategy and framework to ensure social value is truly embedded in the Mears culture

At a strategic level, we see social value as part of the 'Red Thread' that binds Mears employees together and defines the values and behaviours we exhibit as we go about our daily work. Our employees set high standards, focusing not just on providing customer service excellence but also on acting as role models. We believe that these values are not predicated by academic achievement or social position, but instead are influenced by attitude, character and the strong work ethic of our teams.

This is translated into practical action which delivers outcomes through a framework of approaches to effectively engage with communities on the ground and robust mechanisms for measuring the social impact that is created.

Our goals

Our work continues to be aligned to our four Mears' Social Value Priorities:

1. Fair for all



Reducing prejudice, improving understanding of differences, supporting social inclusion

2. Championing local



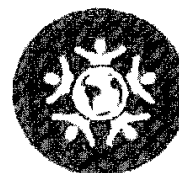
Improving the wellbeing of people and the communities we serve

3. Creating chances



Providing career, skills and employment opportunities

4. Healthy planet



Making a positive contribution to our planet

Our governance

How do we ensure we continue to do the right things?

To drive social value throughout the business, we continue to operate our Social Value Board, which is endorsed and chaired by our Executive Management Team. Our Social Value Board ensures we take a strategic approach to corporate social responsibility and embed it into every area of our business. The board is endorsed by three external experts whose role it is to challenge us to drive forward our social value agenda and to hold us to account.

Going forward

Focus areas for the Social Value Board in 2018 and beyond

- ~ Ensuring measurement continues to be relevant and real. Measuring the right things within the social value framework is key, to drive outcomes and impacts that are real and long lasting.
- ~ Making a real impact through the Group brand, to reinforce Mears as a leading socially responsible business. 2019 will see us building on this through a series of national theme campaigns developed with the members, demonstrating the overarching work of the Group on employability, wellbeing, diversity and inclusion.

Meet our Social Value Board external experts



Richard Kennedy

Richard is chair of the board for Social Value UK and co-chair of Social Value International.



Mears Group is an organisation which truly understands the importance of the social value they create both through their core business and community activities. In my opinion this will future proof the business for shareholders, customers, and the communities in which Mears operates.



Keith Edwards

Keith is the lead associate for the Housing Quality Network in Wales and author of several reports for local authorities, national bodies and the Welsh Government, and previously Director of the Chartered Institute of Housing (CIH) Cymru for 14 years.



In my book we need to take a longer-term view and make sure that what we do has a positive impact on people and communities. I think Mears gets this and that's why I am pleased to be part of the Social Value Board.



Barry Malki

Barry is Head of Communities for HACT, an innovation agency supporting the housing sector. Outside of this he serves on the boards of several youth charities and acts as a speaker for Save the Children.





I hope that by working with Mears as part of its Social Value Board, we can steer the business to maximise the benefits to the communities in which it operates.

Strategic report
Social value and impact continued

Non-financial statement

We aim to comply with the Non-Financial Reporting requirements contained in sections 414CA and 414CB of the Companies Act of 2006. The below table and information it refers to is intended to help stakeholders understand our position on key non-financial matters.

Commitments	Community commitment	Environmental matters	Human rights, anti-corruption and anti-bribery
Policies and diligence	<p>We have a clear social value plan with four strategic priorities.</p> <ol style="list-style-type: none"> 1. Fair for all: Reducing prejudice, improving understanding of differences, supporting social inclusion 2. Championing local. Improving the wellbeing of people and the communities we serve. 3. Creating chances. Providing career, skills and employment opportunities. 4. Healthy planet. Making a positive contribution to our planet. <p>We have a Social Value Board with independent Directors.</p>	<p>Mears recognises and is fully committed to reduce its impact on the environment.</p> <p>We are determined to minimise our carbon footprint and minimise waste to landfill.</p> <p>We have a commitment to reduce landfill by 5% per year and to achieve or exceed a diversion rate of waste from landfill of 95%.</p> <p>Our policies include:</p> <ul style="list-style-type: none"> ~ delivering environmental supply chain. ~ fleet environmental policy. ~ environmental reporting. 	<p>Our policies include:</p> <ul style="list-style-type: none"> ~ modern slavery and human trafficking; ~ preventing engagement of child labour; ~ whistleblowing policy; ~ anti-bribery, and ~ gender equality
Status	<p>In 2018 we generated in excess of £24m in social value.</p> <p>Mears Group has been recognised for its outstanding environmental, social and governance practices by gaining a place in the FTSE4Good Index – which places Mears in the top 9% of companies in the index which measures commitment to environmental, social and governance practices.</p>	<p>We have set environmental targets to reduce our waste to landfill each year and we are currently achieving over 95%. Our water/effluent discharge is only through our offices and on-site colleagues. Mears Group PLC does not release water by any other source.</p> <p>In 2018 we recycled 31,698 tonnes of waste, a diversion from landfill of 95.88%.</p> <p>Mears Group has full visibility of its waste disposal processes across the whole company, including our subcontractors.</p>	<p>Mears is proud of our Social Mobility Champion status, creating opportunities and enabling people to develop new skills in some of the most disadvantaged and marginalised communities in the UK.</p> <p>We are committed to ensuring that there is no modern slavery or human trafficking in our supply chains or in any part of our business. We are committed to acting ethically and with integrity in all our business relationships, and implementing and enforcing effective systems and controls.</p>
Description of principal risks and impact of business activity	 Read more on pages 30–31		
Non-financial key performance indicators	 Read more on pages 30–31		
Business model	 Read more on pages 30–31		

Employees

We want to be a great place to work and to place our colleagues at the very heart of what we do.

Our policies include.

- ~ whistleblowing;
- ~ family friendly;
- ~ safeguarding;
- ~ equality, diversity and inclusion; and
- ~ approach to labour standards compliance.

Mears aims to be a great place to work and we have recently been awarded a place in the 25 Best Big Companies to Work For in conjunction with the Sunday Times. We are accredited as an Investor in People and have been awarded Diversity Network Accreditation.

Our employees are at the heart of our business and we provide staff benefits, a commitment to a transparent pay policy and a commitment to training and development.

Red Thread

Wearing the Mears badge carries a lot of responsibility. All Mears colleagues are bound by a common set of behaviours. We call this the Red Thread. It is in our DNA and it helps us achieve more as individuals, as a team, and as a company.

- ~ Motivation: There are no limits; we can all reach our personal goals and aspirations. Individually and collectively we can deliver the services our customers expect a little bit better every day
- ~ Empowerment: Great leaders are not born; they grow. We urge employees to take the initiative, take ownership and take responsibility, and support them every step of the way.
- ~ Customer focus: It is very simple; we are here to serve. The success of Mears is built on 360-degree service and appreciating that the needs of clients and customers are complex and multi-dimensional.
- ~ Role models. Everyone who represents the Company is expected to lead by example, whether they are looking after vulnerable people or making sure the homes of elderly tenants are properly maintained
- ~ High standards. We set industry-wide standards and encourage everyone to work hard, present themselves well and keep raising the bar. If we do, success is guaranteed

Health and safety

We aim to be industry leaders in creating a safe working environment.

Mears operates a full health and safety training programme. We fully monitor accident frequency rates and have a proud record on safety within our workplaces and contracts.

Our policies include:

- ~ reducing accidents by 10% per year,
- ~ implementing a behavioural safety and change programme; and
- ~ increasing near miss reporting

In 2018 we reduced Accidents Rates by over 10% and achieved the RoSPA Highly Commended Industry Sector Award (16 consecutive Golds), for our continued commitment to accident and ill-health prevention.

We successfully continued our certification to ISO 9001, ISO 14001 and OHSAS 18001. We also attained a diversion to landfill of over 95%.

Over the year we have carried out over 50,000 hours of training to ensure we continue our commitment to improving the skills and awareness of all employees.

We continue to improve our working practices and monitoring regimes to ensure that we continue to improve and look at additional ways in which to create a safer and environmentally friendly environment for all of our employees and partners to work.

In 2019 we will continue to challenge our standards and look to continuously improve the safety environment for all of our employees.



Felix Road charity

Delivering social value in practice

Mears Foundation

The Mears Foundation is chaired by Bob Holt, former Chairman of Mears Group PLC, with committed support from nominated board members from across the business. It was established to help improve the lives of young people, vulnerable groups, the elderly and those with significant health issues, in the UK and abroad, through practical help, support and intervention. It aims to provide support through volunteering and hands on help for nominated causes, not just financial support. This year, teams across the Group have been taking part in a variety of events, specifically focusing on social isolation.

Making a difference: Who has benefitted?

Silver Surfer Computer Club

This club supports service users to develop basic computer and internet skills to enable them to surf the net, shop online, access social networks, hobbies and interests and support groups.

The idea came about when a member of staff purchased a laptop for his 82 year old father. He realised that there was no support available to help him learn the basics of how to use the computer or the internet. Our staff member provided the support himself, helping his father become proficient, even develop a following on Facebook! Seeing the impact this has had on his father's life, the staff member wanted to provide the same benefit to other residents of Mears' extra care schemes.

The project aims to utilise the skills of the Mears IT team to provide a helpline which provides basic IT advice and support. Longer term, it hopes to work in collaboration with a charity such as Alzheimer's Society to develop the use of assistive technology to try and help people with memory loss.

iPads for Young Bristol

Mears Foundation delivered iPads for Young Bristol, a youth-driven charity working in the city.

Party time for Meet and Mingle, Stowmarket

The Mears Foundation generously donated £500 to the Mears Care, Stowmarket's Meet and Mingle group. This group was set up to help with social isolation in the local community, over the last few years day centres have been closing so this group has been a big asset to the community.

Felix Road charity

The Mears Foundation delivered a cheque to the Felix Road charity to support its adventure playground project. The charity opens the playground for children to use for free and runs self-defence and martial arts classes for children and adults.

Social value at Mears

Nothing demonstrates the way we are delivering social value like the real stories of how our work is impacting people and communities on the ground. The following pages describe our approach and tell just some of the stories of how we are delivering social value under each of our four priority areas.



Focus on: Fair for all

Reducing prejudice, improving understanding of differences, supporting social inclusion

Our commitment and approach to diversity and inclusion:

Addressing the shortage of women in trades

A staggering 99% of tradespeople are male; this does not look set to change any time soon with low numbers of women taking up apprenticeships in this area. At Mears we are working to address the issue, along with our social housing partners, through our Tradeswomen into Maintenance project which is working with women to identify the barriers to getting and retaining jobs in Repairs and Maintenance, raise awareness about the opportunities available to women in the sector, and support women already employed in trades roles.

Sarah's story

Sarah Bull is an apprentice plumber working for Celtic Horizons, in partnership with United Welsh

"I've always enjoyed manual work and plumbing, but I never thought it was possible because I had never seen a woman plumber," she said

"I attended college, working towards level 1 and instantly loved everything about plumbing. While completing level 2, I was lucky enough to get an apprenticeship with Celtic Horizons. While at Celtic Horizons, I have also had the opportunity to be a Tradeswoman Ambassador for the Tradeswomen into Maintenance project."

Gender diversity table

	Male	Female
2017		
Board	8	3
Senior Manager	24	7
Employee	5,222	6,353
2018		
Board	8	3
Senior Manager	26	8
Employee	4,789	5,304



I've always enjoyed manual work and plumbing, but I never thought it was possible because I had never seen a woman plumber.

Sarah Bull
Apprentice plumber





Focus on: Fair for all *continued*

Inclusive Culture Pledge marks Mears' commitment to prioritise diversity and inclusion

Mears is a committed member of leading companies from the energy, transport, engineering and creative sectors in taking the Inclusive Culture Pledge, overseen by leading diversity consultancy EW Group.

We work in some of the most diverse communities in the UK and we believe we are stronger in every way when our workforce fully reflects those communities. The pledge helps us to focus on five areas of diversity and inclusion development: leadership, people, data, brand and future, providing a framework to build on the work we are already doing to improve equality and diversity across the business. 2018 saw a business-wide training focus on all managers and senior colleagues attending a diversity and inclusion training and awareness course

Gary Jackson, Group Director of Communications & Customer Success, said, "We are a national Social Mobility Champion and, as such, we have a responsibility to support and promote good practice in diversity and inclusion, which is a fundamental enabler to greater social mobility. Over the next 12 months, we are building on the work of 2018 to make colleagues further aware and actively involved in helping to improve diversity and inclusion through every level of our work. Our accreditation reports from 2018 will provide an ideal opportunity for us to build on our good practice, while challenging us to do more where we need to."

Mears supports Alzheimer's Society Dementia-Friendly Housing Charter

Mears has signed up to the Dementia-Friendly Housing Charter. This charter seeks to make the housing sector – including housing organisations, corporate bodies and sector professionals – aware of the challenges of living with dementia so that it can improve home environments for people with the condition

Gary Jackson, Group Director of Communications & Customer Success, said, "By becoming a more dementia-friendly provider, we will be able to support and help people to stay in the setting of their choice for as long as possible, and by understanding the condition, we can make a huge difference to people living with dementia and their quality of life."

YourMK team volunteering to support Mind

During the summer, colleagues from YourMK – our regeneration partnership with Milton Keynes Council – spent the day volunteering alongside residents and staff from the local branch of Mind to make improvements to a community garden.

The mental health charity uses the garden each week to run wellbeing and support sessions for a group of local people, but the garden needed some TLC to get it ready for the autumn. Colleagues from Mears' Gas Planning and Customer Success teams went along to prune, dig, paint and gravel areas of the garden, working hard to get it in top shape for the local group.



The interest YourMK has shown in volunteering with the group has given them a great sense of pride. The help offered has made the group feel valued and recognised. It has enabled the larger jobs to be completed and we can now look forward to planning the garden for next year.

Sue Varley
Group leader



YourMK team
volunteering to
support MIND



Focus on: Championing local

Improving the wellbeing of people and the communities we serve

We work closely with our partners and clients to identify local social value projects to get involved in

This local approach makes all the difference. Through the development of branch social value plans, we can push the boundaries to deliver real impact, enabling individuals and the communities in which we operate to flourish and thrive.

Food-wise classes in Lambeth

Wellbeing is a key focus, so a recent project to deliver food budgeting, cooking and nutrition classes in Lambeth was a great success, with groups coming together to learn some key skills to support their lifestyle, making healthy meals for only £1.00.

Art sessions are a hit with young and old

A new project running at Blaise Weston Court in Bristol is using art to bridge the generation gap between members of the local community.

Since it started in October, the Paint Pals project has been bringing together the older residents of the care scheme and young people from Torwood House School each month to work together to produce beautiful works of art.

The project was started with a £1,500 grant from the Bristol Ageing Better Community Kick-Start Fund. Members of the Blaise Weston Social Club applied for the money, which will pay for a year of monthly art sessions, culminating in an exhibition of the works later this year. Beyond this, the group hopes to find additional funds to continue the project into the future.

Bridging the generation gap



Learning key skills

Supporting the homeless in Glasgow

Our Glasgow branch decided to help and support the homeless people in Glasgow for many reasons. But one event really brought it to life for us.

James's story

James, one of our carers working in Glasgow, was supporting a wheelchair service user one day when he found himself in a situation in a busy Glasgow street where the wheel had come off the wheelchair and he was struggling to get help.

The service user himself was unable to help because of his lack of mobility and the pair watched as numerous people just passed by. This was very distressing for James as he knew he was not able to fix the chair alone and if they were to remain in this situation, the service user would have been at risk of harm.

Then one person did stop; a young homeless man who came over and helped James re-align the wheel on the wheelchair and then walked the pair to the taxi rank to ensure that no further help was needed. He even offered James the £5 note he was carrying to help pay for the taxi fare to take the service user home. James thanked him but declined the offer of money.

This made us all think: why had only the vulnerable homeless person stopped? And what could we do as a branch to help repay the kindness of this person?

So, we decided to support two small local charities that work with people who are homeless: All 2 together now and H4TH (Help for the Homeless).

Fundraising, donated clothing, sleeping bags and toiletries poured in from the teams to help support the two charities and the people of Glasgow.

Over 100 winter survival packs, which will help people living on the streets to get through the Scottish winter were purchased from donations and fund raising.



Focus on: Creating chances



Providing career, skills and employment opportunities

Creating chances

Mears works in some of the most marginalised communities in the UK. We recognise that we can make a positive difference by creating chances for learning and career development, providing individuals in those communities with entry routes into employment.

Over the last 12 months, Mears has developed and implemented programmes to upskill the existing Mears workforce as well as individuals living in the local community who are not employed by Mears

Heather Hughes, Head of Training and Development, said, "I am delighted to see Mears has made a difference to peoples' lives and provided new opportunities; it's an incredibly worthwhile investment

"Our training facilities and resources have been used by various stakeholders in local communities for wide-ranging apprenticeships and other courses, enabling so many people to progress. It has been great to see the diversity of programmes we have on offer, and the innovative work to address the under-representation of women in construction."

Chief Executive Officer David Miles says there are clear business benefits for investing in apprentices.

"It's a great way of growing our own talent within the business," he says "Our apprentices bring fresh ideas and enthusiasm and keep our qualified staff up to date with modern technology and practices. The result is a highly skilled, loyal workforce, trained to work in the Mears way. Ultimately, that helps us to deliver the very best service to our customers". David goes on to explain that Mears' drive for running apprenticeship programmes is not confined to business outcomes:



We work in some of the most marginalised communities in the country. At the heart of everything we do is the desire to make a positive difference in those communities. Giving people the opportunity to learn a skill and build a career is a great way to do that.

David Miles
Chief Executive Officer



Focus on: Healthy planet



Skilled workforce trained to work in the Mears way

Making a positive contribution to our planet

Mears is responsible for the maintenance of 15% of all social housing in the UK – more than 700,000 homes. We visit more than 30,000 people several times a week to deliver care and support in their homes. We recognise we have a big responsibility to minimise the environmental impact of our activities. For an organisation of our size, even small changes can deliver big impacts.

Mears' approach to positively impact supply chain environmental value

Delivering social value with our supply partners

At Mears, we believe we are more effective in delivering social value where we can share resources, skills, experience and financial support with our supply partners. To ensure a consistent approach throughout our supply chain, we expect our suppliers to have or adopt similar business principles to our own. Our suppliers are required to acknowledge the significance of social, environmental and ethical matters in their conduct and must have a commitment to working towards improving quality standards and performance in these areas.

Above all, we expect suppliers to be able to demonstrate compliance with all the UK, EU and international legislation that applies to business operations from modern slavery, anti-bribery and health, safety and wellbeing laws to product specific regulations.

Social value: what is the future agenda focus?

Whilst the Public Services (Social Value) Act 2012 is making a difference, with a greater proportion of public sector procurement spend being shaped by the Act and increased focus from organisations to support individuals, local communities and economies, more can be done.

2018 announcements from the Minister for the Cabinet Office say the Act will be extended to ensure that all Government departments explicitly evaluate social value when commissioning services, as opposed to considering social value when awarding Central Government contracts. This provides a positive indicator for later extension to Local Government contracts and the public sector to follow.

The Social Housing Green Paper provided a sound platform for the voice and engagement of residents to come back to the fore, in shaping and responding to service in their communities – again, a further positive move to progressing the social value agenda.

Mears is excited by these positive indicators and has already started to put plans into place to actively and continually deliver more impact, at a national and local level, through our social value activities.

We are proud of our reputation as a company that makes a POSITIVE difference; enabling individuals and communities to flourish and thrive.

Together we really can make Mears a better business.



We work closely with our suppliers, who see this as a great opportunity to collaboratively invest for the improvement of our communities. We have a commitment to continuously increase the number of local SME subcontractors on our approved list, ensuring that a proportion of contract spend remains within the local economy by supporting increased revenue generation and increasing employment opportunities.

Ian Watson
Procurement Director

The strategic report from pages 1 to pages 63 was approved by the board and signed on its behalf by.

D J Miles
Chief Executive Officer
22 March 2019

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Corporate governance

Introduction to corporate governance

An effective culture of governance



Kieran Murphy
Chairman

Dear shareholder,

On behalf of the Board, I am pleased to present my first corporate governance report for the year ended 31 December 2018. As in previous years, we report against the UK Corporate Governance Code (the 'Code') issued by the Financial Reporting Council (FRC). I am pleased to confirm that during 2018 we have fully complied with the provisions of the Code.

Effectiveness

The Board continues to set itself high standards of corporate governance. Our corporate governance report, issued within our Annual Report, details how we approach governance and the areas of focus for the Board in 2018 and into the future. The Board utilises the Group's established governance framework, based upon the Code, to support the operation of good governance practices throughout the Mears business.

In accordance with the Code, the performance of the Board, its Committees and individual Directors is evaluated on an annual basis, with the 2017 evaluation being externally facilitated.

Changes to the Board

At the 2018 Annual General Meeting (AGM), the Board said farewell to Peter Dicks, Non-Executive Director. Having reached nine years' service, Peter did not stand for re-election.

In July 2018, as part of the continuing evolution of the Board, the then Chairman, Bob Holt, indicated his intention to the Board not to stand for re-election at the 2019 AGM. The Board commenced a considered, competitive and structured process for the recruitment of the new Chairman and I was delighted to be offered the position during December 2018. I would like to place on record my thanks to Bob Holt, who joined the Group in 1995 shortly before its flotation for his many years of service.

Engage our workforce

In June 2018, the Company became one of the first listed companies in the UK to appoint an Employee Director, Amanda Hillerby, clearly underlining the Company's commitment to progressive business practice and corporate governance. Mears understands the vital role that our workforce plays in the success of the Group.

Succession

Under the Code, succession planning is one of the most important roles vested in non-executive directors. Your Board recognises this role wholeheartedly and this has been clearly demonstrated in recent years with your Board evolving steadily, reflecting the development of both the Company and its key operating markets, and bringing valuable relevant sector experience and knowledge to the Board.

The evolution and succession within the Mears boardroom has been a continuous process and one which the Company intends to continue in line with the Group's development.

Shareholder engagement

The Board continued to engage with shareholders in an open and meaningful way throughout 2018. Since my appointment, I have met with each of our major shareholders to understand their views and concerns. I have also been present at a Capital Markets Day, attended by all our major shareholders, hosted by the Chief Executive Officer. I hope shareholders take the opportunity to meet other Board members at the 2019 AGM.

K Murphy
Chairman
kieran.murphy@mearsgroup.co.uk
22 March 2019



In June 2018, the Company became one of the first listed companies in the UK to appoint an Employee Director, Amanda Hillerby, clearly underlining the Company's commitment to progressive business practice and corporate governance.

The right skills and experience to deliver our strategy



1. Kieran Murphy
Non-Executive Chairman

Age: 60

Tenure: 3 months

Skills and experience:

Kieran has spent much of his career working in finance, holding senior positions. At Kleinwort Benson, he built a market-leading corporate finance advisory business in the building and construction sector and became a member of the bank's Investment Bank Management Committee. More recently, at Gleacher Shacklock, the boutique corporate finance advisory firm, Kieran extended his advisory work into the business services sector.

Principal external appointments:

Aliaxis SA
Ordnance Survey
University of London

2. David J Miles
Chief Executive Officer

Age: 53

Tenure: 22 years (12 years on the Board)

Skills and experience:

David joined Mears in 1996 and, prior to his appointment to the Board in January 2007, was Managing Director of the Mears Social Housing division. Prior to joining Mears, David held a senior position with the Mitie Group. His background is in electrical engineering.

Principal external appointments:

None

3. Andrew C M Smith
Finance Director

Age: 46

Tenure: 19 years (12 years on the Board)

Skills and experience:

Andrew joined Mears in 1999 and, prior to his appointment to the Board, was Finance Director covering the Group's subsidiaries. Andrew qualified as a Chartered Accountant in 1994 and worked in professional practice prior to joining Mears.

Principal external appointments:

None

4. Jason Burt
Non-Executive Director

Age: 53

Tenure: 2 years

Skills and experience:

Jason was a senior partner at Plexus Law and has 32 years experience of defending complex regulatory prosecutions and employers' and public liability claims, bringing significant experience in the area of health and safety. Jason chairs a Health, Safety and Environment core group (Compliance Committee), driving good working and health and safety practices into the Group's governance structures. Jason is also a member of the Audit Committee.

Principal external appointments:

None

5. Roy Irwin
Non-Executive Deputy Chairman

Age: 64

Tenure: 2 years

Skills and experience:

Roy has significant experience in the social housing sector, having lately been Chief Inspector of the Audit Commission following a career of over 30 years in public sector housing. Since 2013, Roy has held the position of Non-Executive Chairman of Plexus and Omega Housing, being Mears' Registered Providers of social housing with the Regulator of Social Housing.

Principal external appointments:

None

6. Julia Unwin CBE
Non-Executive Director

Age: 62

Tenure: 3 years

Skills and experience:

Julia is former Chief Executive of the Joseph Rowntree Foundation and the Joseph Rowntree Housing Trust. She has significant experience in the housing and care sectors, having been a member of the Housing Corporation Board for ten years.

Principal external appointments:

Yorkshire Water Services Limited
Financial Reporting Council

7. Alan Long
Executive Director

Age: 56

Tenure: 13 years (9 years on the Board)

Skills and experience:

Alan joined Mears in 2005 and, prior to his appointment to the Board in August 2009, was Managing Director of the Group's Care division, having previously held the position of Group Sales and Marketing Director. Prior to joining Mears, Alan held senior roles at Britannia Building Society, Mars and Smith & Nephew.

Principal external appointments:

None

8. Geraint Davies CBE
Non-Executive Director

Age: 64

Tenure: 3 years

Skills and experience:

Geraint is a fellow member of the Institute of Chartered Accountants in England and Wales. He was previously a partner for a leading professional practice for over 25 years. His commercial experience includes working with Registered Social Landlords and a number of organisations in the healthcare sector.

Principal external appointments:

Cardiff International Airport Limited

9. Elizabeth F Corrado
Non-Executive Director

Age: 53

Tenure: 1 year

Skills and experience:

Elizabeth was until recently an Executive Director of the Power to Change charitable trust, with a focus on creating innovative projects in housing and energy, enabling investment into UK communities at scale and generating both financial and social returns for investors and local communities. Liz previously held senior positions in investment banking providing advice and structured finance to both the Government and a range of business sectors.

Principal external appointments:

None

10. Amanda L Hillerby
Employee Nominated
Non-Executive Director

Age: 30

Tenure: 9 months

Skills and experience:

Amanda has worked for the Group since 2011, commencing her career on the Group's graduate management programme during which she worked across all areas of the business including Care, Housing and Central Support. Amanda is currently delivering a national role of Quality Manager within the Care division.

Principal external appointments:

None

11. Ben Westran
Company Secretary

Age: 42

Tenure: 15 years

(4 years as Company Secretary)

Skills and experience:

Ben is a Chartered Accountant and, prior to his appointment as Company Secretary, was Group Financial Controller and Director of a number of the Group's subsidiaries. Ben joined the Group in 2004 having previously worked in professional practice.

Principal external appointments:

None

How the Board operates

The Board leads and provides strategic direction to the Group and carries ultimate responsibility for management of the Group's activities and financial performance. The Board acknowledges **accountability to shareholders for proper conduct of the business, and responsibility for the long-term success of the Group, having regard to the interests of all stakeholders.**

The Board's prime objective is to ensure the ongoing commercial and financial success of the Group. The Board provides entrepreneurial leadership of the Group within a sound and prudent risk management framework using effective internal control systems which enable risk to be assessed and managed. The Board sets the Group's strategic objectives, and the nature and extent of principal risks it is willing to take in achieving these strategic objectives, and ensures that the necessary financial and human resources are in place for the Group to meet these objectives. The Board sets the Group's values and standards, and ensures that the Group's obligations to its shareholders and others are understood and met.

Corporate governance framework

As a Board we aim to be sector leaders in our standards of corporate governance across the business.

The governance framework extends to operational activities, as outlined in the risk management process on pages 38 to 42.

Leadership and effectiveness

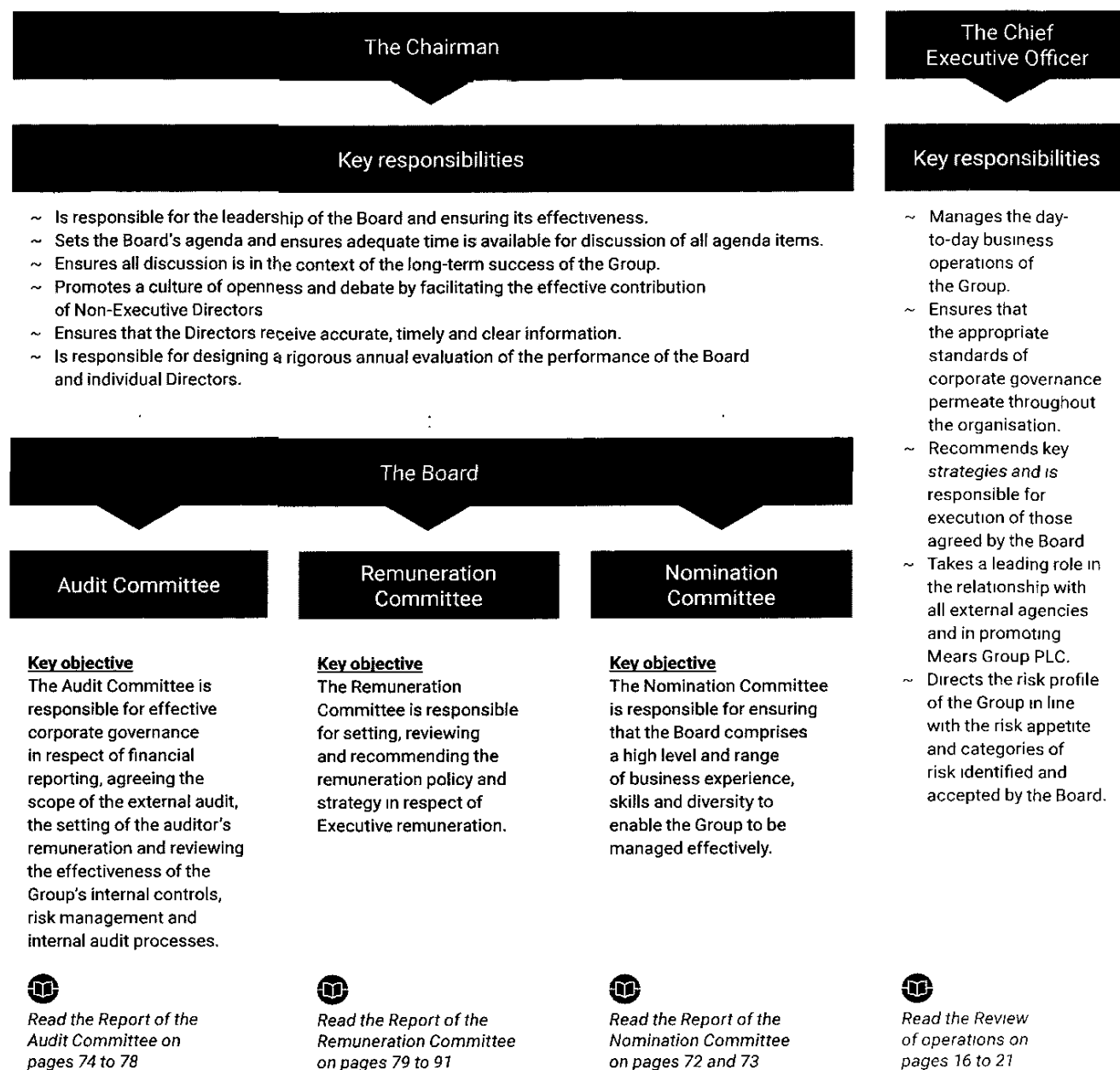
Our Board

Role and responsibilities

- ~ Develop proposals on strategy and deliver value to shareholders and stakeholders.
- ~ Monitor management activity and performance against targets.
- ~ Provide constructive challenge to management.
- ~ Set parameters for promoting and engaging the interest of shareholders and investors.
- ~ Ensure satisfactory dialogue with shareholders takes place.

Matters reserved for the Board's decision

- ~ Group strategy, business objectives, long-range plans and annual budgets.
- ~ Annual and interim results approval
- ~ Material acquisitions, disposals and contract bidding approval.
- ~ Major changes to internal controls, risk management or financial reporting policies and procedures.
- ~ Changes to advisers.
- ~ Setting the risk appetite of the Group.
- ~ Changes to capital and management structure.
- ~ Succession planning for the Board and senior management.
- ~ Board appointments and independence.
- ~ Appointment, termination and remuneration of Directors and the Company Secretary.



Divisional Boards

Key objective

Carries out activities delegated by the Board, including

- ~ Day-to-day operational management of the business
- ~ Monitoring service delivery performance measures and driving improvements.
- ~ Financial performance reviews and comparison to forecasts and updated forecasts
- ~ Business development activity not subject to Board approval

Corporate governance
Corporate governance report continued
Leadership

Board composition and meetings in 2018

Governance framework

Our governance framework supports the development of good governance practices throughout the Group. No one individual has unfettered powers of decision. The Board works closely with the Executive team which ensures Board behaviours and culture are effectively communicated and embedded within the Group. Regular updates are received from the Executive Directors in order to keep the Non-Executive Board members informed of how the business is progressing.

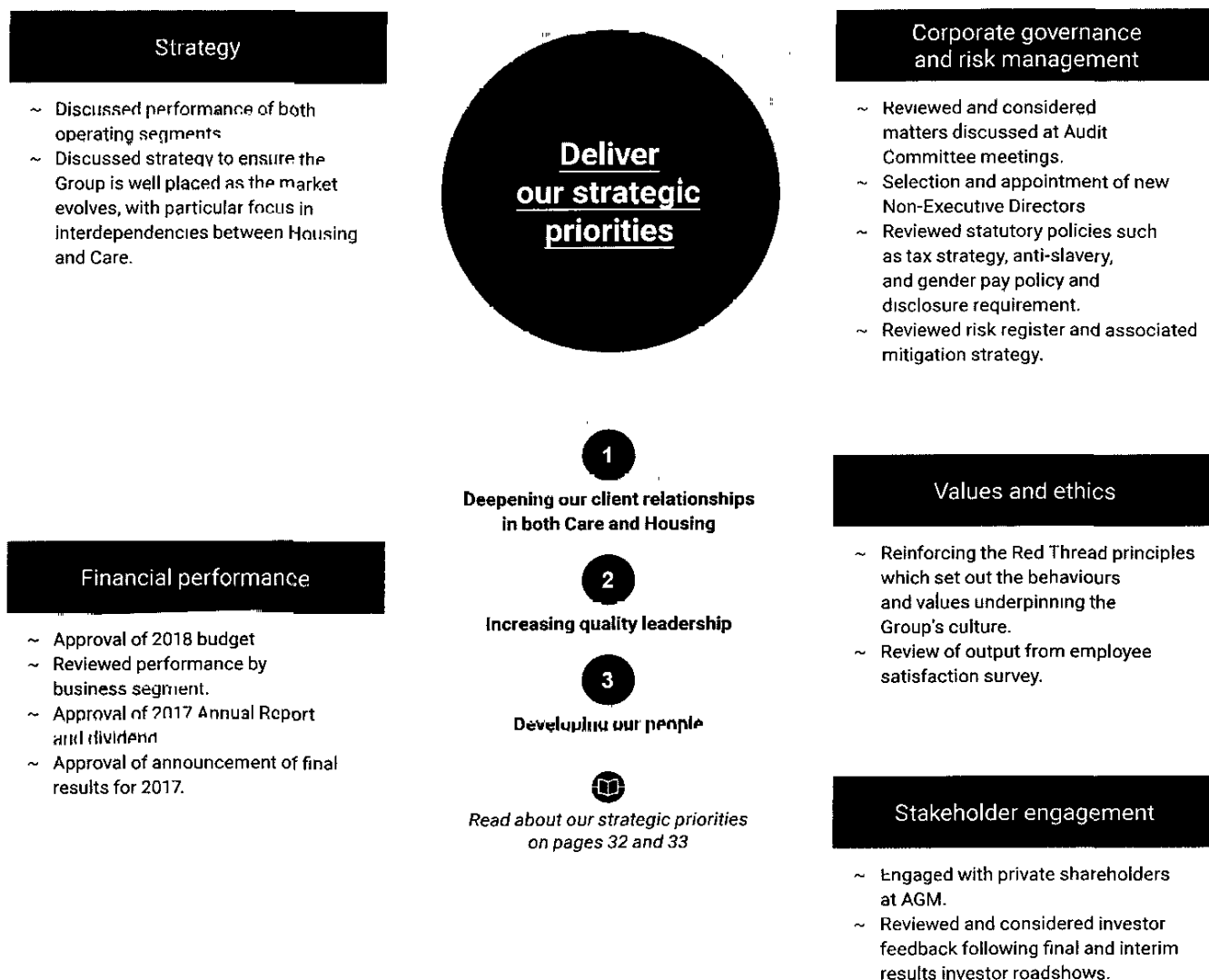
Role	Potential	Attended	Responsibilities include
Chairman			
Kieran Murphy	0	0	~ Promoting a culture of challenge, debate, openness and support
Bob Holt	6	6	~ Leadership of the Board and ensuring its effectiveness ~ Ensuring Directors allocate sufficient time to the Company to discharge their responsibilities effectively ~ Effective communication between the Board, the sub-committees and its key stakeholders ~ Ensuring the Board demonstrates culture, values and behaviours of the Group ~ Ensuring the Board presents a fair, balanced and understandable assessment of the position and prospects of the Group
Senior Independent Director			
Peter Dicks	2	2	~ Being the principal conduit between the Chairman, Non-Executive Directors and shareholders
Julia Unwin	6	6	~ Leading the annual performance evaluation of the Chairman, including collecting the views of the Executive Directors ~ Providing a sounding board for the Chairman
Independent Non-Executive Directors			
Jason Burt	6	6	~ Promoting the highest standards of integrity, probity and corporate governance throughout the Group and the Board
Roy Irwin	6	6	~ Constructively challenging decisions proposed by the Executive Directors
Julia Unwin	6	6	~ Assisting in developing proposals on strategy
Geraint Davies	6	6	~ Contributing to the performance evaluation of the Chairman
Elizabeth Corrado	6	6	~ Briefing the Board on decisions made and key issues from each Committee Chair
Non-Independent Non-Executive Directors			
Amanda Hillerby	3	3	~ Promoting the highest standards of integrity and probity ~ Assisting in developing proposals on strategy ~ Ensuring that the Board receives full, open and honest insight and views from its workforce on how strategic initiatives are being implemented ~ Helping to provide the wider workforce with a better understanding of how the Board operates
Executive Directors			
David Miles Chief Executive Officer	6	6	~ Managing the day-to-day running of the business in line with the strategy and objectives set by the Board ~ Ensuring the Board is supplied with sufficient and appropriate information on a timely basis ~ Leading the business within the scope set by the Board ~ Developing strategy and setting objectives to meet the Group strategy ~ Managing the Group's operation to ensure it meets the risk appetite set by the Board
Andrew Smith Group Finance Director	6	6	~ Supporting the Chief Executive Officer in developing strategy and meeting objectives ~ Establishing strong control processes ~ Managing the treasury activities in accordance with the credit risk appetite set by the Board ~ Supporting the Chief Executive Officer with investor relations ~ Leading the development of talent within the finance function
Alan Long Group Executive Director	6	6	~ Supporting the Chief Executive Officer in developing strategy and meeting objectives ~ Supporting the Chief Executive Officer in managing external communications and investor relations ~ Setting the Group social value policies and procedures ~ Leading the operational leadership and development function of the Group

In addition to planned Board meetings, the Chairman meets with the Non-Executive Directors to discuss, on a less formal basis, Group performance, strategy, governance and Board succession plans. The Executive Directors do not attend these meetings.

The Board considers all Non-Executive Directors who served during the year to be independent in terms of judgement and character and free from any relationship that might materially interfere with the exercise of independent judgement.

Activities of the Board during the year

Board discussion during 2018 to deliver strategic priorities



Corporate governance

Corporate governance report continued

Effectiveness

Board performance evaluation overview

The performance evaluation process included:

- ~ a review of the areas of Board roles and responsibility;
- ~ an internally facilitated review by the Chairman, which included meeting with all Board members individually,
- ~ the structure and composition of the Board and its Committees and the performance of the Committees;
- ~ the quantity, quality and scope of information provided to the Board;
- ~ an assessment of the appropriateness of Directors' terms of reference,
- ~ the content of Board meetings and presentations to meetings, and
- ~ the openness of communications between the Board members and the Executive Management team.

Director information, induction and development

It is a key responsibility of the Chairman to ensure all Non-Executive Directors receive appropriate training and development to ensure they can discharge their duties to the Board and the Committees to the best of their ability. Non-Executive Directors are fully engaged with their ongoing development, which is discussed when each Non-Executive Director has their annual individual meeting with the Chairman.

All Directors have access to the Company Secretary, who is responsible for all Board compliance requirements, to ensure they are updated on all legislative developments. In addition to this, the Company Secretary ensures the Board agenda and papers are provided at least seven days in advance of the meeting. Minutes and actions from previous meetings are distributed on a timely basis. As per the Board policies and procedures, any Non-Executive Director may, on request through the Company Secretary, meet with any member of staff in the Group. Non-Executive Directors are able to request the support of an independent adviser from the Company Secretary.

The quality and timeliness of information provided by the Company Secretary was included as part of the Board evaluation. The findings were that information was thorough and relevant, and in all instances provided suitably in advance.

There were no new appointments during the year. However, since the year end, Non-Executive Chairman, Kieran Murphy, received an individual induction, which included meetings with senior management, advisers and shareholders. Kieran also attended the Group's annual conference which provided access to a cross-section of the colleagues.

Board appraisal

Performance evaluation of the Board, its Committees and individual Directors takes place on an annual basis. Every three years, the review is externally facilitated with the last external review being 2017. Board performance evaluation was externally facilitated. Each Board member provided feedback and key observations on the Board's effectiveness as well as suggestions for further enhancement. The Chairman reviewed the range of feedback provided and identified some broad themes. Some recommendations were proposed which have been implemented, but the overall conclusion was that the Board is working effectively. In addition, the performance of the Chairman is evaluated by the Senior Independent Director, having collected the views of the other Directors.

Independence of Non-Executive Directors and re-election of Directors

The Board adopts the principles of the Code regarding tenure of the board, and seeks to strike an appropriate balance between continuity of experience and refreshment. Rigorous review is applied in assessing the continuous independence of Directors having served for over nine years, with attention to ensuring that they remain independent in character and judgement, and continue to present an objective constructive challenge. In respect of Peter Dicks, the Board recognises that independence cannot be determined arbitrarily on the basis of a set period of time. The Board concluded that Peter Dicks remained independent for the report period.

To promote best practice governance, and in accordance with the requirements of the Code, each of the current Directors will offer themselves for re-election annually. Following the evaluation of the Board's performance during the year, it is confirmed that the performance of each of the Non-Executive Directors continues to be effective and that they are considered to demonstrate appropriate commitment to the role. The AGM papers include an accompanying statement as to why the Board believes each Non-Executive Director should be re-elected.

Indemnifications of Directors

In accordance with our Articles of Association and to the extent permitted by the laws of England and Wales, Directors are granted an indemnity from the Company in respect of liabilities incurred as a result of their position in office. However, our indemnity does not cover Directors or officers in the event of being proven of acting dishonestly or fraudulently.

Shareholder engagement

Principal methods of communication with investors

- Annual Report and Accounts
- Interim statements
- ~ Trading updates
- ~ Quarterly newsletters
- ~ Group website (www.mearsgroup.co.uk)

Investor relations

The Company is committed to maintaining good communication with investors. Normal shareholder contact is the responsibility of the Executive Directors, who respond on a daily basis to queries from institutional and private investors. The Chairman, the Senior Independent Director and other Non-Executive Directors are available to shareholders to discuss any matters they wish to raise. The Directors regularly meet shareholders at operational locations, which both parties find more rewarding as it provides greater insight into the business and its processes. All Directors are available at each AGM and shareholder participation is encouraged.

The Board is committed to maintaining regular contact through the provision of the Annual Report, regular Interim Reports and regular trading updates. This information can be found on the Group's website (www.mearsgroup.co.uk).

There is an active programme of communication with existing and potential shareholders. There is increased dialogue with institutional investors following the publication of final and interim results, which is facilitated through a series of formal presentations. The Company has also looked to hold additional investor days during the year to ensure that they are better informed of market and Company developments. A Capital Markets Day in June 2018 covered 'The changing nature of affordable housing in the UK'. A further day in February 2019 provided background information on the Asylum Accommodation and Support Services Contract (ASSC) award and the Mitre Property Services acquisition (MPS).

The Group regularly receives and responds to questions raised by small private shareholders through the investor enquiry portal within the Group's website. In addition, a number of private shareholders attend the Company's AGM.

Feedback from communication with shareholders and other investors, where necessary, is discussed at Board Meetings. Feedback from this year's shareholder dialogue included the following:

- ~ Shareholders are generally supportive of the progress made by the Group in respect of Housing Maintenance and Management.
- ~ There is a range of differing views in respect of Care but a large number of shareholders are negative in respect of this area, given challenges of recruitment and retention together with risks to reputation.
- ~ Shareholders have been critical of the Group's financial performance, in particular the reliability of forecasts and cash generation.
- ~ Views on succession planning and a feeling that there is less reliance on the Group Chief Executive Officer.

The Group also has regular dialogue with its banking partners, valuing the close relationship with Barclays and HSBC.

J Unwin
Senior Independent Non-Executive Director
julia.unwin@mearsgroup.co.uk
22 March 2019

Q1 2018

Investor meetings prior to the close period.

Following release of final results for 2017, investor roadshow spanning six days, meeting with both 'buy' and 'sell' sides.

Q2 2018

Regular update meetings with existing and prospective shareholders.

AGM held in June 2018, providing an opportunity to meet a number of private investors.

Capital Markets Day held in June 2018 to focus on 'The changing nature of Affordable Housing in the UK'.

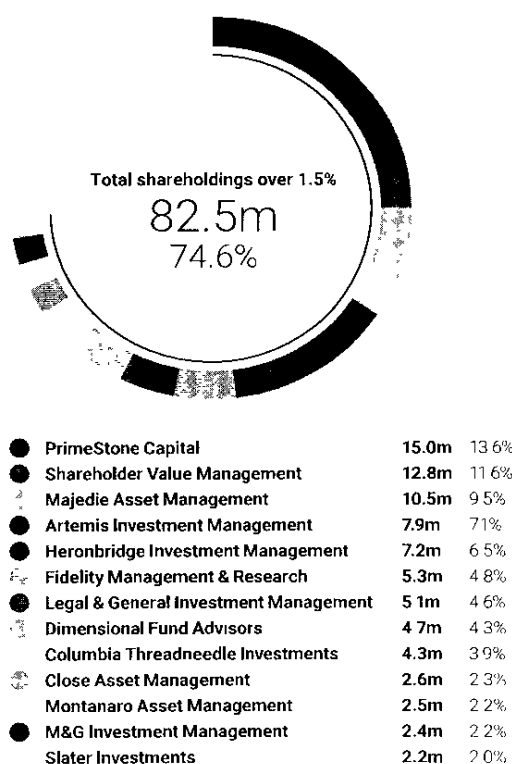
Q3 2018

Following release of interim results for 2018, investor roadshow spanning five days, meeting with both 'buy' and 'sell' side.

Q4 2018

Regular update meetings with existing and prospective shareholders.

Investor lunch providing cross-section of fund managers to meet the key management beneath the PLC Board.



Corporate governance

Report of the Nomination Committee



J Unwin
Nomination Committee Chairman

Meeting attendance	
J Unwin	● ● ●
R Holt	● ● ●
K Murphy	—
A Hillerby (Non-independent, in attendance)	● ●

Key
Attended ● Absent ●

During the first quarter of 2018, the Group advertised internally for an Employee Director. The Board understands the vital role that our workforce plays in the success of the Group. The Board believes that this role will ensure that the Board receives full, open and honest insight and views from its workforce on how strategic initiatives are being implemented and will provide the workforce with a better understanding of how the Board operates. The interview process was very proactive, with applicants delivering presentations to the panel. In June 2018, Amanda Hillerby was appointed to the Board. Mears is one of the first listed companies to take this bold step. I firmly believe that better employee representation can improve the quality of decision making. The benefits of listening to employees and engaging them in both consultation and decision making are already widely recognised.

In July 2018, as part of the continuing evolution of the Board, the Chairman, Bob Holt, indicated his intention to the Board not to stand for re-election at the 2019 AGM. The Board commenced a rigorous appointment process utilising the expertise of an external recruitment consultant and open advertising. The external recruitment consultants used have no connection with the Company. The external recruitment consultant assisted with short-listing candidates. Following this rigorous process, Kieran Murphy was appointed to the Board in January 2019.

We have considered the culture of the Board and the Group as a whole during our discussions this year. The Mears culture is articulated in the Social value section of the Strategic Report, which can be found on pages 52 to 61. The Nomination Committee plays a vital role in embedding a positive culture throughout the Group. This is done by ensuring our succession planning and appointment processes identify candidates who demonstrate our vision, values and desired culture. This will continue to be an area of focus for the Nomination Committee going forward.

Role of the Committee

The Nomination Committee's responsibilities include:

- ~ keeping under review the composition of the Board and succession to it, and succession planning for senior management positions within the Group;
- ~ making recommendations to the Board concerning appointments to the Board, whether of Executive or Non-Executive Directors, having regard to the balance of skills, knowledge, experience and diversity of the Board;
- ~ reviewing the length of service of Non-Executive Directors to ensure a progressive refreshing of the Board, whilst retaining the correct level of experience;
- ~ making recommendations to the Board concerning the re-appointment of any Non-Executive Director at the conclusion of his/her specified term and the re-election of any Director by shareholders under the retirement provisions of the Company's Articles of Association;
- ~ managing a formal, rigorous and transparent procedure for any appointments of new Directors to the Board;
- ~ prior to the appointment of a Director, requiring that the proposed appointee discloses any other business interests that may result in a conflict of interest and reports any future business interests that could result in a conflict of interest; and
- ~ ensuring that, on appointment to the Board, Non-Executive Directors receive a formal letter of appointment setting out clearly what is expected of them in terms of time commitment, Committee service and involvement outside Board meetings.

Activities during the year

- ~ Reviewed Board effectiveness, Board governance, Executive and Non-Executive Director succession and deliberation of person requirements for the appointments to the Board
- ~ *Carried out appointment process for Employee Director*
- ~ Carried out a rigorous appointment process to appoint a replacement for Bob Holt, recommended to the Board the appointment of Kieran Murphy as the new Non-Executive Chairman
- ~ Recommended to the Board that all Directors stand for re-election
- ~ Reviewed the performance of the Committee against its terms of reference
- ~ Reviewed and discussed the internal leadership and development programme to ensure its appropriateness for succession to the Board

Diversity

We have a number of active diversity initiatives across the Group, including the Tradeswomen into Maintenance project and our social mobility focus, as mentioned in the Chairman's introduction to corporate governance

The Committee receives updates on all diversity initiatives, and monitors the level of engagement and investment. The Executive Directors are challenged by the Nomination Committee to ensure that these diversity initiatives remain high profile

The appointments in 2018 have increased the diversity of our Board in terms of gender and experience. I am delighted that the Board now comprises 30% female Directors, which falls broadly in line with the recommendation of the Hampton-Alexander Review to target 33% female board representation by 2020. Notwithstanding this, the Committee follows a rigorous appointment process which the Committee feels is free from bias

Director induction

Following Board approval, a tailored induction programme is developed between the Committee and the Group's insourced leadership and development team

The terms and conditions of each appointment of Non-Executive Directors are made available on request of the Company Secretary, and are available for inspection at the AGM

J Unwin

Nomination Committee Chairman

julia.unwin@mearsgroup.co.uk

22 March 2019

Corporate governance
Report of the Audit Committee
Accountability



G Davies
Audit Committee Chairman

Meeting attendance

G Davies	● ● ● ● ● ● ● ●
J Burt	● ● ● ● ● ● ● ●
E Corrado	● ● ● ● ● ● ● ●

Key

Attended ● Absent ●

This report sets out how the Committee has fulfilled its responsibilities during the year. This report also sets out, in relation to financial reporting matters, the significant issues that were considered and how they were addressed.

A new committee dealing with health, safety and environmental risks has been formed. This Compliance Committee is a sub-committee of the Audit Committee and is chaired by Jason Rurt. With his detailed knowledge of the factors which cause and drive regulatory prosecutions and employers' and public liability claims he is ideal for the role. The extent to which the full integration of health, safety and environmental risks are now embedded in the governance structures of the Group is highlighted by the members of the Compliance Committee who include the Group's Chief Executive Officer, Chief Risk Officer, Health and Safety Director and Health and Safety Solicitor. The Compliance Committee has detailed terms of reference which include

- ~ to review and monitor the Group's policies in relation to health, safety and environmental (HSE) matters;
- ~ to review HSE risks and risk assessments on the Group risk register and mitigation actions and controls related thereto including subcontractor controls and related procurement, and
- ~ to review Group buildings compliance and safety including fire and other risks

I have continued to have a number of detailed review meetings with the Chief Risk Officer

In relation to financial reporting the two primary significant judgements remain the carrying value of Care goodwill and revenue recognition. Both of these continue to have a high level of materiality and carry a significant level of judgement. In reaching its conclusions the Committee has had very detailed discussions with management and gained assurance from the detailed procedures carried out by the external auditor, Grant Thornton UK LLP.

A third key judgement is the assumptions surrounding the defined benefit pension valuations. Despite the valuations being prepared by independent actuaries the Committee is very aware that, in a volatile economic environment, assumptions around bond rates and discount rates are less predictable and small movements in these assumptions can result in a material change to the carrying value of assets and liabilities in a reporting period. Given the requirement that the Annual Report is fair, balanced, concise and understandable, the Committee supports the analysis prepared by the Finance Director on pages 45 to 51 which enables stakeholders to understand the differing risks associated with our LGPS and non-LGPS pension schemes and the impact of gender equalisation.

In relation to risk management and internal controls, the Chief Risk Officer manages an extended internal audit team whose annual plan is based on the Group risk register and is approved by the Committee. The 2018 Annual Internal Audit Report, presented to the Committee for approval in February 2019, included more coverage than ever before. I was particularly pleased to note the extent to which management has responded positively and quickly to the system changes suggested by the internal audit work.

During the year, the audit engagement was tendered. Following a rigorous process which is discussed in greater detail later in this report, the Audit Committee chose Grant Thornton UK LLP to retain the audit, which was ratified by the AGM. As Grant Thornton UK LLP was reappointed the Audit Committee has reviewed the independence regulations and recommended to the Board that the audit be retendered for the years beginning 1 January 2022 at which time Grant Thornton UK LLP will not be invited to retender. The Committee will continue to review the independence and effectiveness of its external audit on an annual basis. The review process includes reviewing the external auditor's plan, and subsequent reports and discussion by the Committee of the appropriateness of audit procedures and processes.

Role of the Committee

The Committee has access to the financial expertise of the Group and its auditor and, if required, can seek further professional advice at the expense of the Group.

The key responsibilities of the Committee are to

- ~ consider the appointment of the external auditor, its reports to the Committee and its independence, including an assessment of its appropriateness to conduct any non-audit work,
- ~ review the financial statements and announcements relating to the financial performance of the Company,
- ~ review the internal audit programme and ensure that the internal audit function is adequately resourced and has appropriate standing within the Company,
- ~ discuss with the external auditor the nature and scope of the audit,
- ~ review, and challenge where necessary, the actions and judgements of management, in relation to the interim and annual financial statements before submission to the Board,
- ~ formally review the effectiveness of the external and internal audit processes,
- ~ consider management's response to any major external or internal audit recommendations,
- ~ review the Company's plans for business continuity,
- ~ review the Company's plans for prevention and detection of fraud, bribery and corruption,
- ~ review the effectiveness of the whistleblowing arrangements, and
- ~ report to the Board on how it has discharged its responsibilities.

The Committee's terms of reference are available on the Company's website and on request from the Company Secretary.

Committee meetings

The Committee met five times during the year with attendance by all members. These meetings were also attended by the Group Chief Executive Officer, the Group Finance Director and the Chief Risk Officer as required by invitation from the Chairman of the Audit Committee. The external auditor, Grant Thornton UK LLP, was invited to all meetings. There was also significant dialogue outside formal meetings between Committee members, Executive Directors and the external auditor, particularly during the audit process and the preparation of the Annual Report. The Audit Committee Chairman meets with the external auditor regularly throughout the year.

Main activities of the Committee during the year **Financial and business reporting**

The Audit Committee shares the responsibility with the Board for reviewing the appropriateness of the Annual Report and half-year announcements, to ensure that they properly reflect the Group's business model, strategic priorities, key risks, and financial and non-financial performance. Consideration is given to the reasonableness of the accounting policies, adherence to accounting standards, and sufficiency and clarity of the information disclosed.

The primary areas of judgement considered by the Committee in relation to the 2018 accounts, and how these were addressed, were

Carrying value of goodwill

For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows, these are termed as cash-generating units (CGUs). Due to the Board successfully integrating the newly acquired Care business into the existing Care business, there have been two CGUs identified: Social Housing and Care. Determining whether goodwill is impaired requires an estimate of the value in use of each of the CGUs to which goodwill has been allocated. The value-in-use calculation involves an estimate of the future cash flows of the CGU and also the selection of an appropriate discount rate to calculate present values. Future cash flows are estimated using the current one-year budget, extrapolated for five years to December 2023 using specific rates with a general terminal growth rate being used thereafter. This has been derived from the extensive business planning process described in greater detail within note 13 to the financial statements on pages 128 to 130. Estimated growth rates over each period are based on past experience and knowledge of the individual sector's markets. The Directors consider that the estimates and judgements involved in determining the value in use of the Care CGU goodwill are the most significant to the Group and they have therefore utilised the services of an external consultant to assist with this impairment review. The value in use is most sensitive to changes in the terminal growth rate, the explicit growth rate during the forecast period and the discount rate.

The sensitivity to changes in these estimations is detailed in note 13 to the financial statements. The Audit Committee takes reassurance from the previous year's impairment review, where the key assumptions have subsequently been found to have been reasonably conservative and that the actual results in the subsequent year have delivered better outcomes than anticipated. The headroom in the period, being the excess between value in use compared with carrying value, has reduced and the Audit Committee is mindful that there is still significant uncertainty in the Care sector and the key assumptions could change and materially impact on the carrying value of the Care business.

The Audit Committee addressed this area of judgement by reviewing the key assumptions proposed by management, notably forecast growth rate, discount rate, terminal growth rate, and carer recruitment and retention rates.

- ~ The Committee reviewed the disclosure in the notes to the financial statements
- ~ This area represented a prime area of audit focus and Grant Thornton UK LLP provided detailed feedback to the Committee.

Corporate governance

Report of the Audit Committee continued

Accountability continued

Revenue recognition

The Audit Committee reviewed in detail the impact of the new accounting standard, IFRS 15, which came into effect on 1 January 2018 and will impact on the timing of recognising revenue and costs on a small number of contracts, whilst being mindful that the comparative figures continue to be prepared using accounting policies under IAS 18. The key changes are as follows:

- ~ Previously IAS 18 'Revenue' and IAS 11 'Construction Contracts' allowed contracts with a variety of services to be combined in certain circumstances in determining the percentage of completion of those multi-service contracts. Disaggregating these contracts to determine the satisfaction of performance obligations, as detailed above, significantly changes the timing of revenue recognition. £19.1m of the reduction in the opening balance of equity at 1 January 2018 relates to the disaggregation of contracts previously combined. The total transaction price of these contracts does not change under IFRS 15.
- ~ The Group's assessment of variable consideration revenue recognition under IFRS 15 is detailed above. The judgement applied under IFRS 15 more closely aligns timing of revenue recognition with cash inflows where the contractual mechanism contains uncertainty. Previously, the Group utilised expected value calculations in determining the variable consideration revenue to be recognised. £4.8m of the reduction in the opening balance of equity at 1 January 2018 relates to the Group's application of IFRS 15 in relation to variable consideration.

The Audit Committee addressed this area of judgement in the following ways:

- ~ The Committee reviewed the key judgements report prepared by management which provided a detailed explanation in respect of the valuation of unbilled works and the recognition of revenues.
- ~ The Committee took comfort from the contract management system which is central in generating the valuation of works (both billed and unbilled) and the integrated process that follows to ensure an accurate cut-off so that revenue is appropriately matched to cost. Grant Thornton UK LLP tested these systems during its audit fieldwork and provided feedback to the Committee on this crucial area, and this area represented a prime area of external audit focus. Grant Thornton UK LLP carried out both controls-based and substantive testing of the amounts recoverable on contracts, adopting a blend of risk-based and random sampling approaches to testing, and provided detailed feedback to the Committee in this area. Grant Thornton UK LLP's comments can be seen on page 98. Grant Thornton UK LLP also carried out a detailed review of the impact of the adoption of IFRS 15.

The acquisition of MPS Housing and MPM Revenue recognition

In November 2018, the group acquired the entire share capital of MPS Housing Limited and Mite Property Management Limited. This acquisition has had a material impact on the financial statements, resulting in the recognition of goodwill and intangible assets of £21.5 million. The goodwill measured at the acquisition date is the fair value of the consideration, including the estimated value of contingent consideration, less the net recognised amount of identifiable assets acquired and liabilities assumed. The Committee was also mindful of the proximity of the acquisition to the year end which was considered to add further risk. Although the estimates are provisional for 2018 and will be finalised during the course of 2019, significant judgement is required in deriving the value assigned to contingent consideration and the identifiable assets.

The Audit Committee addressed this area of judgement in the following ways:

- ~ obtaining an understanding of the acquisition through review of legal agreements and discussion with management. The Committee took comfort from the fact that the acquired activities are very similar in nature to the Group's core activities, and management have been shown over many years to a high level of expertise in this area. This was reflected in a good understanding of the underlying contracts and the bases for valuing unbilled works,
- ~ considering the assumptions set by management in respect of discount rate, customer attrition and long term growth rate through the sales pipeline. These are the most sensitive assumptions which impact upon both the estimated value of the contingent consideration and the recognition of acquired intangibles, and
- ~ this area represented a prime area of external audit focus and Grant Thornton UK LLP provided detailed feedback to the Committee.

Defined benefit pension valuation

A number of key estimates have been made, which are given below and which are largely dependent on factors outside the control of the Group:

- ~ Inflation rates
- ~ Mortality
- ~ Discount rate
- ~ Salary and pension increases

Details of the particular estimates used are included in the pensions note (note 29) to the financial statements on pages 144 to 147.

Where the Group has a contractual right to recover the costs of making good any deficit pension scheme, the fair value of that asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. The Directors have made judgements in respect of whether any of the deficit is as a result of such situations.

The right to recover costs is also limited to situations where the cap on contributions payable by the Group is not set so as to contribute to reducing the deficit in the scheme. The Directors, in conjunction with the scheme actuaries, have made judgements in respect of the predicted future service cost and contributions to the scheme to reflect this in the fair value of the asset recognised.

The Audit Committee addressed this area of judgement in the following ways

- ~ The Committee reviewed the key assumptions proposed by management, notably assumptions in respect of discount rate, RPI, CPI and future salary increases. Given the materiality of this area, the Committee reviewed a report prepared by PricewaterhouseCoopers LLP which validated the assumptions set by management and provided a comparison with other quoted companies
- ~ The Committee reviewed the accounting treatment of pension related transactions. Full disclosure has been provided within the pensions note (note 26) to the financial statements on pages 144 to 147 and the Committee concurred with the analysis provided on pages 47 and 50 of the Financial Review in respect of defined benefit scheme pension obligations
- ~ Given the technical nature of this area, the Committee placed reliance upon the actuarial reports prepared by the respective scheme actuaries in respect of each of the defined benefit pension schemes, including an assessment of gender equalisation

New standards and interpretations not yet applied

The Group is required to disclose information on standards that are in issue, not yet effective that have not been early adopted in the financial statements

The Committee has met with management to discuss management's interpretation and proposed implementation of IFRS 16 'Leases'. Following these discussions, the Committee reviewed the disclosures within Principal Accounting Policies on pages 105 and 114

The Committee satisfied itself of the appropriateness of the disclosures after the discussions with management and the review of the disclosures by the external auditor

Internal controls and risk management

With respect to its oversight of risk management and internal controls, the Board reviewed and discussed a wide range of matters with management, internal audit and external audit, as appropriate. This extends to cover all material controls, including operational, compliance and financial controls and risk management systems. The Directors are satisfied that procedures are in place to ensure that the Group complies with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting published by the Financial Reporting Council in September 2014.

The Board has delegated some of these responsibilities to the Audit Committee which has reviewed the effectiveness of the system of internal controls and ensured that any remedial action has been or is being taken on any identified weaknesses. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss. It includes all controls including financial, operational and compliance controls and risk management procedures.

In addition, the Audit Committee has a new sub-committee, the Compliance Committee. An overview of the terms of reference of this Committee is included within the Audit Committee Chairman's introduction, the Compliance Committee reports to the Audit Committee under these terms of reference.

The Group has an ongoing process for identifying, evaluating and managing the significant risks faced by the Group. The Group endeavours to ensure that the appropriate controls, systems and training are in place and has established procedures for all business units to operate appropriate and effective risk management.

The processes used to assess the effectiveness of the internal control systems are ongoing, allowing a cumulative assessment to be made, and include the following:

- ~ Delegation of day-to-day management to operational management within clearly defined systems of control, including
 - the identification of levels of authority within clearly identified organisational reporting structures,
 - the identification and appraisal of financial risks both formally, within the annual process of preparing business plans and budgets, and informally, through close monitoring of operations,
 - a comprehensive financial reporting system within which actual results are compared with approved budgets, quarterly reforecasts and previous years' figures on a monthly basis and reviewed at both local and Group level, and
 - an investment evaluation procedure to ensure an appropriate level of approval for all capital and revenue expenditure
- ~ Discussion and approval by the Board of the Group's strategic directions, plans and objectives and the risks to achieving them, combined with regular reviews by management of the risks to achieving objectives and actions being taken to mitigate them
- ~ Review and approval by the Board of annual budgets, combined with regular operational and financial reviews of performance against budget, prior year results and regular forecasts by management and the Board
- ~ Regular reviews by the Board and the Audit Committee of identified fraudulent activity and actions being taken to remedy any control weaknesses
- ~ Regular reviews by management and the Audit Committee of the scope and results of internal and external audit work across the Group and the implementation of recommendations
- ~ Consideration by the Board and by the Audit Committee of the major risks facing the Group and of the procedures in place to manage them and to ensure controls react to changes in the Group's overall risk profile. These include health and safety, people, legal compliance, quality assurance, insurance and security, and reputational, social, ethical and environmental risks
- ~ Discussion relating to a presentation from the IT Director on cyber-security, including an assessment of vulnerabilities and the programmes being implemented to protect the Group against this evolving and potentially catastrophic risk
- ~ Consideration and discussion relating to regular updates from the Finance Director regarding developments within the finance function

The Board has reviewed these procedures and considers them appropriate given the nature of the Group's operations. The Chief Risk Officer and the Finance Director presented a report on the robustness of the internal controls for the year and an internal audit plan for 2019. The Committee has concluded that the system of internal controls and risk management is embedded into the operations of the Group and the actions taken to mitigate any weaknesses are carefully monitored.

Corporate governance

Report of the Audit Committee continued

Accountability continued

The key controls in place are

- ~ a defined organisational structure and an appropriate level of delegated responsibility to operational management,
- ~ authorisation limits for financial and non-financial transactions,
- ~ written operational procedures,
- ~ a robust system of financial budgeting and forecasting,
- ~ a robust system of financial reporting with actual results compared to budget and forecast results, and
- ~ regular reporting of operational performance and risks to the Board, including the work of the Compliance Committee

In 2014 a detailed review of internal controls was performed by independent internal audit outsourced partners KPMG. This work was commissioned on a risk-based approach and was performed to provide the Committee with independent assurance over the quality of risk management and strength of internal controls. The procedures performed by KPMG were undertaken within inherently risky areas that would affect KPI performance. This assignment was finalised during 2015 and the independent view of internal controls was that controls were generally adequate, though improvements were suggested. The improvements have been implemented as envisaged in the 2016 Annual Report, KPMG, as outsourced internal audit resource, carried out an updated review of centralised controls and processes. Management has accepted recommendations from the 2017 updated review.

The Company has in place internal control and risk management systems in relation to the Company's financial reporting process and the Group's process for the preparation of consolidated accounts. The consolidated financial statements are produced by the Group finance function, which is responsible for the review and compilation of reports and financial results from each of the operating subsidiaries in accordance with the Group reporting procedures. The consolidated financial statements are supported by detailed working papers. The Audit Committee is responsible for overseeing and monitoring these processes, which are designed to ensure that the Company complies with relevant regulatory reporting and filing requirements. As at the end of the period covered by this report, the Audit Committee, with the participation of the Chief Executive Officer and the Finance Director, evaluated the effectiveness of the design and operation of disclosure controls and procedures designed to ensure that information required to be disclosed in financial reports is recorded, processed, summarised and reported within specified time periods.

The Committee carried out a review of its effectiveness with input from Committee and Board members, management and the external auditor. The review concluded that the Audit Committee members had sufficient expertise and committed time to discharge their responsibilities.

External audit related services

As noted in the Annual Report last year and approved by shareholders at the AGM last June the audit was tendered during the year. Two 'Big Four' firms and the incumbents, Grant Thornton UK LLP, having confirmed their interest in tendering, were contacted in January 2018 and invited to meet key personnel including the Group Finance Director, the Chief Risk Officer and myself as Chair of the Audit Committee during February and March. The firms were asked for their written submissions in April 2018 with their fee proposals provided separately in a sealed envelope. The fee proposals were only opened after the Audit Committee had scored and ranked the quality of the written proposals and subsequent presentations and interviews, so that the focus of the Audit Committee was on the quality of the submissions being presented.

The Audit Committee determined the key criteria for the appointment would include: audit professional scepticism and challenge of the executive, business understanding and sector knowledge, seniority and experience of the audit team to be deployed, transitional planning where applicable, the depth of involvement of the proposed Senior Statutory Auditor, and detailed confirmation of the independence of the both the firm and the individual working directly on the audit.

After the presentations and interviews the Audit Committee chose Grant Thornton UK LLP to retain the audit based on the overall highest scores. The fee proposal was then reviewed, which did not alter our view. The Audit Committee then recommended Grant Thornton UK LLP to the Board which confirmed its appointment, which was ratified by the AGM.

As Grant Thornton UK LLP was reappointed the Audit Committee has reviewed the independence regulations and recommended to the Board that the audit be retendered for the years beginning 1 January 2022 at which time Grant Thornton UK LLP will not be invited to retender.

The Company has adopted a strict policy of prohibiting the external auditor from carrying out non-audit services, in order to safeguard audit objectivity and independence. The Committee is responsible for approval of all non-audit services provided by Grant Thornton UK LLP, however, this is considered to be in exceptional circumstances only. In such an exceptional event, the Audit Committee would approve only where the Company would be disadvantaged by engaging an alternative provider, for instance where Grant Thornton UK LLP possesses a detailed knowledge of the structure of the business or an understanding of the markets that the Group operates in. No non-audit services were provided by Grant Thornton UK LLP during 2018.

G Davies
Audit Committee Chairman
geraint.davies@mearsgroup.co.uk
22 March 2019

Corporate governance

Report of the Remuneration Committee



R Irwin
Remuneration Committee Chairman

Meeting attendance

R Irwin	● ● ● ●
J Unwin	● ●
K Murphy	–
P Dicks	● ●
A Hillerby (Non-independent, in attendance)	●

Key

Attended ● Absent ●

Dear shareholder,

I am pleased to deliver my first report since taking over as Committee Chairman

The Directors' remuneration policy report sets out the Company's remuneration policy for Directors. This policy was subject to a binding vote at the 2017 AGM and will remain unchanged for a period of at least three years. For completeness, the policy is detailed in full within this Annual Report

The Annual Report on Remuneration sets out payments and awards made to the Directors and details the link between Company performance and remuneration for the 2018 financial year. This report, together with this letter, is subject to an advisory shareholder vote at the 2019 AGM

You will have read earlier in the Annual Report that 2018 has been a solid year. The financial results were satisfactory although shareholders have been critical around the cash flow, and the working capital absorbed in areas such as *Housing Development*. The Group did register significant success in the period in securing three regions of the Asylum Accommodation and Support Contract. The contract is valued at £1bn over the ten-year term and was the key sales target for the year. Another highlight was completing the acquisition of certain business assets from the property maintenance business of Mitie. The transaction took several months to complete, and the final valuation and deal structure is credit to the Executive team

The Directors' achievement against their key performance indicators is detailed on pages 34 to 37. The Committee, in reviewing the performance of the business, concluded that no award should be made under the EIP in respect of 2018, a view with which the Executive Directors agreed

I am mindful that the Directors' remuneration policy is not delivering the desired outcomes in terms of motivation, retention and alignment in the interests of senior management with shareholders. It is my intention to commence dialogue during 2019 to ensure that we have a revised remuneration policy before the start of 2020, which will be ratified through a binding vote at the 2020 AGM

The Remuneration Committee is acutely aware of the sensitivity around increasing pay levels in excess of the general workforce. In this regard we have broadened the Committee terms of reference and strengthened its membership through the inclusion of our new Chairman Kieran Murphy and also, from last autumn, our Employee Director Amanda Hillerby. The Executive team is also mindful of the pay structure of the wider workforce, and has emphasised its desire to ensure that, where possible, resources are targeted to those at the lower end of the pay scale. No pay increases are proposed for the Executive team for the coming year

I hope you find the information in this report helpful and I look forward to your support at the forthcoming AGM. I am always happy to hear from the Company's shareholders and you can contact me direct, or via the Company Secretary, Ben Westran, if you have any questions on this report or more generally in relation to the Company's remuneration

R Irwin
Remuneration Committee Chairman
roy.irwin@mearsgroup.co.uk
22 March 2019

Corporate governance

Remuneration policy

Directors' remuneration policy

Remuneration policy and philosophy

Remuneration policy	How is this achieved?
A simple and transparent remuneration structure that retains and motivates Executives while being sympathetic to Mears' operating environment from both an external and internal perspective.	<ul style="list-style-type: none"> ~ Conservative levels of fixed remuneration balanced with one annual incentive strongly linked to performance ~ The performance element of the annual incentive incorporates robust financial, operational and strategic KPIs that are aligned with an evolving business strategy in an uncertain economic environment ~ All incentive payments are deferred into equity over a five-year period ensuring clear alignment with shareholders' interests and 'at-risk' remuneration
A proportion of each Executive's total compensation should be linked to performance related pay and the provision of equity	~ All incentive payments are delivered in 'deferred' shares. At stretching performance, around one third of the Executive Directors' total remuneration is based on the achievement of key corporate metrics that are aligned to the Company's long-term strategy
There should be a commitment to fostering a performance culture that aligns an individual's rewards with the key corporate metrics that drive shareholder value creation	<ul style="list-style-type: none"> ~ The performance measures used in the Executive Incentive Plan are directly aligned with our corporate goals and as such ensure that there is no payment for poor performance ~ The Committee will ensure that the remuneration package does not lead to irresponsible behaviour and that it takes appropriate account of risk

Executive Directors

The table below sets out the key elements of the policy for Executive Directors

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Base salary			
<p>The purpose of the base salary is to</p> <ul style="list-style-type: none"> ~ help recruit and retain key individuals, ~ reflect the individual's experience, role and contribution within the Group, and ~ ensure fair reward for 'doing the job' 	<p>The Committee reviews base salaries annually in April</p> <p>The Committee will retain the discretion to increase an individual's salary where there is a significant difference between current levels and a market competitive rate. When determining base salaries and whether to increase levels the Committee will take the following into consideration</p> <ul style="list-style-type: none"> ~ the performance of the individual Executive Director, ~ the individual Executive Director's experience and responsibilities, ~ the impact on fixed costs of any increase, ~ pay and conditions throughout the Group, and ~ the economic environment <p>When setting the salary levels for the Executive Directors, in addition to the factors summarised above, salary levels paid by companies of a similar size and complexity to Mears are taken into account</p>	<p>The annual increase will not exceed 10% of annual base salary</p> <p>The Committee is guided by the general increase for the broader employee population but may decide to award a lower increase for Executive Directors or indeed exceed this to recognise, for example, an increase in the scale, scope or responsibility of the role and/or to take into account relevant market movements</p> <p>The Company will set out in the section headed Statement of implementation of remuneration policy, in the following financial year, the salaries for that year for each of the Executive Directors</p>	Not applicable
Other benefits			
To provide benefits that are valued by the recipient and are appropriately competitive	The Executive Directors receive additional benefits including a company-provided car or an allowance in lieu, life assurance and private medical insurance. Other benefits may be provided where appropriate. Benefits in kind are not pensionable.	Benefit values vary year on year depending on premiums and the maximum potential value is the cost of these provisions	Not applicable
Pension			
To provide a framework to save for retirement that is appropriately competitive	All Executive Directors receive a contribution into their respective defined contribution plans, which are subject to periodic review to ensure that they remain in line with rates applicable in the market. Only the base salary is pensionable.	The Executive Directors receive a contribution of 15% of salary	Not applicable

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Executive Incentive Plan (EIP)			
<p>To provide a link between reward and corporate performance in order to appropriately retain and motivate the Executive Directors and senior management who are critical to executing the business strategy</p> <p>To align the interests of Executive Directors and senior management more closely with shareholders over the longer term and provide a greater exposure to share price movements over this period</p>	<p>Annual awards of nil-cost options will be made based on the achievement of annual performance measures</p> <p>Awards will be made in two parts</p> <ul style="list-style-type: none"> ~ 50% of the maximum award will be granted in deferred shares ('Part A'), and ~ 50% of the maximum award will be granted based on the achievement of a range of annual performance measures ('Part B') <p>Both awards will vest 60% after three years, with a further 20% after four years and the remaining 20% after five years</p> <p>The Committee may award dividends/dividend equivalents on shares to the extent that the shares vest</p> <p>In exceptional circumstances (such as recruitment) the Committee retains the discretion to provide an element of the award in cash</p> <p>Further details of the operation of the EIP, including the performance measures for 2019, are set out on page 90</p>	<p>Annual awards made to Executive Directors will be capped at a maximum of 200% of salary. For Part A of the award, 100% will vest if the EPS metric is met in full. For Part B of the award</p> <ul style="list-style-type: none"> ~ 20% of the award will vest for threshold performance, and ~ 100% of the award will vest for maximum performance <p>There is straight-line vesting between these points</p>	<p>The performance measure for Part A will be earnings per share</p> <p>The performance measures for Part B of the 2019 awards are as follows: earnings per share (EPS), return on capital employed (ROCE), cash conversion, customer satisfaction, and health and safety</p> <p>The Remuneration Committee has discretion to set performance measures and weightings on an annual basis, with performance measures for the next financial year set out in the Statement of Implementation on pages 89 and 90</p> <p>The EIP contains malus (up to date of vesting) and clawback (two years post vesting) provisions</p>
All-employee share plans			
Encourages employees to own shares in order to increase alignment over the longer term	<p>All employees are eligible to participate in the Company's Share Incentive Plan (SIP) and Sharesave Plan (Save As You Earn)</p> <p>Under the terms of the Sharesave Plan all employees can apply for three or five-year options to acquire the Company's shares priced at a discount of up to 20%</p> <p>Under the terms of the SIP the Company can choose to offer free shares, partnership shares, matching shares (up to two for one on any partnership shares purchased) and/or dividend shares</p> <p>In addition the Company operates a discretionary unapproved share plan and a Company Share Option Plan (CSOP). No awards to Executive Directors are proposed under these plans</p>	Under the SIP, Sharesave Plan and CSOP, the maximum amount is equal to the regulatory limits set from time to time	Not applicable
Shareholding requirement			
Secures a long-term locked-in alignment between the Executive Directors and shareholders, ensuring that they build up and maintain a minimum level of shareholding throughout their employment with the Company	<p>The shareholding requirement will operate in the following manner</p> <ul style="list-style-type: none"> ~ only shares unconditionally owned by the Executive Director will count against the requirement, and ~ shares can be built up over a five-year period from implementation of the policy through the vesting and retention of share awards and/or MIP/EIP payments 	Minimum shareholding requirement is 400% of salary	Not applicable

Corporate governance

Remuneration policy continued

Reasons for selecting performance measures

The Committee wanted to ensure that the performance measures selected provide a holistic assessment of overall corporate performance and tie in to the non-financial objectives that the Company embraces throughout the organisation

EPS growth has been selected as it provides direct alignment to the Company's strategic objectives over the long term and is also transparent, fully understood by participants and an externally audited metric over which they have line of sight

The use of ROCE and cash conversion (previously incorporated as underpins) ensures that quality of earnings is protected and the Company maintains strong working capital management

Customer satisfaction and health and safety performance conditions are included as these are key KPIs that the Company focuses on and, by performing strongly in these areas, it will help win new contracts with end users and support new innovative operating models

Targets are calibrated to reflect the Committee's assessment of good to exceptional performance and taking into account internal budgets and the current economic environment

Differences in remuneration policy for all employees

The Company sets terms and conditions for employees which reflect the different legislative and labour market conditions that operate in each of our jurisdictions. We will always meet or exceed national minimum standards for terms and conditions of employment in each of our business areas. Pay arrangements in our businesses also reflect local performance with personal increases based on achievement, individually assessed. Mears believes in the value of continuous improvement, both for the individual and for the Company

In general, all employees receive base salary, benefits and pension, and are eligible to participate in the Company's share plans. Share awards and bonus plans are cascaded down below Executive level to senior management, aligning the Senior Management Team to deliver value for the Group

The remuneration of the Executive Directors and Senior Executives is more heavily weighted towards variable pay than for other employees, with a large proportion of their overall package dependent on successful and sustained execution of the business strategy over the longer term

Committee discretions

The Committee will operate the EIP according to the plan rules. The Committee retains discretion, consistent with market practice, in a number of regards to the operation and administration of these plans. These include, but are not limited to, the following

- ~ The participants
- ~ The timing of grant of an award
- ~ The size of an award
- ~ The determination of vesting
- ~ Discretion required when dealing with a change of control or restructuring of the Group
- ~ Determination of the treatment of leavers based on the rules of the plan and the appropriate treatment chosen
- ~ Adjustments required in certain circumstances (e.g. rights issues, corporate restructuring events and special dividends)
- ~ The annual review of performance measures and weighting for the EIP and exercise conditions
- ~ In exceptional circumstances, the payment of a proportion of the EIP in cash

These discretions, which in certain circumstances can be operated in both an upward and a downward manner, are consistent with market practice and are deemed necessary for the proper and fair operation of the schemes in order to achieve their original purpose. It is the Committee's policy, however, that there should be no element of reward for poor performance and any upward discretion will only be applied in exceptional circumstances

Illustrations of application of remuneration policy

For illustrative purposes we set out below how the policy would operate at three levels of performance

- ~ Minimum performance includes only fixed pay (salary, benefits and pension)
- ~ On-target performance includes Part A of the EIP and 60% of Part B of the EIP
- ~ Maximum performance includes the maximum opportunity under the EIP

Fixed pay is base salary for 2019 plus the value of pension and other benefits

The charts demonstrate the balance between fixed and variable pay for minimum, threshold and maximum performance for Executive Directors' remuneration in 2019 in line with the relevant policy

Approach to recruitment remuneration

In the event that the Company recruits a new Executive Director (either from within the organisation or externally), when determining appropriate remuneration arrangements, the Committee will take into consideration all relevant factors (including, but not limited to, quantum, the type of remuneration being offered and the jurisdiction the candidate was recruited from) to ensure that arrangements are in the best interests of both the Company and its shareholders, without paying more than is necessary to recruit an Executive of the required calibre

The Committee would generally seek to align the remuneration of any new Executive Director following the same principles as for the current Executive Directors (set out in the policy table on pages 80 and 81)

The elements that would be considered by the Company for inclusion in the remuneration package for a new Director are in line with those offered to existing Directors (see the policy table on page 84 for more details)

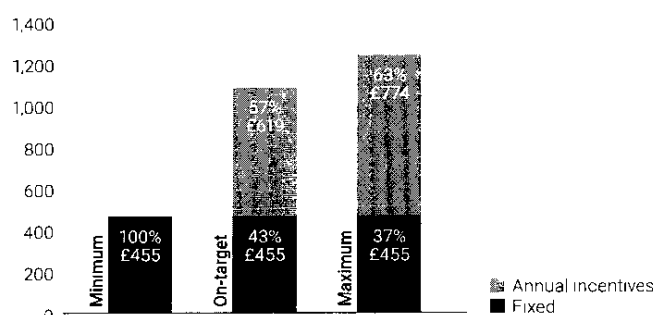
- ~ Salary and benefits including defined contribution pension participation or a salary supplement in lieu of pension provision
- ~ Participation in the EIP of up to 200% of salary
- ~ Participation in all-employee share plans operating at that time
- ~ Costs relating to, but not limited to, relocation, legal, financial, tax and visa advice and pre-employment medical checks

The maximum variable remuneration will be 200% of salary

The Committee may make awards on appointing an Executive Director to 'buy out' remuneration arrangements forfeited on leaving a previous employer. Awards made by way of compensation for forfeited awards would be made on a comparable basis, taking account of performance achieved (or likely to be achieved), the proportion of the performance period remaining and the form of the award. Compensation could be in cash or shares.

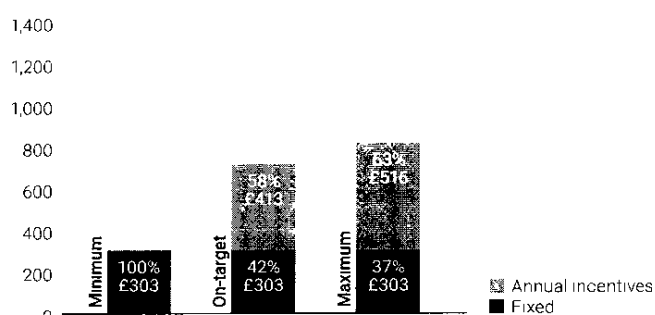
D J Miles

Remuneration (£'000)



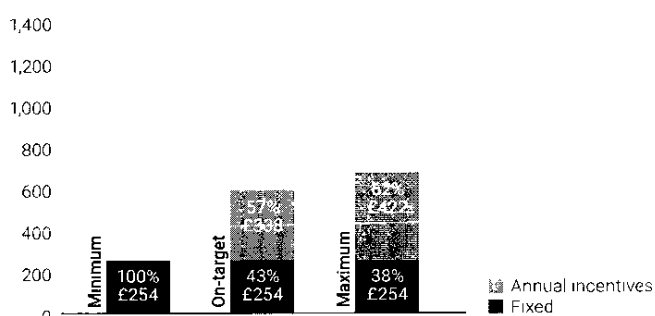
A C M Smith

Remuneration (£'000)



A Long

Remuneration (£'000)



Corporate governance

Remuneration policy continued

Service contracts and payment for loss of office

Director	Date of contract/letter of appointment	Notice period by Company or Director
Executive		
D J Miles	June 2008	Twelve months
A C M Smith	June 2008	Twelve months
A Long	August 2009	Twelve months
Chairman/Non-Executive		
K Murphy	January 2019	Six months
G Davies	October 2015	Six months
J Unwin	January 2016	Six months
J Burt	February 2017	Six months
R Irwin	February 2017	Six months
E Corrado	September 2017	Six months
A Hillerby	June 2018	Three months

All Executive Directors' contracts are rolling and, therefore, will continue unless terminated by written notice. In the event of the termination of an Executive Director's contract, salary and benefits will be payable during the notice period. There will, however, be no automatic entitlement to bonus payments or share incentive grants during the period of notice.

The rules of the EIP set out what happens to awards if a participant ceases to be an employee or Director of Mears before the end of the vesting period. Generally, any outstanding share awards will lapse on such cessation, except in certain circumstances.

If the Executive Director ceases to be an employee or Director as a result of death, injury, ill health, redundancy, retirement, the sale of the business or company that employs the individual or any other reason at the discretion of the Committee, then they will be treated as a 'good leaver' under the plan rules.

Under the EIP, a proportion of a good leaver's award will vest on cessation of employment by reference to the time elapsed from grant to cessation. The Committee has discretion to determine the period during which the good leaver may exercise their award after cessation.

On a change of control, all awards under the EIP will vest immediately.

Chairman and Non-Executive Directors

The Board as a whole is responsible for setting the remuneration of the Non-Executive Directors, other than the Chairman, whose remuneration is determined by the Committee and recommended to the Board.

The table below sets out the key elements of the policy for the Chairman and Non-Executive Directors.

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
To provide compensation that attracts individuals with appropriate knowledge and experience	<p>Fee levels are reviewed periodically taking into account independent advice and the time commitment required of Non-Executive Directors.</p> <p>The fees paid to the Chairman and the fees of the other Non-Executive Directors aim to be competitive with other listed companies which the Committee (in the case of the Chairman) and the Board (in respect of the Non-Executive Directors) consider to be of equivalent size and complexity.</p> <p>Non-Executive Directors receive a base fee and additional fees for the role of Senior Independent Director or membership and/or chairmanship of certain Committees.</p> <p>The Chairman receives a single fee and does not receive any additional fees for membership and/or chairmanship of Committees.</p> <p>Non-Executive Directors also receive reimbursement of reasonable expenses (and any tax thereon) incurred through undertaking their duties and/or Company business.</p>	<p>Any increase in Non-Executive Director base fees or additional Committee/membership fees (if introduced) may be above the level awarded to other employees, given that they may only be reviewed periodically and may need to reflect any changes to time commitments or responsibilities.</p> <p>The maximum potential value of any benefits provided is the cost of these provisions.</p> <p>The Company will pay reasonable expenses incurred by Non-Executive Directors.</p> <p>Current fee levels are set out in the Statement of Implementation on page 90.</p>	<p>Non-Executive Director fees are not performance related.</p> <p>Non-Executive Directors do not receive any variable remuneration element.</p>

Other Non-Executive appointments

Executive Directors have an obligation to inform the Board, specifically the Remuneration Committee, of any Non-Executive positions held or being contemplated and of the associated remuneration package. The Remuneration Committee will consider the merits of each case and carefully consider the work and time commitment required to fulfil the Non-Executive duties and the potential benefit to the Group and then determine whether the remuneration should be retained by the Executive or passed over to the Group.

Consideration of employment conditions elsewhere in the Group in developing policy

In setting the remuneration policy for Executive Directors, the Remuneration Committee takes into account Group and business unit performance including both financial performance and safety improvements in the year. Due to the wide variety of labour market conditions and the markets in which we operate, pay rates are not normally considered when considering Executive Director base pay reviews. The Remuneration Committee reviews and notes the salaries of Senior Executives within the Group.

The Committee has not expressly sought the views of employees and no remuneration comparison measurements were used when drawing up the Directors' remuneration policy. Through the Board, however, the Committee is updated as to employee views on remuneration generally.

Consideration of shareholder views

The Committee is committed to an ongoing dialogue with shareholders and seeks shareholder views when any significant changes are being made to remuneration arrangements. We remain sensitive to the views of shareholders and sought to consult many of our largest shareholders regarding the changes we made to the remuneration policy in 2017.

The Company will continue to monitor shareholder comments and retain an open dialogue as necessary.

Corporate governance

Annual remuneration report 2018

Annual report on remuneration

This section of the remuneration report contains details of how the Company's remuneration policy for Directors was implemented during the financial year

Single total figure of remuneration (audited)

Executive Directors

The remuneration of Executive Directors showing the breakdown between elements and comparative figures is shown below. Figures provided have been calculated in accordance with the regulations

Executive Director (£'000)	Year	Salary	Taxable benefits	Pension	Annual incentives	Total remuneration
D J Miles	2018	387	10	58	~	455
	2017	369	19	55	~	443
A C M Smith	2018	258	6	39	~	303
	2017	250	7	37	~	294
A Long	2018	211	11	32	~	254
	2017	205	12	31	~	248

Non-Executive Directors

The remuneration of Non-Executive Directors showing the breakdown between elements and comparative figures is shown below. Figures provided have been calculated in accordance with the regulations

Chairman and Non-Executive Director (£'000)	Year	Salary	Taxable benefits	Pension	Annual incentives	Total remuneration
R Holt	2018	220	–	–	–	220
	2017	233	14	38	–	285
G Davies	2018	70	–	–	–	70
	2017	60	–	–	–	60
J Unwin	2018	70	–	–	–	70
	2017	60	–	–	–	60
R Irwin	2018	70	–	–	–	70
	2017	42	–	–	–	42
J Burt	2018	70	–	–	–	70
	2017	58	–	–	–	58
E Corrado	2018	55	–	–	–	55
	2017	14	–	–	–	14
A Hillerby	2018	29	2	–	–	31
	2017	–	–	–	–	–
K Murphy	2018	–	–	–	–	–
	2017	–	–	–	–	–
P F Dicks	2018	35	–	–	–	35
	2017	60	–	–	–	60
M G Rogers	2018	–	–	–	–	–
	2017	20	–	–	–	20
D L Hosein	2018	–	–	–	–	–
	2017	20	–	–	–	20

Additional details in respect of single total figure table (audited)

The performance measures and targets for the EIP for the year ended 31 December 2018 are detailed below. Despite the fact that a number of performance targets were met, the Executive team requested that no awards are made under the EIP in respect of the 2018 financial year.

Description	Weighting	Calculation	Targets
Earnings per share (EPS)	40%	<ul style="list-style-type: none"> ~ Growth in diluted EPS ~ Diluted EPS is stated before exceptional costs and amortisation of acquisition intangibles and is adjusted for a normalised tax charge from 1 January 2018 to 31 December 2018 ~ Base figure of 30.36p to be used 	Threshold ~ 8% EPS growth leads to 20% maximum contribution Maximum ~ 13% EPS growth leads to 100% maximum contribution ~ Straight-line contribution between 8% and 13%
Return on capital employed (ROCE)	20%	<ul style="list-style-type: none"> ~ Operating profit divided by capital employed ~ Operating profit is stated before acquisition intangible amortisation and exceptional costs ~ Capital employed is defined as total assets less current liabilities less all balances relating to bank borrowings and overdrafts classified within non-current liabilities at 31 December 2018 	Threshold ~ 15% ROCE leads to 20% maximum contribution Maximum ~ 20% ROCE leads to 100% maximum contribution ~ Straight-line contribution between 15% and 20%
EBITDA cash conversion	20%	<ul style="list-style-type: none"> ~ Cash inflow from operating activities as a proportion of EBITDA measured at 31 December 2018 	Threshold ~ 80% cash conversion leads to 20% maximum contribution Maximum ~ 100% cash conversion leads to 100% maximum contribution ~ Straight-line contribution between 80% and 100%
Customer satisfaction	10%	<ul style="list-style-type: none"> ~ The measure is the percentage of customers who rate our service as 'excellent' ~ This output is generated from around 80,000 customer surveys carried out during 2018 	~ A level of customer service 'excellent' rating of 90% must be achieved in order to deliver a maximum contribution
Health and safety	10%	<ul style="list-style-type: none"> ~ The measure is accident frequency rate (AFR). It is calculated as the number of reportable incidents divided by the number of hours worked, multiplied by 100,000 	~ An AFR below 0.25 must be achieved in order to deliver a maximum contribution

The actual performance achievement is summarised below:

Performance measures	Actual	% of target satisfied
EPS growth	4%	0%
ROCE	17%	45%
EBITDA to cash conversion	4%	0%
Customer service – 'excellent' rating	93%	100%
AFR	0.22	100%

The Remuneration Committee and the Executive team have agreed that no awards will be made under the EIP in respect of the 2018 financial year.

Corporate governance
Annual remuneration report 2018 continued

Statement of Directors' shareholding and share interests (audited)

Directors' share interests are set out below

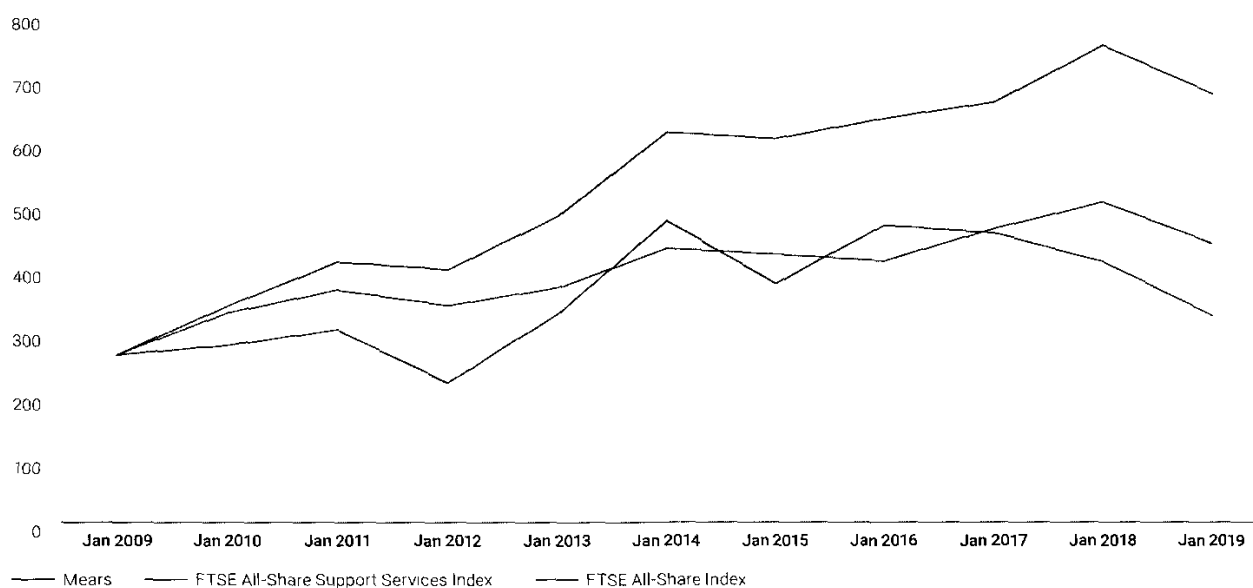
Director	Number of beneficially owned shares	Share interests		Total interests held at year end
		Vested but unexercised	Options	
D J Miles	175,020	164,729	—	339,749
A C M Smith	110,000	69,333	—	179,333
A Long	36,230	56,727	—	92,957
K Murphy	—	—	—	—
G Davies	2,500	—	—	2,500
J Unwin	—	—	—	—
J Burt	—	—	—	—
R Irwin	—	—	—	—
E Corrado	—	—	—	—
A Hillerby	—	—	—	—

Shareholder dilution

In accordance with the Association of British Insurers' guidelines, the Company can issue a maximum of 10% of its issued share capital in a rolling ten-year period to employees under all its share plans. In addition, of this 10% the Company can issue 5% to satisfy awards under discretionary or Executive plans. The Company operates all its share plans within these guidelines.

Performance graph and table (unaudited)

The graph below shows the Group's performance, measured by TSR, compared with the constituents of the FTSE All-Share Support Services sector over the last nine years. The index is the most relevant to compare the Group's performance against its peers.



The table below shows the Chief Executive Officer's remuneration package over the past nine years, together with incentive payout/vesting as compared to the maximum opportunity

Year	Name	Single figure of total remuneration (£'000)	Bonus payout (as % maximum opportunity)	Long-term incentive accrual rate (as % maximum opportunity)
2018	D J Miles	455	–	–
2017	D J Miles	443	–	–
2016	D J Miles	436	–	–
2015	D J Miles	436	–	20%
2014	D J Miles	412	–	35%
2013	D J Miles	825	–	100%
2012	D J Miles	409	–	–
2011	D J Miles	384	–	–
2010	D J Miles	270	–	–
	R Holt	600	–	–
2009	R Holt	1,095	100%	–

Percentage change in Chief Executive Officer's remuneration (unaudited)

The table below compares the percentage change in the salary of the Chief Executive Officer with that of the wider employee population

	Remuneration		
	Salary entitlement	Benefits	Bonus/incentives
Chief Executive Officer	–	–	–
Office salaries	1.3%	–	–

The Chief Executive Officer's basic salary equates to 10.3 times the pay of the average administrative employee, normalised to reflect a 60 hour working week. On a similar basis, the Chief Executive Officer's pay equates to 15.8 times the lowest paid worker. This will reduce to 15.1 times following the pay increases to be applied in April 2019.

Relative importance of spend on pay (unaudited)

The table below sets out the relative importance of spend on pay in the financial year and previous financial year compared with other disbursements from profit.

Significant distributions	Disbursements from profit in financial year 2018 (£'000)	Disbursements from profit in previous financial year 2017 (£'000)	% change
Total Directors' pay	1,628	1,634	–
Profit distributed by way of dividend	12,539	12,219	+2%
Underlying profit before tax	38,522	37,122	+4%

Statement of implementation of remuneration policy in the following financial year

Executive Directors

Salary

The salary entitlements for the forthcoming year are set out below

Executive Director	2019 £	2018 £	% change
D J Miles	386,817	386,817	0%
A C M Smith	257,912	257,912	0%
A Long	211,019	211,019	0%

Corporate governance

Annual remuneration report 2018 continued

Pension

Details of pension contributions for the year ended 31 December 2019 are set out below

Executive Director	Pension
D J Miles	15%
A C M Smith	15%
A Long	15%

EIP

As set out in the policy table, the EIP is split into two parts: the deferred share award and the performance share award. Set out below is the maximum opportunity of each part for the year ended 31 December 2019

Part A – Deferred share award (% of salary)	Part B – Performance share award (% of salary)
100%	100%

For the 2019 EIP, the performance share award threshold level of vesting is 20% for each measure. The measures and weightings are set out below

Condition	Weighting	Payout range (threshold to maximum opportunity)
EPS	40%	20%–100%
ROCE	40%	20%–100%
EBITDA cash conversion		20%–100%
Other	20%	20%–100%
Customer satisfaction		20%–100%
Health and safety		20%–100%

In setting targets, the Committee takes into consideration (amongst other items)

- ~ the Company's business plan,
- ~ consensus forecasts for the Company, and
- ~ alignment with the Company's business strategy

Non-Executive Directors

The following table sets out the fee rates for the Non-Executive Directors

	2019	2018	% change
Chairman fee	160,000	220,000	-27%
Base fee	50,000	50,000	0%
Committee Chairman fee	15,000	15,000	0%
Committee membership fee	5,000	5,000	0%

Role of the Committee and activities

The Committee determines the total individual remuneration packages of each Executive Director of the Group and certain other senior employees (and any exit terms) and recommends to the Board the framework and broad policies of the Group in relation to Senior Executive remuneration. The Committee determines the targets for all of the Group's performance related remuneration and exercises the Board's powers in relation to all of the Group's share and incentive plans.

There is a formal and transparent procedure for developing policy on Executive remuneration and for determining the remuneration of individual Directors.

The Remuneration Committee is responsible for

- ~ determining and agreeing with the Board the broad remuneration policy for
 - the Chairman, the Executive Directors and senior management, and
 - the Executive Directors' remuneration and other benefits and terms of employment, including performance related bonuses and share options, and
- ~ approving the service agreements of each Executive Director, including termination arrangements

No Director is involved in determining his/her own remuneration

Annual overview

The Committee has continued to work to build investor confidence with regard to its Executive remuneration policies and remains committed to the following actions

- ~ Improving the level of openness and transparency in remuneration reporting through a detailed Annual Remuneration Report
- ~ Operating a structured incentive arrangement with clear financial performance targets for each year
- ~ Undertaking a regular review of the remuneration policies for Executive Directors and other Senior Executives within the Group to ensure that they remain appropriate to retain and motivate such individuals
- ~ Considering pay policies within the Group as a whole when determining Executive Directors' remuneration packages
- ~ Encouraging Executive Directors and Senior Executives to build up a meaningful shareholding in the Company to more closely align the interests of shareholders and Executives
- ~ Being kept fully aware and informed on developments and best practice in the field of remuneration and corporate governance from external advisers, institutional shareholders and their representative bodies

Notwithstanding the above, the Committee recognises that the success of the Group is dependent on the efforts of key individuals and that they should be fairly rewarded for their efforts and contributions in making Mears the success it is

Statement of voting at general meeting

The table below shows the historical voting outcomes in respect of the remuneration policy and Annual Remuneration Report

Item	Votes for	%	Votes against	%	Votes withheld
To approve the Annual Report on Remuneration	77,588,906	93	5,532,133	7	4,000

The total number of ordinary shares eligible to vote at the 2018 AGM was 103,621,576. Every shareholder has one vote for every ordinary share held.

Corporate governance Report of the Directors

The Directors present their report together with the consolidated financial statements for the year ended 31 December 2018.

Principal activities

The principal activities of the Group are the provision of a range of outsourced services to the public and private sectors. The principal activity of the Company is to act as a holding company.

Business review

The Company is required to set out a fair review of the business of the Group during the reporting period. The information that fulfils this requirement can be found in the Strategic Report, Review of Operations and Financial Review. The results of the Group can be found within the consolidated income statement. Information required to be disclosed in respect of emissions and future developments is included within the Strategic Report.

Dividend

The final dividend in respect of 2017 of 8.55p per share was paid in July 2018. An interim dividend in respect of 2018 of 3.55p was paid to shareholders in November 2018. The Directors recommend a final dividend of 8.85p per share for payment on 4 July 2019 to shareholders on the Register of Members on 14 June 2019. This has not been included within the consolidated financial statements as no obligation existed at 31 December 2018.

Corporate governance

Details of the Group's corporate governance are set out on pages 66 to 71.

Key performance indicators (KPIs)

We focus on a range of key indicators to assess our performance. Our performance indicators are both financial and non-financial and ensure that the Group targets its resources around its customers, employees, operations and finance. Collectively they form an integral part of the way that we manage the business to deliver our strategic goals. Our primary performance indicators are detailed on pages 34 to 37.

Directors

The present membership of the Board is set out with the biographical detail on pages 64 and 65.

In line with current practice, all of the Directors will retire and, being eligible, offer themselves for re-election at the AGM in May 2019. Any person appointed by the Directors must retire at the next AGM and will be eligible for re-election at that meeting.

The beneficial interests of the Directors in the shares of the Company at 31 December 2018 are detailed within the Remuneration Report on page 88.

The process governing the appointment and replacement of Directors is detailed within the Report of the Nomination Committee on pages 72 and 73.

Amendment to Articles of Association

The Company's Articles of Association can be amended only by a special resolution of the members, requiring a majority of not less than 75% of such members voting in person or by proxy.

Share capital authorisations

The 2018 Annual General Meeting (AGM) held in June 2018 authorised

- ~ the Directors to allot shares within defined limits. The Companies Act 2006 requires directors to seek this authority and, following changes to Financial Services Authority (FSA) rules and institutional guidelines, the authority was limited to one third of the issued share capital, a total of £345,405 plus an additional one third of issued share capital of £345,405 that can only be used for a rights issue or similar fundraising,
- ~ the Directors to issue shares for cash on a non-preemptive basis. This authority was limited to 10% of the issued share capital of £103,620 and is required to facilitate technical matters such as dealing with fractional entitlements or possibly a small placing, and
- ~ the convening of general meetings (other than an AGM) on 14 days' notice. This results from a European Union directive that became effective on 3 August 2010 and will override Section 307 of the Companies Act 2006 where the requirement to give 21 days' notice for certain meetings has been amended.

Further details of these authorisations are available in the notes to the 2018 Notice of AGM. Shareholders are also referred to the 2019 Notice of AGM, which contains similar provisions in respect of the Company's equity share capital as detailed below.

AGM

The 2019 AGM will be held on 31 May 2019 at 9.30am and a formal Notice of Meeting and Form of Proxy will be issued in advance. *The ordinary business to be conducted will include the reappointment of all Directors.*

Principal risks and uncertainties

Risk is an accepted part of doing business. The Group's financial risk management is based on sound economic objectives and good corporate practice. The Board has overall responsibility for risk management and internal controls within the context of achieving the Group's objectives. Our process for identifying and managing risks is set out in more detail within the Corporate Governance Statement. The key risks and mitigating factors are set out on pages 40 to 42. Details of financial risk management and exposure to price risk, credit risk and liquidity risk are given in note 24 to the financial statements.

Contracts of significance

The Group is party to significant contracts within each segment of its business. The Directors do not consider that any one of those contracts is essential in its own right to the continuation of the Group's activities.

Payment policy

The Company acts purely as a holding company and as such is non-trading. Accordingly, no payment policy has been defined. However, the policy for Group trading companies is to set the terms of payment with suppliers when entering into a transaction and to ensure suppliers are aware of these terms. Group trade creditors during the year amounted to 55 days (2017: 60 days) of average supplies for the year.

Capital structure

The Group is financed through both equity share capital and debt. Details of changes to the Company's share capital are given in note 26 to the financial statements. The Company has a single class of shares – ordinary 1p shares – with no right to any fixed income and with each share carrying the right to one vote at the general meetings of the Company. Under the Company's Articles of Association, holders of ordinary shares are entitled to participate in any dividends pro-rata to their holding. The Board may propose and pay interim dividends and recommend a final dividend for approval by the shareholders at the AGM. A final dividend may be declared by the shareholders in a general meeting by ordinary resolution but such dividend cannot exceed the amount recommended by the Board.

Substantial shareholdings

As at 27 February 2019 the Company has been notified of, or is aware of, the shareholders holding 1.5% or more of the issued share capital of the Company, as detailed in the table below.

Fund manager	City	Shares (m)	% IC
PrimeStone Capital	London	15.0	13.6%
Shareholder Value Management	Frankfurt	12.8	11.6%
Majedie Asset Management	London	10.5	9.5%
Artemis Investment Management	Edinburgh, London	7.9	7.1%
Heronbridge Investment Management	Bath	7.2	6.5%
Fidelity Management & Research	Boston	5.3	4.8%
Legal & General Investment Management	London	5.1	4.6%
Dimensional Fund Advisors	London	4.7	4.3%
Columbia Threadneedle Investments	London	4.3	3.9%
Close Asset Management	London	2.6	2.3%
Montanaro Asset Management	London	2.5	2.2%
M&G Investment Management	London	2.4	2.2%
Slater Investments	London	2.2	2.0%

Disabled employees

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Group continues and that appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

GHG emissions

The Group's carbon emissions data for the year is provided below. Scope 1 emissions, which are generated from owned or controlled sources such as vehicles, have reduced while Scope 2 emissions, which are from the generation of purchased energy, have increased. This is as a result of the change in mix between traditional maintenance work, which naturally requires significant vehicle usage and management of properties, which consume electricity. There has also been an overall reduction as a result of more efficient working practices across the Group.

These figures have been generated from independently provided reports of carbon emissions or energy usage from a variety of sources and, where necessary, energy usage has been converted into carbon emissions using the 2018 dataset provided by the Department for Environment, Food & Rural Affairs.

Scope	Units	2017	2018
Scope 1	Tonnes CO ₂ e	19069	17437
Scope 2	Tonnes CO ₂ e	1482	2008
Scope 1 and Scope 2		2017	2018
Intensity tonnes CO ₂ e/£m Revenue		22.83	22.36

Employee information and consultation

The Group has received recognition under the 'Investors in People' award. The Group continues to involve its staff in the future development of the business. Information is provided to employees through a daily news email, a quarterly newsletter posted out to all staff, the Group website and the intranet to ensure that employees are kept well informed of the performance and objectives of the Group.

CREST

CREST is the computerised system for the settlement of share dealings on the London Stock Exchange. CREST reduces the amount of documentation required and also makes the trading of shares faster and more secure. CREST enables shares to be held in an electronic form instead of the traditional share certificates. CREST is voluntary and shareholders can keep their share certificates if they wish. This may be preferable for shareholders who do not trade in shares on a frequent basis.

Auditor

Grant Thornton UK LLP offers itself for reappointment as auditor in accordance with Section 489 of the Companies Act 2006.

By order of the Board

B Westran
Company Secretary
ben.westran@mearsgroup.co.uk
22 March 2019

Statement of Directors' responsibilities In respect of the Directors' Report and financial statements

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors are required to prepare Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and have elected to prepare the Company financial statements in accordance with United Kingdom 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 and profit or loss of the Group and 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 accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- ~ prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the financial statements and Remuneration Report comply with the Companies Act 2006 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that

- ~ so far as each Director is aware there is no relevant audit information of which the Company's auditor is unaware; and
- ~ the Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

To the best of our knowledge

- ~ the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole, and
- ~ the Annual Report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The Directors are responsible for preparing the Annual Report in accordance with applicable law and regulations. The Board considers the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and that it provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

Going concern

We principally operate in robust defensive markets, social housing and care, where spend is largely non-discretionary and our contracts tend to be long-term partnerships.

The Group had net debt of £65.9m at 31 December 2018. The core debt required to satisfy the day-to-day requirements of the business is in the region of £120m. This represents significant headroom against the £155m unsecured revolving credit facility, with an additional accordion mechanism allowing the facility to be increased to a maximum of £45m, maturing in November 2022.

After reviewing the Group and Company's budget for the next financial year and longer-term plans, the Directors consider that, as at the date of approving the financial statements, it is appropriate to adopt the going concern basis in preparing the financial statements.

On behalf of the Board

A C M Smith
Finance Director
andrew.smith@mearsgroup.co.uk
22 March 2019

Corporate governance

Independent auditor's report

To the members of Mears Group PLC

Our opinion on the financial statements is unmodified

We have audited the financial statements of Mears Group PLC (the 'parent company') and its subsidiaries (the 'group') for the year ended 31 December 2018, which comprise the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated balance sheet, the Consolidated cash flow statement, the Consolidated statements of changes in equity, the parent company balance sheet, the parent company statement of changes in equity and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' (United Kingdom Generally Accepted Accounting Practice).

In our opinion

- ~ the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2018 and of the group's profit for the year then ended,
- ~ the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union,
- ~ the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- ~ the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the 'Auditor's responsibilities for the audit of the financial statements' section of our report. We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

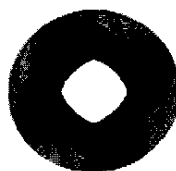
Conclusions relating to principal risks, going concern and viability statement

We have nothing to report in respect of the following information in the annual report, in relation to which the ISAs (UK) require us to report to you whether we have anything material to add or draw attention to

- ~ the disclosures in the annual report set out on pages 38–42 that describe the principal risks and explain how they are being managed or mitigated,
- ~ the directors' confirmation set out on page 40 of the annual report that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity,

- ~ the directors' statement set out on page 96 of the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the directors' identification of any material uncertainties to the group and the parent company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements,
- ~ whether the directors' statement relating to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit, or
- ~ the directors' explanation set out on pages 43–44 of the annual report as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions

Overview of our audit approach



- ~ We determined materiality for the audit of the financial statements as a whole to be £2.0 million,
- ~ Key audit matters were identified as revenue recognition (including contract accounting, contract assets and contract accruals), goodwill impairment, defined benefit pension schemes and acquisition accounting (including valuation of goodwill and intangibles), and
- ~ We performed full scope audit procedures on the financial information of six companies and specific audit procedures over certain balances and transactions at four further companies to gain sufficient, appropriate audit evidence over all material balances at both divisional and group levels. We performed analytical procedures on the financial information on the remaining thirty three companies in the group.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those that had the greatest effect on the overall audit strategy, the allocation of resources in the audit, and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Corporate governance
Independent auditor's report *continued*
To the members of Mears Group PLC

Key Audit Matter – Group

How the matter was addressed in the audit – Group

Revenue recognition (including contract accounting, contract assets and contract accruals)

Our audit work included, but was not restricted to:

Revenue is recognised throughout the group as the fair value of consideration receivable in respect of the performance of contracts and the provision of services. The group adopted International Financial Reporting Standard (IFRS) 15 'Revenue from Contracts with Customers' for the financial year ended 31 December 2018.

Determining the amount of revenue to be recognised requires management to make significant judgements and estimates in the application of the new IFRS, the stage of completion of certain contracts and the recoverability of work-in-progress, mobilisation costs and contract assets.

We therefore identified revenue recognition, including contract accounting, contract assets and contract accruals, as a significant risk, which was one of the most significant assessed risks of material misstatement.

- ~ assessing whether the accounting policies adopted by the directors are in accordance with the requirements of IFRS 15, and whether management accounted for revenue in accordance with the accounting policies, including the accounting and disclosure for the transition to the new IFRS,
- ~ testing key controls, where applicable, over the recognition of revenue and the allocation of costs to the contracts, covering invoicing and cost approvals and for the Care business unit to timesheet authorisation,
- ~ selecting contracts by reference to materiality and other risk factors including loss making contracts, contracts with significant aged contract assets and receivables balances or significant increases in these balances, contracts with disputes, and contracts relating to site locations we visited during the year,
- ~ selecting a further sample of revenue transactions, contract assets and contract accruals balances, to ensure coverage across the group,
- ~ assessing, for the selected items and samples, whether the revenue recognised is in accordance with the group's accounting policies by agreeing details to contract terms, support for costs on which the revenue is derived, re-performing management's calculations and assessing management's assumptions and assertions underpinning their forecasts for contracts' future performance by reference to supporting documentation, such as contract KPIs, historical performance against forecasts, actual performance against previous estimates and discussions with key contract accounting personnel,
- ~ investigating the recoverability of contract assets and work-in-progress balances by reference to post balance sheet cash collection, certifications performed by the group or external quantity surveyors, reviewing the quality of supporting evidence, including internal and external legal opinions, expert value reports and correspondence with customers, and examining the group's historical experience of recovery,
- ~ identifying contracts that were at risk of incurring future losses during the remaining life of the contract. This included assessing all potentially onerous contracts in the prior year, but also any that had incurred significant losses during 2018, and
- ~ examining such contracts and challenging management's assumptions and assertions relating to the future results of those contracts by reference to supporting evidence such as management's plans to return the contract to profit, forecast models, previous history of turning around loss making contracts and correspondence with clients where appropriate.

The group's accounting policy on revenue recognition is shown in 'Principal accounting policies – group' to the financial statements on pages 108–109 and related disclosures are included in note 1. The Audit Committee identified revenue recognition as a primary area of judgement in its report on page 78 where the Audit Committee also described the action that it has taken to address this issue.

Key observations

Based on our audit work, we did not identify any material misstatement in the revenue recognised in the year to 31 December 2018 or in the contract assets and contract accrual balances as at that date.

Goodwill impairment	Our audit work included, but was not restricted to:
<p>The directors are required to make an annual assessment to determine whether the carrying value of goodwill of £196.7 million is impaired. Past experience has indicated that there is significant headroom in the goodwill balance relating to the Social Housing division Cash Generating Unit ('CGU') but limited headroom in the goodwill balance relating to the Care division CGU, which accounts for £112.4 million of the carried goodwill.</p> <p>The process for assessing whether an impairment exists under Internal Accounting Standard (IAS) 36 'Impairment of Assets' is complex. Calculating the value in use, through forecasting cash flows related to CGUs and the determination of the appropriate discount rate and other assumptions to be applied can be highly judgemental and can significantly impact the results of the impairment review.</p> <p>We therefore identified the impairment review of goodwill undertaken by management in relation to the Care division as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<ul style="list-style-type: none"> ~ assessing whether the accounting policies adopted by the directors are consistent with the prior year and in accordance with the requirements of IAS 36, ~ obtaining management's discounted cash flow forecast for the Care division used in the impairment review and comparing it to our understanding of the division and recalculating the arithmetical accuracy of those calculations, ~ testing and challenging the assumptions utilised in the impairment models, including the increase in carer hours, the new contract wins and the ability to pass on uplifts in payroll costs to local authorities, ~ considering whether the market level assumptions used were appropriate and where possible, benchmarking these assumptions against available industry data including assessing these against the work done by an external expert, ~ performing sensitivity analysis on the various assumptions used for this model to consider the headroom levels for various scenarios, and ~ testing the accuracy of management's forecasting through a comparison of budget to actual data and historical variance trends and investigating the cash flows for exceptional or unusual items or assumptions. <p>The group's accounting policy on impairment is shown in 'Principal accounting policies – group' to the financial statements on page 107 and related disclosures are included in note 13. The Audit Committee identified carrying value of goodwill as a primary area of judgement in its report on page 77, where the Audit Committee also described the action that it has taken to address this issue.</p> <p>Key observations</p> <p>Based on our audit work, we found the valuation methodologies and assumptions made in management's assessment of goodwill impairment were appropriate. We consider that the group's disclosure to be in accordance with IAS 36 and have found no material errors in calculations.</p>
Defined benefit pension schemes	Our audit work included, but was not restricted to:
<p>The group operates a number of defined benefit pension schemes and is admitted body of a number of other defined benefit pension schemes. At 31 December 2018 the defined benefit pension schemes had a combined net surplus of £20m, of which £14m is recognised in the financial statements as recoverable. The gross value of the pension assets and obligations which form the net surplus amounted to £439m and £419m respectively.</p> <p>The measurement of the obligations in accordance with IAS 19 'Employee benefits' involves significant judgement and their valuation is subject to complex actuarial assumptions. Small variations in those actuarial assumptions can lead to a materially different value of pension liabilities being recognised within the group financial statements.</p> <p>We therefore identified the valuation of the defined benefit pension schemes obligations as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<ul style="list-style-type: none"> ~ assessing whether the accounting policies adopted by the directors are appropriate and in accordance with the requirements of IAS 19, ~ utilising the expertise of our actuarial specialists in order to review the appropriateness of the assumptions used in the calculation of the obligations and testing the appropriateness of the valuation methodologies and their inherent actuarial assumptions by benchmarking key assumptions such as discount rates, wages and salary growth rates and mortality rates to available market data, ~ testing the accuracy of underlying membership data utilised by the group's actuaries for the purpose of calculating the scheme liabilities by selecting a sample of employees and agreeing membership to underlying records, ~ directly confirming the existence and valuation of pension scheme assets with asset managers for group schemes and analysing the movements on assets for admitted body schemes, and ~ checking the treatment of Guaranteed Minimum Pension (GMP) service cost and ensuring this has been accounted and disclosed for correctly. <p>The group's accounting policy on defined benefit pensions is shown in 'Principal accounting policies – group' to the financial statements on page 110 and related disclosures are included in note 29. The Audit Committee identified defined benefit pension valuation as a primary area of judgement in its report on page 78, where the Audit Committee also described the action that it has taken to address this issue.</p> <p>Key observations</p> <p>Based on our audit work, we found the actuarial assumptions used for the defined benefit pension schemes to be reasonable. We consider that the group's disclosure appropriately describes the significant degree of inherent uncertainty in the assumptions and estimates and the potential impact on future periods of revisions to these estimates. We found no material errors in calculations.</p>

Corporate governance
Independent auditor's report continued
To the members of Mears Group PLC

Acquisition accounting (including valuation of goodwill and intangibles)	Our audit work included, but was not restricted to:
<p>During the year the group acquired the entire share capital of MPS Housing Limited and Mitie Property Management Limited. This acquisition has had a material impact on the financial statements, resulting in the recognition of goodwill and intangible assets on consolidation of £20.7 million into the group.</p> <p>The group measures goodwill at the acquisition date as being the fair value of consideration, including the estimated value of deferred consideration, transferred less the net recognised amount of identifiable assets acquired and liabilities assumed. Goodwill of £3.3 million was recognised as a result of the acquisition of MPS Housing Limited and Mitie Property Management Limited.</p> <p>Under IAS 38 'Intangible Assets', intangible assets acquired in a business combination are deemed to have a cost to the group equal to their fair value at the acquisition date. Intangible assets of £17.4 million were recognised as a result of the acquisition. These intangibles were valued, based on discounted cash flow forecasts prepared by management, which require judgement by the Directors around key assumptions such as revenue growth, discount rates, customer attrition and long term growth rates.</p> <p>On initial recognition, the assets and liabilities acquired in a business combination are included in the consolidated balance sheet at their fair values, which are also used as the basis for subsequent measurement in accordance with the group accounting policies. Determining the fair value of certain assets and liabilities requires judgement to be exercised by the Directors, particularly in respect of estimating the value in use of assets acquired and capturing contingent liabilities not previously recognised in the financial statements.</p> <p>Due to the significant financial statement impact of the acquisition, as well as the high level of estimation required in determining the appropriate accounting treatment, we therefore identified acquisition accounting, including valuation of goodwill and intangibles, as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<ul style="list-style-type: none"> ~ assessing whether the accounting policies adopted by the directors are in accordance with the requirements of IAS 38, ~ obtaining an understanding of the acquisition through review of legal agreements and discussion with management of both Mears and the acquired companies, ~ re-performing management's calculation of the fair value of the consideration, including the estimated value of the deferred consideration transferred less the net recognised amount of identifiable assets acquired and liabilities assumed, ensuring this is in accordance with the requirements of IFRS 3 "Business Combinations", ~ using our internal valuation expert to evaluate and assess the assumptions used, including discount rates, growth rates and forecast future trading performance, in the calculation of the fair value of the intangibles recognised, ~ testing the accuracy of the data used in the intangibles valuation by agreeing data to pertinent supporting documentation such as long-term growth forecasts, ~ testing significant fair value adjustments made to the assets and liabilities acquired, and challenging management's assumptions in the value in use assigned to certain assets, and ~ assessing the adequacy of disclosures in respect of the acquisition to ensure these are in accordance with IAS 38 and IFRS 3. <p>The group's accounting policy on acquisition accounting is shown in 'Principal accounting policies – group' to the financial statements on pages 105–106 and related disclosures are included in note 28.</p> <p>Key observations</p> <p>Based on our audit work, we found that the assumptions and judgements used in management's accounting treatment of the Mitie acquisition were reasonable. We also note that the valuation of goodwill and intangibles is not materially misstated. We found no material errors in the underlying calculations.</p>

We did not identify any key audit matters relating to the audit of the financial statements of the parent company.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality in determining the nature, timing and extent of our audit work and in evaluating the results of that work.

Materiality was determined as follows:

Materiality measure	Group	Parent
Financial statements as a whole	<p>We determined materiality for the audit of the financial statements as a whole to be £2.0 million.</p> <p>Our determination of materiality included a consideration of a number of benchmarks that we believe to be of importance to the users of the financial statements, most notably the group's preliminary earnings before interest, tax and amortisation. This benchmark is considered particularly important due to the significant level of user focus on this figure in assessing the group's performance.</p> <p>The level of materiality however, was not determined using a single particular benchmark as we considered the financial statements in their entirety, therefore the appropriate amount of materiality was determined to be £2.0 million based on a review of the financial statements, and this amount was evaluated for appropriateness by reference to a range of key benchmarks.</p> <p>Materiality for the current year is higher than the level that we determined for the year ended 31 December 2017 as a result of the increased adjusted earnings before interest, tax and amortisation in the current year.</p>	<p>We determined materiality for the audit of the parent company financial statements to be £0.75 million.</p> <p>Our determination of materiality included a consideration of a number of benchmarks that we believe to be of importance to the users of the financial statements, most notably the company's total assets. This benchmark is considered particularly important due to the principal activity of the company being an investment holding company.</p> <p>The level of materiality however was not determined using a single particular benchmark as we considered the financial statements in their entirety, therefore the appropriate amount of materiality was determined to be £0.75 million based on a review of the financial statements, and this amount was evaluated for appropriateness by reference to a range of key benchmarks.</p> <p>Materiality for the current year is higher than the level that we determined for the year ended 31 December 2017 as a result of the increase in total assets of the company at the year end.</p>
Performance materiality used to drive the extent of our testing	Based on our risk assessment, including the group's overall control environment, we determined a performance materiality of 75% of the financial statement materiality.	Based on our risk assessment, including the company's overall control environment, we determined a performance materiality of 75% of the financial statement materiality.
Specific materiality	We determined a lower level of specific materiality for certain areas such as directors' remuneration and related party transactions.	We determined a lower level of specific materiality for certain areas such as directors' remuneration and related party transactions.
Communication of misstatements to the audit committee	We communicate misstatements exceeding £0.1 million and misstatements below that threshold that, in our view, warrant reporting on qualitative grounds.	We communicate misstatements exceeding £0.038 million and misstatements below that threshold that, in our view, warrant reporting on qualitative grounds.

Corporate governance

Independent auditor's report continued

To the members of Mears Group PLC

An overview of the scope of our audit

Our audit approach was a risk-based approach founded on a thorough understanding of the group's business, its environment and risk profile. In order to address the risks described above as identified during our planning procedures, we performed a full scope audit of the financial statements of the parent company, Mears Group PLC and of the group's operations throughout the United Kingdom.

The companies of the group were evaluated by the group engagement team based on a measure of materiality considered as a percentage of total group assets, revenues and earnings before taxes, to assess the significance of the component and to determine the planned audit response. For those components that we determined to be significant components, either a full scope approach or specific procedures in relation to specific balances and transactions were carried out. This approach was determined based on their relative materiality to the group and our assessment of audit risk, this approach is in line with our approach used in the prior year.

The group's companies vary significantly in size. We performed full scope audits at six companies. Specific audit procedures over certain balances and transactions were performed on a further four companies, to give appropriate coverage of all material balances at both divisional and levels. Together, the reporting units subject to audit procedures, being full scope and specific procedures, were responsible for 92% of the group's revenues, 82% of the group's earnings before interest, tax and amortisation and 50% of group's total assets. We performed analytical procedures over the remaining thirty three companies.

For significant components requiring a full scope approach, an interim visit was conducted before the year end to undertake substantive procedures in advance of the final visit and to evaluate the group's internal control environment. We sought wherever possible, to rely on the effectiveness of the group's internal controls which allows us to reduce substantive testing. We then undertook substantive testing on significant transactions and material account balances, including the procedures outlined above in relation to the key risks. For the components where specific procedures were carried out a similar testing strategy was applied, focused on the significant transactions and material account balances.

The remaining non-significant components of the group were subject to analytical procedures over their financial performance and position after taking into account the risks identified above and the significance of the component to the group.

Other information

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

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

We have nothing to report in this regard.

In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

- ~ Fair, balanced and understandable set out on page 96 – the directors consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit, or
- ~ Audit committee reporting set out on pages 76 to 80 – the section describing the work of the audit committee does appropriately address matters communicated by us to the audit committee, or
- ~ Directors' statement of compliance with the UK Corporate Governance Code set out on page 64 – the parts of the directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

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

- ~ the information given in the strategic report and the report of the directors for the financial year for which the financial statements are prepared is consistent with the financial statements, and
- ~ the strategic report and the report of the directors have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report under the Companies Act 2006

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the report of the directors.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion

- ~ adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or
- ~ the parent company financial statements and the part of the directors' remuneration report to be audited 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

Responsibilities of directors for the financial statements

As explained more fully in the statement of directors' responsibilities set out on page 96, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error

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

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements

We are responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. Owing to the inherent limitations of an audit, there is an unavoidable risk that material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the ISAs (UK). Our audit approach is a risk-based approach and is explained more fully in the 'An overview of the scope of our audit' section of our audit report

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 and through discussion with the directors and other management (as required by auditing standards), and from inspection of the group's regulatory correspondence 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. This included communication from the group to component audit teams of relevant laws and regulations identified at group level.

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

The group is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies legislation), distributable profits 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.

The group is subject to many other laws and regulations, we did not identify any others where the consequences of non-compliance alone could have a material effect on amounts or disclosures in the financial statements.

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 (irregularities) 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. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

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

Other matters which we are required to address

Following the recommendation of the audit committee, we were appointed by the Audit Committee in 1996 to audit the financial statements for the year ending 31 December 1996 and subsequent financial periods.

Corporate governance

Independent auditor's report continued To the members of Mears Group PLC

The period of total uninterrupted engagement is twenty two years, covering the years ending 31 December 1996 to 31 December 2018. *Following the recommendation of the audit committee, we were appointed by the board of the directors in 2017 to audit the financial statements for the years ending 31 December 2017 to 31 December 2021*

The non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company and we remain independent of the group and the parent company in conducting *our audit*

Our audit opinion is consistent with the additional report to the audit committee

Use of our report

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

Rebecca Eagle
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
Birmingham
22 March 2019

Financial statements

Principal accounting policies – Group

Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with IFRS as adopted by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS and therefore the consolidated financial statements comply with Article 4 of the EU International Accounting Standards (IAS) Regulation. The financial statements are prepared under the historical cost convention as modified by the revaluation of derivative financial instruments and share-based payments.

The most significant changes in accounting policies from the previous year were the introduction of IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments' for which the impact of introduction has been disclosed in note 3. The accounting policies remain otherwise unchanged from the previous year except for the modification of a number of standards with effect from 1 January 2018. Changes include Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2) and Annual Improvements 2014–2016 (which made amendments to IFRS 1 and IAS 28). The adoption of these amendments had no material effect on the Group's financial statements.

The preparation of financial statements in conformity with UK Generally Accepted Accounting Practice (UK GAAP) requires the use of estimates and judgements that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the year. Although these estimates are based on the Directors' best knowledge of the amounts, actual results may ultimately differ from those estimates. The most significant estimates made by the Directors in these financial statements are set out in 'Use of judgements and estimates' on pages 112 to 113.

Mears Group PLC is incorporated and domiciled in England and Wales (registration number 3232863). Its registered office and principal place of business is 1390 Montpellier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH. Mears Group PLC's shares are listed on the London Stock Exchange.

The Directors consider that, as at the date of approving the financial statements, there is a reasonable expectation that the Group and the Company have adequate resources to continue in operational existence for the foreseeable future. For this reason, the Directors continue to adopt the going concern basis in preparing the financial statements. The Directors have discussed the principal risks and uncertainties of the business in the Risk Management section on pages 38 to 42.

Basis of consolidation

The Consolidated Balance Sheet includes the assets and liabilities of the Company and its subsidiaries and is made up to 31 December 2018. Entities over which the Group has the ability to exercise control over financial and operating policies are accounted for as subsidiaries. Control is achieved where the Company has existing rights that give it the current ability to direct the activities that affect the Company's returns and exposure or rights to variable returns from the entity. Interests acquired in entities are consolidated from the effective date of acquisition and interests sold are consolidated up to the date of disposal.

All significant intercompany transactions and balances between Group enterprises, including unrealised profits arising from intra-group transactions, are eliminated on consolidation, no profit is taken on sales between Group companies.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling shareholders' share of changes in equity since the date of the combination. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interest having a deficit balance.

A joint venture is a joint arrangement whereby the parties that have joint control have the rights to the net assets of the arrangement. Investments in joint ventures are accounted for using the equity method of accounting. Under this method, the Group's share of post-acquisition profits or losses is recognised in the Consolidated Income Statement, the cost of the investment in a given joint venture, together with the Group's share of that entity's post-acquisition changes to shareholders' funds, is included in investments within the Consolidated Balance Sheet.

Business combinations

Business combinations are accounted for using the acquisition method. The acquisition method involves the recognition at fair value of all identifiable assets and liabilities, including contingent liabilities of the subsidiary at the acquisition date, regardless of whether or not they were recorded in the financial statements of the subsidiary prior to acquisition. On initial recognition, the assets and liabilities of the subsidiary are included in the Consolidated Balance Sheet at their fair values, which are also used as the bases for subsequent measurement in accordance with the Group accounting policies. Goodwill is stated after separating out identifiable intangible assets. Goodwill represents the excess of acquisition cost over the fair value of the Group's share of the identifiable net assets of the acquired subsidiary at the date of acquisition.

Where applicable, the consideration for an acquisition includes any assets or liabilities arising from a contingent consideration arrangement, measured at fair value at the acquisition date. Subsequent changes in such fair values are adjusted against the cost of acquisition where they result from additional information obtained up to one year from the acquisition date about facts and circumstances that existed at the acquisition date. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are recognised in accordance with IFRS 9 in the Consolidated Income Statement.

Costs relating to acquisitions in the year have been expensed.

Financial statements

Principal accounting policies – Group continued

Business combinations continued

For transactions with non-controlling parties that do not result in a change of control, the difference between the fair value of the consideration paid and the amount by which the non-controlling interest is adjusted is recognised in equity

Any business combinations prior to 1 January 2010 were accounted for in accordance with the standards in place at the time, which differ in the following respects: transaction costs directly attributable to the acquisition formed part of the acquisition costs, contingent consideration was recognised if, and only if, the Group had a present obligation, the economic outflow was more likely than not and a reliable estimate was determinable, and subsequent adjustments to the contingent consideration were recognised as part of goodwill

Property, plant and equipment

Items of property, plant and equipment are stated at historical cost, net of depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow into the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the Consolidated Income Statement during the financial period in which they are incurred.

Freehold land is not depreciated. Depreciation on other assets is calculated to write down the cost less estimated residual value over their estimated useful economic lives. The rates generally applicable are:

Freehold buildings	– 2% p a , straight line
Leasehold improvements	– over the period of the lease, straight line
Plant and machinery	– 25% p a , reducing balance
Fixtures, fittings and equipment	– 25% p a , reducing balance
Motor vehicles	– 25% p a , reducing balance

Residual values are reviewed annually and updated if appropriate. The carrying value is reviewed for impairment in the period if events or changes in circumstances indicate the carrying value may not be recoverable. An asset's carrying value is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within administrative expenses in the Consolidated Income Statement.

Intangible assets

In accordance with IFRS 3 (Revised) 'Business Combinations', an intangible asset acquired in a business combination is deemed to have a cost to the Group of its fair value at the acquisition date. The fair value of the intangible asset reflects market expectations about the probability that the future economic benefits embodied in the asset will flow to the Group. Where an intangible asset might be separable, but only together with a related tangible or intangible asset, the group of assets is recognised as a single asset separately from goodwill where the individual fair values of the assets in the Group are not reliably measurable. Where the individual fair values of the complementary assets are reliably measurable, the Group recognises them as a single asset provided the individual assets have similar useful lives. Intangible assets are amortised over the useful economic life of those assets.

Development costs incurred on software development are capitalised when all the following conditions are satisfied:

- ~ completion of the software module is technically feasible so that it will be available for use,
- ~ the Group intends to complete the development of the module and use it,
- ~ the software will be used in generating probable future economic benefits,
- ~ there are adequate technical, financial and other resources to complete the development and to use the software, and
- ~ the expenditure attributable to the software during its development can be measured reliably

Costs incurred making intellectual property available for use (including any associated borrowing costs) are capitalised when all of the following conditions are satisfied:

- ~ completion of the data set is technically feasible so that it will be available for use,
- ~ the Group intends to complete the preparation of the data and use it,
- ~ the data will be used in generating probable future economic benefits,
- ~ there are adequate technical, financial and other resources to complete the data set and to use it, and
- ~ the expenditure attributable to the intellectual property during its development can be measured reliably

Intangible assets continued

Development costs not meeting the criteria for capitalisation are expensed as incurred. Careful judgement by management is applied when deciding whether the recognition requirements for development costs have been met. This is necessary as the economic success of any development is uncertain and may be subject to future technical problems at the time of recognition. Judgements are based on the information available at each balance sheet date. In addition, all internal activities related to the research and development of new software are continually monitored by management.

The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Directly attributable costs include employee costs incurred on software development.

Amortisation commences upon completion of the asset and is shown within other administrative expenses. Until the asset is available for use on completion of the project, the assets are subject to impairment testing only. Development expenditure is amortised over the period expected to benefit.

The identifiable intangible assets and associated periods of amortisation are as follows:

Order book	– over the period of the order book, typically three years
Client relationships	– over the period expected to benefit, typically five years
Development expenditure	– over four to five years, straight line
Intellectual property	– over the period of usefulness of the intellectual property, typically five years

Goodwill

Goodwill arises on the acquisition of subsidiaries and represents any excess of the cost of the acquired entity over the Group's interest in the fair value of the entity's identifiable assets and liabilities acquired and is capitalised as a separate item. Goodwill is recognised as an intangible asset.

Under the business combinations exemption of IFRS 1, goodwill previously written off directly to reserves under UK GAAP is not recycled to the Consolidated Income Statement on calculating a gain or loss on disposal.

Impairment

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows – cash-generating units (CGUs). As a result, some assets are tested individually for impairment and some are tested at CGU level. Goodwill is allocated to those CGUs that are expected to benefit from synergies of the related business combination and represent the lowest level within the Group at which management monitors the related cash flows.

Goodwill or CGUs that include goodwill and those intangible assets not yet available for use are tested for impairment at least annually. All other individual assets or CGUs are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised in the Consolidated Income Statement for the amount by which the asset's or CGU's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of fair value, reflecting market conditions less costs to sell, and value in use based on an internal discounted cash flow evaluation. Impairment losses recognised for CGUs, to which goodwill has been allocated, are credited initially to the carrying amount of goodwill. Any remaining impairment loss is charged pro-rata to the other assets in the CGU. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognised may no longer exist.

Assets held for sale

Assets held for sale are recognised at the lower of their carrying amount and their fair value less costs to sell and separately presented on the face of the balance sheet. These assets are expected to be held for a limited duration prior to being sold.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is the actual purchase price of materials.

Work in progress

Work in progress is included in inventories after deducting any foreseeable losses and payments on account not matched with revenue. Work in progress represents costs incurred on speculative construction projects where a customer has not yet been identified. Work in progress is stated at the lower of cost and net realisable value. Cost comprises materials, direct labour and any subcontracted work that has been incurred in bringing the inventories and work in progress to their present location and condition.

Contract assets

Contract assets are included in trade and other receivables and represent revenue recognised in excess of the total of payments on account and amounts invoiced.

Financial statements

Principal accounting policies – Group continued

Trade receivables

Trade receivables represent amounts due from customers in respect of invoice. They are initially measured at their transaction price and subsequently remeasured at amortised cost.

Retention assets represent amounts held by customers for a period following payment of invoices, to cover any potential defects in the work. Retention assets are included in trade receivables and are therefore initially measured at their transaction price.

Accounting for taxes

Income tax comprises current and deferred taxation.

Current tax assets and/or liabilities comprise those obligations to, or claims from, fiscal authorities that are unpaid at the balance sheet date. They are calculated according to the tax rates and tax laws applicable to the accounting periods to which they relate, based on the taxable profit for the year.

Where an item of income or expense is recognised in the Consolidated Income Statement, any related tax generated is recognised as a component of tax expense in the Consolidated Income Statement. Where an item is recognised directly to equity or presented within the Consolidated Statement of Comprehensive Income, any related tax generated is treated similarly.

Deferred taxation is the tax expected to be repayable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and corresponding tax bases used in the computation of taxable profit and is accounted for using the balance sheet liability method.

Deferred taxation liabilities are generally recognised on all taxable temporary differences in full with no discounting. Deferred taxation assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. However, deferred tax is not provided on the initial recognition of goodwill, nor on the initial recognition of an asset or liability, unless the related transaction is a business combination or affects tax or accounting profit.

Deferred taxation is calculated using the tax rates and laws that are expected to apply in the period when the liability is settled or the asset is realised, provided they are enacted or substantively enacted at the balance sheet date. The carrying value of deferred taxation assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available against which taxable temporary differences can be utilised. Deferred tax is charged or credited to either the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income or equity to the extent that it relates to items charged or credited. Deferred tax relating to items charged or credited directly to equity is also credited or charged to equity.

Revenue

IFRS 15 'Revenue from Contracts with Customers' replaces the previous measurement standards IAS 18 'Revenue' and IAS 11 'Construction Contracts'. IFRS 15 has been applied using the modified retrospective approach on transition which results in an adjustment to the opening balance of equity at 1 January 2018 and no restatement of the prior period. The scope of the transitional adjustment is all contracts with customers which span the 1 January 2018 transition date. For the comparative period, the financial statements are reported under the aforementioned accounting standards, IAS 18 and IAS 11.

IFRS 15 provides a single, principles-based, five-step model to be applied to all sales contracts as outlined below. It is based on the transfer of control of goods and services to customers and replaces the separate models for goods, services and construction assets. The detail below sets out the principal types of contract and how the revenue is recognised in accordance with IFRS 15.

The Group's contract portfolio has been assessed by operating segment. The contracts with customers in Housing have a wide variation of goods and services being provided to customers with differing performance obligations and levels of complexity. Within Housing, IFRS 15 does not apply to lease contracts within the scope of IAS 17 'Leases'. In Care, there is a single performance obligation within all contracts and the segment follows a single revenue recognition methodology. None of the Group's contracts are considered to have a significant financing component.

Housing

Schedule of rates (SOR) contracts

These contracts are primarily for repairs and maintenance services. Revenue is derived using a fixed pricing schedule, which allows each job to be identified and valued. This pricing schedule is referred to as the SOR, which determines the transaction price. Each work order represents a performance obligation and as the customer controls the asset being enhanced through the works, the performance obligation is satisfied over time. The stage of completion of the work order is assessed and an appropriate proportion of the expected transaction price recognised in revenue.

Revenue continued**Housing continued****Lump sum contracts**

Lump sum contracts may involve delivering a range of goods and services, typically repairs, maintenance and capital works, however, there is a single fixed lump sum payment per period which represents the transaction price. The obligation within a lump sum contract is deemed to be being available to deliver the goods and services in the scope of the contract, not the actual performance of the individual works orders themselves. Therefore revenue will be recognised on a straight-line basis as performance obligations are being met over time.

Contracting

For contracting projects, the contract states the scope and specification of the construction works to be carried out, for a fixed price. Mears is continuously satisfying this single performance obligation as cost is incurred, determining progress against the performance obligation on an input basis. The customer controls the site or output as the work is being performed on it and therefore revenue is recognised over time where there is an enforceable right to payment for works completed to date and the work completed does not create an asset with an alternative use to the Group. An assessment is made of costs incurred to date and the costs required to complete the project. If a project is not deemed to be profitable, the unavoidable costs of fulfilling the contract are provided for immediately. This category also includes construction contracts where an end customer has not yet been identified and the revenue is recognised at a point in time, rather than over time.

Variable consideration

The Group's Housing revenue includes elements of variable consideration. Where there is uncertainty in the measurement of variable consideration, at both the start of the contract and subsequently, management will consider the facts and circumstances of the contract in determining either the most likely amount of variable consideration when the outcome is binary, or the expected value based on a range of possible considerations. Included within this assessment will be the extent to which there is a high probability that a significant reversal in variable consideration revenues will not occur once the uncertainty is subsequently resolved. This assessment will include consideration of the following factors: the total amount of the variable consideration, the proportion of consideration susceptible to judgements of customers or third parties, the length of time expected before resolution of the uncertainty, and the Group's previous experience of similar contracts.

Rental income

Where the Group is acting as principal, lessor operating lease revenue is recognised in revenue on a straight-line basis over the tenancy in accordance with IAS 17 'Leases', which will be replaced by IFRS 16 'Leases' from 1 January 2019.

Where the Group is providing a management service, Mears recognises revenue as an agent (the net management fee) on a straight-line basis. Where significant initial costs are required to make good the housing to perform Housing Management activities, the costs directly attributable to the initial upgrade will be recognised as costs incurred to fulfil a contract and held within current assets, to the extent that it is determined that costs are recoverable.

Care

The stand-alone selling prices for providing care are overtly stated in the contract, and the method of application of the rate of charge is on a unit of time basis, usually expressed as a rate per visit. Revenue will be recognised in respect of this single performance obligation, by reference to the chargeable rate and time for completed care visits in the period.

From time to time, care contracts with customers include a fixed fee per period for performing a consistent scope of care. For these contract types, the revenue recognition is consistent with lump sum contracts above.

There is a shift towards rewarding providers of care on the basis of achievement of specific outputs achieved and moving away from the traditional input-based, per-hour measurement. Care outputs are either achieved or not achieved and are determined by service user. Revenue will be recognised when the specific performance obligation has been satisfied.

Segment reporting

Segment information is presented in respect of the Group's operating segments based on the format that the Group reports to its chief operating decision maker.

The Group considers that the chief operating decision maker comprises the Executive Directors and Senior Executives of the business.

Exceptional costs

Exceptional costs are disclosed on the face of the Consolidated Income Statement where these are material and considered necessary to explain the underlying financial performance of the Group. They are either one-off in nature or necessary elements of expenditure to derive future benefits for the Group which have not been capitalised in the Consolidated Balance Sheet.

Costs of restructure are only considered to be exceptional where the restructure is transformational and the resultant cost is significant.

Acquisition costs are only considered to be exceptional where the acquisition and the resultant cost are significant.

Financial statements

Principal accounting policies – Group continued

Employee benefits

Retirement benefit obligations

The Group operates both defined benefit and defined contribution pension schemes as follows

i) Defined contribution pensions

A defined contribution plan is a pension plan under which the Group pays fixed contributions to an independent entity. The Group has no legal obligations to pay further contributions after payment of the fixed contribution.

The contributions recognised in respect of defined contribution plans are expensed as they fall due. Liabilities and assets may be recognised if underpayment or prepayment has occurred and are included in current liabilities or current assets as they are normally of a short-term nature.

The assets of the schemes are held separately from those of the Group in an independently administered fund.

ii) Defined benefit pensions

The Group contributes to defined benefit schemes which require contributions to be made to separately administered funds.

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligations for any benefits from this kind of pension plan remain with the Group, even if plan assets for funding the defined benefit plan have been set aside.

Scheme liabilities are measured using the projected unit funding method, applying the principal actuarial assumptions at the balance sheet date. Assets are measured at market value. In accordance with IFRIC 14, the asset that is recognised is restricted to the amount by which the IAS 19 (Revised) service cost is expected, over the lifetime of the scheme, to exceed funding contributions payable in respect of accruing benefits.

Where the Group has a contractual obligation to make good any deficit in its share of a Local Government Pension Scheme (LGPS) but also has the right to recover the costs of making good any deficit from the Group's client, the fair value of that guarantee asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. The right to recover costs is also limited to situations where the cap on employer contributions payable by the Group is not set so as to contribute to reducing the deficit in the scheme. Movements in the guarantee asset are taken to the Consolidated Income Statement and to the Consolidated Statement of Comprehensive Income to match the movement in pension assets and liabilities.

Actuarial gains and losses are taken to the Consolidated Statement of Comprehensive Income as incurred. For this purpose, actuarial gains and losses comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

Other movements in the net surplus or deficit are recognised in the Consolidated Income Statement, including the current service cost, any past service cost and the effect of curtailments or settlements. The net interest cost is also charged to the Consolidated Income Statement. The amount charged to the Consolidated Income Statement in respect of these plans is included within operating costs.

The Group's contributions to the scheme are paid in accordance with the rules of the scheme and the recommendations of the scheme actuary.

Share-based employee remuneration

All share-based payment arrangements that were granted after 7 November 2002 and had not vested before 1 January 2005 are recognised in the consolidated financial statements in accordance with IFRS 2.

The Group operates equity-settled and cash-settled share-based remuneration plans for its employees. All employee services received in exchange for the grant of any share-based remuneration are measured at their fair values. These are indirectly determined by reference to the fair value (excluding the effect of non-market-based vesting conditions) of the share options awarded. Their value is determined at the date of grant and is not subsequently remeasured unless the conditions on which the award was granted are modified. The fair value at the date of the grant is calculated using the Black Scholes option pricing model and the cost is recognised on a straight-line basis over the vesting period. Adjustments are made to reflect expected and actual forfeitures during the vesting period. For Save As You Earn (SAYE) plans, employees are required to contribute towards the plan. This non-vesting condition is taken into account in calculating the fair value of the option at the grant date.

All share-based remuneration is ultimately recognised as an expense in the Consolidated Income Statement. For equity-settled share-based payments there is a corresponding credit to the share-based payment reserve, for cash-settled share-based payments the Group recognises a liability at the balance sheet date.

Upon exercise of share options, the proceeds received net of any directly attributable transaction costs up to the nominal value of the shares issued are allocated to share capital, with any excess being recorded as share premium.

Leases

In accordance with IAS 17 'Leases', the economic ownership of a leased asset is transferred to the lessee if they bear substantially all the risks and rewards related to the ownership of the leased asset. The related asset is recognised at the time of inception of the lease at the fair value of the leased asset or, if lower, the present value of the lease payments plus incidental payments, if any, to be borne by the lessee. A corresponding amount is recognised as a finance leasing liability, irrespective of whether some of these lease payments are payable upfront at the date of inception of the lease.

Subsequent accounting for assets held under finance lease agreements, i.e. depreciation methods and useful lives, correspond to those applied to comparable acquired assets. The corresponding finance leasing liability is reduced by lease payments less finance charges, which are expensed to finance costs. Finance charges represent a constant periodic rate of interest on the outstanding balance of the finance lease liability.

All other leases are treated as operating leases. Payment on operating lease agreements is recognised as an expense on a straight-line basis over the lease term. Associated costs, such as maintenance and insurance, are expensed as incurred.

Financial instruments

Financial assets and liabilities are recognised in the Consolidated Balance Sheet when the Group becomes party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Group are as follows:

Financial assets, loans and receivables

From 1 January 2018, the assets generated from goods or services transferred to customers are now presented as either receivables or contract assets, in accordance with IFRS 15. The assessment of impairment of receivables or contract assets from 1 January 2018 is in accordance with IFRS 9 'Financial Instruments'.

All of Mears' cash flows from customers are solely payments of principal and interest, and do not contain a significant financing component. Financial assets generated from all of the Group's revenue streams are therefore initially measured at their fair value, which is considered to be their transaction price (as defined in IFRS 15) and are subsequently remeasured at amortised cost.

Under IFRS 9, Mears will now recognise a loss allowance for expected credit losses (ECL) on financial assets subsequently measured at amortised cost using the 'simplified approach'. Individually significant balances are reviewed separately for impairment based on the credit terms agreed with the customer. Other balances are grouped into credit risk categories and reviewed in aggregate.

Trade receivables, contract assets and cash at bank and in hand are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Trade receivables and contract assets are initially recorded at fair value net of transaction costs, being invoiced value less any provisional estimate for impairment should this be necessary due to a loss event. Trade receivables are subsequently remeasured at invoiced value, less an updated provision for impairment. Any change in their value through impairment or reversal of impairment is recognised in the Consolidated Income Statement.

Cash and cash equivalents include cash at bank and in hand and bank deposits available with no notice or less than three months' notice from inception that are subject to an insignificant risk of changes in value. Bank overdrafts are presented as current liabilities to the extent that there is no right of offset with cash balances. The Group considers its revolving credit facility to be an integral part of its cash management. During the year, the Comprehensive Statement of Cash Flows has been re-presented to show this separately from cash and cash equivalents. This has resulted in a net increase in revolving credit facility of £43.2m (2017 decrease: £14.7m) being added to cash movements on financing activities in the Comprehensive Statement of Cash Flows and a commensurate adjustment to cash movement for the year, resulting in a cash and cash equivalents figure of £279m (2017: £24.8m). A memo has been added to the Comprehensive Statement of Cash Flows to show cash and cash equivalents and the rolling credit facility in total.

Following initial recognition, financial assets are subsequently remeasured at amortised cost using the effective interest rate method.

Financial liabilities

The Group's financial liabilities are overdrafts, trade and other payables including contingent consideration, and interest rate swaps. They are included in the Consolidated Balance Sheet line items 'Short-term borrowings and overdrafts', 'Trade and other payables', 'Financial liabilities' and 'Other liabilities'.

All interest related charges are recognised as an expense in 'Finance costs' in the Consolidated Income Statement with the exception of those that are directly attributable to the construction of a qualifying asset, which are capitalised as part of that asset.

Bank and other borrowings are initially recognised at fair value net of transaction costs. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognised respectively in finance income and finance costs. Borrowing costs are recognised as an expense in the period in which they are incurred with the exception of those which are directly attributable to the construction of a qualifying asset, which are capitalised as part of that asset.

Trade payables on normal terms are not interest bearing and are stated at their fair value on initial recognition and subsequently at amortised cost.

Contingent consideration is initially recognised at fair value and is subsequently measured at fair value through the Consolidated Income Statement.

Financial statements

Principal accounting policies – Group continued

Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to interest rate risks arising from operational and financing activities

Derivative financial instruments are recognised initially and subsequently at fair value, with mark-to-market movements recognised in the Consolidated Income Statement except where cash flow hedge accounting is applied

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties

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

Hedge accounting for interest rate swaps

Where an interest rate swap is designated as a hedge of the variability in cash flows of an existing or highly probable forecast loan interest payment, the effective part of any valuation gain or loss on the swap instrument is recognised in 'Other comprehensive income' in the hedging reserve. The cumulative gain or loss is removed from equity and recognised in the Consolidated Income Statement at the same time as the hedged transaction. The ineffective part of any gain or loss is recognised in the Consolidated Income Statement immediately.

When a hedging instrument or hedge relationship is terminated but the hedged transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer probable, the cumulative unrealised gain or loss recognised in equity is recognised in the Consolidated Income Statement immediately.

Nature and purpose of each reserve in equity

Share capital is determined using the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Equity-settled share-based employee remuneration is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The hedging reserve represents the effective part of any gain or loss on a cash flow hedge which has not been removed from equity and recognised in the Consolidated Income Statement.

The merger reserve relates to the difference between the nominal value and total consideration in respect of the acquisition of Careforce Group plc, Supporta plc and Morrison Facilities Services Limited where the Company was entitled to the merger relief offered by the Companies Act 2006.

Dividends

Dividend distributions payable to equity shareholders are included in 'Current financial liabilities' when the dividends are approved in a general meeting prior to the balance sheet date.

Use of judgements and estimates

The preparation of financial statements requires management to make estimates and judgements that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenditure during the reported period. The estimates and associated judgements are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying judgements are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

In the preparation of these consolidated financial statements, estimates and judgements have been made by management concerning the selection of useful lives of property, plant and equipment, provisions necessary for certain liabilities, when to recognise revenue on long-term contracts, actuarial judgements, discount rates used within impairment reviews, the underlying share price volatility for valuing equity-based payments and other similar evaluations. Actual amounts could differ from those estimates.

Use of judgements and estimates *continued***Critical judgements in applying the Group's accounting policies****Revenue recognition**

Previously IAS 18 'Revenue' and IAS 11 'Construction Contracts' allowed contracts with a variety of services to be combined in certain circumstances in determining the percentage of completion of those multi-service contracts. Under this standard, revenue was recorded to reflect the expected profit margin on the contract based on the overall stage of completion. Disaggregating these contracts to determine the satisfaction of performance obligations, as detailed above, significantly changes the timing of revenue recognition, as in many contracts, stage of completion is now assessed at the individual job level. £19.1m of the reduction in the opening balance of equity at 1 January 2018 relates to the disaggregation of contracts previously combined. The total transaction price of these contracts does not change under IFRS 15.

The Group's assessment of variable consideration revenue recognition under IFRS 15 is detailed above. The judgement applied under IFRS 15 more closely aligns timing of revenue recognition with cash inflows where the contractual mechanism contains uncertainty. Previously, the Group utilised expected value calculations in determining the variable consideration revenue to be recognised. £4.8m of the reduction in the opening balance of equity at 1 January 2018 relates to the Group's application of IFRS 15 in relation to variable consideration. The total amount of variable consideration will not change under IFRS 15.

Joint arrangements

The Group participates in a number of joint arrangements where control of the arrangement is shared with another party. A joint arrangement is classified as a joint operation or as a joint venture, depending on management's assessment of the legal form and substance of the arrangement.

The classification can have a material impact on the consolidated financial statements. The Group's share of assets, liabilities, revenue, expenses and cash flows of joint operations would be included in the consolidated financial statements on a line-by-line basis, whereas the Group's investment and share of results of joint ventures are shown within single line items in the Consolidated Balance Sheet and Consolidated Income Statement respectively.

Key sources of estimation uncertainty**Contract recoverability**

Determining future contract profitability requires estimates of future revenues and costs to complete. In making these assessments there is a degree of inherent uncertainty. The Group utilises the appropriate expertise in determining these estimates and has well-established internal controls to assess and review the expected outcome.

Impairment of goodwill

Determining whether goodwill is impaired requires an estimate of the value in use of the CGUs to which goodwill has been allocated. The value-in-use calculation involves an estimate of the future cash flows of the CGUs and also the selection of appropriate discount rates to calculate present values. Future cash flows are estimated using the current one-year budget forecast, extrapolated for a future growth rate. The estimated growth rates are based on past experience and knowledge of the individual sector's markets. Changes in the estimated growth rate could result in variations to the carrying value of goodwill. The estimated cash flows and future growth rates are based on past experience and knowledge of the sector. The value in use is most sensitive to changes in the terminal growth rate, the explicit growth rate and the discount rate. The sensitivity to changes in these estimations is detailed in note 13.

Defined benefit assets

Scheme assets for LGPS have been estimated by rolling forward the published asset position from the previous year using market index returns over the period. This is considered to provide a good estimate of the actual scheme assets and the values will be updated to actuals each time a triennial valuation takes place.

Defined benefit liabilities

A number of key estimates have been made, which are given below, and which are largely dependent on factors outside the control of the Group.

- ~ inflation rates,
- ~ mortality,
- ~ discount rate, and
- ~ salary and pension increases

Details of the particular estimates used are included in the pensions note. Sensitivity analysis for these key estimates is included in note 29.

Where the Group has a contractual obligation to make good any deficit in its share of an LGPS but also has the right to recover the costs of making good any deficit from the Group's client, the fair value of that asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. The Directors have made judgements in respect of whether any of the deficit is as a result of such situations.

The right to recover costs is also limited to situations where the cap on employer contributions to be suffered by the Group is not set so as to contribute to reducing the deficit in the scheme. The Directors, in conjunction with the scheme actuaries, have made judgements in respect of the predicted future service cost and contributions to the scheme to reflect this in the fair value of the asset recognised.

Financial statements

Principal accounting policies – Group continued

New standards and interpretations not yet applied

IFRS 16 'Leases'

IFRS 16 replaces the existing leasing accounting guidance, which includes IAS 17 'Leases' and IFRIC 4 'Determining Whether an Arrangement Contains a Lease'. The standard is effective for periods beginning on or after 1 January 2019.

The standard requires lessees to account for most contracts using an on-balance sheet model, with the distinction between operating and finance leases being removed. There is no change to the revenue recognition methodology for lessor operating leases.

The standard provides certain exemptions from recognising leases on the balance sheet, including where the asset is of low value or the lease term is 12 months or less. In addition, the standard makes changes to the definition of a lease to focus on, amongst other things, which party has the right to direct the use of the asset.

Under the new standard, the Group will be required to recognise right of use lease assets and lease liabilities on the balance sheet. The right of use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. Liabilities are measured based on the present value of future lease payments over the lease term. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, amongst others.

The recognition of the depreciation of right of use lease assets and interest on lease liabilities over the lease term will have no overall impact on profit before tax over the life of the lease, however, the result in any individual year will be impacted and the change in presentation of costs will likely be material to the Group's key financial metrics. Under IAS 17, the charge is booked in full to operating profit. Metrics which will therefore be affected will include operating profit and operating margin, interest and interest cover, Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) and operating cash flow.

Furthermore, the principal amount of cash paid and interest in the cash flow statement will be presented separately as a financing activity. Operating lease payments under IAS 17 would have been presented as operating cash flows. There will be no overall net cash flow impact.

The Group will use the modified retrospective transition method on adoption. Under this method, the asset is calculated as if IFRS 16 had always been applied, however, the liability is calculated as if all leases start on 1 January 2019, which will result in no change to comparative numbers but an adjustment within the reserves of the Group.

The impact of IFRS 16 to the Group, at the point of transition is detailed on page 51 in the Financial Review.

Information on the undiscounted amount of the Group's operating lease commitments under IAS 17 'Leases', the current leasing standard, is disclosed in the Group's annual financial statements. The leases substantially relate to property leases used to perform Housing activities as an operating lease lessor, and vehicle leases used in performing Housing activities.

Other new standards and amendments

A number of other standards have been modified. These include IFRIC 23 'Uncertainty over Income Tax Treatments', Plan Amendment, Curtailment or Settlement (Amendments to IAS 19) and Annual Improvements to IFRS standards 2015–2017 (various standards). None of these amendments are expected to have a material effect on the Group's financial statements.

Financial statements
Consolidated income statement
For the year ended 31 December 2018

	Note	2018 £'000	2017 £'000
Continuing operations			
Sales revenue	1	869,843	900,184
Cost of sales		(662,825)	(676,482)
Gross profit		207,018	223,702
Other administrative expenses		(166,177)	(184,551)
Exceptional costs	8	(5,657)	–
Amortisation of acquisition intangibles	14	(4,434)	(10,638)
Total administrative costs		(176,268)	(195,189)
Operating profit before exceptional costs and amortisation of acquisition intangibles	2	40,841	39,151
Operating profit	2	30,750	28,513
Finance income	5	1,154	751
Finance costs	5	(3,473)	(2,780)
Profit for the year before tax, exceptional costs and amortisation of acquisition intangibles		38,522	37,122
Profit for the year before tax		28,431	26,484
Tax expense	9	(3,606)	(4,315)
Profit for the year from continuing operations		24,825	22,169
Discontinued operations			
Exceptional loss from discontinued operations	10	–	(16,500)
Tax income from discontinued operations	9	–	3,176
Loss for the year after tax from discontinued operations		–	(13,324)
Profit for the year from continuing and discontinued operations		24,825	8,845
Attributable to:			
Owners of the Parent		24,064	7,582
Non-controlling interest		761	1,263
Profit for the year		24,825	8,845
Earnings per share – from continuing operations			
Basic	12	23.05p	20.28p
Diluted	12	22.91p	20.10p
Earnings per share – from continuing and discontinued operations			
Basic	12	23.05p	7.35p
Diluted	12	22.91p	7.29p

The accompanying accounting policies and notes form an integral part of these financial statements

Financial statements
Consolidated statement of comprehensive income
For the year ended 31 December 2018

	Note	2018 £'000	2017 £'000
Profit for the year		24,825	8,845
Other comprehensive income/(expense)			
Which will be subsequently reclassified to the Consolidated Income Statement			
Cash flow hedges			
~ losses arising in the year	24	–	(54)
~ reclassification to the Consolidated Income Statement	24	325	645
Decrease in deferred tax asset in respect of cash flow hedges	25	(45)	(143)
Which will not be subsequently reclassified to the Consolidated Income Statement			
Actuarial (loss)/gain on defined benefit pension scheme	29	(9,431)	13,879
Increase/(decrease) in deferred tax asset in respect of defined benefit pension schemes	25	1,792	(2,637)
Other comprehensive (expense)/income for the year		(7,359)	11,690
Total comprehensive income for the year		17,466	20,535
Attributable to:			
Owners of the Parent		16,705	19,272
Non-controlling interest		761	1,263
Total comprehensive income for the year		17,466	20,535

The accompanying accounting policies and notes form an integral part of these financial statements

Financial statements
Consolidated balance sheet
As at 31 December 2018

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	Note	2018 £'000	2017 £'000
Assets			
Non-current			
Goodwill	13	197,073	193,642
Intangible assets	14	31,570	17,266
Property, plant and equipment	15	24,956	22,037
Pension and other employee benefits	29	17,368	27,308
Deferred tax asset	25	5,500	4,314
		276,467	264,567
Current			
Assets classified as held for sale	17	12,442	13,941
Inventories	18	29,751	18,705
Trade and other receivables	20	178,194	153,912
Current tax assets		609	111
Cash at bank and in hand	24	27,876	24,770
		248,872	211,439
Total assets		525,339	476,006
Equity			
Equity attributable to the shareholders of Mears Group PLC			
Called up share capital	26	1,105	1,036
Share premium account		82,224	60,204
Share-based payment reserve		2,021	1,469
Hedging reserve	24	(46)	(326)
Merger reserve		46,214	46,214
Retained earnings		79,189	100,897
Total equity attributable to the shareholders of Mears Group PLC		210,707	209,494
Non-controlling interest		(427)	96
Total equity		210,280	209,590
Liabilities			
Non-current			
Long-term borrowing and overdrafts	24	78,780	50,559
Pension and other employee benefits	29	3,802	4,966
Deferred tax liabilities	25	7,710	7,098
Financial liabilities	22	15	79
Other payables	23	7,478	5,036
		97,785	67,738
Current			
Borrowings related to assets classified as held for sale	24	15,000	13,941
Short-term borrowing and overdrafts		15,000	–
Trade and other payables	21	187,233	184,484
Financial liabilities	22	41	253
Current liabilities		217,274	198,678
Total liabilities		315,059	266,416
Total equity and liabilities		525,339	476,006

The financial statements were approved and authorised for issue by the Board of Directors and were signed on its behalf on 22 March 2019

D J Miles A C M Smith
Director Director

Company number: 03232863

The accompanying accounting policies and notes form an integral part of these financial statements

Financial statements
Consolidated cash flow statement
For the year ended 31 December 2018

	Note	2018 £'000	2017 £'000
Operating activities			
Result for the year before tax		28,431	26,484
Adjustments	27	15,641	21,148
Change in inventories		(11,045)	(7,471)
Change in trade and other receivables		(13,948)	(109)
Change in trade and other payables		(17,490)	(11,381)
Cash inflow from operating activities of continuing operations before taxation		1,589	28,671
Taxes paid		665	(3,776)
Net cash inflow from operating activities of continuing operations		2,254	24,895
Net cash outflow from operating activities of discontinued operations		(1,610)	(9,354)
Net cash inflow from operating activities		644	15,541
Investing activities			
Additions to property, plant and equipment		(7,667)	(5,572)
Additions to other intangible assets		(3,089)	(3,661)
Proceeds from disposals of property, plant and equipment		144	204
Net cash inflow/(outflow) in respect of property for resale		1,499	(13,941)
Acquisition of subsidiary undertakings		(27,500)	(5,000)
Net cash acquired with subsidiary undertakings		(4,185)	–
Sale of subsidiary undertaking		–	1,582
Net cash disposed of with subsidiary		(26)	(1,234)
Loans made to other entities (non-controlled)		(139)	(232)
Interest received		389	351
Net cash outflow from investing activities		(40,574)	(27,503)
Financing activities			
Proceeds from share issue		22,089	1,894
Receipts from borrowings related to assets classified as held for sale		1,059	13,941
Acquisition of non-controlling interests		(6,163)	–
Net movement in revolving credit facility		43,221	(14,719)
Discharge of finance lease liability		(479)	(1,954)
Interest paid		(3,602)	(2,591)
Dividends paid – Mears Group shareholders		(12,539)	(12,218)
Dividends paid – non-controlling interests		(550)	(525)
Net cash inflow/(outflow) from financing activities		43,036	(16,172)
Cash and cash equivalents, beginning of year		24,770	52,904
Net increase/(decrease) in cash and cash equivalents		3,106	(28,134)
Cash and cash equivalents, end of year		27,876	24,770
The Group considers its revolving credit facility to be an integral part of its cash management			
~ cash at bank and in hand		27,876	24,770
~ revolving credit facility		(93,780)	(50,559)
Cash and cash equivalents, including revolving credit facility		(65,904)	(25,789)

The accompanying accounting policies and notes form an integral part of these financial statements

Consolidated statement of changes in equity

For the year ended 31 December 2018

	Attributable to equity shareholders of the Company							Total equity £'000
	Share capital £'000	Share premium account £'000	Share-based payment reserve £'000	Hedging reserve £'000	Merger reserve £'000	Retained earnings £'000	Non-controlling interest £'000	
At 1 January 2017	1,026	58,320	1,975	(774)	46,214	92,555	(642)	198,674
Net result for the year	–	–	–	–	–	7,582	1,263	8,845
Other comprehensive income	–	–	–	448	–	11,242	–	11,690
Total comprehensive income for the year	–	–	–	448	–	18,824	1,263	20,535
Deferred tax on share-based payments	–	–	–	–	–	404	–	404
Issue of shares	10	1,884	–	–	–	–	–	1,894
Share option charges	–	–	826	–	–	–	–	826
Share option exercises	–	–	(1,332)	–	–	1,332	–	–
Dividends	–	–	–	–	–	(12,218)	(525)	(12,743)
At 1 January 2018	1,036	60,204	1,469	(326)	46,214	100,897	96	209,590
Impact of change in accounting policies	–	–	–	–	–	(26,342)	–	(26,342)
Adjusted balance at 1 January 2018	1,036	60,204	1,469	(326)	46,214	74,555	96	183,248
Net result for the year	–	–	–	–	–	24,064	761	24,825
Other comprehensive income	–	–	–	280	–	(7,639)	–	(7,359)
Total comprehensive income for the year	–	–	–	280	–	16,425	761	17,466
Deferred tax on share-based payments	–	–	–	–	–	14	–	14
Issue of shares	69	22,020	–	–	–	–	–	22,089
Share option charges	–	–	552	–	–	–	–	552
Changes in non controlling interests	–	–	–	–	–	734	(734)	–
Dividends	–	–	–	–	–	(12,539)	(550)	(13,089)
At 31 December 2018	1,105	82,224	2,021	(46)	46,214	79,189	(427)	210,280

The accompanying accounting policies and notes form an integral part of these financial statements

Financial statements
Notes to the financial statements – Group
For the year ended 31 December 2018

1. Revenue

The Group's revenue disaggregated by pattern of revenue recognition is as follows

	2018 £'000	2017 £'000
Schedule of rates contracts	235,738	213,292
Contracting and variable consideration	236,625	251,920
Lump sum contracts	173,272	183,314
Rental income	107,595	117,595
Care services	116,613	134,063
	869,843	900,184

All of the above categories fall exclusively within the Housing segment with the exception of Care services, which falls exclusively within the Care segment

A total of £0.3m of revenue was recognised in respect of the balance of contract liabilities at 1 January 2018 (2017: £nil)

Schedule of rates and care service revenue is typically invoiced between one and 30 days from completion of the performance obligation. Contracting and variable consideration revenue is typically invoiced based on the stage of completion of the overall contract. Lump sum revenue is typically invoiced monthly in arrears. Rental income is typically invoiced monthly in advance. Payment terms for revenue invoiced are typically 30 to 60 days from the date of invoice.

2. Segment reporting

Segment information is presented in respect of the Group's operating segments. Segments are determined by reference to the internal reports reviewed by the Board.

The Group had two operating segments during the year:

- ~ Housing – services within this sector comprise a full housing management service predominantly to Local Authorities and other Registered Social Landlords, and
- ~ Care – services within this sector comprise personal care services to people in their own homes

All of the Group's activities are carried out within the United Kingdom and the Group's principal reporting to its chief operating decision maker is not segmented by geography.

The principal financial measures used by the chief operating decision maker and the Board to review the performance of the operating segments are those of revenue growth and operating margins in both the core divisions of Housing and Care. The operating result utilised within the key performance measures is stated before amortisation of acquisition intangibles and costs relating to the long-term incentive plans.

	2018			2017		
	Housing £'000	Care £'000	Total £'000	Housing £'000	Care £'000	Total £'000
Operating segments						
Revenue	753,230	116,613	869,843	766,121	134,063	900,184
Operating result before exceptional costs, amortisation of acquisition intangibles and long-term incentive plans	37,627	3,766	41,393	39,478	499	39,977
Operating margin before exceptional costs amortisation of acquisition intangibles and long-term incentive plans	5.00%	3.23%	4.76%	5.15%	0.37%	4.44%
Long-term incentive plans	(552)	–	(552)	(826)	–	(826)
Operating result before exceptional costs and amortisation of acquisition intangibles	37,075	3,766	40,841	38,652	499	39,151
Exceptional costs			(5,657)			–
Amortisation of acquisition intangibles			(4,434)			(10,638)
Operating profit			30,750			28,513
Net finance costs			(2,319)			(2,029)
Tax expense			(3,606)			(4,315)
Profit for the year from continuing activities			24,825			22,169

All revenue and all non-current assets arise within the United Kingdom. All of the revenue reported is external to the Group. No revenue in respect of a single customer comprises more than 8% of the total revenue reported.

2. Segment reporting *continued*

In addition, the following disclosures have been provided in respect of segmental analysis required by IFRS 8 'Operating Segments'

	2018			2017		
	Housing £'000	Care £'000	Total £'000	Housing £'000	Care £'000	Total £'000
Operating segments						
Segment assets	402,148	123,191	525,339	350,902	125,104	476,006
Segment liabilities	(277,620)	(37,439)	(315,059)	(203,334)	(63,082)	(266,416)
Property, plant and equipment additions	8,059	642	8,701	7,517	604	8,121
Depreciation	5,146	658	5,804	5,304	801	6,105
Amortisation of acquisition intangibles	3,738	696	4,434	7,606	3,032	10,638
Amortisation of other intangibles	2,409	–	2,409	2,130	–	2,130

3. Changes in accounting policies

As detailed in the principal accounting policies, there have been two significant mandatory accounting changes which apply from 1 January 2018 the adoption of IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments'. The impact to retained earnings as a result of these changes is detailed below

	Retained earnings £'000
Retained earnings as previously stated at 31 December 2017	100,897
Impact of restatement on Trade and other receivables (IFRS 15)	(29,537)
Impact of restatement on Deferred tax asset (IFRS 15)	5,611
Impact of restatement on Trade and other receivables (IFRS 9)	(2,818)
Impact of restatement on Deferred tax asset (IFRS 9)	402
Retained earnings as restated at 1 January 2018	74,555

The impact to the debtor provision is detailed below

	Debtor provision £'000
Debtor provision under IAS 39 as previously stated at 31 December 2017	6,710
Reversal of debtor provision under IAS 39	(6,710)
Recognition of debtor provision under IFRS 9	9,528
Debtor provision under IFRS 9 as restated at 1 January 2018	9,528

The effect of the application of IFRS 15 and IFRS 9 on the year ended 31 December 2018 is detailed below

	As would have been reported under old accounting standards £'000	Impact of IFRS 15 £'000	Impact of IFRS 9 £'000	As reported under new accounting standards £'000
Consolidated income statement for the year ended 31 December 2018				
Sales revenue	868,965	878	–	869,843
Other administrative expenses	(116,395)	–	218	(166,177)
Tax expense	(3,398)	(167)	(41)	(3,606)
Consolidated balance sheet as at 31 December 2018				
Deferred tax asset	5,475	–	25	5,500
Trade and other receivables	209,454	(28,659)	(2,601)	178,194
Retained earnings	110,424	(28,659)	(2,576)	79,189
Consolidated statement of cash flows as at 31 December 2018				
Results for the year before tax	27,335	878	218	28,431
Change in trade and other receivables	(9,322)	(878)	(218)	(10,418)

The change to IFRS 15 has no impact on the lifetime profitability of the contracts and there are no cash flow impacts. The impact of this standard has been to increase the operating result for 2018 by £0.9m. Moving forward, it is expected to have a positive impact in respect of operating profit as performance obligations are met.

The impact of IFRS 9 has been to increase the operating result for 2018 by £0.2m. Moving forward, this new standard is likely to result in an earlier recognition of credit loss, resulting in an impairment in trade receivables and contract assets. Based on the current activities of the Group, it is unlikely that this impairment would be material in any single year.

Financial statements

Notes to the financial statements – Group continued For the year ended 31 December 2018

4. Operating costs

Operating costs, relating to continuing activities, include the following

	2018 £'000	2017 £'000
Share-based payments	552	826
Depreciation	5,804	6,105
Amortisation of acquisition intangibles	4,434	10,638
Amortisation of other intangibles	2,409	2,130
Loss/(profit) on disposal of subsidiary	44	(961)
Loss on disposal of property, plant and equipment	37	24
Hire of plant and machinery	4,948	5,266
Other operating lease rentals	105,822	110,658

Fees payable for audit and non-audit services during the year were as follows

	2018 £'000	2017 £'000
Fees payable to the auditor for the audit of the Group's financial statements	55	65
Other fees payable to the auditor in respect of		
~ auditing of accounts of subsidiary undertakings pursuant to legislation	325	265
~ other audit related fees	9	9
Total auditor's remuneration	389	339

5. Finance income and finance costs

	2018 £'000	2017 £'000
Interest charge on overdrafts and short-term loans	(3,039)	(2,017)
Interest charge on hedged items (effective hedges)	(325)	(645)
Other interest	(2)	(4)
Finance costs on bank loans, overdrafts and finance leases	(3,366)	(2,666)
Interest charge on defined benefit obligation	(77)	(114)
Unwinding of discounting	(30)	–
Total finance costs	(3,473)	(2,780)
Interest income resulting from short-term bank deposits	35	20
Interest income resulting from defined benefit asset	773	440
Unwinding of discounting	–	40
Other interest income	346	251
Finance income	1,154	751
Net finance charge	(2,319)	(2,029)
Gains and losses on hedged items recognised in other comprehensive income		
Losses arising in the year	–	(54)
Reclassification to the Consolidated Income Statement	325	645
Changes in mark-to-market of interest rate swaps (effective hedges)	325	591

6. Employees

Staff costs during the year were as follows

	2018 £'000	2017 £'000
Wages and salaries	233,877	272,794
Social security costs	20,975	23,806
Other pension costs	9,532	8,627
	264,384	305,227

The average number of employees of the Group during the year was

	2018 £'000	2017 £'000
Site workers	3,382	3,638
Carers	4,558	5,980
Office and management	2,642	2,962
	10,582	12,580

Remuneration in respect of Directors was as follows

	2018 £'000	2017 £'000
Emoluments	1,507	1,389
Gains made on the exercise of share options	–	1,148
Pension contributions to personal pension schemes	121	161
	1,628	2,698

During the year contributions were paid to personal pension schemes for three Directors (2017: four)

During the year no Directors (2017: four) exercised share options

7. Share-based employee remuneration

As at 31 December 2018 the Group maintained six share-based payment schemes for employee remuneration

Details of the share options outstanding are as follows

	2018		2017	
	Number '000	Weighted average exercise price p	Number '000	Weighted average exercise price p
Outstanding at 1 January	2,938	287	2,555	256
Granted	530	237	1,619	317
Forfeited/lapsed	(583)	323	(229)	326
Exercised	(133)	297	(1,007)	193
Outstanding at 31 December	2,752	265	2,938	287

The weighted average share price at the date of exercise for share options exercised during the period was 3.47p. At 31 December 2018, 0.3m options had vested and were still exercisable at prices between 1p and 266p. These options had a weighted average exercise price of 230p and a weighted average remaining contractual life of 1.4 years.

The fair values of options granted were determined using the Black Scholes option pricing model. Significant inputs into the calculation include the market price at the date of grant and exercise prices. Furthermore, the calculation takes into account the future dividend yield, the share price volatility rate and the risk-free interest rate.

The underlying expected share price volatility was determined by reference to historical data. The Company expects the volatility of its share price to reduce as it matures. The risk-free interest rate was determined by the implied yield available on a zero-coupon Government bond at the date of grant. Adjustments are made to reflect expected and actual forfeitures during the vesting period due to failure to satisfy service conditions. In the case of the SAYE scheme, the expected forfeitures take account of the requirement to save throughout the life of the scheme. There were 0.5m options granted during the year and 0.6m options that lapsed during the year. The market price at 31 December 2018 was 335p and the range during 2018 was 274p to 440p.

Financial statements

Notes to the financial statements – Group continued For the year ended 31 December 2018

7. Share-based employee remuneration continued

All share-based employee remuneration will be settled in equity. The Group has no legal obligation to repurchase or settle the options.

The Group recognised the following expenses related to share-based payments:

	2018 £'000	2017 £'000
Giving rise to share-based payment reserve		
~ SAYE	307	295
~ Share Plan	245	71
~ MIP	–	460
Giving rise to liabilities		
~ MIP	–	–
	552	826

All-employee share incentive plan

Options are exercisable at a price equal to the average quoted market price of the Company's shares on the three dealing days prior to the date of grant. The vesting period is three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Options are forfeited if the employee leaves Mears before the options vest. All options issued under this plan have vested or were forfeited.

Unapproved Company Share Option Plan (CSOP)

Options are exercisable at nominal value. The vesting period is three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Options are forfeited if the employee leaves Mears before the options vest. With the introduction of the LTIP in 2008, the Remuneration Committee has decided that no further awards will be made under the unapproved CSOP. All options issued under this plan have vested or were forfeited.

Save As You Earn (SAYE) scheme

Options are available to all employees. Options are granted for a period of three years. Options are exercisable at a price based on the quoted market price of the Company's shares at the time of invitation, discounted by up to 20%. Options are forfeited if the employee leaves Mears Group before the options vest, which impacts on the number of options expected to vest. If an employee stops saving but continues in employment, this is treated as a cancellation, which results in an acceleration of the share-based payment charge.

The Mears Group PLC Long-term Incentive Plan (LTIP)

The LTIP was introduced in October 2008 following shareholder approval. The award of options is offered to a small number of key senior management, subject to achieving performance conditions. No options have been issued under this plan since 2010 and all options have vested.

Management Incentive Plan (MIP)

The MIP was introduced in 2013 following shareholder approval. The award of options is offered to a small number of key senior management. The MIP is a share-based payment plan which is settled through a combination of cash and shares. No further issues will be made under this plan and the remaining options vest in 2019.

Executive Incentive Plan (EIP)

The EIP was introduced in June 2017 following shareholder approval. The award of options is offered to key senior management subject to performance conditions as detailed on page 87 of the Remuneration Report.

8. Exceptional costs

Exceptional costs incurred in the period which are considered non-trading or non-recurring in nature are detailed below:

	2018 £'000	2017 £'000
Costs of restructure	3,584	–
Costs of acquisition	524	–
Exceptional legal costs	1,549	–
	5,657	–

The costs of restructure relate to the rationalisation of the Group's central services and largely comprise non-recurring staff costs.

The costs of acquisition relate to the acquisition of MPM Housing Limited and MPS Housing Limited, as detailed in note 28.

Exceptional legal costs were incurred in respect of a property lease. Given the size of this item and unique circumstance of the dispute, the Directors believe this should be treated as an exceptional item to better reflect the underlying financial performance.

9. Tax expense

Tax recognised in the Consolidated Income Statement

	2018 £'000	2017 £'000
United Kingdom corporation tax	(893)	5,341
Adjustment in respect of previous periods	(270)	(18)
Total current tax recognised in Consolidated Income Statement	(1,163)	5,323
Deferred taxation charge		
~ on defined benefit pension obligations	124	(6)
~ on share-based payments	(116)	240
~ on accelerated capital allowances	88	(153)
~ on amortisation of acquisition intangibles	(843)	(1,888)
~ on short-term temporary timing differences	(224)	247
~ on corporate tax losses	(60)	1,122
~ impact of change in statutory tax rates	-	(168)
~ impact of transition to new accounting standards	5,990	-
Adjustment in respect of previous periods	(190)	(402)
Total deferred taxation recognised in Consolidated Income Statement	4,769	(1,008)
Total tax expense recognised in Consolidated Income Statement on continuing operations	3,606	4,315
Total tax credit recognised in Consolidated Income Statement on discontinued operations	-	(3,176)
Total tax expense recognised in Consolidated Income Statement	3,606	1,139

The charge for the year can be reconciled to the result for the year as follows

	2018 £'000	2017 £'000
Result for the year before tax	28,431	9,984
Result for the year multiplied by standard rate of corporation tax in the United Kingdom for the period of 19.0% (2017: 19.3%)	5,402	1,922
Effect of		
~ expenses not deductible for tax purposes	260	167
~ income not subject to tax	(159)	(133)
~ tax relief on exercise of share options	(24)	(170)
~ statutory tax rate changes	-	(168)
~ temporary timing differences not previously recognised in deferred tax	203	(33)
~ tax losses not previously recognised in deferred tax	(1,616)	(26)
~ adjustment in respect of prior periods	(460)	(420)
Actual tax expense	3,606	1,139

Deferred tax is recognised on both temporary and permanent differences between the treatment of items for tax and accounting purposes. Deferred tax on the amortisation of acquisition intangibles is a permanent difference and arises because no tax relief is due on this kind of amortisation.

The transition to IFRS 15 and IFRS 9 at the start of the current period resulted in an opening deferred tax balance. The £6.0m deferred tax charge in respect of transition to new accounting standards is as a result of this opening deferred tax balance unwinding during 2018.

Tax losses generated in previous years which are expected to be utilised against future profits are recognised as a deferred tax asset and a subsequent charge arises as those losses are utilised. No deferred tax asset is recognised in respect of losses of £28.4m (2017: £34.2m) across several entities in the Group as it is not expected that they will be eligible to be utilised against profits in the future.

Deferred tax is also recognised on short-term temporary timing differences, primarily relating to provisions. These differences are expected to reverse in the following year and arise because tax relief is only available when the costs are incurred.

Capital allowances represent tax relief on the acquisition of property, plant and equipment and are spread over several years at rates set by legislation. These differ from depreciation, which is an estimate of the use of an item of property, plant and equipment over its useful life. Deferred tax is recognised on the difference between the remaining value of such an asset for tax purposes and its carrying value in the accounts.

Financial statements

Notes to the financial statements – Group continued For the year ended 31 December 2018

9. Tax expense continued

The following tax has been charged to other comprehensive income or equity during the year

	2018 £'000	2017 £'000
Deferred tax (credit)/charge recognised in other comprehensive income		
~ on defined benefit pension obligations	(1,792)	2,637
~ on cash flow hedges	45	143
Total deferred tax (credit)/charge recognised in other comprehensive income	(1,747)	2,780
Deferred tax recognised directly in equity		
Deferred tax credit		
~ on share-based payments	(14)	(404)
Total deferred tax recognised in equity	(14)	(404)
Total tax		
Total current tax	(1,163)	2,147
Total deferred tax	3,008	1,368

10. Discontinued activities

The Group previously completed the disposal of its Mechanical and Electrical division which included an entity operating in the United Arab Emirates ('Haydon LLC'). As part of that disposal, the Group ultimately retained the beneficial interest in 1% of the share capital of this UAE company due to the Group still carrying a number of performance guarantees in place at the time of the disposal, which unravel as the underlying contracts reach the end of their defects liability period.

During the year, the Group has incurred cash costs of £1.6m in respect of costs of litigation associated with the performance guarantees. The Group is carrying a remaining provision of £2.2m in respect of the two outstanding performance guarantees amounting to £3.9m, resulting in a residual contingent liability of £1.7m. Mears does not believe that there is any justification for the guarantee holders making a call on these guarantees, given that the contracts to which they are attached were concluded several years ago. The Directors believe the current position is sufficiently conservative, however if both bonds were to be called, and in the event that Mears recovered none of the debtor balance owed, this would result in a further loss to be recognised of £1.7m. This provision of £2.2m is reported within other creditors. The £1.7m is disclosed as a contingent liability.

11. Dividends

The following dividends were paid on ordinary shares in the year

	2018 £'000	2017 £'000
Final 2017 dividend of 8.55p (2017 final 2016 dividend of 8.40p) per share	8,860	8,651
Interim 2018 dividend of 3.55p (2017 interim 2017 dividend of 3.45p) per share	3,679	3,567
	12,539	12,218

The proposed final 2018 dividend of 8.85p per share has not been included within the consolidated financial statements as no obligation existed at 31 December 2018.

12. Earnings per share

	Basic (continuing)		Basic (discontinued)		Basic (continuing and discontinued)	
	2018 p	2017 p	2018 p	2017 p	2018 p	2017 p
Earnings per share	23.05	20.28	–	(12.93)	23.05	7.35
Effect of amortisation of acquisition intangibles	4.25	10.32	–	–	4.25	10.32
Effect of full tax adjustment	(2.22)	(2.31)	–	(0.19)	(2.22)	(2.50)
Effect of exceptional costs	4.16	–	–	13.12	4.16	13.12
Normalised earnings per share	29.24	28.29	–	–	29.24	28.29

	Diluted (continuing)		Diluted (discontinued)		Diluted (continuing and discontinued)	
	2018 p	2017 p	2018 p	2017 p	2018 p	2017 p
Earnings per share	22.91	20.10	–	(12.81)	22.91	7.29
Effect of amortisation of acquisition intangibles	4.22	10.23	–	–	4.22	10.23
Effect of full tax adjustment	(2.20)	(2.28)	–	(0.20)	(2.20)	(2.48)
Effect of exceptional costs	4.13	–	–	13.01	4.13	13.01
Normalised earnings per share	29.06	28.05	–	–	29.06	28.05

A normalised EPS is disclosed in order to show performance undistorted by the amortisation of acquisition intangibles and exceptional costs. The Group defines normalised earnings as excluding the amortisation of acquisition intangibles and exceptional costs and adjusted to reflect a full tax charge. The profit attributable to shareholders before and after adjustments for both basic and diluted EPS is:

	Normalised (continuing)		Normalised (discontinued)		Normalised (continuing and discontinued)	
	2018 £'000	2017 £'000	2018 £'000	2017 £'000	2018 £'000	2017 £'000
Profit/(loss) attributable to shareholders	24,064	20,906	–	(13,324)	24,064	7,582
~ amortisation of acquisition intangibles	4,434	10,638	–	–	4,434	10,638
~ full tax adjustment	(2,310)	(2,367)	–	(206)	(2,310)	(2,573)
~ exceptional costs	4,342	–	–	13,530	4,342	13,530
Normalised earnings	30,530	29,177	–	–	30,530	29,177

The calculation of EPS is based on a weighted average of ordinary shares in issue during the year. The diluted EPS is based on a weighted average of ordinary shares calculated in accordance with IAS 33 'Earnings per Share', which assumes that all dilutive options will be exercised. The additional normalised basic and diluted EPS use the same weighted average number of shares as the basic and diluted EPS.

	2018 Million	2017 Million
Weighted average number of shares in issue	104.40	103.10
~ dilutive effect of share options	0.65	0.93
Weighted average number of shares for calculating diluted earnings per share	105.05	104.03

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Notes to the financial statements – Group continued For the year ended 31 December 2018

13. Goodwill

	Goodwill arising on consolidation £'000	Purchased goodwill £'000	Total £'000
Gross carrying amount			
At 1 January 2017	193,306	406	193,712
Disposal of subsidiary	(70)	-	(70)
At 1 January 2018	193,236	406	193,642
Additions on acquisition	2,916	515	3,431
At 31 December 2018	196,152	921	197,073
Accumulated impairment losses			
At 1 January 2017, at 1 January 2018 and at 31 December 2018	-	-	-
Carrying amount			
At 31 December 2018	196,152	921	197,073
At 31 December 2017	193,236	406	193,642

Goodwill on consolidation arises on the excess of cost of acquisition over the fair value of the net assets acquired on purchase of a company

Purchased goodwill arises on the excess of cost of acquisition over the fair value of the net assets acquired on the purchase of the trade and assets of a business by the Group

Details of additions on acquisitions in the year are set out in note 28

Goodwill is not amortised but is reviewed for impairment on an annual basis or more frequently if there are any indications that goodwill may be impaired. Goodwill acquired in a business combination is allocated to groups of cash-generating units (CGUs) according to the level at which management monitors that goodwill. Goodwill is carried at cost less accumulated impairment losses.

The carrying value of goodwill is allocated to the following CGUs

	Goodwill arising on consolidation £'000	Purchased goodwill £'000	Total £'000
Housing	96,501	921	97,422
Care	99,651	-	99,651
	196,152	921	197,073

An asset is impaired if its carrying value exceeds the unit's recoverable amount, which is based on value in use. At 31 December 2018 impairment reviews were performed by comparing the carrying value with the value in use for the CGUs to which goodwill has been allocated.

The Housing CGU's value in use is calculated from the Board-approved one-year budgeted cash flows and extrapolated cash flows for the next four years discounted at a post-tax discount rate of 8.5% over a five-year period with a terminal value. The impairment reviews incorporated a terminal growth assumption of 1.7%, in line with the UK long-term growth rate.

The Care CGU's value in use is calculated from a detailed business plan deriving cash flows over a five-year review period, discounted at a post-tax discount rate of 8.5% over a five-year period with a terminal value. The impairment review incorporated a terminal growth assumption of 2.5%, which, whilst marginally higher than the UK long-term growth rate of 1.7%, is supported by the underlying demographics underpinning strong organic growth in adult social care.

The estimated growth rates are based on knowledge of the individual CGU's sector and market and represent management's base level expectations for future growth. Changes to revenue and direct costs are based on past experience and expectation of future changes within the markets of the CGUs. All CGUs have the same access to the Group's treasury function and borrowing arrangements to finance their operations.

The rates used were as follows:

	Post-tax discount rate	Pre-tax discount rate	Volume growth rate (years 1-5)	Terminal growth rate
Housing	8.50%	10.27%	3.00%	0.00%
Care	8.50%	10.27%	4.57%	2.50%

13. Goodwill continued

Housing

The contracts awarded within the Housing sector are significant in size and the contract terms typically average six years in duration. In addition, Mears has a good track record in retaining contracts on expiry and typically retains over 80% of expiring contracts.

Budgeted operating profits during the budget period are estimated by reference to the operating margin achieved in the period leading up to the start of the budget period, flexed for known changes in either the pricing mechanism or the cost base at a contract level. There is no inclusion of any anticipated efficiency improvements which have not been formally committed to before the year end.

The Directors consider that reasonably possible changes in these key assumptions would not cause a CGU's carrying amount to exceed its recoverable amount.

Care

Management recognises that there remain significant difficulties within the homecare market, although the sector is increasingly attracting the interests of the national media. The introduction of the National Living Wage in April 2016 proved a significant boost for providers, with a large number of Local Authorities materially increasing their charge rates, recognising that too much of the cost increase in recent years had been absorbed by care providers. This trend has continued with subsequent rises to the National Living Wage in 2017 and 2018. Providers have typically passed these rate increases on to their carers in full, adding some stability in a sector where recruitment and retention represent a significant constraint. Management is particularly pleased that all Local Authorities in Scotland, which covers around one third of the care activities, have adopted the Scottish Living Wage, which as at 1 April 2019 increases to £9.00 per hour. This compares with the statutory National Living Wage of £8.21 per hour.

Notwithstanding these improvements, market conditions remain challenging. The Directors note that, given these pressures, the number of national providers is reducing, which reflects the difficult conditions but does provide opportunity for the Group, where customers are seeking to work with a reputable national provider. The Group remains highly selective in bidding new contract opportunities but the pipeline for new contract bidding remains healthy. Management will only bid where the contract pricing provides good visibility of profitability, including a clear mechanism for future price increases and where there is a strategic opportunity to provide Housing services to the Local Authority client, either separately to a Care contract, or incorporated within a Care contract. Management has noted a lack of competition in opportunities which combine Housing and Care elements, where the customer is seeking a single contractor for the works. Whilst there are still examples of poor commissioning practices, the Directors are confident there are sufficient new bidding opportunities to deliver against the Group's growth forecast.

As part of the annual impairment testing, management performed an extensive business planning process which involved a detailed review, on a contract-by-contract basis, of charge rates and carer pay rates. The process allowed management to appraise the performance of branches against objectives set, and further increased understanding of the main drivers behind financial performance at a contract level. A key driver around the operational and financial success of each contract continues to be the recruitment and retention of care workers. Carer pay rates continue to be the principal barrier to successful recruitment and retention, but in addition there are a number of factors around culture, working practices and recognition which impact upon maintaining a stable workforce.

The business plan identified a number of key factors, which are built in to the value-in-use calculation.

- ~ Mears has continued to be highly selective, targeting those contracts where the pricing, longevity and spend certainty allow Mears to deliver a high quality service at sustainable margins. In 2018, a win rate of 60% was achieved from new contract bidding, which is in line with historical norms. Despite this, management has significantly reduced the Care growth forecast to equate to an increase of 2,000 hours per week, which will be achieved through annual new contract bidding. This emphasises management's desire to ensure new work won will enhance earnings.
- ~ Recruitment and retention of quality care workers continues to be challenging. The churn rate of care workers varies at a branch level, depending on non-financial factors such as culture, working practices and recognition. However, the overall churn rate has remained at a constant level between 40% and 50% for the last three years. Management has invested in retention activities to standardise best practices and will continue this focus during 2019. However, recruitment remains challenging and this is expected to continue during the short term. Mears recognises that traditional localised recruitment plays a vital role, aiding recruitment from the existing carer workforce pool. In an attempt to encourage new talent to the care at home market, Mears is utilising innovative recruitment tools to ensure breadth of coverage in attracting new care workers to the sector. This, in turn, will allow branches to focus on their localised recruitment efforts. Mears' internal recruitment plan anticipates modest growth during the medium and long term which, on average, equates to three additional carers per year per branch, this represents an increase of 250 carers per year on an existing workforce of 5,000 carers, which is considered realistic. However, conservatively, the business plan underpinning the impairment review has stripped out this expected increase and assumes no growth as a result of improved recruitment and retention practices.
- ~ Mears is committed to leading the way with carer pay rates, the increase in the National Living Wage will further increase direct costs from 1 April 2019. Management's desire is to maintain a significant differential between Mears' pay rates and the National Living Wage to ensure it remains the employer of choice in the homecare sector and can attract new employees to the sector. The process of branch closures which followed the introduction of the National Living Wage in April 2016 has resulted in a live contract portfolio that allows Mears to comfortably meet National Living Wage requirements, whilst having clear margin visibility. The Government has confirmed an increase in the National Living Wage of 4.9% from 1 April 2019. As a result, management has assumed an increase in carer pay rates of 4.9% per annum. Management is confident that charge rate increases will be received from clients to match the increase in the cost base. The percentage increase assumed for charge rates matches that of carer pay rates in each year throughout the business plan.

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Notes to the financial statements – Group continued For the year ended 31 December 2018

13. Goodwill continued

Care continued

Management considers that the Care value-in-use calculation is most sensitive to changes in the terminal growth rate, discount rate and EBITA margin. The table below shows the sensitivity of the headroom (£m) to simultaneous changes in the discount rate and the long-term growth rate.

Long-term growth rate	Discount rate					
	7.9%	8.1%	8.3%	8.5%	8.7%	8.9%
1.9%	18.9	14.4	10.2	6.3	2.6	(0.9)
2.1%	22.9	18.1	13.7	9.5	5.6	1.9
2.3%	25.8	20.8	16.2	11.8	7.7	3.9
2.5%	30.3	25.0	20.0	15.4	11.1	7.0
2.7%	35.2	29.5	24.2	19.2	14.6	10.3
2.9%	40.4	34.3	28.6	23.3	18.4	13.9
3.1%	46.1	39.5	33.4	27.8	22.5	17.7

14. Other intangible assets

	Acquisition intangibles			Other intangibles			
	Client relationships £'000	Order book £'000	Total acquisition intangibles £'000	Development expenditure £'000	Intellectual property £'000	Total other intangibles £'000	Total intangibles £'000
Gross carrying amount							
At 1 January 2017	72,138	28,317	100,455	13,237	224	13,461	113,916
Revisions	459	–	459	–	–	–	459
Additions	–	–	–	3,662	–	3,662	3,662
Disposals	–	(350)	(350)	–	–	–	(350)
At 1 January 2018	72,597	27,967	100,564	16,899	224	17,123	117,687
Additions	–	18,058	18,058	3,089	–	3,089	21,147
Disposals	–	–	–	(12)	–	(12)	(12)
At 31 December 2018	72,597	46,025	118,622	19,976	224	20,200	138,822
Accumulated amortisation							
At 1 January 2017	56,344	24,347	80,691	7,088	224	7,312	88,003
Amortisation charge for period	7,363	3,275	10,638	2,130	–	2,130	12,768
Disposals	–	(350)	(350)	–	–	–	(350)
At 1 January 2018	63,707	27,272	90,979	9,218	224	9,442	100,421
Amortisation charge for period	3,227	1,207	4,434	2,409	–	2,409	6,843
Disposals	–	–	–	(12)	–	(12)	(12)
At 31 December 2018	66,934	28,479	95,413	11,615	224	11,839	107,252
Carrying amount							
At 31 December 2018	5,663	17,546	23,209	8,361	–	8,361	31,570
At 31 December 2017	8,890	695	9,585	7,681	–	7,681	17,266

Revisions to acquisition intangibles additions in prior years relate to liabilities not accrued at the time of the acquisition. These revisions are not considered sufficiently material to warrant restatement of the prior year balances.

Development expenditure is an internally developed intangible asset and relates largely to the development of the Group's Housing job management system, the Group's Care management system and the national Planning Portal website. Development expenditure is amortised over its useful economic life of 5.0 years. The weighted average remaining economic life of the asset is 3.6 years (2017: 3.7 years).

Intellectual property is amortised over its useful economic life, typically 5.0 years.

Amortisation of development expenditure is included within other administrative expenses. Amortisation of acquisition intangibles is presented separately.

The value placed on the order book is based on the cash flow projections over the contracts in place when a business is acquired. Due to uncertainties in trying to forecast revenues beyond the contract term, the Directors have taken a measure of conservatism and value contracts over the contractual term only. The value of the order book is amortised over its remaining life.

The value placed on the customer relationships is based on the non-contractual expected cash inflows. These cash flow projections assume a customer attrition rate of 5% based on three-year historical trends.

15. Property, plant and equipment

	Freehold property £'000	Leasehold improvements £'000	Plant and machinery £'000	Fixtures, fittings and equipment £'000	Motor vehicles £'000	Assets under construction £'000	Total £'000
Gross carrying amount							
At 1 January 2017	788	13,953	2,890	46,670	1,295	–	65,596
Additions	–	2,107	99	5,915	–	–	8,121
Disposals	–	–	–	(2,472)	(20)	–	(2,492)
Disposal of subsidiary	–	–	–	(159)	–	–	(159)
At 1 January 2018	788	16,060	2,989	49,954	1,275	–	71,066
Additions	–	2,366	286	2,456	–	3,593	8,701
Acquisition of subsidiary	254	–	–	–	–	–	254
Disposals	(110)	–	(170)	(1,770)	(274)	–	(2,324)
Disposal of subsidiary	–	(2)	–	(91)	–	–	(93)
At 31 December 2018	932	18,424	3,105	50,549	1,001	3,593	77,604
Depreciation							
At 1 January 2017	–	8,877	1,925	33,288	1,241	–	45,331
Provided in the year	20	1,188	280	4,606	11	–	6,105
Eliminated on disposals	–	–	–	(2,244)	(20)	–	(2,264)
Disposal of subsidiary	–	–	–	(143)	–	–	(143)
At 1 January 2018	20	10,065	2,205	35,507	1,232	–	49,029
Provided in the year	5	1,170	229	4,388	12	–	5,804
Acquisition of subsidiary	7	–	–	–	–	–	7
Eliminated on disposals	(5)	–	(170)	(1,713)	(256)	–	(2,144)
Disposal of subsidiary	–	–	–	(48)	–	–	(48)
At 31 December 2018	27	11,235	2,264	38,134	988	–	52,648
Carrying amount							
At 31 December 2018	905	7,189	841	12,415	13	3,593	24,956
At 31 December 2017	768	5,995	784	14,447	43	–	22,037

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Notes to the financial statements – Group *continued* For the year ended 31 December 2018

16. Investments

The subsidiary undertakings within the Group at 31 December 2018 are shown below

	Proportion held	Country of registration	Nature of business
3c Asset Management Limited	100%	England and Wales	Maintenance services
Careforce Group Plc	100%	England and Wales	Dormant
Coulter Estates Limited	100%	Scotland	Dormant
Electrical Contracting Services (UK) Limited	100%	England and Wales	Dormant
Evolve Housing Limited	50%	England and Wales	Dormant
Heatherpark Community Services Limited	100%	Scotland	Dormant
Helcim Group Limited	100%	England and Wales	Dormant
Helcim Homes Limited	100%	England and Wales	Dormant
ILS Group Limited	100%	Scotland	Dormant
ILS Trustees Limited	100%	Scotland	Dormant
Independent Living Services (ILS) Limited	100%	Scotland	Provision of care
Jackson Lloyd Limited	100%	England and Wales	Dormant
Laidlaw Scott Limited	100%	Scotland	Dormant
Let to Birmingham Limited	100%	England and Wales	Housing management services
Manchester Working Limited	80%	England and Wales	Maintenance services
Mears Care (Holdings) Limited	100%	England and Wales	Intermediate holding company
Mears Care (Northern Ireland) Limited	100%	Northern Ireland	Dormant
Mears Care (Scotland) Limited	100%	Scotland	Provision of care
Mears Care Limited	100%	England and Wales	Provision of care
Mears Community Care Agency Limited	100%	England and Wales	Dormant
Mears Decorating Services Limited	100%	England and Wales	Dormant
Mears Direct Limited	80%	England and Wales	Dormant
Mears Energy Limited	100%	England and Wales	Dormant
Mears Estates Limited	100%	England and Wales	Grounds maintenance
Mears Facility Management Limited	100%	England and Wales	Dormant
Mears Home Improvement Limited	100%	England and Wales	Maintenance services
Mears Homecare Limited	100%	England and Wales	Provision of care
Mears Homes Limited	100%	England and Wales	Dormant
Mears Housing Limited	100%	England and Wales	Dormant
Mears Housing Management Limited	100%	England and Wales	Housing management services
Mears Housing Management (Holdings) Limited	100%	England and Wales	Intermediate holding company
Mears Housing Portfolio (Holdings) Limited	100%	England and Wales	Intermediate holding company
Mears Housing Portfolio (London) Limited	100%	England and Wales	Property acquisition
Mears Housing Portfolio 1 Limited	100%	England and Wales	Property acquisition
Mears Housing Portfolio 2 Limited	100%	England and Wales	Property acquisition
Mears Housing Portfolio 3 Limited	100%	England and Wales	Property acquisition
Mears Housing Portfolio 4 Limited	100%	England and Wales	Property acquisition

16. Investments continued

	Proportion held	Country of registration	Nature of business
Mears Insurance Company Limited	99.99%	Guernsey	Insurance services
Mears Learning Limited	90%	England and Wales	Training provider
Mears Limited	100%	England and Wales	Maintenance services
Mears Modular Homes Limited	100%	England and Wales	Dormant
Mears New Homes Limited	90%	England and Wales	House building
Mears Scotland (Housing) Limited	100%	Scotland	Dormant
Mears Scotland (Services) Limited	66.67%	Scotland	Maintenance services
Mears Scotland LLP	66.67%	Scotland	Maintenance services
Mears Social Housing Limited	100%	England and Wales	Dormant
Mears Wales Limited	100%	England and Wales	Dormant
MHM Property Services Limited	100%	England and Wales	Maintenance services
MPM Housing Limited	100%	England and Wales	Support services
MPS Housing Limited	100%	England and Wales	Maintenance services
Morrison Facilities Services Limited	100%	Scotland	Maintenance services
Nurseplus Limited	100%	Scotland	Dormant
O&T Developments Limited	100%	England and Wales	Housing management services
Omega Housing Limited	100%	England and Wales	Housing registered provider
Planning Portal Limited	75%	England and Wales	Dormant
Plexus UK (First Project) Limited	100%	England and Wales	Housing registered provider
PortalPlanQuest Limited	75%	England and Wales	Professional services
Potton Road Management Company Limited	90%	England and Wales	Dormant
PS Business Services Limited	100%	Scotland	Dormant
PS Payroll Services Limited	100%	England and Wales	Dormant
Scion Group Limited	100%	England and Wales	Dormant
Scion Property Services Limited	100%	England and Wales	Dormant
Scion Technical Services Limited	100%	England and Wales	Maintenance services
Supporta Limited	100%	England and Wales	Dormant
Supporta Services Limited	100%	England and Wales	Dormant
Tando Homes Limited	100%	England and Wales	Housing management services
Tando Property Services Limited	100%	England and Wales	Housing management services
Terraquest Group Limited	100%	England and Wales	Dormant
Terraquest Limited	100%	England and Wales	Dormant
Terraquest Solutions Limited	100%	England and Wales	Professional services

All subsidiary undertakings with the exception of Evolve Housing Limited and Manchester Working Limited prepare accounts to 31 December. Evolve Housing Limited prepares accounts to 30 June in line with its historical accounting reference date. Manchester Working Limited prepares accounts to 31 March in line with the minority shareholder.

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Notes to the financial statements – Group *continued* For the year ended 31 December 2018

16. Investments *continued*

The Group includes the following five trading subsidiaries with non-controlling interests: Manchester Working Limited, Mears Learning Limited, Mears New Homes Limited, Mears Scotland LLP and PortalPlanQuest Limited. The table below sets out selected financial information in respect of those subsidiaries.

	2018 £'000	2017 £'000
Revenue and profits		
Revenue	112,612	121,392
Expenses and taxation	(108,835)	(117,185)
Profit for the year	3,777	4,207
Other comprehensive expense	–	–
Total comprehensive income	3,777	4,207
Profit for the year allocated to non-controlling interests	761	1,263
Total comprehensive expense allocated to non-controlling interests	–	–
Net assets		
Non-current assets	314	1,469
Current assets	58,633	41,019
Current liabilities	(24,825)	(18,254)
Non-current liabilities	(33,887)	(22,337)
Total assets less total liabilities	235	1,897
Equity shareholders' funds	662	1,801
Non-controlling interests	(427)	96
Total equity	235	1,897

The Group held investments in the following joint ventures at 31 December 2018:

	Proportion held	Country of registration	Nature of business
Asert LLP	50%	England and Wales	Dormant
Sapphire Homes London Limited	50%	England and Wales	Property acquisition
Sapphire Homes London No. 1 Limited	50%	England and Wales	Property acquisition
Sapphire Homes London No. 2 Limited	50%	England and Wales	Property acquisition
Sapphire Homes London No. 3 Limited	50%	England and Wales	Dormant
Sapphire Homes London No. 4 Limited	50%	England and Wales	Dormant
Sapphire Homes London No. 5 Limited	50%	England and Wales	Dormant
Sapphire Homes London No. 6 Limited	50%	England and Wales	Dormant
Talking Assets Limited	50%	England and Wales	Dormant
YourMK LLP	50%	England and Wales	Maintenance services

The carrying amount of the above joint ventures was £nil (2017: £nil).

16. Investments continued

The following UK subsidiaries will take advantage of the audit exemption set out within Section 479A of the Companies Act 2006 for the year ended 31 December 2018

	Registration number
3c Asset Management Limited	02859913
Ardmore Home Care Limited	NI028313
Coulter Estates Limited	SC148145
Heatherpark Community Services Limited	SC314108
ILS Group Limited	SC285635
Independent Living Services (ILS) Limited	SC184499
Jackson Lloyd Limited	00981979
Let to Birmingham Limited	08757503
Mears Care (Northern Ireland) Limited	NI035273
Mears Community Care Agency Limited	03485601
Mears Estates Limited	03720903
Mears Home Improvement Limited	03716517
Mears Housing Management (Holdings) Limited	04726480
Mears Housing Portfolio (Holdings) Limited	10908305
Mears Housing Portfolio (London) Limited	10953521
Mears Housing Portfolio 1 Limited	10953330
Mears Housing Portfolio 2 Limited	10952666
Mears Housing Portfolio 3 Limited	10953300
Mears Housing Portfolio 4 Limited	10952906
MHM Property Services Limited	07448134
Nurseplus Limited	SC200513
Scion Group Limited	03905442
Scion Technical Services Limited	03671450

17. Assets held for sale

	2018 £'000	2017 £'000
Property held for sale	12,442	13,941

During the year, the Group acquired, held and disposed of property assets that are classified as held for sale prior to their disposal to long-term funding partners. These acquisitions were funded by a £15m (2017: £30m) rolling credit facility which is separate from the Group's main facility.

18. Inventories

	2018 £'000	2017 £'000
Materials and consumables	5,951	5,559
Work in progress	23,800	13,146
	29,751	18,705

The Group consumed inventories totalling £662.8m during the year (2017: £676.5m). No items are being carried at fair value less costs to sell (2017: £nil).

19. Construction contracts

Revenue of £39.1m (2017: £26.1m) relating to construction contracts has been included in the Consolidated Income Statement.

	2018 £'000	2017 £'000
Contract costs incurred	34,557	22,953
Recognised gross profits	4,542	3,130
Recognised gross losses	–	–
	39,099	26,083
Balances outstanding comprise		
– due from customers for construction contract work	3,907	1,332

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Notes to the financial statements – Group continued For the year ended 31 December 2018

20. Trade and other receivables

	2018 £'000	2017 £'000
Current assets		
~ trade receivables	63,787	51,602
~ contract assets on non-construction contracts	95,441	88,948
~ prepayments and accrued income	18,966	13,362
Total trade and other receivables	178,194	153,912

Trade receivables are normally due within 30 to 60 days and do not bear any effective interest rate. All trade receivables and accrued income are subject to credit risk exposure. Housing customers are typically Local Authorities and Housing Associations where credit risk is minimal. Care customers are typically Local Authorities and NHS Trusts where credit risk is minimal.

The ageing analysis of trade receivables is as follows:

	2018 £'000	2017 £'000
Neither impaired nor past due	52,879	44,717
Less than three months past due but not impaired	5,826	2,323
More than three months past due but not impaired	5,082	4,562
Total trade and other receivables	63,787	51,602

21. Trade and other payables

	2018 £'000	2017 £'000
Trade payables	100,664	103,432
Accruals and contract liabilities	59,373	45,905
Social security and other taxes	20,348	18,425
Contract liabilities for non-construction contract work	613	326
Finance lease liabilities	376	304
Other creditors	5,859	16,092
Total trade and other payables	187,233	184,484

Due to the short duration of trade payables, management considers the carrying amounts recognised in the Consolidated Balance Sheet to be a reasonable approximation of their fair value.

Included in other creditors is £2.0m (2017: £nil) relating to contingent consideration on acquisitions, £nil (2017: £5.0m) relating to deferred consideration on acquisitions and £nil (2017: £6.2m) relating to a forward purchase agreement in respect of 25% of Tando Property Services Limited, Tando Homes Limited and O&T Developments Limited.

22. Financial liabilities

	2018 £'000	2017 £'000
Current liabilities		
~ interest rate swaps	41	253
Non-current liabilities		
~ interest rate swaps	15	79
Total financial liabilities	56	332

23. Long-term other liabilities

	2018 £'000	2017 £'000
Finance lease liabilities	892	540
Other creditors	6,586	4,496
Total long-term other liabilities	7,478	5,036

24. Financial instruments

The Group uses a limited number of financial instruments comprising cash and liquid resources, borrowings, interest rate swaps and various items such as trade receivables and trade payables that arise directly from its operations. The main purpose of these financial instruments is to finance the Group's operations. The Group seeks to finance its operations through a combination of retained earnings and borrowings and investing surplus cash on deposit. The Group uses financial instruments to manage the interest rate risks arising from its operations and sources of finance but has no interests in the trade of financial instruments.

Categories of financial instruments

	2018 £'000	2017 £'000
Financial assets		
Amortised cost		
Trade receivables	63,787	51,602
Cash at bank and in hand	27,876	24,770
	91,663	76,372
Financial liabilities		
Fair value (level 2)		
Interest rate swaps – effective	(56)	(332)
Fair value (level 3)		
Deferred consideration in respect of acquisitions	–	(11,163)
Contingent consideration in respect of acquisitions	(2,000)	–
Amortised cost		
Borrowings related to assets held for sale	(15,000)	(13,941)
Bank borrowings and overdrafts	(93,780)	(50,559)
Trade payables	(100,664)	(103,432)
Accruals and contract liabilities	(59,373)	(45,905)
Other creditors	(11,714)	(10,269)
	(282,587)	(246,460)
	(190,924)	(170,088)

The IFRS 13 hierarchy level categorisation relates to the extent the fair value can be determined by reference to comparable market values.

The classifications range from level 1, where instruments are quoted on an active market, through to level 3, where the assumptions used to arrive at fair value do not have comparable market data.

The fair values of interest rate swaps have been calculated by a third party expert discounting estimated future cash flows on the basis of market expectations of future interest rates (level 2).

The amount of contingent consideration payable is generally determined by future expected profits of the acquired businesses. The fair values of contingent consideration have been calculated by the Directors by reference to expected future income and expenditure in respect of the acquired businesses.

There have been no transfers between levels during the year.

Fair value information

The fair value of the Group's financial assets and liabilities is as disclosed above and approximates to the book value.

Financial risk management

The Group's activities expose it to a variety of financial risks: market risk (including interest rate risk and price risk), credit risk, and liquidity risk. The main risks faced by the Group relate to the availability of funds to meet business needs and the risk of credit default by customers. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

Risk management is carried out under policies and guidelines approved by the Board of Directors.

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Notes to the financial statements – Group continued For the year ended 31 December 2018

24. Financial instruments continued

Borrowing facilities

The Group's borrowing facilities are drawn on as required to manage its cash needs. Banking facilities are reviewed regularly and extended and replaced in advance of their expiry.

The Group had total borrowing facilities of £185m with Barclays Bank PLC, HSBC Bank PLC and Lloyds Bank PLC, of which £110m was utilised at 31 December 2018.

The facilities comprise a committed four-year £130.0m revolving credit facility, a 364-day £15.0m loan and an unsecured overdraft facility of £10.0m. The undrawn amounts at 31 December 2018 were a £65.0m revolving credit facility and an overdraft facility of £10.0m. In addition, the Group has a property acquisition credit facility of £30m to acquire and build portfolios for resale. At 31 December 2018, assets held for resale utilising this facility amounted to £12.4m (2017: £13.9m). At 31 December 2018, the associated draw-down for these acquisitions was £15.0m (2017: £13.9m), funding both these assets for resale together with also part-funding the modular homes included within fixed assets.

Interest rate risk management

The Group finances its operations through a mixture of retained profits and bank borrowings from major banking institutions at floating rates of interest based on LIBOR. The Group's exposure to interest rate fluctuations on borrowings is managed through the use of interest rate swaps, hence the fixed rate borrowings relate to floating rate loans where the interest rate has been fixed by a hedging arrangement. The fair value of interest rate exposure on financial liabilities of the Group as at 31 December 2018 was

	Interest rate			Total £'000
	Fixed £'000	Floating £'000	Zero £'000	
Financial liabilities – 2018	70,000	40,000	–	110,000
Financial liabilities – 2017	64,500	–	11,163	75,663

The Group's policy is to accept a degree of interest rate risk, provided the effects of the various potential changes in rates remain within certain prescribed parameters.

Accordingly, at 31 December 2018 the Group had hedged the first £70.0m of the £185.0m total borrowing facilities by entering into interest rate swap arrangements with Barclays Bank PLC and HSBC Bank PLC. The arrangement with Barclays Bank PLC consists of two £15.0m swap contracts expiring in August 2021, with quarterly maturity, matching the underlying facility. The arrangement with HSBC Bank PLC consists of three swap contracts totalling £40.0m expiring in December 2020, with quarterly maturity, matching the underlying facility.

The maturity of the interest rate swap contracts is as follows:

	2018		2017	
	Nominal amount hedged £'000	Average applicable interest rates %	Nominal amount hedged £'000	Average applicable interest rates %
Within one year	–	–	30,000	1.85%
One to two years	40,000	0.84%	–	–
Two to five years	30,000	0.96%	40,000	0.84%
More than five years	–	–	–	–

Effective interest rates

Interest rate swaps with fair value liabilities of £0.1m (2017: £0.3m) and average remaining lives of two years and five months have been accounted for in financial liabilities.

The Group's overall average cost of debt, including effective interest rate swaps, is 2.5% as at 31 December 2018 (2017: 2.3%). Excluding these swaps the average is 2.3% (2017: 1.6%).

24. Financial instruments continued**Cash flow hedging reserve**

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Income Statement when the hedged item affects the Consolidated Income Statement.

Movements during the year were

	£'000
At 1 January 2017	(774)
Amounts transferred to the Consolidated Income Statement	645
Revaluations during the year	(54)
Deferred tax movement	(143)
At 1 January 2018	(326)
Amounts transferred to the Consolidated Income Statement	325
Revaluations during the year	–
Deferred tax movement	(45)
At 31 December 2018	(46)

At 31 December 2018 the Group had minimal exposure to movements in interest rates as the remaining interest rate risk was offset by the Group's cash and short-term deposits.

If the interest rates had been 0.5% higher or lower and all other variables were held constant, the Group's profit before taxation for the year ended 31 December 2018 and reserves would decrease or increase, respectively, by £0.4m (2017: £0.3m).

Liquidity risk management

The Group seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably.

Management monitors rolling forecasts of the Group's liquidity reserve (comprising undrawn borrowing facilities and cash and cash equivalents) on the basis of expected cash flows. This is generally carried out at a local level in the operating companies of the Group in accordance with the practice and limits set by the Group. These limits vary by location and take into account the liquidity and nature of the market in which the entity operates.

The quantum of committed borrowing facilities of the Group is regularly reviewed and is designed to exceed forecast peak gross debt levels. For short-term working capital purposes, the Group utilises bank overdrafts as required. These facilities are regularly reviewed and are renegotiated ahead of their expiry date.

The table below shows the maturity profile of the Group's financial liabilities.

	Within 1 year £'000	1–2 years £'000	2–5 years £'000	Over 5 years £'000	Total £'000
2018					
Non-derivative financial liabilities					
Borrowings related to assets held for sale	15,000	–	–	–	15,000
Bank borrowings	15,000	–	78,780	–	93,780
Trade and other payables	163,813	6,669	–	–	170,482
Deferred and contingent consideration in respect of acquisitions	–	–	–	–	–
Derivative financial liabilities					
Interest rate swaps – effective	41	15	–	–	56
2017					
Non-derivative financial liabilities					
Borrowings related to assets held for sale	13,941	–	–	–	13,941
Bank borrowings	–	–	50,559	–	50,559
Trade and other payables	154,606	4,155	–	–	158,761
Deferred and contingent consideration in respect of acquisitions	11,163	–	–	–	11,163
Derivative financial liabilities					
Interest rate swaps – effective	253	65	14	–	332

The Group has disclosed core bank borrowings of £80.0m as due in two to five years. Whilst the amounts borrowed could be repaid each quarter, the Group's intention is to align core bank borrowings with its interest rate swaps.

Financial statements

Notes to the financial statements – Group continued For the year ended 31 December 2018

24. Financial instruments continued

Credit risk management

The Group's credit risk is primarily attributable to its trade receivables, contract assets and work in progress

Trade receivables are normally due within 30 to 60 days. Trade and other receivables included in the Consolidated Balance Sheet are stated net of a bad debt provision which has been estimated by management following a review of individual receivable accounts. There is no Group-wide rate of provision and provision made for debts that are overdue is based on prior default experience and known factors at the balance sheet date. Receivables are written off against the bad debt provision when management considers that the debt is no longer recoverable.

Housing customers are typically Local Authorities and Housing Associations. Care customers are typically Local Authorities and NHS Trusts. The nature of both of these customers means that credit risk is minimal. Other trade receivables contain no specific concentration of credit risk as the amounts recognised represent a large number of receivables from various customers.

The Group continually monitors the position of major customers and incorporates this information into its credit risk controls. External credit ratings are obtained where appropriate.

Details of the ageing of trade receivables are shown in note 20.

Deferred and contingent consideration

The table below shows the movements in deferred and contingent consideration

	Deferred £'000	Contingent £'000	Total £'000
At 1 January 2017	16,163	294	16,457
Paid in respect of acquisitions	(5,000)	–	(5,000)
Released on reassessment	–	(294)	(294)
At 1 January 2018	11,163	–	11,163
Increase due to new acquisitions in the year	–	2,000	2,000
Paid in respect of acquisitions	(11,163)	–	(11,163)
At 31 December 2018	–	2,000	2,000

Contingent consideration represents an estimate of future consideration likely to be payable in respect of acquisitions. Contingent consideration is discounted for the likelihood of payment and for the time value of money. Contingent consideration becomes payable based on the profitability of acquired businesses or, in the case of one specific acquisition, the utilisation of certain timing differences in respect of corporation tax. The fair value of contingent consideration is estimated by forecasting future profits and utilising the forecast to determine the likely contingent consideration payable.

Information as to the likely timing of payments in respect of these provisions' financial liabilities is provided earlier within this note.

Capital management

The Group's objectives when managing capital are

- ~ to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders,
- ~ to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk, and
- ~ to maintain an optimal capital structure to reduce the cost of capital.

The Group sets the amount of capital in proportion to risk. The Group manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The capital structure of the Group consists of net debt as disclosed below and equity as disclosed in the Consolidated Statement of Changes in Equity.

	2018 £'000	2017 £'000
The Group considers its revolving credit facility to be an integral part of its cash management		
~ cash at bank and in hand	27,876	24,770
~ revolving credit facility	(93,780)	(50,559)
Cash and cash equivalents, including revolving credit facility	(65,904)	(25,789)

25. Deferred taxation

Deferred tax is calculated on temporary differences under the liability method

Deferred tax assets

The following deferred tax assets were recognised by the Group as at 31 December 2018

	Pension scheme £'000	Share-based payments £'000	Cash flow hedges £'000	Tax losses £'000	Short-term temporary differences £'000	Total £'000
At 1 January 2017	1,513	340	–	2,172	1,679	5,704
(Debit)/credit to Consolidated Income Statement	(84)	(267)	199	(1,015)	(87)	(1,254)
Debit to Consolidated Statement of Changes in Equity	–	404	–	–	–	404
(Debit)/credit to Consolidated Statement of Comprehensive Income	(397)	–	(143)	–	–	(540)
At 1 January 2018	1,032	477	56	1,157	1,592	4,314
Impact of change in accounting policies	–	–	–	–	6,013	6,013
Adjusted balance at 1 January 2018	1,032	477	56	1,157	7,605	10,327
(Debit)/credit to Consolidated Income Statement	(66)	116	–	250	(5,853)	(5,553)
Debit to Consolidated Statement of Changes in Equity	–	14	–	–	–	14
(Debit)/credit to Consolidated Statement of Comprehensive Income	(243)	–	(45)	–	–	(288)
Resulting from business combinations	–	–	–	–	1,000	1,000
At 31 December 2018	723	607	11	1,407	2,752	5,500

In accordance with IFRS 2 'Share-based Payment', the Group has recognised an expense for the consumption of employee services received as consideration for share options granted. A tax deduction will not arise until the options are exercised. The tax deduction in future periods is dependent on the Company's share price at the date of exercise. The estimated future tax deduction is based on the options' intrinsic value at the balance sheet date.

The cumulative amount credited to the Consolidated Income Statement is limited to the tax effect of the associated cumulative share-based payment expense. The excess has been credited directly to equity. This is presented in the Consolidated Statement of Comprehensive Income.

In addition to those recognised, unused tax losses totalling £28.4m (2017: £34.2m) have not been recognised as the Directors do not consider that it is probable that they will be recovered.

Deferred tax liabilities

The following deferred tax liabilities were recognised by the Group as at 31 December 2018

	Pension scheme £'000	Acquisition intangibles £'000	Cash flow hedges £'000	Total £'000
At 1 January 2017	3,127	3,904	89	7,120
(Credit)/debit to Consolidated Income Statement	(90)	(2,083)	(89)	(2,262)
Debit to Consolidated Statement of Comprehensive Income	2,240	–	–	2,240
At 1 January 2018	5,277	1,821	–	7,098
(Credit)/debit to Consolidated Income Statement	58	(842)	–	(784)
Debit to Consolidated Statement of Comprehensive Income	(2,035)	–	–	(2,035)
Resulting from business combinations	–	3,431	–	3,431
At 31 December 2018	3,300	4,410	–	7,710

Intangible assets acquired as part of a business combination are capitalised at fair value at the date of the acquisition and amortised over their useful economic lives. The UK tax regime calculates tax using the individual financial statements of the members of the Group and not the consolidated accounts. Hence, the tax base of acquisition intangible assets is £nil. The estimated tax effect of this £nil tax base is accounted for as a deferred tax liability which is released over the period of amortisation of the associated acquisition intangible asset.

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Notes to the financial statements – Group continued For the year ended 31 December 2018

26. Share capital and reserves

Classes of reserves

Share capital represents the nominal value of shares that have been issued

Share premium represents the difference between the nominal value of shares issued and the total consideration received

Share-based payment reserve represents employee remuneration which is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Income Statement when the hedged item affects the Consolidated Income Statement

The merger reserve relates to the difference between the nominal value and total consideration in respect of acquisitions, where the Company was entitled to the merger relief offered by the Companies Act 2006

Share capital

	2018 £'000	2017 £'000
Allotted, called up and fully paid		
At 1 January 103,567,091 (2017 102,559,799) ordinary shares of 1p each	1,036	1,026
Issue of 133,164 (2017 1,007,292) shares on exercise of share options	1	10
Issue of 6,787,331 (2017 nil) shares as a placement	68	–
At 31 December 110,487,586 (2017 103,567,091) ordinary shares of 1p each	1,105	1,036

During the year 133,164 (2017 1,007,292) ordinary 1p shares were issued in respect of share options exercised. In addition, the Group raised funds through a placement of 6,787,331 (2017 nil) ordinary 1p shares. The difference between the nominal value of £0.07m and the total consideration of £22.02m has been credited to the share premium account

27. Notes to the Consolidated Cash Flow Statement

The following non-operating cash flow adjustments have been made to the result for the year before tax

	2018 £'000	2017 £'000
Depreciation	5,804	6,105
Loss on disposal of property, plant and equipment	37	24
Profit on disposal of subsidiary	44	(961)
Amortisation	6,843	12,768
Share-based payments	552	826
IAS 19 pension movement	(655)	31
Finance income	(389)	(351)
Finance cost	3,405	2,706
Total	15,641	21,148

Movements in financing liabilities during the year are as follows

	Revolving credit facility	Borrowings relating to assets held for resale	Finance leases	Total
At 1 January 2017	65,278	–	113	65,391
Inception of new finance leases	–	–	2,685	2,685
Cash inflows/(outflows)	(14,719)	13,941	(1,954)	(2,732)
At 1 January 2018	50,559	13,941	844	65,344
Inception of new finance leases	–	–	903	903
Cash inflows/(outflows)	43,221	1,059	(479)	43,801
At 31 December 2018	93,780	15,000	1,268	110,048

28. Acquisitions and disposals

On 30 November 2018 the Group acquired certain business assets and contracts from the Mitie property services division. The transaction was facilitated via the purchase of the entire share capital of MPM Housing Limited and MPS Housing Limited for a total consideration of £22.5m. In addition, contingent consideration of a maximum of £12.5m may become payable based on a multiple of profit before tax for the acquired entities. The Directors have assessed the fair value of this contingent consideration as £2.0m. This is based on the present value of the expected consideration to be paid calculated by reference to anticipated profits of the business over the next two years. It is primarily sensitive to changes in those anticipated profits.

The acquisition was undertaken in order to strengthen the Group's offering in its Housing segment. It provides access to new clients and has significant synergies with the wider Group.

The effect of the acquisition of MPM and MPS is disclosed below.

	Total £'000
Assets	
Non-current	
Property, plant and equipment	248
Deferred tax asset	1,000
Current	
Trade receivables	32,175
Other receivables	7,278
Total assets	40,701
Liabilities	
Current	
Bank overdraft	(4,185)
Trade payables	(10,985)
Other payables	(18,423)
Total liabilities	(33,593)
Net assets acquired at fair value	7,108
Intangible assets recognised	17,392
Deferred tax recognised in respect of intangible assets	(3,304)
	21,196
Goodwill	3,304
	24,500
Satisfied by	
~ cash	22,500
~ contingent consideration	2,000
	24,500

In addition to the amounts noted above, the Group acquired £0.6m of liabilities in respect of a further acquisition. This other acquisition resulted in £0.6m of intangibles capitalised, a £0.1m deferred tax liability and £0.1m of goodwill capitalised.

Intangible assets of £18.1m have been recognised in respect of these acquisitions. They represent the expected value to be derived from the existing order books of the acquired businesses. The Directors consider that the value assigned to goodwill represents the benefits to the Group arising from synergies with its existing business.

The trade receivables detailed above are disclosed net of provisions totalling £4.3m and therefore the gross contractual amounts receivable total £36.5m. All the effects of these acquisitions on the Group's assets and liabilities are disclosed as provisional due to the proximity of the acquisitions to the balance sheet date.

In the period ended 31 December 2018, the acquisitions contributed revenue of £9.0m and a £0.5m operating loss before amortisation of acquisition intangibles.

For the year ended 31 December 2018, had the acquisitions taken place on 1 January 2018, the combined Group full year revenue is estimated at £998.3m and the combined Group profit for the year before taxation is estimated at £24.7m.

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Notes to the financial statements – Group *continued* For the year ended 31 December 2018

28. Acquisitions and disposals *continued*

Analysis of net outflow in respect of the purchase of the subsidiary undertakings

	Total £'000
Cash consideration	(22,500)
Net overdraft acquired with subsidiary undertakings	(4,185)
Net cash disposed of with subsidiary	(26)
Transactions with non-controlling interests	(6,163)
Cash payments in respect of prior year acquisitions	(5,000)
	(37,874)

On 1 January 2018 the Group reassessed the level of control it held over Mears 24/7 LLP and concluded that the threshold for control was no longer being met. As a result, the Group has not consolidated the results of Mears 24/7 LLP from 1 January 2018 and net assets of £0.04m, including cash of £0.03m, were derecognised. The Group ceased to be a partner on 12 September 2018.

On 4 January 2018, the Group acquired the remaining 25% of the share capital of O&T Developments Limited, Tando Property Services Limited and Tando Homes Limited for a total consideration of £6.2m.

29. Pensions

Defined contribution schemes

The Group operates a defined contribution Group personal pension scheme for the benefit of certain employees. The Group contributes to personal pension schemes of certain Directors and senior employees. The Group operates a stakeholder pension plan available to all employees. During the year, the Group contributed £4.0m (2017: £3.0m) to these schemes.

IAS 19 'Employee Benefits'

The Group contributes to 30 (2017: 30) principal defined benefit schemes on behalf of a number of employees which require contributions to be made to separately administered funds.

These pension schemes are operated on behalf of Mears Limited, Mears Care Limited, Morrison Facilities Services Limited and their subsidiary undertakings. The assets of the schemes are administered by trustees in funds independent from the assets of the Group.

In certain cases, the Group will participate under Admitted Body status in the Local Government Pension Scheme. The Group will contribute for a finite period up until the end of the particular contract. The Group is required to pay regular contributions as detailed in the scheme's schedule of contributions. In some cases these contributions are capped and any excess can be recovered from the body from which the employees originally transferred. Where the Group has a contractual right to recover the costs of making good any deficit in the scheme from the Group's client, the fair value of that asset has been recognised within the Group's pension assets. Certain judgements around the value of this asset have been made and are discussed in the judgements and estimates disclosure within the accounting policies.

The disclosures in respect of the two (2017: two) Group defined benefit schemes and the 28 (2017: 28) other defined benefit schemes in this note have been aggregated.

Costs and liabilities of the schemes are based on actuarial valuations. The latest full actuarial valuations for the schemes were updated to 31 December 2018 by qualified independent actuaries using the projected unit funding method.

The principal actuarial assumptions at the balance sheet date are as follows:

	2018	2017
Rate of increase of salaries – first year	2.00%	2.00%
Rate of increase of salaries – second year	3.15%	2.00%
Rate of increase of salaries – long term	3.15%	3.10%
Rate of increase for pensions in payment – based on CPI with a cap of 5%	2.20%	2.25%
Rate of increase for pensions in payment – based on RPI with a cap of 5%	3.05%	3.05%
Rate of increase for pensions in payment – based on CPI with a cap of 3%	1.90%	1.95%
Rate of increase for pensions in payment – based on RPI with a cap of 3%	2.45%	2.45%
Discount rate	2.95%	2.70%
Retail prices inflation	3.15%	3.10%
Consumer prices inflation	2.15%	2.20%
Life expectancy for a 65-year-old male	22.3 years	22.4 years
Life expectancy for a 65-year-old female	24.5 years	24.7 years

29. Pensions continued**IAS 19 'Employee Benefits'** continued

The amounts recognised in the Consolidated Balance Sheet and major categories of plan assets are

	2018			2017		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Equities – quoted	29,567	153,190	182,757	54,481	202,333	256,814
Equities – unquoted	–	13,927	13,927	–	21,669	21,669
Bonds – quoted	93,562	58,113	151,675	74,412	67,850	142,262
Bonds – unquoted	–	2,106	2,106	–	2,418	2,418
Property – quoted	4,352	6,215	10,567	4,258	6,258	10,516
Property – unquoted	–	5,875	5,875	–	13,562	13,562
Cash	25,391	29,348	54,739	24,174	31,437	55,611
Group's estimated asset share	152,872	268,774	421,646	157,325	345,527	502,852
Present value of funded scheme liabilities	(136,548)	(282,368)	(418,916)	(132,591)	(324,920)	(457,511)
Funded status	16,324	(13,594)	2,730	24,734	20,607	45,341
Guarantee	–	16,947	16,947	–	7,026	7,026
Scheme surpluses not recognised as assets	–	(6,111)	(6,111)	–	(30,025)	(30,025)
Pension asset/(liability)	16,324	(2,758)	13,566	24,734	(2,392)	22,342

The amounts recognised in the Consolidated Income Statement are as follows

	2018			2017		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Current service cost	2,091	3,483	5,574	2,826	3,252	6,078
Past service cost	150	–	150	–	199	199
Settlement and curtailment	–	(234)	(234)	–	–	–
Administration costs	121	–	121	142	72	214
Total operating charge	2,362	3,249	5,611	2,968	3,523	6,491
Net interest	(730)	34	(696)	(246)	25	(221)
Total charged to the result for the year	1,632	3,283	4,915	2,722	3,548	6,270

Past service cost above includes a charge of £150,000 in respect of the Group's estimate of the impact of GMP equalisation, following the recent Lloyds Banking Group ruling

Cumulative actuarial gains and losses recognised in equity are as follows

	2018			2017		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
On TUPE transfer of employees	–	(21,303)	(21,303)	–	(373)	(373)
Return on plan assets in excess of that recorded in net interest	(7,270)	(19,427)	(26,697)	3,942	(6,918)	(2,976)
Actuarial gain/(loss) arising from changes in demographic assumptions	(5,601)	221	(5,380)	15,686	1,082	16,768
Actuarial (loss)/gain arising from changes in financial assumptions	7,197	17,293	24,490	(1,064)	(9,617)	(16,681)
Actuarial gain arising from liability experience	(3,967)	(676)	(4,643)	(28)	31,447	31,419
Effects of limitation of recognisable surplus	–	24,102	24,102	–	(14,278)	(14,278)
Total gains and losses recognised in equity	(9,641)	210	(9,431)	12,536	1,343	13,879
At 1 January	6,807	(5,592)	1,215	(5,129)	(6,935)	(12,664)
Total at 31 December	(2,834)	(5,382)	(8,216)	6,807	(5,592)	1,215

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Notes to the financial statements – Group continued
For the year ended 31 December 2018

29. Pensions *continued*

IAS 19 'Employee Benefits' *continued*

Changes in the present value of the defined benefit obligations are as follows

	2018			2017		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Present value of obligations at 1 January	132,591	324,920	457,511	137,721	410,258	547,979
Current service cost	2,241	3,483	5,724	2,826	3,252	6,078
Past service cost	–	–	–	–	199	199
Scheme administration costs	–	–	–	–	22	22
Interest on obligations	3,560	7,499	11,059	4,148	9,052	13,200
Plan participants' contributions	321	1,064	1,385	374	1,136	1,510
Benefits paid	(4,536)	(5,751)	(10,287)	(3,884)	(6,107)	(9,991)
Contract transfer	–	(31,907)	(31,907)	–	(72,584)	(72,584)
Settlements	–	(2,062)	(2,062)	–	–	–
Actuarial gain arising from changes in demographic assumptions	5,601	(221)	5,380	(15,686)	(1,082)	(16,768)
Actuarial loss arising from changes in financial assumptions	(7,197)	(15,333)	(22,530)	7,064	12,221	19,285
Actuarial loss/(gain) arising from liability experience	3,967	676	4,643	28	(31,447)	(31,419)
<i>Present value of obligations at 31 December</i>	136,548	282,368	418,916	132,591	324,920	457,511

Changes in the fair value of the plan assets are as follows

	2018			2017		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Fair value of plan assets at 1 January	157,325	352,553	509,878	149,529	422,691	572,220
Expected return on plan assets	4,290	7,653	11,943	4,394	9,027	13,421
Employer's contributions	2,863	2,707	5,570	3,112	3,127	6,239
Plan participants' contributions	321	1,064	1,385	374	1,136	1,510
Benefits paid	(4,536)	(5,751)	(10,287)	(3,884)	(6,107)	(9,991)
Scheme administration costs	(121)	–	(121)	(142)	(50)	(192)
Contract transfer	–	(53,210)	(53,210)	–	(72,957)	(72,957)
Settlements	–	(1,828)	(1,828)	–	–	–
Return on plan assets above/(below) that recorded in net interest	(7,270)	(17,467)	(24,737)	3,942	(4,314)	(372)
<i>Fair value of plan assets at 31 December</i>	152,872	285,721	438,593	157,325	352,553	509,878

History of experience gains and losses is as follows

	Group schemes				
	2018 £'000	2017 £'000	2016 £'000	2015 £'000	2014 £'000
Fair value of scheme assets	152,872	157,325	149,529	116,512	115,818
Net present value of defined benefit obligations	(136,548)	(132,591)	(137,721)	(111,327)	(106,710)
Net surplus	16,324	24,734	11,808	5,185	9,108
Experience adjustments arising on scheme assets					
Amount	(7,270)	3,942	27,129	(4,984)	10,624
Percentage of scheme assets	(4.8%)	2.5%	18.1%	(4.3%)	9.2%
Experience adjustments arising on scheme liabilities					
Amount	3,967	28	(1,000)	(5,193)	(910)
Percentage of scheme liabilities	2.9%	0.0%	(0.7%)	(4.7%)	(0.9%)

29. Pensions *continued*

IAS 19 'Employee Benefits' *continued*

	Other schemes				
	2018 £'000	2017 £'000	2016 £'000	2015 £'000	2014 £'000
Fair value of scheme assets	285,721	352,553	422,691	352,690	347,034
Net present value of defined benefit obligations	(282,368)	(324,920)	(410,258)	(333,839)	(331,666)
Net surplus	3,353	27,633	12,433	18,851	15,368
Asset value not recognised as surplus	(6,111)	(30,025)	(15,747)	(19,988)	(17,717)
Net deficit	(2,758)	(2,392)	(3,314)	(1,137)	(2,349)
Experience adjustments arising on scheme assets					
Amount	(25,033)	(4,314)	59,020	(7,406)	22,125
Percentage of scheme assets	(8.8%)	(1.2%)	14.0%	(2.1%)	6.4%
Experience adjustments arising on scheme liabilities					
Amount	676	(31,447)	(1,714)	(819)	(9,828)
Percentage of scheme liabilities	0.2%	(9.7%)	(0.4%)	(0.2%)	(3.0%)

Funding arrangements are agreed for each of the Group's defined benefit pension schemes with their respective trustees. The employer's contributions expected to be paid during the financial year ending 31 December 2019 amount to £5.4m.

Each of the schemes manages risks through a variety of methods and strategies to limit downside in falls in equity markets, movement in inflation and movement in interest rates.

The Group's defined benefit obligation is sensitive to changes in certain key assumptions. The sensitivity analysis below shows how a reasonably possible increase or decrease in a particular assumption, in isolation, results in an increase or decrease in the present value of the defined benefit obligation as at 31 December 2018.

	Decrease £'000	Increase £'000
Rate of inflation – decrease/increase by 0.1%	(1,552)	1,141
Rate of increase in salaries – decrease/increase by 0.1%	(139)	134
Discount rate – decrease/increase by 0.1%	3,283	(3,058)
Life expectancy – decrease/increase by 1 year	(5,704)	6,131

30. Operating lease commitments

Non-cancellable operating lease rentals payable were as follows:

	Land and buildings		Other	
	2018 £'000	2017 £'000	2018 £'000	2017 £'000
Payable				
Within one year	44,899	42,520	13,523	14,038
Between two and five years	38,877	29,829	17,290	14,511
After more than five years	69,583	44,051	–	–
	153,359	116,400	30,813	29,600

Operating lease payments represent rentals payable by the Group for certain of its office properties and Housing Management residential properties, the hire of vehicles and the hire of other equipment. These leases have durations ranging from one to 15 years. No arrangements have been entered into in respect of contingent rental payments.

31. Capital commitments

The Group had no capital commitments at 31 December 2018 or at 31 December 2017.

32. Contingent liabilities

The Group has guaranteed that it will complete certain Group contracts that it has commenced. At 31 December 2018 these guarantees amounted to £18.7m (2017: £21.7m).

As detailed in note 7, the Group has a facility in place guaranteeing the performance of a number of M&E projects in Haydon Mechanical and Electrical Company LLC ('Haydon LLC'). The guarantees will fall away as the final accounts are agreed and the associated guarantees released. As at 31 December 2018, guarantees amounted to £3.9m (2017: £3.8m) and a balance of £2.2m has been provided for against this balance.

The Group had no other contingent liabilities at 31 December 2018 or at 31 December 2017.

Financial statements

Notes to the financial statements – Group continued For the year ended 31 December 2018

33. Related party transactions

Identity of related parties

The Group has a related party relationship with its pension schemes, its subsidiaries and its Directors

Pension schemes

Details of contributions to pension schemes are set out in note 29 to the financial statements

Subsidiaries

The Group has a central treasury arrangement in which all subsidiaries participate. The Directors do not consider it meaningful to set out details of transfers made in respect of this treasury arrangement between companies, nor do they consider it meaningful to set out details of interest or dividend payments made within the Group

Transactions with key management personnel

The Group has identified key management personnel as the Directors of Mears Group PLC

Key management personnel held the following percentage of voting shares in Mears Group PLC

	2018 %	2017 %
Directors	0.3	0.4

Key management personnel's compensation is as follows

	2018 £'000	2017 £'000
Salaries including social security costs	1,778	1,765
Contributions to defined contribution pension schemes	121	161
Share-based payments	100	150
	1,999	2,076

Further details of Directors' remuneration are disclosed within the Remuneration Report

Dividends totalling £0.04m (2017: £0.04m) were paid to Directors during the year

Transactions with other related parties

During the year the Group made additional loans to YourMK LLP, an entity in which the Group is a 50% member, totalling £0.1m (2017: £0.2m)

At 31 December 2018, the Group was owed £0.5m (2017: £0.4m) by YourMK LLP

Financial statements

Principal accounting policies – Company

Statement of compliance

Mears Group PLC is a public limited company incorporated in England and Wales. Its registered office is 1390 Montpelier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH.

Basis of preparation

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards, including FRS 101 and the Companies Act 2006. The financial statements have been prepared on the historical cost basis except for the modification to a fair value basis for certain financial instruments specified in the accounting policies below. The financial statements are presented in Sterling.

The Company has taken advantage of the exemption in Section 408 of the Companies Act 2006 from disclosing its individual profit and loss account.

The Company has taken advantage of the reduced disclosures for subsidiaries and the ultimate parent provided for in FRS 101 and has therefore not provided a cash flow statement or certain disclosures in respect of share-based payments.

The principal accounting policies of the Company are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated.

Goodwill

Goodwill representing the reallocation of amounts previously classed as investments upon the hive-across of trade and assets is capitalised and amortised on a straight-line basis over its estimated useful economic life.

Share-based employee remuneration

All share-based payment arrangements that were granted after 7 November 2002 are recognised in the financial statements.

The Group operates equity-settled and cash-settled share-based remuneration plans for its employees. All employee services received in exchange for the grant of any share-based remuneration are measured at their fair value. These are indirectly determined by reference to the fair value of the share options awarded. Their value is determined at the date of grant and is not subsequently remeasured unless the conditions on which the award was granted are modified. The fair value at the date of the grant is calculated using the Black Scholes option pricing model and the cost is recognised on a straight-line basis over the vesting period. Adjustments are made to reflect expected and actual forfeitures during the vesting period.

Share-based remuneration in respect of employees of the Company is ultimately recognised as an expense in the profit and loss account. For equity-settled share-based payments there is a corresponding credit to the share-based payment reserve, for cash-settled share-based payments the Company recognises a liability at the balance sheet date. The Company operates share-based remuneration plans for employees of subsidiaries using the Company's equity instruments. The fair value of the compensation given in respect of these share-based compensation plans less payments received from subsidiaries in respect of those share-based payments is recognised as a capital contribution.

Upon exercise of share options, the proceeds received, net of any directly attributable transaction costs up to the nominal value of the shares issued, are allocated to share capital with any excess being recorded as share premium.

Deferred taxation

Deferred tax is recognised on all timing differences where the transactions or events that give the Company an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred by the balance sheet date. Deferred tax assets are recognised where it is more likely than not that they will be recovered. Deferred tax is measured using rates of tax and laws that have been enacted or substantively enacted by the balance sheet date.

Financial statements

Principal accounting policies – Company continued

Retirement benefits

i) Defined contribution pension scheme

The pension costs charged against profits are the contributions payable to individual policies in respect of the accounting period

ii) Defined benefit pensions

The Company contributes to defined benefit schemes which require contributions to be made to separately administered funds.

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligations for any benefits from this kind of pension plan remain with the Group, even if plan assets for funding the defined benefit plan have been set aside.

Scheme liabilities are measured using the projected unit funding method, applying the principal actuarial assumptions at the balance sheet date. Assets are measured at market value. The asset that is recognised is restricted to the amount by which the service cost is expected, over the lifetime of the scheme, to exceed funding contributions payable in respect of accruing benefits.

Actuarial gains and losses are taken to the Consolidated Statement of Comprehensive Income as incurred. For this purpose, actuarial gains and losses comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

Other movements in the net surplus or deficit are recognised in the profit and loss account, including the current service cost, any past service cost and the effect of curtailments or settlements. The interest costs less the expected return on assets are also charged to the Consolidated Income Statement. *The amount charged to the Consolidated Income Statement in respect of these plans is included within operating costs.*

The Company's contributions to the schemes are paid in accordance with the rules of the schemes and the recommendations of the actuary.

Investments

Investments in equity shares which are not publicly traded and where fair value cannot be measured reliably are measured at cost less impairment. *Dividends on equity securities are recognised in income when receivable.*

Financial instruments

Financial assets and liabilities are recognised in the Consolidated Balance Sheet when the Company becomes party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Company are as follows:

Financial assets

Basic financial assets, including trade and other receivables, amounts due to Group companies and cash and cash equivalents, are initially recognised at transaction price, unless the arrangement constitutes a financing transaction, where the transaction is measured at the present value of the future receipts discounted at a market rate of interest.

Such assets are subsequently carried at amortised cost using the effective interest rate method.

At the end of each reporting period financial assets measured at amortised cost are assessed for objective evidence of impairment. If an asset is impaired the impairment loss is the difference between the carrying amount and the present value of the estimated cash flows discounted at the asset's original effective interest rate. The impairment loss is recognised in profit or loss.

Financial assets are derecognised when (a) the contractual rights to the cash flows from the asset expire or are settled, (b) substantially all the risks and rewards of the ownership of the asset are transferred to another party, or (c) despite having retained some significant risks and rewards of ownership, control of the asset has been transferred to another party which has the practical ability to unilaterally sell the asset to an unrelated third party without imposing additional restrictions.

Cash and cash equivalents include cash at bank and in hand and bank deposits available with no notice or less than three months' notice from inception that are subject to an insignificant risk of changes in value. Bank overdrafts are presented as current liabilities to the extent that there is no right of offset with cash balances.

Retirement benefits continued**Financial liabilities**

Basic financial liabilities, including trade and other payables, and amounts payable to Group companies that are classified as debt, are initially recognised at transaction price, unless the arrangement constitutes a financing transaction, where the debt instrument is measured at the present value of the future receipts discounted at a market rate of interest

Bank borrowings are non-basic financial liabilities and are initially recognised at fair value, being the present value of future payments discounted at a market rate of interest. Bank borrowings are remeasured at fair value.

Derivatives, including interest rate swaps, are not basic financial instruments.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Changes in the fair value of derivatives are recognised in profit or loss in finance costs or finance income as appropriate, unless they are included in a hedging arrangement.

Financial liabilities are derecognised when the liability is extinguished, that is when the contractual obligation is discharged or cancelled or expires.

Offsetting

Financial assets and liabilities are offset and the net amounts presented in the financial statements when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

Hedge accounting for interest rate swaps

The Company applies hedge accounting for transactions entered into to manage the cash flow exposures of borrowings. Interest rate swaps are held to manage the interest rate exposures and are designated as cash flow hedges of floating rate borrowings.

Changes in the fair values of derivatives designated as cash flow hedges, and which are effective, are recognised directly in equity. Any ineffectiveness in the hedging relationship (being the excess of the cumulative change in fair value of the hedging instrument since inception of the hedge over the cumulative change in the fair value of the hedged item since inception of the hedge) is recognised in the Consolidated Income Statement.

The gain or loss recognised in other comprehensive income is reclassified to the Consolidated Income Statement when the hedge relationship ends. Hedge accounting is discontinued when the hedging instrument expires or no longer meets the hedging criteria, the forecast transaction is no longer highly probable, the hedged debt instrument is derecognised or the hedging instrument is terminated.

Critical judgements and key sources of estimation uncertainty

Critical judgements in applying the Company's accounting policies and key sources of estimation uncertainty are disclosed in the Group's accounting policies on pages 112 to 113.

Financial statements
Parent Company balance sheet
As at 31 December 2018

	Note	2018 £'000	2017 £'000
Non-current assets			
Intangible assets: goodwill		–	–
Investments	5	58,123	58,123
		58,123	58,123
Current assets			
Debtors	6	194,112	143,944
Cash at bank and in hand		191	2,276
		194,303	146,220
Creditors: amounts falling due within one year	7	(38,848)	(5,141)
Net current assets		155,455	141,079
Total assets less current liabilities		213,578	199,202
Creditors: amounts falling due after more than one year	8	(78,795)	(50,079)
Provisions for liabilities			
Pension liability	13	(1,044)	(2,574)
		133,739	146,549
Capital and reserves			
Called up share capital	10	1,105	1,036
Share premium account		82,224	60,204
Share-based payment reserve		2,021	1,469
Hedging reserve		(46)	(326)
Profit and loss account		48,435	84,166
Shareholders' funds		133,739	146,549

The Parent Company has taken advantage of Section 408 of the Companies Act 2006 and has not included its own profit and loss account in these financial statements. The Group profit for the year includes a loss of £23.2m (2017 profit: £49.3m) which is dealt with in the financial statements of the Company.

The financial statements were approved by the Board of Directors on 22 March 2019.

D J Miles A C M Smith
Director Director

Company number: 03232863

The accompanying accounting policies and notes form an integral part of these financial statements.

Financial statements

Parent Company statement of changes in equity For the year ended 31 December 2018

	Share capital £'000	Share premium account £'000	Share- based payment reserve £'000	Hedging reserve £'000	Retained earnings £'000	Total equity £'000
At 1 January 2017	1,026	58,320	1,975	(774)	45,184	105,731
Net result for the year	–	–	–	–	49,263	49,263
Other comprehensive expense	–	–	–	448	605	1,053
Total comprehensive (expense)/income for the year	–	–	–	448	49,868	50,316
Issue of shares	10	1,884	–	–	–	1,894
Share option charges	–	–	826	–	–	826
Share option exercises	–	–	(1,332)	–	1,332	–
Dividends	–	–	–	–	(12,218)	(12,218)
At 1 January 2018	1,036	60,204	1,469	(326)	84,166	146,549
Impact of change in accounting policies	–	–	–	–	(443)	(443)
Adjusted balance at 1 January 2018	1,036	60,204	1,469	(326)	83,723	146,106
Net result for the year	–	–	–	–	(23,239)	(23,239)
Other comprehensive expense	–	–	–	280	490	770
Total comprehensive (expense)/income for the year	–	–	–	280	(22,749)	(22,469)
Issue of shares	69	22,020	–	–	–	22,089
Share option charges	–	–	552	–	–	552
Dividends	–	–	–	–	(12,539)	(12,539)
At 31 December 2018	1,105	82,224	2,021	(46)	48,435	133,739

The accompanying accounting policies and notes form an integral part of these financial statements

Financial statements
Notes to the financial statements – Company
For the year ended 31 December 2018

1. Result for the financial year

This result for the year is stated after charging auditor's remuneration of £55,000 (2017: £65,000) relating to audit services

2. Directors and employees

Employee benefits expense

	2018 £'000	2017 £'000
Wages and salaries	13,755	17,891
Social security costs	1,920	2,477
Other pension costs	774	795
	16,449	21,163

The average number of employees of the Company during the year was

	2018 Number	2017 Number
Management	339	411

Remuneration in respect of Directors was as follows

	2018 £'000	2017 £'000
Emoluments	1,507	1,389
Gains made on the exercise of share options	–	1,148
Pension contributions to personal pension schemes	121	161
	1,628	2,698

During the year contributions were paid to personal pension schemes for three Directors (2017: four)

During the year no Directors (2017: three) exercised share options

3. Share-based employee remuneration

As at 31 December 2018 the Group maintained six share-based payment schemes for employee remuneration. The details of each scheme are included within note 7 to the consolidated financial statements.

All share-based employee remuneration will be settled in equity. The Group has no legal obligation to repurchase or settle the options.

In total, £0.2m of employee remuneration expense has been included in the Company's profit and loss account for 2018 (2017: £0.2m), which gave rise to additional paid-in capital.

4. Dividends

The following dividends were paid on ordinary shares in the year

	2018 £'000	2017 £'000
Final 2017 dividend of 8.55p (2017: final 2016 dividend of 8.40p) per share	8,860	8,651
Interim 2018 dividend of 3.55p (2017: interim 2017 dividend of 3.45p) per share	3,679	3,567
	12,539	12,218

The proposed final 2018 dividend of 8.85p per share has not been included within the financial statements as no obligation existed at 31 December 2018.

5. Fixed asset investments

	Investment in subsidiary undertakings £'000
At 1 January 2018 and 31 December 2018	58,123

Details of the subsidiary undertakings of the Company are shown in note 16 to the consolidated financial statements.

6. Debtors

	2018 £'000	2017 £'000
Amounts owed by Group undertakings	193,084	142,531
Other receivables	498	868
Deferred tax asset	530	545
	194,112	143,944

The deferred tax asset above of £0.5m (2017: £0.5m) is due after more than one year. The recoverability of the deferred tax asset is dependent on future taxable profits. The Company expects to realise sufficient profits to enable the deferred tax asset to be recovered.

7. Creditors: amounts falling due within one year

	2018 £'000	2017 £'000
Bank loan	15,000	–
Bank overdraft	21,032	–
Interest rate swaps	41	253
Accruals	2,292	4,061
Corporation tax	453	347
Other payables	30	480
	38,848	5,141

8. Creditors: amounts falling due in more than one year

	2018 £'000	2017 £'000
Bank borrowings	78,780	50,000
Contingent consideration	–	–
Interest rate swaps	15	79
	78,795	50,079

The Company has disclosed core bank borrowings of £78.8m as due in two to five years. Whilst the amounts borrowed could be repaid each quarter, the Company's intention is to align core bank borrowings with its interest rate swaps.

Included in other creditors is £nil (2017: £nil) relating to deferred consideration on acquisitions.

9. Financial instruments

The Company has the following financial instruments:

	2018 £'000	2017 £'000
Financial assets that are debt instruments measured at amortised cost		
~ other receivables	–	50
Financial liabilities that are measured at fair value through other comprehensive income		
~ interest rate swaps	(56)	(332)
Financial liabilities that are measured at amortised cost		
~ bank borrowings	(93,780)	(50,000)
~ accruals	(3,902)	(4,061)
~ other payables	(30)	(480)
	(97,712)	(54,541)

There have been no changes during the period or cumulatively in the fair value of bank borrowings attributable to changes in the credit risk of the instrument. The change attributable to changes in own credit risk is not material due to the short life of individual draw-downs within bank borrowings. The difference between the carrying amount and the amount expected to be paid at maturity is not material due to the short life of individual draw-downs within bank borrowings.

The Company pays a margin over and above LIBOR on bank borrowings. The margin is based on the ratio of Group consolidated net borrowings to Group consolidated adjusted EBITDA and could have varied between 1.2% and 2.2% during the year.

The Company has entered into interest rate swaps to receive interest at LIBOR and pay interest at fixed rates. At 31 December 2018, these consist of two £15.0m swap contracts expiring in August 2021 with a fixed interest rate of 0.96%, one £20.0m swap contract expiring in December 2020 with a fixed interest rate of 0.84% and two £10.0m swap contracts expiring in December 2020 with fixed interest rates of 0.84%. The swaps have quarterly maturity matching the underlying debt.

Financial statements

Notes to the financial statements – Company continued

For the year ended 31 December 2018

9. Financial instruments continued

These instruments are used to mitigate the Company's exposure to any interest rate movements. The fair value of the interest rate swaps is a liability of £0.1m (2017: £0.3m).

During 2018, a hedging loss of £nil (2017: £0.1m) was recognised in other comprehensive income for changes in the fair value of the interest rate swap and £0.3m (2017: £0.6m) was reclassified from the hedge reserve to profit and loss.

The Company seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably.

Management monitors rolling forecasts of the Group and Company's liquidity reserve (comprising undrawn borrowing facilities and cash and cash equivalents) on the basis of expected cash flows. The quantum of committed borrowing facilities of the Group and Company is regularly reviewed and is designed to exceed forecast peak gross debt levels. For short-term working capital purposes, the Group and Company utilise bank overdrafts as required. These facilities are regularly reviewed and are renegotiated ahead of their expiry date.

10. Share capital and reserves

	2018 £'000	2017 £'000
Allotted, called up and fully paid		
At 1 January 103,567,091 (2017: 102,559,799) ordinary shares of 1p each	1,036	1,026
Issue of 133,164 (2017: 1,007,292) shares on exercise of share options	1	10
Issue of 6,787,331 (2017: nil) shares as a placement	68	–
At 31 December 110,487,586 (2017: 103,567,091) ordinary shares of 1p each	1,105	1,036

During the year 133,164 (2017: 1,007,292) ordinary 1p shares were issued in respect of share options exercised. In addition, the Group raised funds through a placement of 6,787,331 (2017: nil) ordinary 1p shares. The difference between the nominal value of £0.07m and the total consideration of £22.02m has been credited to the share premium account.

Classes of reserves

Share capital represents the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Share-based payment reserve represents employee remuneration which is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Income Statement when the hedged item affects the Consolidated Income Statement.

11. Capital commitments

The Company had no capital commitments at 31 December 2018 or at 31 December 2017.

12. Contingent liabilities

The Company has guaranteed that it will complete certain Group contracts that its subsidiaries have commenced. At 31 December 2018 these guarantees amounted to £18.7m (2017: £21.7m).

As detailed in note 7 to the Group financial statements, the Group has a facility in place guaranteeing the performance of a number of M&E projects in Haydon Mechanical and Electrical Company LLC ('Haydon LLC'). The guarantees will fall away as the final accounts are agreed and the associated guarantees released. As at 31 December 2018, guarantees amounted to £3.9m (2017: £3.8m) and a balance of £2.2m has been provided for against this balance.

The Company had no other contingent liabilities at 31 December 2018 or at 31 December 2017.

13. Pensions

Defined contribution schemes

The Company contributes to personal pension schemes of the Directors

Defined benefit scheme

The Company operates a defined benefit pension scheme for the benefit of certain employees of its subsidiary companies. The assets of the schemes are administered by trustees in a fund independent from the assets of the Company.

Costs and liabilities of the scheme are based on actuarial valuations. The actuarial valuations were reviewed and updated to 31 December 2018 by a qualified independent actuary using the projected unit method.

The principal actuarial assumptions at the balance sheet date are as follows:

	2018	2017
Rate of increase of salaries – first year	2.00%	2.00%
Rate of increase of salaries – second year	3.15%	2.00%
Rate of increase of salaries – long term	3.15%	3.10%
Rate of increase for pensions in payment – based on RPI with a cap of 5%	3.05%	3.05%
Rate of increase for pensions in payment – based on RPI with a cap of 3%	2.45%	2.45%
Discount rate	2.95%	2.80%
Retail prices inflation	3.15%	3.10%
Consumer prices inflation	2.15%	2.20%
Life expectancy for a 65-year-old male	20.9 years	21.9 years
Life expectancy for a 65-year-old female	23.8 years	23.7 years

The amounts recognised in the Parent Company Balance Sheet and major categories of plan assets as a percentage of total plan assets are:

	2018 £'000	2017 £'000
Equities	7,721	9,860
Bonds	9,734	7,718
Cash	1,488	840
Group's estimated asset share	18,943	18,418
Present value of funded scheme liabilities	(19,987)	(20,992)
Funded status	(1,044)	(2,574)
Related deferred tax asset	198	489
Pension liability	(846)	(2,085)

The amounts recognised in the profit and loss account are as follows:

	2018 £'000	2017 £'000
Current service cost	36	75
Administration cost	–	–
Total operating charge	36	75
Net interest	58	112
Total charged to the result for the year	94	187

	2018 £'000	2017 £'000
Present value of obligations at 1 January	20,992	21,337
Current service cost	36	75
Interest on obligations	581	643
Plan participants' contributions	5	10
Benefits paid	(502)	(517)
Actuarial gain arising from changes in demographic assumptions	(430)	(822)
Actuarial gain/(loss) arising from changes in financial assumptions	(574)	355
Actuarial loss arising from liability experience	(121)	(89)
Present value of obligations at 31 December	19,987	20,992

Financial statements

Notes to the financial statements – Company continued For the year ended 31 December 2018

13. Pensions continued

Defined benefit scheme continued

Changes in the fair value of the plan assets are as follows

	2018 £'000	2017 £'000
Fair value of plan assets at 1 January	18,418	17,153
Expected return on plan assets	523	531
Employer's contributions	1,019	1,050
Plan participants' contributions	5	10
Benefits paid	(502)	(517)
Return on plan assets above that recorded in net interest	(520)	191
Fair value of plan assets at 31 December	18,943	18,418

The movements in the net pension liability and the amount recognised in the Balance Sheet are as follows

	2018 £'000	2017 £'000
Deficit in schemes at 1 January	(2,574)	(4,184)
Current service cost	(36)	(75)
Contributions	1,019	1,050
Other finance income	(58)	(112)
Actuarial gain arising from changes in demographic assumptions	430	822
Actuarial (loss)/gain arising from changes in financial assumptions	574	(355)
Actuarial loss arising from liability experience	121	89
Return on plan assets above that recorded in net interest	(520)	191
Deficit in schemes at 31 December	(1,044)	(2,574)

The employer's contributions expected to be paid during the financial year ending 31 December 2019 amount to £0.4m

14. Related party transactions

Identity of related parties

The Group has a related party relationship with its pension schemes, its subsidiaries and its Directors

Pension schemes

Details of contributions to pension schemes are set out in note 13 to the financial statements

Subsidiaries

The Group has a central treasury arrangement in which all subsidiaries participate. The Directors do not consider it meaningful to set out details of transfers made in respect of this treasury arrangement between companies, nor do they consider it meaningful to set out details of interest or dividend payments made within the Group

Transactions with key management personnel

The Group has identified key management personnel as the Directors of Mears Group PLC. Details of transactions are disclosed in note 33 to the consolidated financial statements

Shareholder information
Five-year record (unaudited)

Strategic report

Corporate governance

Financial statements

Shareholder information

Consolidated Income Statement (continuing activities)

	2018 £'000	2017 £'000	2016 £'000	2015 £'000	2014 £'000
Revenue by business segment					
Housing	753,230	766,121	787,530	735,129	714,733
Care	116,613	134,063	152,570	146,010	124,007
Continuing activities	869,843	900,184	940,100	881,139	838,740
Gross profit	207,018	223,702	244,894	232,132	225,041
Operating profit before acquisition intangible amortisation and exceptional costs	40,841	39,151	41,850	38,662	42,995
Exceptional items	(5,657)	–	–	–	–
Operating profit	30,750	28,513	31,160	27,825	30,667
Profit for the year before tax	28,431	26,484	29,372	25,920	29,677
PBT before acquisition intangible amortisation and exceptional costs	38,522	37,122	40,062	36,757	42,005
Earnings per share					
Basic	23.05p	20.28p	23.54p	20.31p	25.03p
Diluted	22.91p	20.10p	23.41p	20.10p	24.65p
Normalised	29.06p	28.05p	30.36p	27.94p	32.20p
Dividends per share	12.40p	12.00p	11.70p	11.00p	10.00p

Consolidated Balance Sheet

	2018 £'000	2017 £'000	2017 £'000	2017 £'000	2017 £'000
Non-current assets	276,467	264,567	262,263	258,201	268,818
Current assets	248,872	211,439	222,158	237,767	217,718
Current liabilities	(217,274)	(198,678)	(194,567)	(219,882)	(190,040)
Non-current liabilities	(97,785)	(67,738)	(91,180)	(84,458)	(102,034)
Total equity	210,280	209,590	198,674	191,628	194,462
Cash and cash equivalents, end of year	(65,904)	(25,789)	(12,374)	822	3,834

Shareholder information

Shareholder and corporate information

Financial calendar

Annual General Meeting

31 May 2019

Record date for final dividend

14 June 2019

Dividend warrants posted to shareholders

4 July 2019

Interim results announced

13 August 2019

Registered office

1390 Montpellier Court
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www.mearsgroup.co.uk

Company registration number

03232863

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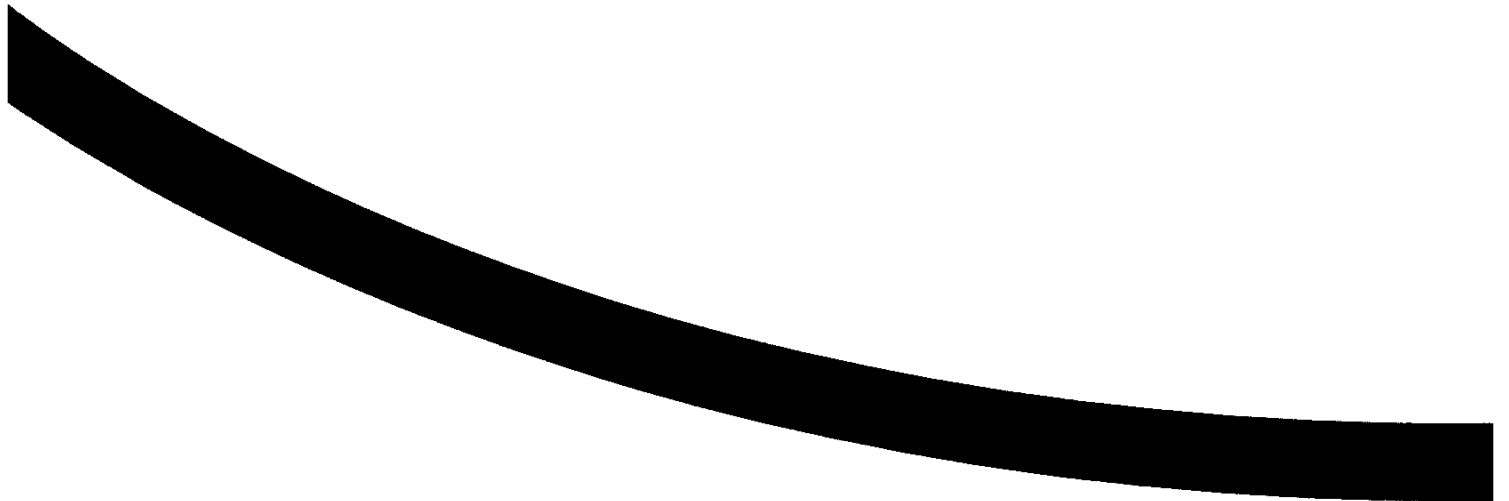
The Group operates a website which can be found at www.mearsgroup.co.uk. This site is regularly updated to provide information about the Group. In particular all of the Group's press releases and announcements can be found on the site.

Registrar

Any enquiries concerning your shareholding should be addressed to the Company's registrar. The registrar should be notified promptly of any change in a shareholder's address or other details.

Investor relations

Requests for further copies of the Annual Report and Accounts, or other investor relations enquiries, should be addressed to the registered office.



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