CAPITA

ANNUAL REPORT 2018

Contents

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Go to previous page

Go to next page

Go to previous view

Go to main contents page

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Photography

The front page photograph – and all the other images in this report – feature Capita employees, unless otherwise stated.

Cautionary statement

The Directors present the Annual Report for the year ended 31 December 2018, which includes the strategic report, governance and audited accounts for this year. Pages 1–98 of this Annual Report comprise a report of the Directors that has been drawn up and presented in accordance with English company law, and the liabilities of the Directors in connection with that report shall be subject to the limitations and restrictions provided by such law. Where the Directors' report refers to other reports or material, such as a website address, this has been done to direct the reader to other sources of Capita plc information which may be of interest. Such additional materials do not form part of this report.

Our purpose – 'we create better outcomes' – is the driving force behind the new Capita.

We want to be a truly responsible business and create better outcomes for:

Our people – by providing an environment in which they can thrive and develop.

Our clients and customers – by being focused on delighting them, both now and in the future.

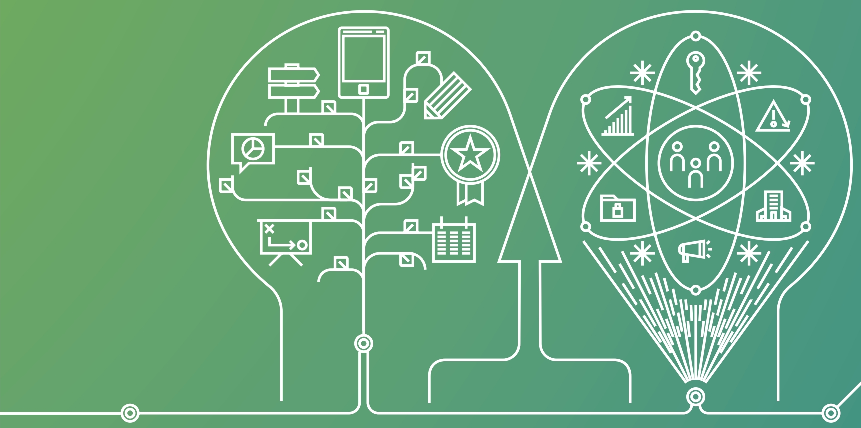
Our suppliers and partners – by treating them fairly and encouraging them to deliver.

Our investors – by delivering against targeted returns.

Society – by acting as a responsible business for the communities we serve.

To deliver our purpose successfully, our corporate values – open, ingenious, collaborative and effective – and behaviours must run through every employee conversation, every client interaction, every contract discussion and everything we do at Capita.

Our purpose should motivate and inspire all our people; it has to guide all our decisions and actions, each and every day.



"Our purpose will underpin Capita's transformation into a truly responsible and sustainable business, founded on good governance and collaboration, and committed to creating better outcomes for all stakeholders."

Jon Lewis, Chief Executive Officer

Overview

Capita at a glance

We have revised our non-statutory reporting measures to improve transparency and make it easier to understand the Group's financial performance.

The revised presentation gives adjusted and reported results, with adjusted results being equivalent to the previous underlying before significant new contracts and restructuring. Our adjusted results exclude items that have a potentially distorting effect.

Adjusted revenue
£3,867.6m
(2017: £4,091.8m)

Reported revenue
£3,918.4m
(2017: £4,234.6m)

Adjusted earnings per share
16.37p
(2017: 27.99p)

Reported earnings per share
17.99p
(2017: (48.82)p)

Adjusted profit before tax
£282.1m
(2017: £383.1m)

Reported profit before tax
£272.6m
(2017: £(513.1)m)

Adjusted free cash flow
£(82.5)m
(2017: £75.4m)

Reported free cash flow[1]
£(260.5)m
(2017: £66.6m)

Software

Revenue
£396.4m
65% public sector
35% private sector

Profit
£112.4m

Employees
4,000

People Solutions

Revenue
£498.3m
40% public sector
60% private sector

Profit
£40.7m

Employees
5,800

Customer Management

Revenue
£794.2m
2% public sector
98% private sector

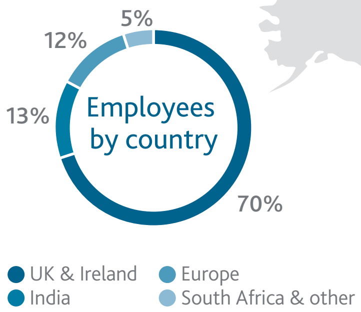
Profit
£39.6m

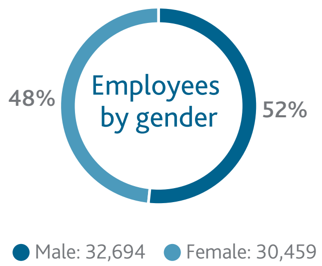
Employees
30,000

The tables above present adjusted results for 2018. The calculation of adjusted figures and our KPIs are contained in the APMs on pages 197–198.
1 The Group has represented and restated its 2017 cash flow statement. Refer to note 29 of the consolidated financial statements for details.

Employees

63,153





Our locations

Government Services

Revenue

£745.5m

100% public sector
0% private sector

Profit

£35.2m

Employees

8,700

IT & Networks

Revenue

£404.0m

52% public sector
48% private sector

Profit

£45.3m

Employees

3,400

Specialist Services

Revenue

£992.2m

21% public sector
79% private sector

Profit

£139.5m

Employees

11,000

Overview continued

How we run our business

Expertise and resources

Market expertise
Customer management, education software, learning and recruitment process management, and local and central government services

Technology and digital resources
Technology-led, digitally-enabled complex services and solutions. Increasing investment in software development and technological capabilities

Client relationships
Partnerships with wide range of clients, from blue-chip businesses to the public sector, delivering insight and developing innovative solutions

People
People-focused business, built around 63,000 skilled and committed employees who have deep understanding of our clients' markets and needs

Global infrastructure
Growing international operation and sales focus, with almost 20,000 people based outside the UK, as far afield as India and South Africa

Generating financial value

Multi-year contracts
Clients procure our services through multi-year contracts. In 2018, 87% of revenue was underpinned by long-term (greater than two years) or short-term (less than two years) contracts

Software licences and support
We provide clients with business-critical software products, earning recurring revenue from implementation, annual licence fees and support and revenue from 'software as a service' arrangements

Transactional services
More than 13% of our revenue comes from our transactional businesses where we earn fees for professional services provided to our clients across a wide range of business functions

Creating better outcomes

We are focused on creating value and better outcomes for all our stakeholders – by designing, implementing and operating essential services; developing and selling specialist software to support critical business functions; and by supporting the people and communities we serve.

Our clients and customers

By delighting them both now and in the future

Metric:
Customer net promoter score

Society

By acting as a responsible business for the communities we serve

Metric:
Community investment and charitable giving

Our people

By providing an environment in which they can thrive and develop

Metric:
Employee net promoter score

Our suppliers and partners

By treating them fairly and encouraging them to deliver

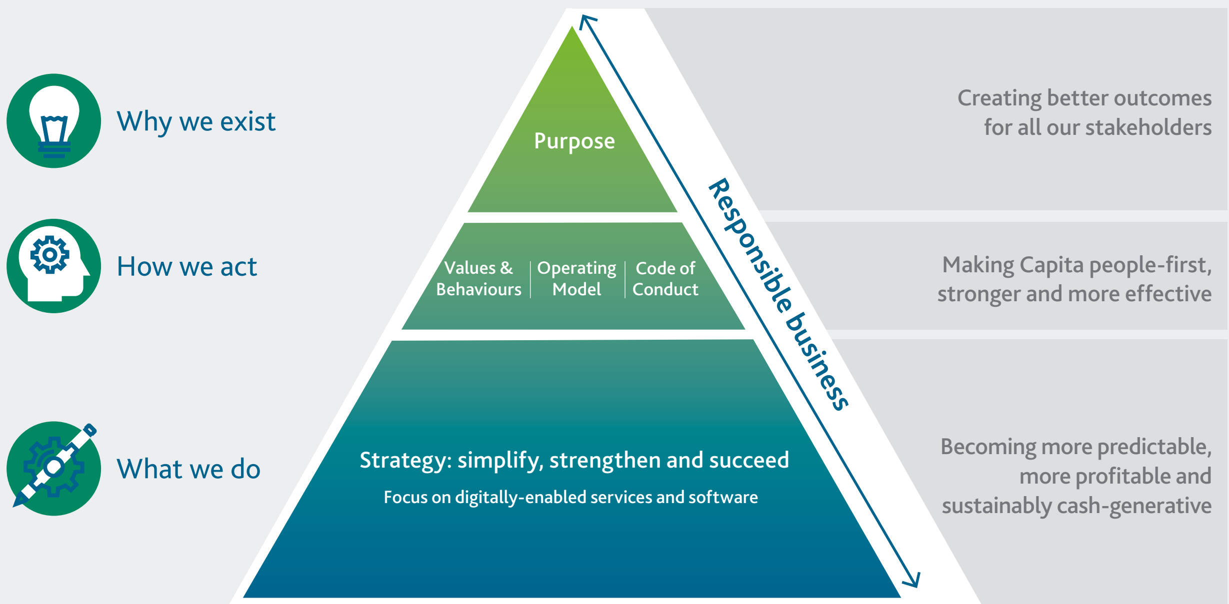
Metric:
Improved supplier payment terms

Our investors

By delivering against targeted returns

Metric:
Sustainable free cash flow

New ways of working



Chairman's introduction

It's been a significant year

"Positive steps have been taken towards the creation of a truly diverse, responsible, sustainable and digitally-enabled organisation."

Sir Ian Powell, Chairman

Every day, Capita affects the lives of millions of people, either directly or indirectly. It is a systemically important business, with an integral role as a services provider across many areas of the economy and society.

Capita is in transition as, under new leadership, our people restructure and rebuild the business. A major turnaround, affecting every aspect of the business, is being undertaken. A corporate purpose has been defined for Capita for the first time. We are working towards our stated objectives of a return to organic growth and sustainable free cash flow.

As we've previously explained, there is a long way to go to complete the Capita transformation. The Board is very conscious that shareholders have been supportive and patient – and that the actions taken and progress made are, as yet, to be evidenced in terms of financial performance.

During 2018, trading conditions and the economic and political environment in which we operate remained uncertain. At the same time, the company has had to recognise and confront a number of challenges. However, much good work has been done and, despite the challenges, real progress made. We've drawn a line under the past, simplified and strengthened, and are regaining forward momentum. I believe we can now look forward positively to what a transformed and repositioned Capita can truly become.

Progress and performance

It's been a significant year in the story of Capita, with positive steps taken towards the creation of a truly diverse, responsible, sustainable and digitally-enabled organisation.

We've made progress in a number of key areas. There is a clearly articulated strategy in place, underpinned by our newly defined purpose that 'we create better outcomes'. A rights issue, backed by healthy proceeds from a series of disposals, has helped address the debt side of the balance sheet and is already funding new investments. We have also agreed a pension deficit recovery plan, and a new operating model has been rolled out.

In terms of financial performance, Capita reported adjusted revenue of £3.9bn in 2018, a decline year-on-year, while adjusted profit before tax was slightly ahead of our expectations at £282.1m.

The Board fully supports the multi-year transformation plan and is monitoring its progress closely. We have again recommended that dividend payments will remain suspended until sufficient sustainable free cash flow is generated.

Governance and diversity

Governance at Capita has been further overhauled in the past year; and not just at Board level, as the changes have gone much wider. The whole organisation is undergoing a fundamental transformation and, as part of that, how it is governed – from the divisions and functions to individual businesses and contracts – has been reviewed and redrawn. Everyone in Capita now has a personal responsibility to help it transform as a purpose-led business.

At an executive level, several more senior managers have arrived in post to provide the company with a first-class new leadership team capable of delivering profound, professional, disciplined change. It's work in progress, but the company-wide controls being put in place will lead to a more stable and efficient Capita; they will enable the business to provide services to the benefit of clients and deliver financial results in a much more effective and predictable way.

The directors and I will continue to review the constitution of the Board; we will ensure it matches the overall purpose of Capita and its new strategic direction. We want a Board with a global perspective and diversity, and we want this reflected throughout the company; that's why the appointment of two employee directors is so significant. We are determined that the perspective of employees is represented at Board level. I'm confident it will mark us out as a forward-looking organisation and help us attract, recruit and retain employees.

As I've insisted since I joined, diversity matters at Capita, and we have made progress, but not enough. In particular, the gender pay gap across the organisation remains disappointing but we are looking at the most effective ways of addressing the problem.

The need for increased diversity is becoming recognised much more as essential across Capita and will continue to be a major focus for me and the leadership team. We are a digitally-enabled company, and require a workforce that reflects those technologies. But innovation increases with diversity of thought, so we need people with different backgrounds, experiences and voices, all given the opportunity to succeed, if the company is to have a sustainable future.

We realise that social mobility and social responsibility are crucial to our business. At Capita, we are well placed to deliver programmes that support the communities we serve. We are involved in numerous schemes, with the specific aims of improving digital education and supporting social mobility, particularly through our graduate and apprenticeship schemes, and community volunteering programmes. It is increasingly clear that encouraging social mobility is not only the right thing to do but will help our business succeed. Being a responsible business also means being open and transparent in the way we manage our operations and deliver our services. We need to be more aware of the effect we have on the communities that we serve and our role in society.

Culture and values

To really transform Capita, we have to achieve cultural and behavioural change – both internally and in all of our external interactions. All our people need to know how to make the right choices for the right reasons, take decisions in the right way and be guided by our new corporate approach, which is no longer based on short-term decisions in pursuit of near-term growth and in-year profitability.

That is why a clear set of values and behaviours has been put in place, underpinned by our purpose and supported and embedded through the new operating model. The purpose goes much further than being simply an over-arching corporate theme. Everything the company does in the years to come must relate back to this purpose in a real and practical way.

Our purpose must act as our guiding star; it's what we're working towards, but it also has to be shown in everything we do. It should challenge every person and every decision, including how and where we invest our money, to achieve better outcomes for each other, our shareholders and clients, and the communities we serve. Delivering on this purpose will enhance the long-term sustainability of the business.

Looking forward

Capita is on the way to becoming a fully transformed business; and I would like to offer my sincere thanks to Jon Lewis, his leadership team and all of our people for working so hard, with such energy and commitment, through a time of significant change.

We must make sure we deliver consistently on our contracts and commitments, and follow through with our corporate purpose. There needs to be a relentless focus on earning the respect and trust of all our stakeholders, including our fellow shareholders, to whom we remain grateful and who have been very supportive throughout the many changes and challenges of the past year.

Chief Executive Officer's review

Our transformation is on track

"Our operating model is our single biggest lever of change. It's the blueprint for how we run the company and makes the reforming Capita real for all stakeholders."

Jon Lewis, Chief Executive Officer

It's now been more than a year since I joined Capita and the company has achieved a considerable amount.

We have launched a multi-year transformation process and are rebuilding the organisation. Our mission is to become 'One Capita', an integrated and refocused business, successful and sustainable, with stronger client relationships. We want to make a positive, responsible contribution to society and be a force for good. From the financial perspective, the business will be more predictable, more profitable and sustainably cash-generative.

This has meant going back to fix the fundamentals and devising a new strategy, underpinned by a company-wide purpose and clear new operating model. We are continuing to execute our strategy – to simplify, strengthen and succeed – and have made real progress on remedying many of the basics. Over the past year, our thousands of people, in the UK and abroad, have proved very resilient. Important work has been done every day, aimed at delivering better outcomes for all stakeholders – our people, shareholders, clients, suppliers and the communities we serve.

Fixing the basics

As outlined in last year's Annual Report, Capita had become overly complex and inefficient, focused on short-term performance, characterised by a lack of long-term planning and investment, and challenged by execution issues on several major contracts.

We made a strong start in 2018 to turning the company around and are on track with the execution of our transformation plan. We started to rebuild, redefining the divisions and creating robust, accountable and centralised functions which define how we do things company-wide.

Further top-level talent has been recruited to senior leadership positions, and a clear sense established of what Capita is and should be, and of how it can succeed. We have introduced a purpose-driven and values-based culture, alongside our operating model. It provides managerial discipline and a corporate blueprint, and is designed to deliver the highest standards of service, delight clients and deliver value for all our stakeholders.

We raised, with shareholder support, £701m gross proceeds in a rights issue, and £408m from disposals; we have de-leveraged our balance sheet. We delivered on our cost-competitiveness initiatives. We agreed a pension deficit reduction plan. We have updated our payment terms for suppliers in the UK and Ireland to build better relationships with our partners.

Our corporate risk profile has stayed largely the same as in 2017. However, we are continually improving the way we manage our risks; effective risk management will be key to the successful delivery of Capita's strategic objectives.

It's a mark of good management teams that they deliver what they said they would deliver, and I'm pleased with our achievements over the past year. We are fundamentally in a much better place. At the end of year one of our three-year turnaround, we are where we expected to be and have a clear plan laid out for 2019.

Purpose and operating model

We recently unveiled Capita's purpose – 'we create better outcomes' – allied to a refreshed set of values and behaviours. For the first time, the company's true purpose has been defined. It is the single reason we exist; it directs and motivates all of us; and shapes all our decisions and actions. Capita never had this before – that is why we had to change, swing the pendulum, and provide direction and clarity.

Cultural and behavioural changes will inevitably take time to become fully integrated into the organisation. But our new purpose and re-emphasised values will be the driving forces behind Capita's transformation into a collaborative business, founded on robust governance. As a responsible business, we've refocused our approach to addressing the most material challenges that we and society face.

How Capita carries out its purpose and delivers better outcomes is now defined by our new operating model. It constitutes the blueprint for how together we run the company – underpinned by a clear strategy, an organised structure, stronger governance and controls, and well-defined accountabilities.

I believe our operating model represents the single biggest lever of change the new leadership team has introduced at Capita. It's truly self-reinforcing, joins everything together corporately, and makes the reforming Capita real for all stakeholders.

Despite being a major step forward, the operating model will also take some time to become truly embedded. I don't expect everything to happen easily. But what I do expect is for every leader and everyone in the company to start making the changes that will reform Capita as a truly purpose-led, values-driven business. This is the journey we are on together and I'm committed to seeing us get there.

Financial performance

For the full year ending 31 December 2018, Capita reported adjusted revenue[1] of £3.9bn. Revenue declined year-on-year, due to the limited benefit from contract wins being outweighed by contract losses and scope and volume changes in Government Services, Customer Management and Specialist Services, including the re-shaping of our Defence Infrastructure Organisation (DIO) contract and Home Office escorting, on which we chose not to re-bid. There was also a decline in transactional revenue in People Solutions and IT & Networks.

Adjusted profit before tax[1] of £282.1m was slightly ahead of our expectations. As expected, we had a free cash outflow in 2018, before rights issue and disposal proceeds.

Net debt was £466.1m, down from £1,117.0m in 2017, reflecting the completion of the rights issue, the receipt of the proceeds from disposals and the free cash outflow. The adjusted net debt to adjusted EBITDA ratio[1] at 31 December 2018 was 1.2 times. More details about our financial performance can be found in the Chief Financial Officer's review on pages 15–20.

Cost competitiveness

Capita has identified a significant, multi-year opportunity to reduce costs and improve operational efficiency, including:

- Reductions in general and administration, IT and property expenses.
- Centralising more of our procurement and driving value from our ~£1bn external spend with suppliers.
- Operational excellence, increasing the use of offshoring and automation, and improving the consistency of our operations.
- Adopting lean methodologies and being smarter in terms of how we work.

We made a strong start on executing these cost competitiveness initiatives in 2018, delivering in-year savings of £70m. We plan to accelerate the realisation of savings from our programmes, and now expect to realise £175m of cumulative savings from these initiatives by the end of 2019. We will invest some of these savings in building our capability to drive growth. The cost of achieving these savings was £55m in 2018 and is expected to be £95m in 2019, making a total of £150m which is included as part of the total restructuring costs.

1 Refer to alternative performance measures on pages 197–198.

Chief Executive Officer's review continued

Targeted investments

Since April, we have formed an investment review committee, chaired by me, for capital allocation. It is part of the disciplined system put in place to ensure more predictable outcomes. The committee supports our goal of investing a total of up to £500m over three years, addressing historical under-investment and, increasingly over time, facilitating organic growth.

We have subsequently approved a number of investments including:

IT systems and infrastructure

- An organisation-wide customer relationship management (CRM) system, giving a holistic view and understanding of our customers, providing robust and granular data to better predict future sales and monetise customer relationships.
- A new human resources system, to improve engagement and development opportunities for all our people.

Services and products

- Software – completing the development of the next version of SIMS (School Information Management System) for secondary schools; an education software parental engagement app; the creation of a cloud-based public safety platform for emergency services products to facilitate new sales opportunities; an initial investment in a payment facilitation solution for Pay360 and the re-platforming of our Retain resource management software to a new SaaS-based (software as a service) solution.
- People Solutions – next generation of the candidate portal; automation of our pre-employment screening system; and the development of a digital on-boarding product to complement our suite of 'hire to retire' services.
- Customer Management – a new digital, omni-channel contact platform to support webchat, automation and messaging.
- Government Services – developing business processing as a service capabilities to provide scalable, replicable services to a wider customer-base. Targeted investments in robotic process automation (RPA) and machine-learning technologies to support the execution of contracts.
- IT & Networks – modernising and strengthening our IT infrastructure; developing new products for cloud services, cybersecurity and workspace agility; automating and improving IT service desk customer experience.

The above are in addition to our ongoing investment in the upgrading of our financial system – to improve our reporting, processes and controls.

Challenging contracts

I have talked previously of three 'problem' contracts which continued to present Capita with some challenges in 2018. But we have made encouraging progress with fixing the performance of these contracts and are delivering against more of the key performance indicators. It is part of how we have introduced a more disciplined, company-wide contractual process.

First, we've completely rebuilt Capita's relationship and partnership with the British Army, and re-set our Recruiting Partnering Project (RPP) contract. We remain committed to making a success of RPP and, thanks to great work being done by our partnership, the contract is starting to show signs of improvement. The number of regular soldier recruitment applications are at a five-year high and we're working hard to reduce the amount of time it takes to join the Army. We have been open about mistakes made in the past and we know there is still a lot for us to do to deliver on our commitments. But RPP is a critical public service to the Armed Forces and we're determined to get it right.

Second, we took firm action towards the end of 2018 over issues relating to our Primary Care Support England (PCSE) contract with NHS England. This followed the discovery of delays in the issuing of cervical screening correspondence, which forms part of the PCSE contract, to thousands of women. We apologised to all the women affected by this administrative error and, following an investigation of the managerial handling of the matter, appropriate internal disciplinary action was taken. We have improved quality processes, and other operational service delivery levels on the contract continue to be stable.

Finally, the transformation of our seven-year customer services contract with mobilcom-debitel – one of Germany's largest mobile, internet services and telecoms products providers – is now progressing well. All revised transformation milestones have been met, including the launch of IOS and Android mobile customer-service apps.

Executing and delivering on our commitments to simplify, strengthen and succeed

2018 – fix, stabilise and set direction

- Rights issue completed
- Strategy in place
- Leadership and governance strengthened
- Disposals executed ahead of plan
- Pension deficit addressed
- Delivered £70m cost-out
- Operating model launched and purpose, values and behaviours defined

2019 – build momentum

- Increase investment
- Build organic growth engine and start shift to consultative selling
- Acceleration of cost competitiveness
- Accelerate offshoring and automation
- Technology and procurement
- Launch our purpose and embed operating model

2020 – deliver our targets

- More consistent and predictable
- Double digit EBIT margins
- +£175m of cost savings
- At least £200m sustainable free cash flow

The aggregate financial loss from these challenging contracts reduced from over £50m in 2017 to around £30m in 2018. We plan to generate an aggregate profit on the contracts in 2020, including reaching break even on the PCSE and mobilcom-debitel contracts by the end of 2020.

Sales and growth

Our transformation programme will continue through 2019 and, in fact, be intensified. All six Capita divisions now have clearly defined value propositions, a simpler set of offerings and, in some cases, a fresh methodology by which to create growth opportunities. While there are early signs that we can make real progress in 2019, there is still much more to do; and we must demonstrate that we can again grow organically.

Transformation of our growth function under a new Chief Growth Officer will be a crucial factor in how we will pivot to growth. We need to become more agile in our thinking, approach and skill-sets.

I have personal experience of running consulting businesses in software tech and the oil and gas industry. At Capita, we already have consulting services – providing insight and expertise in our chosen markets – but they have been run in silos and not leveraged across the business. I am convinced that a stronger consulting capability at Capita is going to remove our revenue dependency on tenders and help create new growth opportunities with existing and new clients. A stronger consulting capacity will also provide opportunities for consultative selling.

A shift to consultative selling, based on industry knowledge, will transform Capita in the sales and marketing area – and leave no-one in any doubt that what we now have instead is a modern-day growth function.

The performance assessment of our existing sales resources and the establishment of a focused customer account management structure, with well-honed consultative selling skills, is helping change how we engage with clients. We are aiming to understand our clients better and build stronger, long-term partnerships, providing the best of Capita to create better outcomes and realise growth opportunities.

This has already seen progress, including in our partnership with Transport for London (TfL). Core to this is the London congestion charge zone, low emissions zone and enforcement contract which involves service provision from five Capita divisions – Government Services (to run the contract), IT & Networks (the underlying IT infrastructure and network provision), Customer Management (customer accounts and enquiries), Software (payment platforms) and Specialist Services (document services). This contract led in turn to the opportunity to provide ultra-low emissions zone charging. More widely, we provide core network, asset, workplace and enforcement services to TfL, as well as infrastructure consultancy. It shows how we can work successfully across divisions and functions, and is a good example of getting account management right.

In 2018, we formed a new pre-bid contract review committee, which is operating well. The committee reviews all contracts above certain financial thresholds, evaluating the risks and commitments to ensure complete alignment with our operational and financial goals. We strike an appropriate balance between delighting the customer, growing operating profit and the risk profile.

Order intake in the year was £1.8bn, largely comprising contract wins and renewals in Customer Management, which won a £300m extension and expansion of our existing contract with Germany's largest integrated telecommunications provider, and in Software.

We also announced a number of new contracts, some of which were delayed from earlier in the year, which are discussed in more detail in the divisional performance section on pages 21–33.

Capita's order book at 31 December 2018 stood at £7.1bn, compared with £8.2bn at 31 December 2017, reflecting that order intake was lower than revenue recognised in the year and low levels of bid activity in 2017. The decline in our order book in 2018 was driven by two parts of the business:

- Life Insurance, which is running off and was impacted by the loss of Prudential.
- Local government, where the market has structurally changed and clients are shifting from long-term multi-activity contracts to buying processes as a service.

The order book for the rest of the business – largely digitally-enabled services and software – was stable. This part of Capita operates in growth markets and includes higher value-added services that we are investing in and want to grow. I expect to see these trends continue this year, as Life Insurance and local government continue to decline and our investment in core propositions begins to bear fruit. Capita continues to plan for a return to year-on-year organic growth in 2020, driven by digitally-enabled services and software.

Digital capabilities

Getting back onto a growth trajectory, and optimising our portfolio, are part of our multi-year transformation process, which we have clearly set out for all stakeholders. The focus of the leadership team at Capita remains firmly on delivering that transformation and prosecuting our strategy of simplify, strengthen and succeed. But we will also need to look ahead carefully to the Capita of the future, based increasingly around our digital capabilities.

The lion's share of the contracts we have today involve a deep understanding of the business processes of a client and the use of technology to provide insight, reduce risk, drive productivity and produce a superior experience for clients' customers. Digitally-enabled transformation is a common thread running through all this.

Chief Executive Officer's review continued

It's why we are investing more in digital technology and entering into strategic IT partnerships. For example, we agreed a five-year strategic partnership with Microsoft for the use of Azure, its cloud computing service, to support the roll-out of our cloud services, particularly in our Software and Customer Management businesses. This will help facilitate the roll-out of the next version of our education software SIMS8 and make it easier to internationalise the business.

We have significantly increased the capacity of our Indian digital development centre in Pune, near Mumbai, which now employs more than 1,100 people developing standardised software, alongside more than 500 colleagues there in IT & Networks. We also agreed a digital partnership with McKinsey to accelerate our analytics and digital transformation capabilities.

There are big opportunities in a fast-changing world – with digitally-based services being purchased in a much more flexible way – which Capita is well equipped to take advantage of. But we need to make sure that our tech solutions are designed and marketed to provide clients and their customers with superior experiences and better outcomes. We have to identify the nature of clients' work, and define the potential for them and us from new digital technology, data and analytics-focused solutions, based on deep industry knowledge.

Investment in our people

Capita is a people-focused business and the leadership team is committed to putting our people at the very centre of how we operate, and on respecting and valuing all of them. We are determined to instil a much stronger commitment to how we attract, develop, reward and retain our talented employees; and for them to start to really experience the positive changes taking place within the business. We want our people to feel part of the company's success, and to be excited and motivated to work hard to help achieve it.

This is why we appointed a Chief People Officer for the first time to run the new people function. We are investing in training and development, and succession and talent management, and have – for the first time at Capita – introduced a performance management and assessment system. Such moves are reflective of being a responsible business and constitute a vital part of how we will succeed.

I am disappointed that our gender pay gap increased in 2018; this is simply not good enough, but we are taking steps to understand and eventually eliminate the gap. We're investing in activity to improving gender and pay equality through our people and responsible business strategies. At the same time, I am very proud that our ranking in the Hampton-Alexander Review of the FTSE 250 has improved, up from 219 in 2017 to 110; it represents progress, though there is clearly still a lot of work to do.

As the Chairman has highlighted, we are also very serious in the leadership team about widening diversity. We want a workforce that is inclusive and reflects the diversity of our communities – as shown by the imminent appointment of two employee directors to the Board, the first such move by a FTSE 250 company since the late 1980s. But, as I have stated previously, this is not a case of gesture politics: employees on the Board does not feel radical to me; it's just the right thing for our company to do.

At a leadership level, we have further strengthened the executive committee to support the delivery of our new strategy. As well as a new Chief Growth Officer, we now also have a Chief Digital Officer; these new growth and digital roles are enormously important in underpinning our strategy. Our Chief Financial Officer joined us in January to form part of our world-class new leadership team, which also includes a Chief General Counsel and leads for the new transformation, corporate development and corporate affairs functions. We now have a mature and disciplined team running Capita in a responsible, sustainable way – with stronger controls and risk-management, and improved quality and assurance.

Global perspective

Capita is clearly not a multinational company in the conventional sense, but we do have an international dimension that I think has been underestimated in the past. While we are the UK's largest business processes outsourcing provider, we also have a growing international operation and sales focus.

Almost 20,000 of our people are based outside the UK and we have employees as far afield as the United States, Ireland, Germany, Poland, Switzerland, India and South Africa. We have myriad capabilities within our global network, with more than 8,000 employees in India and 3,000 people in Cape Town.

Indeed, our workforce in South Africa – where we've been winning new work – is set to expand over the next two years. We currently deliver services including customer service, sales, debt collection and technical support from two centres in Cape Town. South Africa represents a new and exciting services destination, offering a unique combination of talented people and commercial advantages. It also has a mature domestic market and an attractive investment climate – with strong public sector support and excellent telecoms infrastructure. South Africa is a people-centric culture; and our presence there is reflective of how we are helping facilitate social mobility.

Overall, our aim is to evolve into a digitally-enabled services, software and consulting business with an increasingly international footprint, which delivers for all its stakeholders and values all its people, whatever their roles and wherever they work.

Responsible business

The transformation of a purpose-driven Capita must be placed in the context of our becoming a truly responsible business.

I've talked about our new strategy, the sense of a refreshed culture and values, and our initiative to put two employees on the Board. The phased £176m pension deficit reduction plan, agreed with the trustees, was in line with a commitment we made in January 2018 and is an important milestone in Capita's transformation. It's a reflection of the importance we place on good corporate responsibility.

We have been working with the Cabinet Office to develop reforms on how the Government partners with the private sector to provide public services. We have welcomed the opportunity to work openly towards the development of a practical framework and approach to procurement and delivery that brings real value to all concerned.

We need to make sure we continue to focus on minimising operational issues and must ensure we are effective in engaging with our new ways of working and operating systems.

However, there is a fresh sense of a reforming Capita with a leadership team that is properly accountable to all its stakeholders, focused on fulfilling contractual obligations, meeting expectations, cultivating better relationships with clients and delighting our customers.

We've also refocused our approach to how we are responding to the most material challenges that our business and society face – youth unemployment, digital exclusion, gender equality, climate change, business governance and ethics.

We are calling our approach responsible business, as it defines how – true to our purpose – we operate, serve society, respect our people and the environment, and deliver a fair return to our investors. We have, for example, recently launched two new charity partnerships with Teach First and Young Enterprise where we aim to empower 100,000 young people to progress into the world of work. Our social credentials are outlined in more detail in the responsible business section on pages 39–43.

But we must improve in these and many other areas, if Capita is to become a genuinely accountable leader within UK plc and help set the agenda for responsible business. The country is grappling with low productivity, slowing economic growth, an ageing population and limited social mobility. Business will have to step up and be part of the solution, be it through technology, including that designed to enhance productivity, innovation, training apprentices and graduates, or by simply providing good jobs.

However, a legacy of the financial crisis is that big companies are still treated with suspicion at best, outright hostility at worst. Business won't get a seat at the table to shape these solutions unless it is trusted and takes its broader role in society seriously, approaching challenges with honesty. I want to show how and why Capita – and big business in the UK – can actually be a force for good in society, and start to change public perceptions.

The way ahead

Overall, I'm pleased with how far we have come at Capita on our transformation journey. After the first of three years, we are on track.

Looking forward, Capita has a clear plan for 2019, including embedding our first ever operating model which defines the way we work as 'One Capita', accelerating our cost-competitiveness programme and investing more in the business to support sustainable growth. These are important stepping stones as we work towards a return in 2020 to organic growth and sustainable cash generation.

Capita still faces a number of challenges; the political and economic environment and trading and market conditions clearly remain uncertain. Yet my confidence in Capita remains undimmed. We want to become a more profitable, sustainable and responsible business, creating long-term value for shareholders – and external challenges will only serve to intensify our attention on the task ahead.

As a more simplified and strengthened company, Capita will be well prepared to take advantage of the opportunities that lie before us in a fast-moving world. I am confident we will maintain our reforming momentum over the coming year – and am excited about the prospects for a successful, technology-driven, digitally-enabled Capita.

Key performance indicators

Measuring our progress

Financial key performance indicators (KPIs)

Adjusted profit before tax[1]
Aim: Achieve long-term growth in profit

£282.1m

2017: £383.1m

Adjusted operating margin[1]
Aim: Maintain adjusted operating margin

8.7%

2017: 10.9%

Adjusted earnings per share (EPS)[1]
Aim: Achieve long-term growth in EPS

16.37p

2017: 27.99p

Adjusted free cash flow[2]
Aim: Achieve sustainable, long-term free cash flow growth

£(82.5)m

2017: £75.4m

Return on capital employed (ROCE)[1]
Aim: Deliver ROCE in excess of our cost of capital

17.9%

2017: 18.4%

Gearing: adjusted net debt to adjusted EBITDA[1]
Aim: Keep ratio of adjusted net debt to adjusted EBITDA in the range of 1.0 and 2.0 times over the long term[3]

1.2x

2017: 2.2x

1 Refer to alternative performance measures on pages 197–198.
2 Refer to note 29 of the consolidated financial statements.
3 As announced on 31 January 2018, the Board's preliminary view is that the appropriate leverage for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA, before the adoption of IFRS 16.

Non-financial KPIs

SME supplier payment terms[1]
Aim: SME suppliers to be paid within 30 days

77%

2017: N/A

Employee retention %
Aim: Improve employee retention rate

72%

2017: 79%

Carbon footprint reduction
Aim: Reduce our carbon footprint annually

4%

2017: 11%

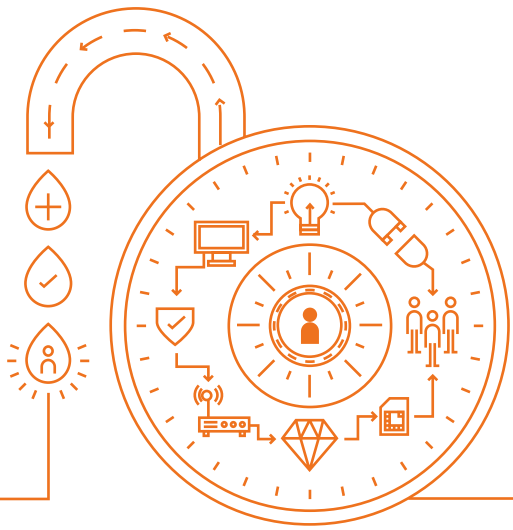
Community investment[2]
Aim: Invest and engage with our local communities to deliver programmes for local needs

£1.5m

2017: £1.9m

1 Suppliers where our annual spend is £1m or greater. SMEs include all businesses with 250 employees or less. Data includes all invoices paid through Capita companies, excluding Capita Resourcing, Capita Travel and Events and Computer Land.
2 Using the London Benchmarking Group methodology.

Note: following the launch of our new strategy and transformation plan, the current financial and non-financial key performance indicators used to measure performance will be reviewed and amended.



Chief Financial Officer's review

We are simplifying and strengthening

I joined the Board in January this year, and have spent time meeting our people, clients, suppliers, shareholders and other stakeholders to gain a better understanding of the business. What has struck me most is the importance to our clients and customers of the services we provide and the commitment of our people to creating better outcomes.

In 2018 we developed and started to deliver on the strategy – simplify, strengthen and succeed – as part of which we launched a multi-year transformation plan, started to simplify Capita and progressed work to make our cost base more competitive. We strengthened the balance sheet by raising new equity and disposing of some non-core businesses. We delivered adjusted profit[1] in line with the January 2018 trading update and remain on track with work to deliver our 2020 financial targets.

We revised our non-statutory reporting measures to improve transparency and make it easier for the readers of our Annual Report to understand the Group's financial performance. Capita is a large and complex set of businesses, has recently implemented IFRS 15, with IFRS 16 to come, and is at the end of the first year of a three-year business transformation. As a result of these factors, work will be done during 2019 to identify additional improvements to the clarity and transparency of the presentation of our financial performance, position and prospects.

As part of our plan to strengthen the balance sheet, we launched a rights issue on 23 April, which received shareholder approval on 9 May and successfully completed later that month. The rights issue raised £701m gross proceeds and £663m after expenses, with a take-up rate of 97.3%.

£408m was raised from non-core disposals in 2018, ahead of the target of £300m. This included £157m from the disposal of Supplier Assessment Services, including Constructionline, £232m from the disposal of ParkingEye, and an aggregate £19m from the disposal of a number of small businesses.

"What has struck me most is the importance to our clients and customers of the services we provide and the commitment of our people to creating better outcomes."

Patrick Butcher, Chief Financial Officer

We also strengthened Executive Committee oversight of financial reporting, including enhanced monthly performance reviews, with clearer financial and operational KPIs at business, division and business unit level, and new governance committees. These include: the Contract Review Committee, set up to review proposed new and amended customer contracts prior to making formal bids; and the Investment Review Committee to approve investment cases and budgetary release for division, function and transformation investment proposals.

1 Refer to alternative performance measures on pages 197–198.

Chief Financial Officer's review continued

Summary of financial performance

Financial highlights

	Adjusted[1] results – continuing operations			Reported results – continuing operations		
	Adjusted[1] 2018 £m	Adjusted[1] 2017 £m	Adjusted[1] YOY change %	**Reported 2018 £m**	Reported 2017 £m	Reported YOY change %
Revenue	**3,867.6**	4,091.8	(5)	**3,918.4**	4,234.6	(7)
Operating profit/(loss)	**335.3**	447.5	(25)	**34.9**	(420.1)	+(108)
Profit/(loss) before tax	**282.1**	383.1	(26)	**272.6**	(513.1)	+(153)
Earnings/(loss) per share	**16.37p**	27.99p	(42)	**17.99p**	(48.82)p	+(137)
Total dividend per share	**–p**	11.1p	(100)	**–p**	11.1p	(100)
Free cash flow[2]	**(82.5)**	75.4	(209)	**(260.5)**	66.6	(491)

1 Refer to the alternative performance measures on pages 197–198. Further details of our performance are contained in our consolidated income statement and in notes 3, 4 and 6 to the consolidated financial statements.
2 The Group has represented and restated its 2017 cash flow statement. Refer to note 29 of the consolidated financial statements for details.

Adjusted profit[1] was in line with the January 2018 trading update. Revenue declined year-on-year, due to the limited benefit from contract wins being outweighed by contract losses and scope and volume changes in a number of divisions. The decline in profit was largely due to revenue decreases from contract losses and volume and scope changes, and the non-repeat of a supplier settlement and the impact of the reshaping of the Defence Infrastructure Organisation (DIO) contract in 2017. This was partially off-set by savings achieved from the cost-out programme, along with the full-year benefit of restructuring begun in prior periods, and certain one-off items in 2018, including contract-related profits that arose on the earlier than planned terminations of contracts.

Reported profit was affected by a number of items, including the costs of the transformation plan and the amortisation and impairment of acquired intangibles and goodwill. An explanation of the major items contributing to 2018 financial performance is provided later in my report.

As expected, we had a reported free cash outflow in 2018, before rights issue and disposal proceeds. This reflects the cash outflow from the final elimination of period-end cash management activity, the continued reduction in deferred income and spend in relation to known commitments, including the Connaught settlement, the separation of Capita Asset Services (including a pension contribution), and restructuring costs and professional fees in support of the transformation plan. We also fully phased out the non-recourse trade receivables financing which was expected in 2019 and made agreed deficit reduction payments into our main defined benefit pension scheme.

Net debt at 31 December 2018 was £466.1m (2017: £1,117.0m), reflecting the completion of the rights issue, the receipt of the proceeds from disposals and the free cash outflow highlighted above. The Board's view is that the appropriate leverage ratio for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA[1] (prior to the adoption of IFRS 16). At 31 December 2018, our adjusted net debt to adjusted EBITDA[1] covenant ratio was 1.2 times (2017: 2.2 times).

Changes to non-statutory reporting

We have simplified our non-statutory reporting measures to improve understanding of the Group's financial performance. Historically, the Group separated underlying, non-underlying results (comprising business exits and specific items) and reported these on the face of the income statement. In the notes, underlying results before significant new contracts and restructuring were disclosed.

There are a number of items that influence the profit reported in any one year. These can lead to significant differences between reported profit and the generation of free cash flow, including:

- IFRS 15 and the timing of reported profits compared to the receipt of cash. Under IFRS 15, revenue is more evenly distributed over the life of contracts, with the timing of profits re-profiled. There are typically lower profits in the early years on contracts, with significant restructuring costs or higher operating costs prior to transformation, with a compensating increase in profits in later years. Typically, cash receipts are aligned to when the costs are incurred. This results in income being deferred and released as we continue to deliver against our obligation to provide services and solutions to our clients. Further reporting improvements are being considered to make the impact of this more transparent.
- Contract terminations which can lead to major gains or losses in the year of termination, and where cash inflows/outflows have occurred in prior years.
- Additional pension contributions to address pension deficits are not reflected in our adjusted[1] or reported profit, in accordance with IAS 19, but will reflect a significant future cash commitment, totalling £176m to 2021, as described below.

To provide better understanding of our financials, we will continue to provide guidance on our sustainable free cash flow targets, with disclosures where the Company has committed to future cash outflows, as was done in relation to the cash contributions to the Group's defined benefit schemes.

The revised presentation provides reported results on the face of the income statement, with a footnote detailing adjusted results, and a note to the accounts providing a reconciliation between reported and adjusted results (note 3 to the consolidated financial statements). Those items which relate to the ordinary course of the Group's operating activities remain within the adjusted results. In the Directors' judgement, a number of items need to be disclosed separately by virtue of their nature, size and/or incidence, in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business. Accordingly, our presentation of the performance of the divisions does not comment on these adjustments, as they do not impact our consideration of in-year performance. We have treated items consistently with the approach adopted at the time of the rights issue in 2018. We will be giving consideration to further improvements in 2019.

1 Refer to alternative performance measures on pages 197–198.

New organisational structure

In April, a new organisational structure was put in place at Capita, with six divisions: Software, People Solutions, Customer Management, Government Services, IT & Networks and Specialist Services. The businesses within Specialist Services are mostly stand-alone and are being managed on a portfolio basis to maximise value. These divisions are supported by a common set of Group capabilities and functions, which have been strengthened. The Group's segmental reporting has been modified to align with management's view of divisional performance, and the 2017 disclosures represented to provide comparability.

2018 financial performance

The major items contributing to 2018 performance are detailed in the following summary of financial performance.

Revenue

Adjusted revenue[1], excluding results from businesses exited in both years, was £3,867.6m (2017: £4,091.8m), an organic decline of 5%.

This was due to the limited benefit from contract wins being outweighed by contract losses and scope and volume changes in Government Services, Customer Management and Specialist Services, including the re-shaping of our DIO contract with the Ministry of Defence, and Home Office escorting, on which we chose not to re-bid. There was also a decline in transactional revenue in People Solutions and IT & Networks.

Adjusted revenue[1] year-on-year	£m
2017	4,092
Contract wins	25
Contract losses	(172)
Scope and volume changes	(61)
Transactional business	(62)
One-offs	48
Other	(2)
2018	**3,868**

Reported revenue decreased by 7% to £3,918.4m (2017: £4,234.6m).

Operating profit

Adjusted operating profit[1] decreased by 25.1% to £335.3m (2017: £447.5m), as a consequence of the revenue decline year-on-year, due to the limited benefit from contract wins being outweighed by contract losses and scope and volume changes in Government Services, Customer Management and Specialist Services, a decline in People Solutions margin, the re-shaping of the DIO contract in Government Services and a one-off supplier settlement in the prior year in IT & Networks. These were partially off-set by cost savings achieved from the transformation plan announced earlier in 2018 along with the full-year benefits of restructuring begun in prior years, and one-off contract-related profits of £6m on Prudential and £9m on Marsh that arose on the earlier than planned terminations of contracts in Specialist Services.

These contract profits arose as a result of the Group's revenue recognition policy under IFRS 15, where revenue is deferred over the expected life of a contract. Where a contract is terminated early, all deferred revenue is pulled forward and recognised in the year of termination. Similarly, any associated contract-specific assets that were being amortised over the expected life of the contract are written off in the year of termination, unless there are alternative uses on other contracts.

Adjusted operating margin[1] was 8.7% (2017: 10.9%). We continue to target double digit adjusted EBIT margins in 2020.

Adjusted operating profit[1] is before charging a number of specific items detailed further below.

The table below provides a reconciliation for 2018 and 2017 between reported and adjusted profit[1].

Reported operating profit for the year was £34.9m (2017: loss £420.1m). Further detail of the specific items charged in arriving at reported operating profit for 2018 is provided in the notes to the financial statements.

The Group's policy is to disclose significant restructuring separately so users of the financial statements can more clearly understand the financial performance of the business. As announced in 2018, the Board has launched a multi-year transformation plan to support the objectives of simplifying and strengthening Capita. The plan includes restructuring, property rationalisation, procurement centralisation, finance transformation and operational excellence. Activities are designed to improve the cost competitiveness of the Group and secure Capita's position in the markets it serves.

Adjusted[1] to reported profit bridge	Operating profit 2018 £m	Operating profit 2017 £m	Profit before tax 2018 £m	Profit before tax 2017 £m
Adjusted[1]	**335.3**	447.5	**282.1**	383.1
Amortisation and impairment of acquired intangibles	**(143.5)**	(138.3)	**(143.5)**	(138.3)
Impairment of goodwill	**(33.8)**	(551.6)	**(33.8)**	(551.6)
Impairment of other non-current assets	**–**	(63.5)	**–**	(63.5)
Impairment of Life & Pensions assets	**–**	(61.2)	**–**	(61.2)
Impairment of loans and investments	**(1.6)**	(9.0)	**(1.6)**	(9.0)
Litigation and claims	**1.8**	(30.0)	**1.8**	(30.0)
GMP and retirement age equalisation	**(5.4)**	–	**(5.4)**	–
Net finance costs	**–**	–	**(18.8)**	2.1
Contingent consideration movements (and acquisition costs in 2017)	**5.0**	0.8	**5.0**	0.8
Business exit – trading	**16.8**	16.8	**16.8**	16.7
Business exit – non-trading expenses	**(29.7)**	(13.7)	**(29.7)**	(13.7)
Business exit – (gain)/loss on disposals	**–**	–	**309.7**	(30.6)
Significant restructuring	**(110.0)**	(17.9)	**(110.0)**	(17.9)
Reported	**34.9**	(420.1)	**272.6**	(513.1)

1 Refer to alternative performance measures on pages 197–198.

Chief Financial Officer's review continued

In prior years, the Board disclosed profit before 'significant new contracts and restructuring'. This altered the previous presentation of significant restructuring. We have further simplified our reporting and now exclude significant restructuring costs from adjusted operating profit[1]. The Board recognises that this reflects a change in presentation but, given the critical nature of the multi-year transformation plan, concluded that this new presentation met the objectives of simplifying the Group's structure. The Board also considered other items that impact the reported results and the consolidated financial statements presented in note 7 to the consolidated financial statements that have a material impact on in-year performance. This policy will remain under review by the Audit and Risk Committee and the costs will be reported over the life of the plan. The costs incurred in 2018 totalled £110.0m and full details are set out in note 3 to the consolidated financial statements. An update will be provided at the next reporting period at 30 June 2019.

The impairment and amortisation of acquired intangibles, including goodwill, amounted to £177.3m (2017: £689.9m). The amortisation of acquired intangibles, and any impairment charges, are reported separately, due to the size of the annual charges and because the performance of the acquired businesses is assessed through the adjusted operating profit[1] which, for internal purposes, excludes any amounts associated with the acquired intangible assets. During the year, impairment charges were recorded in relation to businesses of £95.5m (2017: £565.6m). As noted in 'divisional performance' on pages 21–33, the local government market for large BPO contracts is declining, with a significant drop-off in the number and size of opportunities coming to market and existing clients choosing to end contracts early and take services back in-house. These events and circumstances led to the recognition of the goodwill impairment charge of £33.8m, as set out in note 15 to the consolidated financial statements.

The Board has considered the appropriate guidance and FRC thematic review on alternative performance measures and concluded that it is appropriate to exclude the above items in arriving at adjusted profit before tax[1].

Finance costs

The adjusted interest charge[1] in 2018, excluding the fair value movement on mark-to-market fixed rate swaps, was £53.2m (2017: £64.4m), reflecting the benefit from the repayment of debt following the rights issue and disposals. Interest cover was 8.2 times for the year (2017: 8.6 times).

Profit before tax

Adjusted profit before tax[1] decreased by 26% to £282.1m (2017: £383.1m). Reported profit before tax increased by 153% to £272.6m (2017: loss £513.1m). Both reported and adjusted profit[1] in 2017 were impacted by significant impairment.

Discontinued operations

The disposal of the Capita Asset Services businesses in 2017 was treated as a discontinued operation as stipulated by IFRS 5. The profit on the disposal of these businesses was £445.4m. This profit is specific to the disposed businesses and is therefore excluded from both the adjusted[1] and reported results of the continuing operations. Adjustments in 2018 to provisions related to this disposal are also disclosed as discontinued.

Taxation

The income tax charge of £27.4m on adjusted profit[1] resulted in an adjusted tax rate of 9.7% (2017: income tax charge of £65.8m and adjusted tax rate 17.2%). This is a reduction year-on-year as a result of deferred tax credits arising from a re-assessment of the recognition of deferred tax assets and true-ups of positions to filed tax returns, together with an unremitted earnings charge, as detailed further in note 10 to the consolidated financial statements. It is expected that the adjusted tax rate will return to a level closer to the UK tax rate of 19% in 2019.

The income tax credit of £0.9m on reported profit resulted in a tax rate of (0.3%) (2017: income tax credit of £14.0m and tax rate (2.7)%). The reported tax rate will generally vary from the adjusted tax rate year-on-year due to the items excluded from adjusted profit[1] in a period, for example non-taxable profits/losses on disposals or non-deductible impairment of certain acquired intangible assets.

Capita has an open and positive working relationship with HMRC, has a designated customer compliance manager, and is committed to prompt disclosure and transparency in all dealings with HMRC and overseas tax authorities. The Group does not have a complex tax structure, nor does it pursue aggressive tax avoidance activities. The Group has a low-risk rating from HMRC. The Group has operations in a number of countries outside the UK. All Capita operations in non-UK jurisdictions are trading operations and pay the appropriate local taxes on these activities. Further detail, regarding the tax strategy, can be found on the Policies and Principles area of the Capita website (capita.com/about-us/policies-and-principles).

In total, Capita contributed £164.3m (2016: £204.8m) in taxes from its UK operations in the year. This consisted of a net refund of £37.5m (2017: £12.7m) of UK corporation tax; £16.0m (2017: £21.4m) in irrecoverable VAT payments; £143.1m (2017: £155.5m) in employer NIC; and £42.7m (2017: £40.6m) in other levies including business rates, import duties, the apprenticeship levy and environmental taxes. Additionally, the Group collected and remitted to the UK Government £360.5m (2017: £409.9m) of VAT and £333.3m (2017: £367.7m) of Capita employee PAYE and NIC. Capita entities in overseas jurisdictions paid £4.6m (2017: £6.4m) of tax on local profits.

Earnings per share

Adjusted basic earnings per share[1] for continuing operations decreased by 42% to 16.37p (2017: 27.99p) as a result of the performance explained above.

The reported basic earnings per share for continuing operations was 17.99p (2017: loss 48.82p).

Dividend

The Board is not recommending the payment of a final dividend (2017: £nil). However, the Board recognises the importance of regular dividend payments to investors in forming part of their total shareholder return and will consider the payment of dividends when the Group is generating sufficient sustainable free cash flow.

1 Refer to alternative performance measures on pages 197–198.

Cash flow

Adjusted free cash flow[2] from continuing operations was an outflow of £82.5m (2017: inflow £75.4m). The Group has represented and restated its 2017 cash flow statement – refer to note 29 of the consolidated financial statements for details.

The Group's free cash flow was affected by the aforementioned decline in profit and a £372.4m working capital outflow from continuing operations. The change in working capital reflected the final elimination of period-end cash management activity, having historically optimised the working capital position at the end of reporting periods, and a £110m outflow from the phasing-out of non-recourse trade receivables financing. Deferred income declined due to limited new large contract wins, termination of contracts and a change in mix of licence sales in our Software division. Net capital expenditure on continuing operations was £139.9m in 2018 (2017: £110.2m), mainly attributable to an increase of investments in systems and infrastructure.

We continue to expect to deliver at least £200m of sustainable free cash flow in 2020, before exceptional and restructuring charges, and the pension deficit recovery payments set out below.

Reported free cash flow was an outflow of £260.5m (2017: inflow £66.6m). This reflected spend in relation to known commitments, including the Connaught settlement, the separation of Capita Asset Services, pension contributions, (which the Directors consider to be debt like in nature), restructuring costs, professional fees, contingent and deferred consideration, litigation and other items.

Net debt

Net debt at 31 December 2018 was £466.1m (2017: £1,117.0m), reflecting the completion of the rights issue and the receipt of the proceeds from the disposal of Supplier Assessment Services, including Constructionline, and ParkingEye, which were partially offset by the free cash outflow.

At 31 December 2018, the Group had £1,108.0m of private placement notes which mature over the period up to 2027. In addition, the Group has £100.0m of bank debt which matures in 2019, and an undrawn £600m revolving credit facility of which £81m matures in August 2020 and £519m in August 2021.

The Board's view is that the appropriate leverage ratio for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA[1] (prior to the adoption of IFRS 16). At 31 December 2018, the Group's adjusted net debt to adjusted EBITDA[1] covenant ratio was 1.2 times (2017: 2.2 times) and interest cover[1] was 8.2 times (2017: 8.6 times).

At each reporting date, the calculation of the Group's debt covenants is assessed, both for that period and subsequent ones. These covenants are calculated based on the adjusted[1] performance of the Group, in that they exclude exceptional items. The Group has been consistent with previous years in its treatments of these items.

Adjusted operating profit to adjusted free cash flow[2]	2018 £m	2017 £m
Adjusted operating profit[1]	**335.3**	447.5
Add back: Depreciation	59.1	56.4
Add back: Amortisation of intangible assets	27.9	15.4
Add back: Impairment of property plant and equipment	6.1	–
Adjusted EBITDA	**428.4**	519.3
Working capital:	**(372.4)**	(263.2)
Non-recourse receivables financing cleared	(110.0)	(23.6)
Full normalisation of period-end cash management	(126.3)	(85.0)
Deferred income	(243.4)	(75.2)
Accrued income	24.8	(52.2)
Other movements in working capital	82.5	(27.2)
Interest	(39.0)	(54.2)
Taxation	26.6	9.5
Capital expenditure	(139.9)	(110.2)
Provision movements and non-cash items	13.8	(25.8)
Adjusted free cash flow[2]	**(82.5)**	75.4

Adjusted to reported free cash flow	2018 £m	2017 £m
Adjusted	**(82.5)**	75.4
Pension deficit contributions	(46.9)	–
Significant restructuring	(100.8)	(45.0)
Business exits	(6.6)	19.5
Other	(23.7)	16.7
Reported	**(260.5)**	66.6

Capital management

The Group's policy is to hold cash and undrawn committed facilities at a level sufficient to fund the Group's operations and its medium-term plans. The Group holds cash and undrawn committed facilities to enable the Group to manage its liquidity risk. At 31 December 2018, the Group held cash and cash equivalents net of overdrafts of £642.7m, and had available to it a committed Revolving Credit Facility of £600m.

The Group agreed comprehensive amendments with the holders of its US private placement notes, euro fixed rate bearer notes and the Schuldschein loan to address certain issues which arose from the early adoption of IFRS 15 and the Group's strategy of disposal of certain non-core businesses. The amendments established a robust framework supporting the new corporate strategy. Further details of the terms of the amendments are set out in note 26 to the consolidated financial statements.

Note 24 to the consolidated financial statements details the Group's future minimum rental payments under its lease arrangements which highlight gross commitments of £736.0m.

1 Refer to alternative performance measures on pages 197–198.
2 Refer to note 29 of the consolidated financial statements for details.

Chief Financial Officer's review continued

Pension

In November, the Group announced that it had agreed a deficit recovery plan with the Trustees of the Capita Pension and Life Assurance Scheme (the 'Scheme').

This pension deficit recovery plan is in line with the commitment made by the Group in January 2018 to reduce the deficit over the medium term as a priority. The actuarial deficit at 31 March 2017, the date of the last triennial valuation, was £185m, before the impact of the recent High Court ruling on Guaranteed Minimum Pension equalisation.

The agreed deficit recovery plan, with payments totalling £176m, aligns with the Group's transformation plan, reflects the higher than expected proceeds the Group received in 2018 from its disposal programme, and incorporates steps to continue to lower the level of investment risk in the Scheme, benefiting the Scheme and the Group.

The expected pension deficit recovery plan payment schedule is:

2018 £m	2019 £m	2020 £m	2021 £m	Total £m
42	71	59	4	176

The current deficit is supported by an asset-backed funding arrangement of c.£70.0m, the value of which is not included in the IAS 19 deficit of £219.0m at 31 December 2018 (31 December 2017: £406.8m). Refer to note 32 to the consolidated financial statements for further detail on the arrangement. In addition, further contributions totalling £21.5m were paid in January 2018, comprising £17.0m following the disposal of Capita Asset Services, and £4.5m following closure of the Scheme in 2017 to future accrual for the majority of members of the Scheme.

IFRS 16 Leases

IFRS 16 was effective for the Group from 1 January 2019 and replaced IAS 17 Leases. The standard will have a material impact for the Group as it introduces a single lessee accounting model and requires the recognition of assets and liabilities for all leases. Rental costs currently recognised in operating profit will be replaced by depreciation of the assets and net finance costs on the liability. The total cash outflow for lease payments will not change. However the payments related to the principal liability will be presented as cash outflows from financing activities, as opposed to the current treatment as cash outflow from operating activities.

At 31 December 2018, the Group held a significant number of operating leases for which the future minimum lease payments amount to £736.0m as disclosed in note 24 to the consolidated financial statements. On adoption of IFRS 16, the expected effect on the balance sheet is the recognition of an asset in the range of £579m to £591m, a liability in the range of £640m to £650m, and an increase in retained deficit in the range of £23m to £25m. The expected effect on the income statement for 2019 is an improvement in EBITDA of £130m to £135m, an improvement in operating profit of £19m to £21m as rental payments are replaced by a lower depreciation charge, and an increase in finance costs of £28m to £30m, resulting in a reduction in profit of £8m to £10m.

The above changes are expected to increase our leverage ratio by 0.6 times. However, the impact on our adjusted net debt to adjusted EBITDA[1] covenant ratio is expected to be neutral to positive as the Group covenants are on frozen GAAP, with the exception of the US private placement notes. The US private placement notes covenant test includes the income statement impact of IFRS 16, but not the balance sheet.

Due to the Group transformation plan, which includes a consolidation of Capita's properties, the Group's lease portfolio is expected to materially change over the next few years. Any changes to the lease portfolio will be accounted for when transacted. The costs arising from the property rationalisation programme will be excluded from adjusted[1] profit in line with the current Group policy.

The Group will continue to implement and refine procedures and processes to apply the new requirements of IFRS16. As a result of this ongoing work, it is possible that there may be some changes to the adoption impact outlined above, before the 30 June 2019 results are issued. However, at this time these are not expected to be material. Further detail of IFRS 16 is provided in note 2 to the consolidated financial statements.

Financial outlook

Capita is entering the second year of a major transformation and the successful delivery of this programme is critical to the future performance of the Group. We expect adjusted net finance costs to be in the region of £40m and adjusted profit before tax to be between £265m and £295m in 2019. We expect our headline net debt to EBITDA ratio to be in the top half of our stated range of 1.0 times to 2.0 times before adoption of IFRS 16.

Our 2020 targets of £175m initial cost savings, double-digit adjusted[1] EBIT margins and at least £200m of sustainable annual free cash flow, before exceptional and restructuring charges and additional pension contributions, remain unchanged.

1 Refer to alternative performance measures on pages 197–198.

Divisional strategy and performance

Divisional structure

We report our financial performance across six operating divisions: five are focused on key growth markets; and the sixth contains a portfolio of stand-alone businesses being managed for value.

Growth platforms					Value platform
Software Specialist, high-margin enterprise products	**People Solutions** Integrated human resources market presence	**Customer Management** Transforming customer experience for our clients	**Government Services** Tech-enabled, public sector business services	**IT & Networks** Enabler for the rest of Capita – with upside from client sales	**Specialist Services** Stand-alone businesses managed for value

Central services: operational, technology, commercial, support functions

Divisional strategy

Our multi-year transformation and strategy – simplify, strengthen and succeed – are driving a change programme across our six divisions. It is focused on strengthening the underlying operating model, creating shared resources and infrastructure, optimising value from the existing portfolio, and investing in our products, services and capabilities. It aims to address underinvestment in the functions and underperformance in our divisions.

	Simplify	Strengthen	Succeed
Software	Develop a shared backbone	Invest in adjacent product offerings, pilot US market	Drive profitable growth and expand internationally
People Solutions	Leverage integrated business structure	Invest in products, platforms, partnerships and analytics	Outperform market and improve cash generation
Customer Management	Roll out best practice consistently	Invest in analytics, infrastructure and tools; expand into new sectors	Extend UK market leadership, turn around Europe margin
Government Services	Focus our portfolio on proven, scalable offerings	Build out partnerships and innovation	Deliver contracts and reliable cash flow
IT & Networks	Leverage single platform; focus on customer	Upgrade data centres, invest in cloud and SD Wan	Fix the basics and support Capita's technology ambitions
Specialist Services	16, mostly stand-alone, operating units	Managed on a portfolio basis	Delivering plan to maximise value for each

The following divisional financial performance is presented on an adjusted revenue and operating profit basis. The 2017 adjusted revenue and operating profit have been restated for the impact of businesses exited in 2018. Reported profit is not included, as the Board assesses divisional performance on adjusted results. The calculation of adjusted figures and our KPIs are contained in the APMs on pages 197–198.

Divisional strategy and performance continued

Software

Adjusted revenue	Order book
£396.4m	£559.6m
2017: £401.7m	2017: £543.4m
Adjusted operating profit	**Adjusted operating margin**
£112.4m	28.4%
2017: £111.7m	2017: 27.8%

Employees

4,000

Key regions

- UK
- US
- India
- Australasia

Key products

Education
- SIMS

Public safety
- ControlWorks

Finance & housing
- Integra

Payments
- Pay360

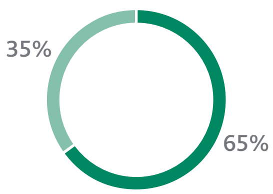
Resource planning
- Retain, Workforce Management

Utilities & transport
- FieldForce

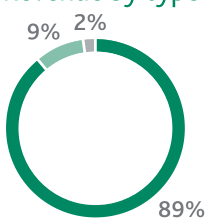
Key markets

- Education
- Local government
- Public safety
- Utilities
- Transport
- Payments
- Financial services
- Private sector

Revenue by market



Revenue by type



Capita's Software division is one of the UK's largest software companies.

Our specialist enterprise software products serve sector specific and cross-sector markets in the UK and overseas. We develop and deliver specialist application software and wider solutions for education, local government, public safety, utilities and transport, consulting and legal, and payments. As a software products provider, our deep industry expertise and functional IP supports critical public services and business processes. Our software and technology expertise forms a differentiating component of Capita's wider digitally-enabled services offering.

Revenue is generated from licence sales, maintenance and support, and implementation. Over 70% of our revenue is recurring and over 80% of licence revenue is recognised over the term of our client relationships, smoothing our revenue profile, irrespective of whether it is a perpetual licence or a 'pay as you go', software as a service (SaaS) model.

Key products

SIMS
Cloud-based MIS system for managing administrative functions in 22,000 primary, secondary and Academy schools, with optional parental engagement, payment and finance modules.

ControlWorks
The UK's leading Contact Management and Control Room solution used by Public Safety Agencies. A single fully integrated application for all Emergency and Non-Emergency contact via a range of channels including voice, web, email, SMS and social media.

Capita One Suite
Enterprise solution for managing all revenue, financial and critical business functions within local authorities, housing sector, social care and education.

Integra
A suite of financial accounting and purchasing software solutions, with the capability to integrate with further systems to provide an end-to-end ERP capability.

Affinity Suite
A powerful enterprise suite of products helping utilities, energy and infrastructure industries manage complex and evolving business challenges.

Retain
A resource planning and management solution used worldwide by professional services and legal firms, providing a consolidated view of engagements, projects or jobs to resources.

Pay360
Multi-channel payment provider providing solutions across payment, fraud, digital collections and compliance capabilities across both private and public sectors.

Strategic priorities 2018–2020:

- Accelerate investment in key products and platforms.
- Transform the software life cycle operations across all products.
- Create a software development centre of excellence for production of standardised software.
- Create scaled, integrated shared service functions.
- Create a market-aligned, high-performing sales force and marketing capability.
- Selective sales drive in UK vertical and international markets.

2018 progress against strategic priorities:

- Defined and commenced investment strategy.
- Established digital development centre in India.
- Introduced product management capability across product portfolio.
- Executed cost competitiveness and offshoring targets.
- Executed US entry strategy for selected products.
- Introduced standardised core processes across 29 businesses.

Our strategy

Our strategic priorities are focused on creating a world-class specialised software products business, investing in our core products with distinctive offerings and providing best-in-class solutions for clients in the UK and in targeted international markets.

The division is implementing the Group's strategy – simplify, strengthen and succeed – and transforming what was once a division of 29 siloed businesses into a single software business. This transformation was started in 2017 and during 2018 many of the structural and operational changes required to create a single business were put in place. We have built a best-in-class digital delivery centre in India for the production of standardised, repeatable software and to support the rest of Capita and are creating scaled, integrated, shared service functions. We are investing in both our existing and new products and markets to defend and grow the business, with the aim of achieving mid to high single digit revenue growth in 2020.

Divisional financial summary

	2018 £m	2017 £m	change %
Adjusted revenue	**396.4**	401.7	(1.3)
Adjusted operating profit	**112.4**	111.7	0.6
Adjusted operating margin	**28.4%**	27.8%	
Order book	**559.6**	543.4	3.0

Our markets and growth drivers

We are a top-five provider of enterprise software products in the UK, a market currently valued at £17bn and expected to grow at 8% CAGR through 2022 (source: Gartner). Our products compete in a wide range of market sectors, primarily in the UK, and in many sectors we have market-leading positions. We mainly compete with other specialist product software providers.

Overall market growth is being driven by software's deepening role in every aspect of business and consumer life. The drive for automation and demand for apps to engage with end-users is set to continue in a digital-first world. In response to slower growth in our more mature markets – particularly in education and secure software – we are focusing on cross-selling opportunities in existing and adjacent markets and strategic expansion into new markets. In response to shrinking education budgets and increasing demand for access to cloud services, we are expanding our offering to schools of complimentary cloud products such as SIMS Pay and SIMS Finance. The payments market is consolidating and growth in e-commerce is driving this demand. The growth of cloud solutions has increased the accessibility of our products and allowed us to offer alternative commercial models for our customers to suit their requirements.

Financial performance

Adjusted revenue fell by 1.3%, reflecting good growth in AMT-Sybex and growth in our cross-sector products, including Payments, which was offset by declines in Healthcare Decisions, as a result of the end of our NHS24 Scotland contract, and Secure Solutions. Education Software was flat. Our book-to-bill ratio was 104%, reflecting an encouraging improvement in order intake, and we expect revenue to grow in 2019.

Adjusted operating profit increased by 1%, due to the aforementioned changes in revenue, investments in sales, including the US pilot, and benefits from transformation actions.

Sales and operational performance

Over the course of 2018 we have been increasing our focus on sales and standardising our sales processes and demand generation marketing, which is resulting in a stronger qualified pipeline.

There were a number of notable wins in the year. In partnership with Motorola Solutions, we were awarded a contract to supply our ControlWorks solution to a major metropolitan police service in Asia. We were also awarded a contract to provide ControlWorks to West Midlands Police, worth £6m over 10 years, and renewed our contract to provide support and maintenance to the Ministry of Justice for digital radio networks across the prison estate in England and Wales for the next five years. Pay360, our payment platform, won a significant contract with Luxon Payments, to support its global e-wallet launch. SIMS won a contract with City Montessori School (CMS) in India, the world's largest private school with more than 56,000 pupils.

We piloted the next cloud-based version of our main education software product SIMS8, launched SIMS Finance, a cloud-based financial reporting product and started development of a 'light-touch' smartphone-enabled version of SIMS for emerging markets. We also set up a marketing and sales operation in the US to roll out selected products, including AMTSybex, Retain, Pay360 and 911eye, and consolidated multiple support desks into an integrated shared service.

The increasing focus on application development offshoring led us to build a strong development skill base in India at a lower cost base, with particular focus on key technologies such as cloud and digital transformation. This will enable us to fully support our multi-year product development cycles, critical to supporting our future sales pipeline.

Divisional strategy and performance continued

People Solutions

Adjusted revenue
£498.3m
2017: £520.5m

Order book
£715.3m
2017: £786.5m

Adjusted operating profit
£40.7m
2017: £62.7m

Adjusted operating margin
8.2%
2017: 12.0%

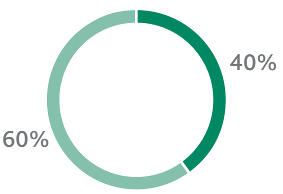
Employees
5,800

Key regions
- UK
- US
- India
- Europe

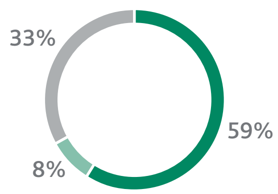
Key services and contracts
- Screening
- Recruitment
- HR services
- Learning services
- Corporate benefits
- Pension administration
- Army recruitment

Key markets
- Financial services
- Central government
- Local government
- Technology
- Utilities
- Defence
- Education

Revenue by market



Revenue by type



People Solutions provides a full suite of HR offerings across the employment life cycle.

They include leading market positions in recruitment process outsourcing (RPO), learning process outsourcing, HR service (including payroll), and pensions and benefits administration, which are supported by our proprietary digital platforms, Orbit, Hartlink and Tessello.

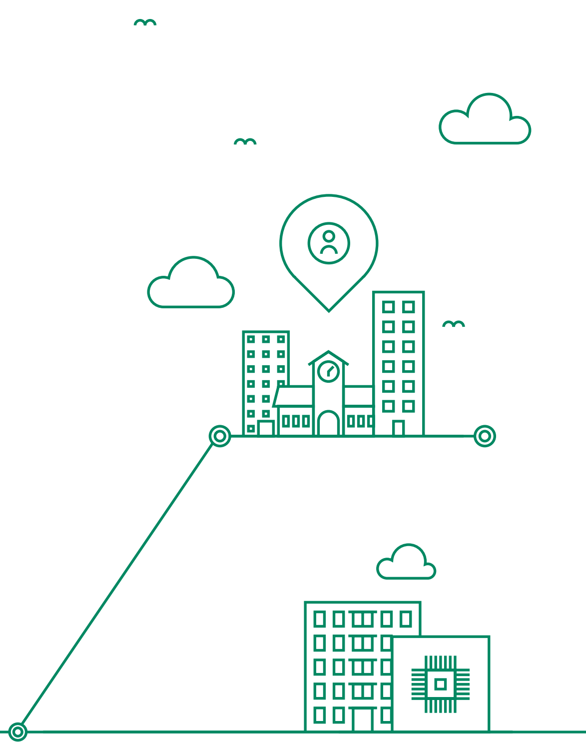
We also provide attraction, screening and performance management services, and best-in-class fire prevention and protection training facilities from the Fire Service College.

Our strategy

In April 2018, we brought our existing HR businesses together under a single leadership team for the first time, to create the People Solutions division.

Our strategy is to derive benefits from the new structure, by creating and leveraging a single sales engine and realising cost savings.

We are investing in our core products and platforms, developing a suite of new products and solutions, strengthening our analytics capability and growing our scalable, repeatable solution.



Strategic priorities 2018–2020:

- Integrate multiple HR businesses into a single end-to-end HR services business.
- Upgrade core products and technology platforms across key client services.
- Develop an enhanced external and cross-divisional sales function and culture.
- Invest in value-add advisory and analytics services to enhance core HR offering.
- Build on and replicate existing solutions to achieve scale.

2018 progress against strategic priorities:

- Creation of a new division with new leadership team and operating model.
- Investments in people and process to address specific operational under performance.
- Investments made in sales, technology platforms and digital.
- Met cost-out targets.
- Identified additional opportunities for automation and offshoring.
- Cultural change programme aligned with Capita-wide, refreshed values and behaviours.

Divisional financial summary

	2018 £m	2017 £m	change %
Adjusted revenue	**498.3**	520.5	(4.3)
Adjusted operating profit	**40.7**	62.7	(35.1)
Adjusted operating margin	**8.2%**	12.0%	
Order book	**715.3**	786.5	(9.1)

Our markets and growth drivers

The UK market for people services was valued at £6bn in 2018 and is expected to grow at an annual growth rate of 5% through to 2022 (source: Nelson Hall). Capita is a leading provider in most segments, including benefits administration where we have an 8% market share, learning process outsourcing with 21% market share and recruitment process outsourcing with 12% market share. The market is being driven by a customer propensity to buy digital self-service, a move away from large-scale contracts to modular product buying, where customers require expert advisory support as they transition to digitally-enabled operating models. In the learning market there is a shift away from traditional classroom training to online personalised and informal development, and the market is experiencing consolidation. Players with digital platforms and access to data and analytics are likely to innovate and win market share.

Financial performance

Adjusted revenue fell by 4.3% as a result of declines in our transactional businesses Capita Resourcing and Learning Services, which were impacted by the transition to a new public sector training framework, previously Civil Service Learning, and the transfer of the Contingent Labour One (CL1) public sector resourcing contract to a new provider in the second half.

Adjusted operating profit decreased, reflecting the above decline in revenue, investment to strengthen the business and lower margins in Employee Solutions, which have yet to be offset by cost reduction actions.

Sales and operational performance

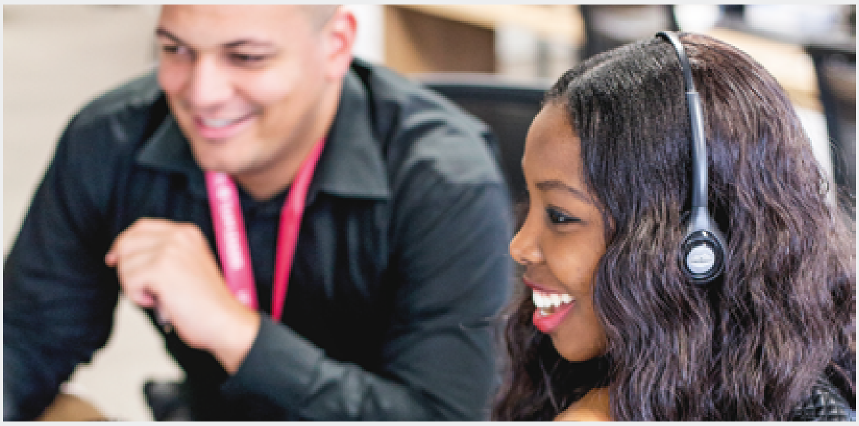
Our forward order book was £715m at year-end. We signed a number of new contracts in the year, including the provision of resourcing services for the Home Office and German energy company Innogy, the management of apprenticeships for the Department of Work and Pensions and provision of learnings services for Vodafone. We also extended our learning services contract with a major retail bank.

We started investments in: the development of a digital onboarding product to complement our suite of 'hire to retire' services; the next generation of the Orbit benefits platform, onto which a number of clients were migrated; our KnowledgePool learning booking system; and the candidate portal of our pre-employment screening system to improve customer experience.

We have re-set our partnership with the Army on the Recruiting Partnering Project (RPP) at a senior level and the contract is starting to show signs of improvement. The number of regular soldier recruitment applications were at a five-year high at the time of writing this Annual Report and we're working hard to reduce the amount of time it takes to be offered a job in the Army. The contract aims and performance were the subject of an National Audit Office report in December 2018, the findings of which related to what are now largely historical contract issues, and we attended a Public Accounts Committee with the Army in January 2019. We have been open about mistakes made in the past and we know there is still a lot for us to do to deliver on our commitments.

Divisional strategy and performance continued

Customer Management



Adjusted revenue	Order book
£794.2m	£2,011.8m
2017: £828.9m	2017: £1,843.6m

Adjusted operating profit	Adjusted operating margin
£39.6m	5.0%
2017: £57.8m	2017: 7.0%

Employees

30,000

Countries of operation

- UK
- Germany
- Switzerland
- South Africa
- India
- Poland
- Argentina
- Bulgaria

Key services and contracts

Services

- Customer experience enhancement
- Revenue generation
- Escalated case/ complaints management
- Digital transformation.

Contracts

- O2
- TV Licensing
- British Gas
- npower

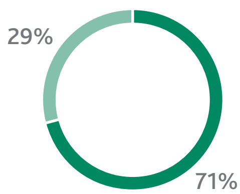
Key markets

- Retail
- Telecoms and media
- Utilities
- Automotive
- Financial services
- Travel and leisure

Revenue by market

- Private sector
- Public sector

Revenue by type



- Long-term contractual
- Short-term contractual

Capita is a leading provider of multi-channel customer engagement services, underpinned by full-service business management capabilities, in the UK, Switzerland and Germany.

We primarily serve customers in the telecommunications, retail and utility sectors, from a mix of onshore locations in Europe and offshore locations in India, Poland, South Africa, Argentina and Bulgaria.

The division also provides remediation, complaints management and collections services, including TV Licensing.
Our approach is to build shared outcome partnerships, increasingly based on partnering for value, not transactional supply. The value we bring to our clients is increasingly built around transforming the customer experience through the application of data insight and analytics. These enable us to manage complex, high-value interactions, drive positive quality improvement, and improve financial benefits for clients.

Our strategy

We have a differentiated strategy and core-value proposition in our markets; our approach is customer experience-led, tech-enabled and underpinned by contracted commitment to business outcomes. We are building capability to underpin our core value proposition that we 'make great customer experience happen'. Our commercial model increasingly includes a commitment to client outcomes such as improvements in the net promoter score, revenue generation, customer acquisition and cost-to-serve, deploying a range of operational, technology and process capabilities from within both Customer Management and the wider Capita group. This commitment to outcomes and 'making great experience happen' is core to our differentiation in the marketplaces in which we operate. Our operational scale allows us to derive meaningful insight from our customer interaction data, driving business improvement across our operations. Consequently, we are able to build longer-term, more strategic partnerships, with richer solutions.

Strategic priorities 2018–2020:

- Invest in our infrastructure to ensure consistent, high-quality service delivery, including facilities, core technology and tools.
- Build new digital platforms to support all channels and customer on behalf of clients.
- Build enhanced data and analytical platforms and capabilities to enable the business to drive insights from customer interactions into our client engagements.
- Implement a stronger operating framework to standardise our operational routines and transfer best practice across our operations, both on and offshore.
- Invest in improved consultative selling capability to increase origination, pipeline and order book.
- To standardise best practice, improve our infrastructure, invest in people, increase our use of technology and offshoring.
- Diversify and accelerate growth in some of our secondary sectors, notably financial services and travel and leisure.

2018 progress against strategic priorities:

- Investment in sales resource to drive origination and consultative selling, reflected in order book growth in 2018.
- Pilots built for both omni-channel and new automation technologies, ahead of full production in 2019, underpinning our differentiated customer experience approach.
- Customer Experience Improvement methodology proposition embedded and rolled out to first tranche of clients.

Divisional financial summary

	2018 £m	2017 £m	change %
Adjusted revenue	**794.2**	828.9	(4.2)
Adjusted operating profit	**39.6**	57.8	(31.5)
Adjusted operating margin	**5.0%**	7.0%	
Order book	**2,011.8**	1,843.6	9.1

Our market and growth drivers

We are the largest provider of customer management services in the UK with a 14% market share. The UK market is estimated to be worth £4bn a year and is expected to grow at approximately 4% per annum through 2022 (source: Nelson Hall). The German and Swiss customer management markets are estimated to be valued at £4bn per annum and are expected to grow at around 5% per annum through to 2022.

In both the UK and Europe, Capita competes with a range of local and global players for transactional contracts, typically priced on a price per FTE hour basis, and a smaller number of strategic players for outcome-based contracts. In Germany, the market has consolidated following a period of low growth and pricing pressure. Clients are seeking partnerships which are characterised less by FTE numbers and more by a range of value-adding services: revenue generation, complaints management, digital channels and data/insight. This increasingly complex service offering provides opportunities for players with deeper outsourcing capabilities. Customer experience is getting wide organisational attention from our clients, as they seek more sustainable models for attracting and retaining customers and driving revenue growth.

Financial performance

Adjusted revenue fell by 4.2%, due to contract scope changes and lower volume in the UK retail and energy sectors and Switzerland. Adjusted operating profit decreased due to: the aforementioned decline in revenue; a weaker performance in Europe, which was impacted by lower profits in Switzerland, and a slightly higher loss on our contract with mobilcom-debitel; increases in some cost items including the adoption of General Data Protection Regulation; and the dropping-out of a one-off contract modification benefit in 2017. Excluded from 2018 adjusted profit is a charge of £61.7m from the impairment of acquired intangibles (refer to note 3 of the consolidated financial statements).

Sales and operational performance

Our order book increased by 10% to £2.0bn in 2018, due to the extension and expansion of existing contracts and signing of new contracts to deliver high-quality services for a number of leading clients, including:

- The extension and expansion of our existing contract with Germany's largest integrated telecommunications provider, taking over the operation of three contact centres and 640 employees. This contract is estimated to be worth £300m (€340m) to Capita to December 2022.
- British Airways selected us to deliver a new five-year contract to deliver enhanced customer services from our global centre in Cape Town, South Africa.
- Expanded contract with Southern Water for end-to-end customer services – including the management of back-office billing processes, correspondence-handling, print and mail – worth £30m over five years.
- Expanded contract with the Financial Services Compensation Scheme (FSCS) – to consolidate all its claims handling services, including all inbound and outbound customer contact – worth £37m over four years and nine months.
- Extensions of our contracts with: npower, worth £41m over three years; Marks & Spencer, worth £70m over five years; and BBC Audience Services for five years.

The transformation of our seven-year customer services contract with mobilcom-debitel – one of Germany's largest mobile, internet services and telecoms products providers – is now progressing well. During 2018, the investment of management time has improved contract performance, and we delivered all transformation milestones on time. This included the roll-out of a new multi-channel telephony platform and the launch of IOS and Android mobile apps. We continue to plan to reach break even on the mobilcom-debitel contract by the end of 2020.

Divisional strategy and performance continued

Government Services

Adjusted revenue
£745.5m
2017: £861.7m

Order book
£2,187.5m
2017: £2,660.6m

Adjusted operating profit
£35.2m
2017: £78.7m

Adjusted operating margin
4.7%
2017: 9.1%

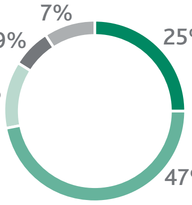
Employees
8,700

Key regions
- UK
- India

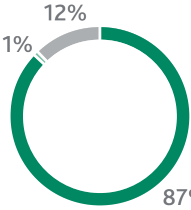
Key services and contracts
- Local government business process management and transactional services
- DWP PIP
- DCC Smart Metering
- Electronic Monitoring
- Primary Care Support England
- TfL Congestion Charging and ULEZ
- STA
- Gas Safe Register

Key markets
- Local government
- Central government
- Defence
- Education and health

Revenue by market



Revenue by type



Capita is a trusted strategic partner to central government for the delivery and transformation of technology-enabled business services.

It includes the operation of large, complex contracts that underpin the achievement of policy outcomes.

We are also a leading provider of support services such as revenues, benefits and back-office processing, IT, HR, and finance to local authorities, and education and health organisations.

Our strategy

Our strategy is to focus on and leverage areas where Capita has core expertise, invest in our transformation, technology and operational capabilities, package more of our services making them simpler to procure, improve the performance of challenging contracts, and implement structured client account management. We are also discontinuing smaller non-core activities such as facilities management and focusing on core areas of collections and disbursement, regulatory and planning services, and customer and digital services. Since April, we have begun a programme to drive operational excellence and put in place continuous improvement plans for all businesses.

Key contracts[1]

Personal Independence Payments (PIP)
Administration of personal independence payments in two regions in England and Northern Ireland

Primary Care Support England (PCSE)
Support services for GPs, pharmacies, opticians and dental practices

Home Office Electronic Monitoring
Administration of tagging for offenders

Transport for London
Administration of Congestion Charge and Ultra Low Emissions Zone

DCC Smart Metering
Management, implementation and development of the national smart metering infrastructure

Birmingham City Council
IT and digital services

Staffordshire County Council (Entrust)
Provisions of support services to schools

London Borough of Barnet
Customer services, finance, HR and property strategic partnership

1 Contracts over 1% of 2018 annual revenue.

Strategic priorities 2018–2020:

- Develop existing core service capabilities as repeatable product propositions to drive growth.
- Continuous programme of operational excellence to improve service delivery.
- Transformation of local government business away from a traditional outsourced contract model to business process as a service (BPaaS) where clients pay for services as they consume and are not tied into lengthy contract commitments.

2018 progress against strategic priorities:

- Local government strategy reviewed and reset to address accelerated market and contract decline.
- Commenced local government transformation programme to change service model.
- Investment in establishing delivery excellence partnership relationships with key government departments.
- Focused resources on securing re-bids with targeted accounts.
- Delivered cost-out targets.

Our market and growth drivers

Capita is one of the largest providers to government in the UK with an estimated market share of 13%. The UK market for central and local government services is valued at £6.7bn a year and estimated to be growing at approximately 3% per annum (source: Nelson Hall). However the local government market for large outsourced contracts is declining with a significant drop-off in the number and size of opportunities coming to market and existing clients choosing to end contracts early and take services back in-house. This accelerated decline is being driven by fiscal pressures, the expectation that this will provide a more flexible cost and delivery model but also an ideological shift away from outsourcing by some council leaderships. This structural decline has proved challenging for the division in the year, and a greater focus has been put on redefining and simplifying our core capabilities alongside managing the declining contracts.

Brexit is still affecting the volume of new policy initiatives by Government departments, resulting in fewer new opportunities for private sector contractors. Following the collapse of Carillion, 2018 was a challenging year for the outsourcing sector, but engagement by Capita with the Cabinet Office has increased and improved as it embarked on a review of contracting. After consultation across the sector, the Government has pledged to take on a greater share of the risk on outsourced public sector contracts, as part of a new set of rules drawn up in February 2019 to improve stability in the sector.

Despite these challenges, Government departments are still actively engaging with the private sector and continue to renew existing contacts and award new work.

Divisional financial summary

	2018 £m	2017 £m	change %
Adjusted revenue	**745.5**	861.7	(13.5)
Adjusted operating profit	**35.2**	78.7	(55.3)
Adjusted operating margin	**4.7%**	9.1%	
Order book	**2,187.5**	2,660.6	(17.8)

Financial performance

Adjusted revenue fell by 13.5%, due to the re-shaping of our Defence Infrastructure Organisation (DIO) contract, which benefited from the recognition of previously deferred income in the prior year, and a decline in our local government long-term strategic partnerships, reflecting the aforementioned market weakness. Adjusted operating profit decreased due to the dropping-out of the £22m one-off benefit from DIO, as previously disclosed, and weakness in local government, which were partially offset by a reduction in loss on Primary Care Support England (PCSE). Excluded from 2018 adjusted profit is a charge of £33.8m from the impairment of goodwill (refer to note 15 of the consolidated financial statements).

Sales and operational performance

Despite the difficulties faced by the company in the early part of 2018, we remain a strategic partner to the Cabinet Office.

We won, renewed and extended a number of contracts in 2018, including:

- Department for Education's Standards and Testing Agency – new contract to manage the administration, processing and support for all primary school national curriculum assessment tests in England.
- Transport for London – implementation and management of the Central London Ultra Low Emission Zone.
- Renewed contracts with Westminster City Council to manage the authority's revenues and benefits services, and the Health and Safety Executive to continue to manage the Gas Safe Register.

In 2018 Capita's subsidiary, SmartDCC, went live with its GB-wide infrastructure for the rollout of second-generation smart meters. Alongside this service, SmartDCC is delivering key programmes of work for the government and energy industry to integrate first-generation smart meters into its network and deliver next-day consumer switching in the energy retail market.

We took firm action towards the end of 2018 over issues relating to our PCSE contract with NHS England. This followed the discovery of delays in the issuing of cervical screening correspondence, which forms part of PCSE, to thousands of women. We apologised to all the women affected by this administrative error and, following an investigation of the managerial handling of the matter, appropriate internal disciplinary action was taken. We have improved quality processes and other operational service delivery levels on the contract continue to be stable. We continue to expect the PCSE contract to reach break even by the end of 2020.

The local government market for large, multi-year deals, declined at an accelerated rate during the year. Southampton, Sheffield and Birmingham City Councils have notified us of their intention to end contracts with them ahead of their contracted end-dates. Barnet Council has agreed to take a small number of services back in-house.

Capita is committed to the local government market and is working closely with all our council partners to agree and manage a smooth transfer of services back to local authority management.

Divisional strategy and performance continued

IT & Networks

Adjusted revenue
£404.0m
2017: £415.4m

Order book
£380.4m
2017: £508.3m

Adjusted operating profit
£45.3m
2017: £62.0m

Adjusted operating margin
11.2%
2017: 14.9%

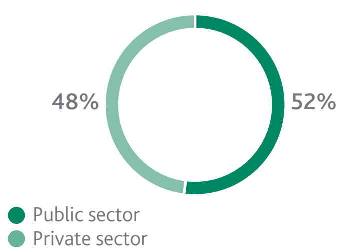
Employees
3,400

Key regions
- UK
- India
- Poland

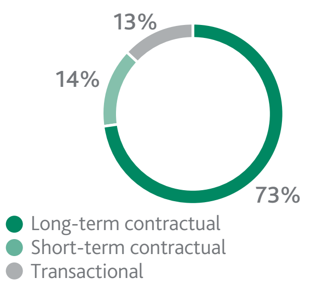
Key services
- Managed networks
- Data centre and cloud infrastructure
- Managed IT support
- Testing
- Cybersecurity and consulting

Key markets
- Local government
- Central government
- Defence
- Education
- Financial services
- Telecoms
- Aerospace
- Transport

Revenue by market



Revenue by type



Capita is one of the top 10 suppliers of IT Services and networks in the UK, focused on the mid-sized market.

Our IT services business acts as a technology enabler across all of Capita's services both internally and externally. We provide end-to-end enterprise IT services and solutions focused around four key areas: digital transformation and innovation; core platforms – cloud, hosted and on-premise and services; LAN and WAN connectivity solutions; and professional services – advising and running IT solutions for our customers, testing, data consulting and cybersecurity.

We operate across the UK and from our operations in India, supporting clients at a local and national level. We have strategic partnerships with leading global IT vendors, have invested in our own portfolio of hosted platforms and operate our own UK-wide network and data centres.

Our strategy

Our strategy is to consolidate separately run entities into single IT & Networks businesses. We will: simplify the service catalogue and professionalise internal relationships; invest in our infrastructure, cloud and people; and build technical and sales capabilities to improve customer experience.

In 2018, we launched the 'One ITS' programme, which is expected to realise significant cost savings over the next three years and includes the introduction of shared service centres with common processes and an increase in the use of offshoring.

We also started a programme to invest in our data centre network to simplify and consolidate the existing environment and improve performance and consistency.

Strategic priorities 2018–2020:

- Consolidation of multiple stand-alone IT business into a single of integrated IT & Networks business.
- Upgrade and consolidation of data centres to create an enhanced resilient and secure client infrastructure.
- Invest in key client propositions across networks, cloud, cyber and digital.
- Develop our people.

2018 progress against strategic priorities:

- Improved our conduct and control environment.
- Upgraded our legacy IT infrastructure (data centres) and technical capabilities.
- Achieved cost competitiveness targets.
- Revamped our brand and client value proposition.
- Improved our services, internal relationships and customer experience.
- Simplified our organisation and our service/product offering.

Divisional financial summary

	2018 £m	2017 £m	change %
Adjusted revenue	**404.0**	415.4	(2.7)
Adjusted operating profit	**45.3**	62.0	(26.9)
Adjusted operating margin	**11.2%**	14.9%	
Order book	**380.4**	508.3	(25.2)

Our markets and growth drivers

The IT infrastructure services market in the UK was estimated to be worth £28bn in 2018. The overall market is expected to grow at 2% a year to 2021 (source: TechMarketView). However, this is highly polarised with high growth in cloud services and shrinking client device support.

While the market is large and growing, it is also changing, providing both opportunities and threats to our current business.

In IT services, the demand for customer value creation is driving digitisation and automation across the sector. Large, fully managed legacy service contracts are being replaced by a 'pick and mix' service model driving a need for a standardised offering with modular add-ons. In Networks, the global shift to digital comes with enormous data, security and network resource requirements. New product areas, such as SD-Wan, are opening up new market opportunities for smaller players to compete with the large telcos.

Financial performance

Adjusted revenue fell by 2.7%, due to contract losses and lower volume in Managed IT Solutions and Enterprise Services. Adjusted operating profit decreased due to the dropping-out of a £9m one-off supplier settlement in the prior year and lower margins in Networking Solutions.

Sales and operational performance

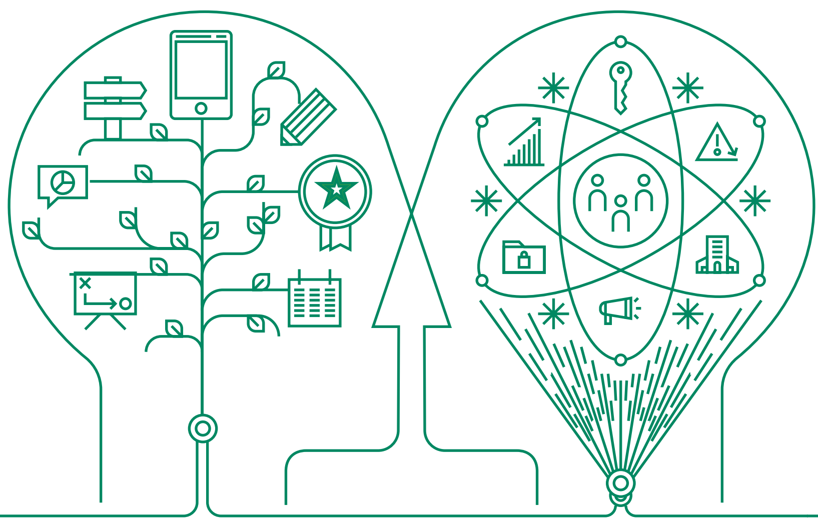
2018 was a year of fixing the basics across the division, bringing together the separate operating businesses and stabilising them. This 'One ITS' programme is expected to realise significant cost savings over three years and includes the introduction of shared service centres with common processes and an increase in the use of offshoring.

Following an IT data centre outage in 2017, we have invested significantly in our existing data centre estate to simplify and consolidate the environment and improve performance and consistency. Plans are progressing for the phasing of legacy clients onto a new cloud infrastructure.

We began work on simplifying our product and service portfolio into six key product lines to position the division for improved client retention and growth. As part of this review, we retired a number of legacy brands and brought all our services together under the Capita brand. In November, a new divisional sales and marketing organisation was created, with additional resource focused on product cross-sell and key account management.

We began the implementation of the Transport for London networks contract in March and successfully went live in late August. Transformation of the network is ongoing and is due to be completed by the end of 2020.

Contract wins and renewals in the year included the NHS Business Services Authority, Ministry of Defence, Kent Public Service Network, North Essex Partnership, Driver and Vehicle Standards Agency, and Transport for London.



Divisional strategy and performance continued

Specialist Services

Adjusted revenue
£992.2m
2017: £1,022.7m

Order book
£1,241.4m
2017: £1,844.8m

Adjusted operating profit
£139.5m
2017: £140.6m

Adjusted operating margin
14.1%
2017: 13.7%

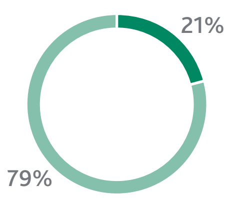
Employees
11,000

Key regions
- UK
- Dubai
- India
- Poland

Key services and businesses
- Life & pensions administration
- Insurance services
- Mortgage processing
- Travel & events
- Enforcement
- Legal services
- Real estate and infrastructure
- AXELOS
- Fera
- Managed print
- Translation & interpreting
- Hardware re-selling

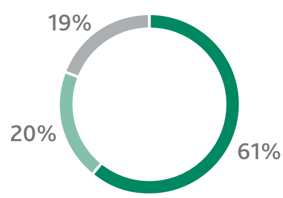
Key markets
- Financial services
- Central and local government
- Education
- Defence
- Housing
- Healthcare
- Technology
- Utilities
- Environment and transport

Revenue by market



- Public sector
- Private sector

Revenue by type



- Long-term contractual
- Short-term contractual
- Transactional

Our Specialist Services division comprises a portfolio of 16 businesses, delivering a range of services offerings through joint ventures, trading businesses and traditional IT-enabled legacy BPO contracts.

The division includes those businesses which either are not within Capita's growth markets and/or have little in common with our other divisions and/or are at an early phase in their development but may be scaled up in the future. These businesses are mostly stand-alone operations and are actively managed on a portfolio basis in order to maximise value and include Life Insurance, Insurance Services, Mortgage Services & Collections, Optima, Travel & Events, Evolvi, Real Estate & Infrastructure, AXELOS, Fera, Managed Print, Hardware Reselling and Enforcement.

Our strategy

Due to the varied nature of the activities in the division, each business has its own strategy uniquely tailored to their service offerings and the needs of their clients which has been defined through a 'value optimisation' programme.

This programme, which involved a detailed review of each business and its market position, identified strategic and tactical opportunities to improve value generation from them.

We enjoy strong market positions in many of the verticals sectors, with strong brands and positive client perception of our services. This provides an ongoing opportunity to leverage Capita's wider client base better, and to simplify and strengthen the portfolio. The focus across the portfolio is on operational excellence, cost-optimisation and leveraging Capita-wide infrastructure, clients and capabilities where possible.

Strategic priorities 2018–2020:

- Manage as a portfolio and focus on continuing 'value optimisation'.
- Rationalise service lines, processes, properties and IT.
- Leverage cross-sell opportunities across portfolio and wider Capita.

2018 progress against strategic priorities:

- Restructured a number of businesses and closed unprofitable service lines.
- Introduced tightly managed investment process and governance.
- Delivered cost competitiveness targets in 2018.
- Investment in a number of product/service enhancements.

Our markets and growth drivers

Specialist Services includes a range of businesses serving public and private clients across multiple vertical sectors, which are generally mature. Our closed book Life Insurance administration business is in structural decline as books run off and some customers, with legacy IT systems, are switching to suppliers who can provide a single digital platform for all their life books.

Divisional financial summary

	2018 £m	2017 £m	change %
Adjusted revenue	**992.2**	1,022.7	(3.0)
Adjusted operating profit	**139.5**	140.6	(0.8)
Adjusted operating margin	**14.1%**	13.7%	
Order book	**1,241.4**	1,844.8	(32.7)

Financial performance

Adjusted revenue decreased by 3%. This reflected good growth at AXELOS and modest growth at Fera and Enforcement, which was outweighed by declines in Real Estate & Infrastructure, Insurance and Life insurance. Revenue included a £38m release of deferred income on the early transfer of Prudential UK's life insurance business to a new supplier in the second half of 2018.

Adjusted operating profit fell by 1%, as a result of increases in AXELOS and Real Estate, which benefited from restructuring actions, which were offset by declines in Managed Print and Mortgage Services. Profits included a £9m one-off benefit on the end of the general insurance contract with Marsh and a £6m one-off benefit on the end of the Prudential contract, which were partly offset by one-off write downs and provisions.

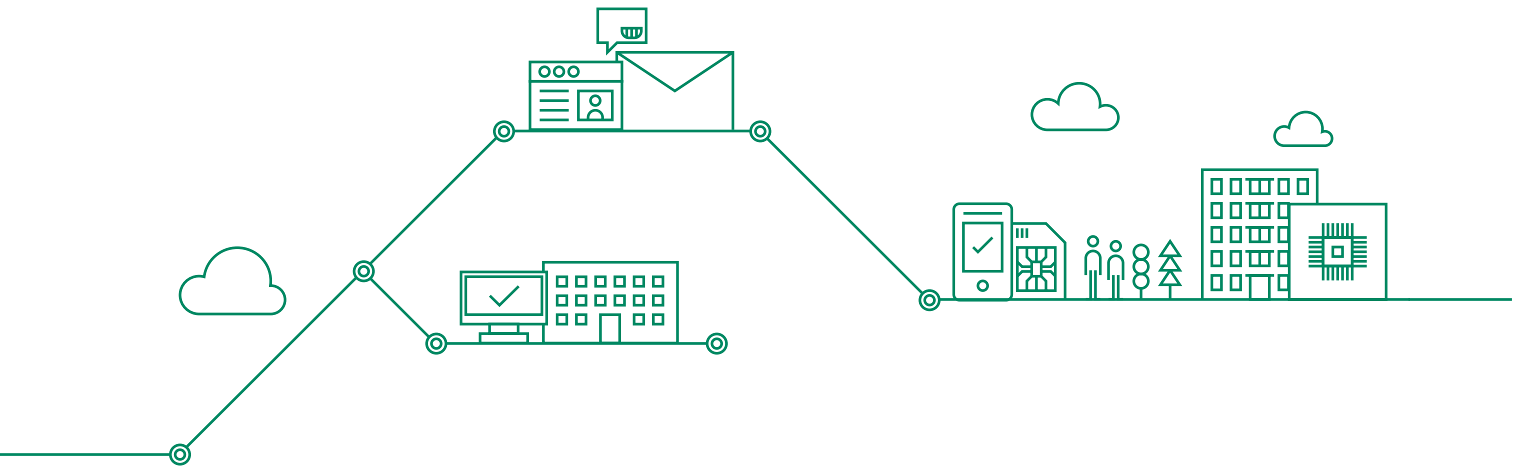
Sales and operational performance

During the year we disposed of a number of businesses, notably Supplier Assessment Services (including Constructionline) and ParkingEye, delivering over £400m in disposal proceeds.

The Life and Insurance Services business was impacted by the loss of the Prudential UK and Marsh contracts. We are focusing the business on supporting our customer services clients, where we are delivering high quality services for open book products.

We have restructured our real estate and infrastructure business, invested in our IT infrastructure and client portals and enhanced our security and compliance in our regulated businesses.

New sales wins in the year included: the award of a new courts enforcement contract by the Ministry of Justice; Travel & Events contracts with the Department for International Trade, and Rolls Royce; and a Customer Solutions win with Electric Ireland, providing collection and credit-control services.



Our people

A new people strategy

With more than 63,000 employees across Capita, a people-focused strategy is fundamental for creating an engaged workforce, who will act as ambassadors for the company, and for creating better outcomes for our colleagues, clients, customers and communities.

The appointment of Capita's first Chief People Officer in April 2018 offered the opportunity to define our new 'HR2020' people strategy and strengthen the people leadership team – to enable us to deliver this strategy across the organisation. The company-wide operating model aligns to and underpins the people strategy, which is itself made up of six key pillars and aims to nurture a culture at Capita of development, inclusivity and wellbeing, in which people are proud to work.

Employee engagement

Improving the culture and engagement with employees at all levels within Capita was one of the company's transformation workstreams throughout 2018 and continues to be a focus in 2019. The objective was to develop a culture where our people feel they matter and understand how their role contributes to the success of the business.

A robust process was undertaken during the autumn of 2018 to define the purpose of Capita, refresh the corporate values, and define the behaviours and manager commitments which underpin the culture of the company. Our purpose – 'we create better outcomes' – was launched in January this year. It states why we exist as a company and, through many proof points both internal and external, we are already starting to bring this purpose alive and create a motivating and inspiring guide by which, beyond just generating profit, decisions and actions are taken.

The Capita values remain the same – open, ingenious, collaborative and effective. However, their refreshed explanation, and the new behaviours and management commitments expected of our employees are at the core of the programme which will follow through into 2020 – to embed how we act and drive an improvement in employee satisfaction.

Following on from the McKinsey Organisational Health Index undertaken at the company in December 2017, a further survey of how our people feel about Capita was carried out between September and October 2018. We had a strong response (66%) to the new Our People Survey, showing that our people recognised the change in the direction and leadership of the company and valued it. One of the outputs was the 'employee net promoter score' (eNPS[1]), which will be a measure of our business performance. The eNPS was selected as one of the five performance metrics for the company's 2018 long-term incentive plan (LTIP) for senior management, with a positive swing of between 6 and 12 points required for the condition to be met. We will monitor the progress of the eNPS closely over the three-year performance period.

A focus for Capita during 2019, as we continue to reshape the organisation, will be on a continued programme of work which will drive further investment in our employees, their careers and training. This will include developing the employee value proposition which sits alongside the company's branding, purpose and values.

Resourcing

Having the right calibre of people at Capita is critical to succeeding in delighting our clients, customers and communities. As part of the HR2020 strategy, resourcing has now been aligned to the current and future transformation activities across the business, ensuring the company attracts the right mix of people, and that there is a broad mix of skills and diversity of thought to continue to drive success. Over the past year, Capita has recruited more than 20,000 people across its global operations but, with a highly competitive and continually changing marketplace, attracting and retaining employees requires more than just a job. Current and future employees are now increasingly interested about the additional benefits offered to support their working and home lives. To stay competitive and improve our ability to attract and retain the best people, the HR2020 strategy will deliver initiatives, such as a revised market competitive benefits package, as well as defined career pathways, and improved access to learning and development opportunities through the Capita Academy.

1 The employee net promoter score (eNPS) is calculated based on one question: 'On a scale of 0-10, how likely is it that you would recommend us to a friend or colleague.' Based on the number an employee selects, they are categorised as a: promoter (score between 9-10); passive (7-8); or detractor (0-6). The final eNPS is the difference between the percentages of promoters and detractors. The lowest possible score is -100, the highest 100. Because the biggest range of scores is for detractors, final totals are frequently negative. A total score above zero can be considered 'good', while any positive swing indicates an improving business.

To reduce attrition rates and retain our best people, we are also making it easier and more attractive for employees to move internally within the business. We have been promoting Capita's unique and diverse market offering and highlighting the vast array of opportunities within different sectors and divisions. The Talent Hub allows current employees to explore and apply for new opportunities internally before roles are advertised externally; and over the past year 16,000 people at Capita have found their next job internally.

Since 2017, overall employee retention rates have reduced, from 79% to 72%, which can be attributed to the significant, ongoing change across the business.

In addition, to help retain great people and understand future resourcing requirements, workforce planning has been developed and deployed company-wide. This is to encourage the business to think about long-term workforce needs, aligned to the corporate strategy. Our resourcing team can now prepare and build virtual talent pools that help to deliver the right skills and capabilities for future business requirements. The process also supports our current workforce, as we can identify where we need to develop our people with the right skills to support the needs of the business through our multi-year transformation.

People strategy pillars

Employee engagement
We want all our people to feel like they matter and understand how they contribute to the success of Capita.

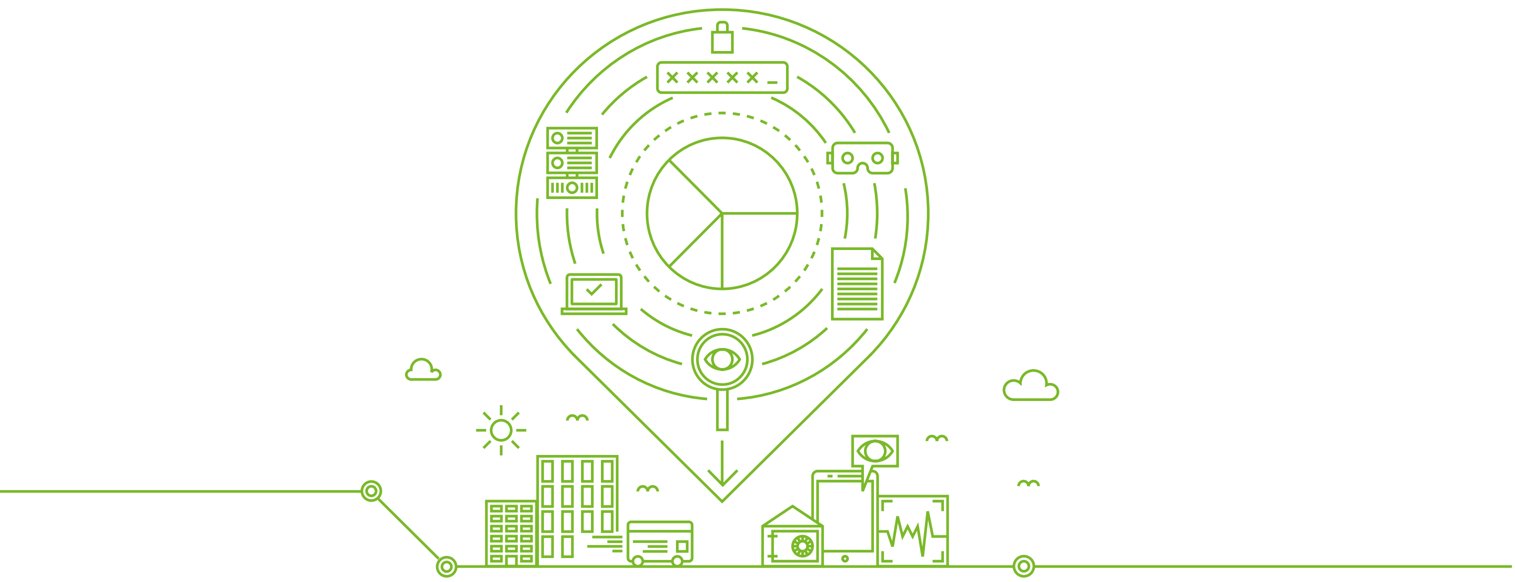
Responsible business
We want to do the right thing for our people, the environment and the communities we serve.

Reward
We want to rebuild employee trust through a transparent meritocracy which recognises our people for both how and what they contribute.

Resourcing
We want to ensure an appropriate pipeline of talent, so we have the right people in the right positions, for now and for the future.

Performance and development
We want to create the climate and tools that help our people be all that they can be.

Systems, process and administration
We want simple and consistent systems, and processes that are easy to use and drive efficiency.



Our people continued

Performance and development

Strengthening leadership

After the arrival of Jon Lewis as Chief Executive Officer in December 2017, a senior leadership review was undertaken to assess the appropriateness of the team to drive forward the magnitude of change required for Capita. As part of this review, a new Executive Committee has been set up, comprising some existing management together with a number of new appointments. The Executive Committee is now made up of six divisional and eight functional executive officers, as well as the Chief Financial Officer, all of whom report in directly to Jon and meet at least once a month.

The introduction of key roles such as Chief People Officer, Chief General Counsel and Chief Transformation Officer has created a balanced new leadership team. Strong functional leads are now able to drive change by setting an appropriate strategy with clear governance for their business area, as well as defining the functional framework and agenda to drive adoption of new governance, structure and compliance across the business.

A focus of the Executive Committee is to identify the desired culture and improve engagement across Capita's skilled 63,000-strong workforce, with the aim of harnessing the collective strength of our talent pool across all levels of the business. The newly strengthened executive team – with the right calibre of people from a variety of backgrounds and sectors – brings together in one team the greater diversity of thought required to drive transformational change.

To embed change successfully throughout the organisation, there has also been a strong focus on developing leaders and managers – to highlight the importance of the right values and behaviours for a successful business. The Capita Academy was launched in 2018 and in December ran a successful pilot, equipping existing managers with the appropriate tools to support the development of our talented people and to consistently embed the new purpose, values and behaviours across the business.

Learning and development

The diverse market offering at Capita creates a variety of opportunities for our people – across different sectors, businesses and industries – which supports our ability to attract and retain our great people. A critical role of the people function at Capita is to ensure that we can provide all our employees with access to varied career opportunities, whether that be progressing upwards, moving laterally into a new business or making a complete change of career path. We will be working on developing these paths across the business through 2019.

The Capita strategy creates a requirement to bring new skills into the business. At the same time, we need to ensure we can develop current employees to be able to take on new roles and help implement and drive forward the changes required for our success. Where new roles have been identified, managers are required to consider current employees for positions and post these internally on the Talent Hub before opening up the role externally. The hub has been successful in improving mobility within the business and the 'Look closer, go further campaign' continues to promote this at all levels and areas within the business. In 2018, 10,306 employees were successful in finding their next career move internally.

Operating model workshop

Discussions among Capita employees on shaping the future structure of our business

Workforce development is also critical to ensure we are able to satisfy external market demands, while continuing to delight our clients with innovative solutions and improving service standards. We continue to invest in our people as a priority, so that learning and development opportunities are accessible across our global operations to all employees, regardless of level or location.

The Capita Academy will be deployed fully in 2019 and made accessible to all employees. The purpose of the academy is to provide better quality training and focus capability development into key strategic skill-sets deemed vital for the company's transformation and future success. The academy will initially comprise five business-wide learning programmes, using a variety of means to deliver content and develop capability across sales, people management, IT, finance and project management.

Reward

Rewarding our people fairly, transparently and in line with the market is critical for building trust, and ensuring that we retain our great people and remain competitive in the job marketplace.

A full audit and assessment of the current benefits offered globally at Capita was carried out in 2018 in order to help improve our offering. We want to ensure we are able to provide benefits which are market-competitive, flexible and suitable for all employees in a range of locations across the world.

In addition, to provide employees with greater transparency around employment structuring, remuneration and career development, work was started with IBM in 2018 to implement a consistent, global job framework. A job framework is a critical component of any organisation and will enable our people to understand how they can progress their career at Capita, while providing benchmarks and guidance around remuneration for all roles in the business. This project will be completed by the end of 2019, with all employees mapped to a job family and framework.

Systems, process and administration

To support the significant changes being undertaken throughout the business, investment was secured to implement a new global HR system which will simplify processes and improve efficiency for all employees. Workday was selected as the new system to be deployed in 2019, alongside a newly established project team that has mapped all company-wide processes to ensure that the new HR system can improve and simplify the way our people work globally. The outcome of the new system will empower our people to take ownership of their own data and better utilise our global delivery centres with the digitisation of more standard processes.

Responsible business

Inclusion and wellbeing

In 2018, we committed to increasing our focus on diversity, inclusion and wellbeing, so that we were able to strengthen our approach and deliver tangible outcomes that make a positive difference to our people. We are delivering on our promise, with inclusion and wellbeing being a key focus theme for our new responsible business strategy and a common thread throughout our people strategy. We are committed to having a workforce that reflects the diversity of our communities and is inclusive, so that all employees can bring their 'whole selves' to work. Our updated values and behaviours also place a greater emphasis on the inclusive culture and behaviour we expect of all our employees and those working on behalf of Capita.

To achieve our goal, we've invested in a systematic review of our data, and insights from employee and client feedback. We've assessed what's worked well and what could work better to develop a new inclusion and wellbeing strategy, which sets out our priorities and key metrics on how we measure our progress, as detailed below:

- Valuing difference – because every single one of us is different, be that how we look, speak, act, or where we come from.
- Gender parity – 48% of our global workforce at all levels is female, but this proportion is not yet reflected at the leadership level.
- Improve data intelligence and reporting across the business – so that we can identify where we need to invest, and what roles and skills are needed to reflect the diversity of our communities.
- Geographically relevant targets – to reflect the differences between the regions in which we operate.

This approach will enable us to deliver our inclusion and wellbeing activity in a way that accelerates the pace of change and provides sustainable and embedded inclusive practices which focus on delivering better outcomes for all our people and our communities.

This is an exciting time for Capita and our inclusion and wellbeing agenda. We're doing things differently, opening up employee engagement and development opportunities through our employee networks, embracing the leadership of our Executive Committee and, importantly, working with our business leads so that inclusion and wellbeing are integral components of how we do business and how we live inclusively at Capita.

Our people continued

Gender pay gap

Capita's workforce profile has an effect, as at many other organisations, on our gender pay gap. We are disappointed that our pay gap has increased since last year and recognise that this is simply not good enough. We have a long way to go but are committed to understanding, proactively reducing and eventually eliminating our gender pay gap.

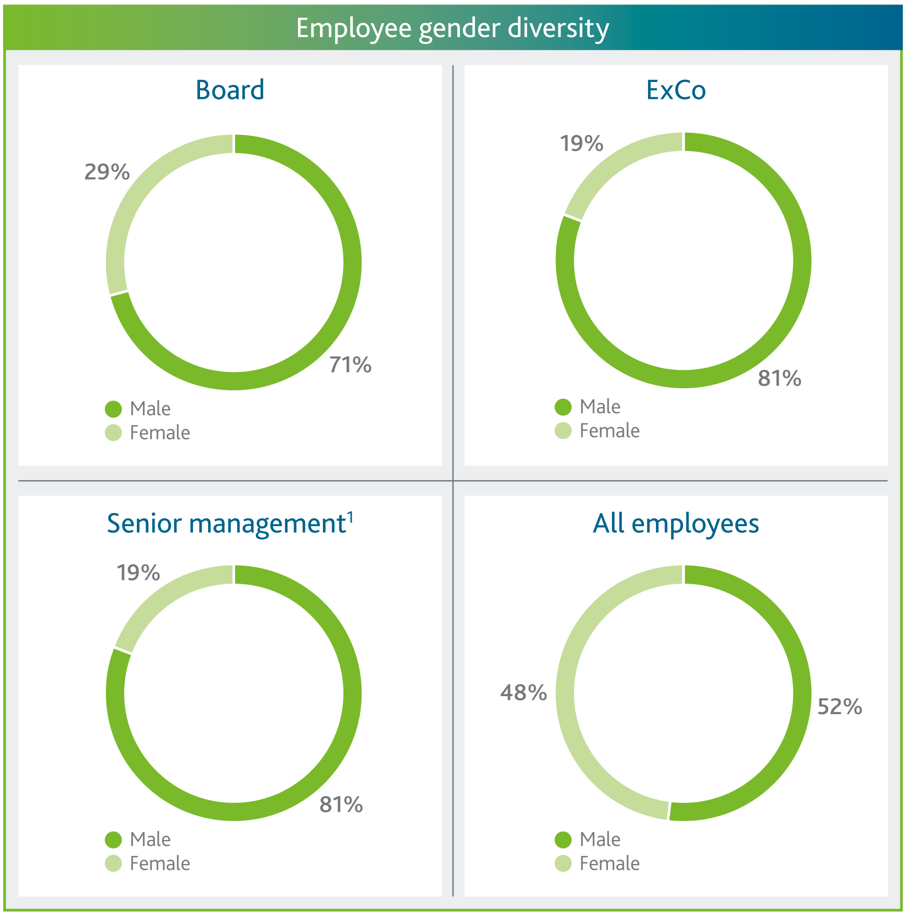
Since we last published our gender pay gap results, we've started investing – through our people and responsible business strategies – in activity that will shift the dial positively in improving gender equality. Our Chief People Officer and new Inclusion and Wellbeing Director are responsible for creating an inclusive workplace for all our people. We recognise that achieving gender parity is part of the solution and, as such, is a key pillar of our new inclusion and wellbeing strategy.

Our gender pay differential for Capita for 2018 compared with 2017 is detailed below:

Hourly pay	2018	2017
Mean (average) pay differential	**31.2%**	26.8%
Median (mid-point) pay differential	**23.4%**	25.3%

Despite an increase in our pay gap from 2017, our ranking within the Hampton-Alexander Review 2018 has improved and we are now ranked 110 in the FTSE 250 (up from 219 in 2017). The Hampton-Alexander Review is an independent review body which aims to increase the number of women on FTSE boards, with an important focus to improve women's representation in senior leadership positions. As a business, Capita recognises and is committed to our role in achieving the review's objectives. Our improved ranking is predominantly due to having more women on our Board and in our newly formed Executive Committee. To achieve this, we ensured that at least one female candidate was included on the shortlist of all Executive Committee recruits. This is a step in the right direction, but we recognise we still have a way to go to really change and achieve real gender parity across Capita.

More detail is disclosed in our Gender Pay Gap Report on our website at www.capita.com/responsibility



1 Senior management includes directors of subsidiary legal entities as per requirements of the Companies Act section 414C(8)(c)(ii) and 414C(10)(b).

Responsible business

Working responsibly for all our stakeholders

Responsible business is integral to our company purpose, operating model and strategy. With our new leadership team in place, we have strengthened our commitment to: be a trusted, accountable partner; create an inclusive culture where our people are proud to work; and operate our business with full regard for the needs of society and the environment.

With the launch of our purpose, backed by a clear set of values and behaviours, we've refocused our approach to addressing the most material challenges that our business and society face. We're calling it our responsible business strategy as it defines how – true to our purpose – we create better outcomes for our people, our communities and the environment.

We have already made some significant commitments: deciding to put two employees on our Board; agreeing a UK pension deficit recovery plan; updating our supplier payment terms in the UK and Ireland; and refocusing our charitable giving. Many of our people across our business are sharing their skills and expertise to address global issues.

Last year, we invested £1.5m in our local communities and our people volunteered more than 5,000 hours.

In addition to the progress achieved in 2018, we have committed to tackling issues which directly affect our clients and communities, such as youth unemployment, digital exclusion, gender equality and climate change. As a business, we understand the magnitude of these issues and recognise that, with the support and dedication of our people, we can make a significant contribution and be part of the solution.

Defining responsible business

At Capita, we affect the lives of millions of people, either directly or indirectly, every day. Through our customer conversations, business operations, digital solutions and responsible business programmes, we have a unique opportunity to be a force for good, helping address global challenges and making a positive contribution to society.

Our five-year responsible business strategy was defined in consultation with colleagues, clients, investors and community groups to identify the most relevant sustainability issues that Capita should be addressing. Our strategy prioritises our actions around these issues through one cross-cutting theme and four focus themes.

Our cross-cutting theme of 'operating responsibly' covers our approach to governance, business ethics, supplier management, client relations, and health and safety.

The four focus themes are:

- Youth skills and jobs: more than 200 million young people globally are unemployed or working while living in poverty[1]; we will empower 100,000 young people in the communities we serve to progress into the world of work through our business operations, products and services, and responsible business programmes.
- Digital inclusion: as many as 11.3 million people in the UK are lacking basic digital skills[2]; we will equip 10,000 people in the communities we serve with the digital skills required for today's world.
- Inclusive workplace: so that all employees can bring their 'whole selves' to work and to address gender equality which still holds women and girls back, especially in the technology sector; we will have a workforce that reflects the diversity of our communities and is inclusive.
- Sustainable innovation: climate change is now affecting every country on every continent[3]; we will reduce our contribution to climate change and support our clients do the same through our products and services.

Embedding responsible business across our operations

We're responding to the relevant global challenges our business and society face through a cross-cutting theme and four focus themes.

Operating responsibly

Governance, business ethics, supplier management, client relations, and health and safety

Youth skills and jobs

Empower 100,000 people progress towards the world of work

4 QUALITY EDUCATION
8 DECENT WORK AND ECONOMIC GROWTH

Digital inclusion

Equip 10,000 people with digital skills

8 DECENT WORK AND ECONOMIC GROWTH

Inclusive workplace

We will have a workforce that reflects the diversity of our communities and is inclusive

3 GOOD HEALTH AND WELL-BEING
5 GENDER EQUALITY
8 DECENT WORK AND ECONOMIC GROWTH

Sustainable innovation

We will reduce our contribution to climate change and support our clients to do the same

11 SUSTAINABLE CITIES AND COMMUNITIES
13 CLIMATE ACTION

Our strategy demonstrates our contribution towards achieving the United Nation's Sustainable Development Goals, as shown above.

1 http://www.ilo.org/global/topics/youth-employment/lang--en/index.htm
2 https://www.goodthingsfoundation.org/areas-of-work/digital-inclusion
3 https://www.un.org/sustainabledevelopment/climate-change-2/

Responsible business continued

Governance

Accountability for our responsible business strategy sits with our Chief People Officer and the Executive Committee who report bi-annually to the Board on progress against our strategy and goals. The Executive Committee provides oversight of the strategy, ensuring appropriate resource is in place to deliver the programmes. A central responsible business function oversees the strategy, developing and delivering business-wide programmes, monitoring performance against stated goals and raising awareness of responsible business practices across all the functions and divisions. As we deliver our strategy through 2019, we will be strengthening our governance and creating action groups which will be responsible for delivering detailed action plans for each of our focus themes.

Delivering our strategy

Youth skills and jobs

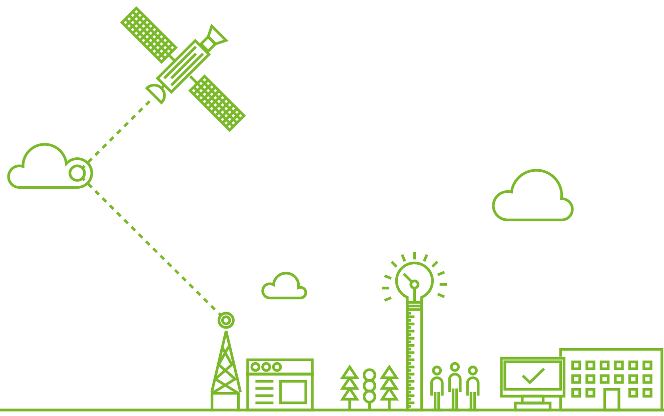
At Capita, we are a support services leader in the education sector, delivering a range of services to schools and academies. Our software solutions support 21,000 schools and 160 universities and colleges in the UK, to help them access information on emerging trends and highlight areas of excellence and underperformance.

As our products and services support schools to thrive, we also support young people to develop the abilities and skills to prepare them for the workplace. By 2023, we want to have empowered 100,000 young people to progress towards work with the help of our products and services, and through our business operations. Our new charity partnerships with Teach First and Young Enterprise will enable our people to volunteer their skills in local schools and colleges.

We continue to bring talented people into our organisation through our apprenticeship scheme. In 2018, we had 456 apprentices working across our businesses.

Tackling youth unemployment in South Africa

Capita South Africa is committed to supporting two of the country's greatest challenges – education and youth employment. The Capita South Africa Scholarship Programme is our commitment to assisting our employees' children with access to education. In 2018 we had 86 beneficiaries in the programme with 15 graduating from our Life Skills programme which gives them the opportunity to access life-skills training, such as goal-setting, conflict management and study skills. We continue our partnership with Sinenjongo High School to support the lack of work readiness skills, helping create meaningful opportunities and careers for young South Africans.



Charity partnership with the Alzheimer's Society

We had a successful year of fundraising and volunteering for our charity partnership with the Alzheimer's Society. Our one-year partnership, which ended in June 2018, created more than 1,300 new Dementia Friends and delivered dementia awareness training to 60 employees. The goodwill of our people saw us raise more than £218,000, which is used to support the invaluable services that the Alzheimer's Society delivers.

Digital inclusion

At Capita, we are at the forefront of the digital revolution, unlocking value for our clients through digital transformation, data analytics and automation. Alongside this, we understand that rising digitisation can make products and services less accessible to some people. We have therefore committed to equipping 10,000 people with digital skills, enabling them to reap the benefits of the digital world we live in. Partnering with local community groups and charities, we will develop and deliver a digital skills programme that helps community centres reach more people, while we will also train our people to become 'digital champions', sharing their skills in local communities.

Salford Digital Eagles

Urban Vision, our joint venture with Salford City Council committed to tackling digital exclusion by signing up to the Salford City Council Digital Eagles scheme. The council is the first in the country to team up with Barclays to train employees to help their colleagues embrace new technology. Digital Eagles aim to improve thousands of lives by equipping and supporting people to reap the benefits of the digital world – such as surfing online safely, improving job prospects or keeping in touch with loved ones. We currently have three Digital Eagles involved in the scheme.

Enabling social mobility

Many people never get the chance to succeed simply because of where they were born or lacked the opportunities to progress in life. Lack of social mobility is a global issue and at Capita, we are well placed to encourage and drive action. Therefore, a focal point of our responsible business themes is social mobility – delivering programmes that support all the communities we live and work but more specifically those areas with low social mobility. This year, we were the proud sponsors of the UK Social Mobility Awards – an awards programme delivered by the charity Making the Leap.

Inclusive workplaces

Last year, we committed to increasing our focus on diversity, inclusion and wellbeing. The purpose of our commitment was to create an environment where our people can bring their whole selves to work and enhance diversity of thought across the business to create better outcomes for our clients and customers. We are delivering on our promise and have developed an inclusion and wellbeing strategy alongside the wider People transformation plans – all underpinned by the updated values and behaviours. All of these now place a greater emphasis on how managers, leaders and their teams can create a more inclusive environment for everyone.

For more information about our approach and gender pay gap, please refer to page 38 in our people section.

Responsible business continued

Sustainable innovation

As a business with more than 300 sites and 63,000 people worldwide, we have an impact on the environment. This is a result of the energy we use to run our buildings, the waste we generate and the business travel we conduct. We measure our environmental performance through reporting our carbon footprint annually in terms of tonnes CO_2 equivalent (tCO_2e) and tonnes CO_2 equivalent per person. We have set a goal to reduce our contribution to climate change and support our clients to do the same through our products and services.

We have successfully reduced our emissions between 2017 and 2018 by 4% and will strive to improve this further by continuing with our energy reduction programme across our UK portfolio. This programme was launched in 2015 and has already provided Capita with savings of £4.4m. In addition, we will improve the quality and scope of our environmental performance data, with the ambition to set a science-based target in 2020 to reduce emissions even further.

We will also be working with our six divisions to identify the products and services we deliver that already help our clients respond and adapt to climate change.

Annual greenhouse gas emissions

We measure our environmental performance through reporting our carbon footprint annually in terms of tonnes CO_2 equivalent (tCO_2e) and tonnes CO_2 equivalent per person. We report separately on our direct emissions from Capita controlled and owned sources (Scope 1), indirect emissions from consumption of electricity, heat or steam (Scope 2) and emissions from third parties (Scope 3). This ensures our compliance to Part 7 of The Companies Act 2006 (Strategic Report and Director's Report) Regulations 2013 which requires certain disclosures in respect of greenhouse gas emissions (the Strategic Report GHG Emission disclosures).

Annual greenhouse gas emissions	2018	2017	2016
Scope 1	**19,975.68**	22,605.38	18,137.00
Scope 2	**45,174.51**	54,261.61	65,094.00
Scope 3	**36,277.00**	29,264.29	34,317.00
Total gross tonnes of CO_2e	**101,850.96**	106,131.29	117,489.00
Total gross tonnes of CO_2e/£1m revenue	**26.33**	25.56	26.97
Total gross tonnes of CO_2e/headcount	**1.52**	1.52	1.61

Notes:

Restated 2017 emissions data to improve the accuracy of reporting, using actual data to replace estimations.

Scope 1: Emissions from Capita sources that are controlled by us, including the combustion of fuel, company owned vehicles and the operation of our facilities.

Scope 2: Emissions from the consumption of purchased electricity, heat or steam.

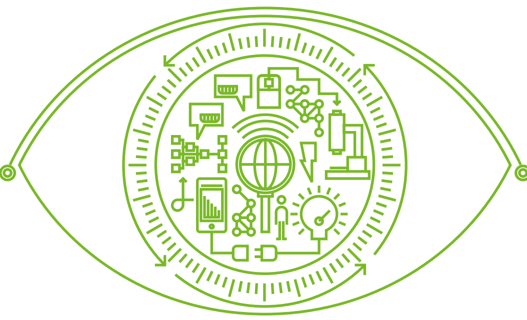
Scope 3: Emissions from non-owned sources related to Capita's activities, including business travel.

Methodology

Our disclosures cover sources of our greenhouse gas emissions from our operations in UK, Ireland, Europe (Poland, Germany, Switzerland, Austria), India and South Africa. Capita converts the consumption data into a carbon footprint with consideration to the World Business Council for Sustainable Development and World Resources Institute's (WBCSD/WRI) Greenhouse Gas Protocol, together with the latest emissions factors from the UK Department for Environment, Food and Rural Affairs (Defra) or, where available, the latest industry factors, such as hotel stays from the Green Tourism Board Scheme.

Helping London to lead on climate change

Capita's Zero Carbon Housing Team, part of Capita Real Estate and Infrastructure, is leading the delivery of the Mayor of London's domestic energy efficiency programme, RE:NEW. The programme aims to reduce emissions from existing homes in London through energy efficiency and renewable energy investments. Our Zero Carbon Team has been working closely with the Greater London Authority to design, develop and deliver the pan-London programme and has so far supported the investment of more than £130m in energy efficiency measures in 37,000 homes in London. This has reduced the equivalent of 32,000 tonnes of carbon dioxide per year, lowered the energy costs of an estimated 4,500 fuel-poor households, while water-saving measures in more than 1,000 homes has saved the equivalent of 16 million litre water bottles.



Operating responsibly

For Capita to operate as a responsible business we are now educating our managers and leaders about their part to play, with the introduction of managers' commitments. The commitments identify ways which managers and leaders can ensure we are operating in the right way for our customer, clients and people. We are committed to embedding responsible business practices across our global operations.

Supplier relations

With 34,657 suppliers, we recognise that Capita's supply chain is critical to the company's success, and the agility, speed and value we need to be competitive. In addition to the work we do for people in our local communities, we also want to support local businesses to grow and succeed. 68% of our suppliers are classed as small and medium-sized enterprises (SMEs), which equates to 19% of supplier expenditure across Capita.

We aim to source responsibly, working with our suppliers to enhance the sustainability of what we buy. Over the past year, we enhanced the questions we ask of our new and renewing suppliers to ensure we work with suppliers who uphold our ethical principles. In addition, to help stamp out modern slavery, we continue to audit our material and high-risk suppliers.

In October, we updated our supplier payment terms, committing to pay small and micro businesses (<50 employees, <£10m turnover) within 14 days and SMEs (<250 employees, <£50m turnover) within 30 days. In the year ended 2018, we paid 76% of micro organisations within 14 days and 77% of our SME suppliers within 30 days or less. In both cases, over 95% were paid within 60 days.

Client relations

We take a holistic approach to the way we support our clients, listening to their needs and requirements to provide the right solutions to help them deliver their services more effectively and efficiently, solve challenges and maintain their competitive positions. We also look to work collaboratively with our clients, tackling local socio-economic issues and delivering long-term value to their communities.

Over the last two years, we have conducted a survey of our key clients to provide a view of their satisfaction. This survey is intended to help us identify where there is potential to add further value to our clients' operations. One of the outputs is the 'customer net promoter score' (cNPS[1]), which will be a measure of our business performance. The cNPS was selected as one of the five performance metrics for the company's 2018 long-term incentive plan (LTIP) for senior management, with a positive swing of between 6 and 12 points required for the condition to be met. We will monitor the progress of the cNPS closely over the three-year performance period.

Protecting our information and data

Protecting the data of our clients, our company and our people is one of the most fundamental and important responsibilities we have. Our Data Protection and Information Security Policies, Standards and Procedures ensure we treat personal information correctly, in accordance with the law and best practice. When we process personal information (including sensitive personal information), we ensure that we comply with these policies, standards and procedures including its collection, storage, use and safe destruction.

In order to ensure compliance with the Data Protection Act 2018 (and General Data Protection Regulations), we have implemented a comprehensive programme including a network of trained privacy professionals who provide expert help and assistance for anyone handling data within our business or on behalf of our clients.

We continue to raise awareness of the importance of data protection and privacy through our mandatory data protection training and ongoing training programmes, in particular the Think Privacy, Think Security campaign.

Health and safety

We conduct our business activities in a manner that aims to prevent the injury and ill health of our people and others. Our global health and safety management system sets the required standards across the company to ensure that our people and businesses understand the right protocols and procedures; and ensure that we are creating a safe working environment, which reduces the risk of accidents and ill health. The system has enabled Capita to reduce its accident rate year-on-year, with a reduction of 25% from 2017 to 2018; and we are committed to continuing this improvement annually in all areas of the business. To encourage a better work-life balance, we also provide opportunities for flexible working (14% of our employees are part-time) and have introduced technology to enable employees to work remotely.

Bribery

We do not tolerate bribery and corruption. Our Anti-Bribery and Corruption Policy applies to all Capita businesses and employees. The Risk and Compliance teams monitor compliance against this policy, ensuring all parts of the business are aware of their responsibilities in terms of charity donations and sponsorships, and facilitating payments, gifts and hospitality. All employees must complete Financial Crime training annually.

Human rights

We aspire to conduct business in a way that values and respects the human rights of all our stakeholders. Our Human Rights Policy details our commitments to upholding the principles of human rights, as set out in the UN Declaration of Human Rights and the International Labour Organisation Core Labour Principles. We comply with all relevant legislation, including the UK Modern Slavery Act which is detailed further online.

Code of Conduct and speaking up (whistleblowing)

We are due to launch a new Code of Conduct that will build on and replace our Ethical Code, to set out what is expected from every person working for, and with our businesses, anywhere in the world.

The Code will be underpinned by our global policies including our Speak Up Policy which sets out the channels available to any person who works for or with us to raise any concerns ('blow the whistle') that our policies are not being followed correctly or that something is illegal, unethical or does not comply with our Code of Conduct.

1 The customer net promoter score (cNPS) is calculated based on one question: 'On a scale of 0-10, how likely is it that you would recommend us to a friend or colleague?' Based on the number a client selects, they are categorised as a: promoter (score between 9-10); passive (7-8); or detractor (0-6). The final cNPS is the difference between the percentages of promoters and detractors. The lowest possible score is -100, the highest 100. Because the biggest range of scores is for detractors, final totals are frequently negative. A total score above zero can be considered 'good', while any positive swing indicates an improving business.

Note: The information required to be contained in the non-financial reporting statement under section 414CA Companies Act 2006 is set out in this responsible business section. Other relevant information about Capita's business model, key performance indicators and approach to risk management are detailed in the strategic report on pages 1–52.

Internal control and risk management

Our risk management is continually evolving

Effective risk management will be key to the successful delivery of Capita's strategic objectives. The company faces a range of business uncertainties and, by using a structured approach to risk management, we are able to understand, assess, mitigate and manage these risks.

The events of early 2018, which led to the rights issue, are a timely reminder of the importance of continually improving the way we manage our risks. The diverse nature of our businesses, the sectors we serve, and the geographical reach of our operations are all key factors in the risk environment facing the Group.

A number of the Group's subsidiaries are regulated by the Financial Conduct Authority (FCA), with others regulated by OFCOM, while some of the healthcare business are covered by health sector regulation. Compliance with regulatory requirements helps set standards for the Group, which are in some cases appropriate for both the regulated and the non-regulated businesses.

To underpin execution of our 'simplify, strengthen and succeed' strategy, work on defining and delivering a new operating model started in 2018. This included reviewing the risks to the successful delivery of this strategy.

Notwithstanding the redefined strategy, the risk profile (shown on page 46) has stayed largely the same as in 2017. However, the changes during the year have allowed us to understand more fully the risks being managed and to plan better and more effective mitigating actions.

The focus on risk through formalised business and executive risk committees continued throughout 2018, with areas of attention flexing to the requirements of the different businesses as well as the wider corporate exposures. We have improved and broadened the information presented by the divisions at monthly business performance reviews to better track a range of financial, non-financial, operational and conduct metrics. These meetings are the primary vehicle for managing corporate performance and the inclusion of these risk indicators demonstrates the standard of behaviours, conduct, culture and level of control expected across the business.

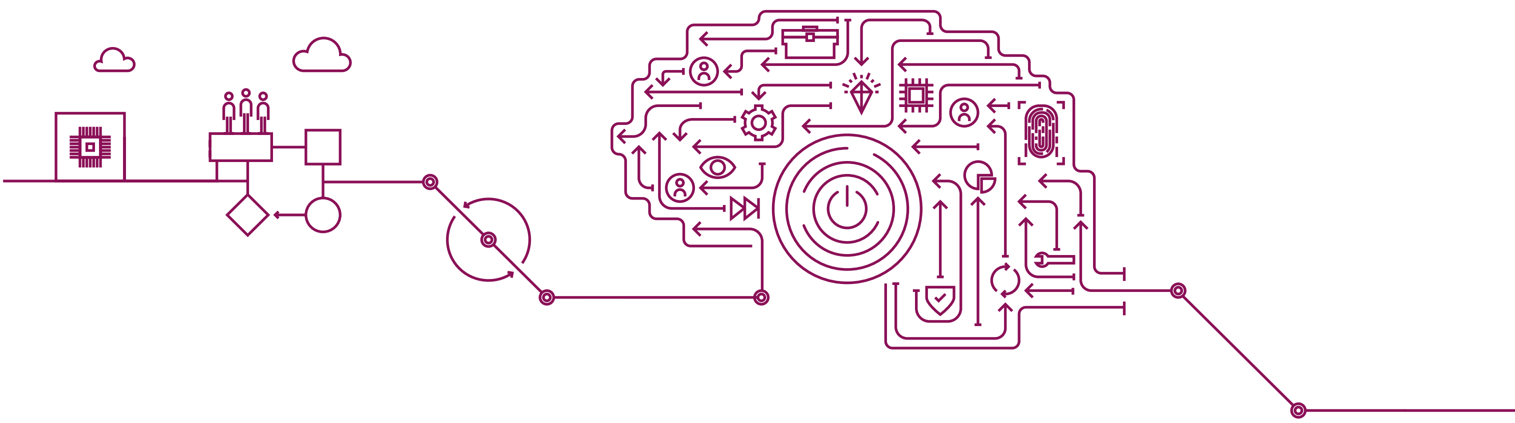
However, there is more to do and in 2019 we will develop and implement a control and risk self-assessment approach (common in many companies) as a core part of improving our risk management framework and approach.

Risk management approach

At Capita, risks are identified and managed across the business, using the risk management framework (RMF). This supports the Board and executive team in embedding effective risk management. The RMF sets out our risk management framework and is maintained by the Risk & Compliance function.

The application of a consistent approach across all business activities should ensure that effective control measures are in place for the risks that have the highest potential impacts. Experience shows that controls have not been embedded consistently within the business and this has resulted in failures and external scrutiny over delivery of our PCSE and RPP contracts.

The Board takes assurance about the management of risk from the 'three lines of defence' model, as shown in the graphic below right. The model is not consistently embedded and some lines of defence are not yet working as they should. Improvements to ensure that the three lines model is effective are underway and will continue during 2019.



Risk governance arrangements

The Board is ultimately responsible for the management of the risks that Capita faces. The risk management framework and the Group's associated risk appetite and tolerance are reviewed by the Board. Significant risks are introduced, if new, or escalated, if changed for specific attention at any time. For example, in 2018 we added a risk related to the overall transformation programme taking place across the Group.

The Board delegates responsibility for regular reviews of the risks managed by Capita through formal terms of reference to the Audit and Risk Committee. The risk management process is overseen by the Audit and Risk Committee. It approves the annual plans for both Group Internal Audit and Risk & Compliance and is provided with regular updates on progress throughout the year with reports on findings, issues, risk incidents and themes for its attention. It sets the external audit scope and receives reports on findings.

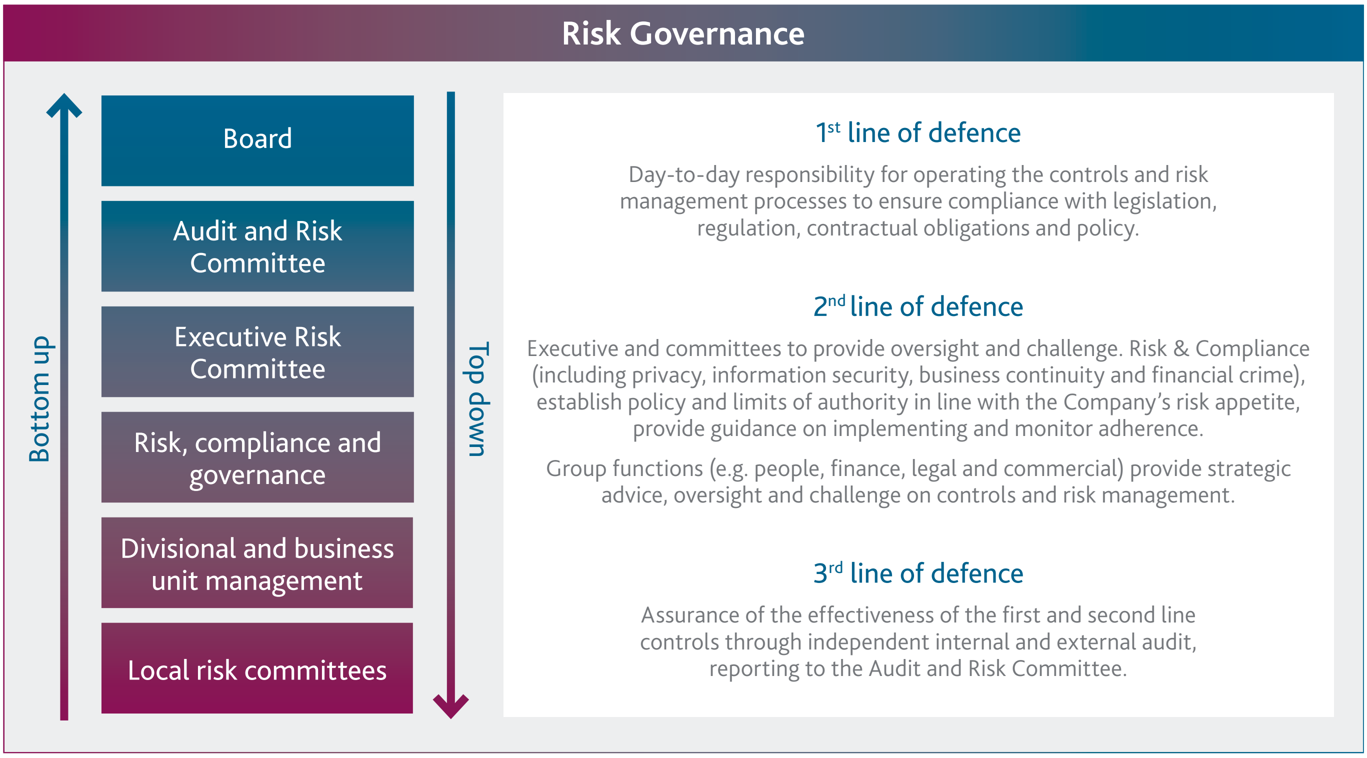
The Executive Risk Committee has the oversight of Capita's overall residual risks. It in turn reports the residual position with narrative from the Executive to the Audit and Risk Committee to allow full sight of the corporate risk profile and material issues.

To ensure there is sufficient oversight of the regulated financial services businesses, a Financial Services Risk Committee is being established in 2019. Capita recognises the importance of the financial services businesses it operates, and the particular risks associated with financial services operations. The Committee will be chaired by an independent Non-Executive Director and will report to the Executive Risk, and Audit and Risk committees.

The company made progress during 2018 to address some of the risks, as well as putting in place the enablers to drive a stronger risk management approach for Capita's principal risks. The progress included:

- Enhancing executive leadership team over a 12-month period with stronger functional leadership.
- Reorganising the business and introducing a new operating model.
- Completing the rights issue.
- Working with the FCA to ensure that the regulated businesses are compliant with the relevant requirements.
- Enhancing the monthly business performance review process to include review of risk.

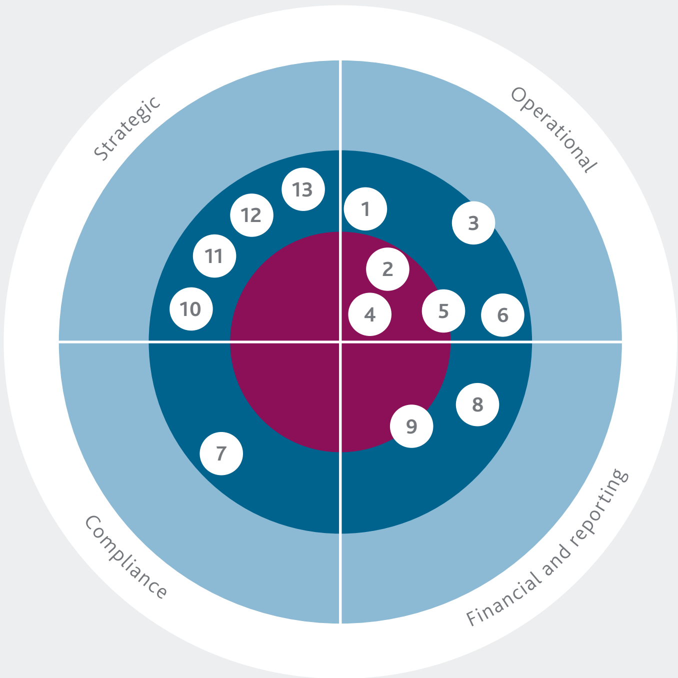
We are working to provide greater consistency in risk management; in particular, an enhanced control and risk self-assessment process is being developed. We are also adapting our risk management framework. Both these enhancements, targeted for 2019, aim to ensure the risk framework remains fit for purpose and further embeds the commitment of the organisational leadership to work within a strong controls culture.



Internal control and risk management continued

Principal risks

Current assessment of principal risks



1 Failures of internal systems of control	8 Failure to achieve financial expectations
2 Failures in information security controls	9 Lack of corporate financial stability
3 Increased business complexity	10 Failure to innovate
4 Operational IT	11 Adverse changes in political landscape
5 Failure to effectively manage our people	12 Reputation
6 Weaknesses in acquisition and contracting	13 Transformation
7 Legal and regulatory	

Risk assessment – exposure to the business if risk materialises:

- Critical: a crisis event; of immediate critical concern; and the maximum level of risk Capita can bear while remaining effective at delivering its strategy.
- Uncomfortable: causing problems that are beginning to put uncomfortable pressure on delivery.
- Tolerance: a bearable, business-as-usual level of risk; recognised as an early-warning indicator; but manageable with the right people and processes in place to respond to the threat.

The graphic above shows the risk position at the end of 2018. There was limited movement of the risk position during the year. The transformation programme which is underway will need to be effective in changing the approach to the areas of risk to be effective.

Principal risk categories

Our risk management framework is based around risk categories against which our businesses measure their risk exposure and report on incidents and issues. The 'critical' risk exposures are reported directly to the Audit and Risk Committee to provide clear line of sight. The principal risks represent the main risks to the strategy and objectives of Capita.

The principal risks and uncertainties which are considered to have a material impact on Capita's performance and achievement of its strategy are set out on the following pages. External and internal risk factors are considered. This is not intended to be an exhaustive and extensive analysis of all risks which may affect our businesses. Additional risks and uncertainties not presently known to management, or currently deemed to be less material, may also have an adverse effect on our objectives.

To repeat, Capita is in year one of a fundamental transformation plan. The principal risks reflect this; in particular, Capita's ability to meet financial expectations, deliver sales growth and protect its reputation, so as to continue to do business. The integrated nature of the transformation plan is designed to mitigate these risks as effectively as possible. Accordingly, such mitigation is dependent on the successful implementation of this plan.

Principal risk	Potential impact	How we manage the risk
1. Failure of internal systems of control Controls do not operate effectively or do not operate at all Assessment at year-end: Uncomfortable **This risk has partly materialised due to some control failings in parts of the business. However, the control environment is assessed as sufficient to avoid material misstatement.**	• Increased fraudulent activity • Increased risk of financial malpractice • Increased regulatory scrutiny • Increased costs associated with remediation activities • Reputational damage • Service detriment to our clients or end-customers • Financial loss	**Mitigating actions in 2018:** • Governance, boards and committees in place to review • Internal Audit programme of work • Monitoring of regulatory requirements • Monthly performance tracking of risk indicators **Future actions:** • Controls and risk self-assessment • Financial Services Risk Committee put in place • Implementation of a new finance system supported by standard processes and controls
2. Failure in information security controls Information held in systems is accessed or shared in breach of policy Assessment at year-end: Critical **During the first half of 2018, some incidents occurred due to inadequate maintenance of infrastructure controls. The cyber-resilience programme is being redesigned to address the highest priority outstanding risks as soon as practical.**	• Significant loss of data • Loss of customer confidence • Failure to win new business • Regulatory censure/fine • Remediation programme at Capita's expense	**Mitigating actions in 2018:** • Capita operates and holds certifications for ISO 27001 • External review of cyber-resilience • Programme of work to remediate issues • Detective controls in place and regularly reviewed to consider new threats • Preventative controls in place and regularly updated to detect new threats • Data protection programme of work carried out **Future actions:** • Comprehensive review of current status of resilience against group and contract requirements • Simplify our cybersecurity through the creation of a single cyber-operations centre • Strengthen our cyber-posture by developing and mandating additional capabilities, including organisational awareness and enhanced training of our people • Work with organisations, such as Security Alliance (a Gartner company), to help assess the threat to Capita by looking from an external viewpoint • Run continuous vulnerability assessments across the estate to proactively identify weaknesses that need to be addressed • Run executive cyber-training to ensure all our senior employees are aware that cybersecurity is a business responsibility and not just an IT responsibility
3. Increased business complexity Business has grown into many diverse business areas Assessment at year-end: Uncomfortable **During 2018, the Group developed a new strategy, simplified its structure and sold some businesses.**	• Lack of clear accountability within the business • Risk and performance management are more difficult to operate effectively, leading to sub-optimal outcomes for all stakeholders • Divisions not working together, duplicating effort and driving up costs	**Mitigating actions in 2018:** • Reorganised business into coherent divisions • Implemented a clear operating model with supporting governance to clarify accountabilities • Simplified the range of market offerings • Strengthened corporate and divisional management • Disposal of non-core businesses **Future actions:** • Embed operating models across business • New customer relationship management tool to be put in place • Financial models agreed where divisions introduce each other

Key ● Critical ● Uncomfortable

Internal control and risk management continued

Principal risk	Potential impact	How we manage the risk
4. Operational IT IT infrastructure is not fit for purpose Assessment at year-end: Critical **During the year, a programme to address ineffective maintenance of the technical infrastructure was established.**	• Disruptions to service lead to loss of revenue • Service credits payable to clients • Loss of confidence in Capita's IT systems	**Mitigating actions in 2018:** • Upgrade technical abilities • Investment in data centre network • Simplified existing IT environment • Change management processes help reduce risk and unplanned outages **Future actions:** • Continued activity on simplifying data centre network Continued investment in IT resilience
5. Failure to effectively manage our people Unable to recruit and retain key employees Assessment at year-end: Uncomfortable **The professionalisation of the people function provides a platform to address the ineffective controls in this area.**	• Loss of key employees • Unable to attract the right people with the right skills • Lack of skilled, competent resource • Increased cost of recruitment due to high attrition rates • Unable to deliver Capita's strategy • Lack of continuity at Executive Committee level	**Mitigating actions in 2018:** • Chief People Officer appointed • Focus on culture from the top • Strengthened senior leadership team • People strategy defined • Improved engagement across the business • Capita Academy launched **Future actions:** • Focus on succession planning and development of employees • Talent reviews, enabling employees to identify new opportunities and to move to new roles within Capita • Investment into new HR systems
6. Weaknesses in acquisition and contracting Entering into poorly worded contracts to our detriment Assessment at year-end: Uncomfortable **Past weaknesses with contract initiation and management are being addressed through stronger governance.**	• Loss of contracts • Lack of ability to acquire new business • Contract terms are punitive • Contract terms are not met or understood • Loss of profits • Exposure to unexpected costs or onerous terms • Brand and reputation damage if not managed effectively • Acquisition synergies are not realised	**Mitigating actions in 2018:** • Contract Review Committee in place to better understand contract risks in new or existing arrangements **Future actions:** • Delivery of a clearly defined Contract Management process • Transactions committee to be put in place

Key: ● Critical ● Uncomfortable

Principal risk	Potential impact	How we manage the risk
7. Legal and regulatory Breaking the law or not meeting regulations Assessment at year-end ● **The environment is more complex and work is underway to strengthen our response in all areas.**	• Censure or fine from a regulator • Reputational damage • Lack of confidence from investors and customers • Data Subject Access requests not completed within required timescales • Increased costs due to remediation activities • Increased regulatory scrutiny which could limit potential for growth	**Mitigating actions in 2018:** • Regular risk committee meetings held throughout the year, including the Audit and Risk Committee • Engagement with regulatory bodies • Specialist team monitoring and engaging with regulators over proposed regulatory or legal changes • Chief General Counsel appointed • Legal team in place across the divisions to manage potential and actual issues **Future actions:** • Financial Services Risk Committee to focus on financial services risk • Development of controls and risk self-assessment tool • Refresh and roll-out of a revised risk framework
8. Failure to achieve financial expectations Adverse performance against our stated business plans Assessment at year-end ● **The Group has clear targets for 2020 and is strengthening business management to secure their delivery.**	• Loss of revenues, profits and/or cash flows • Failure to return to organic revenue growth • Loss in shareholder value • Undermines investor confidence • Erodes corporate position in the market • Weakens our ability to attract and retain the best people	**Mitigating actions in 2018:** • Move to a multi-year strategic planning range • Detailed bottom-up Board-approved business plan for 2019 and 2020 • Enhanced monthly performance reviews • Clearer financial and operational KPIs at business, divisional and functional level • New Executive Committee governance committees • Appointed Chief Growth Officer **Future actions:** • Delivery of upgraded financial systems, processes and controls • Deep-dive review of businesses to assess progress against the new strategy • Plan to drive revenue growth
9. Lack of corporate financial stability Failure to manage financial exposures and access to finance Assessment at year-end ● **The balance sheet is stronger and more resilient, with more to do in 2019.**	• Increase in leverage • Inflexible balance sheet • Lack of cash to invest • Inability to grow • Lack of confidence from investors and customers	**Mitigating actions in 2018:** • Launched new strategy • Completion of the rights issue • Disposal of non-core businesses • Reduction in leverage • Early repayment of debt • Targeted investment • Achieving £70m of cost-out savings • Developed a plan to address pension deficit **Future actions:** • Further repayment of debt

Key ● Critical ● Uncomfortable

Internal control and risk management continued

Principal risk	Potential impact	How we manage the risk
10. Failure to innovate Not keeping up with technology or other changes Assessment at year-end **During 2018, more governance and structures were set up to support innovation.**	• Inability to grow and develop into new markets • Loss of new and existing business to competitors • Erodes corporate position in the market • Weakens our ability to attract and retain the best people • Unable to compete with others who are innovative	**Mitigating actions in 2018:** • Strengthened the executive team with a Chief Digital Officer and Chief Growth Officer • Working with external technology partners to develop our digital offering • Share market innovation best practice internally
11. Adverse changes in political landscape Unable to operate under a different political regime Assessment at year-end **2018 saw some changes but the environment remains uncertain.**	• Fewer outsourcing opportunities offered by the public sector • Existing business no longer outsourced • Exposure to markets with limited growth opportunities • Loss of revenues, profits and/or cashflows	**Mitigating actions in 2018:** • Engagement with Government and other parties (e.g. regulators) to understand current thinking • Preparations made in relation to Brexit • Understanding of client requirements for Brexit if there is a transition period or no deal with Europe **Future actions:** • Build a broader base of understanding about Capita as a transforming business, committed to delivery of service • Demonstrate value delivered in public sector
12. Reputation Poorly thought of by our stakeholders Assessment at year-end **There were some issues with challenging contracts in 2018 but the building blocks for a better reputation are in place.**	• Loss of confidence in Capita • Clients suffer reputational damage • Fewer or no new contracts • Loss of revenues, profits and/or cash flows • Unattractive proposition for shareholders to invest in	**Mitigating actions in 2018:** • Director of Corporate Affairs appointed • Reactive and proactive management of media stories • Working with selected media to promote Capita's positive image **Future actions:** • Deliver new corporate affairs strategy • Ensure Capita's multi-year transformation is understood and clearly communicated to all stakeholders • Embed new corporate purpose, and refreshed values and behaviours
13. Transformation Making the business fit for the future Assessment at year-end **This was a new risk in 2018 due to the scale and pace of the company transformation underway.**	• A more complex business that is unmanageable • Loss of revenues, profits and/or cash flows • Money spent on transformation is wasted • Business is not fit for the future	**Mitigating actions in 2018:** • 'Blueprint' used to ensure consistent approach to operating model across divisions and functions • Chief Transformation Officer appointed • Focus by Executive Committee on risks • Simplification is the way to strengthen the business **Future actions:** • Complete operating model work • Embed the new model

Key: Critical, Uncomfortable

Emerging risk

Impact of Brexit

While the details around the UK's scheduled departure from the EU remained unclear at the time of writing this Annual Report, Capita has continued to review a range of Brexit scenarios and conducted contingency planning. We have taken steps to manage risk in specific areas and are not aware of any material company-specific impacts from Brexit. We are therefore confident that there will be no significant disruption to the services we offer clients.

Capita employs a significant number of EU nationals, and we want to see maximum certainty for our valued employees and colleagues. We are providing guidance and support for those who are applying for settled status in the UK.

Our preparations for any Brexit scenario, including a 'no deal' exit, include safeguards to ensure resilience around potential changes to data protection rules, procurement rules and immigration requirements. As with other companies, Capita would be subject to any deterioration in the economy occurring as a result of Brexit.

We continue to monitor political developments and consider scenarios as the Government's plans and positions develop.

Other risk factors

Protecting our information and data

Protecting the data of our clients, our company and our people is one of the most fundamental and important responsibilities we have. Our Data Protection and Information Security Policies, Standards and Procedures ensure we treat personal information correctly, in accordance with the law and best practice. When we process personal information (including sensitive personal information), we ensure that we comply with these policies, standards and procedures including its collection, storage, use, retention, transfer, deletion and safe destruction.

In order to ensure compliance with the Data Protection Act 2018 (and General Data Protection Regulations), we have implemented a comprehensive programme, including a network of trained privacy professionals who provide expert help and assistance for anyone handling data within our business or on behalf of our clients.

We continue to raise awareness of the importance of data protection and privacy through our mandatory data protection training and ongoing training programmes, in particular the Think Privacy; Think Security campaigns.

Cyber-attacks

Cyber-attacks continue to negatively impact all industry sectors.

Capita fully recognises the persistent cyber-threat posed by criminals and nation-states, and that cyber-attacks are increasing both in their number and in their sophistication.

The Board remains focused on ensuring our businesses and systems are resilient against the latest cyber-threats and have instigated a cyber-resilience programme. Supported by external and internal cybersecurity subject matter experts, the cyber-resilience programme liaises with our businesses and IT providers to implement and maintain robust preventative security controls throughout Capita's IT estate. As a managed service provider, we recognise our role within our client's supply chain, and the increasing cyber-threat posed by nation-state resourced actors targeting our clients.

We continue to work closely with UK Government agencies and our partner organisations, to help protect our clients' digital assets and services, and the key parts of the national information infrastructure with which we are entrusted.

Viability statement

The transformation plan described earlier in the strategic report underpins the viability of the Group and parent company.

As noted on page 65, for the going concern assessment, the Board has considered base-case projections for the period to 31 December 2020 which are derived from the 2019–2020 business plans. Provision C.2.2 of the 2016 revised Code requires the Directors to also consider the viability of the Group over a longer-term period and for this viability statement the Board has assessed the prospects for the Group using the base-case forecasts over an extended period to 31 December 2021. The Board considers this three-year period to be appropriate, as there is sufficient clarity to consider the business prospects and the base case over this period provides a foundation to stress test against severe but plausible downside scenarios.

In assessing the going concern assumption, the Board has undertaken a robust assessment of the forecast out-turns and assessed identified downside risks on a probability-weighted basis and mitigating actions. The downside risks include a number of severe but plausible scenarios, also on a probability-weighted basis, incorporating under-performance against the business plan, execution risk associated with the transformation plan and unexpected cash outflows. These financial downsides (Scenario 1) capture political, economic and reputation risks.

In considering the viability of the Group, the Board has extended the financial downside scenarios above to include stress testing and sensitivity analysis of the impact of various severe but plausible potential scenarios involving the threats posed by other principal risks. These have included (but are not limited to) scenarios in respect of:

Scenario 2: An information security breach – a significant loss of data or release of a significant amount of sensitive personal client data. The Board has considered, among other items, the potential impact to cash and profits arising from potential penalties and fines, compensation payments and negative impacts from such reputational damage in terms of an inability to win new business or retain existing contracts.

Scenario 3: Regulatory risks – serious breach of FCA or other regulators rules impacting large number of clients and/or causing systematic damage to financial services system; and failure of financial crime controls around anti-money laundering (AML) assessment, due diligence and sanction assessment leading to a significant AML incident and investigation. The Board has considered among other items potential fines, and any actions taken that may prohibit or suspend the Group from operating within certain regulatory regimes.

Scenario 4: The efficacy of IT and infrastructure systems and controls – a significant IT incident causes failure to key systems for hosted services to major clients with failure of recover solution causing a 'black-out' for up to two weeks. The Board has considered among other items any contractual penalties that may arise, capital costs required to address any immediate infrastructure improvements, potential contract terminations and the negative impact on new contract wins.

Scenario 5: A wider economic impact on Group financial stability – uncertainty of earnings as a result of a change in the UK Government to a party with a strong mandate for radical policy change and/or the UK's withdrawal from the European Union. The Board has considered among other items new barriers to entry, changes to corporate taxation, and the termination of public sector contracts.

The Board has conducted stress tests against each individual scenario in order to test the resilience of the Group taking into account the efficacy of possible mitigating actions.

In addition to testing individual scenarios, the Board also considered the impact of a combination of the scenarios, again using a probability weighting, over the assessment period. This was in order to stress test an aggregation of severe but plausible risks occurring that would represent the greatest potential financial impact but in the short-term and longer-term viability period.

The Directors considered mitigating factors that could be employed when reviewing these scenarios and the effectiveness of the actions at their disposal, which were applied to the models. An example of the actions identified included adjusting the Group's investment in discretionary and maintenance capital projects, having due regard to the need to ensure the integrity of the Group's IT systems is not compromised nor the security of the data held therein; and further reduction in discretionary operating expenditure. The Board also considered the Group's current financing arrangements and potential ability to replace the revolving credit facility with a bank facility of a size consistent with one of the scenarios modelled, should this be required. The Board was satisfied that this, and other mitigating actions identified, were appropriate in reviewing the impact of the scenarios arising.

Based on this assessment and assuming the successful implementation of the transformation plan, the Directors have a reasonable expectation that the Group and parent company will be able to continue in operation and meet their liabilities as they fall due over the period of their assessment.

The strategic report was approved by the Board and signed on behalf of the Board:

Francesca Todd
Group Company Secretary
13 March 2019

CORPORATE GOVERNANCE

Chairman's report

"Our plan to appoint two employees to the Board is further evidence of our commitment to inclusivity and engagement."

Sir Ian Powell
Chairman

I am pleased to present this report on the work of the Board during 2018, formed of this section (pages 54–63) and the section headed 'Other statutory and regulatory information' (pages 63–68).

Results for 2018

In the Chief Executive Officer's review on pages 8–13 we have detailed the results for the year. It has been a significant year for Capita and the Board and we remain confident that the transformation programme we are pursuing will deliver the right outcomes.

Board activities in 2018

The Board has a standing schedule to meet nine times a year but holds further meetings as required, operating with an open culture. In 2018, the Board has had to deal with many key matters, as it seeks to set the Group on a sustainable path for the future and address historical issues.

A structured approach is taken when setting Board and Committee meetings – they are aligned with the Company's financial calendar. We set an agenda to cover the wide range of matters that are brought to our attention, ensuring each is given appropriate time and focus.

Governance has a key role to play in the culture of the organisation and I believe the Board and senior management changes we have made in 2018 will drive improved governance and performance across the whole of the business. Patrick Butcher was appointed as Chief Financial Officer at the end of 2018 and details of the new Executive Committee are set out below.

Senior management

Capita currently comprises six divisions and we continue to review the structure of our businesses and management to ensure it is appropriate. An Executive Committee, under Jon Lewis's leadership, was formed during the year. This committee brings together the six leaders of the new divisional structure and a number of new functional roles, including chief officers for Corporate Development, Digital, Growth, People, and Transformation, a Chief General Counsel and Director of Corporate Affairs. These new roles include several new hires to Capita. The committee's focus is on improving culture and engagement across the workforce, with the aim of harnessing the collective strength of Capita's talented pool of people across all levels of the organisation. The Board believes that the management team as a whole now have the credibility, knowledge, values and behaviours required to drive Capita's business forward and achieve success across its chosen markets. Further detail about the Executive Committee can be found on pages 58–59.

Engagement and diversity

Our plan to appoint two employees to the Board is further evidence of our commitment to inclusivity and engagement. We received a large number of applications and are following a rigorous selection process, which includes external independent review. The intention is for the successful candidates to be announced shortly and I look forward to welcoming them onto the Board in due course.

Over the last two years, we have brought focus to the diversity agenda at Capita and have made some progress, but not enough. We are fully committed to improving diversity and details of how this is being addressed are included in the strategic report on page 37–38.

As an organisation of more than 63,000 people and one of the UK's largest employers, Capita must recruit, retain, develop and reward its people well, if it is to achieve its goals. Its purpose, culture, values and behaviours have to empower and encourage all of Capita's people to ensure everyone has the opportunity to fulfil their potential, irrespective of background.

Board effectiveness

Corporate governance principles

We continue to pursue the highest standards of corporate governance and business practice, including the principles embodied in the UK Corporate Governance Code 2016 (2016 Code), which permeate all aspects of the Board's activity.

In particular, the principles in the 2016 Code relating to leadership and effectiveness are addressed through a strong and experienced group of independent Non-Executive Directors together with the ongoing division of responsibility between running the Board and running Capita's business. Furthermore, the Board's effectiveness was subject to an external evaluation in 2018, details of which are set out below.

The 2016 Code principles relating to accountability and remuneration are addressed through the work of the Audit and Risk Committee and Remuneration Committee respectively and those committee reports are set out on pages 71–79 and 80–98. The principles in the 2016 Code regarding relations with shareholders are addressed through the ongoing programme of shareholder engagement activity, a summary of which can be found on pages 62–63.

In July 2018, the Financial Reporting Council (FRC) refreshed and updated the 2016 Code and published the UK Corporate Governance Code 2018 (2018 Code) which will apply to Capita in respect of the 2019 financial year. Where appropriate, disclosures relating to the 2018 Code are included in this Annual Report and Accounts 2018.

Board evaluation

Board evaluation is undertaken annually, with external evaluation every three years. In late 2018, an external evaluation of the Board and its committees was undertaken by Independent Board Evaluation, who have no other relationship with Capita. This comprised a series of interviews with Board members and key stakeholders who regularly interact with the Board, including Executive Committee members and senior management, auditors, brokers, external legal counsel and the Group Company Secretary. The findings of the review were presented to the Board. Reports on committees were presented to the committee chairmen and circulated to the Board.

The review took place against a backdrop of considerable change, both in terms of Board composition and activity. During 2018, new appointments strengthened the Board and Executive Committee, including the appointment of Patrick Butcher as Chief Financial Officer and Claire Chapman as Chief General Counsel. As part of developing a new strategy for Capita, the Board led the delivery of a rights issue in April 2018. The review also included a report on the performance of individual directors and of the Chairman.

The evaluation concluded that, overall, the Board had performed well through the period, demonstrating good leadership, an ability to support and challenge, with a high level of engagement and commitment.

The evaluation has given the Board an opportunity to review its practices, and set a base-line standard from which to progress and measure going forward.

A separate meeting of the Board took place to discuss fully the evaluation and its findings, focusing on the following themes and developing actions for 2019:

- Longer-term vision and strategy – extending the time-frame of strategic discussion and emerging risks during the year, with an annual deep focus on strategy and risk appetite.
- Improve the Board's understanding of employees' views – through the appointment of Employee Directors, site visits and working with the Chief People Officer on top talent, succession planning and diversity.
- Succession planning – a skills and capabilities matrix would be developed by the Nomination Committee to help enhance Board succession planning.
- Board programme – to ensure the Board programme and agendas facilitate appropriate exposure to Capita's business and senior management.

Risk & Compliance and Internal Audit

On pages 44–51 of the strategic report we have described the roles of Group Risk & Compliance and Group Internal Audit together with the risk framework and internal controls for Capita.

In order for the Board to ensure that the strategic direction of Capita is appropriate and has the appropriate risk oversight, numerous meetings are held throughout the year. These include individual meetings between the Chief Risk & Compliance Officer and the Group Internal Audit Director with the Chairman of the Audit and Risk Committee, as well as normal scheduled meetings. Risks are identified and categorised in a number of ways and are prioritised and delegated in accordance with the risk ratings provided to the risk owner.

Both the Chief Risk & Compliance Officer and the Group Internal Audit Director report to the Chief Financial Officer and independently to the Audit and Risk Committee. Both report respectively on the internal audit programme and risk and compliance management activities and on the internal audit programme across Capita. They have access to all members of the Board and hold regular meetings with the Executive Directors and meet with the Audit and Risk Committee Chairman at least every quarter.

Directors

The Directors of the Company currently in office are listed on pages 56–57.

All members of the Board will stand for re-election (Patrick Butcher for election) at the forthcoming AGM. All Board members have received a formal performance evaluation, as described, which demonstrates that each Director continues to be effective and committed to the role.

John Cresswell has informed the Board of his intention to step down as Chairman of the Remuneration Committee, but he will remain on the Board as a Non-Executive Director. John took up a new CEO role in 2018 and feels he can no longer provide Capita with the time and attention the Committee Chairman's role requires. He will continue to chair the Committee until a replacement is appointed.

The following pages in this section consist of our corporate governance and remuneration reports. I hope that you will find these and the entire Annual Report and Accounts informative. The Board will be happy to receive any feedback you may have.

Sir Ian Powell
Chairman
13 March 2019

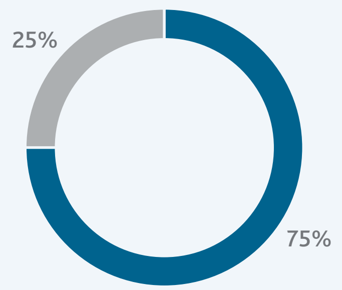
Board members

At 31 December 2018, the Board comprised seven Directors, made up of the Chairman, Chief Executive Officer and five independent Non-Executive Directors.

We have an experienced team in place to support our strategy and to meet the opportunities and challenges that the Group faces. As the Group develops, we will regularly review the Board composition to ensure it meets the needs of the business.

At 31 December 2018, we had two female Directors and five male Directors. By the end of January 2019, we had two female and six male Directors, following the appointment of Patrick Butcher as Chief Financial Officer. It is expected that diversity at both Board and senior leadership level will continue to be a focus of the Board.

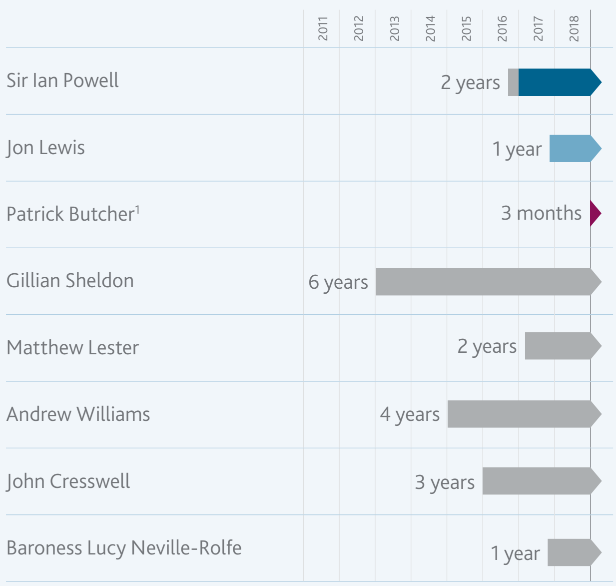
Board diversity



● Male
● Female

Gender split at 1 January 2019

Board Directors: length of tenure



1 Joined the Board on 1 January 2019

Key

Chairman | CEO | CFO

Non-Executive Director

Chairman

The Chairman is responsible for leadership of the Board and ensuring its effectiveness on all aspects of its role. This includes setting the Board's agenda and ensuring that adequate time is available for discussion of all agenda items, in particular strategic issues. The Chairman should also promote a culture of openness and debate, by facilitating the effective contribution of Non-Executive Directors in particular and ensuring constructive relations between Executive and Non-Executive Directors. The Chairman is responsible for ensuring that the Directors receive accurate, timely and clear information, and should ensure there is effective communication with shareholders.

Sir Ian Powell | N

Chairman

Appointed to Board: September 2016

Independent at appointment: Yes

Key skills and experience: Sir Ian was appointed Non-Executive Director in September 2016 and Chairman in January 2017. He is a chartered accountant and, before retiring in June 2016, was Chairman and Senior Partner of PwC UK for eight years, responsible for leadership and management of PwC UK. He joined PwC in 1977, serving in various roles of increasing responsibility, including Head of Advisory, before being elected Chairman and Senior Partner.

Other current appointments: Chairman of Police Now; trustee of The Old Vic, and of Wellbeing of Women; member of the Development Committee at The National Gallery; board member at London First.

Executive Directors

The Executive Directors are responsible for the day-to-day running of all aspects of the Group's business. This responsibility is different from the Chairman's role in running the Board. The role of Chief Executive Officer is separate from that of Chairman to ensure that no one individual has unfettered powers of decision-making.

Jon Lewis

Chief Executive Officer

Appointed: December 2017

Key skills and experience: Before joining Capita, Jon was Chief Executive Officer of Amec Foster Wheeler, the multinational consultancy, engineering and project management business. Prior to that, he had a 20-year career at Halliburton Company Inc in the United States, one of the world's largest oil field service companies, where he held a number of senior roles, including Senior Vice-President and member of the Halliburton Executive Committee. Jon has a doctorate in geology from the University of Reading, ran a contract research organisation at Heriot-Watt University, and attended the Executive Program at Stanford University Graduate School of Business.

Board responsibilities: Managing and developing Capita's business to achieve the Company's strategic objectives.

External appointments: Board member of Equinor

Patrick Butcher

Chief Financial Officer

Appointed: January 2019

Key skills and experience: Before joining Capita, Patrick was Group Chief Financial Officer at Go-Ahead Group. He is a member of the Institute of Chartered Accountants (South Africa) and has more than 17 years' experience as a finance director at board level in transport and infrastructure companies. He was formerly Group Finance Director of Network Rail, as well as holding finance director roles at English, Welsh and Scottish Railways (now DB Schenker), and London Underground. Patrick has extensive experience from working as a management consultant and auditor for Deloitte LLP. He is a former member of the British Transport Police Authority.

Board responsibilities: Overall control and responsibility for all financial aspects of the business's strategy.

Additional responsibilities: Property; Procurement; Commercial relationships and Supplier relationships.

External appointments: None.

Non-Executive Directors

The Non-Executive Directors should constructively challenge and help develop proposals on strategy. They should scrutinise the performance of management in meeting agreed goals and objectives, and monitor the reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of Executive Directors and have a prime role in appointing and, where necessary, removing Executive Directors, and in succession planning.

Gillian Sheldon | ANR

Senior Independent Director

Appointed: September 2012

Independent: Yes

Key skills and experience: Gillian was appointed to the Board in September 2012, before being made Senior Independent Director in January 2013. She is a senior adviser in Credit Suisse UK's investment banking division where she has gained substantial experience of advising boards across a wide range of complex situations and transactions. Prior to joining Credit Suisse, Gillian worked for seven years at NM Rothschild & Sons.

Other current appointments: Senior adviser at Credit Suisse; trustee of BBC Children in Need; member of Corporate Advisory Board of the Royal Academy of Arts.

Matthew Lester | ANR

Non-Executive Director

Appointed: March 2017

Independent: Yes

Key skills and experience: Matthew is a chartered accountant with over 20 years' experience in senior finance roles. He was Group Chief Financial Officer of Royal Mail plc from November 2010 to July 2017. Matthew has also served as Group Chief Financial Officer for ICAP plc from May 2006 to November 2010. Before this, he held senior roles at Diageo plc and Kleinwort Benson.

Other current appointments: Non-executive director of Man Group plc and Barclays plc.

John Cresswell | ANR

Non-Executive Director

Appointed: November 2015

Independent: Yes

Key skills and experience: John is Chief Executive Officer of Bibby Line Group Limited. He has substantial experience leading, growing and advising media and broadcast organisations at CEO and executive director levels, having worked in the technology, media and telecommunications sector for 25 years. John is a chartered accountant and attended the Advanced Management Program at Harvard Business School. Most recently, he served for four-and-a-half years as CEO of Arqiva. Before that, he held a number of executive director roles on the board of ITV plc, and was formerly a director of Liverpool Football and Athletic Grounds plc and of Ambassador Theatre Group.

Other current appointments: Chief Executive Officer of Bibby Line Group Limited.

Andrew Williams | ANR

Non-Executive Director

Appointed: January 2015

Independent: Yes

Key skills and experience: Andrew has been Chief Executive of Halma plc, a leading specialist in safety, health and environmental technologies since 2005. He started his career at Halma in 1994 as manufacturing director of a subsidiary company and went on to hold a wide range of senior management positions across the group. Andrew is a chartered engineer and a production engineering graduate of Birmingham University. He attended the Advanced Management Program at Wharton Business School, University of Pennsylvania, in 2004.

Other current appointments: Chief Executive of Halma plc.

Baroness Neville-Rolfe DBE CMG | ANR

Non-Executive Director

Appointed: December 2017

Independent: Yes

Key skills and experience: Baroness (Lucy) Neville-Rolfe has been a member of the House of Lords since 2013, and served between 2014 and 2017 as a Government minister in the Business and Culture departments, and as Commercial Secretary to the Treasury. She has a senior background in international retail, governance, legal and regulatory issues, and communications. She worked at Tesco plc from 1997 to 2013, serving on the board from 2006. Before joining Tesco, Lucy was a civil servant, serving in the Prime Minister's Policy Unit at Number 10 between 1992 and 1994, and finally as Director of the Deregulation Unit. Her non-executive directorships have included ITV plc and Metro AG.

Other current appointments: Chairman of Assured Food Standards; non-executive director of Secure Trust Bank plc, Thomson Reuters Founders Share Company, and Health Data Research UK; and governor of London Business School.

Key to committees

A Audit and Risk   N Nomination   R Remuneration   ANR Committee chair

Changes in the year

Nick Greatorex

Chief Financial Officer

Appointed to Board: March 2015

Stepped down from Board: September 2018

Chris Sellers

Group Business Development Director

Appointed to Board: January 2017

Stepped down from Board: January 2018

Executive Committee

Capita's Executive Committee is chaired by Jon Lewis, the Company's Chief Executive Officer, and comprises 15 executive officers and functional heads, who are entirely accountable for their particular division or function.

The divisions are aligned around our key growth markets: Software, People Solutions, Customer Management, Government Services and IT & Networks. Alongside them sits our sixth division, Specialist Services. All are aligned with Capita's overall strategy – to simplify, strengthen and succeed.

1. Patrick Butcher

Chief Financial Officer

Patrick, who joined Capita at the start of 2019, is responsible for developing and implementing financial strategy and policy to support the sustainable growth of the business in a stable and predictable way.

2. Garry Dryburgh

Chief Transformation Officer

Garry is responsible for developing, orchestrating and communicating our multi-year transformation programme.

3. Jim Vincent

Executive Officer, Specialist Services

Jim leads the division which comprises a portfolio of unique businesses and commercial ventures, providing a diverse range of services to private and public sector clients.

4. Ismail Amla

Chief Growth Officer

Ismail is responsible for supporting our transformation and organic growth plans, including the simplification of business development and marketing, and driving change in the sales model.

5. Chris Baker

Executive Officer, Software

Chris leads this division which comprises a group of diverse businesses, creating digital and software solutions to make our clients' businesses more efficient and cost-effective.

6. Mike Barnard

Executive Officer, Customer Management

Mike leads the division which provides market-leading contact centre, data, analytics and digital services. He is also responsible for support operations across multiple sectors.

7. Katja Hall

Director of Corporate Affairs

Katja is responsible for both internal and external communications, including employee engagement, reputation strategy, media relations, and public affairs and policy.

8. Rupert Green
Chief Corporate Development Officer
Rupert is responsible for our strategy development and execution, investor relations, and for mergers, acquisitions and divestments.

9. Serge Taborin
Chief Digital Officer
Serge is responsible for developing our technology offering, driving innovation and identifying how digital technologies will shape future customer propositions and business models.

10. Jon Lewis
Chief Executive Officer
Jon is responsible for the overall management and development of Capita, to achieve the Company's strategic objectives – and return the business to organic growth and sustainable free cash flow in 2020.

11. Erika Bannerman
Executive Officer, People Solutions
Erika leads the division and has responsibility for a portfolio of market-leading HR businesses across resourcing, learning services, pensions administration and employee benefits.

12. Will Serle
Chief People Officer
Will is responsible for the delivery of the HR and people strategy, supporting and advising the organisation to evolve Capita's culture and ways of working for all our employees.

13. Joe Hemming
Executive Officer, IT & Networks
Joe leads the division which provides market-leading IT outsourcing and network solutions to key clients, including within central and local government, and in the education and healthcare sectors.

14. Claire Chapman
Chief General Counsel
Claire is responsible for providing expert and strategic legal advice to the leadership team and the Board, with a focus on legal and regulatory risk management, M&A, corporate projects, governance and contracts.

15. Patrick Elliott
Interim Executive Officer, Government Services
Patrick leads the division which delivers technology-enabled business services for a broad spectrum of central government, local authority, healthcare and other public sector clients.

Corporate governance statement

Corporate Governance Code

Capita plc and its subsidiaries (the Group) remain committed to maintaining high standards of corporate governance. The UK Corporate Governance Code 2016 (the Code) applies to accounting periods beginning on or after 17 June 2016. Throughout the accounting period to which this report relates, the Company complied with all relevant provisions set out in sections A to E of the Code. The UK Corporate Governance Code 2018 (the 2018 Code) was published in July 2018 and applies to accounting periods beginning on or after 1 January 2019. Where appropriate, additional voluntary disclosures have been made in compliance with the 2018 Code. Copies of the Code and the 2018 Code are available from the Financial Reporting Council's website www.frc.org.uk.

Board changes during the year

The following changes to the composition of the Board took place during the year:

Name	Date	Position
Chris Sellers	23 January 2018	Stepped down as Group Business Development Director
Nick Greatorex	30 September 2018	Stepped down as Chief Financial Officer

Further information on changes to the Board is set out in the Nomination Committee report on page 70. Patrick Butcher, Chief Financial Officer, was appointed as a Director on 1 January 2019.

Board composition

The composition of the Board at 31 December 2018 and from 1 January 2019 is shown below:

	Executive Directors	Independent Non-Executive Directors
At 31 December 2018	Jon Lewis	Sir Ian Powell[1] Gillian Sheldon Matthew Lester John Cresswell Andrew Williams Baroness Lucy Neville-Rolfe
At 1 January 2019	Jon Lewis Patrick Butcher	Sir Ian Powell[1] Gillian Sheldon Matthew Lester John Cresswell Andrew Williams Baroness Lucy Neville-Rolfe

1 Independent on appointment in accordance with the 2016 Code.

Board meetings and attendance

During 2018, the Board held nine scheduled meetings, excluding ad hoc meetings. Attendance of the Directors is shown below; the maximum number of meetings a Director could attend is in brackets.

	Board meetings
Sir Ian Powell	9(9)
Jon Lewis	9(9)
Gillian Sheldon	9(9)
Matthew Lester	9(9)
John Cresswell	8(9)
Andrew Williams	9(9)
Baroness Lucy Neville-Rolfe	9(9)
Nick Greatorex[1]	6(7)
Chris Sellers[2]	0

1 Nick Greatorex stepped down from the Board on 30 September 2018.
2 Chris Sellers stepped down from the Board on 23 January 2018.

Additional ad hoc meetings were held in the first half of 2018 in connection with the rights issue and various related matters. Meetings held outside the normal schedule need to be flexible and are often held by telephone.

Any Director's absence from Board meetings was previously agreed with the Chairman of the Board or the Chief Executive Officer.

During 2018, the following formal Director meetings took place:

- The Chairman held one-to-one individual review sessions with each Executive Director and each Non-Executive Director.
- The Non-Executive Directors met without Executive Directors.
- The Non-Executive Directors met with just the Chief Executive Officer.
- The Non-Executive Directors met without the Chairman, led by the Senior Independent Director.

Board leadership

There is a clear division of responsibility between the running of the Board by Sir Ian Powell as Chairman and responsibility for the running of the Group's business by Jon Lewis as CEO.

During the year, Sir Ian as Chairman and Gillian Sheldon as Senior Independent Director held meetings comprising solely the Non-Executive Directors. Gillian also met with the Non-Executive Directors without Sir Ian. Both Sir Ian and Gillian are available to meet with significant shareholders when requested.

Governance and strategy

The Group recognises the contribution made by good governance to the Company's success and changes made at both Board and Executive Committee level demonstrate the importance of embedding the right structures with the right people to deliver the Group's strategy.

Role of the Board

The Board

Role of the Board

To promote Capita's long-term sustainable success, generating value for shareholders and contributing to wider society.

Matters reserved for the Board

- Strategy and management
- Structure and capital
- Financial reporting
- Internal controls
- Major contracts
- Shareholder communication
- Board membership

Nomination Committee

- Board and committee composition
- Succession planning
- Diversity
- People strategy

Read more on page 70.

Audit and Risk Committee

- External audit
- Financial reporting
- Risk management and internal controls
- Internal audit

Read more on pages 71 to 79.

Remuneration Committee

- Remuneration policy
- Remuneration principles
- Incentive design and setting of targets
- Executive and senior management remuneration

Read more on pages 80 to 98.

In addition to their statutory duties, the Directors must ensure that the Board focuses effectively on all its accountabilities.

Section 172 of the Companies Act 2006 requires Directors to act in a way they consider, in good faith, would be most likely to promote the success of the Company for the benefit of shareholders as a whole. In doing so, the Directors must have regard (among other matters) to:

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

The Board determines the strategic objectives and policies of the Group to best support the delivery of long-term value, providing overall strategic direction within an appropriate framework of rewards, incentives and controls. The Board is collectively responsible for the success of the Company: the Executive Directors are directly responsible for running the business operations; and the Non-Executive Directors are responsible for bringing independent judgement and scrutiny to decisions taken by the Board. The Non-Executive Directors must satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust. Following presentations by executive and divisional management and a disciplined process of review and challenge by the Board, clear decisions on policy or strategy are adopted, and the executive management are fully empowered to implement those decisions.

Stakeholder interests and the matters listed above are factored into all Board discussions and decisions.

Corporate governance statement continued

Board independence

Non-Executive Directors are required to be independent in character and judgement. All relationships that may interfere materially with this judgement are disclosed as required under the conflicts of interest policy. The Board has determined that all the Non-Executive Directors who served during the year were independent and that, before and upon appointment as Chairman, Sir Ian Powell met the criteria of independence as outlined in the Code.

The Board does not believe that a Non-Executive's tenure interferes materially with their ability to act in the best interests of the Group. The Board also believes that each of the Non-Executives has retained independence of character and judgement and has not formed associations with management or others that may compromise their ability to exercise independent judgement or act in the best interests of the Group.

The Board is satisfied that no conflict of interest exists for any Director. This matter is a standing agenda item at Board meetings.

Matters reserved for the Board

A formal schedule of matters reserved for the Board has been adopted and these include, but are not limited to:

- Strategy and management, including responsibility for the overall leadership of the Group, setting the Group's values and standards, and overview of the Group's operational management.
- Structure and capital, including changes relating to the Group's capital structure and major changes to the Group's corporate structure, including acquisitions and disposals, and changes to the Group's management and control structure.
- Financial reporting, including the approval of the Annual Report and Accounts, half-yearly report, trading statements, preliminary announcement for the final results and dividend, treasury and accounting policies.
- Internal controls, ensuring that the Group manages risk effectively by approving its risk appetite and monitoring aggregate risk exposures.
- Contracts, including approval of all major capital projects and major investments, including the acquisition or disposal of interests of more than 3% in the voting shares of any company or the making of any takeover offer.
- Ensuring satisfactory communication with shareholders.
- Board membership and other appointments, including changes to the structure, size and composition of the Board, and succession planning for the Board and senior management.

Board of Directors' inductions and training

Following appointment to the Board, all new Directors receive an induction tailored to their individual requirements. They are encouraged to meet and be briefed on the roles of key people across the Group and have open access to all business areas and employees to build up an appropriate level of knowledge of the business that extends beyond formal papers and presentations to the Board. All Directors have received an appropriate induction for their roles within Capita, including some or all of the following:

- The nature of the Group, its business, markets and relationships.
- Meetings with the external auditor, lawyers, brokers and relevant operational and functional senior management.
- Board procedures, including meeting protocols, committee activities and terms of reference, and matters reserved for the Board.
- Overviews of the business via Monthly Performance Review (MPR) reports.
- The Group approach to risk management.

Ongoing training and briefings are also given to all Directors, including external courses as required.

Group Company Secretary

All Board members have access to independent advice on any matters relating to their responsibilities as Directors and as members of the various committees of the Board at the Group's expense.

Francesca Todd, as Group Company Secretary, is available to all Directors and is responsible for ensuring that all Board procedures are complied with.

The Group Company Secretary has direct access and responsibility to the chairmen of the standing committees and open access to all the Directors. The Group Company Secretary has been appointed as Secretary to the Audit and Risk, Remuneration, and Nomination committees to ensure that there are no conflicts of interest. The Group Company Secretary meets regularly with the Chairman of the Board, the chairmen of the Audit and Risk, and Remuneration committees, and briefs them on areas of governance and committee requirements.

During the year, a new role of Chief General Counsel was created to oversee the Group's legal and regulatory capability, as a separate function from the role of Group Company Secretary. The two roles collaborate closely but, in order to avoid a conflict of interest, the Group Company Secretary is solely responsible for Board and Group governance.

Shareholder engagement

There is an active engagement programme with the Company's investors. The Executive Directors meet regularly with institutional investors to discuss and obtain feedback on the business, performance, strategy and corporate governance, and address any issues of concern. This is undertaken through a combination of roadshows, group or one-to-one meetings and attendance at Support Services conferences. The Chairman and Non-Executive Directors are also available to meet with existing institutional shareholders throughout the year.

The Investor Relations team has day-to-day responsibility for managing investor communications and always acts in close consultation with the Board. All members of the Board, including the Non-Executive Directors, receive a report on any significant discussions with shareholders and anonymous feedback that follows the annual and half-yearly presentations to investment analysts and institutional investors. All analyst reports concerning Capita are circulated to the Directors and the Board is kept informed of changes in the share register.

Following the rights issue in April 2018, the Chief Executive Officer, Chief Financial Officer, Head of Investor Relations and Chief Corporate Development Officer engaged extensively with existing and potential institutional investors, ensuring all investors fully understood the new strategy, the transformation programme and the planned use of the rights issue proceeds.

In July 2018, the Chairman of the Remuneration Committee consulted with Capita's top 30 investors on proposed targets and measures for the 2018 long-term incentive plan. Further details are set out in the Directors' remuneration report.

In September 2018, the Chairman, Chairman of the Remuneration Committee and Senior Independent Director held a governance forum attended by the Company's top 30 investors. This enabled Capita's largest shareholders to engage directly with Non-Executive Directors on the Company's strategy, transformation programme, employee Board directors and wider corporate governance issues.

2018 calendar of investor events

January	Trading update
April	Rights issue 2017 full-year results UK and US investor roadshows
June	Annual general meeting
August	2018 half-year results UK investor roadshow
September	US investor roadshow Governance forum
November	JP Morgan 'Best of British' investor conference

Shareholder meetings

All shareholders are encouraged to attend the annual general meeting (AGM) and information for shareholders is available on the Company's website www.capita.com. The Non-Executive Directors are available to meet with shareholders to understand their views more fully. The Chairman is available to the significant shareholders of Capita. Directors, including chairmen of the various committees, are present at the AGM to answer any questions. The Board particularly encourages communication with, and the participation of, private investors at the AGM.

Shareholder communications

In addition to attendance at the AGM, shareholders can also access up-to-date information through the Group's website at www.capita.com. A telephone helpline, 0871 664 0300, provides a contact point directly to the Group's registrars. Lines are open between 9.00am and 5.30pm, Monday to Friday, excluding public holidays in England and Wales. Private shareholders can also raise queries by email to enquiries@linkgroup.co.uk.

Remuneration Committee

Details of the Remuneration Committee and its activities are given in the Directors' remuneration report on pages 80–98.

Risk management and internal control

The Board monitors the Company's risk management and internal control systems and carries out an annual review of their effectiveness. The Audit and Risk Committee report contains further details. The monitoring and review includes all material controls, including financial, operational and compliance controls. This process is regularly reviewed by the Board. The Group's key internal control procedures are fully documented within the strategic report on pages 44–45.

Furthermore, through the operation of the risk governance process, the Directors confirm, for the purposes of provision C.2.1 of the Code, 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. A description of those risks, together with how they are being managed or mitigated, is set out on pages 46–51.

Other statutory and regulatory information

Strategic report

The Company is required to prepare a fair review of the business of the Group during the financial year ended 31 December 2018 and of the position of the Group at the end of the financial year, and a description of the principal risks and uncertainties facing the Group (known as a 'strategic report'). The purpose of the strategic report is to enable shareholders to assess how the Directors have performed their duty under Section 172 of the Companies Act 2006 (duty to promote the success of the Company). The information that fulfils the requirements of the strategic report can be found on pages 1–52. Details of the Group's business goals, strategy and model are on page 4.

Corporate governance report

The corporate governance statement as required by Rule 7.2.1 of the Financial Conduct Authority's Disclosure Guidance and Transparency Rules (DTRs) is set out on pages 60–67.

Management report

For the purposes of Rule 4.1.5R(2) and Rule 4.1.8R of the DTRs, this Directors' report and the strategic report on pages 1–52 comprise the management report.

Post-balance sheet events

There have been no material events since the balance sheet date.

Election to apply FRS 101 – Reduced Disclosure Framework

The parent company continues to apply UK GAAP in the preparation of its individual financial statements in accordance with FRS 101 and these are contained on pages 178–195. FRS 101 applies IFRS as adopted by the European Union with certain disclosure exemptions. No objections have been received from shareholders.

Appointment, re-appointment and removal of Directors

Directors are appointed and may be removed in accordance with the Articles of Association of the Company and the provisions of the Companies Act 2006.

All Directors are subject to election at the first AGM after their appointment and, in accordance with Provision 18 of the 2018 Code, to annual re-election thereafter. A resolution to re-elect each Director will therefore be proposed at the AGM on 14 May 2019.

No person, other than a Director retiring at the meeting, shall be appointed or re-appointed a Director of the Company at any general meeting unless he/she is recommended by the Directors.

No person, other than a Director retiring at a general meeting as set out above, shall be appointed or re-appointed unless between seven and 35 days' notice, executed by a member qualified to vote on the appointment or re-appointment, has been given to the Company of the intention to propose that person for appointment or re-appointment, together with notice executed by that person of his/her willingness to be appointed or re-appointed.

Group activities

Capita is one of the UK's leading providers of digitally-enabled business services and software, with a growing international operation and sales focus. We seek to solve the complex challenges of clients, enhancing the use of technology and data, increasing productivity, and improving customer and public services. Our portfolio, delivered from six divisions, comprises specialist functions of sector-specific software, digitally-enabled business process management, IT and networks services, customer services, HR, and specialist business support services. We aim to create better outcomes for all our stakeholders, and add value to the economies and communities we serve.

A review of the development of the Group and its business activities during the year is contained in the strategic report on pages 1–52. The operational and financial performance of our divisions are detailed on pages 21–33.

Results and dividends

The Group's reported profit before tax amounted to £272.6m (2017 loss: £513.1m). As previously announced, the Directors do not recommend the payment of a final dividend (2017: nil). The total dividend for the year was nil (2017: 11.1p per share). The employee benefit trust, which holds shares for the purpose of satisfying employee share scheme awards, has waived its right to receive future dividends on shares held within the trust.

Corporate governance statement continued

Conflicts of interest

Under the Companies Act 2006, Directors are under an obligation to avoid situations in which their interests can or do conflict, or may possibly conflict, with those of the Company. A policy and procedures are in place for identifying, disclosing, evaluating and managing conflicts so that Board decisions are not compromised by a conflicted Director. The Company's Articles of Association give the Board power to authorise matters that give rise to actual or potential conflicts. Procedures are reviewed annually to ensure they are operating effectively.

No other material conflicts of interest have been declared. All conflicts of interest are reviewed annually by the Board and included in year-end attestations by the Directors. None of the Directors of the Company has a material interest in any contract with the Company or its subsidiary undertakings, other than their contracts of employment.

Prior to his resignation, the Board had authorised Nick Greatorex's conflict as a trustee of the Capita Pension and Life Assurance Scheme and gave specific guidance on this conflict going forward. Nick Greatorex did not participate in the discussion or vote on the guidance given.

Major shareholders

At 31 December 2018, the Company had received notifications in accordance with the Disclosure Guidance and Transparency Rules (DTRs) that the following were interested in the Company's shares:

Shareholder	Number of shares	% of voting rights at 31 December 2018	Number of shares direct	Number of shares indirect
Veritas Asset Management LLP[1]	199,998,295	11.99	—	199,998,295
Invesco Ltd	186,602,551	11.18	—	186,602,551
Investec Asset Management Ltd	149,745,521	8.98	—	149,745,521
RWC Asset Management LLP	124,238,394	7.45	—	124,238,394
Schroder Investment Management	104,619,507	6.27	—	104,619,507
Woodford Investment Management LLP	93,362,659	5.60	93,362,659	—
Coltrane Asset Management, L.P	82,388,589	4.94	5,140,000	77,248,589
BlackRock, Inc.	73,282,516	4.39	—	73,282,516
Marathon Asset Management LLP	66,623,803	3.99	—	66,623,803
Veritas Funds PLC	55,077,146	3.30	—	55,077,146
Vanguard Group	53,669,912	3.22	53,669,912	—
Jupiter Asset Management	53,335,560	3.20	—	53,335,560

1 This includes the holding of Veritas Funds PLC.

At 5 March 2019, the Company had received notifications in accordance with the DTRs that the following were interested in the Company's shares:

Shareholder	Number of shares	% of voting rights at 5 March 2019	Number of shares direct	Number of shares indirect
Veritas Asset Management LLP[1]	192,533,863	11.54		192,533,863
Invesco Ltd	191,409,106	11.47		191,409,106
Investec Asset Management Ltd	153,805,729	9.22		153,805,729
RWC Asset Management LLP	127,012,876	7.61	127,012,876	
Schroder Investment Management	101,030,829	6.06		101,030,829
Woodford Investment Management LLP	93,562,659	5.60	93,562,659	
Coltrane Asset Management, L.P	82,388,589	4.94	5,140,000	77,248,589
BlackRock, Inc.	74,230,358	4.45		74,230,358
Marathon Asset Management LLP	64,756,810	3.88		64,756,810
Veritas Funds PLC	55,009,900	3.30		55,009,900
Vanguard Group	54,711,874	3.28	54,711,874	
Norges Bank Investment Management	54,273,873	3.25	54,273,873	
Jupiter Asset Management	53,573,060	3.21		53,573,060

1 This includes the holding of Veritas Funds PLC.

Directors' interests

Details of Directors' interests in the share capital of the Company are listed on page 95.

Rights issue

During the year the Company undertook a three for two rights issue at 70p per new share to raise £701m which was fully underwritten by Citigroup Global Markets Limited and Goldman Sachs International. The majority of shareholders (approximately 97.25%) took up their rights and subscribers were procured for the remaining 2.75%.

Share capital

At 7 March 2019, 1,671,273,523 ordinary shares of 2 1/15p each were in issue, fully paid up and quoted on the London Stock Exchange. There are 2,858,331 shares held in treasury (representing 0.17% of total issued share capital) and the total number of voting shares is 1,668,415,192. During the year ended 31 December 2018, 1,001,032,281 new ordinary shares were issued in connection with the rights issue; options exercised pursuant to the Company's share schemes were satisfied by the transfer of shares from treasury (28,057 shares) and from the Employee Benefit Trust (32,367 shares). No shares have been allotted under the Company's share option schemes since the end of the financial year to the date of this report. Of the total issued share capital, 12,030,742 shares (representing 0.72%) are held within the Employee Benefit Trust used for satisfying employee share options.

The share price at 31 December 2018 was 112.25p. The highest share price in the year was 428.6p and the lowest was 100.7p. The highest share price in the year does not reflect the dilutive impact of the issue of new ordinary shares in Capita's 3 for 2 rights issue, which would result in an adjusted high share price of 261.36p.

The Company renewed its authority to re-purchase up to 10% of its own issued share capital at the Annual General Meeting in June 2018. During the year, the Company did not purchase any shares (2017: nil).

Viability statement

This statement is detailed in full on page 52.

The Directors have assessed the viability of the Group over the three-year period to 31 December 2021, taking into account the Group's current position and the potential impact of the principal risks set out in the strategic report. Based on this assessment, the Directors have a reasonable expectation that the Group is and will continue to be viable.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the strategic report on pages 1–52. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described on pages 100–104. In addition, note 26 to the financial statements on pages 144–152 includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit risk and liquidity risk.

In determining the appropriate basis of preparation of the financial statements for the year ending 31 December 2018, the Directors are required to consider whether the Group can continue in operational existence for the foreseeable future.

Having taken decisive action to strengthen the balance sheet through the raising of new equity and the disposal of non-core businesses, and undertaking a rigorous assessment of the financial forecast, the Board have concluded that the Group will continue to have adequate financial resources to realise their assets and discharge its liabilities as they fall due.

Accordingly, the Directors have formed the judgement that it is appropriate to prepare these consolidated financial statements on the going concern basis.

Auditor review

The auditor has reviewed the statements regarding going concern (see page 65) and longer-term viability (see page 52) and those parts of the statement of compliance with the Code relating to: (i) Directors' and auditor's responsibilities; (ii) the 'fair, balanced and understandable' statement; (iii) confirmation of robust risk assessment and monitor and review of effectiveness of risk management and internal control systems; and (iv) Audit and Risk Committee composition, role and responsibilities. Further details are in the auditor's report (pages 166–177).

Disabled persons

It is the Group's policy to give full consideration to suitable applications for employment of disabled persons and to ensure that any reasonable adjustments are made to either the workplace or job content to accommodate a person's disabilities. Employees with a disability are eligible to participate in career development opportunities available to all employees and will be supported to do so. Opportunities also exist for employees of the Group who become disabled to continue in their employment with any reasonable adjustments being made or to be retrained for other positions in the Group.

Corporate governance statement continued

Employee development and engagement

In the second half of 2018, Capita launched a plan for the people function which focuses on all 63,000 people within the Group and covers various topics, including development and engagement. This represents a new commitment and a new way of managing our people. A key focus in employee engagement has been on helping our employees understand Capita's purpose and how their role contributes to the overall success of the organisation. Further details about Capita's new purpose, which was launched in January 2019, are on pages 1 and 9. In addition, we worked with over 1,000 employees, at all levels and in various locations worldwide, to bring our values to life, identifying five behaviours for each of the four values that help our employees understand what is expected of them and what they can expect of others. Finally, we launched a series of eight manager commitments which identify key expectations for all our managers, describing our expectations of how they should manage their teams. All of this was launched using a variety of channels, including Yammer, the internal social networking channel, and 'town hall' meetings, which gave an opportunity to listen to our people.

Employee surveys were conducted in 2017 and 2018 allowing us to monitor changes in how our people feel about working for Capita and providing the opportunity to suggest how the employee experience could be improved. We will continue to ask our employees every year, as it is a key method of assessing the impact of the HR plan.

Employees receive corporate news through: internal notice board statements; the employee intranet, Capita Connections; Yammer; and regular email updates on business performance from both divisional Executive Officers and the Executive Directors. Capita Connections enables employees to find out what is happening in the wider Group and to share information within and between business units, and employees are encouraged to contribute news, views and feedback. Capita maintains a strong communications network and employees are encouraged, through its open door policy and 'Ask Jon' portal, to ask questions and discuss with management matters of interest to the employee and subjects affecting day-to-day operations of the Company. The 'Ask Jon' portal was launched in early 2018 and provides a platform for all employees to submit to the CEO their questions and thoughts across a range of different business-related topics and have their questions answered by Jon.

Capita has an established UK employee share purchase plan designed to promote employee share ownership and to give employees the opportunity to participate in the future success of the Company. An international share incentive plan is available to employees in Ireland and Poland.

In keeping with its belief that employees are the Company's most valuable asset, Capita operates employee recognition schemes both at central and divisional level. In addition, the Local Heroes campaign gives our people and senior management the opportunity to celebrate each other and recognise how people across Capita have contributed to the success of the business. Each month, Capita celebrates the individuals who are helping the Group to simplify, strengthen and succeed, be innovative and have a positive effect on our local communities and environment.

Our people plan also has a clear focus on performance and development. This will be driven by the launch of Capita Academy, which will focus on introducing consistent approaches to managing performance and developing our people, while ensuring we recruit and develop for the future by sourcing and developing graduates and apprentices. These activities will ensure we have not only the correct quality of people delivering to our customers, but also an appropriate leadership pipeline for the future. We have already started on this journey, with the pilot of an academy programme focused on equipping managers with the leadership skills and behaviours necessary for success.

Political donations

The Group did not make any political donation or incur any political expenditure during the year (2017: £nil).

Greenhouse gas emissions

Details of the Group's greenhouse gas emissions, including metrics and methodology, are set out on page 42 of the strategic report.

Financial instruments

The Group's financial instruments comprise primarily loan notes, bearer bonds, bank loans, finance leases and overdrafts. The principal purpose of these is to raise funds for the Group's operations. In addition, various other financial instruments such as trade creditors and trade debtors arise directly from its operations. From time to time, the Group also enters into derivative transactions, primarily interest rate swaps, currency swaps and forward exchange contracts, the purpose of which is to manage interest risk and currency risk arising from the Group's operations and its sources of finance.

The main financial risks, to which the Group has exposure, are interest rate risk, liquidity risk, credit risk and foreign currency risk.

The Group borrows in selected currencies at fixed and floating rates of interest and makes use of interest rate swaps and currency swaps to generate the desired currency and interest rate risk profile.

In respect of liquidity risk, the Group aims to maintain a balance between continuity of funding and flexibility through the use of multiple sources of funding with a broad spread of maturities. In respect of credit risk, the Group trades only with recognised, creditworthy third parties. It is the Group's policy that all clients who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debt is not significant.

With respect to credit risk arising from the other financial assets of the Group, such as cash, financial investments and derivative instruments, the Group's exposure is the potential default of the counterparty. The Group manages its operations to avoid any excessive concentration of counterparty risk and takes all reasonable steps to seek assurance that the counterparties can fulfil their obligations.

The Group is not generally exposed to significant foreign currency risk, except in respect of its overseas operations in Europe, India and South Africa, which generate exposure to movements in EUR, CHF, INR and ZAR exchange rates. The Group seeks to mitigate the risk of this exposure by entering forward currency instruments, including non-deliverable forward contracts, to fix the GBP cost of highly probable forecast transactions denominated in INR and ZAR. A proportion of exposures to EUR is mitigated through borrowings in that currency. Further details of the Group's financial instruments can be found in note 26 to the consolidated financial statements on pages 144–152.

Qualifying third-party indemnity provisions for the benefit of Directors

Under the Companies Act 2006, companies are under an obligation to disclose any indemnities which are in force in favour of their directors. The current Articles of Association of the Company contain a provision that enables the Company to indemnify the Directors of the Company in respect of certain liabilities and costs that they might incur in the execution of their duties as Directors. Such provisions have been in force during the year and are in force at the date this report is approved. Copies of the relevant extract from the Articles of Association are available for inspection at the registered office of the Company during normal business hours on any weekday and will be available at the venue of the 2019 Annual General Meeting from 15 minutes before the meeting until it ends.

All Directors have deeds of indemnity. These will be available for inspection at the Annual General Meeting with the service contracts.

Powers of Directors

The business of the Company is managed by the Directors who are subject to the provisions of the Companies Act 2006, the Articles of Association of the Company and any directions given by special resolution, including the Company's power to repurchase its own shares.

The Company's Articles of Association may only be amended by a special resolution of the Company's shareholders.

Change of control

All the Company's share schemes contain provisions in relation to a change of control. Outstanding options and awards would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions at that time.

Capita has a number of borrowing facilities provided by various banks and other financial institutions. Capita's bank debt contains a change of control provision under which the banks may require immediate repayment in full on a change of control of Capita plc. The loan notes issued by Capita contain a change of control provision which is likely to require the Group to offer to prepay in full if a change of control event occurs.

There are a number of significant client agreements which contain provisions relating to change of control, which in some cases could present a right of termination of the contract.

Rights and restrictions attaching to shares

Under the Company's Articles of Association, holders of ordinary shares are entitled to participate in the receipt of dividends pro rata to their holding. The Board may propose and pay an interim dividend and recommend a final dividend in respect of any accounting period out of the profits available for distribution under English law. A final dividend may be declared by the shareholders in general meeting by ordinary resolution, but no dividend may be declared in excess of the amount recommended by the Board.

At any general meeting, a resolution put to vote shall be decided on a poll, and every member who is present in person or by proxy shall have one vote for every share of which they are the holder.

No person holds securities in the Company carrying special rights with regard to control of the Company. The Company is not aware of any agreements between holders of securities that may result in restrictions on the transfer of securities or on voting rights.

Restrictions on transfer of shares

The Company's Articles of Association allow Directors to, in their absolute discretion, refuse to register the transfer of a share in certificated form unless the instrument of transfer is lodged, duly stamped, at the registered office of the Company, or at such other place as the Directors may appoint and (except in the case of a transfer by a recognised person where a certificate has not been issued in respect of the share) is accompanied by the certificate for the share to which it relates and such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer. They may also refuse to register any such transfer where it is in favour of more than four transferees or in respect of more than one class of shares.

The Directors may refuse to register a transfer of a share in uncertificated form in any case where the Company is entitled to refuse (or is exempted from the requirement) under the Uncertificated Securities Regulations to register the transfer.

Annual general meeting

The 2019 annual general meeting (AGM) of the Company will be held at Linklaters LLP, One Silk Street, London EC2Y 8HQ on Tuesday 14 May 2019. At the AGM a number of resolutions will be proposed. The resolutions are set out in the Notice of Meeting, which is sent to shareholders with the 2018 Annual Report and includes notes explaining the business to be transacted. The Notice of Meeting is also available on the Company's website at www.capita.com.

In June 2018, shareholders granted authority for the Company to purchase up to 166,838,714 ordinary shares. This authority will expire at the conclusion of the 2019 AGM. No shares were purchased during 2018. A resolution to renew this authority will be put to shareholders at the 2019 AGM.

The Directors consider that each of the resolutions is in the best interests of the Company and the shareholders as a whole, and recommend that shareholders vote in favour of all of the resolutions.

For other general meetings the notice given would be 14 clear working days.

Cross-references

For the purposes of LR 9.8.4R, the following information is located as set out below:

Listing Rule	Subject	Page No.
9.8.4 (1)	Capitalisation of interest	111
9.8.4 (12-13)	Shareholder waiver of dividends	63

Corporate governance statement continued

Directors' responsibilities in respect of the Annual Report and the financial statements

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

Company law requires the Directors to prepare Group and parent company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and applicable law, and have elected to prepare the parent company financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice) including FRS 101 Reduced Disclosure Framework.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent company and of their profit or loss for that period. In preparing each of the Group and parent company 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, for the Group financial statements, whether they have been prepared in accordance with IFRSs as adopted by the EU.
- State, for the parent company financial statements, whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements.
- Assess the Group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern.
- Use the going concern basis of accounting unless they intend either to liquidate the Group or the parent company or to cease operations, or have no realistic alternative but to do so.

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

Under applicable law and regulations, the Directors are also responsible for preparing a strategic report, Directors' report, Directors' remuneration report and corporate governance statement that comply with that law and those regulations.

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

Directors' responsibility statement

We, the Directors of the Company, confirm that 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.
- The strategic 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 Annual Report and Accounts, taken as whole, are fair, balanced and understandable, and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

The Directors' Report (pages 54–98) has been approved by the Board.

On behalf of the Board.

Francesca Todd
Group Company Secretary
13 March 2019

Capita plc

Registered in England and Wales No. 2081330

Committees

Terms of reference

The terms of reference of the Nomination, Remuneration, and Audit and Risk committees (standing committees) were reviewed during the year. The terms of reference are summarised below and, along with the matters reserved for the Board, are displayed in full in the investor centre at www.capita.com/investors.

Terms of reference	Brief description of responsibilities
Nomination Committee	• Reviews composition of the Board. • Recommends appointment of new Directors. • Considers succession plans for Board and senior management positions. • Oversees development of diverse pipeline for succession.
Audit and Risk Committee	• Reviews accounting policies and contents of financial reports. Monitors internal control environment. • Considers adequacy, effectiveness and scope of external and internal audit programme. • Oversees relationship with external Auditor. • Monitors risk profile and obtains assurance that principal risks have been properly identified and appropriately managed.
Remuneration Committee	• Sets policy for Board and senior management remuneration. • Approves individual remuneration awards. Agrees changes to senior executive incentive plans.
Disclosure Committee	• Comprises any two of the Chairman, Senior Independent Director and the Executive Directors. Responsible for the appropriate identification and management of inside information, including any decision to delay public disclosure.

Membership

Membership of the Company's standing committees at the end of the year is shown below:

	Sir Ian Powell	Gillian Sheldon	Matthew Lester	John Cresswell	Andrew Williams	Baroness Lucy Neville-Rolfe
Nomination	C	X	X	X	X	X
Audit and Risk		X	C	X	X	X
Remuneration		X	X	C	X	X

(C) Chairman

Frequency of meetings and attendance

During 2018, the Nomination Committee met four times, the Remuneration Committee met 12 times and the Audit and Risk Committee met nine times. A number of unscheduled committee meetings took place during the year in connection with the rights issue and significant changes to senior management. Some Directors were unable to attend every additional ad hoc meeting due to prior commitments. Attendance of Directors at committee meetings is shown in the following table:

	Audit and Risk Committee	Remuneration Committee	Nomination Committee
Number of meetings	**9**	**12**	**4**
Sir Ian Powell[1]	n/a	n/a	4
Gillian Sheldon	8	12	4
Matthew Lester	9	8	4
John Cresswell	7	12	4
Andrew Williams	9	11	4
Baroness Lucy Neville-Rolfe	8	11	4

1 Sir Ian Powell is not a member of the Audit and Risk, and Remuneration committees, but was invited to, and attended, all meetings.

Consideration of meeting times has to include flexibility to hold meetings outside this timetable and meetings of this nature tend to be held by telephone.

Any Director's absence from meetings of the Audit and Risk, Remuneration or Nomination committees was previously agreed with the Chairman of the Board, the Chief Executive Officer or the chairman of the relevant committee.

Nomination Committee

Members:

- Sir Ian Powell
- Gillian Sheldon
- Matthew Lester
- John Cresswell
- Andrew Williams
- Baroness Lucy Neville-Rolfe

"Capita sees significant business benefit from the diversity of thought that comes from people with a wide range of backgrounds at all levels in the Group."

Sir Ian Powell
Chair
Nomination Committee

The Committee met four times in 2018 and members' attendance record is shown on page 69.

The Group Company Secretary acts as Secretary to the Committee and is available to assist the members of the Committee as required, ensuring that timely and accurate information is distributed accordingly.

The Committee reports and makes recommendations to the Board in relation to its activities and deliberations. It is authorised under its terms of reference to obtain the advice of independent search consultants. The Committee's terms of reference were reviewed and updated during the year and can be found on Capita's website at www.capita.com/investors.

Diversity

Capita's equality and diversity policy, which includes the Board, is based on the belief that success is a direct result of the experience and quality of its people. Inherent within this approach is an acceptance and embracing of diversity in all its forms and an endorsement that the entire workforce, including the Board, be representative of the community in which Capita operates. Key aims of the policy are to ensure equality, diversity and inclusion in the workplace and to promote a culture where everyone is treated with respect and dignity.

Capita sees significant business benefit from the diversity of thought that comes from people with a wide range of backgrounds at all levels in the Group. Only by encouraging this diversity and by fostering talent throughout the business can the Group expect to achieve further diversity in senior management. Capita has a network of diversity champions across the businesses and the Group's training and mentoring initiatives actively support the fostering of talent at all levels in the business across the Company's diverse workforce. The Board and senior management teams across Capita are fully committed to working to provide an environment where everyone has the opportunity to fulfil their potential. The Group will continue to appoint and promote people on merit and in line with the skills and attributes identified for each post. Further information on diversity, inclusion and wellbeing is on pages 37–38 of the strategic report.

Gender balance

At 31 December 2018, female representation on the Board and Executive Committee was 29% and 20% respectively. From 1 January 2019, following Patrick Butcher's appointment to the Board, female representation is 25% and 19% respectively. At 31 December 2018, female representation among senior management[1] and their direct reports was 28%.

1 The 2018 Code defines senior management as the Executive Committee and the Group Company Secretary.

Responsibilities and activities

Key responsibilities	Activity in 2018
• Identify and nominate appropriate candidates for appointment to the Board, having due regard to the provisions of the 2018 Code and, in particular, the balance of skills, knowledge and experience on the Board and the diversity of its composition. • Keep the structure and size of the Board and the leadership needs of the organisation under review and ensure that plans are in place for orderly succession and appointment to the Board. • Review the time commitment required from Non-Executive Directors, the performance of Directors and all declarations of interest made by Board members. • Consider Capita's diversity position.	• Succession planning for the Board generally and for other senior positions below Board level. • Recruitment and appointment of new Chief Financial Officer: the external search agency, Lygon Group, was used for this appointment and it has no other connection with the Group. • Consideration of Directors' performance, length of service, interests and potential conflicts to ensure independence of NEDs and that all Directors could stand for re-election or election at the AGM. • Discussed and approved the resignations of Nick Greatorex and Chris Sellers.

Audit and Risk Committee

Members:

- Matthew Lester
- Gillian Sheldon
- John Cresswell
- Andrew Williams
- Baroness Lucy Neville-Rolfe

"A key area of focus will be to ensure the Group's new operating model delivers a more efficient control and risk process."

Matthew Lester
Chair
Audit and Risk Committee

This year's independent evaluation of the Committee has concluded that the Committee fulfils its role of supporting the Board in its review of the integrity of the Group's financial reporting, monitoring the effectiveness of the Group's systems of risk management and internal controls, and overseeing the activities of the Group's internal audit function and its external auditor.

In line with Capita's multi-year transformation, the Committee meetings have changed to go deeper into relevant issues. However, more is required if the Committee is to become really effective. Now that the senior leadership team is complete and Capita is on a sounder footing, this is an achievable objective. The other key area of focus for the Committee will be to ensure the Group's new operating model delivers a more efficient control and risk process.

Committee membership and attendance

All members of the Committee are independent and I am considered to have recent and relevant financial experience for the purposes of the UK Corporate Governance Code 2016.

To encourage effective communication, in addition to the above members, the Board Chairman, Chief Executive Officer, Chief Financial Officer, Chief General Counsel and Director of Group Finance are invited to attend Committee meetings along with certain members of the senior management team, the Group Internal Audit Director, the Chief Risk & Compliance Officer, and representatives from KPMG, the Group's external auditor. Opportunity exists at the end of each Committee meeting for the representatives of the internal and external audit teams to meet with the Committee in the absence of management and both have access to the Committee should they wish to voice any concerns outside formal meetings.

Committee performance was assessed as part of the externally facilitated Board evaluation (see page 55 for more information). The Board is satisfied that the combined knowledge and experience of its members is such that the Committee discharges its responsibilities in an effective, informed and challenging manner and that, as a whole, the Committee has competence relevant to the sector in which the Company operates.

The Group Company Secretary acts as Secretary to the Committee and is available to assist the members of the Committee as required, ensuring that timely and accurate information is distributed accordingly.

How the Committee operates

The Committee has established an annual forward agenda to cover the key events in the financial reporting cycle, specific risk matters identified by the Committee and standing items that the Committee is required to consider in accordance with its terms of reference. The annual agenda is supported by agenda setting meetings held in advance of each Committee meeting, led by me and attended by senior management. Their purpose is to identify key issues impacting the business that may require consideration by the Committee.

Reports are received from the Group Risk & Compliance and Group Internal Audit departments and new sales wins and their contract terms are reviewed from a risk and accounting perspective as appropriate. At each Committee meeting, the members may receive other reports and presentations covering key financial reporting, risk, compliance and audit matters which are delivered by key senior personnel who attend by invitation to enable any clarification or queries to be provided to the Committee. I report to the Board the key matters of discussion and make any significant recommendations as necessary.

Audit and Risk Committee continued

Role and responsibilities

The Audit and Risk Committee is responsible for carrying out the audit functions as required by DTR 7.1.3R and assists the Board in fulfilling its oversight responsibilities in respect of the Company and the Group. The Committee's key responsibilities are:

Financial reporting	• To review the reporting of financial and other information to the shareholders of the Company and monitor the integrity of the financial statements, including the application of key judgements in determining reported outcomes to ensure that they are fair, balanced and understandable.
Risk management, internal controls and compliance	• To review and assess the adequacy of the systems of internal control and risk management and monitor the risk profile of the business.
Internal audit	• To approve the annual internal audit plan, review the effectiveness of the internal audit function and review all significant recommendations and ensure they are addressed in a timely manner.
External audit	• To review the effectiveness and objectivity of the external audit process, assess the independence of the external auditor and ensure appropriate policies and procedures are in place to protect such independence.
Cybersecurity	• To review and assess cybersecurity risk and governance including IT security for the Group and monitor risks within this area.
Effectiveness	• To report to the Board on how it has discharged its responsibilities.

The Audit and Risk Committee's terms of reference set out in full the role, responsibilities and authority of the Committee and can be found on the Company's website at www.capita.com/investors. These were reviewed and updated during the year.

How the Committee discharged its roles and responsibilities in 2018

The Committee met nine times during the year and attendance at each meeting is shown on page 69. Meetings are planned around the Company's financial calendar. Additional meetings were held during the first part of the year to discuss the impact of the new strategic plan and the rights issue, and to consider certain additional financial reporting in respect of the rights issue.

Financial reporting

Accounting judgements and significant accounting matters

As part of the process of monitoring the integrity of the financial information presented in the half-year results and the Annual Report and Accounts, the Committee reviewed the key accounting policies and judgements adopted by management to ensure that they were appropriate. The significant areas of judgement identified by the Committee, in conjunction with management and the external auditor, together with a number of areas that the Committee deemed significant in the context of the financial statements are set out in the tables on pages 73–75.

The Committee is assisting the Board to review the key metrics to be used to measure the value creation for Capita's shareholders, recognising that historical measures such as profitability may not be as relevant as free cash flow, given the impact certain policies have on the timing of recognition of profits and cash inflows. The Chief Financial Officer's review sets out the key areas where current accounting requirements separate profit recognition from cash flows.

During 2018, the Committee received presentations from the Executives and divisional management on the performance of major contracts. This included an analysis of the IFRS 15 reported profits and highlighted the particular challenges of measuring performance for a contracting business. For certain projects the contract lifetime models benefit from the recognition of deferred income, for which there is no future cash inflow, as the associated cash has been received in prior-year transformation milestone receipts.

The recognition of deferred income is a positive reflection of the Group's delivery against its future performance obligations. This 'business as usual' activity is a core value, as it underpins the continued delivery of valuable services and solutions to the Group's customers. The flip-side comes when the Group's transformation plan successfully secures new contract wins, as the early cash milestones are likely to be significant, generating new deferred income and with cash in excess of profits in the early years.

Accordingly, the Committee is reviewing with the Board how free cash flow can be used to reflect the value creation for shareholders, recognising that outside the core contracting activities there are other commitments, and in particular the pension deficit repayment plan; free cash flow will not always be reflected in the reported profits (refer to note 29 to the consolidated financial statements). The Board will continue to review how the different measures are presented and the Committee has requested management that carries out a fundamental review of how free cash flow is disclosed, so the reader can obtain a clear understanding of the key value drivers.

Fair, balanced and understandable

At the Board's request, the Committee considered whether the half-year results and the Annual Report and Accounts were fair, balanced and understandable and whether the information provided was sufficient for a reader of the statements to understand the Group's position and performance, business model and strategy. The Committee reviewed both the narrative and financial sections of the reports to ensure they were consistent and gave a balanced view of the performance of the business in the year and that appropriate weight was given to both positive and negative aspects. The Committee also assessed whether important communications issued during the year were presented clearly.

The Committee considered whether the Annual Report and Accounts enable readers to understand the Company's financial position and prospects, as well as assess its going concern status and longer-term viability.

Significant issues in relation to the financial statements considered by the Audit and Risk Committee

Revenue and profit recognition

Matter considered	Action	Outcome
There is significant risk on long-term contracts related to revenue recognised from variations or scope changes, where significant judgement is required to be exercised by management. There is a risk that revenue may be recognised even though it is not probable that consideration will be collected, which could be due to uncertainties over contractual terms and ongoing negotiations with clients.	The Committee received regular updates on all major contracts during the year and specifically reviewed the material judgements as part of the year-end close process. The Committee has also considered the recognition of onerous provisions, where appropriate, and the lifetime profitability of contracts.	The revenue recognition policy includes disclosure of the significant judgements and estimates in relation to its application and the Committee is satisfied that these have been properly disclosed. The Committee is satisfied that the disclosures given within the accounts are sufficient to gain a proper understanding of the methodology of accounting for revenue across the Group, including the recognition of deferred income at the balance sheet date.

Contract fulfilment assets

Matter considered	Action	Outcome
The adoption of IFRS 15 has led to the recognition of contract fulfilment assets (CFAs). Judgements are involved in assessing whether the costs incurred on a contract, or an anticipated contract meet the capitalisation criteria as set out under the standard. In addition, the amortisation of these assets involves estimation of the expected life of the contract.	As part of the adoption of IFRS 15, the Committee has considered and challenged the significant judgements and estimates involved in determining the carrying value of CFAs. As part of the review of all major contracts, the Committee has also considered the recoverability of CFAs. During the year, the Committee discussed certain CFAs where their recoverability was in doubt. Management agreed not to capitalise these until the necessary actions to underpin the contracts' profitability had taken place.	The Committee is satisfied that appropriate judgements and estimates have been made in determining the carrying value of CFAs and the extent of impairment of CFAs recognised in these statements is appropriate. The Committee is satisfied that the accounting policy note provides sufficient clarity as to the new policy adopted.

Impairment of intangible assets, goodwill and parent company's investment in subsidiaries

Matter considered	Action	Outcome
The Group carries significant asset balances in respect of goodwill and intangible assets related to its acquisition activity. In addition, the parent company carries a material balance of investment in subsidiaries on its financial statements. The impairment assessment requires the application of judgement concerning future prospects and forecasts.	The Committee has reviewed the robustness of the impairment model and challenged the appropriateness of assumptions used to calculate and determine the existence of impairment. The Committee considered the events and circumstances that have led to the impairment charges since the publication of the interim results in August 2018. In particular, the Committee considered the continuing challenges both operationally and within the market served, the continued attrition in sales and the more significant contract terminations experienced. The impairment of goodwill and intangible assets at Group level indicates that there may also be impairment of investment in subsidiaries on the parent company's financial statements. Accordingly, the Committee has reviewed the assumptions and calculation of impairment of these investments.	The Committee is satisfied that the impairment of goodwill and intangibles recognised in these statements is in line with expectations given the performance of certain areas of the Group's business in the year and the update on the trading outlook. The Committee is also satisfied that the assumptions, methodology and disclosure in note 15 to the consolidated financial statements are sufficient to give the reader an understanding of the action taken and the sensitivities within the goodwill and intangible assets balance to any further impairment risk. Of particular importance to the Committee was the inclusion of sufficient disclosures to set out the events and circumstances that have led to the impairment charges recorded in the year. The Committee also considered that any impairment of investment in subsidiaries at the parent company level were appropriate and properly accounted for.

Audit and Risk Committee continued

Items excluded from adjusted results

Matter considered	Action	Outcome
As stated in its accounting policies, Capita separates its results between adjusted and reported to provide useful disclosure to aid the understanding of the performance of the Group. The Committee needs to ensure a fair and balanced treatment of what is and is not included as an adjusting item.	The Committee has reviewed the individual items excluded from adjusted results, in particular the items relating to pensions. The Committee has requested further information concerning the origination of the items where they felt it was necessary to enable a conclusion to be drawn as to whether the chosen presentation achieved the stated principal. The Committee has considered the accounting policy by reference to guidance issued by the FRC and the need to ensure any alternative performance measures are presented with equal prominence to reported figures and on a consistent basis year-on-year. The Committee considered the appropriate presentation to apply for the costs associated with the transformation plan which are presented as an 'adjustment' to the reported results. The plan is extensive and covers a number of Capita-wide initiatives to address the cost competitiveness of the businesses and to simplify and strengthen the Group. Categories of expenditure include costs typically associated with major restructuring such as severance payments, but also include costs related to the offshoring of activities and the introduction of automation and digital solutions, a Group-wide property rationalisation and finance transformation project. To support these activities, external professional fees are being incurred in addition to dedicated internal costs. Where such costs are incremental and directly related to the transformation plan, the Committee has concluded that such costs should be included in the overall transformation costs that are separately presented. In agreeing this presentation, the Committee was mindful of the guidance issued by the FRC in November 2017 in terms of multi-year major 'restructuring' programmes. This directs boards to define the costs to be presented separately, set borders to capture only relevant costs, and emphasises that disclosures to explain the costs must be transparent and of high quality. The Committee considers that this guidance has been applied and note 3 to the consolidated financial statements provides details of the costs incurred in 2018. The Committee will continue to review this policy in 2019 and beyond, as the transformation programme continues.	The Committee concurs with management's view that the presentation of items excluded from adjusted results provides useful disclosure to aid the understanding of the performance of the Group and agree that the items excluded meet with the stated policy for recognition. Note 3 to the consolidated financial statements sets out the items that are separately presented, and the Committee is satisfied that this provides sufficient information to inform a reader on each category presented. The Committee also notes that the approach is consistent with that used for the rights issue in 2018. The Committee has asked the new CFO to continue to review the approach in 2019.

Provisions and contingent liabilities

Matter considered	Action	Outcome
There is judgement applied in the level of provisioning across the Group. This involves making an assessment of the size, timing and probability of economic outflows due to the occurrence of a past event. It is therefore important to understand the judgement being made as well as the estimate of any accompanying outflow of funds.	The Committee has reviewed the disclosure in the financial statements, in particular it has challenged management to justify provisioning levels where a range of outcomes has been identified.	The Committee is satisfied with the fact patterns underlying the provisions, with both the treatment and levels of provision being properly justified.

Pensions

Matter considered	Action	Outcome
The measurement of the defined benefit liability in respect of defined benefit pension schemes operated within the Group is a complex area, relying on assumptions on inflation, mortality, corporate bond yields, expectations of returns on assets and a number of other key inputs. There is a risk that any one of these could lead to misstatement of the Group's liability in respect of pension obligations and the pension charge or movement recognised in the income statement or statement of comprehensive income.	The Committee has reviewed the disclosure as presented in the accounts. The Committee also challenged the key assumptions and reviewed the sensitivity to changes in some of the key assumptions both on a stand-alone basis as well as in the context of defined benefit schemes across other external benchmarks.	The Committee is satisfied that the estimation of the Group's pension liabilities and the narrative that accompanies them gives the required level of information for a reader of the accounts to determine the impact on the Group of its pension obligations.

Going concern

Matter considered	Action	Outcome
Consideration of the going concern assumption is the responsibility of the Board, and the Committee conducted an assessment as part of its support role, given the inherent judgements required to be made in relation to the forecasts and definitions within the covenant calculations.	The going concern assertion has a significant impact on the basis of preparation of the financial statements. The Committee considered the business plan projections that cover the two years to 31 December 2020. The Committee considered the assumptions behind the plausible but severe downside scenarios used for stress testing the Group's ability to meet its obligations as they fall due. It also considered and challenged the mitigating actions proposed by management. The Committee has challenged the key assumptions, as set out on page 65. The Committee considered compliance with the key covenants included in the Group's committed facilities and private placement notes, including maximum ratios of adjusted net debt to adjusted EBITDA. The Committee considered the judgements made by management in calculating the adjusted EBITDA. In particular, consideration was given to consistency of treatment with the prior year, including the exclusion of restructuring. Applying the downside scenarios, the Committee concluded that, assuming no mitigating actions are taken, the available headroom is sufficient to operate within the 3.0 times adjusted net debt to adjusted EBITDA ratio. The Committee considered the going concern assumption disclosures. The Committee considered the requirements of the Code as it applies to the Group's viability statement including the three-year period of assessment which aligns with the Group's planning horizon and the processes supporting the viability statement. After significant discussion and having considered the various stress testing scenarios that were presented as part of the viability assessment alongside the liquidity and debt positions of the business, the Committee determined that the three-year measurement period continued to be appropriate and that the viability statement (as set out on page 52) should be recommended to the Board for approval.	The Committee is satisfied that page 65 includes detailed disclosures concerning the going concern assertion and key assumptions applied to inform the users of the assessment undertaken by the Board.

Audit and Risk Committee continued

Other issues considered in relation to the financial statements

Materiality

Materiality is important in determining the risk attached to any judgement. The Committee considers the audit materiality set by the external auditor to ensure that the Audit and Risk Committee is informed of individual items above a certain threshold that are most likely to have an impact on the financial statements. The Audit and Risk Committee reviews the external auditor's report and the individual items that breach the materiality thresholds and assess their relative impact on the reported statements. These are: income statement, balance sheet, statement of changes in equity and cash flow, as well as the notes to the accounts.

The Committee requests further clarification from both the external auditor, the Chief Financial Officer and Director of Group Finance as to the nature of these items and also their relative importance in the financial statements.

After having made such enquiries, the Audit and Risk Committee is satisfied that materiality has been applied correctly in the accounts and that material items brought to its attention remain unadjusted where its inclusion would not cause detriment to the overall reading of the financial statements.

Disclosure of information to the auditor

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

Statutory auditor

The Committee provides a forum for reporting by the Group's auditor (KPMG) and it advises the Board on the appointment, independence and objectivity of the auditor and on fees earned for both statutory audit and non-audit work. The Committee discusses the nature, scope and timing of the statutory audit with the auditor and, in making a recommendation to the Board on auditor reappointment, performs an annual, independent assessment of the auditor's suitability and performance.

The external auditor attends meetings of the Committee and provides updates on statutory reporting, non-audit fees and ongoing audit items.

The auditor has opportunity to raise concerns with the Chairman separately and in private session with the Committee. Specifically, the Committee asks the auditor if discussion of business performance in the strategic report is consistent with the impression of Capita the auditors have gained. Any material discrepancies are discussed (refer to the independent auditor's report).

Auditor independence

The Committee takes seriously its responsibility to put in place safeguards to auditor objectivity and independence. The Company is committed to ensuring appropriate independence in its relationship with the auditor and the key safeguards are:

- The Chief Financial Officer monitors the independence of the auditor as part of the Group's assessment of auditor effectiveness and reports to the Audit and Risk Committee.
- The Chief Financial Officer monitors the level and nature of non-audit fees accruing to the auditor, and specific assignments are discussed in advance with the auditor and flagged for the approval of the Audit and Risk Committee, as appropriate, and in accordance with the Company's policy on the provision of non-audit services by the auditor. The Audit and Risk Committee reviews, in aggregate, non-audit fees of this nature on a six-monthly basis and considers implications for the objectivity and independence of the relationship with the auditor.
- The auditor provides confirmations of its independence to the Audit and Risk Committee every six months.

Ensuring conflicts of interest are avoided is a fundamental criterion in the selection of any third-party auditor. Such conflicts may arise across public or private sector clients and key supplier relationships, for example, and are a key determinant in the award process for external audit assignments.

Non-audit services and fees

The Committee has established a policy on the provision of services by the Group's auditor. The policy describes the circumstances in which the auditor may be permitted to undertake non-audit work for the Group. The Committee oversees compliance with the policy and considers and approves requests to use the Auditor for non-audit work. Any assignment where the expected fee is above £150,000 requires specific approval from the Committee or a member of the Committee. The Group Company Secretary deals with day-to-day administration of the policy, facilitating requests for approval by the Committee. All work with the external auditor outside of the audit has to be pre-approved by the Chief Financial Officer. The auditor undertook various non-audit work in 2018 primarily related to their role as Reporting Accountant in connection with the rights issue, and the Interim Review. Only the Audit and Risk Committee can authorise the scope and policy on non-audit fees.

Non-audit fees this year are 23% (2017: 17%) of all fees paid to the external auditor. The Committee continued to receive updates throughout the year on approval of fees exceeding the threshold stated above.

The policy is reviewed annually by the Committee. During 2018, our external auditor, KPMG, announced a new policy with regard to the provision of non-audit services to FTSE 350 audit clients and this is therefore applicable to non-audit services provided to Capita plc.

With effect from 1 January 2019, to avoid the perception of a conflict, KPMG will not perform, and will not approve requests from other KPMG member firms to perform, non-audit services for FTSE 350 listed audit clients other than services closely related to the audit. Such services include those required by laws and regulations, or where it is more practical for the external auditor to perform the service (e.g. reporting accountant role related to certain public company transactions). KPMG will also continue to deliver the Interim Review which though technically classified as a non-audit service, relates closely to the audit.

Details of audit and non-audit fees are given in note 7 to the consolidated financial statements and a summary of non-audit fees is shown in the table below.

	2018 £m	2017 £m
Non-audit services		
Taxation compliance services	—	0.1
Services related to corporate finance transactions	—	0.1
Other assurance services	**1.6**	0.8
Total non-audit services	**1.6**	1.0

External auditor performance

The Committee discussed the performance of KPMG during the period and was satisfied that the level of communication and reporting was in line with requirements. This also included a review of effectiveness and quality of the audit process, audit planning and a post-audit evaluation.

The Committee has ensured that the evaluation is integrated with other aspects of their role related to ensuring the quality of the financial statements – obtaining evidence of the quality of the auditor's judgements made throughout the audit, in identifying audit risks, determining materiality and planning their work accordingly, as well as in assessing issues.

Financial Reporting Council: audit quality inspections

Each year the Audit Quality Review team (AQR) of the FRC issues a report that sets out the principal findings arising from the audit quality inspections conducted in the previous calendar year across a sample of audits for all major audit firms. The AQR's objective is to monitor and promote improvements in the quality of auditing. The reports highlight improvements required to promote audit quality, and areas of good practice. The FRC publishes separate reports on the individual firms, including KPMG.

The Committee received a presentation from the KPMG lead audit partner on the findings from the FRC Audit Quality Inspection Report for KPMG and the proposed improvement plans put forward by KPMG in response, including details of the Audit Quality Transformation Programme initiated by KPMG. The Committee will closely monitor progress against these plans.

AQR review of the Capita 2017 audit by KPMG

During the year, the 2017 audit of Capita plc by KPMG was reviewed by the FRC's AQR.

Certain matters for improvement were identified, including how KPMG evidenced all areas of the audit work performed, and the conclusions reached, concerning the Company's impairment models. The AQR also highlighted good practice observations in relation to KPMG's challenge over going concern and the approach adopted to auditing Capita's long-term contracts. The Audit and Risk Committee and KPMG have discussed the review findings and the identified improvement observations, and are satisfied with responses to be implemented by KPMG in the 2018 audit.

Overall, the results of the review raised no issues which cast doubt on the fundamental quality of Capita's external audit and the Committee remains satisfied with the efficiency and effectiveness of the audit. KPMG LLP have also discussed more generally the firm's process for enhancing audit quality which includes internal quality reviews. KPMG LLP reported to the Audit and Risk Committee as part of their April 2018 report on these matters, with the Audit and Risk Committee concluding that the findings were being addressed.

External audit tender

The Company's audit services were last subject to a tender process in 2010, at which time KPMG Audit Plc, subsequently KPMG LLP, replaced Ernst & Young LLP as the Group's auditor. The lead audit partner is rotated on a five-yearly basis. The current lead audit partner rotated on to the audit at the conclusion of the 2016 audit. There are no contractual obligations which restrict the Committee's choice of auditor.

Under the requirements of the Statutory Audit Services Order and the EU Audit Directive and Audit Regulation, the provision of audit services should be re-tendered every 10 years. The complex nature of the Group requires that a knowledge base is built up year-on-year by the incumbent to ensure that the external audit is conducted with a proper understanding of the Group's operations and the nature of the risks that it faces. This is an important factor in ensuring audit quality.

The Group has complied with the provisions of the Statutory Audit Services Order.

A pre-selection process was carried out in preparation for the tender. Pre-qualification questionnaires were completed to identify those firms with sufficient FTSE experience, sector expertise, and resources to provide a good cultural fit and which were not conflicted by virtue of substantial ongoing non-audit work. Following detailed reviews and preliminary meetings with potential firms, a shortlist was identified and firms asked to submit proposals against a detailed invitation to tender.

Following review and agreement on a final shortlist, partners of two firms met with management and members of the Committee to outline further the skills and attributes expected of an external audit team. The selection criteria were developed into a scorecard for the Audit Committee. The categories were:

- technical competency and experience
- high-quality tailored audit
- culture and teaming
- innovation and technology.

The final short-listed firms met with divisional and central services management, and the CEO and Committee Chairman met with key partners for one-to-one discussions. Following feedback from management, each of the two firms presented to the Committee Chairman, Baroness Lucy Neville-Rolfe, CFO, Director of Group Finance, Head of Procurement and Director of Commercial & Financial Accounting in December 2018, ahead of the Committee making its final decision for recommendation to the Board. Following the detailed tender process, the Committee recommended to the Board that KPMG be re-appointed as external auditor.

External auditor re-appointment

A resolution to re-appoint KPMG as the external auditor of the Company will be put forward at the forthcoming annual general meeting. If approved, KPMG will hold office from the conclusion of this meeting until the conclusion of the next general meeting at which accounts are laid before the Company, and their remuneration will be fixed by the Committee.

Review of risk management and internal control

The Committee is responsible for reviewing the effectiveness of the Group's system of internal control and risk management. The risk management framework and processes are set out on pages 44–51.

Effectiveness and efficiency of risk management

During the year, the Committee focused on key risk themes such as IT resilience, cyber-risk, management of client money, regulatory risk, information security and data management. The Committee received reports on the following themes during the year:

- IT resilience and ensuring that customer data was kept safely and in a controlled manner.
- Financial Services regulated businesses, in particular, conduct matters, the significance within the Group of the regulated environment and co-operation with the Financial Conduct Authority.
- Primary Care Support England contract with NHS England where some performance obligations had not been correctly identified in line with the contract.

As a consequence of the above areas, a review of the first line control framework has been instigated to ensure that lessons are learned across the business and that appropriate controls are in place.

This together with other matters reported to the Committee highlighted areas where there is a need for improvement in operational risk management and verification by internal audit.

Audit and Risk Committee continued

However, the Committee concluded the risk management processes were materially adequate and there were no material weaknesses requiring specific disclosure.

Effectiveness and efficiency of financial controls

As noted in the Annual Report and Accounts 2017, Capita has embarked on a finance transformation which it expects will drive improved data quality, standardisation of activities performed by the finance community and optimise the use of offshoring and shared service centre delivery models. These actions are designed to develop and deliver better processes and controls across the business, improving the financial risk framework employed by the business.

As part of this programme, in the year under review, an evaluation of financial controls was undertaken by the senior finance team to review the material financial controls that are in place and to identify areas where these might only be partially effective or be inefficient in achievement of their purpose. The results of the review completed by management was shared with KPMG to ensure the combined approach delivers value within the context of an external audit and the robustness of the financial statements. Any material issue was dealt with through mitigating activities.

Learnings gained from the review will be considered by senior management within the construct of the wider finance transformation to ensure that the financial risk framework is improved and strengthened. This is expected to deliver value to both the business and its stakeholders by improving the safeguarding of the Group's financial position and additionally to our external auditor in relation to the scoping, efficiency and planning of their audit.

As part of its remit to ensure the robustness of the Group's internal control frameworks, the combination of the findings from the above exercise and the scoping of the programme will be monitored by the Committee.

The Committee concluded financial control processes were materially adequate and there were no material weaknesses requiring specific disclosure.

Internal audit

The Group Internal Audit function has an administrative reporting line to the Chief Financial Officer and an independent reporting line to me as Chairman of the Committee. The function has in place a co-sourcing arrangement with PricewaterhouseCoopers LLP which adds expertise and breadth to the work of the in-house audit team.

During the year, a programme of internal audits was completed. The scope of audit work generally focuses on assessing the adequacy and effectiveness of controls including management oversight and the degree of management risk awareness within the businesses that are subject to audit.

Throughout the year, the Group Internal Audit function provides written reports to the Group Audit and Risk Committee on the work carried out to date and the in-flight work to be completed. A verbal update accompanies each report submitted to the Committee. An annual report is provided each year summarising the key matters arising. The representations given set out strengths and weaknesses identified during the work, together with any recommendations for remedial action or further review.

The Group Internal Audit team reported weaknesses in compliance with Group policies, particularly the Group Security Standards, controls over data management, system access and measures to safeguard both employees and the public. In all cases, management has responded with appropriate action to mitigate the associated risks and Divisional Executive management have increased visibility on those issues of significance. In addition, there has been focus by senior management to improve the control environment through the closure of previously overdue audit actions.

The Committee reviews management's response to the matters raised and ensures that any action is commensurate with the level of risk identified, whether real or perceived.

Through the regular interaction between the Committee and Group Internal Audit Director, as well as the reports received from the function, the Committee is able to assess and satisfy itself that the Group's provision of internal audit is effective. At the request of the Committee, a review of the function is currently under way as part of Capita's wider transformation programme, in order to ensure the function provides assurance in an efficient as well as effective manner. In particular, this will seek to leverage the control and risk self-assessment process, referred to in the 'internal control and risk management' section of the strategic report, and focus on business unit key-control reviews. This review is being undertaken by the Group Internal Audit Interim Director who joined Capita in October 2018 following the departure of the previous incumbent Head of Internal Audit during the year.

Anti-bribery and whistleblowing

Capita has a Group-wide anti-bribery and corruption policy, which is in compliance with the Bribery Act 2010. Procedures are reviewed periodically to ensure continued effective compliance in Group businesses around the world.

A 'Speak Up' policy provides the framework to encourage and give the workforce confidence to 'blow the whistle' and report irregularities. Employees are encouraged to raise concerns with designated individuals and there is a dedicated email hotline to make it easy to raise concerns. These are investigated on behalf of the Board and reported to it, together with details of corrective action taken. Following the introduction of the 2018 Code, oversight of these arrangements is now a matter reserved for the Board.

Matthew Lester

Chairman
Audit and Risk Committee

13 March 2019

Group Executive Risk Committee

The Group Executive Risk Committee (ERC) assesses risk across all Capita businesses and reports to the Audit and Risk Committee. It holds scheduled meetings on a quarterly basis. Membership comprises the CEO, CFO, Chief General Counsel, Group Commercial Director, Chief Risk & Compliance Officer and the six divisional Executive Officers. The Group Internal Audit Director has a standing invitation, and the Non-Executive Directors have an open invitation, to attend all meetings. Following the resignation of Tim Brooke as independent committee chairman in August 2018, the role of chairman was assumed by the CEO, Jon Lewis.

The ERC's role is to oversee and challenge the key risk and compliance activities and issues in Capita's businesses by:

- Reviewing the residual risk profile of Capita businesses, along with ensuring appropriate remedial actions are taken in line with Group objectives and risk appetites.
- Reviewing and monitoring Group control function activity and oversight plans.
- Tracking key regulatory changes affecting the Group's businesses.
- Tracking key business developments, including bids, acquisitions and offshoring developments.
- Receiving updates on regulatory capital issues, e.g. Internal Capital Adequacy Assessment Process (ICAAP).
- Receiving updates on conduct risk issues.
- Reviewing, and recommending for adoption, policies applicable to the Group's businesses.
- Identifying items for the attention of the Board or Group Audit and Risk Committee.

The scope of the Committee covers all Capita businesses, including regulated activity in all jurisdictions in which the Group operates.

The Committee structure was reviewed during the year and, in November 2018, the Group Technology & Security Risk Committee, which focused on risk relating to information systems and security, and IT infrastructure, was merged into the ERC to simplify risk oversight. However, in order to retain an element of independent oversight of risk within Capita's regulated businesses, the former Financial Services Risk Committee will be reconstituted during 2019 to take on this responsibility, with an independent chairman, as a committee of the ERC. Where appropriate, matters will be escalated to the ERC, which reports regularly to the Audit and Risk Committee, and feedback from both committees will be provided to the Audit and Risk Committee on a regular basis.

During 2018, the ERC met four times and the Group Technology & Security Risk Committee met three times prior to being merged into the ERC. Membership and meeting attendance are set out in the tables on this page. The maximum number of meetings that could be attended is shown in brackets.

Group Executive Risk Committee:

Name of member	Title	Number of meetings attended
Jon Lewis (Chairman)[1]	Chief Executive Officer	4(4)
Patrick Butcher[2]	Chief Financial Officer	0(0)
Mike Barnard	Executive Officer, Customer Management	4(4)
Joe Hemming	Executive Officer, IT & Networks	3(4)
Patrick Elliott	Interim Executive Officer, Government Services	1(1)
Erika Bannerman	Executive Officer, People Solutions	4(4)
Jim Vincent	Executive Officer, Specialist Services	4(4)
Chris Baker	Executive Officer, Software	2(4)
Claire Chapman	Chief General Counsel	4(4)
Rob Tolfts	Group Commercial Director	4(4)
Sue Williams	Chief Risk & Compliance Officer	2(2)
Nick Greatorex[3]	Chief Financial Officer	2(2)
Tim Brooke[4]	Independent Chairman	2(2)
Stephen Sharp[5]	Executive Officer, Government Services	3(3)
Peter Hepworth[6]	Executive Officer, Professional Services	1(1)
Chris Terry[7]	Group Risk & Compliance Director	2(2)

1 Jon Lewis chaired two of the four meetings following Tim Brooke's resignation.
2 Patrick Butcher was appointed as a Director of Capita plc, and joined the ERC, on 1 January 2019.
3 Nick Greatorex, former Chief Financial Officer, resigned from the Board and all committees on 30 September 2018.
4 Tim Brooke, former independent Chairman, resigned as chairman of the ERC on 31 August 2018.
5 Stephen Sharp, former Executive Officer for Government Services, left Capita on 7 November 2018.
6 Peter Hepworth, former Executive Officer for Professional Services, left Capita on 21 May 2018.
7 Chris Terry, former Group Risk & Compliance Director, left Capita on 27 August 2018.

Group Technology & Security Risk Committee:

Name of member	Title	Number of meetings attended
Sue Williams (Chairman)	Chief Risk & Compliance Officer	1(1)
Jon Lewis	Chief Executive Officer	3(3)
Mark Brown	Chief Information Officer	2(3)
Claire Chapman	Chief General Counsel	1(2)
Nick Greatorex[1]	Chief Financial Officer	2(2)
Chris Terry[2]	Group Risk & Compliance Director	2(2)

1 Nick Greatorex, former Chief Financial Officer, resigned from the Board and all committees on 30 September 2018.
2 Chris Terry, former Group Risk & Compliance Director, left Capita on 27 August 2018.

Directors' remuneration report

Members:

- John Cresswell
- Gillian Sheldon
- Matthew Lester
- Andrew Williams
- Baroness Lucy Neville-Rolfe

"Our incentive plans are aligned with our business transformation to drive better outcomes for all stakeholders."
John Cresswell
Chair
Remuneration Committee

Annual statement

I am pleased to present the Remuneration Committee report for the year ended 31 December 2018. As Sir Ian Powell notes in his introduction, Capita is a business in transition as our leadership team and people restructure and build. The Remuneration Committee has invested significant time working with the CEO in building the leadership team, with Patrick Butcher joining as CFO and seven new appointments to the Executive Committee.

We received strong support for our 2017 Annual Report on Remuneration and we have spent significant time considering performance measures and targets for 2018 and 2019 to ensure they are meaningful, robust and aligned with our strategy.

Context to the Committee's decisions in the year

Since the arrival of Jon Lewis in late 2017, the business has begun a major transformation, with a rights issue, the formulation of a new business strategy and a series of disposals. Capita is now a much stronger business with a solid balance sheet, and a clear strategy for transformation that will see the business simplify, strengthen and succeed. Our overall remuneration framework has a number of specific objectives. It is designed to focus on value creation and share ownership to align the high-calibre executives appointed in 2017 and 2018 with the completion of the transformation and the delivery of the outcomes promised to shareholders. There are multiple considerations in the design of the overall framework to: ensure long-term shareholder value creation; and recognise Group performance and the individual's specific contribution to it, through an appropriate balance of short and long-term reward, as well as consideration of the level of reward available to employees in the wider Group. A good example of this is the pension contribution (or cash in lieu) for our CEO and CFO, which is the same level as is offered to other employees in the UK at 5% of salary.

We consulted with major shareholders to obtain their views on the design of our long-term incentive plan. Feedback received has been incorporated into the plan design for 2019; further detail is shared below. The Committee has also decided to introduce an additional two-year holding period for all share awards from 2019 onwards. In addition, the Committee has incorporated a discretion allowing the Committee to override formulaic outcomes in line with the changes to the new Corporate Governance Code.

Committee membership and attendance

All members of the Committee are Independent Non-Executive Directors. None of the Committee members have day-to-day involvement with the business nor do they have any personal financial interest, except as shareholders, in the matters to be recommended. The number of formal meetings held and the attendance by each member is shown in the table on page 69. The Committee also held informal discussions as required.

To encourage effective communication, in addition to the above members, the Board Chairman, Chief Executive Officer, and senior human resources personnel are invited to attend all or part of Committee meetings along with representatives from Deloitte, the Group's remuneration advisers.

The performance of the Committee is assessed as part of the Board performance evaluation undertaken annually.

The Group Company Secretary acts as Secretary to the Committee and is available to assist the members of the Committee as required, ensuring that timely and accurate information is distributed accordingly.

How the Committee operates

The Committee has an annual agenda to cover the key planning and decision events in the annual remuneration cycle.

Each meeting is supported by an agenda-setting discussion held in advance with the Chief People Officer, Group Reward Director, Group Company Secretary and Deloitte to identify issues impacting remuneration that may require consideration by the Committee.

Regular reports including updates in corporate governance and regulatory developments are received from Deloitte. At each Committee meeting the members may receive other reports and presentations covering the annual pay review, incentive scheme arrangements, gender pay reporting, salary proposals for members of the senior team and approval of remuneration packages for new members of the CEO's team.

The Remuneration Committee's terms of reference set out in full the role, responsibilities and authority of the Committee and can be found on the Company's website at www.capita.com/investors. These were reviewed and updated during the year.

How the Committee discharged its roles and responsibilities in 2018

The Committee met 12 times during the year and attendance at each meeting is shown on page 69. In 2018, the Committee held a number of unscheduled meetings to both consider and approve the termination arrangements of exiting Directors and consider and approve the remuneration package for the incoming CFO.

Board changes in 2018

There were a number of changes at Board level in 2018: Chris Sellers stepped down from the Board on 23 January 2018, and left the Group on 31 January 2018; and Nick Greatorex stepped down from the Board and left the Group on 30 September 2018.

The termination arrangements are set out on page 97. The terms are in accordance with our remuneration policy and contractual obligations, and were considered equitable in the circumstances.

The Board conducted a thorough external search for our new Chief Financial Officer which resulted in Patrick Butcher being appointed to the Board with effect from 1 January 2019. The Remuneration Committee agreed a remuneration package for Patrick that reflected his considerable experience, comprising an annual salary of £430,000 and, in lieu of a pension scheme contribution, a cash contribution equivalent to 5% of base salary in line with our wider workforce.

Patrick will also be eligible to participate in the Company's annual bonus plan and long-term incentive plan (LTIP) in line with our policy. Buy-out remuneration awards were granted in relation to Patrick's appointment to compensate him for deferred share awards that he forfeited when he left Go-Ahead Group plc. Full details of these awards which are consistent in value and structure with the forfeited awards can be found on page 94.

Variable pay outcomes for 2018

Annual bonus

The maximum annual bonus for the Executive Directors that could be earned in relation to 2018 performance was 200% of salary (unchanged from 2017).

As reported in the Annual Report 2017, the Remuneration Committee exercised discretion in respect of 2017 bonus payments and determined that no bonus would be paid to Executive Directors for a second consecutive year. In this context, and with a new CEO recently appointed, the Executive Directors bonus plan for 2018 was redesigned to align with the transformation plan. Accordingly, the bonus plan was based on a rounded assessment of Group financial performance, incorporating free cash flow, cost-out measures alongside adjusted profit before tax (PBT)[1] as well as a set of individual non-financial objectives that directly align to what is required to deliver the transformation plan. Based on the assessment of performance against targets, the achievement of the financial element is 75% of maximum.

In 2018, under the leadership of Jon Lewis, the Group reported adjusted profit before tax ahead of expectations. Jon oversaw a strategic review of the business, built a new leadership team, and has shown highly effective and visible leadership. He has delivered significant progress in establishing a culture that places importance on integrity, transparency, accountability, collaboration and inclusion. The transformation of the business continues at pace and significant improvements have been delivered in efficiency and competitiveness. There was unanimous support for the decision to make an award to reflect the contribution that the new CEO has made to strengthening the business and positioning it for success. Based on this achievement, the Remuneration Committee has determined that the CEO should receive a bonus of 85% of the 200% opportunity, of which 50% is payable in shares vesting after three years and the remainder as cash and subject to the usual statutory deductions of tax and national insurance.

Nick Greatorex, the former CFO, delivered a very successful rights issue and completed the US debt negotiation. He also set up the programme that resulted in very strong performance against the cost-out target, which exceeded expectations, and delivered what was required to allow the launch of the finance transformation programme. The Remuneration Committee determined that Nick delivered against the personal element of his bonus in full, before leaving Capita on 30 September 2018. Therefore, the total bonus paid to Nick for the period to 30 September 2018 was 87.51% of the maximum of his pro-rated bonus opportunity.

1 Adjusted profit before tax before significant new contracts and restructuring.

Vesting of 2016 LTIP award

Vesting of the LTIP Award granted in 2016 was determined by a combination of earnings per share (EPS) and return on capital employed (ROCE) performance and absolute share price, all assessed over the three-year period to 31 December 2018. As the share price performance target was not met, these awards will lapse in full during 2019.

Pay decisions for 2018

Performance measures for 2018 LTIP award

Our corporate strategy aims to simplify and strengthen the business so that it is more focused and predictable – with improved returns, stronger client relationships and sustainable free cash flow. The Committee set five, equally weighted performance measures for the 2018 LTIP award which are directly aligned to successful delivery of this strategy. Any pay-out against these measures is subject to satisfaction of a general performance underpin focused on underlying and operational performance. The Committee can therefore, in its discretion, reduce the level of vesting from than that achieved based on the formulaic application of the five applicable performance measures alone.

The three financial measures (underpinned by financial/operational performance assessment) are key deliverables of the new strategy. The 'target' level of performance for each measure is stated on page 96 and reflects the targets stated in the April 2018 strategy announcement and rights issue prospectus:

- Annualised cost savings – part of Capita's new strategy involves improving cost competitiveness and operational efficiency, which includes reducing general and administrative expenses, centralising procurement, standardising and investing in processes and systems, and increasing the use of offshoring and automation. The Board is targeting annualised initial cost savings of £175m by the end of 2020 from these initiatives compared to the prior forecasted cost. If this was achieved, there would be a 50% vesting of this proportion of the award.
- Free cash flow – the successful implementation of the new strategy is expected to generate at least £200m of sustainable annual, post-tax free cash flow in 2020 before exceptional and restructuring charges, and additional pension contributions. If the free cash flow target is met, 50% of this proportion of the award would vest.
- EBIT margin – successful delivery of the strategy is expected to deliver a double-digit EBIT margin within three years, which would result in at least 50% vesting of this proportion of the award. The EBIT margin range has been set between 9% to 12%.

To complement the financial measures, the LTIP awards are also subject to two key non-financial deliverables of the new strategy (again underpinned by financial/operational performance assessment) in order to drive cultural change and emphasise their importance to management, employees and other stakeholders:

- Customer satisfaction – client demands are changing with fewer long-term, large-scale deals and more incremental sales on existing contracts, or smaller new contracts in which companies prove their value and grow over time. Improving the client experience is therefore fundamental to Capita's long-term success. The customer net promoter score is used to assess this metric. A threshold target of a six-point positive swing in the customer net promoter score would allow for a 25% vesting of this proportion of the award. The maximum would vest if there was a 12-point positive swing in customer net promoter score.
- Employee engagement – a key focus of the new strategy is improving culture and engagement across all levels of the organisation and producing better aligned behaviour around winning and execution of contracts. The employee net promoter score is used to assess this metric. If a six-point positive swing in employee net promoter score was achieved, 25% of this proportion of the award would vest. The maximum would vest, if there was a 12-point positive swing in employee net promoter score.

For both of these non-financial measures, the Remuneration Committee has set targets that require significant improvement over the three-year performance period.

Directors' remuneration report continued

Pay decisions for 2019

Base salaries

Base salary for Jon Lewis is fixed at £725,000 and will be reviewed in 2021. Patrick Butcher's base salary of £430,000 will be reviewed in 2020 and annually thereafter.

Annual bonus

The Remuneration Committee has reviewed the annual bonus plan to ensure it continues to align with the Group's transformation programme. As there has been no material change in our new corporate strategy, the structure of the proposed financial performance measures for the 2019 annual bonus remains broadly unchanged, although some minor adjustments have been made. For 2019 there is no cost-out target and organic revenue growth is being included. This reflects the momentum gained on transformation in 2018, and the need to shift the focus to organic revenue growth and profit improvement. The non-financial performance measures support the delivery of our three strategic pillars which are simplify, strengthen and succeed. Adjusted PBT, free cash flow, organic revenue growth and strategic/personal targets will be stretching for the 2019 financial year. The Committee deems the specific details of the performance measures and targets to be commercially sensitive, as they are directly linked to the forward-looking strategic plans of the business. Full disclosure will be provided in the Annual Report on Remuneration for 2019, provided these details are no longer considered sensitive.

The maximum bonus opportunity will remain at 200% of salary for Jon Lewis, and Patrick Butcher will have a maximum bonus opportunity of 175% of salary, which is a reduction to the prior CFO maximum of 200% of salary. The split between Group financial metrics and personal and strategic measures will be two-thirds financial and one-third non-financial which represents a greater weighting on financial measures compared to 2018. Any bonus pay-outs will be conditional upon Capita achieving an adjusted PBT underpin target. If warranted by the circumstances at the time, the Remuneration Committee may consider exercising its discretion in relation to bonus pay-outs.

Performance measures for 2019 LTIP award

As there has been no further material change in our new corporate strategy, the structure of the proposed performance measures for 2019 LTIP awards remains broadly unchanged from that used for 2018 LTIP awards. However, our proposal does contain three changes, which were informed by feedback from shareholders:

Addition of organic revenue growth as a performance measure

As outlined in our April 2018 strategy update, Capita's reported growth has been largely driven by acquisitions and organic growth has had less emphasis. A return to stronger organic revenue growth is an important goal in the next phase of our business transformation and accordingly has been added as a performance measure for the 2019 LTIP award cycle.

Removal of annualised cost savings as a performance measure

Business simplification is a key element of the initial phase of our strategic transformation. As we expect 2020 to represent the end of the initial simplification phase, we have concluded that it would be inappropriate to retain cost savings as a performance measure for the 2019 LTIP award where the performance period runs to the end of 2021. This change also avoids the risk of executives potentially being rewarded twice for delivery of the same cost savings.

Reduction of the weighting for customer and employee performance measures

When we consulted with shareholders about the 2018 LTIP award, there was widespread support for our use of customer and employee measures as being fundamental to Capita's long-term success. However, some shareholders expressed concern about the proportion of the award subject to these non-financial measures (notwithstanding the performance underpin which looks at underlying financial and operational performance). Recognising these concerns, the Committee has reduced the weighting on customer/employee measures to 25% of the 2019 LTIP award (2018:40%), with the proportion to be reviewed again for future awards.

Performance underpin	Performance measure	Weighting	
		2018 LTIP award	2019 LTIP award
Assessment of the underlying financial and operational performance of Capita over the performance period.	Free cash flow	20%	25%
	EBIT margin	20%	25%
	Organic revenue growth	–	25%
	Annualised cost savings	20%	–
	Customer satisfaction	20%	12.5%
	Employee engagement	20%	12.5%

Further details of the targets are on page 91. For awards made from 2019 onwards, there will be a requirement for Executive Directors to hold shares for an additional two-year period following the three-year performance period. Jon Lewis's LTIP award will be in respect of shares worth 300% of salary. Patrick Butcher's award will be worth 200% of salary (agreed as part of his appointment) and consistent with awards granted to his predecessor.

Shareholding guidelines

Following the decision in 2017 to increase the minimum shareholding guideline for Executive Directors, the minimum requirement is 200% of salary for the Chief Financial Officer and 300% for the Chief Executive Officer. Directors are expected to retain at least half of vested share awards (post-tax) until they are compliant with the guideline. The Committee is in the process of developing a post-employment shareholding policy which will be disclosed in the Annual Report 2019.

Shareholder views

During 2018, we consulted with our top 30 shareholders to obtain their views on the proposed performance measures and targets for the 2018 LTIP award. We received a wide range of feedback, which was helpful to the Committee in coming to the decision to implement the measures and targets as detailed on page 96. Further feedback from shareholders has been reflected in the measures and weightings for the 2019 LTIP, as set out above, which in consultation received strong support from major shareholders. Details of voting on remuneration resolutions at the AGM in June 2018 are set out on page 89.

I hope you will find this report to be clear and helpful in understanding our remuneration practices and that you will be supportive of this year's advisory vote to approve the Annual Report on Remuneration at the AGM (set out on pages 89–98). The Committee will continue to consult widely with shareholders to respond to their expectations of remuneration policy and reporting and welcomes feedback.

Committee Chair

I have informed the Board of my intention to step down as Chair of the Committee after three-and-a-half years, but will remain on the Board as a Non-Executive Director. I took up a new CEO role in 2018 and feel I can no longer provide Capita with the time and attention the Chair's role requires. I will remain as Chair until a replacement is appointed to ensure a smooth handover.

John Cresswell
Chair
Remuneration Committee
13 March 2019

Remuneration policy

At the AGM in June 2017 shareholders approved, with a 89.2% majority, the remuneration policy which sets out the Company's policy on the remuneration of Executive and Non-Executive Directors. The remuneration policy became effective from the conclusion of the AGM and will apply until 31 December 2020 unless a revised policy is approved by shareholders and comes into force before that date.

For the benefit of shareholders we have included the remuneration policy on the following pages. Textual changes have been made, where appropriate, to ensure the report is relevant within the context of this Directors' remuneration report. The original remuneration policy, as approved by shareholders, can be found in the Directors' remuneration report of the 2016 Annual Report & Accounts (which can be found in the Investors section of our website).

The Committee is responsible, on behalf of the Board, for establishing appropriate remuneration arrangements for the Chairman, Executive Directors, Executive Committee and Group Company Secretary. The remuneration of Non-Executive Directors is determined by the Board.

The information provided in this section of the remuneration report is not subject to audit.

Responsibilities and activities of the Remuneration Committee

The Committee is responsible for determining and agreeing with the Board the policy on Executive Directors' remuneration, including setting the over-arching principles, parameters and governance framework and determining the initial remuneration package of each Executive Director. In addition, the Committee monitors the structure and level of remuneration for the senior management team and, when setting remuneration Executive Directors, take into account workforce remuneration and alignment of incentives and rewards with culture.

In setting the remuneration policy for the Executive Directors, the Committee ensures that the arrangements are in the best interest of both the Group and its shareholders, by taking into account the following general principles:

- To ensure total remuneration packages are simple and fair in design so that they are valued by participants.
- To ensure that total remuneration is clear, predictable and highly performance orientated, without being excessive.
- To balance performance-related pay between the achievement of financial performance objectives and delivering sustainable performance; creating a clear connection between performance and reward and providing a focus on sustained improvements in profitability and returns.
- To provide a significant proportion of performance-linked pay in shares allowing senior management to build a significant shareholding in the business and, therefore, aligning management with shareholders' interests and the Group's performance, without encouraging excessive risk-taking.

Consideration of shareholder views

The Company is committed to maintaining good communications with investors. The Committee considers the AGM to be an opportunity to meet and communicate with investors, giving shareholders the opportunity to raise any issues or concerns they may have. In addition, the Committee will seek to engage directly with major shareholders and their representative bodies should any material changes be proposed to the policy.

Directors' remuneration report continued

Remuneration policy table

The following table sets out the key aspects of the policy.

Base salaries

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
To attract and retain talent by ensuring base salaries are sufficiently competitive.	Normally reviewed annually in December, with any changes usually effective in January. The Committee may award salary increases at other times of the year if it considers it to be appropriate. The review takes into account: • Salaries in similar companies and comparably-sized companies • Remuneration Policy • Economic climate • Market conditions • Group performance • The role and responsibility of the individual Director • Employee remuneration across the broader workforce.	There is no prescribed maximum monetary annual increase to base salaries. Any annual increase in salaries is at the discretion of the Committee, taking into account the factors stated in this table and the following principles: • Salaries would typically be increased at a rate consistent with the average salary increase (in percentage of salary terms) for the broader workforce. • Larger increases may be considered appropriate in certain circumstances (including, but not limited to, a change in an individual's responsibilities or in the scale of their role or in the size and complexity of the Group). • Larger increases may also be considered appropriate if a Director has been initially appointed to the Board at a lower than typical salary.	Individual and business performance are considerations in setting base salaries.

Annual bonus and deferred annual bonus (DAB) Plan

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Performance measures are selected to focus Executives on delivery of the Group business plan for the financial year.	The bonus scheme is reviewed annually to ensure that bonus opportunity and performance measures continue to support the business plan. Stretching targets are set at the start of each financial year. Performance against targets is reviewed following completion of the final accounts for the period under review. 50% of any bonus earned is normally delivered in shares deferred for three years under the DAB plan, with the remainder delivered in cash or Deferred Shares at the Executive Director's discretion. An additional payment may be made at the time of vesting in respect of dividends that would have accrued on Deferred Shares during the deferral period. Malus and clawback provisions apply to all annual bonus and DAB awards for a period of up to three years after the determination of the annual bonus.	Maximum opportunity of 200% of salary.	Executive Directors' performance is measured over a one-year period relative to challenging targets for selected measures of Group financial, strategic or individual performance. The majority of the bonus will be determined by measure(s) of Group financial performance. A sliding scale is set for each Group financial measure: 50% of the bonus will be paid at target performance, increasing to 100% for maximum performance. Any bonus pay-out is ultimately at the discretion of the Committee.

Long-term incentive plan (LTIP)

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Designed to reward and retain Executives over the longer term while aligning their interests with those of shareholders. To link reward to key longer-term business targets. To encourage share ownership.	LTIP awards are usually granted in the form of nil cost options. Award levels for each award are set by the Committee at a level appropriate, in the Committee's opinion, with the individual's performance and experience. Performance targets applying to LTIP awards are relevant to business plan priorities and aligned with shareholder interests. Vesting is dependent on the achievement of performance conditions usually measured over a three-year period. Awards from 2019 must be retained for a further two years after vesting. An additional payment may be made at the time of vesting in respect of dividends that would have accrued on LTIP awards during the vesting period. Malus and clawback provisions apply to all LTIP awards for a period up to the fifth anniversary of grant.	The maximum annual award permitted under the LTIP is shares with a market value (as determined by the Committee) of 300% of salary.	Performance is measured relative to selected measures of Group financial or share price performance, with the precise measures and weighting of the measures determined by the Committee ahead of each award. Performance targets are reviewed annually by the Committee and are set appropriate to the economic and political outlook and risk factors prevailing at the time, ensuring that such targets remain challenging in the circumstances, while remaining realistic enough to motivate and incentivise management. 25% of the awards vest at a threshold vesting point, rising to 100% vesting at a maximum vesting point.

Benefits

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Designed to be consistent with benefits available to employees in the Group.	Benefits include car allowance, private medical insurance, travel and property hire. Executive Directors can also participate in all-employee share plans. The Committee has discretion to add additional benefits which are not currently provided, such as relocation expenses.	Benefit provision varies between different Executive Directors. While there is no maximum level set by the Committee, benefits provision will be set at a level the Committee considers appropriate and be based on individual circumstances. Participation in the Company's HMRC-approved all-employee share plan will be limited by the maximum level prescribed by HMRC.	Not performance-related.

Pension

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Designed to be consistent with benefits available to employees in the Group.	Pension contributions are paid into the Group's defined contribution scheme and/or as a cash allowance.	5% of salary	Not performance-related.

Directors' remuneration report continued

Non-Executive Director (NED) fees

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Market competitive fees are set so as to attract and retain Non-Executive Directors with required skills, experience and knowledge so that the Board can effectively carry out its responsibilities.	Reviewed periodically by the Board. Fee levels set by reference to market rates, taking into account the individual's experience, responsibilities, time commitment and pay decisions for the broader workforce. NED fees comprise payment of an annual basic fee and additional fees for further Board responsibilities such as: • Senior Independent Director • Audit Committee Chairman • Remuneration Committee Chairman. The Chairman of the Board receives an all-inclusive fee. No NED participates in the Group's incentive arrangements or pension plan or receives any other benefits other than where travel to the Company's registered office is recognised as a taxable benefit in which case a NED may receive grossed-up costs of travel as a benefit.	As for the Executive Directors, there is no prescribed maximum monetary annual increase. An aggregate annual sum of £1m increased only to take account of the effect of inflation as measured by the Retail Price Index or such index as the Directors consider appropriate or such other amount as the Company may by ordinary resolution decide.	Not performance-related.

Malus and clawback provisions apply to all incentive awards granted to Executive Directors. These provisions permit the Committee to recover bonus awards for up to three years after the determination of the annual bonus and up to the fifth anniversary of the grant of LTIP awards. The potential circumstances in which malus or clawback provisions can be applied include a material misstatement of the Group's financial results, if an individual deliberately misleads relevant parties regarding financial performance or if their actions cause reputational damage or amount to serious misconduct or conduct which causes significant financial loss.

The annual bonus performance measures are Group financial, strategic or individual measures which are selected annually so as to be consistent with key priorities for the Group.

The LTIP performance measures are chosen to provide alignment with our longer-term strategy of growing the business in a sustainable manner that will be in the best interests of shareholders and other key stakeholders in the Company.

Targets are set on sliding scales that take account of internal strategic planning and external market expectations for the Company. Only modest rewards are available for achieving threshold performance with maximum rewards requiring substantial outperformance of challenging strategic plans approved at the start of each year.

Share incentive plans incorporate the right to receive an amount (in cash or additional shares) equal to the value of dividends which would have been paid on the shares under an award that vests up to the time of vesting/release. This amount may be calculated assuming that the dividends have been re-invested in the Company's shares on a cumulative basis.

The Committee operates incentive arrangements for the Executive Directors in accordance with their respective rules, the Listing Rules and the HMRC rules where relevant. The Committee, consistent with market practice and the scheme rules, retains discretion over a number of areas relating to the operation and administration of the plans. These include (but are not limited to) the following:

- Who participates
- The form in which the award is granted and settled (e.g. shares, nil cost options, cash)
- The timing of the grant of award and/or payment
- The size of an award (up to individual and plan limits) and/or a payment
- Discretion relating to the measurement of performance in the event of a 'good leaver' scenario or a change of control or reconstruction of the Company
- Determination of a good leaver (in addition to any specified categories) for incentive plan purposes
- Adjustments required in certain circumstances (e.g. share capital variation, rights issues, demerger, corporate restructuring, special dividends)
- The ability to vary or substitute any performance condition(s) if circumstances occur which cause it to determine that the original condition(s) have ceased to be appropriate, provided that any such variation or waiver is fair, reasonable and not materially less difficult to satisfy than the original condition (in its opinion). In the event that the Committee were to make an adjustment of this sort, a full explanation would be provided in the next remuneration report.

The Committee reserves the right to make any remuneration payments and/or payments for loss of office (including exercising any discretions available to it in connection with such payments) notwithstanding that they are not in line with the Policy set out above where the terms of the payment were agreed: (i) before the 2014 AGM (when the Company's first shareholder-approved Directors' Remuneration Policy came into effect); (ii) before the Policy set out above came into effect, provided that the terms of the payment were consistent with the shareholder-approved Directors' Remuneration Policy in force at the time they were agreed; or (iii) at a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, the payment was not in consideration for the individual becoming a Director of the Company. For these purposes 'payments' includes the Committee satisfying awards of variable remuneration and, in relation to an award over shares, the terms of the payment are 'agreed' at the time the award is granted.

The Committee may make minor amendments to the policy set out in this Policy Report (for regulatory, exchange control, tax or administrative purposes or to take account of a change in legislation) without obtaining shareholder approval for that amendment.

Application of our remuneration policy

When determining Executive Director remuneration policy and practices, the Committee reviews workforce remuneration and related polices and the alignment of incentives and rewards with culture.

LTIP awards are granted across the senior management population in order to encourage a high level of employee share ownership. While vesting of regular LTIP awards made to Executive Directors is always subject to performance conditions, awards to other senior management may, where appropriate (such as to assist in retention of key talent), be subject only to continued employment. Another key difference in the policy for Executive Directors is that remuneration is more heavily weighted towards long-term variable pay than other employees. This ensures that there is a clear link between the value created for shareholders and the remuneration received by the Executive Directors. The Committee did not formally consult with employees in respect of the design of the policy, although the Committee will keep this under review.

Directors' recruitment and promotions

The Committee takes into account the need to attract, retain and motivate the best person for each position, while at the same time ensuring a close alignment between the interests of shareholders and management.

If a new Executive Director were to be appointed, the Committee would seek to align their remuneration package with other Executive Directors in line with the policy table. However, flexibility would be retained to offer additional remuneration on appointment outside the policy if the Committee believe it may be appropriate to make 'buy-out' awards or payments in respect of remuneration arrangements and contractual terms forfeited on leaving a previous employer. The Committee would look to replicate the arrangements being forfeited as closely as possible and in doing so, would take account of relevant factors including the nature of the remuneration and contractual terms, performance conditions and the time over which they would have vested or been paid.

The Committee would seek to structure awards on recruitment to be in line with the Company's remuneration framework so far as practical but, if necessary, the Committee may also grant such awards outside of that framework as permitted under Listing Rule 9.4.2. If appropriate, a new appointee's incentives in their year of joining may be subject to different targets to other Executive Directors. The Committee may also agree that the Company will meet certain relocation and incidental expenses as it considers appropriate.

The maximum level of variable remuneration which may be granted (excluding awards to compensate for remuneration arrangements and contractual terms forfeited on leaving the previous employer) to new Executive Directors in the year of recruitment shall be limited to 500% of salary (the maximum limit allowed within the policy table).

The initial notice period for a service contract may be up to 24 months, which is longer than the policy of a 12-month notice period, provided it reduces to 12 months within a short space of time.

For an internal appointment or an appointment following the Company's acquisition of or merger with another company, any incentive amount awarded in respect of a prior role may be allowed to vest on its original terms, or adjusted as relevant to take into account the appointment. Any other ongoing remuneration obligations or terms and conditions existing prior to appointment may continue.

The Committee retains discretion to make appropriate remuneration decisions outside the standard Policy to meet the individual circumstances of recruitment when:

- An interim appointment is made to fill an Executive Director role on a short-term basis.
- Exceptional circumstances require that the chairman or a Non-Executive Director takes on an executive function on a short-term basis.

In the event of the appointment of a new Non-Executive Director, remuneration arrangements will normally be in line with the structure set out in the policy table for Non-Executive Directors. However, the Committee (or the Board as appropriate) may include any element listed in the policy table or any other element which the Committee considers is appropriate given the particular circumstances excluding any variable elements, with due regard to the best interests of shareholders.

Directors' service agreements and payments for loss of office

The Committee regularly reviews the contractual terms of the service agreement to ensure these reflect best practice.

The service contracts for Executive Directors are for an indefinite period and provide for a 12-month notice period. They do not include provisions for predetermined compensation on termination that exceed 12-months' salary, pension and benefits. There are no arrangements in place between the Company and its Directors that provide for compensation for loss of office following a takeover bid. All Directors are appointed for an indefinite period but are subject to annual re-election at the annual general meeting.

In circumstances of termination on notice, the Committee will determine an equitable compensation package, having regard to the particular circumstances of the case. The Committee reserves the right to make payments in connection with a Director's cessation of office or employment where the payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of a compromise or settlement of any claim arising in connection with the cessation of a Director's office or employment. Any such payments may include, but are not limited to, paying any fees for outplacement assistance and/or the Director's legal and/or professional advice fees in connection with his cessation of office or employment. The Committee has discretion to require notice to be worked or to make payment in lieu of notice or to place the Director on garden leave for the notice period.

Directors' remuneration report continued

The annual bonus may be payable in respect of the period of the bonus plan year worked by the Director; there is no provision for an amount in lieu of bonus to be payable for any part of the notice period not worked. The Remuneration Committee has some discretion on bonus pay-outs.

DAB deferred shares will vest on the date of leaving, other than in circumstances of dismissal for gross misconduct.

For entitlement to unvested LTIP shares, the rules contain discretionary provisions setting out the treatment of awards where a participant leaves for designated reasons (i.e. participants who leave early on account of injury, disability or ill health, death, a sale of their employer or business in which they were employed, statutory redundancy or any other reason at the discretion of the Committee). In these circumstances, a participant's awards will not be forfeited on cessation of employment and instead will continue to vest on the normal vesting date or earlier at the discretion of the Committee, subject to the performance conditions attached to the relevant awards. The awards will, other than in exceptional circumstances, be scaled back on a time pro-rated basis.

In the event of a change of control, all unvested LTIP awards would vest, to the extent that any performance conditions attached to the relevant awards have been achieved. LTIP awards will, other than if the Committee determines otherwise, be scaled back pro rata for the proportion of the performance period worked by the Director prior to the change of control. Unvested DAB deferred shares would vest in the event of a change of control.

Non-Executive Directors' terms of engagement

Non-Executive Directors are appointed by letter of appointment for an initial period of three years. Each appointment is terminable by three months' notice on either side. At the end of the initial period, the appointment may be renewed by mutual consent, subject to annual re-election at the AGM.

The service agreements and Non-Executive Directors' letters of appointment are available for inspection during normal business hours at the Company's registered office, and available for inspection at the AGM.

Annual Report on Remuneration

This part of the remuneration report has been prepared in accordance with The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 and paragraphs 9.8.6R and 9.8.8 of the Listing Rules. The Annual Report on Remuneration will be put to an advisory shareholder vote at the 2019 AGM. The information on pages 92–97 has been audited as indicated.

External advice received

Deloitte LLP was, following a review, appointed by the Remuneration Committee during 2012 to provide advice on Executive remuneration matters. During the year, the Committee received independent and objective advice from Deloitte primarily on market practice, disclosure within the accounts and stakeholder liaison. Deloitte was paid £160,100 in fees during 2018 for these services (charged on a time plus expenses basis). The Committee considers Deloitte's advice on remuneration to be independent and objective, and notes that Deloitte is a founding member of the Remuneration Consultants Group. As such, Deloitte operates voluntarily under the code of conduct in relation to Executive remuneration consulting in the UK. In addition, other practices of Deloitte, separate from the Executive remuneration practice, have provided services to the Group in respect of tax, property, advice to internal audit and other ad hoc advisory projects during the year.

The fees were considered appropriate for the work undertaken. Where appropriate, fees were tendered with other providers to ensure that the fees were in line with market practice and standards.

The Committee also consulted with Jon Lewis to provide further information to the Committee on the performance and proposed remuneration for the Chief Financial Officer and other senior management, but not in relation to his own remuneration.

Shareholder voting at the AGM

The 2018 Directors' remuneration report will be presented to shareholders at the annual general meeting in May 2019. At the AGM in 2018, the actual voting in respect of the ordinary resolution to approve the remuneration report for the year ended 31 December 2017 was as set out below. Details of the last shareholder vote on our remuneration policy are also set out below.

	Votes cast 'for'	Votes cast 'against'	Abstentions[1]
Remuneration report: for the year ended 31 December 2017	1,268m	13.8m	3.61m
	98.9%	1.1%	–
Remuneration policy: voted on in June 2017	503.9m	60.8m	0.09m
	89.2%	10.8%	–

1 A vote abstained is not a vote in law and is not counted in the calculation of the proportion of votes 'for' and 'against' a resolution.

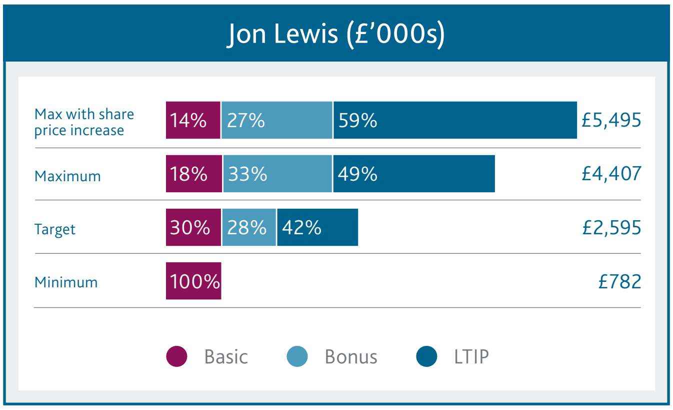
Directors' remuneration report continued

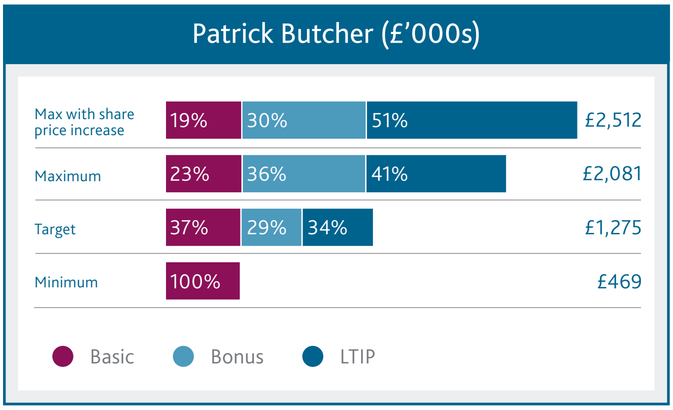
Statement of implementation of the remuneration policy for 2019

The value and composition of the Executive Directors' remuneration packages under the policy for the year ending 31 December 2019 at a minimum, target and maximum performance level are set out in the charts below.

The charts are for illustrative purposes only and actual outcomes may differ from that shown.

Each chart is broken down to show how the total under each scenario is made up of fixed elements of remuneration, the annual bonus and the LTIP.





Basic includes the base salary, benefits and pension (i.e. the fixed elements of remuneration).

Notes

The scenarios in the above charts are defined as follows:

	Minimum	Performance in line with expectations (target)	Maximum
Fixed elements of remuneration	Base salary at 1 January 2019 Estimated value of benefits provided under the remuneration policy 5% of salary pension provision		
Annual bonus: pay-out shown as a maximum opportunity	0%	50% of maximum	100% of maximum
LTIP: pay-out shown as a maximum opportunity	0%	50% of maximum	100% of maximum

As set out in the policy table above, the maximum permitted annual bonus opportunity is 200% of salary and the maximum permitted LTIP award is 300% of salary. The charts above reflect the maximum bonus (200% of salary for the CEO and 175% of salary for the CFO) and maximum LTIP award (300% of salary for the CEO and 200% of salary for the CFO) that could be earned in 2019. The maximum that can be earned by the CFO in 2019 is lower than the maximum permitted under the policy.

In these charts, deferred shares are presented within the bonus and dividend equivalents have been excluded.

In these charts, LTIP awards have been shown both at face value with no share price growth and a 50% share price growth across the performance period under the maximum scenario.

All-employee share plans have been excluded.

Base salary

Base salary for Jon Lewis is unchanged and fixed at £725,000 until 1 January 2021. Patrick Butcher joined Capita on 10 December 2018 and the Board on 1 January 2019; his salary is £430,000.

Accordingly, base salaries for 2019 are:

	Base salary from 1 January 2019
Jon Lewis	£725,000
Patrick Butcher	£430,000

Fees for the Chairman and Non-Executive Directors

A summary of the fees for 2019 are as follows:

	Fee from 1 January 2019 or date of appointment
Sir Ian Powell, Chairman	£325,000
Gillian Sheldon, Senior Independent Director	£75,000
Matthew Lester, Audit and Risk Committee Chairman[1]	£75,000
John Cresswell, Remuneration Committee Chairman[1]	£75,000
Andrew Williams	£64,500
Baroness Lucy Neville-Rolfe	£64,500

1 Chairmen of Committees have had a fee increase from £64,500 following a review of the time commitment associated with these roles. Other Non-Executive Directors' fees are unchanged.

At the 2019 AGM, shareholders will be asked to approve the election and remuneration of two Employee Directors. They will receive a basic fee of £64,500 each and further details of their remuneration will be set out in an explanatory memorandum which will be available 15 days before the AGM on the Company's website and at the Company's registered office, and will be available for inspection at the AGM itself.

Annual bonus for 2019

The CEO's maximum bonus opportunity for 2019 will be 200% of base salary and the CFO's maximum bonus opportunity for 2019 will be 175% of base salary, with 50% of any bonus normally deferred into shares for three years.

As explained in the Remuneration Committee Chairman's statement, the Executive Director bonus plan for 2019 continues to align with the transformation plan, with a combination of financial and individual non-financial objectives that support the delivery of our strategy. Accordingly, the following weightings and measures have been agreed by the Committee:

	Weighting	
	Jon Lewis	Patrick Butcher
Group financial performance measures	67% (Adjusted PBT, free cash flow, organic revenue growth)	67% (Adjusted PBT, free cash flow, organic revenue growth)
Group strategic and individual performance measures	33%	33%

The Remuneration Committee may consider exercising discretion on annual bonus pay-outs. No payment would be made if Capita failed to achieve an adjusted PBT target for 2019.

Details of the Group strategic and individual performance measures and the targets for the Group financial performance measures are considered commercially sensitive by the Board and so will be disclosed retrospectively in the 2019 remuneration report.

Any bonus payments will be subject to malus and clawback provisions as outlined in the Directors' remuneration policy.

Long-term incentive to be granted in 2019

Awards will be granted over shares worth 300% of salary to Jon Lewis and worth 200% of salary to Patrick Butcher. Awards will vest subject to (i) assessment by the Remuneration Committee of the underlying financial and operational performance of Capita over the three-year period to 31 December 2021 (the 'underpin'), and (ii) subject to satisfaction of the underpin, organic revenue growth, free cash flow, margin enhancement, customer satisfaction and employee engagement performance over the same three-year period to 31 December 2021.

Performance measures, weighting and targets for the 2019 LTIP award, and the performance underpin, are as follows:

Performance underpin	Performance measure	Weighting	Threshold	Target	Stretch
			(25% vests)	(50% vests)	(100% vests)
Assessment of the underlying financial and operational performance of Capita over the performance period	Free cash flow[1]	25%	£190m	£210m	£250m
	EBIT margin[1]	25%	9%	10%	12%
	Organic revenue growth[1]	25%	£3,900m	£3,950m	£4,050m
	Customer satisfaction	12.5%	6 point positive swing in NPS	8 point positive swing in NPS	12 point positive swing in NPS
	Employee engagement	12.5%	6 point positive swing in NPS	8 point positive swing in NPS	12 point positive swing in NPS

1 For the financial year 2021.

The Committee has actively considered how it may ensure executives do not benefit from share price volatility in the timing of the 2019 LTIP award, and the implications for ensuring future gains are reflective of underlying performance. The Committee has therefore decided that the number of shares in the 2019 LTIP award will be calculated using the higher of either the closing price on the day immediately prior to the award,or the post-rights issue price of 122.08p.

As stated in the notes to the Policy table, the Committee retains discretion to make adjustments required in certain circumstances including varying the performance conditions if circumstances occur which cause it to determine that the original conditions have ceased to be appropriate, provided that any such variation or waiver is fair, reasonable and not materially less difficult to satisfy than the original condition (in its opinion). In the event that the Committee were to make an adjustment of this sort, a full explanation would be provided in the next remuneration report.

The Committee also has a general discretion to override formulaic outcomes in line with the changes to the UK Corporate Governance Code.

Any vested LTIP awards will be subject to malus and clawback provisions as outlined in the Directors' Remuneration Policy.

The net number of shares received on vesting of LTIP awards will be subject to an additional two-year holding period after the initial three-year vesting period.

Directors' remuneration report continued

Directors' remuneration earned in 2018 – single-figure table (audited)

The table below summarises Directors' remuneration received in 2018.

Single figure remuneration

		Base salary and fees	Benefits	Pension or Pension Allowance	Annual Bonus[4]	LTIP	Total Remuneration
Ian Powell	2018	325,000	347	—	—	—	325,347
	2017	325,000	216	—	—	—	325,216
Jon Lewis[1]	2018	725,000	24,809	36,250	1,228,150	—	2,014,209
	2017	60,417	41,216	3,021	—	—	104,654
Gillian Sheldon	2018	75,000	153	—	—	—	75,153
	2017	75,000	216	—	—	—	75,216
Matthew Lester	2018	64,500	770	—	—	—	65,270
	2017	53,750	216	—	—	—	53,966
John Cresswell	2018	64,500	229	—	—	—	64,729
	2017	64,500	216	—	—	—	64,716
Andrew Williams	2018	64,500	154	—	—	—	64,654
	2017	64,500	—	—	—	—	64,500
Baroness Lucy Neville-Rolfe	2018	64,500	13	—	—	—	64,513
	2017	4,607	—	—	—	—	4,607
Nick Greatorex[2,3,5]	2018	307,500	25,543	15,375	538,125	—	886,543
	2017	454,048	30,163	20,500	—	—	504,711
Chris Sellers[3,5]	2018	30,000	5,555	1,500	—	—	37,055
	2017	360,000	83,714	18,000	—	—	461,714

1 Jon Lewis was appointed Chief Executive Officer on 1 December 2017. He is also a Non-Executive Director of Equinor ASA and received and retained a fee of NOK 212,623.
2 Nick Greatorex was appointed interim CEO in respect of the period from 16 September 2017 to 30 November 2017 and was paid an allowance of £12,500 per month in respect of his additional responsibilities up to 31 December 2017 (including a one-month handover period to Jon Lewis). This is reflected in the 2017 figure for base salary.
3 Chris Sellers and Nick Greatorex stepped down from the Board on 23 January 2018 and 30 September 2018 respectively. Amounts shown in the table for Chris Sellers and Nick Greatorex relate to the period of time during which they served as Directors.
4 50% of Jon Lewis's bonus will be deferred into shares under the Deferred Annual Bonus Plan.
5 2017 comparatives updated to present the value of the final matching shares award under the UK all-employee scheme for Nick Greatorex £279 and Chris Sellers £310.

For 2017, in addition to the amounts noted above, total remuneration was also paid to the following Directors who left during 2017: Paul Bowtell £27,091; Andy Parker £494,070; and Vic Gysin £416,931.

Base salary includes base salary plus fixed cash allowances which are a normal part of the fixed remuneration package and usual local practice. Benefits include all taxable benefits as defined by paragraph 11(1) of Schedule 8 to the Accounts regulations. This includes private medical insurance, company car allowance, work travel, accommodation and the value of matching awards under the UK all-employee scheme. In 2017, for Jon Lewis, this figure also included one-off legal fees associated with the negotiation of his service contract. Employee entertainment has also been included under benefits and in some cases this cost will be for more than the individual Director themselves.

Performance targets for the 2016 LTIP awards were, for awards of more than 20,000 shares, EPS growth of 6% (18.75% vest) to 12% (75% vest), average ROCE 14% (6.25% vest) to 16% (25% vest) over the three-year period to 31 December 2018 and average share price at vesting must not be lower than at grant. For awards of 12,001 to 20,000 shares and awards up to 12,000 shares the targets were identical except that 50% and 75%, respectively, of the award would vest at 6% EPS. As the share price at vesting was lower than grant, the award did not vest.

No Director waived any fees or salary for 2018.

Patrick Butcher commenced employment with Capita on 10 December 2018 and became an Executive Director on 1 January 2019; accordingly, he has not been included in the single figure table for 2018.

Annual bonus for 2018 (audited)

The maximum annual bonus for the Executive Directors that could be earned in relation to 2018 performance was 200% of salary (unchanged from 2017).

The annual bonus that could be paid to Executive Directors in respect of 2018 performance was determined by a combination of Group financial performance alongside an adjusted PBT threshold target underpin and Executive Directors' personal contributions. For Jon Lewis, the split between Group financial metrics and personal and strategic measures was 60:40 and for Nick Greatorex it was 50:50. 50% of the bonus was payable for achieving target performance with 100% payable for achieving the maximum target. 25% of bonus was payable for achieving the threshold target.

The table below illustrates the components of the financial metrics at maximum and actual pay-outs for the targets set for the period to 31 December 2018. There is a straight-line outcome calculation between the threshold target and on-target performance and between on-target and maximum performance. Actual adjusted PBT of £282.1m exceeded the threshold underpin of £245m and therefore based on the assessment of performance against the targets, the achievement on the financial element is 75% of maximum.

	Financial performance weighting	Threshold target performance (25%)	On-target performance (50%)	Maximum performance (100%)	Actual performance and bonus pay-out	Achievement against measure (% maximum opportunity for this measure)
Adjusted profit before tax (pre bonus and includes disposals/ HfS businesses)	50%	£245m	£275m	£297.5m	£282.1m	66%
Free cash flow (adjusted cash position)	25%	£1m	£21m	£41m	£27.5m[1]	66%
Cost-out	25%	£69.9m	£80.0m	£120m	£120m	100%
Financial metrics bonus pay-out						75%

1 Adjusted free cash flow changed for earlier-than-planned clearance of non-recourse trade receivables financing.

In respect of 2018, 40% of Jon Lewis's annual bonus was payable on three equally weighted personal and strategic objectives set on joining Capita which were:

Objective	Delivery	Weighting	Percentage achieved
Completing a full strategic review – deliver a Board agreed strategy and three-year plans for the business by September 2018	In the absence of any prior strategy, and in order to secure a rights issue necessary to address the balance sheet issues discovered upon his arrival at Capita, Jon undertook a strategic review of the business that resulted in Board approval of our simplify, strengthen and succeed strategy, components of which include: • The definition of our five growth platforms; and a portfolio of non-core (value maximisation) businesses, managed within Specialist Services. • A set of unambiguous financial commitments for 2020. • Divisional strategic imperatives that focus leadership efforts and guide resource allocation. • Completion of key disposals to further strengthen the balance sheet. Jon successfully communicated the strategy to employees (the 2018 internal survey found that 81% understood our strategy). The strategy and its associated rights issue, together with the necessary focus on operational imperatives in 2018, have created a much-needed stable foundation on which to embark on the next phase of strategic simplification and focus, which will be undertaken in 2019. There has been positive evolution of the share register, as our strategy is now shaping the markets we focus upon and the allocation of resources to grow the business. The Remuneration Committee deemed performance to exceed expectation for the first 12 months in role and so awarded the maximum achievement to the non-financial element relating to this objective.	13.34%	100%
Driving cultural change – through behaviour and leadership demonstrate positive impact on the values and culture of the Company across the year	The Committee deemed performance to be very strong. Jon has shown highly effective and visible leadership throughout 2018 and over the course of the last 12 months has delivered significant progress in establishing a culture that places importance on integrity, transparency, accountability, collaboration and inclusion. Changes in the executive team and a new approach to managing business reviews was implemented and embedded alongside high levels of engagement with wider stakeholders including employees, suppliers and partners. A new purpose, refreshed values with underpinning behaviours, a revised code of conduct and several new governance and leadership forums have been established which operationalise the culture change being driven from the top. Recent survey results indicate 94% of employees feel they can ask Jon any question, which speaks to a culture of trust. The improvement in the Hampton-Alexander gender diversity rankings year-on-year (from below 200 in 2017 up to 110 and a green status for the first time in 2018). All stakeholders (including clients and external bodies) are now voicing recognition of a reforming Capita. Based on Jon's achievement, the Remuneration Committee has awarded the maximum achievement to the non-financial element relating to this objective.	13.33%	100%
Building the leadership team – restructure the senior management team and bring in top team as appropriate	Jon took decisive action very early on, regarding changes required in the executive team. Proven capability was brought into Capita within the first month to ensure the business had the expertise necessary to address operational imperatives, define strategy and launch the rights issue. Through the year, and shaped by the new strategy, Jon built an experienced Executive Committee (which included seven new roles) with the required professional competencies, values and behaviours necessary to create a collegiate and effective team. Members of the executive team are making a material contribution, have been well received by the broader organisation, including by the Board, and are working well as a team under Jon's leadership. Stakeholders (internal and external) recognise the strength of team now in place. The Remuneration Committee deemed performance to be very strong and awarded the maximum achievement to the non-financial element relating to this objective.	13.33%	100%

Directors' remuneration report continued

The Remuneration Committee has determined that Jon Lewis has achieved the full 40% of his personal and strategic measures. Therefore, the total bonus paid to Jon Lewis for the period to 31 December 2018 was 85% (£1,228,150) of the maximum bonus opportunity, of which £614,075 will be deferred into the shares to be held for three years under the Deferred Annual Bonus Plan. The remainder will be paid as cash, subject to the usual statutory deductions of tax and national insurance.

In respect of 2018, 50% of Nick Greatorex's annual bonus was payable on four equally weighted strategic and personal objectives which are listed below:

- Complete rights issue in 2018 raising £701m from investors including five-year planning, strategy and investor roadshow.
- Complete the US PP debt renegotiation in 2018 prior to the launch of the rights issue, including the covenant changes as required by IFRS 15 and the pre-approval of the divestment programme.
- Set up and lead the cost competitiveness workstream of the transformation programme to deliver the 2018 cost programme, delivering the £70m cost savings set out in the rights issue.
- Ensure the finance transformation programme receives a satisfactory internal audit rating in 2018 and the key milestones for 2018 remain on track for a November 2019 go-live date.

Nick delivered a very successful rights issue, completed the US debt negotiation, set up the programme that resulted in very strong performance against the cost-out target that exceeded expectation, and delivered what was required to allow the launch of the finance transformation programme. The Remuneration Committee has determined that Nick Greatorex achieved the full 50% of his personal and strategic measures before leaving Capita on 30 September 2018. Therefore, the total bonus paid in cash with no deferral to Nick Greatorex for the period to 30 September 2018 was 87.51% (£538,125) of his pro-rated maximum bonus opportunity.

Long-term incentive awards in 2018 (audited)

	Number of shares			
Name of Director	LTIP award	LTIP award following rights issue adjustment	(£) Face value of LTIP award[1]	Percentage of salary[2]
Jon Lewis	1,202,986	1,972,776	2,175,000	300%
Nick Greatorex	453,539	743,758	820,000	200%

1 The date of the grant was 24 April 2018. The closing price on the preceding day of £1.8080 was used to determine the number of shares.
2 Percentage calculated using base salary as at date of award (Jon Lewis – £725,000; Nick Greatorex – £410,000).

LTIP awards are granted as nil-cost options and awarded as a percentage of salary. Awards will vest three years from the date of grant subject to (i) assessment by the Remuneration Committee of the underlying financial and operational performance of Capita over the three-year period to 31 December 2020 (the 'underpin'), and (ii) subject to satisfaction of the underpin, annualised cost savings, free cash flow, margin enhancement, customer satisfaction and employee engagement performance over the same three-year period to 31 December 2020. 25% of LTIP awards vest for achieving threshold performance. Performance targets for the 2018 award were set following consultation with major shareholders. Full details of the performance conditions relating to these awards are outlined on page 96.

Buy-out remuneration awards in 2018

	Number of shares	
Name of Director	2018 award	Total
Patrick Butcher	288,078	288,078

1 The date of the grant was 11 December 2018. The closing price on the preceding day of £1.06 was used to determine the number of shares.

Patrick Butcher was granted a buy-out award under the LTIP as part of his remuneration package on appointment, which will vest in two tranches – 15 November 2019 and 15 November 2021 – subject to continued employment. The award is equal to the value of 6,770 Go-Ahead Group plc shares on 10 December 2018, using their close price of £15.80, and £198,398 representing the value of his forfeited deferred share award which were subject to continued employment.

Directors' interests and shareholding guidelines (audited)

In line with the new remuneration policy approved in 2017, Executive Directors are expected to hold 200% (300% for the Chief Executive Officer) of salary in shares in the Company. This must be built up over a period of five years from appointment. The guidelines include shares held beneficially and also shares within the DAB that have been deferred over the three-year period. Any shares in the DAB used for this are calculated net of tax. Share awards that are subject to performance conditions are not included.

Directors' interests and shareholding guidelines (audited)

Director	Beneficially held interests at 31 December 2018[3]	Beneficially held interests at 31 December 2017[3]	Interests in share incentive schemes, awarded without performance conditions at 31 December 2018	Interests in share incentive schemes, awarded without performance conditions at 31 December 2017	Interests in share incentive schemes, awarded subject to performance conditions at 31 December 2018	Interests in share incentive schemes, awarded subject to performance conditions at 31 December 2017	Interests in share option schemes where performance conditions have been met but not exercised at 31 December 2018	Interests in share option schemes where performance conditions have been met but not exercised at 31 December 2017	Percentage of shareholding target requirement at 31 December 2018	Percentage of shareholding target requirement at 31 December 2018 – based on cost of investment
Ian Powell	30,000	8,400	—	—	—	—	—	—	—	—
Jon Lewis	402,030	—	—	—	1,972,776	—	—	—	21%	21%
Gillian Sheldon	12,500	3,000	—	—	—	—	—	—	—	—
Matthew Lester	21,745	8,698	—	—	—	—	—	—	—	—
John Cresswell	10,500	3,000	—	—	—	—	—	—	—	—
Andrew Williams	100,000	10,000	—	—	—	—	—	—	—	—
Lucy Neville-Rolfe	13,842	—	—	—	—	—	—	—	—	—
Nick Greatorex[1, 4]	54,426	21,125	28,057	17,109	1,176,789	337,726	—	—	—	—
Chris Sellers[2, 4]	21,380	21,337	—	—	259,943	259,943	—	—	—	—

1 Stepped down from the Board on 30 September 2018.
2 Stepped down from the Board on 23 January 2018.
3 Beneficially held interests includes those held by connected persons.
4 2018 interests are shown as at date of resignation from the Board.

Between the end of the financial year and 13 March 2019, Jon Lewis acquired 437 shares under the Capita UK all-employee share incentive plan, increasing their beneficial interest in ordinary shares of the Company to 402,467.

Share plans (audited)

Plan name: deferred annual bonus (DAB) plan

Deferred award – this is the deferred element of an individual's bonus. Any deferral is made on a gross basis into deferred shares or as a net restricted share award. The deferred shares are held for a period of three years from the date of award. This part is not subject to performance conditions. As no bonus was awarded in 2017 and 2018, there is no corresponding DAB deferred award.

Unvested DAB deferred/restricted awards at 31 December 2018

	Number of shares			
Name of Director	**2016 award**	**2017 award**[1]	**2018 award**[1]	**Total**
Jon Lewis	N/A	N/A	N/A	N/A
Nick Greatorex[2]	28,057	N/A	N/A	28,057

1 No bonus was awarded in 2017 and 2018 (in respect of 2016 and 2017 performance) therefore no deferred award was made.
2 Figures as at date of resignation from Board (30 September 2018) and adjusted to reflect the effect of the rights issue.

Plan name: long-term incentive plan (2017 LTIP)

At the annual general meeting in 2017, the LTIP was approved by shareholders. Under the plan rules the Committee can award up to three times salary.

The vesting of awards will depend on performance measured over a three-year period.

Unvested LTIP awards at 31 December 2018

	Number of shares			
Name of Director	**2016 award**	**2017 award**	**2018 award**	**Total**
Jon Lewis	N/A	N/A	1,972,776	1,972,776
Nick Greatorex[1]	165,278	267,753	743,758	1,176,789
Chris Sellers[2]	88,685	261,222	N/A	349,907

LTIP figures for each Executive Director have been adjusted to reflect the effect of the rights issue.

1 Figures at date of resignation from Board (30 September 2018).
2 Figures at date of resignation from Board (23 January 2018) before any pro-rata reductions.

Capita adopted IFRS 15 Revenue from Contracts with Customers with effect from 1 January 2017, resulting in revenue and profits being recognised later across the life of many contracts, with potentially lower profits or losses in the early years of contracts and potentially higher profits in later years. In light of this change, the Committee considered what, if any, adjustments should be made to the EPS and ROCE targets applicable to the outstanding LTIP awards granted 2017 and concluded this would be reviewed at the end of the performance period 31 December 2019 to ensure the position did not become materially easier to achieve under the new standard. The 2016 LTIP awards is subject to a share price underpin of £10.17 and therefore will not vest.

Directors' remuneration report continued

Unvested LTIP (buy-out) remuneration awards at 31 December 2018

	Number of shares	
Name of Director	2018 award	Total
Patrick Butcher	288,078	288,078

Patrick Butcher was granted a buy-out award as part of his remuneration package on appointment which will vest in two tranches, 15 November 2019 and 15 November 2021, subject to continued employment.

Performance criteria

2016

Performance measure	Performance condition
EPS – 75% of the award is measured on EPS growth	EPS growth: 6%–12% per annum Vesting percentage: 18.75%–75% of award Straight line vesting occurs between these points.
ROCE – 25% of the award is measured on average ROCE	Average ROCE: 14%–16% Vesting percentage: 6.25%–25% of award Straight-line vesting occurs between these points.
Share price underpin	Capita's average share price at the vesting date must not be below the share price at the date of grant (£10.17).

2017

Performance underpin	Performance measure	Performance condition
Assessment of the underlying financial and operational performance of Capita over the performance period.	EPS – 75% of the award is measured on EPS growth	EPS growth: 3%–8% per annum Vesting percentage: 18.75%–75% of award Straight-line vesting occurs between these points.
	ROCE – 25% of the award is measured on average ROCE	Average ROCE: 11%–15% Vesting percentage: 6.25%–25% of award Straight-line vesting occurs between these points.

2018

Performance underpin	Performance measure	Weighting	Threshold (25% vests)	Target (50% vests)	Stretch (100% vests)
Assessment of the underlying financial and operational performance of Capita over the performance period.	Annualised cost savings	20%	£160m	£175m	£205m
	Free cash flow	20%	£180m	£200m	£240m
	EBIT margin	20%	9%	10%	12%
	Customer satisfaction	20%	6 point positive swing in NPS	8 point positive swing in NPS	12 point positive swing in NPS
	Employee engagement	20%	6 point positive swing in NPS	8 point positive swing in NPS	12 point positive swing in NPS

A straight-line vesting occurs between these points.

Satisfaction of options

When satisfying awards made under its share plans, the Company uses newly issued, treasury or purchased shares as appropriate.

Dilution

All awards are made under plans that incorporate the overall dilution limit of 10% in 10 years. The estimated dilution from existing awards, including Executive and all-employee share awards, was approximately 1.94% of the Company's share capital at 31 December 2018.

Executive Directors' service agreements

Details of the service agreements are set out below:

Executive Directors	Date of joining the Company	Notice period
Jon Lewis	1 December 2017	12 months
Patrick Butcher	10 December 2018	12 months

Non-Executive Directors' terms of engagement

In 2018, all Non-Executive Directors were considered to be independent of the Company.

Non-Executive Directors	Date of joining the Board	Expiry date of current appointment
Ian Powell	1 September 2016	31 December 2019
Gillian Sheldon	1 September 2012	31 August 2020
Andrew Williams	1 January 2015	31 December 2020
John Cresswell	17 November 2015	16 November 2021
Matthew Lester	1 March 2017	28 February 2020
Baroness Lucy Neville-Rolfe	6 December 2017	5 December 2020

Payments to former Directors (audited)

No payments (other than regular pension benefits commenced in previous years and legacy share plan maturities which were reported in previous years) were made during the year ended 31 December 2018 to any past Director of the Company.

The 2016 LTIP lapsed in full for Vic Gysin, Chris Sellers and Nick Greatorex.

As previously disclosed, Vic Gysin exercised his 2015 and 2016 DAB awards on leaving Capita and received a payment of £47,073. Nick Greatorex exercised his 2016 DAB award over 28,057 shares on leaving Capita and retained 14,843 shares (after sales for tax).

Payments for loss of office (audited)

Chris Sellers stepped down from the Board on 23 January 2018 and left Capita on 31 January 2018. The agreed termination comprises a payment in lieu of notice of £360,000 in respect of salary for his 12-month notice period, £4,500 in respect of accrued holiday entitlement and £250 in consideration for enhanced post-employment undertakings. The Remuneration Committee having exercised its discretion, Chris's outstanding LTIP awards (as detailed on page 95) will remain capable of vesting in accordance with the rules of the scheme, subject to achievement of applicable performance measures and, where relevant, reduced pro-rata to reflect Chris' period of employment (including the notice period) as a proportion of each award's three-year vesting period. His 2016 LTIP award did not vest and lapsed in full. Up to £16,000 (excluding VAT) will be paid directly to third-party service providers in respect of: (i) legal services relating to Chris' settlement; and (ii) outplacement and training services, and he will continue to receive life assurance cover (reduced to a level of two times base salary) and private medical insurance cover consistent with current levels until 31 January 2019.

Nick Greatorex stepped down from the Board and left Capita on 30 September 2018 following market announcements on 18 July 2018 and 22 August 2018. Nick Greatorex will receive the payments set out below (less any required tax withholdings). The payments are in full and final settlement of all claims against the Company and are in accordance with the Company's remuneration policy and where relevant, his service agreement. The agreed termination arrangement comprises payment in lieu of notice of notice of £445,500 in respect of salary and benefits including pension for his 12-month notice period, a final settlement payment of £403,773 arising out of or in connection with his employment and £250 in consideration for enhanced post-employment undertakings. He was eligible for a bonus of up to £615,000 (being his pro-rated maximum bonus opportunity, reflecting his period of service in the year). He received an actual payment of £538,125 as detailed on page 94. His DAB award of 28,057 shares vested on 30 September 2018. The Remuneration Committee having exercised its discretion, Nick's outstanding LTIP awards (as detailed on page 95) remain capable of vesting in accordance with the rules of the scheme, subject to achievement of applicable performance measures, reduced pro-rata to reflect his period of employment (rounded up on a whole-year basis) as a proportion of each award's three-year vesting period. His 2016 LTIP award did not vest and lapsed in full. Up to £25,000 (excluding VAT) will be paid directly to third-party service providers in respect of legal services relating to Nick's departure. Nick continues to receive private medical insurance cover consistent with current levels until 30 September 2019.

Percentage change in remuneration levels

The table below shows change in base compensation, benefits and annual bonus for the CEO in the 2018 financial year, compared to the average for all employees:

	Chief Executive Officer[1]		All employees
	At 31 December 2018 £	% change 2018 v 2017	% change 2018 v 2017
Base compensation	725,000	— %	3.72 %
Benefits	24,809	(58.3)%	(1.07)%
Bonus	1,228,150		(1.1)%

1 CEO figures represent those disclosed in the single figure table on page 92. As there was no bonus payable to the CEO in respect of 2017 no percentage change is shown.

This all-employee information is based on UK employees only, as it was felt that using overseas payroll data would distort the information.

Relative importance of the spend on pay

The table below shows the spend on employee costs in the 2018 financial year, compared to dividends:

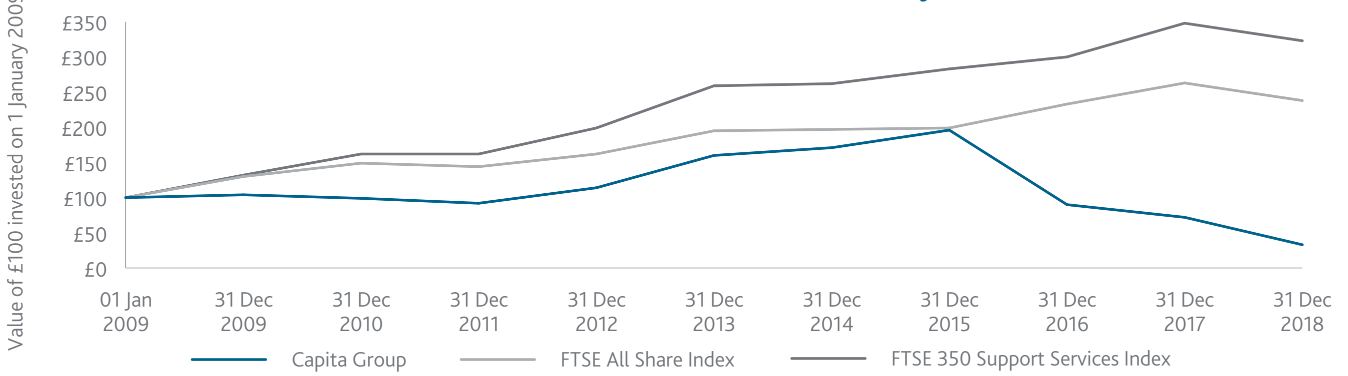
	2018 £m	2017 £m	% change
Employee costs	1,993.1	2,218.9	(10.2)%
Dividends	—	211	(100.0)%

Directors' remuneration report continued

Performance graph and CEO pay

The following chart compares the value of an investment of £100 in the Company's shares with an investment of the same amount in the FTSE All-Share Index and the FTSE 350 Support Services Index, assuming that all dividend income is re-invested.

Capita vs. FTSE all-share index and FTSE 350 support services index value of investment of £100 on 1 January 2009



The Committee is of the opinion that this comparison provides a clear picture of the performance of the Group, relative to both a wide range of companies in the UK and also a specific group of companies within the same sector. Over the 10-year period to 31 December 2018, £100 invested in Capita on 1 January 2009 would be worth £33 at 31 December 2018 compared to £238 for an investment in the FTSE All-Share Index and £325 for an investment in the FTSE 350 Support Services Index.

The total remuneration figures for the CEO during the 2018 financial year are shown in the table below. Consistent with the calculation methodology for the single figure for total remuneration, the total remuneration figure includes the total annual bonus award based on that year's performance and the LTIP award based on the three-year performance period ending in the relevant year. The annual bonus pay-out and LTIP award vesting level as a percentage of the maximum opportunity are also shown for this year.

Year	CEO – single figure of total remuneration	Annual bonus pay-out against maximum opportunity	Long-term incentive vesting rates against maximum opportunity
2018	£2,014,209	85%	—%
2017	£741,376	—%	—%
2016	£682,958	—%	—%
2015	£2,520,428	50%	71.365%
2014	£2,558,998	100%	67.2%
2013	£2,326,250	75%	54.5%
2012	£2,038,233	100%	47.75%
2011	£1,833,308	—%	56.02%
2010	£1,399,675	100%	88.567%
2009	£1,621,793	75%	100%

Note: the vesting rates for the long-term incentives are averaged between the LTIP and the DAB vesting rates for 2010–2013 and 2015. For 2014, this is the actual vesting for the LTIP as there is no DAB maturity in 2014.

Note: figures for 2010–2013 are based on remuneration for Paul Pindar. Figures for 2014–2016 are based on remuneration for Andy Parker. Figures for 2017 are based on remuneration paid to Andy Parker as CEO until 15 September 2017, to Nick Greatorex as interim CEO from 16 September 2017 to 30 November 2017, and to Jon Lewis as CEO from 1 December 2017.

Approval of the Directors' remuneration report

The Directors' remuneration report was approved by the Board on 13 March 2019.

John Cresswell
Chair
Remuneration Committee
13 March 2019

FINANCIAL STATEMENTS

Consolidated income statement

For the year ended 31 December 2018

	Notes	2018 Total reported £m	2017 Total reported £m
Continuing operations:			
Revenue		**3,918.4**	4,234.6
Cost of sales		**(2,951.4)**	(3,182.0)
Gross profit		**967.0**	1,052.6
Administrative expenses	3,4,7	**(932.1)**	(1,472.7)
Operating profit/(loss)	3,4,7	**34.9**	(420.1)
Net finance costs	9	**(72.0)**	(62.4)
Gain/(loss) on business disposal	4	**309.7**	(30.6)
Profit/(loss) before tax	3	**272.6**	(513.1)
Income tax credit/(expense)	10	**0.9**	(14.0)
Profit/(loss) for the year from continuing operations		**273.5**	(527.1)
Discontinued operations:			
Profit for the year	5	**5.6**	416.4
Total profit/(loss) for the year		**279.1**	(110.7)
Attributable to:			
Owners of the Company		**269.0**	(117.1)
Non-controlling interests	34	**10.1**	6.4
		279.1	(110.7)
Earnings/(loss) per share	11		
Continuing:			
– basic		**17.99p**	(48.82)p
– diluted		**17.77p**	(48.82)p
Total operations:			
– basic		**18.37p**	(10.72)p
– diluted		**18.15p**	(10.72)p

	Notes	2018 Total reported £m	2017 Total reported £m
Adjusted operating profit	3	**335.3**	447.5
Adjusted profit before tax	3	**282.1**	383.1
Adjusted earnings per share	11	**16.37p**	27.99p
Adjusted and diluted earnings per share	11	**16.17p**	27.99p

The above and accompanying notes are an integral part of the financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2018

	Notes	2018 £m	2018 £m	2017 £m	2017 £m
Profit/(loss) for the year			**279.1**		(110.7)
Other comprehensive income/(expense):					
Items that will not be reclassified subsequently to profit or loss					
Actuarial gain/(loss) on defined benefit pension schemes	32	**134.9**		(51.4)	
Income tax effect	10	**(22.9)**		8.8	
			112.0		(42.6)
			112.0		(42.6)
Items that will or may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations			**2.0**		(4.6)
Net investment hedge of foreign operations		**—**		10.4	
			—		10.4
Gain on cash flow hedges	26	**2.0**		2.0	
Reclassification adjustments for (income)/expenses included in the income statement	26	**(2.5)**		0.3	
Income tax effect	10	**0.1**		(0.4)	
			(0.4)		1.9
			1.6		7.7
Other comprehensive income/(expense) for the year net of tax			**113.6**		(34.9)
Total comprehensive income/(expense) for the year net of tax			**392.7**		(145.6)
Attributable to:					
Owners of the Company			**382.6**		(152.0)
Non-controlling interests	34		**10.1**		6.4
			392.7		(145.6)

The accompanying notes are an integral part of the financial statements.

Consolidated balance sheet

As at 31 December 2018

	Notes	2018 £m	2017 £m
Non-current assets			
Property, plant and equipment	13	**213.6**	219.3
Intangible assets	14,15	**1,587.7**	1,812.1
Contract fulfilment assets	17	**264.2**	252.5
Financial assets	18	**109.1**	132.3
Deferred taxation	10	**144.6**	159.3
Trade and other receivables	19	**26.2**	28.0
		2,345.4	2,603.5
Current assets			
Financial assets	18	**18.2**	88.7
Disposal group assets held for sale	4	**—**	5.9
Trade and other receivables	19	**771.7**	775.8
Cash	20	**957.5**	921.7
Income tax receivable	10	**0.9**	25.6
		1,748.3	1,817.7
Total assets		**4,093.7**	4,421.2
Current liabilities			
Trade and other payables	21	**668.7**	755.2
Deferred income	22	**980.3**	1,201.2
Overdrafts	20	**314.8**	443.3
Financial liabilities	23	**303.1**	265.6
Disposal group liabilities held for sale	4	**—**	1.4
Provisions	25	**96.8**	164.1
		2,363.7	2,830.8
Non-current liabilities			
Trade and other payables	21	**11.6**	17.0
Deferred income	22	**277.3**	314.0
Financial liabilities	23	**1,084.2**	1,721.7
Deferred taxation	10	**15.2**	12.2
Provisions	25	**19.4**	48.5
Employee benefits	32	**219.0**	406.8
		1,626.7	2,520.2
Total liabilities		**3,990.4**	5,351.0
Net assets/(liabilities)		**103.3**	(929.8)
Capital and reserves			
Issued share capital	27	**34.5**	13.8
Share premium	27	**1,143.3**	501.3
Employee benefit trust and treasury shares	27	**(11.2)**	(0.2)
Capital redemption reserve		**1.8**	1.8
Foreign currency translation reserve		**1.6**	(0.4)
Cash flow hedging reserve		**1.5**	1.9
Retained deficit		**(1,135.3)**	(1,517.2)
Surplus/(deficit) attributable to owners of the Company		**36.2**	(999.0)
Non-controlling interests	34	**67.1**	69.2
Total equity		**103.3**	(929.8)

The accompanying notes are an integral part of the financial statements.

The accounts were approved by the Board of Directors on 13 March 2019 and signed on its behalf by:

Jon Lewis
Chief Executive Officer

Patrick Butcher
Chief Financial Officer

Company registered number: 02081330

Consolidated statement of changes in equity

For the year ended 31 December 2018

	Share capital £m	Share premium £m	Employee benefit trust and treasury shares £m	Capital redemption reserve £m	Retained earnings/ (deficit) £m	Foreign currency translation reserve £m	Cash flow hedging reserve £m	Total £m	Non-controlling interests £m	Total equity/ (deficit) £m
At 1 January 2017	13.8	501.3	(0.2)	1.8	(1,131.8)	(6.2)	—	(621.3)	68.4	(552.9)
Profit/(loss) for the year	—	—	—	—	(117.1)	—	—	(117.1)	6.4	(110.7)
Other comprehensive (expense)/income	—	—	—	—	(42.6)	5.8	1.9	(34.9)	—	(34.9)
Total comprehensive (expense)/ income for the year	—	—	—	—	(159.7)	5.8	1.9	(152.0)	6.4	(145.6)
Share based payment	—	—	—	—	2.9	—	—	2.9	—	2.9
Equity dividends paid	—	—	—	—	(211.0)	—	—	(211.0)	(5.6)	(216.6)
Investment in non-controlling interest	—	—	—	—	(11.1)	—	—	(11.1)	—	(11.1)
Movement in put options held by non-controlling interests	—	—	—	—	(6.5)	—	—	(6.5)	—	(6.5)
At 1 January 2018	13.8	501.3	(0.2)	1.8	(1,517.2)	(0.4)	1.9	(999.0)	69.2	(929.8)
Profit for the year	**—**	**—**	**—**	**—**	**269.0**	**—**	**—**	**269.0**	**10.1**	**279.1**
Other comprehensive income/(expense)	**—**	**—**	**—**	**—**	**112.0**	**2.0**	**(0.4)**	**113.6**	**—**	**113.6**
Total comprehensive income/ (expense) for the year	**—**	**—**	**—**	**—**	**381.0**	**2.0**	**(0.4)**	**382.6**	**10.1**	**392.7**
Share based payment	**—**	**—**	**—**	**—**	**3.4**	**—**	**—**	**3.4**	**—**	**3.4**
Deferred income tax relating to share based payments	**—**	**—**	**—**	**—**	**0.4**	**—**	**—**	**0.4**	**—**	**0.4**
Shares issued/(purchased) (note 27)	**20.7**	**642.0**	**(11.0)**	**—**	**—**	**—**	**—**	**651.7**	**—**	**651.7**
Equity dividends paid	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**(12.2)**	**(12.2)**
Movement in put options held by non-controlling interests	**—**	**—**	**—**	**—**	**(2.9)**	**—**	**—**	**(2.9)**	**—**	**(2.9)**
As at 31 December 2018	**34.5**	**1,143.3**	**(11.2)**	**1.8**	**(1,135.3)**	**1.6**	**1.5**	**36.2**	**67.1**	**103.3**

Share capital – The balance classified as share capital is the nominal proceeds on issue of the Company's equity share capital, comprising 2 1/15p ordinary shares.

Share premium – The amount paid to the Company by shareholders, in cash or other consideration, over and above the nominal value of shares issued to them.

Employee benefit trust and treasury shares – Shares that have been bought back by the Company which are available for retirement or resale; shares held in the employee benefit trust have no voting rights and do not have entitlement to a dividend.

Capital redemption reserve – The Company can redeem shares by repaying the market value to the shareholder, whereupon the shares are cancelled. Redemption must be from distributable profits. The Capital redemption reserve represents the nominal value of the shares redeemed.

Foreign currency translation reserve – Gains or losses resulting from the process of expressing amounts denominated or measured in one currency in terms of another currency by use of the exchange rate between the two currencies. This process is required to consolidate the financial statements of foreign affiliates into the total Group financial statements and to recognise the conversion of foreign currency or the settlement of a receivable or payable denominated in foreign currency at a rate different from that at which the item is recorded.

Cash flow hedging reserve – This reserve records the portion of the gain or loss on a hedging instrument in a cash flow hedge that is determined to be an effective hedge.

Retained earnings – Net profits kept to accumulate in the Group after dividends are paid and retained in the business as working capital.

Non-controlling interests (NCI) – This represents the equity in a subsidiary that is not attributable directly or indirectly to the parent company.

The accompanying notes are an integral part of the financial statements.

Consolidated cash flow statement

For the year ended 31 December 2018

	Notes	2018 £m	Restated[1] 2017 £m
Cash generated from operations	29	**(75.7)**	225.4
Cash generated from/(used by) discontinued operations	5	**(99.2)**	6.7
Income tax received	10	**25.3**	9.5
Net interest paid		**(52.5)**	(54.2)
Net cash inflow/(outflow) from operating activities		**(202.1)**	187.4
Cash flows from investing activities			
Purchase of property, plant and equipment	13	**(89.4)**	(66.2)
Purchase of intangible assets	14	**(70.1)**	(71.0)
Proceeds from sale of property, plant and equipment/intangible assets	7, 13, 14	**1.9**	23.1
Acquisition of subsidiary undertakings and businesses	16	**—**	(24.5)
Cash acquired with subsidiary undertakings	16	**—**	4.5
Deferred consideration received		**5.2**	11.8
Cancellation of put options		**(6.8)**	—
Deferred consideration paid	23	**(11.1)**	(5.8)
Contingent consideration paid		**(19.8)**	(11.7)
Purchase of financial assets		**(0.9)**	(0.7)
Net proceeds on disposal of subsidiary undertakings	4	**407.8**	17.0
Cash disposed of with subsidiary undertakings	4	**(11.2)**	(0.1)
Cash flows from investing activities used by discontinued operations	5	**—**	825.2
Net cash inflow/(outflow) from investing activities		**205.6**	701.6
Cash flows from financing activities			
External dividends paid	12	**—**	(211.0)
Dividends paid to non-controlling interest	12	**(12.2)**	(5.6)
Purchase of shares	27	**(11.0)**	—
Capital element of finance lease rental payments		**(0.2)**	(2.1)
Issue of share capital net of issue costs	27	**662.7**	—
Repayment of loan notes	26	**(577.2)**	(124.1)
Proceeds/(Repayment) of fixed rate swaps	26	**103.6**	(84.6)
Repayment of term debt	26	**—**	(550.0)
Financing arrangement costs		**(3.7)**	(2.1)
Net cash inflow/(outflow) from financing activities		**162.0**	(979.5)
Increase in cash and cash equivalents		**165.5**	(90.5)
Cash and cash equivalents at the beginning of the period		**478.4**	565.8
Movement in exchange rates		**(1.2)**	3.1
Cash and cash equivalents as at 31 December		**642.7**	478.4
Cash and cash equivalents comprise:			
Cash at bank and in hand	20	**957.5**	921.7
Overdrafts	20	**(314.8)**	(443.3)
Total		**642.7**	478.4

	Notes	2018 £m	Restated[1] 2017 £m
Adjusted cash generated from operations	29	**69.8**	**230.3**
Adjusted free cash flows	29	**(82.5)**	**75.4**

1 The Group has represented and restated its cash flow statement. Refer to note 29 for details.

Notes to the consolidated financial statements

1 Corporate information

The consolidated financial statements of Capita plc for the year ended 31 December 2018 were authorised for issue in accordance with a resolution of the Directors on 13 March 2019. Capita plc is a public limited company incorporated in England and Wales whose shares are publicly traded.

The principal activities of the Group are given in the strategic report on pages 1–52.

2 Summary of significant accounting policies

Changes to non-statutory reporting

The Group has simplified its non-statutory reporting measures to improve transparency and make it easier for the readers of its annual report and accounts to understand its financial performance. Historically, the Group presented underlying and non-underlying results (comprising business exits and specific items) on the face of the income statement. In the notes, underlying results before significant new contracts and restructuring was disclosed. The revised presentation has only the reported results on the face of the income statement, with a footnote detailing adjusted profit and earnings per share, and a reference to a note to the consolidated financial statements (see note 3) providing a reconciliation between reported and adjusted profit. The presentation of the cash flow statement and additional cash flow information in note 29 have also been revised to show the same split.

Adjusted profit

IAS 1 permits an entity to present additional information for specific items to enable users to better assess the entity's financial performance. In practice these items are commonly referred to as 'specific' or 'non-underlying' items although such terminology is not defined in IFRS and accordingly there is a level of judgement required in determining what items to separately identify. The Board has adopted a policy to separately disclose those items that it considers are outside the underlying operating results for the particular year under review and against which the Group's performance is assessed.

Those items which relate to the ordinary course of the Group's operating activities remain within adjusted profit. The following items are excluded from adjusted profit: acquired intangible amortisation, impairment of goodwill and acquired intangibles, acquisition contingent consideration movements, the financial impact of business exits or businesses in the process of being exited, acquisition expenses, movements in the mark-to-market valuation of certain financial instruments, the impact of significant new contracts and restructuring (see below), and other specific non-recurring items in the income statement. In the Directors' judgement, these need to be disclosed separately (see notes 3, 4, 5, 9 and 10) by virtue of their nature, size and/or incidence, in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying in-year performance of the business. The Board does not consider these items when assessing the performance of the in-year performance and accordingly these items are also excluded in the discussion of divisional performances in the strategic report.

Under IFRS 15, contracts potentially recognise lower profits or losses in their early years where there are significant upfront restructuring costs or higher operating costs prior to transformation. As such, following the adoption of IFRS 15, the Board adopted a policy to separately disclose the operating profit/loss from significant new contract wins in-period and significant restructuring, in order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the underlying business. The impact of these significant new contracts and restructuring are excluded in arriving at adjusted profit. A significant new contract is assessed as that which is significant and either entirely new to the Group, or a significant amendment to the scope and scale of an existing contract. The Group continually assesses the resourcing levels, both at a divisional level and also in relation to the management and delivery of individual contracts. This results in restructuring in the normal course of business and any such charges are recorded in adjusted profit. A significant restructuring is assessed as that above this normal level of restructuring. As discussed in the strategic report, a major transformation plan has been launched and costs incurred in support of this, including external adviser costs, are presented as restructuring charges. Contract terminations arising in the normal course of business and which result in the disposal of a contract fulfilment asset and/or a true-up of revenue recognised, will be included within adjusted profit, and separately disclosed if considered material (see note 3).

This policy is kept under review by the Board and the Audit and Risk Committee, and is discussed in the Committee's report on pages 71–79. The Audit and Risk Committee will keep under review the policy for presentation significant restructuring costs separately, as the programme covers multiple years. Accordingly, the Committee is cognisant of the need to ensure that costs are defined and that appropriate borders are set for such an extended and critical programme.

Except for the disposal of our Capita Asset Services businesses, none of our 2018 or 2017 business exits or businesses in the process of being exited meet the definition of 'discontinued operations' as stipulated by IFRS 5, which requires disclosure and the restatement of comparative information where the relative size of a disposal or business closure is significant. Accordingly, the separate presentation described above does not fall within the requirements of IFRS 5 concerning discontinued operations. The 2017 adjusted comparatives are restated for business exits or businesses in the process of being exited in 2018 to enable better comparability.

Assets held for sale

The Group classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than continued use.

For this to be the case, the asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable. For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset (or disposal group), and an active programme to locate a buyer and complete the plan must have been initiated. Further, the asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Notes to the consolidated financial statements continued

2 Summary of significant accounting policies continued

Significant accounting judgements, estimates and assumptions

The preparation of financial statements in line with generally accepted accounting principles requires the Directors to make judgements and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements and the reported income and expense during the presented periods. Although these judgements and assumptions are based on the Directors' best knowledge of the amount, events or actions, actual results may differ.

The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are as follows:

- The measurement of revenue and resulting profit recognition – due to the size and complexity of some of the Group's contracts, there are significant judgements to be applied, including the measurement and timing of revenue recognition and the recognition of related balance sheet items (such as contract fulfilment assets, capitalisation of costs to obtain a contract, trade receivables, accrued income and deferred income) that result from the performance of the contract (see (e) and (s) below, and the 'divisional strategy and performance' section of the strategic report). This is particularly in respect of contracts that are in the transformation stage and pre-inflection point, such as PCSE and mobilcom-debitel.

  The Group is required to estimate the contract profitability, including the costs to complete the contract. The ability to accurately forecast such costs involves estimates around cost savings to be achieved over time, anticipated profitability of the contract, as well as future performance against any contract-specific KPIs that could trigger variable consideration or service credits. The Group first assesses whether the contract assets are impaired and then further considers whether any onerous contract exists. To mitigate the level of uncertainty in making these estimates the Group regularly compares actual performance of the contracts against previous forecasts and considers whether there have been any changes to significant judgements. Following this review, as outlined in note 17, contract fulfilment asset provisions for impairment of £22.2m (£2017: £14.1m) were identified relating to assets capitalised in the year and recognised within adjusted cost of sales.

  Due to the level of uncertainty and combination of variables associated with those estimates there is a significant risk that there could be material adjustment to the carrying amounts of onerous contract provisions within the next financial year. The future range of possible outcomes in respect of the assumptions and significant judgements made to determine the carrying value of onerous contracts could result in either a material increase or decrease in the value of contract fulfilment assets or onerous contract provisions in the next financial year. The extent to which actual results differ from estimates made at the reporting date depends on the combined outcome and timing of a large number of variables associated with performance across multiple contracts. Given this wide spread of contracts, it is not practical to provide a quantitative analysis of the aggregated judgements that are applied, and we do not believe that disclosing a potential range of outcomes on a consolidated basis would provide meaningful information to a reader of the accounts. Due to commercial sensitivities, we do not specifically disclose the amounts involved on any individual contract. The Board has discussed in the strategic report the outlook on the key contracts that are pre-inflection to provide context for a reader to assess the results and performance of the underlying division.

- The measurement of intangible assets other than goodwill in a business combination – on the acquisition of a business the identifiable intangible assets may include licences, customer lists and brands. The fair value of these assets is determined by discounting estimated future net cash flows generated by the asset as in most cases no active market for the assets exists and therefore no observable value. The use of different assumptions for the expectations of future cash flows and the discount rate would change the valuation of the intangible assets. The relative size of the Group's intangible assets, excluding goodwill, makes the judgements surrounding the estimated useful lives material to the Group's financial position and performance. Refer to (j) below and note 14.

- The measurement and impairment of goodwill – the amount of goodwill initially recognised as a result of a business combination is dependent on the allocation of the purchase price to the fair value of the identifiable assets acquired and the liabilities assumed. The determination of the fair value of the assets and liabilities is based, to a considerable extent, on management's judgement. Allocation of the purchase price affects the results of the Group as finite lived intangible assets are amortised. The Group determines whether goodwill is impaired on an annual basis or more frequently if required and this requires an estimation of the fair value less cost of disposal of the cash generating units to which the intangible assets are allocated utilising an estimation of future cash flows and choosing a suitable discount rate (see note 15).

- The measurement of defined benefit obligations – the accounting cost of these benefits and the present value of pension liabilities involve judgements about uncertain events including such factors as the life expectancy of members, the salary progression of our current employees, price inflation and the discount rate used to calculate the net present value of the future pension payments. We use estimates for all of these factors in determining the pension costs and liabilities incorporated in our financial statements. The assumptions reflect historical experience and our judgement regarding future expectations (see note 32).

- The measurement of provisions and contingent liabilities – measuring and recognising provisions and the exposures to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation and arbitration, as well as other contingent liabilities (see notes 25 and 31). Judgement is necessary in assessing the likelihood of success of any claim and whether a liability will arise, and to quantify the possible range of the financial settlement. Because of the inherent uncertainty in this evaluation process, actual losses may be different from the originally estimated provision.

For further details on the sensitivity of carrying amounts to the methods, assumptions and estimates used, the reason for the sensitivity, the expected resolution of uncertainties, and the range of reasonable possible alternatives for each of the above, refer to the policies and notes referenced.

The Directors apply judgement when considering the presentation of items in arriving at adjusted profit. As discussed above, the Group separately presents specific items in the income statement, which in the Directors' judgement, need to be disclosed separately by virtue of their nature, size and/or incidence in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business (see note 3). This judgement has an impact on the calculation of covenants (refer to (b)).

(a) Statement of compliance

The consolidated financial statements of Capita plc (the Company) and all of its subsidiaries (the Group) have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006.

The parent company has applied FRS 101 – Reduced Disclosure Framework in the preparation of its individual financial statements and these are contained on pages 178–195. FRS 101 applies IFRS as adopted by the European Union with certain disclosure exemptions.

2 Summary of significant accounting policies continued

(b) Basis of preparation

The consolidated financial statements have been prepared under IFRS where certain financial instruments and the pension assets have been measured at fair value. The carrying value of recognised assets and liabilities that are hedged are adjusted to record changes in the fair values attributable to the risks that are being hedged. The consolidated financial statements are presented in pounds sterling and all values are rounded to the nearest tenth of a million (£m) except when otherwise indicated.

In determining the appropriate basis of preparation of the financial statements for the year ending 31 December 2018, the Directors are required to consider whether the Group can continue in operational existence for the foreseeable future. Having taken decisive action to strengthen the balance sheet through the raising of new equity and the disposal of non-core businesses, and undertaking a rigorous assessment of the financial forecast, the Board have concluded that the Group will continue to have adequate financial resources to realise their assets and discharge its liabilities as they fall due.

Accordingly, the Directors have formed the judgement that it is appropriate to prepare these consolidated financial statements on the going concern basis. Therefore, the consolidated financial statements do not include any adjustments which would be required if the going concern basis of preparation is inappropriate.

The Group's committed revolving credit facility, bank term loan facilities and private placement loan notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. The Group's covenanted maximum ratio is 3.0 times or to 3.5 times depending on the debt instrument in question. They are tested semi-annually.

The Group had net debt of £466.1m as at 31 December 2018 (2017: £1,117.0m) and adjusted net debt of £494.7m as at 31 December 2018 (2017: £1,153.0m). Net debt is reported in note 29 – additional cash flow information. Adjusted net debt is used to calculate the gearing ratio adjusted net debt to adjusted EBITDA (refer to the alternative performance measures on pages 197–198).

The Group's calculation of adjusted net debt to adjusted EBITDA at 31 December 2018 was 1.2 times and was compliant with the relevant ratios.

(c) Basis of consolidation

The consolidated financial statements comprise the financial statements of Capita plc and its subsidiaries as at 31 December each year. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

Subsidiaries are consolidated from the date on which control is transferred to the Group until control is transferred out of the Group. Where there is a loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which Capita plc has control and the profit or loss on disposal is calculated as the difference between the fair value of the consideration received and the carrying amount of the assets (including goodwill) disposed of. Losses applicable to the non-controlling interests in a subsidiary are attributed to the non-controlling interests even if that results in the non-controlling interests having a deficit balance.

(d) Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial year except for the adoption of IFRS 9 Financial Instruments. In addition, the Group has adopted the new amendments to standards and new IFRIC as detailed below.

Initial adoption of IFRS 9 Financial Instruments

IFRS 9 Financial Instruments replaces IAS 39 Financial Instruments: Recognition and Measurement for annual periods beginning on or after 1 January 2018, bringing together all three aspects of the accounting for financial instruments: classification and measurement; impairment; and hedge accounting. With the exception of hedge accounting, which the Group applied prospectively, the Group has applied IFRS 9 retrospectively, with the initial application date of 1 January 2018. There has been no restatement to the comparative balances for the period beginning 1 January 2017 as there are no requirements under the standard to restate comparatives.

The Group has performed an assessment to understand the requirements of IFRS 9 and how these differ from IAS 39 and has concluded there is no significant impact on the consolidated financial statements from the date of adoption. There were no differences between previous carrying amounts and consequently no adjustment has been made to opening retained earnings. The updated account policy is set out in (r).

Annual improvements to IFRS Standards 2014–2016 Cycle

As part of its annual improvements cycles, the International Accounting Standards Board amended various standards primarily with a view to removing inconsistencies and clarifying wording.

Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions

The amendments are intended to eliminate diversity in practice, are narrow in scope and address three specific areas of classification and measurement.

Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

The amendments provide two options for entities that issue insurance contracts within the scope of IFRS 4: the 'overlay approach' or the 'deferral approach'. The application of both approaches is optional and an entity is permitted to stop applying them before the new insurance contracts standard is applied.

Amendments to IAS 40: Transfers of Investment Property

The amendment provides clarity that an entity shall transfer a property to, or from, investment property when, and only when, there is evidence of a change in use. A change of use occurs if property meets, or ceases to meet, the definition of investment property. A change in management's intentions for the use of a property by itself does not constitute evidence of a change in use.

IFRIC 22: Foreign Currency Transactions and Advance Consideration

These amendments are intended to eliminate diversity in practice when recognising the related asset, expense or income on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration received or paid in a foreign currency.

Notes to the consolidated financial statements continued

2 Summary of significant accounting policies continued

(e) Revenue

The Group generates revenue largely in the UK and Europe.

The Group operates a number of diverse businesses and accordingly applies a variety of methods for revenue recognition, based on the principles set out in IFRS 15. Many of the contracts entered into are long-term and complex in nature, given the breadth of solutions the Group offers.

The revenue and profits recognised in any period are based on the delivery of performance obligations and an assessment of when control is transferred to the customer.

In determining the amount of revenue and profits to record, and related balance sheet items (such as contract fulfilment assets, capitalisation of costs to obtain a contract, trade receivables, accrued income and deferred income) to recognise in the period, management is required to form a number of key judgements and assumptions. This includes an assessment of the costs the Group incurs to deliver the contractual commitments and whether such costs should be expensed as incurred or capitalised. These judgements are inherently subjective and may cover future events such as the achievement of contractual milestones, performance KPIs and planned cost savings. In addition, for certain contracts, key assumptions are made concerning contract extensions and amendments, as well as opportunities to use the contract developed systems and technologies on other similar projects.

Revenue is recognised either when the performance obligation in the contract has been performed (so 'point in time' recognition) or 'over time' as control of the performance obligation is transferred to the customer.

For all contracts, the Group determines if the arrangement with a customer creates enforceable rights and obligations. This assessment results in certain Master Service Agreements (MSAs) not meeting the definition of a contract under IFRS 15 and as such the individual call-off agreements, linked to the MSA, are treated as individual contracts.

The Group enters into contracts which contain extension periods, where either the customer or both parties can choose to extend the contract or there is an automatic annual renewal, and/or termination clauses that could impact the actual duration of the contract. Judgement is applied to assess the impact that these clauses have when determining the appropriate contract term. The term of the contract impacts both the period over which revenue from performance obligations may be recognised and the period over which contract fulfilment assets and capitalised costs to obtain a contract are expensed.

For contracts with multiple components to be delivered such as transformation, transitions and the delivery of outsourced services, management applies judgement to consider whether those promised goods and services are: (i) distinct – to be accounted for as separate performance obligations; (ii) not distinct – to be combined with other promised goods or services until a bundle is identified that is distinct; or (iii) part of a series of distinct goods and services that are substantially the same and have the same pattern of transfer to the customer.

At contract inception the total transaction price is estimated, being the amount to which the Group expects to be entitled and has rights to under the present contract. This includes an assessment of any variable consideration where the Group's performance may result in additional revenues based on the achievement of agreed KPIs. Such amounts are only included based on the expected value or the most likely outcome method, and only to the extent that it is highly probable that no revenue reversal will occur.

The transaction price does not include estimates of consideration resulting from change orders for additional goods and services unless these are agreed.

Once the total transaction price is determined, the Group allocates this to the identified performance obligations in proportion to their relative stand-alone selling prices and recognises revenue when (or as) those performance obligations are satisfied.

The Group infrequently sells standard products with observable stand-alone prices due to the specialised services required by clients and therefore the Group applies judgement to determine an appropriate stand alone selling price. More frequently, the Group sells a customer bespoke solution, and in these cases the Group typically uses the expected cost plus margin or a contractually stated price approach to estimate the stand-alone selling price of each performance obligation.

The Group may offer price step downs during the life of a contract, but with no change to the underlying scope of services to be delivered. In general, any such variable consideration, price step down or discount is included in the total transaction price to be allocated across all performance obligations unless it relates to only one performance obligation in the contract.

For each performance obligation, the Group determines if revenue will be recognised over time or at a point in time. Where the Group recognises revenue over time for long-term contracts, this is in general due to the Group performing and the customer simultaneously receiving and consuming the benefits provided over the life of the contract.

For each performance obligation to be recognised over time, the Group applies a revenue recognition method that faithfully depicts the Group's performance in transferring control of the goods or services to the customer. This decision requires assessment of the real nature of the goods or services that the Group has promised to transfer to the customer. The Group applies the relevant output or input method consistently to similar performance obligations in other contracts.

When using the output method the Group recognises revenue on the basis of direct measurements of the value to the customer of the goods and services transferred to date relative to the remaining goods and services under the contract. Where the output method is used, in particular for long-term service contracts where the series guidance is applied (see below for further details), the Group often uses a method of time elapsed which requires minimal estimation. Certain long-term contracts use output methods based upon estimation of number of users, level of service activity or fees collected.

If performance obligations in a contract do not meet the over time criteria, the Group recognises revenue at a point in time (see below for further details).

The Group disaggregates revenue from contracts with customers by contract type, as management believe this best depicts how the nature, amount, timing and uncertainty of the Group's revenue and cash flows are affected by economic factors. Categories are: 'long-term contractual – greater than two years'; and 'short-term contractual – less than two years'. Years based from service commencement date.

2 Summary of significant accounting policies continued

Long-term contractual – greater than two years

The Group provides a range of services in the majority of its reportable segments under customer contracts with a duration of more than two years.

The nature of contracts or performance obligations categorised within this revenue type is diverse and includes: (i) long-term outsourced service arrangements in the public and private sectors; and (ii) active software licence arrangements (see definition below).

The Group considers that the services provided meet the definition of a series of distinct goods and services as they are: (i) substantially the same; and (ii) have the same pattern of transfer (as the series constitutes services provided in distinct time increments (e.g. daily, monthly, quarterly or annual services)) and therefore treats the series as one performance obligation. Even if the underlying activities performed by the Group to satisfy a promise vary significantly throughout the day and from day to day, that fact, by itself, does not mean the distinct goods or services are not substantially the same. For the majority of long-service contracts with customers in this category, the Group recognises revenue using the output method as it best reflects the nature in which the Group is transferring control of the goods or services to the customer.

Active software licences are those where the Group has a continuing involvement after the sale or transfer of control to the customer, which significantly affects the intellectual property to which the customer has rights. The Group is in a majority of cases responsible for any maintenance, continuing support, updates and upgrades and accordingly the sale of the initial software is not distinct. The Group's accounting policy for licences is discussed in more detail below.

Short-term contractual – less than two years

The nature of contracts or performance obligations categorised within this revenue type is diverse and includes: (i) short-term outsourced service arrangements in the public and private sectors; and (ii) software maintenance contracts.

The Group has assessed that maintenance and support (i.e. on-call support, remote support) for software licences is a performance obligation that can be considered capable of being distinct and separately identifiable in a contract if the customer has a passive licence. These recurring services are substantially the same as the nature of the promise is for the Group to 'stand ready' to perform maintenance and support when required by the customer. Each day of standing ready is then distinct from each following day and is transferred in the same pattern to the customer.

Transactional (Point in time) contracts

The Group delivers a range of goods or services in all reportable segments that are transactional services for which revenue is recognised at the point in time when control of the goods or services has transferred to the customer. This may be at the point of physical delivery of goods and acceptance by a customer or when the customer obtains control of an asset or service in a contract with customer-specified acceptance criteria.

The nature of contracts or performance obligations categorised within this revenue type is diverse and includes: (i) provision of IT hardware goods; (ii) passive software licence agreements; (iii) commission received as agent from the sale of third-party software; and (iv) fees received in relation to delivery of professional services.

Passive software licences are licences which have significant stand-alone functionality and the contract does not require, and the customer does not reasonably expect, the Group to undertake activities that significantly affect the licence. Any ongoing maintenance or support services for passive licences are likely to be separate performance obligations. The Group's accounting policy for licences is discussed in more detail below.

Contract modifications

The Group's contracts are often amended for changes in contract specifications and requirements. Contract modifications exist when the amendment either creates new or changes the existing enforceable rights and obligations. The effect of a contract modification on the transaction price and the Group's measure of progress for the performance obligation to which it relates, is recognised as an adjustment to revenue in one of the following ways:

a. prospectively as an additional separate contract;

b. prospectively as a termination of the existing contract and creation of a new contract;

c. as part of the original contract using a cumulative catch up; or

d. as a combination of (b) and (c).

For contracts for which the Group has decided there is a series of distinct goods and services that are substantially the same and have the same pattern of transfer where revenue is recognised over time, the modification will always be treated under either (a) or (b); (d) may arise when a contract has a part-termination and a modification of the remaining performance obligations.

The facts and circumstances of any contract modification are considered individually as the types of modifications will vary contract by contract and may result in different accounting outcomes.

Judgement is applied in relation to the accounting for such modifications where the final terms or legal contracts have not been agreed prior to the period end as management need to determine if a modification has been approved and if it either creates new or changes existing enforceable rights and obligations of the parties. Depending upon the outcome of such negotiations, the timing and amount of revenue recognised may be different in the relevant accounting periods. Modification and amendments to contracts are undertaken via an agreed formal process. For example, if a change in scope has been approved but the corresponding change in price is still being negotiated, management use their judgement to estimate the change to the total transaction price. Importantly, any variable consideration is only recognised to the extent that it is highly probable that no revenue reversal will occur.

Principal versus agent

The Group has arrangements with some of its clients whereby it needs to determine if it acts as a principal or an agent as more than one party is involved in providing the goods and services to the customer. The Group acts as a principal if it controls a promised good or service before transferring that good or service to the customer. The Group is an agent if its role is to arrange for another entity to provide the goods or services. Factors considered in making this assessment are most notably the discretion the Group has in establishing the price for the specified good or service, whether the Group has inventory risk and whether the Group is primarily responsible for fulfilling the promise to deliver the service or good.

This assessment of control requires judgement in particular in relation to certain service contracts. An example is the provision of certain recruitment and learning services where the Group may be assessed to be agent or principal dependent upon the facts and circumstances of the arrangement and the nature of the services being delivered.

Where the Group is acting as a principal, revenue is recorded on a gross basis. Where the Group is acting as an agent, revenue is recorded at a net amount reflecting the margin earned.

Notes to the consolidated financial statements continued

2 Summary of significant accounting policies continued

Licences

Software licences delivered by the Group can either be right to access ('active') or right to use ('passive') licences. Active licences are licences which require continuous upgrade and updates for the software to remain useful, all other licences are treated as passive licences. The assessment of whether a licence is active or passive involves judgement. The key determinant of whether a licence is active is whether the Group is required to undertake activities that significantly affect the licensed intellectual property (or the customer has a reasonable expectation that it will do so) and the customer is, therefore, exposed to positive or negative impacts resulting from those changes.

When software upgrades are sold as part of the software licence agreement (i.e. software upgrades are promised to the customer), the Group applies judgement to assess whether the software upgrade is distinct from the licence (i.e. a separate performance obligation). If the upgrade is considered fundamental to the ongoing use of the software by the customer, the upgrades are not considered distinct and not accounted for as a separate performance obligation.

The Group considers for each contract that includes a separate licence performance obligation all the facts and circumstances in determining whether the licence revenue is recognised over time or at a point in time from the go live date of the licence.

Contract fulfilment assets

Contract fulfilment costs are divided into: (i) costs that give rise to an asset; and (ii) costs that are expensed as incurred.

When determining the appropriate accounting treatment for such costs, the Group firstly considers any other applicable standards. If those other standards preclude capitalisation of a particular cost, then an asset is not recognised under IFRS 15.

If other standards are not applicable to contract fulfilment costs, the Group applies the following criteria which, if met, result in capitalisation: (i) the costs directly relate to a contract or to a specifically identifiable anticipated contract; (ii) the costs generate or enhance resources of the entity that will be used in satisfying (or in continuing to satisfy) performance obligations in the future; and (iii) the costs are expected to be recovered. The assessment of this criteria requires the application of judgement, in particular when considering if costs generate or enhance resources to be used to satisfy future performance obligations and whether costs are expected to be recoverable.

The Group regularly incurs costs to deliver its outsourcing services in a more efficient way (often referred to as 'transformation' costs). These costs may include process mapping and design, system development, project management, hardware (generally in scope of the Group's accounting policy for property, plant and equipment), software licence costs (generally in scope of the Group's accounting policy for intangible assets), recruitment costs and training.

The Group has determined that, where the relevant specific criteria are met, the costs for (i) process mapping and design; (ii) system development; and (iii) project management are likely to qualify to be capitalised as contract fulfilment assets.

The incremental costs of obtaining a contract with a customer are recognised as a contract fulfilment asset if the Group expects to recover them. The Group incurs costs such as bid costs, legal fees to draft a contract and sales commissions when it enters into a new contract.

Judgement is applied by the Group when determining what costs qualify to be capitalised in particular when considering whether these costs are incremental and whether these are expected to be recoverable. For example, the Group considers which type of sales commissions are incremental to the cost of obtaining specific contracts and the point in time when the costs will be capitalised.

The Group has determined that the following costs may be capitalised as contract fulfilment assets: (i) legal fees to draft a contract (once the Group has been selected as a preferred supplier for a bid); and (ii) sales commissions that are directly related to winning a specific contract.

Costs incurred prior to selection as preferred supplier are not capitalised but are expensed as incurred.

Utilisation, derecognition and impairment of contract fulfilment assets and capitalised costs to obtain a contract

The Group utilises contract fulfilment assets to cost of sales over the expected contract period using a systematic basis that mirrors the pattern in which the Group transfers control of the service to the customer. The utilisation charge is included within cost of sales. Judgement is applied to determine this period, for example whether this expected period would be the contract term or a longer period such as the estimated life of the customer relationship for a particular contract if, say, renewals are expected.

A contract fulfilment asset is derecognised either when it is disposed of or when no further economic benefits are expected to flow from its use or disposal.

Management is required to determine the recoverability of contract related assets within property, plant and equipment, intangible assets as well as contract fulfilment assets, accrued income and trade receivables. At each reporting date, the Group determines whether or not the contract fulfilment assets are impaired by comparing the carrying amount of the asset to the remaining amount of consideration that the Group expects to receive less the costs that relate to providing services under the relevant contract. In determining the estimated amount of consideration, the Group uses the same principles as it does to determine the contract transaction price, except that any constraints used to reduce the transaction price will be removed for the impairment test.

Where the relevant contracts are demonstrating marginal profitability or other indicators of impairment, judgement is required in ascertaining whether or not the future economic benefits from these contracts are sufficient to recover these assets. In performing this impairment assessment, management is required to make an assessment of the costs to complete the contract. The ability to accurately forecast such costs involves estimates around cost savings to be achieved over time, anticipated profitability of the contract, as well as future performance against any contract-specific KPIs that could trigger variable consideration, or service credits. Where a contract is anticipated to make a loss, these judgements are also relevant in determining whether or not an onerous contract provision is required and how this is to be measured.

Deferred and accrued income

The Group's customer contracts include a diverse range of payment schedules dependent upon the nature and type of goods and services being provided. The Group often agrees payment schedules at the inception of long-term contracts under which it receives payments throughout the term of the contracts. These payment schedules may include performance-based payments or progress payments as well as regular monthly or quarterly payments for ongoing service delivery. Payments for transactional goods and services may be at delivery date, in arrears or part payment in advance.

Where payments made are greater than the revenue recognised at the period end date, the Group recognises a deferred income contract liability for this difference. Where payments made are less than the revenue recognised at the period end date, the Group recognises an accrued income contract asset for this difference.

At each reporting date, the Group assesses whether there is any indication that accrued income assets may be impaired by considering whether the revenue remains highly probable that no revenue reversal will occur. Where an indicator of impairment exists, the Group makes a formal estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

2 Summary of significant accounting policies continued

Onerous contracts

The Group reviews its long-term contracts to ensure that the expected economic benefits to be received are in excess of the unavoidable costs of meeting the obligations under the contract. The unavoidable costs are the lower of the net costs of termination or the costs of fulfilment of the contractual obligations. The Group recognises the excess of the unavoidable costs over economic benefits due to be received as an onerous contract provision.

(f) Foreign currency translation

The functional and presentation currency of Capita plc and its UK subsidiaries is the pound sterling (£). Transactions in foreign currencies are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement with the exception of differences on foreign currency borrowings that provide a hedge against a net investment in a foreign operation. These are taken directly to equity until the disposal of the net investment, at which time they are recognised in the consolidated income statement.

Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currencies of overseas operations include the euro, Indian rupee, South African rand, and the US dollar. As at the reporting date, the assets and liabilities of the overseas operations are retranslated into the presentation currency of Capita plc at the rate of exchange ruling at the balance sheet date and their income statements are translated at the weighted average exchange rate for the year.

The exchange differences arising on the re-translation are taken directly to a separate component of equity. On disposal of a foreign operation, the deferred cumulative amount recognised in equity relating to that particular foreign operation shall be recognised in the income statement.

The Group has elected not to record cumulative translation differences arising prior to the transition date as permitted by IFRS 1 as at 31 December 2004. In utilising this exemption, all cumulative translation differences were deemed to be zero as at 1 January 2004 and all subsequent disposals shall exclude any translation differences arising prior to the date of transition.

(g) Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

- Freehold buildings and long leasehold property – over 50 years.
- Leasehold improvements – period of the lease.
- Plant and equipment – 3 to 10 years.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognised in the income statement in the administrative expenses line item.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset (retired). Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year in which the item is derecognised.

(h) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the respective assets. All other borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

The Group capitalises borrowing costs for all qualifying assets where construction commenced on or after 1 January 2009.

(i) Business combinations and goodwill

Business combinations are accounted for by applying the acquisition method as at the acquisition date, which is the date on which control is passed to the Group.

Goodwill

Following initial recognition, goodwill is stated at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill arising on acquisitions prior to 31 December 1997 remains set-off directly against reserves and does not get recycled through the income statement.

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units which are expected to benefit from the combination's synergies. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation.

Goodwill disposed of in these circumstances is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Acquisitions and disposals of non-controlling interests

Acquisitions and disposals of non-controlling interests that do not result in a change of control are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognised as a result of such transactions. The adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary. Any difference between the price paid or received and the amount by which non-controlling interests are adjusted is recognised directly in equity and attributed to the owners of the parent company.

Prior to the adoption of IAS 27 (Amended), goodwill was recognised on the acquisition of non-controlling interests in a subsidiary, which represented the excess of the cost of the additional investment over the carrying amount of the interest in the net assets acquired at the date of the transaction.

Notes to the consolidated financial statements continued

2 Summary of significant accounting policies continued

(j) Intangible assets

Intangible assets acquired separately are capitalised at cost and those identified in a business acquisition are capitalised at fair value as at the date of acquisition. In the case of capitalised software development costs, research expenditure is written off to the income statement in the period in which it is incurred. Development expenditure is written off in the same way unless and until the Group is satisfied as to the technical, commercial and financial viability of individual projects. Where this condition is satisfied, the development expenditure is capitalised and amortised over the period during which the Group is expected to benefit.

Following initial recognition, the carrying amount of an intangible asset is its cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. There were no indefinite-lived assets in 2018 or 2017. Amortisation is charged on assets with finite lives and this expense is taken to the income statement through the administrative expenses line item.

Intangible assets with finite lives are only tested for impairment, either individually or at the cash-generating unit level, where there is an indicator of impairment.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

Intangible assets identified and recognised since transition to IFRS are profiled, on a straight-line basis, as follows:

Intangible assets acquired in business combinations –

- brands are amortised over their useful economic lives of between 5 and 10 years
- I.P., software and licences are amortised over their useful economic lives of between 5 and 20 years
- contracts and committed sales are amortised over their useful economic lives of between 1.5 and 15 years
- client lists and relationships are amortised over their useful economic lives of between 4 and 10 years.

Intangible assets purchased or internally capitalised –

- capitalised software development costs are amortised over their useful economic lives of between 5 and 15 years
- software and licences are amortised over their useful economic lives of between 5 and 20 years
- other intangibles are amortised over their useful economic lives of 3 to 15 years.

(k) Recoverable amount of non-current assets

At each reporting date, the Group assesses whether there is any indication that a non-current asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. The recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets.

(l) Investments and other financial assets

Classification

Applicable from 1 January 2018, the Group classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through OCI or through profit or loss); and
- those to be measured at amortised cost.

The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows.

For investments in equity instruments that are not held for trading, this will depend on whether the Group has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The Group reclassifies debt investments when and only when its business model for managing those assets changes.

Regular way purchases and sales of financial assets are recognised on trade date (that is, the date on which the Group commits to purchase or sell the asset). Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all the risks and rewards of ownership.

Measurement

At initial recognition, the group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Debt instruments

Subsequent measurement of debt instruments depends on the Group's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Group classifies its debt instruments:

Amortised cost: assets that are held for collection of contractual cash flows, where those cash flows represent solely payments of principal and interest, are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as a separate line item in the statement of profit or loss.

2 Summary of significant accounting policies continued

FVOCI: assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses, which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in other gains/(losses). Interest income from these financial assets is included in finance income using the effective interest rate method. Foreign exchange gains and losses are presented in other gains/(losses), and impairment expenses are presented as a separate line item in the statement of profit or loss.

FVPL: assets that do not meet the criteria for amortised cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within other gains/(losses) in the period in which it arises.

Equity instruments

The Group subsequently measures all equity investments at fair value. Where the Group's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognised in profit or loss as other income when the Group's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognised in other gains/(losses) in the statement of profit or loss as applicable. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

Impairment

From 1 January 2018, the Group assesses, on a forward-looking basis, the expected credit losses associated with its debt instruments carried at amortised cost and FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

Accounting policies applied until 31 December 2017

The Group has applied IFRS 9 retrospectively, but has elected not to restate comparative information. As a result, the comparative information provided continues to be accounted for in accordance with the Group's previous accounting policy, as shown below:

All investments are initially recorded at their fair value. Subsequently they are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

Investment loans are measured at amortised cost using the effective interest method.

Available-for-sale financial assets are measured at their fair value with unrealised gains or losses being recognised directly in equity. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognised in the income statement.

Financial assets at fair value through the income statement (disclosed in investment income) include financial assets designated upon initial recognition as at fair value through the income statement.

Financial assets may be designated upon initial recognition as at fair value through profit or loss if the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy.

(m) Trade and other receivables

The Group assesses on a forward-looking basis the expected credit losses associated with its receivables carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. For trade receivables, the Group applies the simplified approach permitted by IFRS 9, resulting in trade receivables recognised and carried at original invoice amount less an allowance for any uncollectible amounts based on expected credit losses.

(n) Cash and cash equivalents

Cash and short-term deposits in the balance sheet comprise cash at bank and in hand and short-term deposits with an original maturity of 3 months or less. For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts. Management has reviewed the classification of certain line items in the 2017 cash flow and identified adjustments required. Accordingly, the cash flow is re-presented and restated but with no change to the net movement in cash and cash equivalents.

(o) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at their fair value less any directly attributable transaction costs.

After initial recognition, loans and borrowings are subsequently measured at amortised cost using the effective interest method, except for instruments designated in fair value hedge relationships. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Gains and losses are recognised in the income statement when the liabilities are derecognised, as well as through the amortisation process.

(p) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when recovery is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost. The Group provides, on a discounted basis, for the future rent expense and related cost of leasehold property (net of estimated sub-lease income) where the space is vacant or currently not planned to be used for ongoing operations.

Notes to the consolidated financial statements continued

2 Summary of significant accounting policies continued

(q) Pension schemes

The Group maintains a number of defined contribution pension schemes and for these schemes the Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense in the income statement as the related service is provided.

In addition, the Group operates a defined benefit pension scheme and participates in a number of other defined benefit pension schemes, all of which require contributions to be made to separate trustee-administered funds. The costs of providing benefits under these schemes are determined separately for each scheme using the projected unit credit method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of the defined benefit obligation) and is based on actuarial advice. Past service costs are recognised immediately in the income statement.

When a settlement (eliminating all obligations for benefits already accrued) or a curtailment (reducing future obligations as a result of a material reduction in the scheme membership or a reduction in future entitlement) occurs, the obligation and related plan assets are re-measured using current actuarial assumptions and the resultant gain or loss recognised in the income statement during the period in which the settlement or curtailment occurs.

Re-measurements of the net defined benefit asset/liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in other comprehensive income and reflected immediately in retained earnings and will not be reclassified to the income statement. The Group determines the net interest expense/income on the net defined benefit asset/liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then net defined benefit asset/liability, taking into account any changes in the net defined benefit asset/liability during the period as a result of contributions and benefit payments.

Current and past service costs are charged to operating profit while the net interest cost is included within net finance costs.

In respect of 3 of the defined benefit pension schemes in which the Group participates, the Group accounts for its legal and constructive obligation over the period of its participation which is for a fixed period only.

The liability on the balance sheet in respect of the defined benefit pension schemes comprises the total for each scheme, or group of schemes, of the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds), less the fair value of plan assets out of which the obligations are to be settled directly. Fair value is based on market price information and in the case of quoted securities is the published bid price. The value of a net pension benefit asset is restricted to the present value of any amount the Group expects to recover by way of refunds from the plan or reductions in the future contributions.

(r) Financial instruments

Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at their fair value less any directly attributable transaction costs.

After initial recognition, loans and borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the income statement over the period of the borrowings using the effective interest method.

Gains and losses are recognised in the income statement when the liabilities are derecognised, as well as through the amortisation process.

Derivative financial instruments

Derivative financial instruments are used to manage exposure to the financial risks of changes in foreign exchange rates and interest rates. The principal derivative instruments used by the Group are foreign currency swaps, interest rate swaps and foreign exchange forward contracts. The Group does not hold or issue derivative financial instruments for trading or speculative purposes.

Derivatives are initially recognised at fair value on the date that a derivative contract is entered into, and they are subsequently re-measured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. The Group designates certain derivatives as either:

- hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedges);
- hedges of a particular risk associated with the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges); or
- hedges of a net investment in a foreign operation (net investment hedges).

At inception of the hedge relationship, the Group documents the economic relationship between hedging instruments and hedged items, including whether changes in the cash flows of the hedging instruments are expected to offset changes in the cash flows of hedged items. The Group documents its risk management objective and strategy for undertaking its hedge transactions.

The fair values of derivative financial instruments designated in hedge relationships are disclosed in note 26. Movements in the hedging reserve in shareholders' equity are shown in note 26. The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months; it is classified as a current asset or liability when the remaining maturity of the hedged item is less than 12 months.

In relation to fair value hedges (for example, receive fixed and pay floating interest rate swaps held as fair value hedges against fixed interest rate borrowings) which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement.

In relation to cash flow hedges, the effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in the cash flow hedge reserve within equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement, within other gains/(losses).

When forward contracts are used to hedge forecast transactions, the Group generally designates only the change in fair value of the forward contract related to the spot component as the hedging instrument. Gains or losses relating to the effective portion of the change in the spot component of the forward contracts are recognised in the cash flow hedge reserve within equity. The change in the forward element of the contract that relates to the hedged item ('aligned forward element') is recognised the income statement at the same time as the hedged transaction. For some hedge relationships, the Group may designate the full change in fair value of the forward contract (including forward points) as the hedging instrument. In such cases, the gains or losses relating to the effective portion of the change in fair value of the entire forward contract are recognised in the cash flow hedge reserve within equity.

2 Summary of significant accounting policies continued

Amounts accumulated in equity are reclassified in the periods when the hedged item affects profit or loss, as follows:

- Where the hedged item subsequently results in the recognition of a non-financial asset, both the deferred hedging gains and losses and the deferred forward points, if any, are included within the initial cost of the asset. The deferred amounts are ultimately recognised in the income statement, since the hedged item affects the income statement.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognised in equity are transferred to the income statement. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction or firm commitment occurs.

Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment, are accounted for in a way similar to cash flow hedges.

Gains or losses on the hedging instrument relating to the effective portion of the hedge are recognised in other comprehensive income and foreign currency translation reserves in equity while any gains or losses relating to any ineffective portion are recognised in the income statement. On disposal of the foreign operation, the cumulative value of any such gains or losses recorded in equity are reclassified to the income statement.

The Group uses loans and foreign exchange derivatives as hedges of its exposures to foreign exchange risks on its investments in foreign subsidiaries.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the income statement and are presented as finance cost excluded from adjusted profits.

Put option arrangements

Put options on the shares of subsidiaries held by non-controlling interest shareholders that oblige the Group to purchase those shares for cash or another financial asset are recognised as a financial liability for the present value of the option exercise price. When the financial liability is recognised initially, that amount is reclassified from equity, and subsequently measured at fair value. Changes in the carrying amount are recognised in equity.

On exercise of the put options, the Group will treat the transaction as the purchase of the non-controlling interest and will apply acquisition accounting as described in (i) Business Combinations and Goodwill – Acquisitions and disposals of non-controlling interests.

(s) Leasing

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date and is concerned with whether the fulfilment of the arrangement is dependent upon the use of a specific asset or assets and the arrangement conveys a right to use the asset.

In assessing whether a lease is an operating lease or a finance lease, judgement needs to be exercised in determining whether or not substantially all the risks and rewards of ownership of the leased asset are held by the Group. Given that finance leases are recognised as liabilities, and operating leases are not, this can have a significant effect on the reported financial position of the Group.

Group as a lessee: Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income. Capitalised leased assets are depreciated over the shorter of the estimated life of the asset or the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

Where a lease is for an asset sold by the Group to the lessor, the two transactions are accounted for separately. If the sale-and-leaseback results in a finance lease, then any gain on the sale is deferred and recognised as income over the lease term. If the leaseback is classified as an operating lease, then any gain is recognised immediately if the sale-and-leaseback terms are at fair value. If the sale-and-leaseback are not deemed to be at fair value then the accounting is as follows:

- If the selling price is at or below fair value, then the gain or loss is recognised immediately. However, if a loss is compensated for by future rentals at below-market price, then the loss is deferred and amortised over the period in which the asset is expected to be used.
- If the selling price exceeds fair value, then that excess is deferred and amortised over the period for which the asset is expected to be used.
- If the fair value of the asset is less than the carrying amount of the asset at the date of the transaction, then that difference is recognised immediately as a loss on the sale.

As noted above the assessment of whether the sale-and-leaseback transactions are at fair value may require significant judgement in addition to that applied to determine whether the lease is an operating or finance lease, and the resulting accounting can have a significant effect on the reported results of the Group.

Group as a lessor: leases where the Group does not transfer substantially all the risks and benefits of ownership of the asset are classified as operating leases. Rental income arising from operating leases is recognised in the income statement on a straight-line basis over the lease term.

(t) Income tax

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from the initial recognition of goodwill;
- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax assets and unused tax losses can be utilised, except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Notes to the consolidated financial statements continued

2 Summary of significant accounting policies continued

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

(u) Share-based payments

The Group operates a number of executive and employee share schemes.

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions).

No expense is recognised for awards that do not ultimately vest as a result of not meeting performance or service conditions. Where all service and performance vesting conditions have been met, the awards are treated as vesting, irrespective of whether or not the market condition is satisfied, as market conditions have been reflected in the fair value of the equity instruments.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, the number of equity instruments that will ultimately vest or, in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity.

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period. In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification. No reduction is recognised if this difference is negative.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any cost not yet recognised in the income statement for the award is expensed immediately. Any compensation paid up to the fair value of the award at the cancellation or settlement date is deducted from equity, with any excess over the fair value being treated as an expense in the income statement.

(v) New standards and interpretations not applied

The IASB have issued the following standards, amendments and interpretations with an effective date after the date of these financial statements. These are effective for annual periods beginning on or after the date indicated:

	Effective date
International Accounting Standards (IAS/IFRSs) and Interpretations (IFRICs)	
Endorsed by the EU:	
IFRS 9 Amendments: Prepayment Features with Negative Compensation	1 January 2019
IFRS 16 Leases	1 January 2019
IFRIC 23 Uncertainty over Income Tax Treatments	1 January 2019
Not yet endorsed by the EU:	
IFRS 17 Insurance Contracts	1 January 2021
IAS 28 Amendments: Long-term Interests in Associates and Joint Ventures	1 January 2019
Annual Improvements to IFRS Standards 2015–2017 Cycle	1 January 2019
IAS 19 Amendments: Plan Amendment, Curtailment or Settlement	1 January 2019
Amendments to References to the Conceptual Framework in IFRS Standards	1 January 2020
IFRS 3 Business Combinations	1 January 2020
Amendments to IAS 1 and IAS 8: Definition of Material	1 January 2020

IFRS 16 Leases

IFRS 16 Leases (IFRS 16) was issued in January 2016, replacing IAS 17 Leases (IAS 17), and other relevant current guidance. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases. IFRS 16 will be effective for annual periods beginning on or after 1 January 2019 with early adoption permitted for entities that apply IFRS 15.

Under the transition rules, the Group will apply IFRS 16 using the modified retrospective approach, with the cumulative effect of applying the standard recognised in retained earnings on 1 January 2019. The Group has elected to apply the short-term lease exemption and low-value items exemption for all lease classes.

The Group has also elected to apply the practical expedient to grandfather the assessment of which arrangements are leases. It will apply IFRS 16 only to contracts that have been classified as leases as at 31 December 2018. Contracts that have not been identified as leases under IAS 17 and IFRS 4 were not reassessed for whether there is a lease.

As at 31 December 2018, the Group held a significant number of operating leases for which the future minimum lease payments amount to £736.0m as disclosed in note 24. As demonstrated below, the standard will have a material impact for the Group as it introduces a single lessee accounting model and requires the recognition of assets and liabilities for all leases.

2 Summary of significant accounting policies continued

The estimated impact for the Group of adopting IFRS 16 is as follows:

Consolidated balance sheet	Footnote	Year ended 31 December 2018 £m	Range of impact on IFRS 16 £m	Expected adoption impact at 1 January 2019 £m
Right-of-use asset	a	—	565–575	565–575
Finance lease receivable	b	—	14–16	14–16
Total assets		4,094	579–591	4,673–4,685
Finance lease liability	c	—	640–650	640–650
Total financial liabilities		3,990	640–650	4,630–4,640
Retained deficit	d	(1,135)	(23)–(25)	(1,158)–(1,160)
Total equity		103	(23)–(25)	78–80

Consolidated income statement	Footnote	Expected adoption impact 2019 £m
EBITDA	e	130–135
Operating profit	e	19–21
Finance costs	e	(28–30)
Profit before tax	e	(8–10)

a. **Right-of-use asset:** total assets will be impacted due to recognition of right-of-use assets on 1 January 2019. The right-of-use assets are initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the adoption date less any lease incentives received at or before the adoption date (reclassified on the opening balance sheet). For a selection of material long-term leases, the Group will apply the modified retrospective method one approach, as if IFRS 16 had always been applied using the incremental borrowing rate at the date of initial application. The right-of-use assets will be subsequently depreciated using the straight-line method to the earlier of the end of the useful life or the end of the lease term.

b. **Finance lease receivable:** total assets will be impacted by recognition of finance lease receivables where the Group acts as an intermediate lessor and has classified the sub lease as a finance lease because the sub-lease is for a substantial amount of the remaining term of the head lease.

c. **Finance lease liability:** total financial liabilities will be impacted due to the recognition of finance lease liabilities. The lease liability will be initially measured at the present value of the lease payments that are not paid at the adoption date, discounted using the Group's incremental borrowing rate. The lease payments comprise fixed payments, including in-substance fixed payments such as service charges and variable lease payments that depend on an index or a rate, initially measured using the minimum index or rate at commencement date. The lease liability will be measured at amortised cost using the effective interest rate method. For leases with termination and extension options, the Group has made an assessment whether the option is reasonably certain to be exercised.

d. **Retained deficit:** Retained deficit change represents the expected cumulative effect of applying the standard. This is due to applying the modified retrospective method one approach for a selection of properties, as explained in note a. above.

e. **Income statement:** Upon adopting IFRS 16, the rental costs currently recognised in operating profit will be replaced by depreciation on the right-of-use asset and net finance costs on the finance lease liability. As the asset is depreciated straight line over the lease term and the interest is accrued using the effective interest rate method, while EBITDA will improve, the profit will be reduced in the earlier years as a result of applying IFRS 16.

The above impacts are expected to increase the leverage ratio by 0.6 times. However the impact on the Group's adjusted net debt to adjusted EBITDA covenant ratio is expected to be neutral to positive as the Group covenants are on frozen GAAP, with the exception of the US private placement notes. The US private placement notes covenant test includes the income statement impact of IFRS 16, but not the balance sheet.

Due to the changes in assets, liabilities, income and expenses that will be recognised as a result of the application of IFRS 16, there are consequent IAS 12 income tax differences that arise on transitional adjustment. The tax impact is expected to be £4m–5m, resulting in an increase in deferred tax assets.

The total cash outflow for lease payments will not change, however the payments related to the principal liability will be presented as cash outflows from financing activities, as opposed to the current treatment as cash outflow from operating activities.

The Group will continue to implement and refine procedures and processes to apply the new requirements of IFRS16. As a result of this ongoing work, it is possible that there may be some changes to the adoption impact above prior to the 30 June 2019 results being issued. However, at this time these are not expected to be material.

Due to the Group transformation plan, which includes a consolidation of Capita's properties, the Group's lease portfolio is expected to materially change over the next few years. Any changes to the lease portfolio will be accounted for when transacted. The costs arising from the property rationalisation programme will be excluded from adjusted profit in line with the current Group policy.

Notes to the consolidated financial statements continued

3 Adjusted operating profit and adjusted profit before tax

The items below are excluded from the adjusted results as the Board has concluded that it is appropriate to do so. These amounts are (or have been) material, and require separate disclosure in order for the users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business. The tax impact of the operating profit adjusting items is a £41.5m credit (31 December 2017: £52.2m credit). The tax impact of the profit before tax adjusting items is a £20.4m credit (31 December 2017: £51.8m credit). These items are discussed further below:

		Operating profit		Profit before tax	
	Notes	2018 £m	2017 £m	2018 £m	2017 £m
Reported		**34.9**	(420.1)	**272.6**	(513.1)
Amortisation and impairment of acquired intangibles	14	**143.5**	138.3	**143.5**	138.3
Impairment of goodwill	15	**33.8**	551.6	**33.8**	551.6
Impairment of other non-current assets	13	**—**	63.5	**—**	63.5
Impairment of Life & Pensions assets	13	**—**	61.2	**—**	61.2
Impairment of loans and investments		**1.6**	9.0	**1.6**	9.0
Litigation and claims		**(1.8)**	30.0	**(1.8)**	30.0
GMP and retirement age equalisation	32	**5.4**	—	**5.4**	—
Net finance costs	9	**—**	—	**18.8**	(2.1)
Contingent consideration movements (and acquisition costs in 2017)		**(5.0)**	(0.8)	**(5.0)**	(0.8)
Business exit – trading	4	**(16.8)**	(16.8)	**(16.8)**	(16.7)
Business exit – non-trading expenses	4	**29.7**	13.7	**29.7**	13.7
Business exit – (gain)/loss on disposals	4	**—**	—	**(309.7)**	30.6
Significant restructuring		**110.0**	17.9	**110.0**	17.9
Adjusted		**335.3**	447.5	**282.1**	383.1

Amortisation and impairment of acquired intangible assets: the Group carries on its balance sheet significant balances related to acquired intangible assets. The amortisation of these assets, and any impairment charges, are reported separately as they distort the in-year trading results, and performance of the acquired businesses is assessed through the underlying operational results. In 2018 the Group amortised £86.7m of which £4.9m belongs to disposed entities and is included in business exit. In addition the Group recognised an impairment charge relating to acquired intangible assets of £61.7m in relation to the Swiss business in Customer Management.

Impairment of goodwill: the Group carries on its balance sheet significant balances related to acquired goodwill. Goodwill is subject to annual impairment testing, and any impairment charges are reported separately as they distort the in-year trading results and IFRS does not permit the recognition of any increases in value of acquisitions, potentially leading to an unbalanced picture being shown over time. Refer to note 15 for further detail on these impairments.

Impairment of other non-current assets: as part of its year-end close process in 2017, Capita undertook a comprehensive review of its tangible and intangible assets. Following the review, management took a decision to impair, as at 31 December 2017, a number of assets relating to specific programmes resulting from changes in client and Capita strategy in the second half of 2017. These impairments have no adverse impact on future cash or trading. Non-current assets amounting to £63.5m (£35.2m property, plant and equipment – see note 13; £28.3m capitalised software intangible assets – see note 14) were written off and excluded from adjusted profit as the assets have no further value to the Group.

Impairment of life and pensions assets: the Group's life and pension business developed a platform to support an existing life and pensions contract, but which could provide services to multiple clients in the future. In 2017, the Group identified there was no longer a market for this platform and accordingly the carrying value of this and associated assets were written off as at 31 December 2017. The impact on the financial statements is a non-underlying charge of £61.2m (£54.7m property, plant and equipment – see note 13; £1.0m capitalised software intangible assets – see note 14; £5.5m contract fulfilment asset – see note 17) representing the write-off of the non-current assets. The charge was excluded from adjusted profit as the assets had no further value to the Group.

Impairment of loans and investments: the Group fully impaired an investment in the year, and a historical loan and investment in the prior year. The charge is reported separately due to its nature and to be consistent to prior years. In 2018 the Group impaired £1.6m of investments.

Litigation and claims: the significant litigation costs provided in 2017 relate to two claims in respect of:

1. a contract within the Group's Real Estate and Infrastructure business notified to the Group during 2017. The related contract began in 2007; and
2. a contract within the Group's Employee Benefits business where more information on the progress of the claim became apparent. The related contract was delivered from 2009.

The amount provided in respect of these two claims has been recognised in non-underlying due to their age and significance.

The gain of £1.8m in 2018 arises from a loss of derecognition of an insurance asset of £3.7m (see note 18), off-set by a release of £5.5m in respect of the above provisions recognised in 2017. The original claim to which the asset related was excluded from adjusted profit due to its nature and size.

GMP and retirement age equalisation: the High Court issued a judgment in October 2018 which concluded that pension schemes should be amended to equalise pension benefits for men and women in relation to guaranteed minimum pension 'GMP' benefits. This will impact many pension schemes including the Group's defined benefit schemes. The Group is working with the Trustees and their advisers to understand the extent to which the judgment crystallises additional liabilities. For the purpose of these financial statements, we have estimated that this will increase the reported liability of the pension schemes by £4.4m and this is reflected as a past service cost in 2018 and thus taken through the income statement. In addition, there is a past service cost of £1m in relation to the correction of a historical retirement age equalisation issue for a small group of members in the main scheme. The amounts provided in respect of GMP and retirement age equalisation are excluded from adjusted profit because they relate to past service costs and therefore not reflective of in-year performance.

3 Adjusted operating profit and adjusted profit before tax continued

Net finance costs: non-underlying net finance costs includes the movements in the mark to market valuation of certain financial instruments, and in 2018, the make-whole costs paid to noteholders on early repayment of principal on the Private Placement loan notes from the proceeds of the rights issue and disposals. Refer to note 9 for further details.

Contingent consideration movements and acquisition-related costs: in accordance with IFRS 3, movements in the fair value of contingent consideration on acquisitions go through the Group income statement. These are reported separately because performance of the acquired businesses is assessed through the underlying operational results and such a charge/credit movement would distort underlying results. Acquisition-related costs incurred with acquisitions are not included in the assessment of business performance which is based on the adjusted results. IFRS requires certain costs incurred in connection with acquired businesses to be recorded within the Group income statement. These charges are not included in the internal assessment of business performance which as above is based on the underlying operational results. These charges are therefore separately disclosed as specific items.

Business exits: the trading result of businesses exited, or in the process of being exited, and the gain or loss on disposals, are disclosed outside the adjusted results. The 2017 results have been restated for the trading of those businesses exited, or in the process of being exited, in 2018 to enable comparability of the adjusted results.

Significant restructuring: in January 2018, the Group announced a multi-year transformation plan. In the period to 31 December 2018, a charge of £110.0m (2017: £17.9m) was recognised in relation to the cost of the transformation plan, and restructuring costs relating to Capita's previously announced cost reduction plan. The costs include the following sub-categories:

- Cost to realise cost savings and efficiencies from the transformation plan (£55m): including significant reductions in overheads via support function restructuring, and the elimination of duplicate roles. These costs also include engaging the Group's property expertise to rationalise and increase the utilisation of Capita's property estate, in metro centres and regionally. As the Group continues to rationalise the property estate cost associated with onerous lease commitments and dilapidation liabilities will be captured and presented as part of the transformation adjustments.
- Professional fees (£31m): incurred to support the delivery of the future strategy, redesign of the Group's operating model, re-ignite sales growth and increasing the proportion of centrally controlled spend, consolidating the supplier base and leveraging the Group's scale.
- Finance transformation (£6m): improving the Group's financial reporting systems, processes and controls, through increasing standardisation, automation and the quality and availability of data. The Group is investing in an upgrade of its financial system and increasing the use of offshoring and shared services. This programme is titled 'Smarter Faster Finance' and all costs associated with this programme are recorded separately, excluding any costs capitalised as part of the investment and the ongoing depreciation and amortisation of such assets.
- Previously announced cost-reduction plan (£18m): restructuring costs related to the Group's cost-reduction plan announced in prior periods, but did not meet the criteria for provision at the end of 2017.

4 Business exit

2018 business exits

Business exits are businesses that have been exited during the year or are in the process of being disposed of. None of these business exits meet the definition of 'discontinued operations' as stipulated by IFRS 5, which requires disclosure and comparatives to be restated where the relative size of a disposal or business closure is significant, which is normally understood to mean a reported segment. Accordingly, the separate presentation described below does not fall within the requirements of IFRS 5 concerning discontinued operations. However, to enable a like-for-like comparison of adjusted results, the 2017 comparatives have been restated to include 2018 business exits.

During the period, the Group disposed of five businesses and exited one business – Capita Specialist Insurance Solutions, Projen (which was held for sale as at 31 December 2017), Medicals Direct Group, Supplier Assessment Services (including Constructionline), ParkingEye and REI Health.

		Non-trading disposal			
Income statement impact	Trading £m	Cash £m	Non-cash £m	Total £m	Total £m
Revenue	**50.8**	—	—	—	**50.8**
Cost of sales	**(20.2)**	—	—	—	**(20.2)**
Gross profit	**30.6**	—	—	—	**30.6**
Administrative expenses	**(13.8)**	**(1.0)**	**(28.7)**	**(29.7)**	**(43.5)**
Operating profit/(loss)	**16.8**	**(1.0)**	**(28.7)**	**(29.7)**	**(12.9)**
Net finance costs	—	—	—	—	—
Gain on business disposal	—	**367.4**	**(57.7)**	**309.7**	**309.7**
Profit before tax	**16.8**	**366.4**	**(86.4)**	**280.0**	**296.8**
Taxation	**(3.1)**	**(23.4)**	—	**(23.4)**	**(26.5)**
Profit after tax	**13.7**	**343.0**	**(86.4)**	**256.6**	**270.3**

Trading revenue and costs represent the current period trading performance of those businesses up to the point of being disposed or exited. The 2017 comparative trading operating profit for the year ended 31 December 2017 was £17.8m, representing a full year of trading.

Non-trading administrative expenses comprise £1.0m of closure costs, £24.3m of goodwill impairment, £4.9m of acquired intangible amortisation and £0.5m release of provisions.

There are no cumulative income or expenses included in other comprehensive income relating to the disposal group.

The gain on disposal of £309.7m arises from the disposal of net assets of £69.0m for £400.7m consideration and costs of disposal of £22.0m. Cash proceeds of £400.7m net of cash disposed amounted to £389.5m.

Notes to the consolidated financial statements continued

4 Business exit continued

Gain on business disposal	Cash £m	Non-cash £m	Total £m
Property, plant and equipment	—	19.9	19.9
Intangible assets	—	12.4	12.4
Goodwill	—	50.9	50.9
Trade and other receivables	—	8.5	8.5
Deferred tax asset	—	0.1	0.1
Trade and other payables	—	(26.8)	(26.8)
Deferred income	—	(4.6)	(4.6)
Income tax payable	—	(1.5)	(1.5)
Deferred tax liability	—	(0.9)	(0.9)
Provisions	—	(0.2)	(0.2)
Cash disposed of	11.2	—	11.2
Total net assets disposed of	11.2	57.8	69.0
Cash purchase consideration received	400.7	—	400.7
Costs of disposal – paid and accrued	(22.0)	—	(22.0)
Proceeds, less costs, on disposal	378.7	—	378.7
Gain on business disposal	367.5	(57.8)	309.7

Cash proceeds in 2018	Cash £m
Cash purchase consideration received	400.7
Settlement of receivables sold as part of the disposal	19.0
Total consideration received	419.7
Cost of disposal – paid in the year	(11.9)
Net proceeds received in year	407.8

Business exit cash flows

Business disposed of during 2018 generated operating cash outflows of £6.6m.

2017 business exits

Business exits are businesses that have been exited during the year or in the process of being disposed of. Except for the disposal of Capita Asset Services (disclosed separately in note 5 'Discontinued Operations'), none of the Group's business exits meet the definition of 'discontinued operations' as stipulated by IFRS 5, which requires disclosure and comparatives to be restated where the relative size of a disposal or business closure is significant, which is normally understood to mean a reported segment. Accordingly, the separate presentation described below does not fall within the requirements of IFRS 5 concerning discontinued operations.

In the Annual Report 2016, we disclosed that the Group intended to dispose of the majority of its specialist recruitment business which no longer fit the Group's business strategy. As at 31 December 2016, this business did not meet the criteria to be treated as held for sale.

In the Annual Report 2017, the disposal of the specialist recruitment business had completed along with the closure of a number of small businesses, and their results are all included within business exits for the period. At 31 December 2017, the Group was in an active process to sell a non-core property business (Projen) and treated this as a disposal group held for sale at that date.

During 2018, the Company disposed of five businesses and exited one business – Capita Specialist Insurance Solutions, Projen (which was held for sale as at 31 December 2017), Medicals Direct Group, Supplier Assessment Services (including Constructionline), ParkingEye and REI Health. The 2017 income statement below has been restated to include the results of these disposed businesses. The total loss before tax in 2017 before restatement was £45.4m and the operating loss in 2017 before restatement was £14.7m.

		Non-trading disposal			
Income statement impact	Trading £m	Cash £m	Non-cash £m	Total £m	Total £m
Revenue	142.8	—	—	—	142.8
Cost of sales	(88.1)	—	—	—	(88.1)
Gross profit	54.7	—	—	—	54.7
Administrative expenses	(37.9)	(4.7)	(9.0)	(13.7)	(51.6)
Operating profit	16.8	(4.7)	(9.0)	(13.7)	3.1
Net finance costs	(0.1)	—	—	—	(0.1)
Loss on business disposal	—	16.3	(46.9)	(30.6)	(30.6)
Profit/(loss) before tax	16.7	11.6	(55.9)	(44.3)	(27.6)
Taxation	(2.2)	—	—	—	(2.2)
Profit/(loss) after tax	14.5	11.6	(55.9)	(44.3)	(29.8)

Trading revenue and costs represent the current year trading performance of those businesses being exited or disposed in 2017 and 2018 (as noted above).

Non-trading disposal and closure costs include the costs of exiting businesses and stranded costs such as property lease and redundancy payments.

The loss on disposal of £30.6m arises from the disposal, in 2017, of net assets of £47.0m for £17.0m cash consideration and costs of disposal of £0.6m.

4 Business exit continued

Non-trading administrative expenses comprise £4.7m of disposal and closure costs and £9.0m of accelerated depreciation, amortisation and impairments.

Balance Sheet – disposal group

At 31 December 2017, the Group was in an active process to sell a non-core property business and has treated this as a disposal group held for sale at this date.

	2017 £m
Intangibles	1.5
Trade and other receivables	4.4
Assets held for sale	5.9
Trade and other payables	(1.4)
Liabilities held for sale	(1.4)

Business exit cash flows

Businesses disposed of and held for sale during 2017 generated operating cash inflows, prior to disposal, of £2.5m.

5 Discontinued operations

The Group disposed of the majority of the Capita Asset Services Division in November 2017.

The disposal met the definition of a discontinued operation as stipulated by IFRS 5. The following presentation, and that included in other notes, follows the requirements of IFRS 5.

	2018			2017		
Discontinued operations:	**Trading £m**	**Non-trading £m**	**Total £m**	Trading £m	Non-trading £m	Total £m
Revenue	—	—	—	261.9	—	261.9
Cost of sales	—	—	—	(94.0)	—	(94.0)
Gross profit	—	—	—	167.9	—	167.9
Administrative expenses	—	**5.6**	**5.6**	(120.3)	(66.2)	(186.5)
Operating profit/(loss)	—	**5.6**	**5.6**	47.6	(66.2)	(18.6)
Net finance costs	—	—	—	0.1	0.8	0.9
Profit on disposal	—	—	—	—	445.4	445.4
Profit before tax	—	**5.6**	**5.6**	47.7	380.0	427.7
Income tax expense	—	—	—	(10.6)	(0.7)	(11.3)
Profit for the period	—	**5.6**	**5.6**	37.1	379.3	416.4

The 2018 non-trading credit to administrative expenses consisted of £5.6m provision releases. The 2017 non-trading administrative expense consisted of amortisation of acquired intangibles of £0.6m and Capita Asset Services indemnity and settlement provision of £65.6m. Non-trading net finance costs included fair value movements on held for sale assets.

As part of the sale it was agreed with the Trustees of the Capita Pension and Life Assurance Scheme that a cash contribution of £17.0m would be made to the Scheme. This was paid in January 2018 (refer to note 32). In addition the Group paid £82.2m in 2018 for costs relating to the disposal, all of which were fully provided for.

The earnings per share impact from discontinued operations is 0.38p (2017: 38.10p) on basic earnings per share and 0.38p (2017: 38.10p) on diluted earnings per share.

Notes to the consolidated financial statements continued

6 Segmental information

The Group's operations are managed separately according to the nature of the services provided, with each segment representing a strategic business division offering a different package of client outcomes across the markets the Group serves. A description of the service provision for each segment can be found in the strategic report on pages 21–33.

As announced in the Annual Report 2017, the Group introduced a new simplified divisional structure in 2018 around five markets: Software, People Solutions, Customer Management, Government Services and IT & Networks. Capita has also formed a sixth division, Specialist Services, which includes those businesses which either (a) are not within Capita's key growth markets and/or (b) are at an early phase in their development but may be scaled up in the future. These businesses are mostly stand-alone operations and are being managed on a portfolio basis in order to maximise value. These divisions are supported by a common set of Group capabilities and functions, and are reported separately as 'Group trading and central services'.

Comparative information has been restated accordingly. The Board believes the changes improve accountability and transparency across the Group.

Before eliminating sales between business units on consolidation, the Group accounts for sales between business units as if they were to a third party at market rates.

The tables below present revenue, trading result and certain asset and liability information for the Group's business segments for the years 2018 and 2017. All operational divisions are continuing and the 2017 segmental information has been restated for the impact of businesses exited or held for sale in 2018 with total adjusted revenue reduced by £76.1m and profit before tax reduced by £17.8m.

Year ended 31 December 2018	Notes	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central services £m	Total adjusted £m	Adjusting items £m	Total reported £m
Continuing operations											
Long-term contractual		353.9	295.2	563.6	647.4	296.5	601.0	13.8	2,771.4	3.2	2,774.6
Short-term contractual		34.7	38.0	228.7	4.7	55.3	201.3	24.5	587.2	47.6	634.8
Transactional (point in time)		7.8	165.1	1.9	93.4	52.2	189.9	(1.3)	509.0	—	509.0
Total segment revenue		396.4	498.3	794.2	745.5	404.0	992.2	37.0	3,867.6	50.8	3,918.4
Trading revenue		447.4	649.4	904.3	758.5	636.8	1,087.0	81.2	4,564.6	—	4,564.6
Inter-segment revenue		(51.0)	(151.1)	(110.1)	(13.0)	(232.8)	(94.8)	(44.2)	(697.0)	—	(697.0)
Total adjusted segment revenue		396.4	498.3	794.2	745.5	404.0	992.2	37.0	3,867.6	—	3,867.6
Business exits – trading	4	—	—	—	—	—	50.8	—	—	50.8	50.8
Total segment revenue		396.4	498.3	794.2	745.5	404.0	1,043.0	37.0	—	—	3,918.4
Adjusted operating profit	3	112.4	40.7	39.6	35.2	45.3	139.5	(77.4)	335.3	—	335.3
Restructuring	3	(9.3)	(12.5)	(10.9)	(6.3)	(4.5)	(15.9)	(50.6)	—	(110.0)	(110.0)
Business exits – trading	4	—	(0.3)	0.3	—	—	16.8	—	—	16.8	16.8
Total trading result		103.1	27.9	29.0	28.9	40.8	140.4	(128.0)	335.3	(93.2)	242.1
Non-trading items:											
Business exits – non-trading	4								—	(29.7)	(29.7)
Other adjusting items	3								—	(177.5)	(177.5)
Operating profit									335.3	(300.4)	34.9
Net finance costs	9								(53.2)	(18.8)	(72.0)
Gain on business disposal	4								—	309.7	309.7
Profit before tax									282.1	(9.5)	272.6
Income tax credit/(expense)	10								(27.4)	28.3	0.9
Profit for the year – continuing operations									254.7	18.8	273.5
Profit for the year – discontinued operations	5								—	5.6	5.6
Profit for the year – total									254.7	24.4	279.1

6 Segmental information continued

Year ended 31 December 2017	Notes	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central services £m	Total adjusted £m	Adjusting items £m	Total reported £m
Continuing operations											
Long-term contractual		361.6	295.2	582.2	752.3	278.7	632.2	22.6	2,924.8	5.2	2,930.0
Short-term contractual		32.6	42.7	245.9	4.1	63.6	198.9	9.1	596.9	81.6	678.5
Transactional (point in time)		7.5	182.6	0.8	105.3	73.1	191.6	9.2	570.1	56.0	626.1
Total segment revenue		401.7	520.5	828.9	861.7	415.4	1,022.7	40.9	4,091.8	142.8	4,234.6
Trading revenue		441.7	662.4	944.1	884.9	652.4	1,119.4	97.4	4,802.3	—	4,802.3
Inter-segment revenue		(40.0)	(141.9)	(115.2)	(23.2)	(237.0)	(96.7)	(56.5)	(710.5)	—	(710.5)
Total adjusted segment revenue		401.7	520.5	828.9	861.7	415.4	1,022.7	40.9	4,091.8	—	4,091.8
Business exits – trading	4	—	55.1	0.8	—	—	86.9	—	—	142.8	142.8
Total segment revenue		401.7	575.6	829.7	861.7	415.4	1,109.6	40.9	—	—	4,234.6
Adjusted operating profit	3	111.7	62.7	57.8	78.7	62.0	140.6	(66.0)	447.5	—	447.5
Restructuring	3	(2.2)	(4.3)	1.3	(3.9)	(1.1)	5.9	(13.6)	—	(17.9)	(17.9)
Business exits – trading	4	—	(1.7)	0.7	—	—	17.8	—	—	16.8	16.8
Total trading result		109.5	56.7	59.8	74.8	60.9	164.3	(79.6)	447.5	(1.1)	446.4
Non-trading items:											
Business exits – non-trading	4								—	(13.7)	(13.7)
Other adjusting items	3								—	(852.8)	(852.8)
Operating profit/(loss)									447.5	(867.6)	(420.1)
Net finance costs	9								(64.4)	2.0	(62.4)
Loss on business disposal	4								—	(30.6)	(30.6)
Profit/(loss) before tax									383.1	(896.2)	(513.1)
Income tax (expense)/credit	10								(65.8)	51.8	(14.0)
Profit/(loss) for the year – continuing operations									317.3	(844.4)	(527.1)
Profit for the year – discontinued operations	5								—	416.4	416.4
Profit/(loss) for the year – total									317.3	(428.0)	(110.7)

Notes to the consolidated financial statements continued

6 Segmental information continued

Order book

The tables below show the order book for each division, categorised into long-term contractual (contracts with length greater than two years) and short-term contractual (contracts with length less than two years). The length of the contract is calculated from the start of the service commencement date. The figures represent the aggregate amount of currently contracted transaction price allocated to the performance obligations that are unsatisfied or partially unsatisfied. Revenue expected to be recognised upon satisfaction of these performance obligations is as follows:

Order book 31 December 2018	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central functions £m	Total £m
Long-term contractual	559.6	715.3	2,011.8	2,187.5	380.4	1,239.1	—	7,093.7
Short-term contractual	—	—	—	—	—	2.3	—	2.3
Total	559.6	715.3	2,011.8	2,187.5	380.4	1,241.4	—	7,096.0

Order book 31 December 2017	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central functions £m	Total £m
Long-term contractual	543.4	786.5	1,843.6	2,660.6	508.3	1,833.7	3.8	8,179.9
Short-term contractual	—	—	—	—	—	11.1	—	11.1
Total	543.4	786.5	1,843.6	2,660.6	508.3	1,844.8	3.8	8,191.0

The table below shows the time bands of the expected timing of revenue to be recognised on long-term contractual at 31 December 2018:

Time bands of long-term contractual in order book	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central functions £m	Total £m
< 1 year	331.3	222.9	602.8	425.3	169.3	336.0	—	2,087.6
1–5 years	196.7	451.3	1,400.1	1,432.7	167.7	683.0	—	4,331.5
> 5 years	31.6	41.1	8.9	329.5	43.4	220.1	—	674.6
Total	559.6	715.3	2,011.8	2,187.5	380.4	1,239.1	—	7,093.7

The order book represents the consideration to which the Group will be entitled to receive from the customers when the Group satisfies the remaining performance obligations in the contracts. However, the total revenue that will be earned by the Group will also include non-contracted volumetric revenue, new wins, scope changes and anticipated contract extensions. These elements have been excluded from the figures in the tables above as they are not contracted. In addition, revenue from contract extensions is also excluded in the order book unless they are pre-priced extensions whereby the Group has a legal binding obligation to deliver the performance obligations during the extension period. The total revenue related to pre-priced extensions that has been included in the tables above amounted to £508.0m (2017: £502.0m). The amounts presented do not include orders for which neither party has performed and each party has the unilateral right to terminate a wholly unperformed contract without compensating the other party.

Of the £7.1bn (2017: £8.2bn) revenue to be earned on long-term contractual, £4.2bn (2017: £4.9bn) relates to material contracts to the Group. This amount excludes revenue that will be derived from frameworks (transactional (point in time) contracts), non-contracted volumetric revenue, non-contracted scope changes and future unforeseen volume changes from these material contracts, which together are expected to contribute an additional £2.2bn (2017: £1.8bn) of revenue to the Group over the life of these contracts.

6 Segmental information continued

Other segment information

31 December 2018	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central functions £m	Total £m
Property, plant and equipment	9.6	44.7	39.9	14.0	33.0	39.9	32.5	213.6
Intangible assets acquired in business combinations	296.7	206.1	155.4	21.5	237.5	468.5	—	1,385.7
Intangible assets capitalised/purchased	71.4	31.9	4.1	10.1	3.4	17.2	63.9	202.0
Contract fulfilment assets	69.8	22.5	38.1	63.4	31.9	38.5	—	264.2
Trade and other receivables	46.6	116.8	150.7	101.7	113.3	224.4	44.4	797.9
Financial assets							127.3	127.3
Deferred taxation							144.6	144.6
Cash							957.5	957.5
Income tax receivable							0.9	0.9
Total assets	494.1	422.0	388.2	210.7	419.1	788.5	1,371.1	4,093.7
Deferred income	205.8	98.6	267.1	333.0	74.3	278.8	—	1,257.6
Trade and other payables	23.9	51.1	95.2	66.4	60.3	187.0	196.4	680.3
Overdrafts							314.8	314.8
Financial liabilities							1,387.3	1,387.3
Deferred taxation							15.2	15.2
Provisions							116.2	116.2
Employee benefits							219.0	219.0
Total liabilities	229.7	149.7	362.3	399.4	134.6	465.8	2,248.9	3,990.4
Total net assets/(liabilities)	264.4	272.3	25.9	(188.7)	284.5	322.7	(877.8)	103.3

31 December 2017	Software £m	People Solutions £m	Customer Management £m	Government Services £m	IT & Networks £m	Specialist Services £m	Group trading and central functions £m	Total £m
Property, plant and equipment	6.6	28.1	31.2	10.9	21.2	70.2	51.1	219.3
Intangible assets acquired in business combinations	321.5	209.5	225.8	58.3	250.5	579.6	—	1,645.2
Intangible assets capitalised/purchased	53.6	34.1	4.8	12.3	4.7	8.6	48.8	166.9
Contract fulfilment assets	73.1	16.3	43.4	39.7	19.3	60.7	—	252.5
Trade and other receivables	65.7	166.9	129.9	99.9	129.5	184.7	27.2	803.8
Financial assets							221.0	221.0
Deferred taxation							159.3	159.3
Disposal group assets held for sale							5.9	5.9
Cash							921.7	921.7
Income tax receivable							25.6	25.6
Total assets	520.5	454.9	435.1	221.1	425.2	903.8	1,460.6	4,421.2
Deferred income	248.0	109.3	287.3	358.4	125.0	381.3	5.9	1,515.2
Trade and other payables	17.8	28.4	50.0	57.2	25.3	67.4	526.1	772.2
Overdrafts							443.3	443.3
Financial liabilities							1,987.3	1,987.3
Provisions							12.2	12.2
Deferred taxation							1.4	1.4
Income tax payable							212.6	212.6
Employee benefits							406.8	406.8
Total liabilities	265.8	137.7	337.3	415.6	150.3	448.7	3,595.6	5,351.0
Total net assets/(liabilities)	254.7	317.2	97.8	(194.5)	274.9	455.1	(2,135.0)	(929.8)

The table below presents revenue by geographical location, and carrying amount of non-current assets by location of those assets.

	2018			2017		
	United Kingdom £m	Non-United Kingdom £m	Total £m	United Kingdom £m	Non-United Kingdom £m	Total £m
Revenue	3,609.7	308.7	3,918.4	3,902.2	332.4	4,234.6
Non-current assets	2,040.3	51.4	2,091.7	2,168.0	143.8	2,311.8

Notes to the consolidated financial statements continued

7 Operating profit

This is stated after charging/(crediting):

	Notes	2018 £m	2017 £m
Depreciation		**59.1**	63.5
Impairment of property, plant and equipment	13	**6.1**	—
Amortisation of capitalised/purchased intangible assets		**27.8**	19.9
Loss/(profit) on sale of property, plant and equipment and intangibles[1]		**11.4**	(4.5)
Minimum lease payments recognised as an operating lease expense		**114.7**	121.1
Foreign exchange differences		**(9.6)**	(5.6)
Contract fulfilment asset utilisation, impairment and derecognition	17	**127.5**	89.3
Property commercialisation		**—**	(2.7)
Contract termination (gains)/losses		**(6.7)**	(6.4)
Gain on early termination of the Prudential and Marsh contracts		**(15.2)**	—
Defence Infrastructure Organisation contract		**—**	(22.0)
Supplier settlement		**—**	(9.2)

The table above includes items only within adjusted operating profit. Specific items excluded from adjusted operating profit are detailed in note 3.

1 The 2017 disclosure of a loss on disposal of £0.5m has been restated to a gain on disposal of £4.5m. This does not have an impact on the reported profit for 2017.

Adjusted operating profit includes the following items:

- **Contract fulfilment asset utilisation, impairment and derecognition:** the Group undertook a comprehensive review of its major contracts to identify indicators of impairment of contract fulfilment assets. Following this review, management provided against costs capitalised as contract fulfilment assets of £22.2m (31 December 2017: £14.1m) within cost of sales. Refer to note 17 for further details of the review.
- **Contract termination gains:** customer contracts usually contain provisions to compensate the Group for exit costs and future profits in the event of early termination. In-year customer contract terminations for customer convenience have led to associated exit fees paid to Capita of £6.7m (2017: £6.4m) being recorded as income in-year. These are included within adjusted operating profit because these amounts are payable to the Group under the terms of the respective contracts being terminated.
- **Prudential, Marsh, and Defence Infrastructure Organisation contracts:** contract terminations arising in the normal course of business and which result in the disposal of a contract fulfilment asset and/or a true-up of revenue recognised, will also be included within the adjusted results and separately disclosed if considered material:
  - In 2018, two contracts in the Specialist Services division ended: (i) the administration of Prudential's life and pensions business transferred to a new supplier resulting in a net £6.0m benefit from the true-up of revenue recognised and the disposal of related assets (including £9.3m included in the loss on disposal of £11.4m of property, plant and equipment and intangibles); and (ii) our general insurance contract with Marsh ended resulting in a £9.2m benefit from the true-up of revenue recognised and disposal of related assets.
  - In 2017, we concluded discussions with the Ministry of Defence in relation to the the Defence Infrastructure Organisation (DIO) contract, which is expected to end in 2019. The 2017 results for the Government Services division included a £22.0m benefit from the re-shaping of the DIO contract.
- **Supplier settlement:** the IT & Networks division benefited from a one-off supplier settlement of £nil (2017: £9.2m).
- **Minimum lease payments:** see note 24 for further details.

Fees payable to the Company's auditor and its associates in respect of:	2018 £m	2017 £m
Audit and audit-related services		
The audit of the Company and Group financial statements	**3.2**	3.8
The audit of the financial statements of subsidiaries of the Company	**1.8**	1.2
Total audit and audit-related services	**5.0**	5.0
Non-audit services		
Taxation compliance services	**—**	0.1
Services related to corporate finance transactions	**—**	0.1
Other assurance services	**1.6**	0.8
Total non-audit services	**1.6**	1.0
Total audit and non-audit services	**6.6**	6.0

The amounts included in the above table relate to fees payable to KPMG LLP and its associates.

8 Employee benefits expense

	Notes	2018 £m	2017 £m
Wages and salaries		**1,702.1**	1,899.5
Social security costs		**175.0**	194.2
Pension costs	32	**112.6**	122.3
Share-based payments	28	**3.4**	2.9
		1,993.1	2,218.9

The expenses above reflect total operations. Employee benefits expense for continuing operations is £1,993.1m (2017: £2,098.6m).

The aggregate amount of Directors' remuneration (salary, bonus and benefits) is shown on page 92 of the remuneration report:

- As shown in note 33 'related-party transactions', the aggregate amount of gains made by Directors on exercise of share options was £0.0m (2017: £0.7m).
- The remuneration of the highest paid Director was £2,014,209 (2017: £1,125,510).
- Payments have been made to a defined contribution pension scheme on behalf of three Directors (2017: five Directors). For the highest paid Director, pension contributions of £36,250 (2017: £21,310) were made.

The average number of employees during the year was made up as follows:	2018 Number	2017 Number
Sales	**1,733**	1,825
Administration	**7,930**	8,148
Operations	**56,239**	59,486
	65,902	69,459

The average number of employees above reflects continuing operations and excludes employees relating to discontinued operations.

9 Net finance costs

	Notes	2018 £m	2017 £m
Interest receivable		**(2.6)**	(0.7)
Private placement loan notes[1]		**40.4**	37.7
Fixed rate interest rate swaps		**—**	2.6
Cash flow hedges recycled to the income statement	26	**(2.5)**	—
Bank loans and overdrafts		**8.5**	15.6
Net interest cost on defined benefit pension schemes	32	**9.4**	9.2
Interest payable		**55.8**	65.1
Net finance costs included in adjusted profit		**53.2**	64.4
Fixed rate interest rate swaps – mark-to-market		**—**	(0.5)
Discount unwind on public sector subsidiary partnership payment	26	**1.7**	1.8
Fair value movement in trade investments		**—**	0.6
Non-designated foreign exchange forward contracts – mark-to-market		**5.1**	(3.4)
Interest payable – business exit[2]	4	**—**	0.1
Fair value hedge ineffectiveness[3]	26	**(3.9)**	(0.6)
Private placement loan notes prepayments costs[4]		**15.9**	—
Net finance costs excluded from adjusted profit		**18.8**	(2.0)
Total net finance costs		**72.0**	62.4

1 Private placement loan notes include US private placement loan notes, euro fixed rate bearer notes and a Schuldschein loan. Included in private placement loan notes interest is £7.0m of additional coupon interest at a rate of 0.75% per annum. Refer to note 23 for further details.
2 Interest payable included within business exit trading. Refer to note 4 for further details.
3 Fair value hedge ineffectiveness includes the costs of the early termination of fair value hedges related to the early repayment of private placement loan notes, ineffectiveness from changes in currency basis, and the movement in mark-to-market valuations on hedge derivatives from the perceived change in the credit worthiness of the counterparties to those instruments.
4 Private placement loan notes prepayment costs includes make-whole costs paid to noteholders on early repayment of principal. The early repayment was made from the proceeds of the rights issue and disposals and further detail is provided in note 23.

Notes to the consolidated financial statements continued

10 Income tax

The major components of income tax expense for the years ended 31 December 2018 and 2017 are set out below.

The income tax credit of £0.9m on reported profit resulted in a tax rate of (0.3%) (2017: income tax credit of £14.0m and tax rate (2.7)%). The reported tax rate will generally vary from the adjusted tax rate year-on-year due to the items excluded from adjusted profit in a period, for example non-taxable profits/losses on disposals or non-deductible impairment of certain acquired intangible assets.

The income tax charge of £27.4m on adjusted profit resulted in an adjusted tax rate of 9.7% (2017: income tax charge of £65.8m and adjusted tax rate 17.2%). This is a reduction year on year as a result of deferred tax credits arising from certain subsidiaries adopting IFRS 15 later and true-ups to filed tax returns, together with an unremitted earnings charge, as detailed further below. It is expected that the adjusted tax rate will return to a level closer to the UK corporation tax rate of 19% in 2019.

Consolidated income statement	2018 £m	2017 £m
Current income tax		
Current income tax charge/(credit)	**11.1**	(35.3)
Adjustment in respect of prior years	**(7.0)**	(10.7)
Deferred income tax		
Origination and reversal of temporary differences	**5.6**	58.1
Adjustment in respect of prior years	**(10.6)**	1.9
	(0.9)	14.0

Consolidated statement of comprehensive income	2018 £m	2017 £m
Income tax on cash flow hedges	**(0.1)**	0.4
Deferred income tax movement in relation to actuarial losses on defined benefit plans	**22.9**	(8.8)
	22.8	(8.4)

Consolidated statement of changes in equity	2018 £m	2017 £m
Deferred income tax movement in relation to share based payment	**(0.4)**	—
	(0.4)	—

The reconciliation between tax expense/(credit) and the product of accounting profit multiplied by the UK corporation tax rate for the years ended 31 December 2018 and 2017 is as follows:

	Footnote	2018 £m	2017 £m
Profit/(loss) before tax		**272.6**	(513.1)
Notional debit/(credit) at UK corporation tax rate of 19.00% (2017: 19.25%)		**51.8**	(98.8)
Adjustments in respect of current income tax of prior years	a	**(7.0)**	(10.7)
Adjustments in respect of deferred tax of prior years	b	**(10.6)**	1.9
Non-deductible expenses – adjusted	c	**5.3**	4.2
Non-deductible expenses – business exit	c	**4.2**	2.9
Non-deductible expenses – specific items	c	**(1.0)**	5.6
(Profit)/loss on disposal	d	**(35.4)**	6.0
Difference in rate recognition of temporary differences		**(4.6)**	(9.9)
Non-deductible intangible impairment	e	**11.0**	102.0
Tax provided on unremitted earnings		**12.8**	—
Attributable to different rates in overseas jurisdictions		**(0.1)**	(3.9)
Movement in unrecognised deferred tax	f	**(27.3)**	14.7
At the effective tax rate of (0.3)% (2017: (2.7%))		**(0.9)**	14.0
Total tax (credit)/expense reported in the income statement		**(0.9)**	14.0

a. The £7.0m prior year credit adjustment includes; (i) a £10.5m credit relating to a reduction in the Group's uncertain tax positions (see below), (ii) a £10.6m debit relating to adjustments which have a corresponding prior-year deferred income tax impact, and (iii) a £7.1m credit relating to true-ups to filed tax returns (2017: the £10.7m prior year adjustment credit includes; (i) a £5.5m credit relating to increased losses available for group relief surrenders arising from acquisitions and disposals in previous years but identified during the period, and (ii) a £5.2m credit relating to adjustments which have a corresponding prior year deferred income tax impact and true ups of positions to filed tax returns).
b. Credits (2017: debits) which have a corresponding prior year current income tax impact and true ups of temporary differences.
c. Adjusted: higher in 2018 mainly due to non-qualifying depreciation. Business exit: relates to costs associated with disposal of businesses detailed in note 4. Specific items: relates to contingent consideration movements (2017: litigation and claims) detailed in note 3.
d. Relates to the application of the UK tax exemption on substantial shareholdings to relevant disposals.
e. Relates to the intangible asset impairments as detailed further in notes 3, 4 and 14.
f. Relates to the decrease (2017: increase) in unrecognised deferred tax on losses. The 2017 consolidated financial statements were prepared under IFRS 15, however the deferred tax positions were calculated on the basis of when subsidiaries would adopt IFRS 15 for statutory financial statements purposes. Subsequent to the finalisation of the 2017 consolidated financial statements, certain subsidiaries adopted IFRS 15 later resulting in a different loss utilisation profile and associated deferred tax asset recognition position.

10 Income tax continued

Deferred income tax

Deferred income tax as at 31 December relates to the following:

	Consolidated balance sheet		Consolidated income statement	
	2018 £m	2017 £m	**2018 £m**	2017 £m
Deferred tax liabilities				
Contract fulfilment assets	**(21.0)**	(41.1)	**(20.1)**	(3.2)
Unremitted earnings	**(12.8)**	—	**12.8**	—
Fair value adjustments on acquisition	**(14.8)**	(39.7)	**(25.0)**	(26.2)
	(48.6)	(80.8)	**(32.3)**	(29.4)
Deferred tax assets				
Accelerated capital allowances	**34.9**	34.9	**—**	(15.6)
Deferred income	**4.7**	63.1	**58.6**	165.4
Share based payments	**1.1**	0.4	**(0.3)**	(0.1)
Pension schemes' liability	**28.1**	55.8	**7.7**	(0.5)
Provisions	**8.6**	13.2	**1.3**	(2.2)
Losses available for offset against future taxable income	**100.6**	60.5	**(40.0)**	(57.6)
	178.0	227.9	**27.3**	89.4
Net deferred tax asset	**129.4**	147.1		
Deferred income tax (credit)/expense			**(5.0)**	60.0

The UK corporation tax rate remained at 19% in 2018 and will decrease further to 17% from 1 April 2020. The deferred tax balances have been adjusted to reflect this change.

Deferred tax has been recognised based on the timing of entity adoption of IFRS 15, interaction of the new loss relief rules, and to the extent that the Group has sufficient future taxable profits against which to offset the temporary differences when they unwind. The recognition for 2018 has been based on the base-case financial forecasts mentioned in the viability statement section of the strategic report. These forecasts provide evidence of sufficient future taxable profits to enable the utilisation of the recognised deferred tax assets.

The Group has unrecognised tax losses of £206.0m (2017: £348.1m) and other temporary differences of £31.0m (2017: £34.5m) that are available for offset against future taxable profits of the companies in which the losses or other temporary differences arose, but have not been recognised as their recoverability is uncertain. These unrecognised tax losses and other temporary differences totalling £237.0m (2017: £382.6m) are made up as follows:

- £161.0m (2017: £344.1m) relates to the UK and has no time expiry. These losses will be subject to recently enacted UK tax loss relief legislation which could result in restricted utilisation in the future.
- £76.0m (2017: £38.5m) relates to various overseas jurisdictions, some of which are being subject to specific loss restriction rules but have no time expiry.
- £85.9m (2017: £101.0m) of the unrecognised tax losses were incurred by companies acquired by the Group and therefore not as a result of the Group's trading performance.

Dividends received from subsidiaries on or after 1 July 2009 are largely exempt from UK tax but may be subject to dividend withholding taxes levied by the overseas tax jurisdictions in which the subsidiaries operate. The gross temporary differences of those subsidiaries affected by such potential taxes is £64.2m (2017: £47.0m). A deferred income tax liability of £12.8m (2017: £nil) has been recognised on the unremitted earnings of those subsidiaries affected by such potential taxes as the Group is able to control the timing of reversal and it is anticipating dividends to be distributed.

Uncertain tax positions

The Group files income tax returns in many jurisdictions. Various tax authorities are currently examining the Group's income tax returns. Tax returns contain matters that could be subject to differing interpretations of applicable tax laws and regulations and the resolution of tax positions, through negotiations with relevant tax authorities or through litigation, can take several years to complete. Tax uncertainties are assessed throughout the year and specifically at the year-end with any associated provisions recognised considering the specific circumstances of each risk, including the merits of technical aspects, previous experience with tax authorities, recent tax law and if relevant, external specialist advice.

In the current period the Group has released £10.5m of provisions in respect of uncertain tax positions relating to overseas tax risks which are no longer considered likely to arise. The release is reflected within the current income tax prior year adjustment.

While it is difficult to predict the ultimate outcome in some cases, the Group does not currently anticipate that there will be any material impact on the Group's financial position or results of operations in the next financial year.

Capita's approach to taxation

Capita has an open and positive working relationship with HMRC, has a designated customer relationship manager, and is committed to prompt disclosure and transparency in all dealings with HMRC and overseas tax authorities. The Group does not have a complex tax structure, nor does it pursue aggressive tax avoidance activities. The Group has a low-risk rating from HMRC. The Group has operations in a number of countries outside the UK. All Capita operations in non-UK jurisdictions are trading operations and pay the appropriate local taxes on these activities. Further detail, regarding the tax strategy, can be found on the Policies and Principles area of the Capita website (capita.com/about-us/policies-and-principles).

Notes to the consolidated financial statements continued

11 Earnings/(loss) per share

Basic earnings/(loss) per share amounts are calculated by dividing net profit for the period attributable to ordinary equity holders of the parent company by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings/(loss) per share amounts are calculated by dividing the net profit for the period attributable to ordinary equity holders of the parent company by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

The weighted average number of ordinary shares for the year ended 31 December 2017 has been restated to reflect the rights issue completed in the period (see note 27). The adjustment to the weighted average number of ordinary shares reflects the bonus element of the rights issue.

The following reflects the earnings and share data used in the basic and diluted earnings/(loss) per share computations:

			Restated		As previously reported	
	2018		2017		2017	
	Continuing operations £m	**Total operations £m**	Continuing operations £m	Total operations £m	Continuing operations £m	Total operations £m
Adjusted profit attributable to shareholders[1]	**239.7**	**239.7**	305.9	305.9	303.6	303.6
Total profit/(loss) attributable to shareholders	**263.4**	**269.0**	(533.5)	(117.1)	(533.5)	(117.1)

1 The adjusted profit attributable to shareholders from continuing operations for the year ended 31 December 2017, previously reported has been restated to reflect change in presentation during the year as well as the businesses that have been disposed of during the year ended 31 December 2018 (see notes 3 and 4).

		Restated	As previously reported
	2018 m	2017 m	2017 m
Weighted average number of ordinary shares (excluding trust and treasury shares) for basic earnings per share	**1,463.9**	1,092.8	665.7
Dilutive potential ordinary shares:			
Employee share options	**18.3**	—	—
Weighted average number of ordinary shares (excluding trust and treasury shares) adjusted for the effect of dilution	**1,482.2**	1,092.8	665.7

At 31 December 2017, 3,395,030 options were excluded from the diluted weighted average number of ordinary shares calculation because their effect would have been anti-dilutive. Under IAS 33-Earnings per Share, potential ordinary shares are treated as dilutive when, and only when, their conversion to ordinary shares would decrease earnings per share or increase loss per share from continuing operations. The Group made a loss in the prior year from continuing operations hence the diluted earnings/(loss) per share for each component of continuing and total operations needs to be the same amount as the basic earnings/(loss) per share.

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of completion of these financial statements.

The earnings per share figures are calculated based on adjusted earnings attributable to ordinary equity holders of the parent company of £239.7m (2017: £305.9m) and reported earnings of £269.0m (2017: loss of £117.1m). They are both included to provide a better understanding of the trading performance of the Group.

				Restated		As previously reported	
		2018		2017		2017	
		Continuing operations p	**Total operations p**	Continuing operations p	Total operations p	Continuing operations p	Total operations p
Basic earnings/(loss) per share	– adjusted	**16.37**	**16.37**	27.99	27.99	45.61	45.61
	– reported	**17.99**	**18.37**	(48.82)	(10.72)	(80.14)	(17.59)
Diluted earnings/(loss) per share	– adjusted	**16.17**	**16.17**	27.99	27.99	45.61	45.61
	– reported	**17.77**	**18.15**	(48.82)	(10.72)	(80.14)	(17.59)

12 Dividends paid and proposed

	2018 £m	2017 £m
Declared and paid during the year		
Ordinary shares (equity):		
Final for 2017 paid: nil per share (2016: 21.2p per share)	**—**	137.1
Interim for 2018 paid: nil per share (2017: 11.1p per share)	**—**	73.9
Dividends paid to shareholders	**—**	211.0
Dividends paid to non-controlling interest	**12.2**	5.6
Total dividends paid	**12.2**	216.6
Proposed for approval at AGM (not recognised as a liability at 31 December)		
Ordinary shares (equity):		
Final for 2018: nil per share (2017: nil per share)	**—**	—

13 Property, plant and equipment

	Leasehold improvements, land and buildings £m	Plant and machinery £m	Total £m
Cost			
As at 1 January 2017	105.0	420.3	525.3
Subsidiaries acquired	0.1	0.1	0.2
Disposal of business	(15.8)	(98.2)	(114.0)
Additions	5.8	63.1	68.9
Disposals – included in adjusted profit	(3.6)	(10.7)	(14.3)
Disposals – excluded from adjusted profit	(7.3)	(91.9)	(99.2)
Asset retirements	(7.6)	(75.2)	(82.8)
Re-class to intangible assets (net)	—	(13.1)	(13.1)
Exchange movement	0.5	0.6	1.1
As at 31 December 2017	77.1	195.0	272.1
Disposal of business	**—**	**(22.8)**	**(22.8)**
Additions	**33.1**	**56.3**	**89.4**
Disposals – included in adjusted profit	**(0.6)**	**(19.7)**	**(20.3)**
Asset retirements	**(5.9)**	**(33.1)**	**(39.0)**
Exchange movement	**(0.7)**	**—**	**(0.7)**
As at 31 December 2018	**103.0**	**175.7**	**278.7**
Depreciation and impairment:			
As at 1 January 2017	38.8	91.8	130.6
Depreciation charged during the year	11.1	58.9	70.0
Impairment – excluded from adjusted profit	—	10.0	10.0
Disposal of business	(6.9)	(32.9)	(39.8)
Disposals – included in adjusted profit	(1.4)	(7.0)	(8.4)
Disposals – excluded from adjusted profit	(1.5)	(17.8)	(19.3)
Asset retirements	(7.6)	(75.2)	(82.8)
Re-class to intangible assets	—	(8.0)	(8.0)
Exchange movement	0.2	0.3	0.5
As at 31 December 2017	32.7	20.1	52.8
Depreciation charged during the year	**9.7**	**50.4**	**60.1**
Impairment – included in adjusted profit	**6.1**	**—**	**6.1**
Disposal of business	**—**	**(2.9)**	**(2.9)**
Disposals – included in adjusted profit	**(0.6)**	**(10.8)**	**(11.4)**
Asset retirements	**(5.9)**	**(33.1)**	**(39.0)**
Exchange movement	**(0.2)**	**(0.4)**	**(0.6)**
As at 31 December 2018	**41.8**	**23.3**	**65.1**
Net book value			
As at 1 January 2017	66.2	328.5	394.7
As at 31 December 2017	44.4	174.9	219.3
As at 31 December 2018	**61.2**	**152.4**	**213.6**

The net book value of plant and machinery includes an amount of £nil (2017: £0.2m) in respect of assets held under finance leases.

Depreciation charged during the year includes £nil (2017: £0.2m) of accelerated depreciation in relation to businesses disposed of.

In 2017 a comprehensive review was undertaken as part of the year-end close process and a number of assets relating to specific programmes resulting from changes in client and Capita strategy in the second half of 2017 were fully written down. Property, plant and equipment amounting to £89.9m was fully written down and excluded from the adjusted profit for the year. The charge is shown above within impairment – excluded from adjusted profit (£10.0m) and disposals – excluded from adjusted profit (£79.9m, being cost £99.2m less accumulated depreciation £19.3m). The write-downs relate to life and pensions assets (£54.7m) and other non-current assets (£35.2m) as detailed in note 3.

Notes to the consolidated financial statements continued

13 Property, plant and equipment continued

The table below reconciles the 2017 disposals and impairments of non-current assets between notes 3, 14 and 17.

	Property, plant and equipment £m	Intangible assets £m	Notes	Contract fulfilment assets £m	Notes	Total £m	Notes
Life and pension assets							
Impairment	—	—		5.5		5.5	
Disposals – cost	56.2	1.0		—		57.2	
Disposals – accumulated depreciation/amortisation	(1.5)	—		—		(1.5)	
	54.7	1.0		5.5		61.2	3
Other non-current assets							
Impairment	10.0	4.0		—		14.0	
Disposals – cost	43.0	39.3		—		82.3	
Disposals – accumulated depreciation/amortisation	(17.8)	(15.0)		—		(32.8)	
	35.2	28.3		—		63.5	3
Total							
Total impairment	10.0	4.0	14	5.5	17	19.5	
Total disposals – cost	99.2	40.3	14	—		139.5	
Total disposals – accumulated depreciation/amortisation	(19.3)	(15.0)	14	—		(34.3)	
	89.9	29.3		5.5		124.7	

14 Intangible assets

	Intangible assets acquired in business combinations						Intangible assets capitalised/purchased			
	Brands £m	IP, software and licences £m	Contracts and committed sales £m	Client lists and relationships £m	Goodwill £m	Total acquired in business combinations £m	Capitalised software development £m	Other intangibles £m	Total capitalised/ purchased £m	Total £m
Cost										
As at 1 January 2017	69.3	96.5	75.3	742.7	2,327.6	3,311.4	197.0	57.9	254.9	3,566.3
Subsidiaries acquired	0.4	6.8	1.3	3.9	15.1	27.5	—	—	—	27.5
Business disposal	(3.0)	(0.4)	—	(50.3)	(266.9)	(320.6)	(17.2)	(0.7)	(17.9)	(338.5)
Additions	—	—	—	—	—	—	43.4	29.5	72.9	72.9
Disposals – included in adjusted profit	—	—	—	—	—	—	(2.7)	(17.5)	(20.2)	(20.2)
Disposals – excluded from adjusted profit	—	—	—	—	—	—	(31.0)	(9.3)	(40.3)	(40.3)
Transfer to assets held for sale	(0.2)	—	—	(3.7)	(7.1)	(11.0)	—	—	—	(11.0)
Re-class from property, plant and equipment	—	—	—	—	—	—	13.1	—	13.1	13.1
Asset retirement	(9.7)	(3.4)	(6.1)	(201.9)	—	(221.1)	(46.6)	(1.9)	(48.5)	(269.6)
Fair value adjustments in 2017 relating to 2016 acquisitions	—	—	—	—	1.2	1.2	—	—	—	1.2
Exchange movement	(0.3)	0.7	—	(2.6)	1.3	(0.9)	0.4	0.1	0.5	(0.4)
As at 31 December 2017	56.5	100.2	70.5	488.1	2,071.2	2,786.5	156.4	58.1	214.5	3,001.0
Subsidiaries acquired	**—**	**—**	**—**	**2.7**	**—**	**2.7**	**—**	**—**	**—**	**2.7**
Business disposal	**(3.5)**	**(6.7)**	**—**	**(38.5)**	**(50.9)**	**(99.6)**	**—**	**(7.3)**	**(7.3)**	**(106.9)**
Additions	**—**	**—**	**—**	**—**	**—**	**—**	**64.8**	**5.3**	**70.1**	**70.1**
Disposals – included in adjusted profit	**—**	**—**	**—**	**—**	**—**	**—**	**(5.0)**	**(0.1)**	**(5.1)**	**(5.1)**
Asset retirement	**(5.7)**	**—**	**(9.2)**	**(108.4)**	**—**	**(123.3)**	**(16.6)**	**(2.2)**	**(18.8)**	**(142.1)**
Exchange movement	**0.1**	**0.2**	**(0.1)**	**6.3**	**0.3**	**6.8**	**0.5**	**0.1**	**0.6**	**7.4**
As at 31 December 2018	**47.4**	**93.7**	**61.2**	**350.2**	**2,020.6**	**2,573.1**	**200.1**	**53.9**	**254.0**	**2,827.1**
Amortisation and impairment										
As at 1 January 2017	28.6	36.7	35.9	468.6	152.0	721.8	73.9	16.4	90.3	812.1
Amortisation charged during the year	11.4	12.8	9.0	92.0	—	125.2	16.6	6.6	23.2	148.4
Impairment – excluded from adjusted profit	0.7	—	4.0	9.3	551.6	565.6	4.0	—	4.0	569.6
Impairment - business exit	—	—	—	—	7.1	7.1	—	—	—	7.1
Business disposal	(2.6)	(0.3)	—	(45.2)	(0.2)	(48.3)	(7.1)	(0.1)	(7.2)	(55.5)
Disposals – included in adjusted profit	—	—	—	—	—	—	(0.8)	(6.7)	(7.5)	(7.5)
Disposals – excluded from adjusted profit	—	—	—	—	—	—	(13.5)	(1.5)	(15.0)	(15.0)
Asset retirement	(9.7)	(3.4)	(6.1)	(201.9)	—	(221.1)	(46.6)	(1.9)	(48.5)	(269.6)
Transfer to assets held for sale	(0.1)	—	—	(2.3)	(7.1)	(9.5)	—	—	—	(9.5)
Re-class from property, plant and equipment	—	—	—	—	—	—	8.0	—	8.0	8.0
Exchange movement	(0.3)	0.1	—	0.8	(0.1)	0.5	0.1	0.2	0.3	0.8
As at 31 December 2017	28.0	45.9	42.8	321.3	703.3	1,141.3	34.6	13.0	47.6	1,188.9
Amortisation charged during the year	**9.7**	**13.3**	**6.1**	**57.6**	**—**	**86.7**	**21.1**	**6.8**	**27.9**	**114.6**
Impairment – excluded from adjusted profit	**—**	**—**	**—**	**61.7**	**33.8**	**95.5**	**—**	**—**	**—**	**95.5**
Impairment – business exit	**—**	**—**	**—**	**—**	**24.3**	**24.3**	**—**	**—**	**—**	**24.3**
Business disposal	**(2.4)**	**(4.7)**	**—**	**(34.2)**	**—**	**(41.3)**	**—**	**(3.9)**	**(3.9)**	**(45.2)**
Disposals – included in adjusted profit	**—**	**—**	**—**	**—**	**—**	**—**	**(0.6)**	**(0.1)**	**(0.7)**	**(0.7)**
Asset retirement	**(5.7)**	**—**	**(9.2)**	**(108.4)**	**—**	**(123.3)**	**(16.6)**	**(2.2)**	**(18.8)**	**(142.1)**
Exchange movement	**0.3**	**0.5**	**(0.1)**	**3.3**	**0.2**	**4.2**	**—**	**(0.1)**	**(0.1)**	**4.1**
As at 31 December 2018	**29.9**	**55.0**	**39.6**	**301.3**	**761.6**	**1,187.4**	**38.5**	**13.5**	**52.0**	**1,239.4**
Net book value										
As at 1 January 2017	40.7	59.8	39.4	274.1	2,175.6	2,589.6	123.1	41.5	164.6	2,754.2
As at 31 December 2017	28.5	54.3	27.7	166.8	1,367.9	1,645.2	121.8	45.1	166.9	1,812.1
As at 31 December 2018	**17.5**	**38.7**	**21.6**	**48.9**	**1,259.0**	**1,385.7**	**161.6**	**40.4**	**202.0**	**1,587.7**

Amortisation charged during the year includes £nil (2017: £1.7m (£0.3m in acquired intangibles and £1.4m in capitalised/purchased intangibles)) of accelerated amortisation in relation to businesses disposed or held for sale.

Goodwill impairments: The Group recognised an impairment charge relating to goodwill of £33.8m (2017: £551.6m). Refer to note 15.

Intangible assets acquired in business combination impairments: Customer Management saw a weaker performance in Europe, which was impacted by lower profits in Switzerland. The Group recognised an impairment charge relating to intangible assets acquired in business combinations of £61.7m in relation to the Swiss business in Customer Management. The recoverable amount of the intangible asset is £12.2m, based on its value in use and a pre-tax discount rate of 11.9%. (2017: In 2017, £14.0m of intangibles acquired in business combinations in relation to the Insurance, Life and Pensions businesses in Specialist Services were identified as impaired).

Notes to the consolidated financial statements continued

14 Intangible assets continued

Intangible assets capitalised impairment and disposals: As part of its year-end close process, Capita undertook a review of its tangible and intangible assets, resulting in £nil (2017: £29.3m resulting from changes in client and Capita strategy) impairments. The 2017 charge is shown in the table within 'impairment – excluded from adjusted profit' (£4.0m) and 'disposals – excluded from adjusted profit' (£25.3m, being cost £40.3m less accumulated depreciation £15.0m). This impairment charge relates to life and pension assets (£1.0m) and other non-current assets (£28.3m). The table in note 13 reconciles the disposals and impairments of non-current assets between notes 3, 13, 14 and 17.

15 Goodwill

Goodwill acquired through business combinations has been allocated to Cash-Generating Units (CGUs), for impairment testing purposes, on the basis of the expected benefit that will accrue to the individual CGU through synergies realised from the acquisitions and integration with the Group as a whole. These represent the lowest level within the Group at which goodwill can be allocated on a reasonable and consistent basis.

The enterprise value of each CGU is dependent on the successful implementation of the transformation plan described earlier in the strategic report. The objective of the new strategy announced in April 2018 is to become a more focused and predicable business with improved returns, stronger client relationships and sustainable free cash flow. The Group has put in place a new organisational structure, which comprises six divisions: Software, People Solutions, Customer Management, Government Services, IT & Networks, and Specialist Services. Following this re-organisation, the Group has reviewed the historical assessment of CGUs and the allocation of goodwill. Reflecting the way management now exercises oversight and monitors the Group's performance, the Board concluded that the lowest level at which goodwill is monitored is at the divisional level for three divisions, and at a sub-divisional level for the other three divisions, and goodwill has been reallocated to these new CGUs or groups of CGUs. As at 31 December 2018, the Group has 9 CGUs or groups of CGUs for the purpose of impairment testing of goodwill. The opening goodwill balance has been reallocated for comparable purposes. As the transformation plan progresses, the Board will continue to assess the level at which management exercise oversight and monitors the Group's performance to ensure the allocation of goodwill to CGUs remains appropriate.

Carrying amount of goodwill allocated to groups of Cash-Generating Units

The following table shows the allocation of goodwill to groups of CGUs.

				Government Services		IT & Networks			
CGU	Software £m	People Solutions £m	Customer Management £m	Central Government £m	Local Government £m	IT Services £m	Network Services £m	Specialist Services £m	Total £m
1 January 2018	275.6	203.5	138.6	8.7	33.8	117.7	108.5	481.5	1,367.9
Additions	—	—	—	—	—	—	—	—	—
Fair value adjustment	—	—	—	—	—	—	—	—	—
Disposals and business exits	—	—	—	—	—	—	—	(75.2)	(75.2)
Exchange movement	—	—	0.1	—	—	—	—	—	0.1
Impairment	—	—	—	—	(33.8)	—	—	—	(33.8)
31 December 2018	**275.6**	**203.5**	**138.7**	**8.7**	**—**	**117.7**	**108.5**	**406.3**	**1,259.0**

Specialist Regulated Services is not included in the table above as goodwill and acquired intangibles were fully impaired in 2017, and therefore an impairment test is not required.

The impairment test

The Group tests intangible assets, including goodwill, for impairment on an annual basis or more frequently if there are indications that any of these assets may be impaired.

The Group's impairment test compares the carrying value of each CGU with its recoverable amount. The recoverable amount of a CGU is the higher of fair value less cost of disposal and value in use. As the Group continues to implement the Group-wide transformation plan it has been determined that for 2018, fair value less costs of disposal will generate the higher recoverable amount. Fair value less costs of disposal have been estimated using discounted cash flows. The fair value measurement was categorised as a Level 3 fair value based on the inputs in the valuation technique used.

In undertaking the annual impairment review, the Directors have considered both external and internal sources of information, and any observable indications that may suggest that the carrying value of goodwill may be impaired.

As set out in 'divisional performance' in the strategic report, the local government market for large BPO contracts is declining with a significant drop-off in the number and size of opportunities coming to market and existing clients choosing to end contracts early and take services back in house. This decline is being driven by fiscal pressures, the expectation that this will provide a more flexible cost and delivery model, but also by an ideological shift away from outsourcing by some council leaderships. The local government BPO market, which we anticipated reducing, declined at an accelerated rate during the year. Southampton, Sheffield and Birmingham City Councils have notified us of their intention to end contracts with us ahead of their contracted-end dates. Barnet Council has agreed to take a small number of services back in House. Capita is committed to the local government market and is working closely with all our Council partners to agree and manage a smooth transfer of services back to council management. The deterioration in the market opportunities and continued challenges were monitored throughout the year and crystallised in the final quarter of 2018 leading to the recognition of the impairment charges as set out in this note.

15 Goodwill continued

The key inputs to the calculations are described below, including changes in market conditions.

Forecast cash flows

In the first half of 2018, the Board approved a five-year strategic plan covering the period from 2018 to 2022. As the five-year strategic plan was approved prior to the finalisation of the Annual Report and Accounts 2017, it was used to derive cash flow forecasts for the purposes of the impairment test for the year ended 31 December 2017.

The bottom-up business planning process completed at the end of 2018, reviewed years two and three (2019 and 2020) of the strategic plan in detail. The resulting business plan for 2019 and 2020 was approved by the Board. For the 2018 impairment test, the 2019 and 2020 business plan was used to derive the cash flow forecasts for the purpose of the impairment test. The cash flows are adjusted to exclude working capital movements as the corresponding balances are not included in the carrying amount. The cash flows also include forecast capital expenditure and restructuring, as well as an allocation the costs of central functions. The Board considered an appropriate methodology to apply in allocating the costs of the central functions, which is a key sensitivity. The forecast 2021 EBITDA measures have been used as these represent a steady state forecast for the Group and an appropriate approximation of the attention and focus of the central functions. As the transformation plan delivers, the Board will assess any changes required to ensure the allocation methodology continues to reflect the efforts of the central functions.

The forecasts are cash flow projections for 2021 and 2022, represent management's assessment of future trends in relevant industries and have been based on data from both external and internal sources.

The long-term growth rate is based on inflation forecasts by recognised bodies and this has been applied to both 2023 and the terminal period. The 2018 long-term growth rate is 1.5% (2017: 1.5%).

Discount rates

Management estimates discount rates using pre-tax rates that reflect the latest market assumptions for the risk-free rate, the equity risk premium and the net cost of debt, which are all based on publicly available external sources.

The table below represents the pre-tax discount rates used on the cash flows. The 2017 rates have not been reported, due to the CGU restructure and the adoption of fair value less costs of disposal.

Division	Pre-tax discount rate %
Software	12.7
People Solutions	12.1
Customer Management	11.9
Central Government	11.4
Local Government	16.8
IT Services	11.1
Network Services	11.1
Specialist Regulated Services	11.5
Specialist Services	11.8

Sensitivity analysis

The impairment testing as described is reliant on the accuracy of management's forecasts and the assumptions that underlie them and also on the selection of the discount and growth rates to be applied. In order to gauge the sensitivity of the result to a change in any one, or combination of the assumptions that underlie the model, a number of scenarios have been run to identify the range of reasonably possible alternatives and measure which CGUs are the most susceptible to an impairment should the assumptions used be varied. This sensitivity analysis is only applicable to the CGUs that have goodwill.

The table below shows how the enterprise value would be impacted (with all other variables being equal) by an increase in discount rate of 1%, or if the business plan was missed by 10% for each of the five years or a decrease of 1% in the long-term growth rate for the Group in total and each of the CGUs. We have also considered the impact of all of the scenarios together and disclosed the impact on impairment in the final column.

	1% increase in discount rate	Miss targets by 10%	Long-term growth rate decrease by 1%	Combination sensitivity	Increase in 2018 impairment using combination scenario
Software	(66.1)	(73.3)	(48.5)	(168.7)	—
People Solutions	(77.5)	(78.4)	(56.2)	(189.4)	—
Customer Management	(43.8)	(31.6)	(34.2)	(96.0)	—
Central Government	(60.4)	(48.2)	(47.5)	(137.0)	—
IT Services	(19.5)	(17.7)	(13.9)	(47.5)	(5.0)
Network Services	(19.7)	(20.0)	(14.4)	(49.4)	—
Specialist Services	(88.1)	(96.4)	(63.6)	(222.2)	—
Total	**(375.1)**	**(365.6)**	**(278.3)**	**(910.2)**	**(5.0)**

Management continue to monitor closely the performance of all CGUs and consider the impact of any changes to the key assumptions. In conclusion, other than the local government impairment in the year, management believe there is no reasonably possible change in the underlying assumptions that would result in a further significant impairment charge in the consolidated income statement.

Notes to the consolidated financial statements continued

16 Business combinations

2018 acquisitions

In October 2018, the Group acquired three operational contact centres as part of extending and expanding an existing customer management contract with Europe's largest integrated telecommunications provider. The consideration was £3 and the acquisition accounting resulted in an intangible asset of £2.7m being recognised.

During the year, the Group settled £11.1m of deferred consideration and £10.4m of contingent consideration payments with regard to previous acquisitions, all of which had been accrued.

The fair value exercise has been completed on a provisional basis for acquisitions made in 2018. The Group will complete this review in 2019, though an adjustment to the carrying value is likely to be insignificant to the acquisition. In the current year, there were no revisions made to fair value adjustments that had been determined provisionally at the immediately preceding balance sheet date.

Contingent consideration

In respect of 2018 acquisitions, there is no contingent consideration. For all historic acquisitions, the range of the additional consideration payment is estimated to be between £nil and £24.7m. Contingent consideration has been calculated based on the Group's expectation of what it will pay in relation to the post-acquisition performance of the acquired entities by weighting the probability of a range of payments to give an estimate of the final obligation.

2017 acquisitions

The Group made a number of acquisitions in 2017 which are shown in aggregate. The fair values of the identifiable assets and liabilities acquired are disclosed in the table below:

	Fair value to Group recognised on acquisition £m
Property, plant and equipment	**0.2**
Intangible assets	**12.4**
Trade and other receivables due in less than one year	**7.5**
Corporation tax	**(0.3)**
Cash and cash equivalents	**4.5**
Trade and other payables (excluding accruals) due in less than one year	**(2.9)**
Accruals due in less than one year	**(2.6)**
Deferred tax	**(2.2)**
Net assets	**16.6**
Goodwill arising on acquisition	**15.1**
	31.7
Discharged by:	
Cash	**23.3**
Deferred consideration	**2.0**
Contingent consideration accrued	**6.4**
	31.7

In all cases, 100% of the ordinary share capital was acquired. The companies acquired have been mainly in the areas of IT & Networks, Travel and Events, Customer Management and Software which complement or extend the Group's existing skill sets and provide opportunities for growth into these markets. In addition, during the year the Group settled £10.8m of deferred consideration and £11.7m of contingent consideration payments with regard to previous acquisitions, all of which had been accrued.

Where this can be determined, the acquired subsidiaries contributed £1.8m to the profit before tax of the Group. If these acquisitions had occurred on 1 January 2017, Group's revenue would have been an estimated £4,237.7m and Group loss before tax would have been an estimated £512.8m. In determining these amounts, management has assumed that the fair value adjustments that arose on the date of acquisition would have been the same if the acquisition had occurred on 1 January 2017. During the year, some of the acquired businesses have been completely integrated into the existing business of the Group and therefore their post-acquisition performance cannot be determined.

Goodwill has arisen on the acquisitions because the fair value of the acquired assets was lower than the consideration paid; the goodwill represents the value to the Group that can be driven from these underlying assets over the life of the acquired businesses, particularly from synergies, and the capabilities of the acquired workforce. The total amount of goodwill recognised in the period that is expected to be deductible for tax purposes is £nil (2016: £nil).

The fair value exercise was completed on a provisional basis for acquisitions made in 2017. In total, the effect of revisions made to fair value adjustments in 2017 that had been determined provisionally at the immediately preceding balance sheet date increased goodwill by £1.2m.

Contingent consideration

In respect of the acquisitions made in 2017, the Group has agreed to pay the vendors additional consideration dependent on the achievement of performance targets in the periods post acquisition. These performance periods are of up to 3 years in duration and will be settled in cash on their payment date on achieving the relevant targets. The Group has included £6.4m as contingent consideration related to the additional consideration, which represents its fair value at the acquisition date. For all historic acquisitions, the range of the additional consideration payment is estimated to be between £nil and £24.7m. Contingent consideration has been calculated based on the Group's expectation of what it will pay in relation to the post-acquisition performance of the acquired entities by weighting the probability of a range of payments to give an estimate of the final obligation.

17 Contract fulfilment assets

	Total £m
At 1 January 2017	240.6
Additions	101.2
Impairment	(14.1)
Derecognition	(9.9)
Utilised during the year	(65.3)
At 31 December 2017	252.5
Additions	**113.8**
Transfers from current contract fulfilment assets	**25.4**
Impairment	**(22.2)**
Derecognition	**(17.4)**
Utilised during the year	**(87.9)**
At 31 December 2018	**264.2**

Impairment

In preparing these consolidated financial statements, management undertook a review to identify indicators of impairment of contract fulfilment assets. Management determined whether or not the contract fulfilment assets and capitalised costs to obtain a contract were impaired by comparing the carrying amount of the asset to the remaining amount of consideration that the Group expects to receive less the costs that relate to providing services under the relevant contract. In determining the estimated amount of consideration, the Group uses the same principles as it does to determine the contract transaction price, except that any constraints used to reduce the transaction price will be removed for the impairment test.

In line with the Group's accounting policy, as set out in note 2, if a contract exhibited marginal profitability or other indicators of impairment, judgement was applied to ascertain whether or not the future economic benefits from these contracts were sufficient to recover these assets. In performing this impairment assessment, management is required to make an assessment of the costs to complete the contract. The ability to accurately forecast such costs involves estimates around cost savings to be achieved over time, anticipated profitability of the contract, as well as future performance against any contract-specific KPIs that could trigger variable consideration or service credits.

Following this review, contract fulfilment asset provisions for impairment of £22.2m (2017: £14.1m) were identified relating to assets capitalised in the year and recognised within adjusted cost of sales.

Derecognition

A contract fulfilment asset is derecognised either when it is disposed of or when no further economic benefits are expected to flow from its use or disposal. In 2018, £17.4m (2017: £9.9m) of contract fulfilment assets were derecognised as the related contracts, Prudential and Marsh, were terminated in the year and the Group had no further use for the assets. Of the assets derecognised in the prior year, £5.5m was included as an adjustment to operating profit and related to the write-off of the carrying value of a platform developed by the Group's life and pension business. The Group's transformation plan identified that there was no longer a market for this platform.

Notes to the consolidated financial statements continued

18 Financial assets

Current financial assets	2018 £m	2017 £m
Deferred consideration[1]	—	3.0
Insurance asset recoverable[2]	1.3	5.0
Held for trading assets[3]	—	0.4
Cash flow hedges	5.0	4.0
Currency swaps in relation to USD denominated loan notes[4]	9.3	72.2
Non-designated foreign exchange forwards and swaps	2.1	4.1
Interest rate swaps in relation to GBP denominated loan notes[5]	0.5	—
	18.2	88.7

Non-current financial assets	2018 £m	2017 £m
Deferred consideration[1]	—	2.2
Investments	6.1	—
Held for trading assets[3]	2.7	4.2
Cash flow hedges	3.3	3.8
Currency swaps in relation to USD denominated loan notes[4]	93.8	113.1
Non-designated foreign exchange forwards and swaps	1.8	3.6
Interest rate swaps in relation to GBP denominated loan notes[5]	1.4	5.4
	109.1	132.3

1 The deferred consideration relates to the sale of the Health business which was classified as held for sale in 2015, and sold in 2016. The amount has been fully recovered.
2 The insurance asset recoverable relates to amounts where the Group has virtual certainty of receiving a contribution in respect of a litigation or insurance claim.
3 Held for trading assets comprise investments in unlisted ordinary shares and fund assets. The unlisted ordinary shares, for which there is no immediately identifiable market and have no fixed maturity date or coupon rate, are carried at cost less impairment. The fund assets, for which there are market values, are recorded at fair value as at 31 December 2018.
4 The cross-currency swaps hedge the Group's exposure to foreign exchange movements and interest rate movements on the Group's USD denominated private placement loan notes. The changes in the fair value of the underlying private placement loan notes arising from movements in interest and foreign exchange rates are offset by the changes in the fair value of the cross-currency swaps recognised above.
5 The interest rate swaps hedge changes in the fair value of the Group's GBP denominated fixed rate private placement loan notes. The change in the fair value of the underlying loan notes arising from changes in interest rates is equivalent to the fair value of the interest rate swaps recognised above. Details of the interest rate swaps, cross-currency swaps and cash flow hedges are provided in note 26.

19 Trade and other receivables

Current	2018 £m	2017 £m
Trade receivables	435.6	379.5
Other receivables	29.4	26.9
Contract fulfilment assets	11.1	39.4
Accrued income	182.9	207.7
Prepayments	112.7	122.3
	771.7	775.8

Non-current	2018 £m	2017 £m
Other receivables	2.3	0.6
Prepayments	23.9	27.4
	26.2	28.0

Trade receivables are non-interest bearing and are generally on 30-day terms.

Consistent with prior years, the Group made use of non-recourse trade receivable financing arrangements provided to it by a number of its relationship banks. There was a net balance of £nil sold on these arrangements as at 31 December 2018 (2017: £110.0m) as the Group phased-out the use of non-recourse trade receivables financing. As these trade receivables have been sold without recourse, the Group has derecognised them in the above table.

At 31 December 2018, we raised a provision of £11.2m (2017: £8.3m) in relation to a loss allowance made against receivables.

19 Trade and other receivables continued

Movements in the loss allowance made against receivables were as follows:

	2018 £m	2017 £m
At 1 January	**8.3**	11.5
Utilised	**(1.4)**	(1.5)
Provided in the year	**9.5**	6.9
Released in the year	**(2.5)**	(8.3)
Business disposal/closure	**(2.7)**	(1.4)
Provisions acquired	**—**	1.1
At 31 December	**11.2**	8.3

At 31 December, the analysis of trade receivables that were past due but not impaired was as follows:

			Past due but not impaired			
	Total £m	Neither past due nor impaired £m	0–3 months £m	4–6 months £m	7–12 months £m	More than 12 months £m
2018	**435.6**	**326.1**	**103.6**	**5.9**	**—**	**—**
2017	379.5	252.1	121.5	5.9	—	—

The Group monitors the level of trade receivables on a monthly basis, continually assessing the risk of default by any counterparty.

Current contract fulfilment assets are costs directly related to a contract or to a specifically identifiable anticipated contract which will be used in satisfying performance obligations in the next 12 months from the balance sheet date.

The Group's accrued income balances solely relate to revenue from contracts with customers. Movements in the accrued income balances were driven by transactions entered into by the Group within the normal course of business in the year, other than £5.1m impairment arising on a contract in Government Services (2017: £nil).

20 Cash, cash equivalents and overdrafts

	2018 £m	2017 £m
Cash at bank and in hand	**957.5**	921.7
Overdrafts	**(314.8)**	(443.3)
	642.7	478.4

Cash at bank earns interest at floating rates based on daily bank deposit rates. The fair value of cash is the same as the carrying amount above. Included in cash at bank and in hand is £nil (2017: £14.0m) held in a 45-day notice of withdrawal money market fund.

Included in Overdrafts are balances totalling £280.3m (2017: £387.7m) held in the Group's notional cash pools under which the bank has the right of offset against Cash at bank – see note 26.

21 Trade and other payables

Current	2018 £m	2017 £m
Trade payables	**214.3**	274.9
Other payables	**10.7**	36.5
Other taxes and social security	**131.2**	150.8
Accruals	**312.5**	293.0
	668.7	755.2

Non-current	2018 £m	2017 £m
Other payables	**1.6**	0.1
Accruals	**10.0**	16.9
	11.6	17.0

Trade payables are non-interest bearing and are settled within terms agreed with suppliers.

Notes to the consolidated financial statements continued

22 Deferred income

Current	2018 £m	2017 £m
Current	**980.3**	1,201.2
	980.3	1,201.2

Non-current	2018 £m	2017 £m
Non-current	**277.3**	314.0
	277.3	314.0

The Group's deferred income balances solely relate to revenue from contracts with customers. Revenue recognised in the reporting period that was included in the deferred income balance at the beginning of the period was £1,220.8m (2017: £1,381.0m). Movements in the deferred income balances were driven by transactions entered into by the Group within the normal course of business in the year, other than the accelerated revenue recognised of £10.0m and £38.4m relating to the ending of our general insurance contract with Marsh and our life and pensions contract with the Prudential respectively (2017: £22.0m from the re-shaping of the DIO contract).

23 Financial liabilities

Current	Notes	2018 £m	2017 £m
Contingent consideration		**—**	12.1
Deferred consideration		**1.3**	11.1
Public sector subsidiary partnership payment		**9.4**	9.4
Put option of non-controlling interests		**107.3**	6.8
Obligations under finance leases	24	**—**	0.2
Other loan notes		**0.3**	—
Term loan		**100.0**	—
Cash flow hedges		**1.2**	1.6
Non-designated foreign exchange forward contracts		**1.4**	0.3
Private placement loan notes[1]		**82.2**	224.1
		303.1	265.6
Non-current			
Contingent consideration		**8.9**	12.5
Deferred consideration		**0.7**	2.0
Public sector subsidiary partnership payment		**34.1**	41.8
Put options of non-controlling interests		**11.2**	115.6
Private placement loan notes[1]		**1,025.8**	1,439.9
Other loan notes		**—**	0.3
Term loan		**—**	100.0
Cash flow hedges		**—**	1.1
Currency swaps in relation to USD denominated loan notes		**3.5**	8.5
		1,084.2	1,721.7

1 Private placement loan notes include US private placement loan notes, euro fixed rate bearer notes and a Schuldschein loan.

Included in financial liabilities is an amount of £1,108.0m (2017: £1,664.0m) which represents the carrying value of the Group's private placement loan notes which should be considered in conjunction with the carrying value of currency and interest rate swaps of:

- £105.0m (2017: £190.7m) included in financial assets; and
- £3.5m (2017: £8.5m) included in financial liabilities.

This gives an effective liability of £1,006.5m (2017: £1,481.8m).

In connection with the Group's transformation strategy and rights issue which were announced on 23 April 2018, Capita agreed amendments to its US private placement loan notes including:

- the introduction of an allowable minimum basket of £50m of both subsidiary indebtedness and permitted liens, in line with the corresponding baskets under Capita's other financing arrangements;
- the carve-out of up to £100m worth of bonds and guarantees from the financial covenant definition of indebtedness;
- certain restructuring costs to be excluded from the calculation of the covenant test, and certain assets to be excluded from the restrictions on disposals;
- the flexibility to increase the leverage covenant under the terms of the private placement notes from 3.0x to 3.5x if Capita would otherwise breach the covenant as a result of first-year losses from significant new contract wins as a result of the adoption of IFRS 15;

23 Financial liabilities continued

- a requirement to offer to prepay as follows until a total of £520m (the 'Prepayment Target') has been repaid (when combined with any repayments of US private placement loan notes, with original maturity dates of July and September 2018 on the scheduled maturity date):
  - the US private placement loan notes with scheduled maturity dates in July and September 2018, plus a make-whole payment;
  - from the proceeds of the rights issue, £150m of principal of the other US private placement loan notes, plus a make-whole payment;
  - from 50% of the net proceeds arising from non-core asset disposals, a pro-rata prepayment of principal across remaining US private placement notes, plus a make-whole payment; and.
- a temporary restriction on the prepayment of certain financial indebtedness and reductions in facility amounts, and a coupon premium of 0.75% until the Fall Away Criteria[1] have been met.

In connection with a waiver allowing consent for the disposal of Parking Eye, in November 2018, Capita agreed amendments to its euro fixed rate bearer notes and Schuldschein loan agreement including:

- a waiver of the limitation on disposals to allow the disposal of Parking Eye;
- a temporary restriction of the prepayment of certain financial indebtedness and reductions in facility amounts;
- a coupon premium of 0.75% until the Fall Away Criteria have been met; and
- an offer to prepay principal from the net proceeds of the Parking Eye disposal, equivalent pro-rata to the prepayment element of the Prepayment Target offered to the noteholders to the US private placement loan notes.

1 The 'Fall Away Criteria' include a one-time test of leverage being less than 1.5x at the 31 December 2018, 30 June 2019 and 31 December 2019 testing periods on a look-forward basis, and the achievement of the Prepayment Target.

The repayments and prepayments made pursuant to the above mentioned agreements with its lenders are set out in the below table.

Event	Date of payment/prepayment	US private placement loan notes	Euro fixed rate bearer notes & Schuldschein loan
		£m equivalent at date of offer to prepay	£m equivalent at date of offer to prepay
Rights issue	June 2018	150.0	—
Loan notes that matured in 2018	June, July and September 2018	222.0	—
Disposal of Supplier Assessment Services	August 2018	70.2	—
Disposal of Parking Eye	November 2018	77.8	48.2
Total payment/prepayment		**520.0**	**48.2**

On 19 November 2018 the Prepayment Target was formally agreed as having been achieved with the noteholders to the US private placement notes. The leverage ratio at 31 December 2018 is 1.2x. The Company reasonably expects the leverage ratio to be less than 1.5x at 30 June 2019 and 31 December 2019. As a consequence, the Company expects to make formal statements to the noteholders of the US private placements loan notes on 14 March 2019 stating the same, at which point the Fall Away Criteria will be met. At this point the temporary conditions referred to above including the 0.75% coupon premium will cease to apply.

The Group incurred financing arrangement fees on the amendments to the US private placement loans during the year amounting to £3.7m which has been included in the carrying value of the private placement loan notes (new issue and amendment fees: 2017: £2.1m). In addition the Group incurred £13.3m of associated prepayment costs and £2.5m of other financing costs which have been included in adjusting finance costs (2017: £nil). Issue and amendment costs are spread over the term of the loan notes. The unamortised balance of issue and amendment costs at the year-end totalled £3.7m (2017: £3.4m).

The Group's bank term loan is a £100m five-year term loan maturing in May 2019 which bears interest at floating rates linked to Libor.

The obligations under finance leases are secured on the assets being financed. The term loan, US private placement loan notes, euro fixed rate bearer notes, and Schuldschein loan are all unsecured.

The public sector subsidiary partnership payment liability is an estimate of the annual preferred payments to be made by AXELOS Limited (the partnership formed with the Cabinet Office) to the Cabinet Office in 2019 to 2023. The payments are funded by AXELOS Limited and are individually contingent on the profits of that business. After the contractual obligations to make these payments have been met or have expired, the shareholders will be entitled to share in the retained profits pro rata to their equity interest in AXELOS Limited.

The third-party non-controlling shareholders of AXELOS Limited and Fera Science Limited hold options to sell their shareholdings to a member of the Group. Accordingly, a liability of £118.5m (2017: £122.4m) has been recognised and a corresponding entry has been recorded against retained earnings. The option held by the non-controlling shareholder in AXELOS became exercisable on 1 January 2019 and as a result is included as a current liability notwithstanding the fact that the Company is not in receipt of any notice of intention to exercise the option.

The option held by the non-controlling shareholder in Fera Science Limited is not expected to become exercisable within a year. As a result the associated liability is recorded as non-current.

During the year, Capita Business Services Limited paid £6.8m in return for an amendment to the terms of the joint venture shareholders' agreement previously entered into with the non-controlling shareholder in Entrust Support Services Limited. The variation agreement cancelled the option previously held by the non-controlling shareholder to sell its shares in Entrust Support Services Limited to Capita Business Services Limited under certain circumstances. As at 31 December 2017 a current liability of £6.8m was recorded in respect of this option.

The Group has available to it a committed Revolving Credit Facility of £600m of which £81m matures in August 2020 and £519m matures in August 2021. The facility is available for the Group's immediate use and £nil was drawn down at 31 December 2018 (2017: £nil).

The covenant terms in respect of the above liabilities are discussed in note 2. Borrowing costs of £nil were capitalised in the year (2017: £nil).

Notes to the consolidated financial statements continued

23 Financial liabilities continued

At 31 December 2018, the Group's US private placement loan notes, euro fixed rate bearer notes, and the Schuldschein loan were as follows:

Private placement loan notes	Interest rate %	Denomination	Face Value (m)	Maturity
Issued 2010				
Series C	4.78	GBP	37.1	30 June 2020
Issued 2011[1]				
Series A	4.85	GBP	37.1	22 July 2019
Series C	4.76	GBP	26.0	19 July 2021
Issued 2013				
Series A	3.73	GBP	55.7	30 September 2020
Issued 2015				
Series C	3.26	GBP	18.6	22 January 2022
Series F	3.54	GBP	7.4	22 January 2025
Series G	3.67	GBP	22.3	22 April 2025
Series I	3.58	GBP	23.8	22 January 2027
Issued 2016				
Series B	2.18	GBP	36.0	27 October 2021
Series D	2.52	GBP	27.5	27 October 2023
Series F	2.77	GBP	18.6	27 October 2026
Total GBP denominated loan notes		GBP	310.1	
Issued 2010[2]				
Series B	4.80	USD	185.7	30 June 2020
Issued 2011[2]				
Series B	4.65	USD	59.4	22 July 2019
Series B	4.50	USD	175.3	19 July 2021
Series A	4.75	USD	37.1	26 July 2021
Issued 2015[2]				
Series A	3.33	USD	29.7	22 January 2022
Series B	3.43	USD	48.3	22 April 2022
Series D	3.45	USD	39.4	22 January 2023
Series E	3.65	USD	74.3	22 January 2025
Series H	3.80	USD	27.5	22 January 2027
Issued 2016[2]				
Series A	3.03	USD	18.6	27 October 2021
Series C	3.37	USD	17.8	27 October 2023
Series E	3.59	USD	19.3	27 October 2026
Total USD denominated loan notes		USD	732.4	
Issued 2015				
Fixed rate bearer notes	2.125	EUR	179.0	10 November 2022
Fixed rate bearer notes	2.875	EUR	60.0	10 November 2027
Schuldschein loan	2.125	EUR	16.0	10 November 2022
Total euro denominated fixed rate bearer notes and Schuldschein loan		EUR	255.0	

1 The Group has entered into interest rate swaps to convert the interest cost to floating rates based on 6-month GBP LIBOR.
2 The Group has entered into currency swaps for the USD issues to achieve a floating rate of interest based on 6-month GBP LIBOR. Further disclosure on the Group's use of hedges is included in note 26.

24 Obligations under leases and hire purchase contracts

The Group uses finance leases and hire purchase contracts to acquire plant and machinery. These leases have terms of renewal and purchase options but no escalation clauses. Renewals are at the option of the lessee.

The value of future minimum lease payments is analysed as follows:

	2018 £m	2017 £m
Not later than 1 year	**0.0**	0.2

The Group has entered into commercial leases on properties, motor vehicles and items of plant and machinery. These leases have an average duration of between 3 and 10 years.

Future minimum rentals payable under non-cancellable operating leases are as follows:

	2018 £m	2017 £m
Not later than 1 year	**99.2**	119.2
Later than 1 year but not later than 5 years	**245.3**	285.8
Later than 5 years	**391.5**	428.0
	736.0	833.0

25 Provisions

	Restructuring provision £m	Business exit provision £m	Asset services indemnity provision £m	Claim and litigation provision £m	Property provision £m	Other £m	Total £m
As at 1 January 2018	10.6	37.0	69.1	64.3	22.5	9.1	212.6
Provisions provided for in the year	**41.9**	**22.7**	**—**	**6.4**	**2.3**	**12.7**	**86.0**
Provisions released in the year	**(5.0)**	**(1.7)**	**(4.6)**	**(7.9)**	**(1.8)**	**(1.7)**	**(22.7)**
Utilisation	**(35.5)**	**(40.9)**	**(61.5)**	**(16.4)**	**(3.5)**	**(3.9)**	**(161.7)**
Provisions acquired	**—**	**—**	**—**	**—**	**0.6**	**1.5**	**2.1**
Disposal of subsidiaries	**—**	**—**	**—**	**—**	**(0.1)**	**—**	**(0.1)**
Reclassification between categories	**—**	**0.4**	**—**	**—**	**(0.1)**	**(0.3)**	**—**
As at 31 December 2018	**12.0**	**17.5**	**3.0**	**46.4**	**19.9**	**17.4**	**116.2**

The provisions made above have been shown as current or non-current on the balance sheet to indicate the Group's expected timing of the matters reaching conclusion.

Judgement is required in measuring and recognising provisions related to pending litigation or other outstanding claims subject to negotiated settlement, mediation and arbitration, as well as other contingent liabilities. Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the financial settlement. Because of the inherent uncertainty in this evaluation process, actual losses may be different from the originally estimated provision. Where practicable, the range of reasonably possible outcomes and sensitivities of the carrying amounts to the methodology, assumptions and estimates, the reason for the sensitivity, the expected resolution of uncertainties and the range of reasonable possible alternatives, are provided below. Where no reliable basis of estimation can be made, no provision is recorded. However, contingent liabilities disclosures are given when there is a greater than a remote probability of outflow of economic benefits.

Restructuring provision: The provision represents the cost of reducing role count where there is a constructive obligation created through communication to affected employees which has crystallised a valid expectation that roles are at risk. Additionally, it reflects the onerous nature of property lease provisions (net of any sub-letting opportunity) on a discounted basis, where due to the reduced requirement for space there is additional surplus capacity. During the year, additional provision has been made for costs as further restructuring opportunities related to the transformation plan have been identified.

Business exit provision: The provision relates to the cost of exiting businesses through disposal or closure including professional fees related to business exits and the costs of separating the businesses being disposed.

Capita Asset Services indemnity provision: In 2017 the Group agreed a full and final settlement with the Financial Conduct Authority (FCA) regarding the Connaught Income Series 1 Fund (the Fund). Capita Financial Managers Limited (CFM) was the Operator of the Fund until September 2009, when it was replaced by an unrelated company as Operator, following which CFM had no further involvement with the Fund. The Fund went into liquidation in 2012 and its liquidator brought a claim against both former Operators, which for its part, Capita settled in 2016 for a sum of £18.5m.

The FCA undertook a formal review of the activities of both Operators and announced that its conclusion was that CFM did not meet all of its regulatory requirements in the period April 2008 to September 2009. To ensure that investors receive appropriate redress and to bring this matter to a close enabling the smooth disposal of CFM, CFM and Capita agreed a full and final settlement with the FCA. In reaching this settlement, the full cooperation which CFM gave to the FCA during the course of its investigation was acknowledged.

CFM agreed to a further £66.0m being made available for the benefit of the Fund's investors, with Capita agreeing to fund this amount. The FCA considered that this payment was sufficient to return the amount originally invested, taking into account any interest, distributions and other payments that had already been received, with the intention of placing investors as closely as possible back into the position they would have been in if they had never invested in the Fund.

This settlement allowed for the available funds to be directed towards the Fund's Investors. Given the circumstances, the FCA did not consider that it would be appropriate to require CFM to pay a financial penalty.

Notes to the consolidated financial statements continued

25 Provisions continued

Capita made provision for the redress payment and associated legal costs of £66.8m as at 31 December 2017. CFM and the FCA subsequently reached agreement, on the basis of third-party calculations of the liability due, such that the final amount of the redress payment will not exceed £61.5m, and accordingly £4.6m of the provision has been released. The final quantum of the redress payments is expected to be determined in the first half of 2019.

Capita completed the disposal of its Asset Services businesses, including CFM, to the Link Group on 3 November 2017. Capita plc, as part of the sale of the Capita Asset Services businesses, has provided an indemnity against certain legacy claims. The provisions held, namely the Asset Services settlement provision which includes provisions for Arch Cru, Connaught and other legacy claims, have therefore been retained within the Group. Giving due consideration to these claims, the Group provided £69.1m (including the £66.8m above) as at 31 December 2017. A provision of £3.0m remains as at 31 December 2018 and is expected to unwind within the next 12 months.

Claims and litigation provision: In addition to the Capita Asset Services Indemnity provision, the Group is exposed to other claims and litigation. The Group makes a provision when a claim has been made where it is more probable than not that a loss might occur. These provisions are reassessed regularly to ensure that the level of provisioning is consistent with the claims that have been reported. The range of values attached to these claims, can be significant and, where obligations are probable and estimable, provisions are made representing the Group's best estimate of the expenditure to be incurred. The Group robustly defends its position on each claim and they are often settled for amounts significantly smaller than the initial claim and may result in no transfer of economic benefits. Therefore, we do not disclose a range of possible outcomes for these claims.

In the period, the Group has settled a number of liabilities which it had provided for in previous years. Additionally, it has provisions, which originate due to the nature of the Group's activities and revised existing provisions where more information on the progress of the claim has become apparent. In addition, £5.5m provision was released from a provision made in 2017 relating to the Group's Real Estate & Infrastructure business.

The Group's exposure to claims is mitigated by having in place a number of large insurers providing cover for the Group's activities, albeit insurance recoveries are only recognised as an asset at the point the recovery is virtually certain. At the 31 December 2017, an asset had been recognised of £5.0m in respect of recoveries under an indemnity, no other recovery assets had been recognised. No recovery assets have been recognised as at 31 December 2018.

Due to the nature of these claims, the Group cannot give an estimate of the period over which this provision will unwind.

Property provision: Includes a provision of £10.7m (2017: £12.8m), made on a discounted basis, for the difference between the market value of property leases acquired in 2011 with the Ventura and Vertex Private Sector acquisitions and the lease obligations committed to at the date the leases were signed by the previous owners. This is in accordance with IFRS 3 (revised) which requires the use of fair value measurement.

The remaining property provision of £9.2m (2017: £9.7m) is made on a discounted basis for the future rent expense and related cost of leasehold property (net of estimated sub-lease income) where the space is vacant or currently not planned to be used for ongoing operations. The expectation is that this expenditure will be incurred over the remaining periods of the leases which range from 1 to 24 years.

Other provisions: Relates to provisions in respect of other potential exposures arising due to the nature of some of the operations that the Group provides, the most significant of which are in respect of immaterial onerous contracts. These are likely to unwind over a period of 1 to 10 years.

26 Financial instruments

Financial risk management objectives and policies

The Group's principal financial instruments comprise cash, bank loans, private placement loan notes, finance leases and derivatives, the purpose of which is to provide liquidity for the Group's operations and to manage its financial risks. The Group has various other financial instruments including trade receivables and trade payables arising from its operations.

The derivatives comprise interest rate swaps, cross-currency swaps, and forward currency contracts held with its relationship banks, all of which have investment grade credit ratings. The derivatives' purpose is to manage interest rate and currency risks arising from the Group's operations and its sources of finance. It is the Group's policy that no speculative trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The Board periodically reviews and agrees policies for managing each of these risks and they are summarised below.

Carrying values and fair values of financial instruments

The following table analyses by classification and category the carrying value of the Group's financial instruments (excluding short-term debtors, creditors, payables/receivables and cash in hand).

The carrying values are a reasonable approximation to the fair value of financial instruments with the exception of the 12 private placement loan notes that remain subject to fixed rate interest. The fair value has been calculated by discounting the expected future cash flows at prevailing foreign exchange spot and forward rate, and interest rate curves. The valuation models use foreign exchange spot and forward rates and interest rate curves. These have a carrying value of £473.3m and a fair value of £459.6m.

The fair value of cash and cash equivalents including receivables and payables approximates to the carrying amount because of the short maturity of these instruments.

The fair value of floating rate borrowings approximates to the carrying value because interest rates are at floating rates where payments are reset to market values at intervals of less than one year. The private placement loan notes that have been hedged to floating rates of interest have a carrying value of £634.7m and a fair value of £634.7m.

26 Financial instruments continued

The fair value of cross-currency and interest swaps is determined using discounted cash flow techniques based on readily available market data. The fair value of the cross-currency and interest rate swaps are provided in note 18 – Financial assets, and note 23 – Financial liabilities.

As at 31 December 2018	At fair value through the P&L £m	Amortised cost £m	Derivatives used for hedging £m	At fair value through OCI £m	Total £m
Financial assets					
Cash	—	957.5	—	—	957.5
Insurance asset recoverable	—	1.3	—	—	1.3
Cash flow hedges	—	—	8.3	—	8.3
Non-designated foreign exchange forwards and swaps	3.9	—	—	—	3.9
Interest rate swaps in relation to GBP denominated loan notes	—	—	1.9	—	1.9
Currency swaps in relation to USD denominated loan notes	—	—	103.1	—	103.1
Investments	—	—	—	6.1	6.1
Held for trading assets	—	—	—	2.7	2.7
	3.9	958.8	113.3	8.8	1,084.8

	At fair value through equity £m	At fair value through the P&L £m	Derivatives used for hedging £m	Other financial liabilities £m	Total £m
Financial liabilities					
Overdrafts	—	—	—	314.8	314.8
Private placement loan notes	—	—	—	1,108.0	1,108.0
Other loan notes	—	—	—	0.3	0.3
Term loan	—	—	—	100.0	100.0
Cash flow hedges	—	—	1.2	—	1.2
Non-designated foreign exchange forwards and swaps	—	1.4	—	—	1.4
Currency swaps in relation to USD denominated loan notes	—	—	3.5	—	3.5
Contingent consideration	—	8.9	—	—	8.9
Deferred consideration	—	—	—	2.0	2.0
Public sector subsidiary partnership payment	—	—	—	43.5	43.5
Put options of non-controlling interests	118.5	—	—	—	118.5
	118.5	10.3	4.7	1,568.6	1,702.1

The aggregate loan note value above of £1,108.0m includes the GBP carrying value of the USD denominated loan notes at 31 December 2018. To mitigate exposure to currency fluctuations the Group has entered into currency swaps which effectively hedge movements in the loan notes' fair value arising from changes in foreign exchange and interest rates. Interest rate swaps hedge exposure to changes in the fair value of GBP denominated loan notes. The fair values of the currency and interest swaps are provided in note 18 – Financial assets and note 23 – Financial liabilities.

Notes to the consolidated financial statements continued

26 Financial instruments continued

At 31 December 2017	At fair value through the P&L £m	Loans and receivables £m	Derivatives used for hedging £m	Available for sale £m	Total £m
Financial assets					
Cash	—	921.7	—	—	921.7
Available-for-sale assets[1]	—	—	—	4.6	4.6
Deferred consideration[1]	—	5.2	—	—	5.2
Insurance asset recoverable[1]	—	5.0	—	—	5.0
Cash flow hedges	—	—	7.8	—	7.8
Non-designated foreign exchange forwards and swaps	7.7	—	—	—	7.7
Interest rate swaps in relation to GBP denominated loan notes	—	—	5.4	—	5.4
Currency swaps in relation to USD denominated loan notes	—	—	185.3	—	185.3
	7.7	931.9	198.5	4.6	1,142.7

	At fair value through the P&L £m	Derivatives used for hedging £m	Other financial liabilities £m	Total £m
Financial liabilities				
Overdraft	—	—	443.3	443.3
Private placement loan notes	—	—	1,664.0	1,664.0
Other loan notes	—	—	0.3	0.3
Term loan	—	—	100.0	100.0
Cash flow hedges	—	2.7	—	2.7
Non-designated foreign exchange forwards and swaps	0.3	—	—	0.3
Currency swaps in relation to USD denominated loan notes	—	8.5	—	8.5
Contingent consideration	—	—	24.6	24.6
Deferred consideration	—	—	13.1	13.1
Obligations under finance leases	—	—	0.2	0.2
Public sector subsidiary partnership payment	—	—	51.2	51.2
Put options of non-controlling interests	—	—	122.4	122.4
	0.3	11.2	2,419.1	2,430.6

1 Classification has changed in 2018 following the adoption of IFRS 9.

The fair value of financial instruments has been calculated by discounting the expected future cash flows at prevailing interest rates, except for held for trading assets (which are unlisted equity securities) and investment loans. The valuation models incorporate various inputs including foreign exchange spot and forward rates and interest rate curves. Unlisted equity securities and investment loans are held at amortised cost. The Group enters into derivative financial instruments with multiple counterparties, all of which are financial institutions with investment grade credit ratings.

Fair value hierarchy

The following tables show the fair value measurement of financial instruments by level of the fair value hierarchy:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

26 Financial instruments continued

At 31 December 2018

	Level 2 fair value £m	Level 3 fair value £m
Financial assets		
Cash flow hedges	**8.3**	—
Non-designated foreign exchange forwards and swaps	**3.9**	—
Held for trading assets	—	**2.7**
Investments	—	**6.1**
Interest rate swaps in relation to GBP denominated loan notes	**1.9**	—
Currency swaps in relation to USD denominated loan notes	**103.1**	—
Total financial assets	**117.2**	**8.8**
Financial liabilities		
Private placement loan notes	**634.7**	—
Cash flow hedges	**1.2**	—
Currency swaps in relation to USD denominated loan notes	**3.5**	—
Contingent consideration	—	**8.9**
Non-designated foreign exchange forwards and swaps	**1.4**	—
Put options of non-controlling interests	—	**118.5**
Public sector subsidiary partnership payment	—	**43.5**
Total financial liabilities	**640.8**	**170.9**

At 31 December 2017

	Level 2 fair value £m	Level 3 fair value £m
Financial assets		
Cash flow hedges	7.8	—
Available-for-sale assets	—	4.6
Non-designated foreign exchange forwards and swaps	7.7	—
Interest rate swaps in relation to GBP denominated loan notes	5.4	—
Currency swaps in relation to USD denominated loan notes	185.3	—
Total financial assets	206.2	4.6
Financial liabilities		
Private placement loan notes	1,059.6	—
Cash flow hedges	2.7	—
Currency swaps in relation to USD denominated loan notes	8.5	—
Contingent consideration	—	24.6
Non-designated foreign exchange forwards and swaps	0.3	—
Public sector subsidiary partnership payment	—	51.2
Put options of non-controlling interests	—	122.4
Total financial liabilities	1,071.1	198.2

During the year ended 31 December 2018, there were no transfers between Level 1 and Level 2 fair value measurements and no transfers into or out of Level 3 fair value measurements.

The floating rate private placement loan notes which have a carrying value of £634.7m and a fair value of £634.7m include the GBP equivalent of the US Dollar denominated loan notes at 31 December 2018.

The fair value of cross-currency and interest swaps is determined using discounted cash flow techniques based on readily available market data.

Contingent consideration arises in business acquisitions where the Group has agreed to pay the vendors additional consideration dependent on the achievement of performance targets in the post-acquisition periods. These performance periods are up to 3 years in duration and will be settled in cash and loan notes if the relevant targets are achieved. The Group provides for such contingent consideration for each acquisition based on an assessment of fair value at the acquisition date. The contingent consideration has been calculated using a probability-weighted range of outturns.

A sensitivity analysis has been performed on the expected contingent consideration of £8.9m. The analysis adjusts the probability of payment of the contingent amounts. A 10% increase in the probability of contingent consideration being paid results in an increase in potential contingent consideration of £1.2m. A 10% decrease in the probability of the contingent consideration being paid results in a decrease in potential contingent consideration of £0.7m.

Notes to the consolidated financial statements continued

26 Financial instruments continued

The public sector subsidiary partnership payment liability is an estimate of the aggregate of annual payments to the Cabinet Office in the years 2019 to 2023 to be made by AXELOS Limited (the partnership formed with the Cabinet Office). This payment is funded by AXELOS Limited and the carrying value of £43.5m has been derived by discounting the expected payment at an annualised rate of 2.8% to present value.

The carrying value of the liability is sensitive to movements in the profitability of AXELOS and is subject to a cap. Under all reasonably plausible scenarios the cap has been reached and therefore the sensitivity to changes in both the discount rate and the cash flows that have been used to calculate it is £nil.

The put options of non-controlling interest are in respect of AXELOS and Fera (see note 23). These are measured at fair value which has been calculated based on the expected amounts that will be paid in cash by the Group to purchase the shares of the non-controlling interests at the expected date of exercise of the options, which has then been discounted at a annualised rate of 2.8% to arrive at its present value.

The sensitivity of the valuation of the put option of the non-controlling interest to movements in both the discount rate and the cash flows that have been used to calculate it are as follows: a 10% increase in the earnings potential of the business results in a £11.3m increase in the valuation; a 10% decrease in the earnings potential of the business results in a £11.8m decrease in the valuation; a 1% increase in the discount rate applied to the valuation results in a £0.7m decrease in the valuation; and a 1% decrease in the discount rate applied to the valuation results in a £0.2m increase in the valuation.

The following table shows the reconciliation from the opening balances to the closing balances for Level 3 fair values.

	Contingent consideration £m	Subsidiary partnership payment £m	Put options of non-controlling interests £m	Investments £m	Held for trading assets £m
At 1 January 2018	24.6	51.2	122.4	—	4.6
Profit and loss movement	**(5.3)**	—	—	—	**(1.9)**
Utilised	**(10.4)**	**(9.4)**	—	—	—
Movement of put options recognised in equity	—	—	**2.9**	—	—
Fair value of assets and liabilities acquired	—	—	—	**6.1**	—
Cancellation of put option	—	—	**(6.8)**	—	—
Discount unwind	—	**1.7**	—	—	—
As at 31 December 2018	**8.9**	**43.5**	**118.5**	**6.1**	**2.7**

Risk management framework

The Group's Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework, which is outlined on pages 44–51 of the strategic report.

Interest rate risk

The Group manages its interest rate exposure, which arises from the private placement loan notes, using a mix of fixed and variable rate financial instruments.

The Group's USD denominated private placement loan notes are at fixed rates that have been swapped to floating rate GBP liabilities with cross-currency swaps. These are designated as fair value hedges against the changes in the fair value of the private placement loan notes that arise from changes in foreign currency exchange and interest rates.

The Group's GBP denominated private placement loan notes are at fixed rates. Certain of these notes have been converted to floating rate GBP interest through interest rate swaps. The swaps are designated as fair value hedges against the changes in the fair value of the private placement loan notes that arise from changes in interest rates.

The GBP equivalent of the underlying nominal value of private placement loan notes that remain at fixed rates of interest at 31 December 2018 was £473.3m. The GBP equivalent of the underlying nominal value of private placement loan notes that are exposed to floating rates of interest was £540.5m. Together with the £100m term loan, the total drawn exposure to floating rates of interest at 31 December 2018 was £640.5m.

This level of floating rate interest exposure, when considered with the floating rate interest received on cash and deposits gives the Group an acceptable overall interest rate risk profile.

The interest rate profile of the interest-bearing financial assets and liabilities of the Group at 31 December was as follows:

As at 31 December 2018	**Within 1 year £m**	**Between 1–2 years £m**	**Between 2–3 years £m**	**Between 3–4 years £m**	**Between 4–5 years £m**	**More than 5 years £m**	**Total £m**
Fixed rate							
Private placement loan notes	—	**92.8**	**36.0**	**191.5**	**27.5**	**125.4**	**473.3**
Floating rate							
Cash in hand	**(957.5)**	—	—	—	—	—	**(957.5)**
Overdraft	**314.8**	—	—	—	—	—	**314.8**
Private placement loan notes	**82.2**	**145.9**	**209.5**	**60.1**	**44.2**	**92.9**	**634.8**
Term loan	**100.0**	—	—	—	—	—	**100.0**
Interest rate swap in relation to GBP denominated loan notes	**(0.5)**	—	**(1.4)**	—	—	—	**(1.9)**
Currency swaps in relation to USD denominated loan notes	**(9.3)**	**(21.8)**	**(35.5)**	**(12.2)**	**(5.3)**	**(15.5)**	**(99.6)**

26 Financial instruments continued

As at 31 December 2017	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Fixed rate							
Private placement loan notes	—	—	124.5	48.2	243.9	186.2	602.8
Obligations under finance leases	0.2	—	—	—	—	—	0.2
Floating rate							
Cash in hand	(921.7)	—	—	—	—	—	(921.7)
Overdraft	443.3	—	—	—	—	—	443.3
Private placement loan notes	224.1	112.7	194.7	275.7	78.1	175.9	1,061.2
Term loan	—	100.0	—	—	—	—	100.0
Interest rate swap in relation to GBP denominated loan notes	—	(2.4)	—	(3.0)	—	—	(5.4)
Currency swaps in relation to USD denominated loan notes	(72.2)	(10.1)	(26.3)	(37.8)	(12.5)	(17.9)	(176.8)

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's profit before tax (through the impact on floating rate borrowings). There is no impact on the Group's equity.

	Increase/(decrease) in interest rates		Effect on profit before tax £m	£m
2018	**0.5%**	**(0.5)%**	**(3.2)**	**3.2**
2017	0.5%	(0.5)%	(4.9)	4.9

Foreign currency risk

The Group's exposure to foreign exchange risk arises primarily from cash flows that are not in the native currency of the relevant operation. The Group is not generally exposed to significant foreign currency transaction risk except where it purchases services in non-native currencies in INR and USD. The Group seeks to mitigate the effect of this exposure by entering forward currency contracts (including Non-deliverable Forward Contracts (NDFs)) to fix the GBP cost of highly probable forecast transactions.

To maximise hedge effectiveness the Group executes the forward currency contracts with terms matching the underlying cash flows.

At 31 December 2018, the Group held foreign exchange forwards against forecast monthly INR costs expected in the years up to and including 2020. These forecast costs have been determined on the basis of the underlying cash flows associated with the delivery of services under executed customer contracts.

In addition the Group holds foreign exchange forwards against committed costs relating to the purchase of cloud software services in USD in years up to and including 2023.

The following table demonstrates the sensitivity to a reasonably possible change in INR and USD exchange rates, with all other variables held constant, of the Group's profit before tax and the Group's equity due to changes in the fair value of the Group's forward exchange contracts.

	US Dollars			Indian rupee		
	Increase/ (decrease) in USD exchange rate	Effect on profit before tax £m	Effect on equity £m	Increase/ (decrease) in INR exchange rate	Effect on profit before tax £m	Effect on equity £m
2018	**5.0%**	**(2.2)**	**(1.3)**	**5.0%**	**—**	**0.6**
2017	—	—	—	5.0%	—	0.7

Hedges

Fair value hedges

The Group has in issue fixed rate USD and GBP private placement loan notes which it has hedged through a combination of interest rate and cross-currency swaps.

At 31 December 2018 the Group had interest rate swaps in place with a notional amount of £63.1m (2017: £85.0m) whereby it receives a weighted average fixed rate of interest of 4.81% (2017: fixed rate of interest 4.81%) and pays variable rates based on 6-month GBP Libor. The swaps hedge the exposure to changes in the fair value of £63.1m (2017: £85.0m) of the Group's private placement loan notes.

The Group had in place currency swaps whereby it receives a fixed rate of interest and pays a variable rate based on 6-month GBP Libor. The currency swaps are being used to hedge the exposure to changes in the fair value of £477.4m (2017: £794.8m) of the Group's loan notes, which have coupon rates ranging from 3.03% to 4.85%.

The currency swaps are being used to hedge the exposure to changes in the fair value of its US dollar denominated loan notes. The loan notes, currency and interest rate swaps have the same critical terms including the amount and the date of maturity (see note 23).

The total loss in the year on the fair value hedges of £27.5m (2017: total loss £184.0m), excluding credit risk, was equal to the gain/loss on the hedged items resulting in no net gain or loss in the income statement apart from hedge ineffectiveness from credit risk and currency basis risk totalling £4.7m credit (2017: £0.6m credit) to the income statement – shown in net finance costs – note 9.

The Group may, at its option, upon notice of not less than 30 days and not more than 60 days, make repayments to its USD and GBP private placement loan notes at a contractual rate.

Notes to the consolidated financial statements continued

26 Financial instruments continued

The impact of the hedged item on the statement of financial position as at 31 December 2018 is, as follows:

	Notional Amount £m	Carrying Amount £m	Line item in the statement of financial position	Change in FV used for measuring ineffectiveness £m
Interest rate swap	**63.1**	**1.9**	**Financial assets**	**(3.5)**

	Notional Amount £m	Carrying Amount £m	Line item in the statement of financial position	Change in FV used for measuring ineffectiveness £m
Currency swap – asset	**432.7**	**103.1**	**Financial assets**	**27.3**
Currency swap – liability	**44.7**	**(3.5)**	**Financial liabilities**	**(0.9)**

The impact of the hedged item on the statement of financial position as at 31 December 2018 is, as follows:

	Carrying Amount £m	Accumulated FV adjustment £m	Line item in the statement of financial position	Change in FV used for measuring ineffectiveness £m
Private placement loan notes	**1,108.0**	**101.5**	**Financial Liabilities**	**(27.5)**

Cash flow hedges

As noted above, the Group holds a series of forward exchange currency contracts in the form of NDFs designated as hedges of highly probable forecast transactions in INR of the Group's Indian operations and committed USD costs.

	2018		2017	
Forward exchange contracts	**Assets £m**	**Liabilities £m**	Assets £m	Liabilities £m
Fair value	**8.3**	**(1.2)**	7.8	(2.7)

The terms of the forward currency contracts have been executed to match the terms of the commitments.

The cash flow hedges are in respect of highly probable forecast monthly costs, based on long-term contracts that the Group has in place, denominated in INR and USD up to 2023. These were assessed to be highly effective at 31 December 2018 and a net cumulative unrealised gain of £4.7m (2017: gain of £5.1m) less income tax credit of £3.3m (2017: credit of £3.2m) was recognised in equity. The net gain recognised on cash flow hedges during the year was £2.0m (2017: net gain £2.0m) while net gains of £2.5m (2017: losses of £0.3m) were reclassified to the income statement and included in finance costs. The tax effect of the net movement in cash flow hedges during the year was a credit to OCI of £0.1m (2017: debit of £0.4m).

Credit risk

The Group trades only with recognised, creditworthy third parties. It is the Group's policy that all clients who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant.

An impairment analysis is performed at each reporting date to measure expected credit losses. The transition to IFRS 9 has not resulted in a material change to the Group's level of receivable provisioning.

With respect to credit risk arising from the other financial assets of the Group, such as cash and cash equivalents, held for trading financial investments, investment loan, certain derivative instruments and accrued income, the Group's exposure to credit risk arises from the risk of a default of the counterparty. The Group manages its operations to avoid any excessive concentration of counterparty risk and the Group takes all reasonable steps to seek assurance from the counterparties to ensure that they can fulfil their obligations.

The Group has a maximum exposure equal to the carrying amount of the above receivables and instruments.

The mark-to-market movement on derivatives includes the extent to which the fair value of these instruments has been affected by the perceived change in the creditworthiness of the counterparties to those instruments and that of the Group itself (own credit risk). The Group is comfortable that the risk attached to those counterparties is not significant and believes that the currency swaps continue to act as an effective hedge against the movements in the fair value of the Group's issued USD denominated loan notes.

Liquidity risk

The Group's policy is to hold cash and undrawn committed facilities at a level sufficient to fund the Group's operations and its medium-term plans.

The Group monitors its risk of experiencing a shortage of funds through a daily cash management process. This process considers the maturity of both the Group's financial investments and financial assets (e.g. accounts receivable, other financial assets) and projected cash flows from operations.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use or availability of multiple sources of funding including private placement loan notes, bank loans, term loans, cash, overdrafts and finance leases over a broad spread of maturities to 2027.

26 Financial instruments continued

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2018 based on contractual undiscounted payments.

As at 31 December 2018	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Overdraft	314.8	—	—	—	—	—	314.8
Private placement loan notes	83.8	238.6	243.3	254.9	72.4	221.0	1,114.0
Other loan notes	0.3	—	—	—	—	—	0.3
Interest on above loan notes	45.0	32.6	26.2	14.8	9.2	20.0	147.8
Term loan	100.0	—	—	—	—	—	100.0
Interest on above term loan	0.8	—	—	—	—	—	0.8
Contingent consideration	—	8.9	—	—	—	—	8.9
Public sector subsidiary partnership payment	9.4	9.4	9.4	9.4	9.4	—	47.0
Put options of non-controlling interests	107.3	—	11.2	—	—	—	118.5
Currency swaps	1.3	1.3	1.3	0.9	0.9	1.4	7.1
Non-designated foreign exchange forwards and swaps	0.1	—	—	—	—	—	0.1
Cash flow hedges	1.0	—	—	—	—	—	1.0
	663.8	290.8	291.4	280.0	91.9	242.4	1,860.3

As at 31 December 2017	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Overdraft	443.3	—	—	—	—	—	443.3
Private placement loan notes	219.0	109.2	310.0	313.6	324.9	363.8	1,640.5
Other loan notes	—	—	0.3	—	—	—	0.3
Interest on above loan notes	65.8	52.4	41.6	33.2	18.6	35.5	247.1
Term loan	—	100.0	—	—	—	—	100.0
Interest on above term loan	1.6	0.6	—	—	—	—	2.2
Contingent consideration	12.1	—	12.5	—	—	—	24.6
Public sector subsidiary partnership payment	9.4	9.4	9.4	9.4	9.4	9.4	56.4
Put options of non-controlling interests	6.8	108.8	—	10.5	—	—	126.1
Obligations under finance leases	0.2	—	—	—	—	—	0.2
Currency swaps	1.4	1.4	1.4	1.4	1.0	2.6	9.2
Non-designated foreign exchange forwards and swaps	0.2	—	—	—	—	—	0.2
Cash flow hedges	1.7	—	—	—	—	—	1.7
	761.5	381.8	375.2	368.1	353.9	411.3	2,651.8

The above payments have been calculated based on the prevailing foreign exchange rates and interest rates at the end of the reporting period. For currency swaps, only payments are included, receipts are excluded.

Master netting or similar agreements

The Group has notional cash pools with its banks under which the bank may net cash balances with overdrafts held by other members of the Group. The effect of this is shown in the table below.

As at 31 December 2018	Gross and net amounts of financial instruments in the balance sheet £m	Related financial instruments that are not offset £m	Net amount £m
Financial assets			
Cash at bank	957.5	(280.3)	677.2
Financial liabilities			
Overdrafts	(314.8)	280.3	(34.5)

As at 31 December 2017	Gross and net amounts of financial instruments in the balance sheet £m	Related financial instruments that are not offset £m	Net amount £m
Financial assets			
Cash at bank	921.7	(387.7)	534.0
Financial liabilities			
Overdrafts	(443.3)	387.7	(55.6)

Notes to the consolidated financial statements continued

26 Financial instruments continued

Capital management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit standing, evidenced by healthy capital ratios, to support its ongoing business operations and to maximise shareholder value. The Group manages its capital structure, and makes adjustments to it, in light of changes in economic conditions. The Group's capital management includes consideration of dividend payments or the return of capital to shareholders or issuing new shares. Focus on capital management forms an important component of Board meetings, with attention on various matters including return on capital employed, ensuring a mix of funding sources to ensure continuity and flexibility, a balance between fixed and floating borrowings, a broad spread of maturities and adequate liquidity headroom.

The Group's capital management process ensures that it meets financial covenants in its borrowing arrangements. Breaches in meeting the financial covenants could permit the Group's lenders to immediately accelerate repayment of loans and borrowings. The Group monitors, as part of its monthly Board review, the adherence to specified consolidated leverage ratios and consolidated net interest expense coverage ratios. There have been no breaches in the financial covenants of any loans and borrowings in the period.

On 23 April 2018, the Company provided a transformation update and proposed rights issue. The proceeds of the rights issue are being used to: (i) support the delivery of Capita's new strategy; (ii) continue to make further investments in the business; and (iii) reduce its indebtedness in order to help achieve its target leverage ratio of between 1.0x and 2.0x adjusted net debt to adjusted EBITDA (prior to the adoption of IFRS 16).

The Group uses long-dated debt, generally private placement loan notes and long-term bank facilities, to enable it to manage refinancing risk and for the general purposes of the Group. There are various constraints preventing the Group in using surplus cash to further reduce its debt. These include the need to maintain adequate liquidity for operations over the course of the planning horizon, cash that is restricted under the terms of its regulated businesses, and the temporary prohibition on the early repayment of debt that was agreed with the lenders of the Group's private placement loan notes as set out above. A further consideration is that future prepayments of debt could result in a requirement for a pound-for-pound acceleration of the payments to the pension scheme.

Capita plc supports the growth of its various financial services businesses. These financial firms are subject to various capital requirements imposed by regulators. These requirements do not apply to Capita plc itself and the Group is not required to provide consolidated returns for regulatory purposes. The board of each regulated firm is responsible for ensuring it has embedded capital management frameworks that test there are adequate financial resources at all times. During the year, each complied with all externally imposed financial services regulatory capital requirements.

The Group seeks to maintain a conservative and efficient capital structure with an appropriate level of gearing. At 31 December 2018, our annualised adjusted net debt to adjusted EBITDA ratio was 1.2x (2017: 2.2x) with annualised interest cover at 8.2x (2017: 8.6x). These ratios are monitored monthly by the Board. The Group's transformation plan includes an assessment of the appropriate financial leverage for the Group over the medium term, to ensure that it has a sustainable capital base to support its clients and operations, increase investment in the business and deliver its future strategy. The Board considers that the appropriate financial leverage for Capita over the medium term should be an adjusted net debt to adjusted EBITDA ratio of between 1.0x and 2.0x (prior to the adoption of IFRS 16).

The Group's debt facilities include typical maintenance obligations including covenant tests on indebtedness and restrictions on the level of liens and indebtedness permitted outside a group of guarantor companies. The Board monitors ongoing compliance with the tests. The Group is satisfied that the procedures in place ensure ongoing full compliance with the covenants.

The Group raises debt in a number of markets including the bank loan market, bank overdraft, finance lease and private placement markets. The Group has available to it a committed Revolving Credit Facility of £600m of which £81m matures in August 2020 and £519m matures in August 2021. The facility was undrawn at 31 December 2018 (2017: undrawn), and is available for the Group's immediate use.

The Group has historically made use of short-term non-recourse invoice financing facilities provided to it by relationship banks. £nil invoices had been sold under these arrangements and not been settled at 31 December 2018 (2017: £110.0m).

The Group has now completed the normalisation of working capital management practices, an objective that was first announced on 31 January 2018. The Group does not expect to use such invoice financing in future. Furthermore, the Group will aim to pay suppliers on time in accordance with agreed terms and not seek to accelerate payments for customers beyond terms previously agreed.

Following the rights issue and strategic disposals made during the year, the Group repaid and prepaid a total of £577.2m of the private placement loan notes, fixed rate bearer notes and the Schuldschein loan (see note 23). The maturity of the remaining balances is spread between 2019 and 2027 (see note 23).

Further to the Board's update on Capita's transformation, capital structure, funding and trading outlook provided on 31 January 2018, the dividend has been suspended until the Company is generating sustainable free cash flow.

The table below presents quantitative data for the components the Group manages as capital:

	2018 £m	2017 £m
Cash in hand	**(957.5)**	(921.7)
Overdraft	**314.8**	443.3
Other loan notes	**0.3**	0.3
Obligations under finance leases	**0.0**	0.2
Private placement loan notes	**1,108.0**	1,664.0
Term loan	**100.0**	100.0
Undrawn available Revolving Credit Facility	**600.0**	600.0
Currency and interest rate swaps	**(101.5)**	(182.2)
At 31 December	**1,064.1**	1,703.9

27 Issued share capital

Allotted, called up and fully paid	2018 m	2017 m	2018 £m	2017 £m
Ordinary shares of 2 1/15p each				
At 1 January	**670.1**	670.1	**13.8**	13.8
Rights issue	**1,001.0**	—	**20.7**	—
At 31 December	**1,671.1**	670.1	**34.5**	13.8

In May 2018, the Group offered a rights issue to existing shareholders on the basis of 3 shares for every 2 fully paid ordinary shares held. The issue was fully subscribed and resulted in the issue of 1,001,032,281 ordinary shares at £0.70 per share.

Share premium	2018 £m	2017 £m
Ordinary shares of 2 1/15p each		
At 1 January	**501.3**	501.3
Rights issue	**642.0**	—
At 31 December	**1,143.3**	501.3

The rights issue raised gross funds of £700.7m. The total amount capitalised to share capital and share premium was £662.7m (£700.7m less issuance costs of £38.0m).

Treasury shares	2018 m	2017 m	2018 £m	2017 £m
Ordinary shares of 2 1/15p				
At 1 January	**2.9**	3.2	**(0.1)**	(0.1)
Shares allotted in the year	**—**	(0.3)	**—**	—
At 31 December	**2.9**	2.9	**(0.1)**	(0.1)

In 2018, the Group made no purchases of shares into Treasury and allotted 28,057 (2017: 283,281) shares with an aggregate nominal value of £580 (2017: £4,420). The total consideration received in respect of these shares was £nil (2017: £nil).

Employee benefit trust shares	2018 m	2017 m	2018 £m	2017 £m
Ordinary shares of 2 1/15p				
At 1 January	**1.6**	1.7	**(0.1)**	(0.1)
Shares allotted in the year	**—**	(0.1)	**—**	—
Shares acquired during the year	**10.4**	—	**(11.0)**	—
At 31 December	**12.0**	1.6	**(11.1)**	(0.1)

The Group will use shares held in the employee benefit trust (EBT) in order to satisfy future requirements for shares under the Group's share option and long-term incentive plans. During the year, the EBT allotted 32,367 (2017: 69,337) ordinary 2 1/15p shares with an aggregate nominal value of £669 (2017: £1,434) to satisfy exercises under the Group's share option and long-term incentive plans. The total consideration received in respect of these shares was £nil (2017: £nil). The Group acquired 3.2m (2017: nil) ordinary 2 1/15p shares paying average market price of £1.87 per share with the total value of £6.0m (2017: £nil). Further, the Group exercised its rights under the rights issue, purchasing 7.2m of shares at £0.70 per share, paying £5.0m. The aggregate value of shares were transferred to the EBT.

The Group has an unexpired authority to re-purchase up to 10% of its issued share capital.

28 Share-based payment plans

The Group operates several share-based payment plans. In April 2018 Capita announced a rights issue. The rights issue was made on the basis of three new shares for every two existing shares held by qualifying shareholders at the record date.

To adjust for the dilutive impact of the 2018 rights issue, for share options held that had not vested by 25 May 2018, Capita granted an additional 1.639 (the adjustment factor) share options for every share option that an employee held to ensure that the fair value remained unchanged after dilution.

The expense recognised for share based payments in respect of employee services received during the year to 31 December 2018 was £3.4m (2017: £2.9m credit), all of which arises from equity-settled share based payment transactions. Details of the schemes are as follows:

Deferred annual bonus plan

This scheme is applicable to Executive Directors. Under this scheme, awards are made annually consisting of only deferred shares, which are linked to the payout under the annual bonus scheme (details of which are contained in the Directors' remuneration report on pages 80–98).

The value of deferred shares is determined by the pay-out under the annual bonus scheme: half of the annual bonus is paid in cash and the remainder is deferred into shares under the deferred annual bonus plan. Directors have the option to defer up to 100% of their annual bonus into deferred shares or net bonus into a restricted share award. The deferred/restricted shares are held for a period of three years from the date of award, during which they are not forfeitable, except in the case of dismissal for gross misconduct.

Notes to the consolidated financial statements continued

28 Share-based payment plans continued

Long-term incentive plans (LTIPs) – 2008 & 2017

The 2008 LTIP was approved and adopted at the AGM on 6 May 2008 and the 2017 LTIP was approved and adopted at the AGM on 13 June 2017. This scheme is open to senior employees and shares will vest according to performance criteria.

For the 2016 award, vesting of the award will depend on share price growth, EPS growth and return on capital employed measured over a three-year period. An award will not vest if Capita's average share price at the date of vesting is below the average share price at the date of grant. 75% of the number of shares which will vest is dependent upon the Company's EPS growth exceeding 6% and on banding within the scheme and 25% of the number of shares which will vest is dependent upon the Company's return on capital employed exceeding 14%, and on banding within the scheme.

For the 2017 award, vesting of the award will depend on EPS growth and return on capital employed measured over a three-year period. 75% of the number of shares which will vest is dependent upon the Company's EPS growth exceeding 3% and on banding within the scheme and 25% of the number of shares which will vest is dependent upon the Company's return on capital employed exceeding 11%, and on banding within the scheme.

For the 2018 award, vesting will depend on annualised cost savings, free cash flow and margin. 100% of the number of shares which will vest is dependent upon the Company's annualised cost savings reaching £205m, free cash flow reaching £240m and margin of 12%. 25% of the number of shares which will vest is dependent upon annualised costs savings reaching £160m, free cash flow reaching £180m and margin of 9%.

1997 Executive share option scheme

This scheme was open to senior employees other than Executive Directors and divisional Executive Directors. The exercise price of the options is equal to the market price of the shares on the date of grant. Options granted under this scheme become exercisable if the growth in the Company's EPS exceeds the growth in RPI by 8% over the three-year vesting period from the date of grant. The contractual life of each option granted is seven years. There are no cash settlement alternatives. During the year ended 31 December 2017, the total outstanding 0.1m share options, with a weighted average exercise prices (WAEP) of £6.83, were forfeited. No further awards were made under this scheme.

2008 & 2017 LTIP

	2018 m	2017 m
Outstanding as at 1 January	**8.9**	8.7
Awarded during the year	**27.1**	4.6
Exercised	**—**	0.0
Forfeited	**(6.3)**	(4.4)
Outstanding as at 31 December	**29.7**	8.9
Exercisable as at 31 December	**—**	—

The weighted average remaining contractual life of the above shares outstanding at 31 December 2018 was 1.5 years (2017: 1.6 years). There are no exercise prices for any options issued under the 2008 LTIP scheme.

Deferred annual bonus plan

The weighted average share price of options at the date of exercise in 2018 was £1.67. The weighted average share price during the year was £1.48 (2017: £5.62).

The total cash value of the Deferred Shares awarded during the year was £nil (2017: £nil).

All schemes

The fair value of the options granted/awarded during the year was £1.10 (2017: £4.37). None of the existing option schemes have exercise prices.

The fair value for the 2017 and 2018 share scheme issues is effectively the market price of a Capita share at the date of grant. Accordingly, no assumptions have been disclosed. The fair value of equity-settled share options granted pre-2017 is estimated as at the date of grant using a multiple simulation option pricing valuation model, taking into account the terms and conditions upon which the options were granted.

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome. In addition, within the 2008 LTIP is an average share price floor under which the share award will not vest. This floor is based on the Company's average share price at the date of vesting. No other features of options grant were incorporated into the measurement of fair value.

29 Additional cash flow information

Operating cash flow for the year ended 31 December 2018

As set out in note 2, the Group has simplified its non-statutory reporting measures to improve transparency and make it easier for the readers of the Annual Report and Accounts to understand its financial performance. The revised presentation is reported results on the face of the income statement, with a footnote detailing adjusting profit and earnings per share, and a note to the accounts (see note 3) providing a reconciliation between reported and adjusted profit. The presentation of the cash flow statement and additional cash flow information in the notes have also been revised to show the same split. Refer to note 3 for detail of the items excluded from adjusted results.

The 2017 cash flow has also been restated to: (i) include £28.9m of cash costs previously omitted from cash flows from investing activities used by discontinued operations; (ii) remove a £33.5m business exit provision from adjusted non-cash items; and (iii) correct a disclosed £0.5m loss of sale of property, plant and equipment to a £4.5m gain. The net result of these items is to reduce net cash inflow from investing activities by £28.9m and to increase net cash inflow from operating activities and reported free cash flow by £28.9m. There is no impact on the reported net movement in cash and cash equivalents as the adjustments were off set within movements in trade and other receivables/payables.

		2018		Restated 2017	
	Note	Adjusted £m	Reported £m	Adjusted £m	Reported £m
Cash flows from operating activities:					
Operating profit/(loss)	3	**335.3**	**34.9**	447.5	(420.1)
Adjustments for non-cash items:					
Depreciation	13	**59.1**	**60.1**	56.4	63.5
Amortisation of intangible assets	14	**27.9**	**114.6**	15.4	144.2
Share based payment expense	28	**3.4**	**3.4**	2.9	2.9
Employee benefits	32	**12.3**	**17.7**	30.8	30.8
(Profit)/loss on sale of property, plant and equipment	7	**11.4**	**11.4**	(4.5)	(4.5)
Accelerated deprecation / amortisation on business exit		**—**	**—**	—	1.9
Contingent consideration		**—**	**(5.4)**	—	(2.5)
Impairment of property plant and equipment	13	**6.1**	**6.1**	—	9.0
Impairment of intangibles acquired in business combinations	14	**—**	**61.7**	—	14.0
Impairment of goodwill and intangible assets	14	**—**	**58.1**	—	551.6
Impairment of contract related assets and investment loan	3	**—**	**—**	—	119.2
Impairment of loans and investments		**—**	**1.6**	—	—
Other adjustments:					
Movement in provisions		**2.8**	**(9.1)**	(25.2)	(22.7)
Other adjustments:					
Pension deficit contribution		**—**	**(42.0)**	—	—
Other contributions into pension schemes		**(16.1)**	**(21.0)**	(29.8)	(29.8)
Professional fees on acquisition		**—**	**—**	—	0.5
Re-measurement of businesses held for disposal		**—**	**—**	—	8.6
Movement in Capita Asset Services settlement provisions		**—**	**—**	—	3.4
Movements in working capital:					
Trade and other receivables		**91.2**	**89.3**	(37.2)	(30.6)
Non-recourse receivables financing		**(110.0)**	**(110.0)**	(23.6)	(23.6)
Trade and other payables		**(98.5)**	**(91.7)**	(115.3)	(111.7)
Deferred income		**(243.4)**	**(243.7)**	(75.2)	(66.8)
Contract fulfilment assets (non current)		**(11.7)**	**(11.7)**	(11.9)	(11.9)
Cash generated from operations		**69.8**	**(75.7)**	230.3	225.4
Adjustments for free cash flows:					
Income tax received		**26.6**	**25.3**	9.5	9.5
Net interest paid		**(39.0)**	**(52.5)**	(54.2)	(54.2)
Purchase of property, plant and equipment	14	**(74.6)**	**(89.4)**	(62.5)	(66.2)
Purchase of intangible assets	15	**(67.2)**	**(70.1)**	(70.8)	(71.0)
Proceeds from sale of property, plant and equipment/intangible assets		**1.9**	**1.9**	23.1	23.1
Free cash flow		**(82.5)**	**(260.5)**	75.4	66.6

Notes to the consolidated financial statements continued

29 Additional cash flow information continued

Adjusted free cash flow and cash generated from operations

	Free cash flow		Cash generated from operations	
	2018 £m	2017 £m	**2018 £m**	2017 £m
Reported	**(260.5)**	66.6	**(75.7)**	225.4
Pension deficit contributions	**46.9**	—	**46.9**	—
Significant restructuring	**100.8**	45.0	**100.8**	45.0
Business exits	**6.6**	(19.5)	**(11.1)**	(23.4)
Other	**23.7**	(16.7)	**8.9**	(16.7)
Adjusted	**(82.5)**	75.4	**69.8**	230.3

Pension deficit contributions: in November 2018, the Group agreed a deficit recovery plan with the Trustees of the Capita Pension and Life Assurance Scheme (the 'Scheme'). The payments under the agreed deficit recovery plan total £176m, of which £42.3m was paid in 2018. In addition, further contributions of £4.5m were made following closure of the Scheme in 2017 to future accrual for the majority of members of the Scheme. These payments have been excluded from adjusted cash flows as the Group treats them like a debt like item.

Significant restructuring: in April 2018, the Group announced a multi-year transformation plan. In the period to 31 December 2018, a cash outflow of £100.8m (2017: £45.0m) was incurred in relation to the cost of the transformation plan, and restructuring costs relating to Capita's previously announced cost reduction plan.

Business exits: the cash flows of businesses exited, or in the process of being exited, and the proceeds on disposals, are disclosed outside the adjusted results. The 2017 results have been restated for those businesses exited, or in the process of being exited, in 2018 to enable comparability of the adjusted results.

Other: includes the cash flows related to other items excluded from adjusted profit.

Reconciliation of net cash flow to movement in net funds/(debt)

				Non-cash flow movements				
	Note	Net debt at 1 January 2018 £m	Cash flow movements £m	Acquisitions in 2018 £m	Foreign exchange movements £m	Fair value changes £m	Other[2] £m	Net debt at 31 December 2018 £m
Cash, cash equivalents and overdrafts	20	**478.4**	**165.5**	—	**(1.2)**	—	—	**642.7**
Other loan notes	23	**(0.3)**	—	—	—	—	—	**(0.3)**
Private placement loan notes[1]	23	**(1,664.0)**	**580.9**	—	**3.1**	**(27.5)**	**(0.5)**	**(1,108.0)**
Currency swaps in relation to USD denominated private	18, 23	**176.8**	**(103.6)**	—	—	**26.4**	—	**99.6**
Interest rate swaps in relation to GBP denominated private	18	**5.4**	—	—	—	**(3.5)**	—	**1.9**
Term loan	23	**(100.0)**	—	—	—	—	—	**(100.0)**
Finance leases	18	**(0.2)**	**0.2**	—	—	—	—	—
Total net liabilities from financing activities		**(1,582.3)**	**477.5**	—	**3.1**	**(4.6)**	**(0.5)**	**(1,106.8)**
Deferred consideration	23	**(13.1)**	**11.1**	—	—	—	—	**(2.0)**
Net debt		**(1,117.0)**	**654.1**	—	**1.9**	**(4.6)**	**(0.5)**	**(466.1)**

1 The sum of these items held at fair value equates to the underlying value of the Group's private placement loan note's debt of £1,006.5m (2017: £1481.8m). Cash flow movement in private placement loan notes includes both repayment of private placement loan notes of £(577.2)m and financing arrangement costs of £(3.7)m.
2 Other comprises the amortisation of the discount on the euro debt issue.

The aggregate private placement loan note's fair value above of £1,108.0m (2017: £1,664.0m) (disclosed in note 23: Financial liabilities) includes the GBP value of the USD, GBP and EUR denominated loan notes at 31 December 2018. To remove the Group's exposure to currency fluctuations it has entered into currency swaps which effectively hedge the movement in the underlying USD loan notes' fair value. The interest rate swap is being used to hedge the exposure to changes in the fair value of GBP denominated private placement loan notes.

29 Additional cash flow information continued

The combined fair value of the interest and currency swaps, of £101.5m (2017: £182.2m), is disclosed in note 18: Financial assets, and note 23: Financial liabilities.

	Note	Net debt at 1 January 2017 £m	Cash flow movements £m	Non-cash flow movements: Acquisitions in 2016 £m	Non-cash flow movements: Foreign exchange movements £m	Non-cash flow movements: Fair value changes £m	Non-cash flow movements: Other[2] £m	Net debt at 31 December 2017 £m
Cash, cash equivalents and overdrafts	20	565.8	(90.5)	—	3.1	—	—	478.4
Other loan notes	23	(0.3)	—	—	—	—	—	(0.3)
Private placement loan notes[1]	23	(1,961.7)	126.2	—	(10.7)	184.0	(1.8)	(1,664.0)
Interest and currency swaps in relation to USD denominated	18, 23	357.9	—	—	—	(181.1)	—	176.8
Interest rate swaps in relation to GBP denominated private	18, 23	7.7	—	—	—	(2.3)	—	5.4
Term loan	23	(650.0)	550.0	—	—	—	—	(100.0)
Finance leases	23	(2.3)	2.1	—	—	—	—	(0.2)
Total net liabilities from financing activities		(2,248.7)	678.3	—	(10.7)	0.6	(1.8)	(1,582.3)
Fixed rate interest rate swaps	23	(85.1)	84.6	—	—	0.5	—	—
Deferred consideration	23	(10.8)	10.8	(2.0)	—	—	(11.1)	(13.1)
Net debt		(1,778.8)	683.2	(2.0)	(7.6)	1.1	(12.9)	(1,117.0)

1 The sum of these items held at fair value equates to the underlying value of the Group's private placement loan note's debt of £1,006.6m (2016: £1,481.8m). Cash flow movement in private placement loan notes includes both repayment of private placement loan notes of £(124.1)m and financing arrangement costs of £(2.1)m.
2 Other comprises the amortisation of the discount on the euro debt issue.

30 Capital commitments

At 31 December 2018, amounts contracted for but not provided in the financial statements for the acquisition of property, plant and equipment amounted to £10.7m (2017: £8.8m), relating to building improvement on a leased property and software upgrades.

31 Contingent liabilities

Contingent liabilities represent potential future cash outflows which are either not probable or cannot be measured reliably.

The Group has provided, through the normal course of its business, performance bonds and bank guarantees of £84.0m (2017: £88.4m).

We are in discussions with a number of the Group's life insurance clients, the outcomes and timings of which are uncertain but could result in the continuation of a contract with amended terms or the termination of a contract. If an operation is terminated, the Group may incur associated costs or accelerate the recognition of deferred income. As the outcome of these discussions is uncertain, the Group has not made any provision for a future outflow of funds that might result from the eventual outcome.

Capita completed the disposal of its Capita Asset Services businesses, including CFM, to the Link Group on 3 November 2017. Capita plc, as part of the sale of the Capita Asset Services businesses, has provided an indemnity against certain legacy claims.

The Capita Group entities are parties to legal actions and claims which arise in the normal course of business. The Group throughout the year needs to apply judgement in determining the merit of litigation against it and the chances of a claim successfully being made. It needs to determine the likelihood of an outflow of economic benefits occurring and whether there is a need to disclose a contingent liability or whether a provision might be required due to the probability assessment.

At any time there are a number of claims or notifications that need to be assessed across the Group. The disparate nature of the Group entities heightens the risk that not all potential claims are known at any point in time. Under the transformation plan, the support functions including commercial and legal are being strengthened and a Chief General Counsel has been appointed. This enhances the current processes in place to assess the likelihood of historical claims arising.

32 Employee benefits

The Group operates both defined benefit and defined contribution pension schemes.

Pension expense included in the income statement

	2018 £m	2017 £m
Defined contribution scheme	**94.9**	86.2
Defined benefit schemes		
Current Service cost	**8.2**	30.0
Administration costs	**2.9**	2.3
Past service cost/(credit)	**6.6**	(1.3)
Settlements	**—**	(0.2)
Total charged to profit before tax	**112.6**	117.0
Interest cost/(income)	**9.4**	9.2
Total in the income statement	**122.0**	126.2

Contributions to the defined contribution schemes are charged to the income statement as they fall due. The Group has no further obligations once the contributions have been made.

At 31 December 2018, retirement obligations were disclosed in relation to 10 (2017: 11) defined benefit pension schemes. The main defined benefit scheme is the Capita Pension and Life Assurance Scheme for which the Group is the sole employing sponsor. Grouped together under 'Other schemes' are nine smaller arrangements.

Notes to the consolidated financial statements continued

32 Employee benefits continued

The Capita Pension and Life Assurance Scheme (Scheme)

The Scheme is an HMRC-registered pension scheme and is subject to standard UK pensions and tax law. Details of the benefits provided are set out in the Scheme's documentation.

Responsibility for the operation and governance of the Scheme lies with a corporate Trustee which is independent of the Group. The Trustee Board is made up of member-nominated and employer-nominated directors plus an independent chairman. The nature of the relationship between the Group and the Trustee Board is governed by the rules of the Scheme and regulations.

The assets of the Scheme are held in a separate fund (administered by the Trustee Board) to meet long-term pension liabilities to beneficiaries. The Trustee Board invest the assets in line with their Statement of Investment Principles, which is regularly reviewed.

The Statement of Investment Principles has been established after taking into consideration the liabilities of the Scheme and the investment risk that the Trustee Board is willing to accept. The Group is consulted before the Statement of Investment Principles is formally adopted.

Benefits are continuing to accrue in the Scheme for a limited group of employees following the closure to future accrual for the majority of members on 30 November 2017.

A full actuarial valuation of the Scheme is carried out every three years by an independent actuary for the Trustee, with the last full valuation carried out at 31 March 2017. The purpose of that valuation is to design a funding plan to ensure that the pension scheme has sufficient assets available to meet future benefit payments, based on assumptions agreed between the Trustee and the Group. The 31 March 2017 valuation showed a funding deficit of £185m (31 March 2014: £1.4m). This equates to a funding level of 86.1% (31 March 2014: 99.8%).

The main reason for the increase in deficit was due to the fall in government bond yields, which was partly offset by greater asset returns than assumed.

As a result of the funding valuation, the Group and the Trustee agreed the following plan to eliminate the deficit of £185m, which is in addition to £21.5m paid in early 2018 as part of the disposal of Capita Asset Services to Link Administration Holdings and reflecting that a number of employers ceased to employ contributing members:

	2018	2019	2020	2021
Deficit contribution	£42m	£71m	£59m	£4m

The next scheme funding assessment is being carried out with an effective date of 31 March 2020. At each scheme funding assessment, the present value of the contributions detailed in the current recovery plan is compared with any shortfall revealed. Where the contributions under the current recovery plan are no longer expected (by the end of periods specified in the recovery plans) to be sufficient to remove the shortfall, a new recovery plan will need to be agreed between the trustees and the Group. Options include increasing contributions due from the Group, extending the recovery periods with additional contributions paid after the expiry of current recovery periods or some combination of the two. The affordability to the Group of any increase in contributions is a primary consideration in the agreement of any new recovery plan.

Where the contributions are more than sufficient to remove the shortfall by the end of the recovery period, options include reducing contributions due, keeping the recovery period the same, or shortening the recovery period.

The Group expects to contribute £86.0m to the Scheme over 2019.

The valuation of liabilities for funding purposes differs to the valuation for accounting purposes (which are shown in these financial statements) mainly due to different assumptions being used and different market conditions at the different valuation dates. The assumptions used for funding purposes are agreed between the Trustee and the Group, with the discount rate being based on the actual assets of the Scheme. While for accounting purposes the assumptions are determined in accordance with IAS19, with the discount rate being based on the yields available on high quality corporate bonds of appropriate currency and term.

As part of the sale of Capita Asset Services businesses to Link Administration Holdings, it was agreed with the Trustees that a cash contribution of £17.0m would be made to the Scheme. This was paid in January 2018.

The Scheme was closed to future accrual for the majority of members on 30 November 2017, with these members joining the Group's main defined contribution scheme. As a result of the Scheme closing to future accrual, there was a past service curtailment gain of £2.3m in 2017 reflecting the affected members moving from active members to deferred members. In addition, a number of employers ceased to employ contributing members of the Scheme. As a consequence of this the Group paid £4.5m into the Scheme during January 2018 and guarantees have been provided by four of these employers in favour of the Scheme (to put them in the same position as if they continued to be participating employers).

In 2012, the Group established the Capita Scotland (Pension) Limited Partnership (the 'Partnership') with the Scheme. Under this arrangement, intellectual property rights (IPR) in specific Group software was transferred to the partnership and the rights to use, develop and exploit this IPR was licensed back to the Group in return for an annual fee. The Scheme's interest in the Partnership entitles it to an annual distribution of £8.0m for 15 years.

The Group's interest in the Partnership is fully consolidated into these Group financial statements. The Group has taken advantage of the exemption conferred by Regulation 7 of the Partnerships (Accounts) Regulations 2008 and has, therefore, not appended the accounts of this qualifying partnership to these financial statements. Separate accounts for the Partnership are not required to be, and have not been, filed at Companies House.

Under IAS 19 (Revised) the interest in the Partnership does not represent a plan asset for Group reporting purposes and therefore the Scheme's deficit position presented in these accounts does not reflect the Scheme's interest in the Partnership. Accordingly, distributions from the Partnership to the Scheme are reflected in these Group accounts as pension contributions to the Scheme on a cash basis as paid.

32 Employee benefits continued

Other schemes

The total employer contributions to the 'Other' schemes for 2019 are estimated to be £3.0m.

Admitted Body arrangements

For the Admitted Body scheme under which benefits are continuing to accrue, the Group will only participate in the scheme for a finite period up to the end of the contract. The Group is required to pay regular contributions as decided by the relevant Scheme Actuary and as detailed in the scheme's Schedule of Contributions. In addition, the Group will be required to pay some or all of any deficit (as determined by the respective Scheme Actuary) that is remaining at the end of the contract. In respect of this, the Group is carrying a sufficient level of provision in these financial statements.

For the scheme to which the Group makes contributions under Admitted Body status (which is part of the Local Government Pension Scheme) responsibility for the governance of the scheme lies with boards which operate under a framework of corporate governance and are responsible for following the relevant statutory regulations. For the local government pension schemes there is a similar funding regime which is set out in the Local Government Pension Scheme (Administration) Regulations 2008.

Other UK schemes

- An allocated section of a Local Government Pension Scheme under which benefits are continuing to accrue where the Group is the employing sponsor.
- A segregated section of a multi-employer scheme in which the Group is a participating employer (under which benefits are not continuing to accrue).
- Three segregated sections in an industry-wide scheme (in one of which benefits are continuing to accrue).

For the non-public sector schemes, the scheme funding regime introduced by the Pensions Act 2004 required trustees to carry out regular funding assessments of the schemes and establish schedules of contributions and recovery plans when there is a shortfall in the schemes. The recovery plans detail the amount and timing of the contributions required to eliminate the shortfall in the schemes. Funding assessments are carried out at least every 3 years. Approximate funding updates are produced at each scheme anniversary, when a full scheme funding assessment is not being undertaken. Each of the Capita sections in these schemes is fully segregated and so there is no cross-subsidy with any other employer's section.

For these schemes, the latest formal valuations for each scheme were carried out between 31 December 2015 and 31 March 2016. The valuations for the other schemes are updated by qualified actuaries at each balance sheet date. Scheme assets are stated at their market valuations at each respective balance sheet date.

For the local government pension scheme there is a similar funding regime which is set out in the Local Government Pension Scheme (Administration) Regulations 2008. When the last contributing member in Capita's section of this scheme ceases to be a member, then this will trigger an exit debt. As at 31 March 2016, this was estimated at £3.1m.

Overseas schemes

The Irish scheme is classed as a cross-border scheme for which the beneficiaries of the scheme have their liabilities, and the trustees hold assets, denominated in euros. The scheme is governed under the UK regulations and subject to the further requirements applying to cross-border schemes.

The Swiss schemes are administered and governed through collective foundations which are separate legal entities. Benefits are continuing to accrue in the Swiss schemes.

There are a further 50 (2017: 55) defined benefit pension arrangements in which various Capita businesses have participated during 2018. These have been included in the defined contribution pension charge on materiality grounds either due to contractual protections or the size of the scheme.

However, one of these defined benefit schemes relates to participation in the Social Housing Pension Scheme which is a non-segregated multi-employer defined benefit pension scheme where it is not currently possible to identify the Group's share of the scheme under IAS 19. For this reason it has been included in the defined contribution pension charge. At the last valuation in 2017, a total deficit of £1,522m was disclosed. Total deficit contributions from all employers as a result of the 2017 valuation were £161m per annum, of which the Group's share is £0.41m per annum. If the Group were to cease to be a participating employer in this scheme there would be an exit debt payable. As at 30 September 2017 this was estimated at £11.9m. The Group's expected employer contributions for this scheme in 2019 is £0.4m.

Risks associated with the Group's pension schemes

These defined benefit pension schemes expose the Group to various risks, with the key risks set out below:

Investment risk: the schemes invest in a wide range of assets with a view to provide long-term investment returns at particular levels. There is a risk that investment returns are lower than expected which, in isolation, could result in a worsening of the funding position of the schemes.

Interest rate risk: the IAS 19 discount rate is derived based on the yields available on good quality corporate bonds of suitable duration. If these yields decrease, then in isolation, this would increase the value placed on the IAS 19 obligation and result in a worsening of the funding position of the schemes.

Inflation risk: the liabilities of the schemes are linked to future levels of inflation. If future inflation is higher than expected then this would result in the cost of providing the benefits increasing and thereby worsening the funding position of the schemes.

Longevity risk: if members live longer than expected, then pensions will be paid for a longer time which will increase the value placed on the liabilities and therefore worsen the funding position of the schemes.

In order to manage these risks, the Group and the trustees carry out regular assessments of these risks. For the main defined benefit scheme the following actions have been taken:

- The Trustee of the Capita Pension and Life Assurance Scheme has entered into two bulk annuity contracts with an insurer in respect of a small number of high individual liability pensioner members (one in 2015 and the second in late 2017) with total value included in the assets at 31 December 2018 of £68.7m (2017: £76.7m).
- The Trustee has entered into a Liability Driven Investment programme. The level of risk that is managed by this is set by various market-related and funding trigger points.

Together, these actions have led to a current level of hedging (interest rate and inflation) of around 65% of the liabilities measured on the trustees' long-term funding basis. As the funding level improves it is planned to further increase the level of hedging.

The hedging aims to match the value of the assets to the movement in liabilities due to inflation and interest rate changes. As part of this strategy and to retain exposure to growth assets, the scheme invests in derivatives to gain synthetic equity exposure. Therefore, the equity allocation shown below is in economic exposure terms (i.e. inclusive of the derivative based position).

Notes to the consolidated financial statements continued

32 Employee benefits continued

Assets and liabilities

Under IAS19, plan assets must be valued at the bid market value at the balance sheet date. Asset valuations have been sourced from the scheme's investment managers and custodians, based on their pricing sources and methodologies. For the main asset categories:

- Equities listed on recognised stock exchanges are valued at closing bid prices.
- Bonds are measured using a combination of broker quotes and pricing models making assumptions for credit and market risks and market yield curves.
- Properties are valued on the basis of open market values.
- Assets in investment funds are valued at fair value which is typically the Net Asset Value provided by the investment manager.
- Certain unlisted investments are valued using a model based valuation such as discounted cash flow.
- The value of bulk annuity contracts have been assessed by discounting the projected cash flows payable under the contracts (projected by an actuary, consistent with the terms of the contract) and is equal to the corresponding liability calculated by reference to the IAS19 assumptions.

The assets and liabilities of the defined benefit pension schemes (excluding additional voluntary contributions) as at 31 December are:

	Capita scheme				Other schemes				Group total	
			2018	2017			2018	2017	2018	2017
	Quoted £m	Unquoted £m	Total £m	Total £m	Quoted £m	Unquoted £m	Total £m	Total £m	Total £m	Total £m
Scheme assets at fair value:										
Equities:										
– UK	3.6	—	3.6	40.6	1.6	0.3	1.9	4.9	5.5	45.5
– Overseas	94.9	96.2	191.1	305.9	7.9	3.1	11.0	10.4	202.1	316.3
– Private	—	—	—	—	—	0.7	0.7	1.5	0.7	1.5
	98.5	96.2	194.7	346.5	9.5	4.1	13.6	16.8	208.3	363.3
Debt securities:										
– UK Government	323.3	(0.1)	323.2	249.9	17.0	—	17.0	13.8	340.2	263.7
– UK Corporate	—	0.1	0.1	45.0	0.4	—	0.4	0.4	0.5	45.4
– Overseas Government	—	17.8	17.8	34.1	2.8	—	2.8	2.6	20.6	36.7
– Overseas Corporate	—	118.5	118.5	137.2	0.5	—	0.5	0.4	119.0	137.6
– Emerging Markets	—	29.2	29.2	29.5	0.3	—	0.3	0.3	29.5	29.8
– Private Debt	—	57.3	57.3	34.6	—	—	—	—	57.3	34.6
– Secured Loans	—	—	—	—	1.6	—	1.6	1.6	1.6	1.6
	323.3	222.8	546.1	530.3	22.6	—	22.6	19.1	568.7	549.4
Property	—	85.7	85.7	78.3	4.8	0.3	5.1	4.8	90.8	83.1
Infrastructure	—	—	—	—	0.5	—	0.5	—	0.5	—
Credit Funds	—	—	—	—	8.0	—	8.0	8.2	8.0	8.2
Asset Backed Securities	—	—	—	—	0.8	—	0.8	0.7	0.8	0.7
Hedge Funds	80.1	135.2	215.3	214.4	0.6	—	0.6	0.6	215.9	215.0
Diversified growth funds	—	—	—	—	4.9	—	4.9	5.0	4.9	5.0
Insurance Contracts	—	68.7	68.7	76.7	—	17.5	17.5	16.4	86.2	93.1
Cash	24.1	1.4	25.5	(144.9)	(1.6)	—	(1.6)	1.2	23.9	(143.7)
Other	—	—	—	—	1.4	2.1	3.5	3.7	3.5	3.7
	104.2	291.0	395.2	224.5	19.4	19.9	39.3	40.6	434.5	265.1
Total	526.0	610.0	1,136.0	1,101.3	51.5	24.0	75.5	76.5	1,211.5	1,177.8
Present value of scheme liabilities			1,342.7	1,493.4			87.8	91.2	1,430.5	1,584.6
Net liability			(206.7)	(392.1)			(12.3)	(14.7)	(219.0)	(406.8)

These amounts do not include any directly owned financial instruments issued by the Group.

There are two assets which have been classified as insurance contracts for the purposes of these accounts:

- The two bulk annuity contracts entered into by the Trustee of the Capita scheme late in 2015 and 2017.
- The investment of the assets in respect of the Swiss schemes occurs by the collective foundations in the context of reinsurance contracts.

Reconciliation of retirement benefits

Explanation of constituents of the Income Statement.

The cost of providing the pension scheme over the year is broken down as follows:

- Service cost is the cost to the Group of future benefits earned by contributing members over the current financial period.
- Past service cost represents the change in the present value of scheme liabilities in the current period in relation to prior years' service.
- Administration costs are those entailed by the pension schemes over the current period.
- Interest cost/(income) is made up of the interest cost on pension liabilities and assets over the current period based on the discount rate adopted at the start of the period.

32 Employee benefits continued

The following table shows a reconciliation from the opening balances to the closing balances for the net defined benefit liability and its components:

	Defined benefit obligation		Fair value of plan assets		Group total Net defined liability	
	2018 £m	2017 £m	**2018 £m**	2017 £m	**2018 £m**	2017 £m
Balance at 1 January	**1,584.6**	1,454.9	**(1,177.8)**	(1,109.7)	**406.8**	345.2
Included in the income statement:						
Current service cost	**8.2**	30.0	**—**	—	**8.2**	30.0
Administration costs	**2.9**	2.3	**—**	—	**2.9**	2.3
Past service cost[1]	**6.6**	(1.3)	**—**	—	**6.6**	(1.3)
Settlements	**—**	(1.8)	**—**	1.6	**—**	(0.2)
Interest cost/(income)	**38.7**	39.8	**(29.3)**	(30.6)	**9.4**	9.2
Sub-total in income statement	**56.4**	69.0	**(29.3)**	(29.0)	**27.1**	40.0
Included in other comprehensive income:						
Actuarial loss/(gain) arising from:						
– demographic assumptions	**(16.1)**	(0.5)	**—**	—	**(16.1)**	(0.5)
– financial assumptions	**(100.7)**	83.9	**—**	—	**(100.7)**	83.9
– experience adjustments	**(39.5)**	14.1	**—**	—	**(39.5)**	14.1
– changes in asset ceiling/minimum liability	**—**	—	**—**	—	**—**	—
Return on plan assets excluding interest	**—**	—	**21.2**	(45.8)	**21.2**	(45.8)
Foreign currency translation	**1.1**	(0.9)	**(0.9)**	0.6	**0.2**	(0.3)
Sub-total in other comprehensive income	**(155.2)**	96.6	**20.3**	(45.2)	**(134.9)**	51.4
Employer contributions	**—**	—	**(80.0)**	(29.8)	**(80.0)**	(29.8)
Contributions by employees	**1.6**	1.6	**(1.6)**	(1.6)	**—**	—
Benefits paid	**(51.6)**	(37.3)	**51.6**	37.3	**—**	—
Contract bulk transfers/business combinations	**(5.3)**	(0.2)	**5.3**	0.2	**—**	—
Balance at 31 December	**1,430.5**	1,584.6	**(1,211.5)**	(1,177.8)	**219.0**	406.8

The defined benefit obligation comprises £1,430.5m (2017: £1,584.6m) arising from schemes that are wholly or partly funded.

Of the total pension cost of £27.1m (2017: £40.0m), £14.8m (2017: £28.5m) was included in cost of sales, £2.9m (2017: £2.3m) was included in administrative expenses, and £9.4m in finance costs (2017: £9.2m).

[1] Past service cost

The past service cost of £6.6m is made up of 3 elements:

- On 26 October 2018, the High Court issued a judgment which concluded that the schemes involved in the case should be amended to equalise pension benefits for men and women in relation to Guaranteed Minimum Pension (GMP) benefits. This will impact many pension schemes. The Group is working with the various trustees and their advisers to understand the extent to which the judgment crystallises additional liabilities in their schemes. This could take over a year to fully rectify. However, for the purpose of these financial reports, we have estimated that this will increase the reported liability of the Scheme by £4.4m and this is reflected as a past service cost in 2018. This cost is excluded from the adjusted profit as set out in note 3. There are still a number of uncertainties over how the equalisation is carried out, including the method of equalisation and any potential appeals about the ruling. Therefore, the overall cost could differ, but we have included our best estimate of this cost based on information known at this time. The impact of this will be considered at the next series of triennial valuations and any changes to future contributions will be assessed at that time.
- In addition, there is a past service cost of £1.0m in relation to the correction of an historic retirement age equalisation issue for a small group of members in the main scheme. This cost is excluded from the adjusted profit as set out in note 3.
- The remaining cost of £1.2m is in relation to the value of additional contractual benefits granted to members over the current period.

Notes to the consolidated financial statements continued

32 Employee benefits continued

Capita scheme

	Defined benefit obligation 2018 £m	Defined benefit obligation 2017 £m	Fair value of plan assets 2018 £m	Fair value of plan assets 2017 £m	Net defined liability 2018 £m	Net defined liability 2017 £m
Balance at 1 January	1,493.4	1,366.4	(1,101.3)	(1,038.0)	392.1	328.4
Included in the income statement:						
Current service cost	6.1	27.9	—	—	6.1	27.9
Administration cost	2.7	2.0	—	—	2.7	2.0
Past service cost including GMP equalisation and curtailment costs	6.0	(1.5)	—	—	6.0	(1.5)
Interest cost/(income)	36.8	37.8	(27.7)	(29.0)	9.1	8.8
Sub-total in income statement	51.6	66.2	(27.7)	(29.0)	23.9	37.2
Included in other comprehensive income:						
Actuarial loss/(gain) arising from:						
– demographic assumptions	(16.0)	(0.5)	—	—	(16.0)	(0.5)
– financial assumptions	(95.6)	81.2	—	—	(95.6)	81.2
– experience adjustments	(39.5)	13.8	—	—	(39.5)	13.8
Return on plan assets excluding interest	—	—	19.0	(42.5)	19.0	(42.5)
Sub-total in other comprehensive income	(151.1)	94.5	19.0	(42.5)	(132.1)	52.0
Employer contributions	—	—	(77.2)	(25.5)	(77.2)	(25.5)
Contributions by employees	—	0.1	—	(0.1)	—	—
Benefits paid	(45.9)	(33.6)	45.9	33.6	—	—
Contract bulk transfers/business combinations	(5.3)	(0.2)	5.3	0.2	—	—
Balance at 31 December	1,342.7	1,493.4	(1,136.0)	(1,101.3)	206.7	392.1

Other schemes

	Defined benefit obligation 2018 £m	Defined benefit obligation 2017 £m	Fair value of plan assets 2018 £m	Fair value of plan assets 2017 £m	Net defined liability 2018 £m	Net defined liability 2017 £m
Balance at 1 January	91.2	88.5	(76.5)	(71.7)	14.7	16.8
Included in the income statement:						
Current service cost	2.1	2.1	—	—	2.1	2.1
Administration cost	0.2	0.3	—	—	0.2	0.3
Past service cost including curtailment	0.6	0.2	—	—	0.6	0.2
Settlements	—	(1.8)	—	1.6	—	(0.2)
Interest cost/(income)	1.9	2.0	(1.6)	(1.6)	0.3	0.4
Sub-total in income statement	4.8	2.8	(1.6)	—	3.2	2.8
Included in other comprehensive income:						
Actuarial loss/(gain) arising from:						
– demographic assumptions	(0.1)	—	—	—	(0.1)	—
– financial assumptions	(5.1)	2.7	—	—	(5.1)	2.7
– experience adjustments	—	0.3	—	—	—	0.3
– changes in asset ceiling/minimum liability	—	—	—	—	—	—
Return on plan assets excluding interest	—	—	2.2	(3.3)	2.2	(3.3)
Foreign currency translation	1.1	(0.9)	(0.9)	0.6	0.2	(0.3)
Sub-total in other comprehensive income	(4.1)	2.1	1.3	(2.7)	(2.8)	(0.6)
Employer contributions	—	—	(2.8)	(4.3)	(2.8)	(4.3)
Contributions by employees	1.6	1.5	(1.6)	(1.5)	—	—
Benefits paid	(5.7)	(3.7)	5.7	3.7	—	—
Contract bulk transfers/business combinations	—	—	—	—	—	—
Balance at 31 December	87.8	91.2	(75.5)	(76.5)	12.3	14.7

32 Employee benefits continued

Breakdown of liabilities for the Capita Scheme

Information about the defined benefit obligation for the Capita Scheme:

	Proportion of overall liability % 2018	Duration (years) 2018	Proportion of overall liability % 2017	Duration (years) 2017
Active members	**7**	**24.6**	8	24.8
Deferred members	**64**	**23.9**	64	24.4
Pensioners	**29**	**13.5**	28	13.8
Total	**100**	**20.9**	100	21.5

Financial and demographic assumptions

	Capita scheme		Other schemes[2]	
Main assumptions:	**2018 %**	2017 %	**2018 %**	2017 %
Rate of price inflation – RPI/CPI	**3.20/2.20**	3.20/2.20	**3.20/2.20**	3.20/2.20
Rate of salary increase	**3.20**	3.20	**3.20**	3.20
Rate of increase of pensions in payment[1]:				
– RPI inflation capped at 5% per annum	**3.10**	3.10	**3.10**	3.10
– RPI inflation capped at 2.5% per annum	**2.20**	2.20	**2.20**	2.20
– CPI inflation capped at 5% per annum	**2.25**	2.25	**2.25**	2.25
– CPI inflation capped at 2.5% per annum	**1.80**	1.80	**1.80**	1.80
Discount rate	**2.85**	2.50	**2.85**	2.50
Expected take up maximum available tax free cash	**85.0**	85.0	**85.0**	85.0

The average future life expectancy from age 65 (in years) for mortality tables used to determine scheme liabilities for the various different schemes at 31 December 2018 and 31 December 2017 are as follows:

	Member currently aged 65 (current life expectancy)				Member currently aged 45 (life expectancy at 65)			
	Male		Female		Male		Female	
	2018	2017	**2018**	2017	**2018**	2017	**2018**	2017
Capita scheme[3]	**22.7**	22.7	**24.3**	24.4	**23.1**	23.1	**25.4**	25.4
Other schemes[4]	**22.7 to 24.2**	22.7 to 24.2	**24.3 to 24.4**	24.4	**23.1 to 25.9**	23.1 to 25.9	**25.4 to 26.2**	25.4 to 26.2

1 There are other levels of pension increase which apply to particular periods of membership.
2 Only the discount rate is relevant to the Admitted Body scheme. Different assumptions apply to non-UK schemes, for example: the discount rate for the Irish Scheme is 2.25% per annum and for the two Swiss schemes, 0.75% per annum in 2018.
3 The assumptions used for the Capita scheme are tailored for each member. The assumptions adopted make allowance for an increase in the longevity in the future. The rate for members currently aged 65 is derived from the pensioner membership and the rate for members reaching age 65 in 20 years' time is derived from non-pensioner membership.
4 This does not apply to the Admitted Body scheme or the Swiss schemes.

Sensitivity analysis

Given the nature and number of assumptions, which are not in the control of the Group, there are a range of reasonably possible outcomes. The table below shows how the value of the defined benefit obligations would increase if the assumptions were changed as shown (assuming all other assumptions remain constant):

Change in assumptions compared with 31 December 2018 actuarial assumptions	Capita scheme £m	Other schemes £m
0.1% decrease in discount rate	**28.0**	**1.3**
0.1% increase in salary increases	**0.5**	**0.1**
0.1% increase in inflation (and related assumption, e.g. salary and pension increases)	**14.6**	**0.9**
1 year increase in life expectancy	**53.7**	**2.7**

Notes to the consolidated financial statements continued

33 Related-party transactions

Compensation of key management personnel

	2018 £m	2017 £m
Short-term employment benefits	11.9	11.3
Pension	0.2	0.2
Share-based payments	—	0.1
	12.1	11.6

Gains on share options exercised in the year by Capita plc Executive Directors were £0.0m (2017: £0.7m) and by key management personnel £0.0m (2017: £0.2m), totalling £0.0m (2017: £0.9m).

During the year, the Group rendered administrative services to Smart DCC Ltd, a wholly-owned subsidiary which is not consolidated (refer to note 34). The Group received £64.3m (2017: £55.5m) of revenue for these services. The services are procured by Smart DCC on an arm's length basis under the DCC licence. The services are subject to review by Ofgem to ensure that all costs are economically and efficiently incurred by Smart DCC.

Capita Pension and Life Assurance Scheme is a related party of the Group. Transactions with the Scheme are disclosed in note 32 – Employee benefits on pages 157–164.

The following companies are substantial shareholders in the Company and therefore a related party of the Company (in each case, for the purposes of the Listing Rules of the UK Listing Authority). The number of shares held on 5 March 2019 was as below:

Shareholder	No. of shares	% of voting rights
Veritas Asset Management LLP[1]	192,533,863	11.54
Invesco Ltd	191,409,106	11.47
Investec Asset Management Ltd	153,805,729	9.22
RWC Asset Management LLP	127,012,876	7.61
Schroder Investment Management	101,030,829	6.06
Woodford Investment Management LLP	93,562,659	5.60
Coltrane Asset Management, L.P	82,388,589	4.94
BlackRock, Inc.	74,230,358	4.45
Marathon Asset Management LLP	64,756,810	3.88
Veritas Funds PLC	55,009,900	3.30
Vanguard Group	54,711,874	3.28
Norges Bank Investment Management	54,273,873	3.25
Jupiter Asset Management	53,573,060	3.21

1 This includes the holding of Veritas Funds PLC.

34 Group composition and non-controlling interests

The Group's subsidiaries are listed in notes 8 and 18 of the parent company financial statements on pages 185 and 190–195. This list includes AXELOS Limited and Entrust Support Services Limited which both have 49% non-controlling interests, and Fera which has a 25% non-controlling interest, none of whose contribution was material to the Group's financial performance, financial position or cash flow in both 2018 and 2017.

The Group holds a majority of the voting rights in all of these subsidiaries and the Directors have determined that, other than the entity commented on below, in each case the Group exercises de facto control.

On 23 September 2014, the Secretary of State for the Department for Energy and Climate Change granted Smart DCC Ltd (DCC), a wholly-owned subsidiary of the Group, a licence to establish and manage the smart metering communications infrastructure, governed by the Smart Energy Code. Each year the Group reassess whether it has control over DCC as required under IFRS 10. The Group's ability to control the relevant activities of DCC is restricted by DCC's operating licence. The power that the Group has over DCC's relevant activities by virtue of owning it is limited (given the restrictions in the licence). That power is held by the board of DCC where the Group has minority representation in compliance with the licence. The Group has therefore not consolidated DCC within its Group accounts. The disclosure of related party transactions with DCC is included in note 33 to these financial statements.

35 Post balance sheet event

As set out in note 25 the Company continues to discuss with the Financial Conduct Authority the final quantum of the redress payments regarding the Connaught Income Series 1 Fund. Since the year end the Company has been notified that it is probable that a reimbursement will be due to Capita. The amount is subject to final agreement but is not material to the financial statements. There are no post balance sheet events that have an adjusting effect on the financial statements.

Statement of Directors' responsibilities

The Directors confirm that, to the best of their knowledge:

- The consolidated financial statements in this report, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union, IFRIC interpretations and those parts of the Companies Act 2006 applicable to companies reporting under IFRS, give a true and fair view of the assets, liabilities, financial position and profit of the Group taken as a whole.
- The parent company financial statements in this report, which have been prepared in accordance with United Kingdom Accounting Standards (UK GAAP) and applicable law, give a true and fair view of the assets, liabilities, financial position and profit of the Company.
- The management report contained in this report includes a fair review of the development and performance of the business and position of the Company and the Group taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board.

Jon Lewis
Chief Executive Officer

Patrick Butcher
Chief Financial Officer

13 March 2019

Independent auditor's report

to the members of Capita plc

1. Our opinion is unmodified

We have audited the financial statements of Capita plc ("the Company") for the year ended 31 December 2018 which comprise the consolidated income statement, consolidated statement of comprehensive income, consolidated balance sheet, consolidated statement of changes in equity, consolidated cash flow statement, company balance sheet, company statement of changes in equity, and the related notes, including the accounting policies in note 2 to the Group financial statements and note 1 to the Parent Company financial statements.

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 International Financial Reporting Standards as adopted by the European Union;
- the Parent Company financial statements have been properly prepared in accordance with UK accounting standards, including FRS 101 *Reduced Disclosure Framework*; 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 are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the Audit & Risk Committee.

We were first appointed as auditor by the Directors on 18 August 2010. The period of total uninterrupted engagement is for the 9 financial years ended 31 December 2018. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

Overview	
Materiality: Group financial statements as a whole	£8m (2017: £12m) 3.8% (2017: 4.8%) of normalised Group profit before tax
Coverage	82% (2017: 82%) of total Group revenue 84% (2017: 85%) of total profits and losses before tax 84% (2017: 78%) of total Group assets

Risks of material misstatement		**vs 2017**
Recurring risks for the Group	Revenue and profit recognition	◀▶
	Impairment of intangible assets and goodwill	◀▶
	Items excluded from adjusted profit	◀▶
	Capitalisation and recoverability of contract assets	◀▶
	Provisions and contingent liabilities	◀▶
	Pensions obligations	◀▶
Recurring risk for the Group and the Parent Company	Going concern	▼
Recurring risks for the Parent Company	Recoverability of Parent Company's investment in, and amounts due from, its subsidiaries	◀▶

2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
Revenue and profit recognition Reported Group revenue of £3,918.4 million (2017: 4,234.6 million). Refer note 2(e), and Audit and Risk Committee report (pages 71-79).	**Accounting treatment** Professional standards require us to make a rebuttable presumption that the fraud risk from revenue is a significant risk. The incentive/pressures on management to achieve bonus targets and/or market consensus increase the risk of fraudulent revenue and profit recognition. **Subjective estimate** Following the adoption of IFRS15 the significant risk on long-term contracts relates to revenue recognised from variations or scope changes, where significant judgment is required to be exercised by the Board. There is a risk that revenue may be recognised even though it is not probable (i.e., not more likely than not) that consideration will be collected, which could be due to uncertainties over contractual terms and ongoing negotiations with customers. For long-term contracts, the contractual arrangements can be complex with regard to variable consideration and service performance measures. This can involve significant judgments that may impact the recognition of revenue and contract profits including, among others, those over: – the interpretation of contract terms concerning future obligations; – the allocation of revenue to performance obligations; – the combining of performance obligations where the services are inter related; and – the consideration of onerous contract conditions and associated loss provisions. For contracts that are in the pre-inflection stage, there are typically increased risks as the transformation activities are still to be completed. The execution risk associated with successful transformation requires judgment to be applied concerning costs to complete and the overall estimation of profit over the lifetime of the contract. There is a risk that such matters are not fully identified resulting in increased profits being recognised or the lack of consideration of contract loss provisions. The effect of these matters is that, as part of our risk assessment, we determined that revenue recognised from long-term contracts has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain revenue recognition accounting policies and the key judgments applied.	**Our procedures included:** **Tests of detail:** – We obtained and inspected a sample of the contractual agreements to understand the contract terms and conditions that underpin the revenue and the profit recognition assumptions and to identify conditions under which variable revenue can arise. – Where contract negotiations are ongoing in relation to variable consideration we discussed the current status with those involved in the negotiations and by reference to the associated signed contract or variations amendment. – We considered the assumptions within the business plans and lifetime assessments, checking that onerous contracts had been recognised appropriately, particularly on contracts that have had a poor performance in the current year and those contracts that are in a pre-inflection phase of transformation. – In determining whether onerous contract provisions should be recorded, we assessed contract profitability forecasts by analysing historic performance relative to contractual commitments over its full term. This included critically assessing the assumptions over future costs including projected savings and the actions required to achieve these by comparison to historical cost savings achieved on similar projects. This assessment covered a sample of contracts including those identified by the Board as being high risk, and comprising the major contracts in a pre-inflection phase. – where significant variable consideration had been recognised, we obtained and inspected the contractual agreements to understand the contract terms and conditions that underpin the revenue recognition assumptions – where relevant we also inspected correspondence with customers or other supporting documentation in relation to the variations or scope; and – we challenged whether the judgments made by the Board are appropriate based on the underlying contractual terms and evidence obtained. **Assessing transparency**: we considered the disclosures in the financial statements to check that these were comprehensive and provided sufficient detail of the revenue recognition policies and of the key judgments applied. **Our findings**: We found the amounts of revenue and profit recognised to be acceptable (2017: acceptable).

Independent auditor's report continued

to the members of Capita plc

	The risk	Our response
Impairment of Intangible Assets and Goodwill The Group records goodwill of £1,259.0 million (2017: £1,367.9 million) and other intangible assets £328.7 million (2017: £444.2 million) – see notes 14 & 15. Refer the Audit and Risk Committee report on pages 71-79.	**Forecast based valuation** We consider the carrying value of intangible assets and goodwill and the risk over potential impairment to be a significant audit risk because of the inherent uncertainty involved in forecasting and discounting future cash flows, which are the basis of the assessment of recoverability. The introduction of the new policies under IFRS15 led to a separation of revenue recognition from cash receipts, and adjustments are required to ensure that the future forecasts used in the impairment assessment approximate to future cash flows. The effect of these matters is that, as part of our risk assessment, we determined that the recoverable amount of goodwill and intangible assets has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. The financial statements (note 15) disclose the sensitivity estimated by the Group. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the key assumptions that drive the value in use calculations, and the key sensitivities that the Board has considered. In addition there is a risk that the disclosures do not adequately explain the events and circumstances that led to the impairment charge recorded in 2018. During the year there has been a change in the CGU structure, which requires explanation in the disclosures.	**Our procedures included:** – **Comparing valuations**: we compared the total amount of discounted cash flows as per the calculations to the Group's market capitalisation and assessed the rationale for the difference at the year end with the support of our own internal valuation specialists. – **Control operation**: we tested the principles and integrity of the Group's discounted cash flow model. – **Tests of detail**: we compared the cash flows used in the impairment model to the output of the Group's budgeting process and against the understanding we obtained about the business areas through our audit, and assessed if these cash flows were reasonable. – This included an assessment over any adjustments made to ensure that the future forecasts approximated to cash flows. – **Historical comparison**: we assessed the historical accuracy of the forecasts used in the Group's impairment model by considering actual performance against prior year budgets, and considering any relevant Group internal audit reports over this process. – **Benchmarking assumptions**: we used external data and our own internal valuation specialists to evaluate the key inputs and assumptions for growth and discount rates. – **Sensitivity analysis**: we performed sensitivity and break-even analyses for the key inputs and assumptions, and identified those cash-generating units we consider most sensitive to impairment. – **Assessing transparency**: we evaluated the adequacy of the disclosures related to the estimation uncertainty, judgments made and assumptions over the recoverability of intangible assets and goodwill, in particular checking that the sensitivity disclosures provided sufficient detail. We also assessed whether the disclosures adequately explained the events and circumstances that led to the impairment charge in 2018. **Our findings**: We found the amounts of intangible assets and goodwill recognised as at 31 December 2018 to be acceptable (2017: acceptable).

	The risk	Our response
Items excluded from adjusted profit Refer note 3 that details items excluded from adjusted profit and the Audit and Risk Committee report on pages 71-79.	**Presentation appropriateness** The Group separately presents adjusted operating profit and adjusted profit before tax as a note to the consolidated income statement and in note 3. The Company's financial highlights and commentary refers to 'adjusted' measures as well as those derived on an adopted IFRS basis. The reasoning behind this presentation is set out in notes to the financial statements. Items to be excluded from adjusted profit are not defined by IFRSs and therefore judgment is required by the Directors to identify such items and to maintain the comparability of results with previous years and in accordance with the Group's accounting policy. As such there is a risk of management bias. Failure to disclose clearly the nature and impact of items excluded from adjusted profit may distort the reader's view of the financial result in the year. **Disclosure quality** During the year the company has simplified the presentation of the consolidated income statement and reduced the number of adjusted profit measures. The disclosures need to include sufficient explanation of the items adjusted to ensure these are transparent and understandable.	**Our procedures included:** **Assessing principles**: – We communicated our consideration on the classification of items excluded from adjusted profit to the Audit and Risk Committee to inform the debate on the Board's assessment of the policy decision to present adjusted profit measures. – We examined the presentation of adjusted profit measures in the front half of the annual report and consider this against applicable guidelines (including the FRC publications on the presentation of alternative performance measures). **Assessing balance**: – We considered whether there are any items included in the adjusted profit measures that it would be more appropriate to exclude from these measures and vice versa. – We also assessed whether there was sufficient balance between credit and debit items that are so separately presented. – We tested on a sample basis items recorded as adjustments to source documentation to assess the appropriateness of classification. – As part of this consideration, we assessed the consistency of application of the Group's accounting policy for the classification of items excluded from adjusted profit year-on-year. **Assessing transparency**: – We assessed whether the basis of the 'adjusted' financial information is clearly and accurately described and consistently applied and that all 'alternative performance measures', together with reconciliations to the adopted IFRS position, are shown with sufficient prominence in the annual report. **Our findings**: We found the amounts presented for adjusted profit to be acceptable (2017: acceptable).

KPMG

Independent auditor's report continued

to the members of Capita plc

	The risk	Our response
Capitalisation and recoverability of contract assets The adoption of IFRS15 has led to the recognition of contract fulfilment assets (see note 17). Refer notes 2(e) & 17, and Audit and Risk Committee report (pages 71-79).	**Accounting application** IFRS15 requires that costs incurred on a contract, or an anticipated contract that generate or enhance the resources of an entity to deliver the contract should be capitalised and amortised over the expected life of the contract. **Subjective estimate** Judgment is required in applying the accounting policy that Capita has introduced to assess whether the costs incurred will enhance the future economic benefits to the Company. Where a contract is not performing as expected the costs capitalised may not be recoverable and an impairment of the asset may need to be recorded. Contract fulfilment assets are required to be amortised over the expected life of the contract and this requires an estimate of any likely contract extensions. The effect of these matters is that, as part of our risk assessment, we determined that the recoverable amount of contract assets has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the capitalisation criteria that are used to assess whether items of expense should be recorded as a contract asset.	**Our procedures included:** – **Tests of detail:** we tested on a sample basis the costs capitalised in 2018 as contract fulfilment assets by reference to the criteria set out in the Group's accounting policy. For each of the assets sampled we obtained third party support, or for internally generated time, we obtained the relevant costing rates and records, to support the basis of capitalisation. – **Sensitivity analysis:** where a contract has performed below budget, we assessed whether there was uncertainty in regard to the recoverability of the contract fulfilment asset through future contract profitability. – **Tests of detail:** we considered on a sample basis the useful economic lives applied to the contract fulfilment assets and assessed the expected contract life by reference to the contract terms or where appropriate any agreed extensions to the original contract. – **Assessing transparency:** we considered the disclosures in the financial statements to assess that these provided sufficient detail of the criteria used to assess whether expense items should be recorded as a contract asset. **Our findings:** We found the amounts of contract assets recognised to be acceptable (2017: acceptable).

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	The risk	Our response
Provisions and Contingent Liabilities See note 25 for details of the provisions totalling £116.2 million as at 31 December 2018 (2017: £212.6 million) and note 31 for a discussion on the contingent liabilities identified. Also refer the Audit and Risk Committee report on pages 71-79.	**Subjective estimates** Significant judgment is required to assess whether actual or potential claims, litigation or fines arising from regulatory oversight, or from contractual arrangements with customers and suppliers, should be recognised as provisions within the financial statements or warrant disclosing as contingent liabilities. The determination and estimation of amounts for these provisions is inherently judgmental by their nature and there is a risk that the estimate is incorrect and any provision is materially misstated. The effect of these matters is that, as part of our risk assessment, we determined that provisions have a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. **Disclosure quality** Where the impact of possible and present obligations is not probable or not reliably measurable, and thus no provision is recorded, failure to adequately disclose the nature of these circumstances within the financial statements may distort the reader's view as to the potential risks faced by the Group.	**Our procedures included:** – **Personnel interviews**: We enquired of the Directors and inspected board minutes for actual and potential claims arising in the year based on any external communications with the Group as noted in any Board discussions, and assessed whether provisions are required for these claims. Our enquiries are included as standard questions in all our meetings with those responsible for preparing the financial statements including the divisional Finance Directors, heads of functions at Group and corporate level, and the Executive Directors. **Tests of detail**: – We obtained an understanding and status of existing claims and litigations via enquiries and examining any relevant correspondence. This included enquiries of the Directors' assessment regarding the likelihood of the existence of obligations, and the basis used to measure any provisions; – We compared the Directors' estimate of the risk and impact of these claims and litigations to third party evidence, where available; – In respect of open matters of claims and litigations, where appropriate, we had discussions with the Group's external legal advisors in respect of the reasonableness of the estimated liability. – **Assessing transparency**: we evaluated the adequacy of the Group's provisions and contingent liability disclosures in the financial statements in accordance with accounting standards, and in particular the disclosure of the estimation uncertainty and the quantification of that uncertainty where appropriate. **Our findings**: We found the amounts included for provisions to be acceptable (2017: acceptable). We found the disclosures included for provisions and contingent liability to be acceptable (2017: acceptable).
Pensions obligations See note 32 for details of the Group pension schemes and their obligations as at 31 December 2018. Also refer to the Audit and Risk Committee report on pages 71-79.	**Subjective estimation** Significant estimates are made in estimating the Group's defined benefit pension obligations and small changes in assumptions and estimates used would have a significant effect on this amount. There is a risk that the assumptions applied are not appropriate in the context of the pension scheme arrangements. The effect of these matters is that, as part of our risk assessment, we determined that the valuation of pension obligations has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. The financial statements (note 32) disclose the sensitivity estimated by the Group. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the key assumptions that the Board has adopted for the purpose of valuing the pension obligations.	**Our procedures included:** – **Assessing the valuer's credentials**: we evaluated the competence and independence of the external actuaries who are engaged by the Group to estimate the pension scheme obligations for the purpose of the financial statements. – **Methodology choice**: we used our internal actuary specialists to consider and critically assess the methodologies applied including benchmarking the key assumptions applied in determining the Group's defined benefit obligations, being the discount rate, inflation rate and mortality/life expectancy. This included a comparison of these key assumptions against externally derived data. – **Assessing transparency**: we evaluated the adequacy of the disclosures in respect of the sensitivity of the obligations to these assumptions. **Our findings**: We found the amounts included for pension schemes obligations to be acceptable (2017: acceptable).

Independent auditor's report continued

to the members of Capita plc

	The risk	Our response
Going concern Refer to note 2(b) and the viability statement on page 52 for the Board's assessment of the appropriateness of the going concern basis of preparation and the Group's longer-term viability. We have assessed this risk as having reduced compared to prior year when there was a material uncertainty related to the planned rights issue, which completed during 2018.	**Disclosure quality** The financial statements explain how the Board has formed a judgement that it is appropriate to adopt the going concern basis of preparation for the group and parent company. The going concern assumption and viability assessment is dependent on the successful implementation of the transformation plan described in the strategic report That judgement is based on an evaluation of the inherent risks to the Group's and Company's business model and how those risks might affect the Group's and Company's financial resources or ability to continue operations, taking into account all available information about the future, which covers a period of at least a year from the date of approval of the financial statements but is not limited to that period. The risks most likely to adversely affect the Group's and Company's available financial resources in the future relate to continued execution risk associated with the Group's transformation plan. These include, but are not limited to, the following: • An inability to sustain the forecast cost savings and achieve cost competitiveness; • An inability to achieve the growth targets in the Group's business plan; • A significant unexpected downturn in performance in one of the group's businesses; and • An increase in attrition and/or continuing reduction in new contract wins. There are also less predictable but realistic second order impacts, such as the impact of Brexit on customer or supplier confidence. In the event that one or more of the above risks were to materialise the Board's assessment of the group's ability to continue as a going concern would involve significant judgment with respect to the ability to comply with debt covenants and maintain liquidity in the future. The risk for our audit was whether or not those risks were such that they amounted to a material uncertainty that may have cast significant doubt about the ability to continue as a going concern. Had they been such, then that fact would have been required to have been disclosed.	**Our procedures included:** **Our sector experience:** – We tested the integrity of the cash flow projections and considered the appropriateness of key assumptions used in preparing those projections, with a specific focus on the cost reduction and revenue growth assumptions. We evaluated these via enquiries with each of the divisional Finance Directors, and other Executives including the Chief Transformation Officer and Chief Growth Officer. We assessed the projections and assumptions by reference to our knowledge of the business and general market conditions and assessed the potential risk of management bias. **Funding assessment:** – We re-performed calculations, for 30 June 2019, 31 December 2019, 30 June 2020 and 31 December 2020, prepared to test expected compliance with the key financial covenant tests to test mathematical accuracy. – We considered the adjustments made in the adjusted EBITDA for the covenant calculations, considering the appropriateness compared to the loan agreements and historical accepted practice with the current lenders. In addition, we inspected the correspondence between the Company and the private placement lenders that set out the proposed items to be excluded in the adjusted EBITDA definition and compared these against the items included in the covenant calculations. **Sensitivity analysis:** – We challenged the level of sensitivities applied (including downside scenarios) for reasonableness based on our knowledge of the business and markets served, and we evaluated whether the Directors' plans to alleviate the downside risk evident from these scenarios were feasible in the circumstances. – We considered management's assessment of the potential impacts of Brexit on the Group along with their plans to mitigate those risks. **Assessing transparency:** – We also assessed the completeness and accuracy of the matters covered in the going concern disclosure, including whether they sufficiently explain the judgements made by the Directors in assessing whether the going concern basis of preparation is appropriate. **Our findings**: we found the going concern disclosure without any material uncertainty to be acceptable (2017: disclosure with a material uncertainty acceptable).

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	The risk	Our response
Recoverability of the Parent Company's investment in, and amounts due from, its subsidiaries Investment carrying value £507.9 million (2017: £220.2 million), and amounts due from subsidiaries £969.5m (2017: £992.7m). Refer to note 1 (accounting policies) and notes 8-9 (financial disclosures) and Parent Company Balance Sheet	**Low risk, high value** The carrying amount of the Parent Company's investment in, and amounts due from, its subsidiaries represents 22.6% and 43.1% (2017: 11.2% and 50.7%) of its total assets respectively. The recoverability is not at a high risk of significant misstatement or subject to significant judgment. However, due to its materiality in the context of the Parent Company financial statements, this is considered to be the area that had the greatest effect on our overall Parent Company audit.	**Our procedures included:** – **Tests of detail**: we compared the carrying amount of the investment, and the amounts due from subsidiaries, with the relevant subsidiary's draft statutory balance sheet to identify whether its net assets, being an approximation of its minimum recoverable amount, was in excess of its carrying amount and assessed whether the subsidiary has historically been profit-making. **Our findings**: we found the Parent Company's assessment of the recoverability of the investment in subsidiaries to be acceptable (2017: acceptable).

We identified the IFRS 15 Opening Balance Restatement as a key audit matter for the prior year audit. We continue to perform procedures over the application of IFRS 15. However, as it is no longer the first year of adoption of IFRS 15, we have not assessed the restatement as one of the most significant risks in our current year audit and, therefore, it is not separately identified in our report this year.

Independent auditor's report continued

to the members of Capita plc

3. Our application of materiality and an overview of the scope of our audit

The materiality for the Group financial statements as a whole was set at £8.0 million, determined with reference to a benchmark of normalised Group profit before tax of £212.2 million, of which it represents 3.8%.

In order to set this benchmark we consider the nature of items excluded in determining adjusted profit before tax. Group reported profit before tax from continuing operations is £272.6 million. We normalised by adding back certain specific items including the profit on business exits – £309.7 million (note 3); impairment charges against goodwill and acquired intangibles – £95.5 million (note 3); claims and litigation provisions release – £1.8 million (note 3); non-trading business exit disposal expense – £29.7 million (note 3); private placement loan notes prepayments costs - £15.9 million (note 9); significant restructuring expense – £110.0 million (note 3). Total adjustments to reported profit before tax amount to £60.4 million resulting in a normalised Group profit before tax for materiality purposes of £212.2 million.

Materiality for the prior year was set at £12.0 million determined with reference to a benchmark of normalised Group profit before tax of £251.5 million, of which it represented 4.8%.

In order to set that benchmark we considered the nature of items excluded in determining adjusted profit before tax. Group originally reported loss before tax was £513.1 million. We normalised by adding back certain specific items including the non-trading business exit disposal expense – £13.7 million (note 3); losses on business disposals – £30.6 million (note 3); impairments of other non-current assets – £63.5 million (note 3); impairments of life and pension assets – £61.2 million (note 3); impairment charges against goodwill and acquired intangibles – £565.6 million (note 14); claims and litigation provisions expense – £30.0 million (note 3). Total adjustments to reported profit before tax amount to £764.6 million resulting in a normalised Group profit before tax for materiality purposes of £251.5 million.

Materiality for the parent company financial statements as a whole was set at £5.2 million (2017: £7.8 million), by reference to component materiality. This is lower than the materiality we would otherwise have determined by reference to total assets, and represents 0.2% of the Company's total assets (2017: 0.7%).

We report to the Audit and Risk Committee any corrected or uncorrected identified misstatements with a profit impact in excess of £0.4 million (2017: £0.6 million), and reclassification misstatements greater than £1m (2017: £0.6 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Audits for Group reporting purposes were performed by component auditors at 28 (2017: 29) key reporting components in the United Kingdom, Switzerland, Germany, and by the Group audit team over 2 key components in the United Kingdom, including the parent company (2017: in the United Kingdom, Switzerland, Germany, Ireland and Guernsey and by the Group audit team over 2 key components in the United Kingdom, including the parent company).

The Group audit team, with the assistance of the component auditors where appropriate, performed procedures on the items excluded from normalised Group profit before tax. These procedures covered approximately 82.3% of total Group revenue (2017: 81.5%); 84.1% of the total profits and losses that made up Group profit before tax (2017: 85.0%); and 84.0% of total Group assets (2017: 78.3%). For the remaining components, we performed analysis at an aggregated Group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The Group operates a shared service centre in London, the outputs of which are included in the financial information of the components it services. The service centre is subject to risk-focused audit procedures, predominantly the testing of transaction processing and review controls. Additional procedures are performed at certain reporting components to address the audit risks not covered by the work performed over the shared service centre.

The Group audit team approved the component materiality levels, which ranged from £0.4 million to £5.2 million (2017: £0.1 million to £7.8 million), having regard to the mix of size and risk profile of the Group across the components.

Detailed audit instructions were sent to the component auditors. These instructions covered the significant audit areas that should be covered by these audits (which included the relevant risks of material misstatement detailed above) and set out the information required to be reported back to the Group audit team. Telephone conference meetings were held with component auditors throughout the audit. At these meetings, the findings reported to the Group team were discussed in more detail, and any further work required by the Group team was then performed by the component auditor.

4. We have nothing to report on going concern

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

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the Group and the Company will continue in operation.

We identified going concern as a key audit matter (see section 2 of this report). Based on the work described in our response to that key audit matter, we are required to report to you if:

- we have anything material to add or draw attention to in relation to the directors' statement in Note 2(b) to the financial statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the Group and Company's use of that basis for a period of at least twelve months from the date of approval of the financial statements ; or
- the related statement under the Listing Rules set out on page 65 is materially inconsistent with our audit knowledge .

We have nothing to report in these respects.

5. We have nothing to report on the other information in the Annual Report

The Directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

Strategic report and Directors' report

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

Directors' remuneration report

In our opinion the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Disclosures of principal risks and longer-term viability

Based on the knowledge we acquired during our financial statements audit, we have nothing material to add or draw attention to in relation to:
- the Directors' confirmation within the viability statement (page 52) 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 and liquidity;
- the Principal Risks disclosures describing these risks and explaining how they are being managed and mitigated; and
- the Directors' explanation in the viability statement of how they have assessed the prospects of the Group, over what period they have done so and why they considered 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.

Under the Listing Rules we are required to review the viability statement. We have nothing to report in this respect.

Independent auditor's report continued

to the members of Capita plc

Our work is limited to assessing these matters in the context of only the knowledge acquired during our financial statements audit. As we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgments that were reasonable at the time they were made, the absence of anything to report on these statements is not a guarantee as to the Group's and Company's longer-term viability.

Corporate governance disclosures

We are required to report to you if:
- we have identified material inconsistencies between the knowledge we acquired during our financial statements audit and the Directors' statement that they consider that 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 position and performance, business model and strategy; or
- the section of the annual report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We are required to report to you if the Corporate Governance Statement does not properly disclose a departure from the eleven provisions of the UK Corporate Governance Code specified by the Listing Rules for our review.

We have nothing to report in these respects.

6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion:
- adequate accounting records have not been kept 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.

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 68, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and 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 they 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

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

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

Irregularities – ability to detect

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 and legal 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.

Firstly, 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, taxation legislation, and pension regulation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the group is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation or the loss of the group's licence to operate. We identified the following areas as those most likely to have such an effect: anti-bribery and corruption, data protection, employment law, health and safety, and regulatory capital and liquidity recognising the broad range of business process outsourcing services offered by the Group that include financial and regulated activities in the Specialist Services, People Solutions and Customer Management divisions, and the Governmental nature of many of the group's customers in the Government Services division. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and other management and inspection of regulatory and legal correspondence, if any. Through these procedures, we became aware of actual or suspected non-compliance and considered the effect as part of our procedures on the related financial statement items. The identified actual or suspected non-compliance was not sufficiently significant to our audit to result in our response being identified as a key audit matter.

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.

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

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

Robert J Brent (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square, London, E14 5GL
13th March 2019

KPMG

Company balance sheet

As at 31 December 2018

	Notes	2018 £m	2017 £m
Fixed assets			
Intangible assets	5	**63.2**	29.7
Tangible assets	6	**26.9**	18.6
Investments	8	**507.9**	220.2
		598.0	268.5
Current assets			
Financial assets	7	**7.1**	8.1
Debtors due within 1 year	9	**1,025.0**	1,099.5
Debtors due after more than 1 year	9	**109.1**	129.5
Cash		**509.9**	452.5
		1,651.1	1,689.6
Creditors: amounts falling due within 1 year	10	**185.2**	276.5
Provisions	10	**28.4**	130.4
Net current assets		**1,437.5**	1,282.7
Total assets less current liabilities		**2,035.5**	1,551.2
Creditors: amounts falling due after more than 1 year	10	**229.9**	281.4
		1,805.6	1,269.8
Capital and reserves			
Called up share capital	12	**34.5**	13.8
Employee benefit trust and treasury shares	12	**(11.2)**	(0.2)
Share premium account	12	**1,143.3**	501.3
Capital redemption reserve		**1.8**	1.8
Merger reserve		**44.6**	44.6
Cash flow hedging reserve		**0.8**	—
Profit and loss account		**591.8**	708.5
		1,805.6	1,269.8

The accompanying notes form part of the financial statements.

The accounts were approved by the Board of Directors on 13 March 2019 and signed on its behalf by:

Jon Lewis
Chief Executive Officer

Patrick Butcher
Chief Financial Officer

Company registered number: 02081330

Company statement of changes in equity

For the year ended 31 December 2018

	Share capital £m	Employee benefit trust and treasury shares £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Cash flow hedging reserve £m	Profit and loss account £m	Total £m
At 1 January 2017	13.8	(0.2)	501.3	1.8	44.6	—	476.1	1,037.4
Profit for the year	—	—	—	—	—	—	440.5	440.5
Total comprehensive income for the year	—	—	—	—	—	—	440.5	440.5
Share based payment	—	—	—	—	—	—	2.9	2.9
Equity dividends paid	—	—	—	—	—	—	(211.0)	(211.0)
At 1 January 2018	13.8	(0.2)	501.3	1.8	44.6	—	708.5	1,269.8
Loss for the year	**—**	**—**	**—**	**—**	**—**	**—**	**(120.1)**	**(120.1)**
Other comprehensive income	**—**	**—**	**—**	**—**	**—**	**0.8**	**—**	**0.8**
Total comprehensive expense for the year	**—**	**—**	**—**	**—**	**—**	**0.8**	**(120.1)**	**(119.3)**
Share based payment	**—**	**—**	**—**	**—**	**—**	**—**	**3.4**	**3.4**
Shares issued/(purchased) (note 12)	**20.7**	**(11.0)**	**642.0**	**—**	**—**	**—**	**—**	**651.7**
As at 31 December 2018	**34.5**	**(11.2)**	**1,143.3**	**1.8**	**44.6**	**0.8**	**591.8**	**1,805.6**

The accompanying notes are an integral part of the financial statements.

Notes to the Company financial statements

1 Accounting policies

(a) Basis of preparation

The accounts are prepared under the historical cost convention and in accordance with applicable accounting standards.

In determining the appropriate basis of preparation of the financial statements for the year ending 31 December 2018, the Directors are required to consider whether the Company can continue in operational existence for the foreseeable future. Having taken decisive action to strengthen the balance sheet through the raising of new equity and the disposal of non-core businesses, the Board are satisfied that the Group will continue to have adequate financial resources to realise their assets and discharge its liabilities as they fall due. Accordingly, the Directors have formed the judgement that it is appropriate to prepare these financial statements on the going concern basis. Therefore, the financial statements do not include any adjustments which would be required if the going concern basis of preparation is inappropriate.

The Group's committed revolving credit facility, bank term loan facilities and private placement notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. The Group's covenanted maximum ratio is 3.0 times or to 3.5 times depending on the debt instrument in question. They are tested semi-annually.

The Group has net debt of £466.1m at 31 December 2018 (2017: £1,117.0m) and adjusted net debt of £494.7m at 31 December 2018 (2017: £1,153.0m). Net debt is reported in note 29 of the consolidated financial statement – additional cash flow information. Adjusted net debt is used to calculate the gearing ratio being adjusted net debt to adjusted EBITDA (refer to the alternative performance measures on pages 197–198).

The Group's calculation of adjusted net debt to adjusted EBITDA at 31 December 2018 is 1.2 times and is compliant with the relevant ratios.

A separate profit and loss account dealing with the results of the parent company undertaking only has not been presented as provided by Section 408 of the Companies Act 2006.

(b) Compliance with accounting standards

These financial statements have been prepared in accordance with Financial Reporting Standard 101 – Reduced Disclosure Framework (FRS 101).

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

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the EU (EU-IFRS) and are on pages 100–164 of this report. In these Company financial statements, the following disclosure exemptions available under FRS 101 have been applied:

- A cash flow statement and related notes;
- Comparative period reconciliations for share capital, tangible fixed assets, and intangible assets;
- Disclosures in respect of transactions with wholly-owned subsidiaries;
- The effects of new but not yet effective IFRSs;
- An additional balance sheet for the beginning of the earliest comparative period following the retrospective change in accounting policy; and
- Disclosures in respect of the compensation of key management personnel.

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

- Certain disclosures required by IFRS 2 Share Based Payments in respect of Group settled share based payments;
- Certain disclosures required by IAS 36 Impairments of assets in respect of the impairment of goodwill and indefinite life intangible assets;
- Certain disclosures required by IFRS 3 Business Combinations in respect of business combinations undertaken by the Company in the prior periods; and
- Disclosures required by IFRS 7 Financial Instrument Disclosures.

(c) Tangible fixed assets

Depreciation is provided on all tangible fixed assets at rates calculated to write-off the cost on a straight-line basis over the expected useful lives of the assets concerned, as follows:

- Computer equipment – 3 to 10 years
- Furniture, fixtures and equipment – 4 to 5 years
- Leasehold improvements – over the period of the lease.

(d) Intangible assets

Intangible assets are valued at cost less any accumulated amortisation and any impairment losses. Amortisation is calculated to write-off the cost in equal annual instalments over their estimated useful life of three to 15 years. In the case of capitalised software development costs, research expenditure is written off to the statement of profit and loss in the period in which it is incurred. Development expenditure is written off in the same way unless and until the Company is satisfied as to the technical, commercial and financial viability of individual projects. Where this condition is satisfied, the development expenditure is capitalised and amortised over the period during which the Group is expected to benefit.

(e) Investments

Fixed asset investments are shown at cost, less provisions for impairment.

Investments held as current assets are stated at the lower of cost and net realisable value.

The carrying values of fixed asset investments are reviewed for impairment if events or changes in circumstances indicate the carrying values may not be recoverable.

1 Accounting policies continued

(f) Pension schemes

The Company participates in a number of defined contribution schemes and contributions are charged to the profit and loss account in the year in which they are due. These schemes are funded and the payment of contributions is made to separately administered trust funds. The assets of these schemes are held separately from the Company. The Company remits monthly pension contributions to Capita Business Services Limited, a subsidiary undertaking, which pays the Group liability centrally. Any unpaid contributions at the year-end have been accrued in the accounts of that company.

The Company also has employees who are members of a defined benefit scheme operated by the Group – the Capita Pension & Life Assurance Scheme (the 'Capita DB Scheme').

As there is no contractual arrangement or stated Group policy for charging the net defined benefit cost of the Capita DB Scheme is recognised fully by the principal employer which is Capita Business Services Limited, a subsidiary undertaking. The Company then recognises a cost equal to its contribution payable for the period. The contributions payable by the participating entities are determined on the following basis:

The Capita DB Scheme provides benefits on a defined benefit basis funded from assets held in a separate trustee-administered fund.

- The Capita DB Scheme is a non-segregated scheme but there are around 200 different sections in the Scheme where each section provides benefits on a particular basis (some based on final salary, some based on career average earnings) to particular groups of employees.
- At each funding assessment of the Capita DB Scheme (carried out triennially), the contribution rates for those sections containing active members are calculated. These are then rationalised such that sections with similar employer contribution rates (when expressed as a percentage of pensionable pay) are grouped together and an average employer contribution rate for each of the rationalised groups calculated.
- The Company's contribution is consequently calculated by applying the appropriate average employer contribution rates to the pensionable pay of its employees participating in the Capita DB Scheme.

A full actuarial valuation of the Capita DB Scheme is carried out every three years by an independent actuary for the Trustee, with the last full valuation carried out at 31 March 2017. The purpose of that valuation is to design a funding plan to ensure that the pension scheme has sufficient assets available to meet future benefit payments, based on assumptions agreed between the Trustee and the Group. The 31 March 2017 valuation showed a funding deficit of £185m (31 March 2014: £1.4m). This equates to a funding level of 86.1% (31 March 2014: 99.8%). The principal employer has agreed to make additional contributions to the Capita DB Scheme totalling £176m over the period from November 2018 to the end of 2021 to address the deficit. The next full valuation is expected to be as at 31 March 2021. Note 32 of the Annual Report sets out more detail.

(g) Leasing commitments

Assets obtained under finance leases are capitalised in the balance sheet and depreciated over the shorter of the lease term and their useful economic lives.

The finance charges under finance leases and hire purchase contracts are allocated to accounting periods over the period of the lease and represent a constant proportion of the balance of capital repayments outstanding. Rentals due under operating leases are charged on a straight-line basis over the lease term.

(h) Deferred taxation

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- Except where the deferred tax liability arises from the initial recognition of goodwill.
- Except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.
- In respect of taxable temporary differences associated with investments in subsidiaries, except where the timing of the reversal of the temporary timing differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible differences and the carry-forward of unused tax assets and unused tax losses can be utilised, except where the deferred income tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction affects neither the accounting profit nor taxable profit or loss.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

(i) Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward exchange contract. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date or if appropriate at the forward contract rate. All differences are taken to the profit and loss account with the exception of differences on foreign currency borrowings, to the extent that they are used to finance or provide a hedge against foreign equity investments, which are taken directly to reserves together with the exchange difference on the carrying amount of the related investments.

(j) National Insurance on share option gains

National Insurance on outstanding share options at the year-end has been grossed up and shown as a provision and a receivable on the balance sheet.

(k) Financial instruments: disclosure and presentation

A separate note dealing with the disclosures of IFRS 7 has been included in the consolidated financial statements on pages 144–152.

Notes to the Company financial statements continued

1 Accounting policies continued

(l) Investments and other financial assets

Classification

Applicable from 1 January 2018, the Company classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through OCI or through profit or loss); and
- those to be measured at amortised cost.

The classification depends on the contractual terms of the cash flows.

For investments in equity instruments that are not held for trading, this will depend on whether the Company has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The Company reclassifies debt investments when and only when its business model for managing those assets changes.

Regular way purchases and sales of financial assets are recognised on trade date (that is, the date on which the Group commits to purchase or sell the asset). Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

Measurement

At initial recognition, the Company measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Debt instruments

Subsequent measurement of debt instruments depends on the cash flow characteristics of the asset. There are three measurement categories into which the Company classifies its debt instruments:

Amortised cost: Assets that are held for collection of contractual cash flows, where those cash flows represent solely payments of principal and interest, are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as a separate line item in the statement of profit or loss.

FVOCI: Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses, which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in other gains/(losses). Interest income from these financial assets is included in finance income using the effective interest rate method. Foreign exchange gains and losses are presented in other gains/(losses), and impairment expenses are presented as a separate line item in the statement of profit or loss.

FVPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within other gains/(losses) in the period in which it arises.

Equity instruments

The Company subsequently measures all equity investments at fair value. Where the cCmpany's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognised in profit or loss as other income when the Company's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognised in other gains/(losses) in the statement of profit or loss as applicable. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

Impairment

From 1 January 2018, the Company assesses, on a forward-looking basis, the expected credit losses associated with its debt instruments carried at amortised cost and FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

Accounting policies applied until 31 December 2017

The Company has applied IFRS 9 retrospectively, but has elected not to restate comparative information. As a result, the comparative information provided continues to be accounted for in accordance with the Company's previous accounting policy, as shown below:

All investments are initially recorded at their fair value. Subsequently they are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

Investment loans are measured at amortised cost using the effective interest method.

Available-for-sale financial assets are measured at their fair value with unrealised gains or losses being recognised directly in equity. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognised in the income statement.

Financial assets at fair value through the income statement (disclosed in investment income) include financial assets designated upon initial recognition as at fair value through the income statement.

Financial assets may be designated upon initial recognition as at fair value through profit or loss if the assets are part of a company's financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy.

1 Accounting policies continued

(m) Trade and other receivables

The Company assesses on a forward-looking basis the expected credit losses associated with its receivables carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. For trade receivables, the Company applies the simplified approach permitted by IFRS 9, resulting in trade receivables recognised and carried at original invoice amount less an allowance for any uncollectible amounts based on expected credit losses.

(n) Cash and cash equivalents

Cash and short-term deposits in the balance sheet comprise cash at bank and in hand and short-term deposits with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(0) Financial instruments

Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at their fair value less any directly attributable transaction costs.

After initial recognition, loans and borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the income statement over the period of the borrowings using the effective interest method.

Gains and losses are recognised in the income statement when the liabilities are derecognised, as well as through the amortisation process.

Derivative financial instruments

Derivative financial instruments are used to manage exposure to the financial risks of changes in foreign exchange rates and interest rates. The principal derivative instruments used by the Company are foreign currency swaps, interest rate swaps and foreign exchange forward contracts. The Company does not hold or issue derivative financial instruments for trading or speculative purposes.

Derivatives are initially recognised at fair value on the date that a derivative contract is entered into, and they are subsequently re-measured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. The Company designates certain derivatives as either:

- hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedges); or
- hedges of a particular risk associated with the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges).

At inception of the hedge relationship, the Company documents the economic relationship between hedging instruments and hedged items, including whether changes in the cash flows of the hedging instruments are expected to offset changes in the cash flows of hedged items. The Company documents its risk management objective and strategy for undertaking its hedge transactions.

In relation to fair value hedges (for example, receive fixed and pay floating interest rate swaps held as fair value hedges against fixed interest rate borrowings) which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement.

In relation to cash flow hedges, the effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in the cash flow hedge reserve within equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement, within other gains/(losses).

When forward contracts are used to hedge forecast transactions, the Company generally designates only the change in fair value of the forward contract related to the spot component as the hedging instrument. Gains or losses relating to the effective portion of the change in the spot component of the forward contracts are recognised in the cash flow hedge reserve within equity. The change in the forward element of the contract that relates to the hedged item ('aligned forward element') is recognised the income statement at the same time as the hedged transaction. For some hedge relationships, the Company may designate the full change in fair value of the forward contract (including forward points) as the hedging instrument. In such cases, the gains or losses relating to the effective portion of the change in fair value of the entire forward contract are recognised in the cash flow hedge reserve within equity.

Amounts accumulated in equity are reclassified in the periods when the hedged item affects profit or loss, as follows:

- Where the hedged item subsequently results in the recognition of a non-financial asset, both the deferred hedging gains and losses and the deferred forward points, if any, are included within the initial cost of the asset. The deferred amounts are ultimately recognised in the income statement, since the hedged item affects the income statement.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognised in equity are transferred to the income statement. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction or firm commitment occurs.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the income statement and are presented as non-adjusting.

Notes to the Company financial statements continued

1 Accounting policies continued

(p) Share-based payments

The Company operates a number of executive and employee share schemes.

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, the number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the profit and loss account, with a corresponding entry in equity.

Subsidiary undertakings of the Company reimburse the Company through the intercompany account for charges attributable to their employees participating in the Company's share schemes.

2 Deferred taxation

	2018 £m	2017 £m
The deferred taxation included in the balance sheet is as follows:		
Accelerated capital allowances	**0.6**	(2.2)
Losses	**3.4**	—
Provisions	**2.0**	4.1
Included in debtors (note 9)	**6.0**	1.9

3 Loss attributable to members of the parent company undertaking

The loss after taxation dealt with in the accounts of the parent company undertaking was £120.1m (2017: profit of £440.5m).

4 Dividends

	2018 £m	2017 £m
Declared and paid during the year		
Ordinary shares (equity):		
Final for 2017 paid: nil per share (2016: 20.6p per share)	**—**	137.1
Interim for 2018 paid: nil per share (2017: 11.1p per share)	**—**	73.9
	—	211.0
Proposed for approval at AGM (not recognised as a liability at 31 December)		
Ordinary shares (equity):		
Final for 2018: nil per share (2017: nil per share)	**—**	—

5 Intangible assets

	Capitalised software development £m	Other intangibles £m	Total £m
Cost			
1 January 2018	0.6	30.1	30.7
Additions	**36.6**	**—**	**36.6**
Retirement	**—**	**(0.2)**	**(0.2)**
31 December 2018	**37.2**	**29.9**	**67.1**
Amortisation			
1 January 2018	—	1.0	1.0
Charge for year	**0.3**	**2.8**	**3.1**
Retirement	**—**	**(0.2)**	**(0.2)**
31 December 2018	**0.3**	**3.6**	**3.9**
Net book value at:			
1 January 2018	0.6	29.1	29.7
31 December 2018	**36.9**	**26.3**	**63.2**

Other intangibles relates to software purchased from third parties.

6 Tangible fixed assets

	Computer equipment £m	Short-term leasehold improvements £m	Total £m
Cost			
1 January 2018	25.5	0.3	25.8
Additions	**0.8**	**12.1**	**12.9**
Asset retirements	**(1.1)**	**(0.1)**	**(1.2)**
31 December 2018	**25.2**	**12.3**	**37.5**
Depreciation			
1 January 2018	6.9	0.3	7.2
Charge for year	**4.1**	**0.5**	**4.6**
Asset retirements	**(1.1)**	**(0.1)**	**(1.2)**
31 December 2018	**9.9**	**0.7**	**10.6**
Net book value at:			
1 January 2018	18.6	—	18.6
31 December 2018	**15.3**	**11.6**	**26.9**

7 Financial assets

Current	**2018 £m**	2017 £m
Cash flow hedges	**5.0**	4.0
Non-designated foreign exchange forwards and swaps	**2.1**	4.1
	7.1	8.1

8 Investments

Fixed asset investments

	Shares in subsidiary undertakings £m
Cost	
1 January 2018	220.2
Additions1	**287.7**
31 December 2018	**507.9**

1 During the year ended 31 December 2018, Capita plc invested a further £180.0m and £107.7m in Capita Life & Pensions Regulated Services Limited and Capita International Limited, respectively.

Direct investments	Registered office	Proportion of nominal value of issued shares held by the Company
Capita Legal Services Limited[2]	30 Berners Street, London, England, W1T 3LR	100%
Capita Financial Services Holdings Limited[1]	30 Berners Street, London, England, W1T 3LR	100%
Capita Group Insurance PCC Limited[2]	Maison Trinity, Trinity Square, St. Peter Port, Guernsey, GY1 4AT, Guernsey	100%
Capita Gwent Consultancy Limited[2]	St David'S House Pascal Close, St. Mellons, Cardiff, CF3 0LW	51%
Capita Holdings Limited[1]	30 Berners Street, London, England, W1T 3LR	100%
Capita International Limited[2]	30 Berners Street, London, England, W1T 3LR	100%
Capita Life & Pensions Regulated Services Limited[2]	30 Berners Street, London, England, W1T 3LR	100%
SIMS Holdings Limited[2]	30 Berners Street, London, England, W1T 3LR	0.001%
Capita Life & Pensions Services Limited[2]	30 Berners Street, London, England, W1T 3LR	100%

1 Investing holding company.
2 Outsourcing services company.

On 13 November 2018, the direct investment in Brokers Educational Supply Teachers Underwriting Agency Limited was dissolved.

Certain subsidiaries of the Group have opted to take advantage of a statutory exemption from having an audit in respect of their individual statutory accounts. Strict criteria must be met for this exemption to be taken and has been agreed to by the Directors of those subsidiary entities. Listed in note 18 to the Company financial statements are subsidiaries controlled and consolidated by the Group, where the Directors have taken advantage of the exemption from having an audit of the entities' individual financial statements for the year ended 31 December 2018 in accordance with Section 479A of The Companies Act 2006.

In order to facilitate the adoption of this exemption, Capita plc, the parent company of the subsidiaries concerned, undertakes to provide a guarantee under Section 479C of the Companies Act 2006 in respect of those subsidiaries.

Details of all indirect subsidiaries, as required under Section 409 of the Companies Act 2006, are reported in note 18 to the Company financial statements.

Notes to the Company financial statements continued

9 Debtors

Debtors due within 1 year	2018 £m	2017 £m
Amounts owed by subsidiary undertakings	**969.5**	992.7
Trade receivables	**1.3**	—
Taxation recoverable	**30.6**	15.3
Other debtors	**0.9**	4.9
Other taxes and social security	**3.7**	4.3
Other debt securities held – current	**1.3**	5.0
Interest rate swaps	**0.6**	—
Currency swap – USD private placement loan notes	**9.3**	72.2
Prepayments and accrued income	**7.8**	5.1
	1,025.0	1,099.5

Debtors due after more than 1 year	2018 £m	2017 £m
Prepayments and accrued income	**2.8**	1.7
Deferred taxation	**6.0**	1.9
Currency swaps	**93.8**	113.1
Interest rate swaps	**1.4**	5.4
Non-designated foreign exchange forwards and swaps	**1.8**	—
Cash flow hedges	**3.3**	7.4
	109.1	129.5

10 Creditors

Amounts falling due within 1 year	2018 £m	2017 £m
Amounts owed to subsidiary undertakings	**17.6**	72.8
Bank overdraft	**107.8**	161.8
Trade creditors	**15.6**	9.2
Other creditors	**2.6**	0.3
Accruals and deferred income	**38.1**	30.5
Cash flow hedges	**1.2**	1.9
Non-designated foreign exchange forwards and swaps	**1.4**	—
Other taxes and social security	**0.9**	—
	185.2	276.5

Provisions	2018 £m	2017 £m
At 31 December 2017	**130.4**	5.8
Reclassified from amounts falling due after more than 1 year	**0.6**	15.0
(Released)/provided in the year	**(13.2)**	107.2
Utilisation	**(89.4)**	(2.6)
Intra-group transfer	**—**	5.0
At 31 December 2018	**28.4**	130.4

The majority of the provisions relate to the claim and litigation provision (£16.4m) and business exit provision (£8.4m). Further detail on these provisions can be found in note 25 to the consolidated financial statements.

Amounts falling due after more than 1 year	2018 £m	2017 £m
Private placement loan notes	**226.5**	271.8
Currency swap	**3.4**	8.5
Cash flow hedges	**—**	1.1
	229.9	281.4

The private placement loan notes are unsecured. The bank overdraft is guaranteed by cash held by other members of the Group.

11 Deferred taxation

	£m
At 1 January 2018	1.9
Deferred tax movement in the year	**4.1**
At 31 December 2018 – included in debtors (note 9)	**6.0**

12 Share capital

Allotted, called up and fully paid	**2018 m**	2017 m	**2018 £m**	2017 £m
Ordinary shares of 21/15p each				
At 1 January	**670.1**	670.1	**13.8**	13.8
Rights issue	**1,001.0**	—	**20.7**	—
At 31 December	**1,671.1**	670.1	**34.5**	13.8

In May 2018, the Group offered a rights issue to existing shareholders on the basis of 3 shares for every 2 fully paid ordinary shares held. The issue was fully subscribed and resulted in the issue of 1,001,032,281 ordinary shares at £0.70 per share.

Share premium	**2018 £m**	2017 £m
Ordinary shares of 21/15p each		
At 1 January	**501.3**	501.3
Rights issue	**642.0**	—
At 31 December	**1,143.3**	501.3

The rights issue raised gross funds of £700.7m. The total amount capitalised to share capital and share premium was £662.7m (£700.7m less issuance costs of £38.0m).

Treasury shares	**2018 m**	2017 m	**2018 £m**	2017 £m
Ordinary shares of 2 1/15p				
At 1 January	**2.9**	3.2	**(0.1)**	(0.1)
Shares allotted in the year	**—**	(0.3)	**—**	—
At 31 December	**2.9**	2.9	**(0.1)**	(0.1)

In 2018, the Group made no purchases of shares into Treasury and allotted 28,057 (2017: 283,281) shares with an aggregate nominal value of £580 (2017: £4,420). The total consideration received in respect of these shares was £nil (2017: £nil).

Employee benefit trust shares	**2018 m**	2017 m	**2018 £m**	2017 £m
Ordinary shares of 2 1/15p				
At 1 January	**1.6**	1.7	**(0.1)**	(0.1)
Shares allotted in the year	**—**	(0.1)	**—**	—
Shares acquired during the year	**10.4**	—	**(11.0)**	—
At 31 December	**12.0**	1.6	**(11.1)**	(0.1)

The Group will use shares held in the employee benefit trust (EBT) in order to satisfy future requirements for shares under the Group's share option and long-term incentive plans. During the year, the EBT allotted 32,367 (2017: 69,337) ordinary 2 1/15p shares with an aggregate nominal value of £669 (2017: £1,434) to satisfy exercises under the Group's share option and long-term incentive plans. The total consideration received in respect of these shares was £nil (2017: £nil). The Group acquired 3.2m (2017: nil) ordinary 2 1/15p shares paying average market price of £1.87 per share with the total value of £6.0m (2017: £nil). Further, the Group exercised its rights under the rights issue, purchasing 7.2m of shares at £0.70 per share, paying £5.0m. The aggregate value of shares were transferred to the EBT.

The Group has an unexpired authority to re-purchase up to 10% of its issued share capital.

Notes to the Company financial statements continued

13 Commitments and contingent liabilities

(a) At 31 December 2018, the Company was committed to making the following payments under non-cancellable operating leases and other agreements:

	2018 £m	2017 £m
Not later than 1 year	**0.1**	0.1
Later than 1 year but not more than 5 years	**—**	0.1
Over 5 years from the balance sheet date	**—**	—
	0.1	0.2

(b) The Company has a committed Revolving Credit Facility amounting to £600.0m (2017: £600.0m), of which £nil had been drawn down at 31 December 2018 (2017: £nil drawn down).

(c) The Company has provided, through the normal course of its business, performance bonds and bank guarantees of £84.0m (2017: £88.4m).

14 Borrowings

	2018 £m	2017 £m
Private placement loan notes	**226.3**	271.8

	2018 £m	2017 £m
Repayments fall due as follows:		
Within 1 year	**—**	—
After more than 1 year:		
In more than 1 year but not more than 2 years	**—**	—
In more than 2 years but not more than 5 years	**172.9**	219.1
In more than 5 years	**53.4**	52.7
Total borrowings	**226.3**	271.8

The Company has issued guaranteed unsecured private placement loan notes as follows:

	Interest rate (%)	Denomination	EUR (m)	Maturity
Issued 2015				
Fixed rate bearer notes	2.125	EUR	179.0	10 November 2022
Fixed rate bearer notes	2.875	EUR	60.0	10 November 2027
Schuldschein loan	2.125	EUR	16.0	10 November 2022
Total of euro denominated private placement loan notes			255.0	

All series are unsecured.

15 Related-party transactions

In the following, figures for purchases and sales are for transactions invoiced during the year inclusive of Value Added Tax where applicable. All transactions are undertaken at normal market prices.

During the year, the Company sold goods/services in the normal course of business to Urban Vision Partnership Limited for £0.1m (2017: £0.1m). The Company purchased goods/services in the normal course of business for £nil (2017: £nil). At the balance sheet date, the net amount receivable from Urban Vision Partnership Limited was £nil (2017: £nil).

During the year, the Company sold goods/services in the normal course of business to Entrust Support Services Limited for £0.6m (2017: £0.3m). The Company purchased goods/services in the normal course of business for £nil (2017: £nil). At the balance sheet date, the net amount receivable from Entrust Support Services Limited was £nil (2017: £nil).

During the year, the Company sold goods/services in the normal course of business to AXELOS Limited for £0.1m (2017: £0.2m). The Company purchased goods/services in the normal course of business for £nil (2017: £nil). At the balance sheet date, the net amount receivable from AXELOS Limited was £nil (2017: £nil).

During the year, the Company sold goods/services in the normal course of business to Capita Glamorgan Consultancy Limited for £0.1m (2017: £0.1m). The Company purchased goods/services in the normal course of business for £nil (2017: £nil). At the balance sheet date, the net amount receivable from Capita Glamorgan Consultancy Limited was £nil (2017: £0.1m).

During the year, the Company sold goods/services in the normal course of business to Fera Science Limited for £0.3m (2017: £1.8m). The Company purchased goods/services in the normal course of business for £0.1 (2017: £nil). At the balance sheet date, the net amount receivable from Fera Science Limited was £nil (2017: £1.5m).

16 Pension costs

The Company operates a defined contribution scheme.

The pension charge for the defined contribution scheme for the year was £2.4m (2017: £4.7m).

17 Share-based payments

The Company operates several share-based payment plans and details of the schemes are disclosed in note 28 of the Group's consolidated financial statements.

The Group recognised an expense for share-based payments in respect of employee services received during the year to 31 December 2018 of £3.4m (2017: £2.9m), all of which arises from equity-settled share-based payment transactions. The total Company expense, after recharging subsidiary undertakings, charged to the profit and loss account in respect of share-based payments was £1.3m (2017: £1.2m).

Notes to the Company financial statements continued

18 Indirect investments

Unless otherwise indicated, all shareholdings comprise ordinary shares, are owned indirectly by the Company and represent 100% of the issued share capital of the subsidiary. Dormant companies are marked (D). Companies sold or dissolved since 31 December 2018 are marked *. Companies are listed under their registered office address as at 31 December 2018.

Company Name	% ownership	Directly held by Capita plc	Share class
30, Berners Street, London, W1T 3LR, England			
ABS Network Solutions Ltd (application for strike off)			
Acutest Limited			
Aghoco 1005 Limited (application for strike off)			
Amity Communications Limited			
AMT-Sybex (Engineering) Limited (in liquidation)			
AMT-Sybex Limited			
Aspire Business Solutions Ltd			
Atlas Master Trust Trustee Limited			
AXELOS Limited	51%		(£0.01 Ordinary B)
BCS Design Ltd			
Beovax Computer Services Limited			
Booking Services International Limited			
Brentside Communications Limited			
BSI 360 Limited (application for strike off)			
BSI Group Limited			
BSI Holdings Limited (in liquidation)			
Call Centre Technology Limited			
Call Vision Technologies Ltd			
Capita (06243477) Limited (application for strike off)			
Capita (6588350) Limited			
Capita (Banstead 2011) Limited			
Capita (D1) Limited			
Capita 03075476 Limited			
Capita Aurora Limited			
Capita Building Standards Limited			
Capita Business Services Ltd			
Capita Commercial Insurance Services Limited			
Capita Consulting Limited (in liquidation)			
Capita Corporate Director Limited			
Capita Customer Management Limited			
Capita Customer Solutions (UK) Limited			
Capita Dubai Limited			
Capita Employee Benefits (Consulting) Limited			
Capita Employee Benefits Holdings Limited			
Capita Employee Benefits Limited			
Capita Employee Benefits Services Limited (in liquidation)			
Capita Financial Services Holdings Limited	100%	•	
Capita Financial Software Limited (application for strike off)			
Capita Glamorgan Consultancy Limited			
Capita GMPS Trustees Limited			
Capita Grosvenor Limited			
Capita Group Secretary Limited			
Capita Hartshead Benefit Consultants Limited (in liquidation)			
Capita Hartshead Consultancy Services Limited (in liquidation)			
Capita Health Holdings Limited			
Capita Health and Wellbeing Limited			
Capita IB Solutions (UK) Limited			
Capita Information Limited (in liquidation)			
Capita Insurance Services Group Limited			
Capita Insurance Services Holdings Limited			
Capita Insurance Services Limited			
Capita Intelligent Building Infrastructure Services Limited			
Capita International Retirement Benefit Scheme Trustees Limited			
Capita IT Services (BSF) Holdings Limited			
Capita IT Services Holdings Limited			
Capita Justice & Secure Services Holdings Limited			
Capita Land Limited			
Capita Legal Services Limited	100%	•	
Capita Life & Pensions Regulated Services Limited	100%	•	
Capita Life & Pensions Services Limited	100%	•	
Capita Managing Agency Limited			
Capita Mortgage Administration Limited			
Capita Mortgage Software Solutions Limited			
Capita Property and Infrastructure (Structures) Limited			
Capita Property and Infrastructure Holdings Limited			
Capita Property and Infrastructure International Holdings Limited			
Capita Property and Infrastructure International Limited			
Capita Property and Infrastructure Limited			
Capita Property and Planning Limited (in liquidation)			
Capita Resourcing Limited			
Capita Retail Financial Services Limited			

Company Name	% ownership	Directly held by Capita plc	Share class
Capita Secure Information Solutions Limited			
Capita Secure Resource Solutions Limited			
Capita SIP Services Limited			
Capita Southampton Limited			
Capita Symonds (Asia) Limited			
Capita Symonds (Health & Safety) Limited (application for strike off)			
Capita Translation and Interpreting Limited			
Capita Travel & Events Holdings Limited			
Capita Travel and Events Limited			
Capita Treasury Services Limited			
Capita Wealth and Distribution Services Limited			
Capita Workforce Management Solutions Limited			
Capita Workplace Technology Limited			
Cardiff Research Consortium (HOG) Limited			
Clinical Solutions Acquisition Limited			
Clinical Solutions Holdings Limited			
Clinical Solutions IP Limited			
CMGL Group Limited			
CMGL Holdings Limited			
Complete Imaging Limited			
Complete Imaging Trustee Company Limited			
Computerland UK Limited			
Contact Associates Limited			
CPLAS Trustees Limited			
Data Mail Systems Limited			
Data Equipment Limited			
Design & Manage Europe Limited	50%		
E.B. Consultants Limited			
Eastgate Insurance Market Solutions Limited			
Eclipse (Hardware) Limited			
Electra-Net (UK) Limited			
Electra-Net Group Limited			
Electra-Net Holdings Limited			
Elsworth Sykes Northern Limited			
Elsworth Sykes Partnership Limited			
Emercom Ltd			
Entrust Education Services Limited			
Equitable Holdings Limited			
ESA Design Limited (in liquidation)			
ESPM Project Management Limited			
Euristix (Holdings) Limited			
Evolvi Rail Systems Limited			
Expotel Hotel Reservations Limited			
Fera Science Limited	75%		(£1.00 Ordinary B)
Fire Service College Limited			
First Retail Finance Limited			

Company Name	% ownership	Directly held by Capita plc	Share class
FirstAssist Services Limited			
Fish Financial Solutions Limited			
Fortek Computers Limited			
FPS Group of Companies Limited			
G2G3 Digital Limited			
G L Hearn Limited			
G L Hearn Management Limited			
Gissings Trustees Limited			
Grosvenor Career Services Limited			
Hallco 1626 Limited			
IBS Opensystems (UK) Limited			
International Reservations Limited			
International Travel Group Limited			
ITR International Translation Resources Limited			
John Crilley Limited			
Knowledgepool Group Limited			
Latemeetings.com Limited			
Leadcall Limited			
Liberty Communication Services Ltd.			
Liberty Printers (Ar And Rf Reddin) Limited			
Lovejoy Partnership Limited (in liquidation)			
Madagans Limited			
Magnos (Holdings) Limited			
Market Mortgage Limited	50%		£0.001 Ordinary Capita Shares
Medicals Direct International Limited			
Metacharge Limited			
Micro Librarian Systems Holdings Limited			
Micro Librarian Systems Limited			
Multi-Tech Contracts Limited			
NB Real Estate Group Limited (in liquidation)			
NB Real Estate Holdings Limited (in liquidation)			
Network Technology Solutions (UK) Limited			
NIS Europe Limited (application for strike off)			
Nova Bidco Limited			
Nova Midco Limited			
NYS Corporate Ltd.			
NYS Holdings Limited			
Octal Business Solutions Limited			
Optilead Limited			
Orange Bus Limited			
Pay360 Limited			
RE (Regional Enterprise) Limited	51%		(£1.00 Ordinary A)
RE Ltd			

Notes to the Company financial statements continued

Company Name	% ownership	Directly held by Capita plc	Share class
Red Procurement and Business Systems Ltd (application for strike off)			
Repair Management Services Limited (application for strike off)			
Resource Management Limited			
Retain International (Holdings) Limited			
Retain International Limited			
Right Document Solutions Holdings Limited			
Right Document Solutions Limited (in liquidation)			
S3dc Limited			
Sbj Benefit Consultants Limited			
Sbj Professional Trustees Limited			
Security Watchdog Limited			
Sigma Seven Limited			
SIMS Holdings Limited	100%	•	
SIMS Limited			
Smart DCC Limited			
Smart Public Limited			
Smiths Consulting Limited (application for strike off)			
Solid State Solutions Limited			
STL Technologies Limited			
Synaptic Software Limited			
Synetrix (Holdings) Limited			
Synetrix Limited			
Tascor E & D Services Limited			
Tascor Services Limited			
Tempus Finance Limited			
The Royal Borough Of Kensington And Chelsea Assured Homes Limited (in liquidation)			
Thirty Three Group Limited			
Trustmarque Solutions Limited			
Updata Infrastructure (North) Limited (application for strike off)			
Updata Infrastructure (UK) Limited			
Updata Infrastructure 2012 Limited			
Ventura (UK) India Limited			
Venues Event Management Limited			
Vision 2 Learn Limited			
Voice Marketing Limited			
Western Mortgage Services Limited			
Westpoint Limited			
Woolf Limited			
33/34 Winckley Square, Preston, Lancashire, PR1 3EL			
Akinika Debt Recovery Limited			
Akinika Limited			
Akinika UK Limited			
Legal & Trade Collections Limited (D)			
9 Bonhill Street, London, EC2A 4DJ			
Cobalt Insurance Holdings Limited	24.60%		

Company Name	% ownership	Directly held by Capita plc	Share class
Civic Centre, Chorley Road, Swinton, M27 5AS			
Urban Vision Partnership Limited	50.10%		(£1.00 Ordinary-b)
Daisy House Suite 1, Lindred Road Business Park, Nelson, Lancashire, BB9 5SR			
Daisy Updata Communications Limited	50%		(£1.00 Ordinary B)
Exchange House, 1 Radian Court, Knowlhill, Milton Keynes, MK5 8PJ			
NB Real Estate Limited (In Liquidation)			
Floor 2, Ibex House, 42-47 Minories, London, EC3N 1DY			
Cost Advocates Limited			
Hepworth House, Claypit Lane, Leeds, LS2 8AE			
Optima Legal Services Limited			
Mr S Fisher, The Grange, Bishops Cleeve, Cheltenham, Gloucestershire, GL52 8YQ			
Cobex Corporate Member No. 1 Limited	50.10%		
5th Floor, Fort Dunlop, Fort Parkway, Birmingham, B24 9FD			
Capita Birmingham Limited (previously Service Birmingham Limited)			
The Riverway Centre, Riverway, Stafford, ST16 3TH			
Entrust Support Services Limited	51%		(£1.00 Ordinary-X)
Unit 8, Wessex Park, Bancombe Road Trading Estate, Somerton, Somerset, TA11 6SB			
Ross & Roberts Limited			
The Courtyard Shoreham Road, Upper Beeding, Steyning, West Sussex, BN44 3TN, England			
Munnypot Limited	14.88%		
42/44 Henry Street, Northampton, Northamptonshire, NN1 4BZ			
Equita Limited			
1 More London Place, London, SE1 2AF			
Inventures Limited (in liquidation)			
Myshares Limited (in liquidation)			
Sector Holdings Limited (in liquidation)			
Westhill Consulting Limited (in liquidation)			
PIFC Consulting Limited (in liquidation)			
4th Floor, Park Gate 161-163, Preston Road, East Sussex, Brighton, BN1 6AF			
Premier Medical Holdings Limited (D)	19.90%		(£1 Ordinary A)
Pavilion Building, Ellismuir Way, Tannochside Park, Uddingston, Glasgow, G71 5PW			

Company Name	% ownership	Directly held by Capita plc	Share class
Barrachd Intelligence Solutions Limited			
Barrachd Limited			
Capita IT Services Limited			
Capita Scotland (Pension) Limited Partnership			
Capita Scotland General Partner (Pension) Limited			
Capita Secure Mobile Solutions Limited			
G2G3 Propulsion Ltd.			
Opin Systems Limited			
24 Blythswood Square, Glasgow, G2 4BG			
Sp Collect Ltd			
Stirling Park LLP			
The Beacon, 176 St Vincent Street, Glasgow, G2 5SG			
Capita Mclarens Limited			
Hillview House, 61 Church Road, Newtownabbey, Co Antrim, BT36 7LQ			
AMT-Sybex (Ni) Limited			
AMT-Sybex Holdings Limited			
Capita Managed IT Solutions Limited			
St David's House, Pascal Close, St Mellons, Cardiff, CF3 0LW			
Capita Gwent Consultancy Limited	51%	•	(£0.01 Preference)
Bedford House, 16 Bedford Street, Belfast, Co Antrim, BT2 7DT			
Learnserve Limited			
2 Grand Canal Square, Grand Canal Harbour, Dublin 2, Ireland			
AMT Group Limited			
AMT-Sybex (I) Limited			
AMT-Sybex (Managed Services) Limited			
AMT-Sybex (Research) Limited			
AMT-Sybex (Software) Limited			
AMT-Sybex Group Limited			
Capita Business Support Services Ireland Limited			
Capita IB Solutions (Ireland) Limited			
Dupree Holdings Limited			
Marrakech (Ireland) Limited			
Marrakech Limited			
Rathcush Limited			
Vilanova Management Limited			
Wabowden Limited			
Unit B, West Cork Technology Park, Clonakilty, Cork, Ireland			
Capita Customer Solutions Limited			
Montague House, Adelaide Road, Dublin 2, Ireland			
Capita Life and Pensions Services (Ireland) Limited	0.001% (99.999% held by a subsidiary)	•	

Company Name	% ownership	Directly held by Capita plc	Share class
12 Castle Street, St. Helier, JE2 3RT			
Capita Symonds (CI) Limited (in liquidation)			
Symonds Group (Jersey) Limited (in liquidation)			(£0.10 Ordinary-a, £0.10 Ordinary-b, £0.10 Ordinary-c)
Maison Trinity, Trinity Square, St. Peter Port, Guernsey, GY1 4AT			
Capita Group Insurance PCC Limited	100%	•	(£1 CG1, £1 CIC2, £1 Ordinary)
Clinch's House, Lord Street, Douglas, IM99 1RZ			
Capita Life and Pensions Services (Isle of Man) Limited			
Capita Services (Isle of Man) Limited			
33-37 Athol Street, Douglas, IM1 1LB, Isle Of Man			
Capita (Isle of Man) Limited (D)			
Deloitte Place, Mriehel ByPass, Mriehel, BKR 3000, Malta			
Capita Symonds (Malta) Limited (in liquidation)			
Käfertaler Str. 190, Mannheim, 68167, Germany			
adato GmbH			
Kelzstraße 21, Saalfeld, 07318, Germany			
3C DIALOG Saalfeld GmbH			
Kommandatenstrasse 22, Berlin, 10969, Germany			
Capita Customer Services (Germany) GmbH			
Capita rentable GmbH			
Capita Süd GmbH			
Capita West GmbH			
Nassauer Ring 39-41, Krefeld, 47803, Germany			
Capita Energie Services GmbH	74.90%		
20, Ostrower Damm, Cottbus, BB, 03046, Germany			
Capita Customer Services (Cottbus) GmbH			
75, Kaiserslauterer Strasse, Halle, 06128, Germany			
Capita Customer Services (Halle) GmbH			
82, Nachtweide, Magdeburg, 39124, Germany			
Capita Customer Services (Magdeburg) GmbH			
21/9, Warszawska Street, 40-009, Katowice, Poland			
ESA spółka z ograniczoną odpowiedzialnością w likwidacji – in liquidation			
Centrum Biurowe Lubicz I,ul. Lubicz 23, 31–503, Krakow, Poland			

Notes to the Company financial statements continued

Company Name	% ownership	Directly held by Capita plc	Share class
Capita (Polska) Spółka z ograniczoną odpowiedzialnoscią			
Hardturmstrasse 101, Zürich, 8005, Switzerland			
TELAG AG			
Konstanzerstrasse 17, Tägerwilen, 8274, Switzerland			
Capita Customer Services AG			
Plant 6, Gate No.2, Godrej & Boyce Complex, Pirojshahnagar, L.B.S Marg, Vikhroli (West), Maharashtra, Mumbai, 400079, India			
Capita India Private Limited			
Capita IT and Consulting India Private Limited			
Capita Offshore Services Private Limited	0.01% (99.99% held by a subsidiary)	•	
Capita SIMS (India) Private Limited			
Capita Symonds India Private Limited			
CS Clinical Solutions India Private Limited			
Wing 'C', Marisoft Annex, Vadgaon sheri, Kalyani Nagat, Maharashtra, Pune, 411014, India			
Ventura (India) Private Limited			
Themistokli Dervi, 3, Julia House, P.C. 1066, Nicosia, Cyprus			
Capita Cyprus Holdings Limited			
Capita Cyprus Limited			
9, Allee Scheffer, L-2520, Luxembourg			
CAPITA (Luxembourg) s.a r.l			
Level No. 3, Gate Village 7, Dubai International Finance Centre, Dubai, PO BOX 49983			
Capita (Dubai FZ) Limited			
1004 Bin Hamoodah Building, Khalifa St., PO Box 113 740, Abu Dhabi			
Capita Property and Infrastructure Consultants LLC	49%		
8th Floor, Union Castle Building, 55 St Georges Mall, Cape Town, 8001, South Africa			
Capita (South Africa) (Pty) Limited			
Full Circle Contact Centre Services (Proprietary) Limited			
Room 615 Zhucheng Building, No Jia 6 Zhongguancun South Street, Beijing 100086, Haidian District, China			
Symonds Project Management Consultancy (Beijing) Ltd			
Suite 4301-5, Tower One Times Square, 1 Matheson Street, Causeway Bay, Hong Kong			
Symonds Travers Morgan (Hong Kong) Limited			
1603 C.C Wu Building, 302-308 Hennessy Road, Wan Chai, Hong Kong			

Company Name	% ownership	Directly held by Capita plc	Share class
Capita IB Solutions (HK) Limited			
803, Manning House, 38 Queen's Road Central, Hong Kong			
ThirtyThree APAC Limited			
Landmark Virtual Offices, Africa Re Building - Plot 1679, Karimu Kotun Street, Lagos, Victoria Island, Nigeria			
Capita Norman + Dawbarn Limited	97.30%		
850 New Burton Road, Suite 201, Dover DE 19904, USA			
Capita (USA) Holdings Inc.			
Capita Business Services (USA) LLC			
Capita CTI (USA) LLC			
Capita Software (US) LLC			
Optilead Inc.			
ThirtyThree USA Inc.			
Corporation Service Company 2711, Centerville Road, Suite 400, Wilmington, County of Newcastle DE 19808, USA			
CAS Services US Inc			
Clinical Solutions Group (International) LLC			
Corporation Trust Centre, 1209 Orange Street, Wilmington, New Castle DE 19801, USA			
Capita Translation and Interpreting LLC			
Suite 13.03, 13th Floor, Menara Tan & Tan, 207 Jalan Tun Razak, 50409 Kuala Lumpur, Malaysia			
Symonds Travers Morgan (Malaysia) SDN. BHD			
Alameda dos Guaramomis, no 930, 1st Floor, Suite 01, Bairro, Moema, CEP 04076-011, Brazil			
Eureka Asessoria Empresarial Ltda	49.90%		
King Abdul Aziz Street, PO Box 7052, Dammam, Saudi Arabia			
Capita Symonds Property and Infrastructure Consultants (KSA) (Capita Saudi Arabia)	50%		

Listed below are subsidiaries controlled and consolidated by the Group, where the Directors have taken the exemption from having an audit of its financial statements for the year ended 31 December 2018. This exemption is taken in accordance with Companies Act Section 479A.

Company Name	%	Registered Office	Company registration	Location	Held directly by Capita plc	Share Class
Brightwave Enterprises Limited	100%	30 Berners Street, London, England, W1T 3LR	7066783	UK		
Brightwave Holdings Limited	100%	30 Berners Street, London, England, W1T 3LR	7462788	UK		
Brightwave Limited	100%	30 Berners Street, London, England, W1T 3LR	4092349	UK		
Capita Gas Registration and Ancillary Services Limited	100%	30 Berners Street, London, England, W1T 3LR	5078781	UK		
Capita HCH Limited	100%	30 Berners Street, London, England, W1T 3LR	2384029	UK		
Capita HELM Corporation Limited	100%	Beacon House, 27 Clarendon Road, Belfast, BT1 3PR	NI025165	UK		
Capita IT Services (BSF) Limited	100%	30 Berners Street, London, England, W1T 3LR	1855936	UK		
Cardiff Research Consortium Limited	100%	30 Berners Street, London, England, W1T 3LR	3962364	UK		
CCSD Services Limited	100%	30 Berners Street, London, England, W1T 3LR	5399460	UK		
CHKS Limited	100%	30 Berners Street, London, England, W1T 3LR	2442956	UK		
Clinical Solutions Finance Limited	100%	30 Berners Street, London, England, W1T 3LR	5337592	UK		
Clinical Solutions International Limited	100%	30 Berners Street, London, England, W1T 3LR	4394761	UK		
Creating Careers Limited	100%	30 Berners Street, London, England, W1T 3LR	03885966	UK		
Cymbio Limited	100%	30 Berners Street, London, England, W1T 3LR	6462086	UK		
Debt Solutions (Holdings) Limited	100%	33-34 Winckley Square, Preston, Lancashire, PR1 3EL	3673307	UK		
Euristix Limited	100%	30 Berners Street, London, England, W1T 3LR	05420948	UK		
Health Analytics Limited	100%	30 Berners Street, London, England, W1T 3LR	6947862	UK		
Marrakech (U.K.) Limited	100%	30 Berners Street, London, England, W1T 3LR	3785263	UK		
PageOne Communications Limited	100%	30 Berners Street, London, England, W1T 3LR	4560277	UK		
Pervasive Limited	100%	30 Berners Street, London, England, W1T 3LR	5679204	UK		
Pervasive Networks Limited	100%	30 Berners Street, London, England, W1T 3LR	3429318	UK		
SDP Regeneration Services 2 Limited	100%	30 Berners Street, London, England, W1T 3LR	4626963	UK		
Smartpoint Limited	100%	30 Berners Street, London, England, W1T 3LR	2831803	UK		
Tempus Finance Limited	100%	30 Berners Street, London, England, W1T 3LR	6943069	UK		
The G2G3 Group Ltd.	100%	Pavilion Building, Ellismuir Way, Tannochside Park, Uddingston, Glasgow, G71 5PW	SC199414	UK		
The Write Research Company Limited	100%	30 Berners Street, London, England, W1T 3LR	04272836	UK		
Thirty Three LLP	100%	30 Berners Street, London, England, W1T 3LR	OC372712	UK		

Shareholder information

In this section we have provided you with some key information to manage your shareholding in Capita plc.

Useful websites

Capita (www.capita.com/investors)

Our corporate site is our main external communication channel where we showcase our services, solutions and innovations from across the wider Company. It also contains an investor section, where institutional and private shareholders can access the latest announcements, financial and statutory information and reports.

Shareholder portal (www.capitashares.co.uk)

Capita's register of shareholders is maintained by Link Asset Services. Our shareholder portal is a secure online site where you can manage your shareholding quickly and easily. You can manage many aspects, such as view your holding, update contact details, manage dividend payments, request to receive shareholder communications by email and register. To register you will need your investor code, which can be found on your share certificate or dividend confirmation.

e-communications

Help us communicate with you in a greener, more efficient and cost-effective way by switching from postal to email communications which means that we will notify you by email each time new shareholder communications have been placed on the Capita website.

Registering for e-communications is very straightforward. Go to our shareholder portal www.capitashares.co.uk. Further information about our shareholder portal is below.

Managing your shareholding

We aim to communicate effectively with our shareholders, via our website www.capita.com/investors. Shareholders who have questions relating to the Group's business or wish to receive further hard copies of annual reports should contact Capita's investor relations team on 020 7799 1525 or email: IRTeam@capita.co.uk.

If you have any queries about your shareholding or dividend payments please contact the Company's registrar, Link Asset Services:

Link Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

Email: enquiries@linkgroup.co.uk
Tel (UK): 0871 664 0300 (Calls cost 12p per minute plus your phone company's access charge)
(Overseas): +44 371 664 0300[1]

Lines are open between 9.00am – 5.30pm, Monday to Friday excluding public holidays in England and Wales.

Share dealing

A quick and easy share-dealing service is available for existing Capita shareholders to either sell or buy Capita plc shares online or by telephone.

For further information go to: www.linksharedeal.com or telephone +44 (0) 371 664 0445[1]. Lines are open between 8.00am - 4.30pm, Monday to Friday excluding public holidays in England and Wales.

If you have only a small number of shares which are uneconomical to sell, you may wish to donate them to charity free of charge through ShareGift (Registered Charity 1052686). Find out more at www.sharegift.org.uk or by telephoning 020 7930 3737.

1 Calls to 0871 numbers cost 12p per minute plus your phone company's access charge. Calls to 0371 numbers are charged at a standard geographic rate and will vary by provider. Calls outside the United Kingdom will be charged at the applicable international rate.

Company contact details

Registered office

Capita plc
30 Berners Street
London W1T 3LR
Tel: 020 7799 1525
Registered in England and Wales with registration number: 2081330

Investor Relations

IRTeam@capita.co.uk
Head of Investor Relations – Andrew Ripper

Company Secretariat

secretariat@capita.co.uk
Group Company Secretary – Francesca Todd

Company advisers

Independent auditor

KPMG LLP

Corporate brokers

Citi
Goldman Sachs

Bankers

Barclays Bank plc
National Westminster Bank plc

Corporate communications

Powerscourt

Registrars

Link Asset Services

Alternative performance measures

The Group presents various alternative performance measures (APMs) as the Directors believe that these are useful for users of the financial statements in helping to provide a balanced view of, and relevant information on, the Group's financial performance, position and cash flows. These APMs are mainly measures which disclose the 'adjusted' performance of the Group excluding specific items which are regarded as adjustments. Those items which relate to the ordinary course of the Group's operating activities remain within adjusted profit. The following items are excluded from adjusted profit: intangible amortisation, impairment of goodwill and acquired intangibles, acquisition contingent consideration movements, the financial impact of business exits or businesses in the process of being exited, acquisition expenses (if material), movements in the mark-to-market valuation of certain financial instruments, the impact of significant new contracts and restructuring (see below), and specific non-recurring items in the income statement. In the Directors' judgement, these need to be disclosed separately (see notes 3, 4, 5 and 9) by virtue of their nature, size and/or incidence, in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business.

In addition, the Group presents other APMs including key performance indicators (KPIs) such as return on capital employed and interest cover by which we monitor our performance and others such as organic and acquisition revenue growth which provide useful information to users which is not otherwise readily available from the financial statements.

APMs presented	2018	2017	% change	Source
Revenue – continuing operations				
Total revenue as reported	**£3,918.4m**	£4,234.6m	(7.5)%	Line item in income statement
Deduct: business exit	**(£50.8m)**	(£66.7m)		Line item in note 6
Deduct: business exited in 2018	**—**	(£76.1m)		Revenue from businesses exited in 2018
1. Adjusted revenue	**£3,867.6m**	£4,091.8m	(5.5)%	Adjusted revenue
Deduct: 2017 acquisitions	**(£2.8m)**	—		Additional contribution in 2018 of acquisitions acquired in 2017
2. Adjusted organic revenue	**£3,864.8m**	£4,091.8m	(5.4)%	Adjusted revenue excluding businesses exited and acquired
Prior year adjusted revenue on a like-for-like basis	**£4,091.8m**	—		From line 1 above
Total acquisitions	**£2.8m**	—		2017 acquisitions plus 2018 acquisitions
3. Growth from acquisitions	**0.1%**	—		Total acquisitions/Prior-year adjusted revenue on a like-for-like basis
Profit – continuing operations				
Operating profit as reported	**£34.9m**	(£420.1m)		Line item in income statement
Adjusting items in note 3	**£300.4m**	£867.6m		
4. Adjusted operating profit	**£335.3m**	£447.5m	(25.1)%	Line item in note 3
5. Adjusted operating margin [KPI]	**8.7%**	10.9%		Adjusted operating profit/adjusted revenue
Profit/(loss) before tax as reported [KPI]	**£272.6m**	(£513.1m)		Line item in income statement
Adjusting items in note 3	**£9.5m**	£896.2m		
6. Adjusted profit before tax [KPI]	**£282.1m**	£383.1m	(26.4)%	Line item in note 3
7. Adjusted earnings per share [KPI]	**16.37p**	27.99p	(41.5)%	Line item in income statement and note 11 - earnings per share

Alternative performance measures continued

		2018	2017	Source
Gearing				
Adjusted operating profit [1]		**£335.3m**	£447.5m	Line item in note 3
Add business exit – trading		**£16.8m**	£16.8m	Line item in note 3
Deduct: non-controlling interest		**(£12.5m)**	(£14.1m)	Underlying EBIT attributable to non-controlling
Deduct: acquisition costs		**£—m**	(£1.7m)	
Add back: share-based payment charge		**£3.4m**	£2.9m	Line item in note 28
Add back: non-current service pension charge		**£9.5m**	£0.8m	Line items in note 32
Add back: amortisation on purchased intangibles		**£27.8m**	£19.9m	Line item in note 7
Adjusted EBITA	a	**£380.3m**	£472.1m	
Add back: pre-acquisition underlying profit		**£—m**	£0.3m	Disclosure in note 16
Deduct business exit – trading		**(£19.7m)**	(£16.8m)	Note 4 - trading profit adjusted for business closure loss
Add back: depreciation		**£65.2m**	£63.5m	Line item in note 7
Covenant calculation - adjusted EBITDA	b	**£425.8m**	£519.1m	
8. Adjusted interest charge		**(£53.2m)**	(£64.4m)	Line item in note 9
Interest cost attributable to pensions		**£9.4m**	£9.2m	Line item in note 9
Cash flow hedges recycled to the income		**(£2.5m)**	—	Line item in note 9
Borrowing costs	c	**(£46.3m)**	(£55.2m)	
9. Interest cover [2]	a/c	**8.2x**	8.6x	Adjusted EBITA/Borrowing costs
Money Market Funds	d	**£—m**	£14.0m	
Net debt	e	**£466.1m**	£1,117.0m	Line information in note 29
Restricted cash [3]	f	**£28.6m**	£22.0m	Cash that may not be applied against net debt for covenant calculation purposes
Adjusted net debt	g = d+e+f	**£494.7m**	£1,153.0m	
10. Adjusted net debt to adjusted EBITDA ratio [KPI]	g / b	**1.2x**	2.2x	Adjusted net debt/adjusted EBITDA

1 Adjusted operating profit excludes items that are separately disclosed and considered to be outside the underlying operating results for the particular year under review and against which the Group's performance is assessed.
2 As noted in the Annual Report and Accounts 2017, on 20 April 2018, Capita agreed various amendments with the noteholders under its US private placement notes. This included the carve-out of up to £100m worth of bonds and guarantees from the definition of indebtedness. For covenant test purposes, this is effective from the 12-month period ended 30 June 2018, but for the Group's alternative performance measures, the comparatives have been restated to be presented on a consistent basis. In addition, the comparatives have been restated to include results of business exits during 2018.
3 Restricted cash includes cash held by FCA regulated entities, cash held in foreign bank accounts in Malaysia and Nigeria and distributable reserves in joint ventures which does not belong to Capita and is excluded from adjusted net debt.

		2018	2017	Source
ROCE				
Adjusted operating profit	a	**£335.3m**	£447.5m	Line item in note 3
Tax rate	b	**9.7%**	17.7%	Line item note 10
Tax	c = a x b	**£32.5m**	£79.2m	Adjusted profit multiplied by tax rate
Adjusted operating profit after tax	d = a - c	**£302.8m**	£368.3m	Adjusted profit less tax
Current year net assets/(liabilities)	e	**£103.3m**	(£929.8m)	Line in balance sheet
Current year adjusted net debt	f	**£464.1m**	£1,103.9m	Line item in note 29 – additional cash flow information, net debt excluding the impact of deferred consideration.
Adjustments to capital employed	g	**£1,276.5m**	£1,359.7m	Includes post-tax impact of accumulated acquired intangible amortisation, fixed rate swaps, put options and pensions
	m^1 = e+f+g	**£1,843.9m**	£1,533.8m	Used in 2018 average capital employed
Less acquisition spend in year	h	**—**	(£18.8m)	Consideration paid - cash acquired + debt acquired, per note 16
Current year capital employed	i = e+f+g+h	**£1,843.9m**	£1,515.0m	
Prior year net liabilities	j		(£552.9m)	
Prior year adjusted net debt	k		£1,682.9m	
Comparative prior year adjustments	l		£1,280.3m	Includes post-tax impact of accumulated acquired intangible amortisation, fixed rate swaps, put options and pensions
Prior year capital employed	m^2 = j+k+l		£2,410.3m	Used in 2017 average capital employed
Average capital employed pre-acquisitions	n = (i+m)/2	**£1,688.9m**	£1,962.7m	
Weighted average acquisition spend in year	o	**£—m**	£35.8m	Pro rata number of months post-acquisition (including contingent and deferred consideration payments)
Average capital employed	p = n+o	**£1,688.9m**	£1,998.5m	
15. ROCE [KPI]	q = d/p	**17.9%**	18.4%	

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