

# Directors' report

## Statutory information contained elsewhere in the Annual Report

Information required to be part of this Directors' report can be found elsewhere in the Annual Report as indicated in the table below, and is incorporated into this report by reference:

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Financial instruments: Information on the Group's financial risk management objectives and policies, and its exposure to credit risk, liquidity risk, interest rate risk and foreign currency risk	146 note 24
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Disclosure specifically required pursuant to the Companies (Miscellaneous Reporting) Regulations 2018 can be found on the following pages:

Statement in the Strategic Report of how Directors have complied with their duty to have regard to the matters in the 2006 Companies Act section 172(1) a – f	Page 52
Statement in the Directors' Report summarising how Directors have engaged with employees and taken account of their interests	Page 64
Statement in the Directors' Report about the corporate governance arrangements applied by the Company	Page 66
Publication of the ratio of the CEO's remuneration to the median, 25th and 75th quartile pay remuneration of their UK employees in the Directors' Remuneration report	Page 104
Illustration of the effect of future share price increases on executive pay outcomes in the Directors' Remuneration report	Page 85

## Management report

The Strategic report on pages 2 to 56 and the Directors' report, as detailed on pages 110 to 113, including information which has been incorporated into those sections by reference, comprise the management report specified by rules 4.1.5R (2) and 4.1.8R of the FCA's Disclosure Guidance and Transparency Rules (DTRs).

## Research and development

One of the Group's principal business streams is the provision of funded research and development (R&D) for customers. The Group also invests in the commercialisation of promising technologies across all areas of business.

In the financial year, the Group recorded £292.3m (2019: £298.9m) of total R&D-related expenditure, of which £270.8 m (2019: £272.9m) was customer-funded work and £21.5m (2019: £26.0m) was internally funded. Additionally, £2.1m (2019: £3.1m) of late-stage development costs were capitalised and £1.4m (2019: £1.1m) of capitalised development costs were amortised in the year.

## Political donations

QinetiQ does not make political donations to parties as that term would be commonly recognised. The legal definition of that term is, however, quite broad and may have the effect of covering a number of normal business activities that would not commonly be perceived to be political donations, such as sponsorship of events.

These may include legitimate interactions in making MPs and others in the political world aware of key industry issues and matters that affect QinetiQ, and that make an important contribution to their understanding of QinetiQ, the markets in which it operates and the work of their constituents.

## Branches

The Company and its subsidiaries have established branches in a number of different countries; their results are, however, not material to the Group's financial results.

## Share capital

As at 31 March 2020, the Company had an allotted and fully paid up share capital of 571,757,121 ordinary shares of 1p each with an aggregate nominal value of £5.7m and one Special Share with a nominal value of £1. The ordinary share total includes 3,794,743 shares held exclusive of voting rights in treasury and 595,063 shares held by employee share trusts.

Details of the shares in issue during the financial year are shown in note 26 on page 153.

## Rights of ordinary shareholders

The holders of ordinary shares are entitled to receive the Company's Reports and Accounts, to attend and speak at general meetings of the Company, to exercise voting rights in person or by appointing a proxy, and to receive a dividend where declared or paid out of profits available for that purpose. For the arrangements of this year's AGM, please see page 67 for further details.

## Rights of special shareholder

The Special Share is held by HM Government through the Secretary of State for Defence (the Special Shareholder) and it may only be held by and transferred to HM Government. It confers certain rights to protect UK defence and security interests. These include:

- The promotion and reinforcement of the MOD compliance principles which require QinetiQ to be an impartial, ethical and responsible contractor by avoiding conflicts of interest in its dealings with the MOD
- The protection of defined strategic assets of the Group, such as certain testing facilities, by providing the Special Shareholder with an option to purchase those assets in certain circumstances
- The right to require certain persons with a material interest in QinetiQ to dispose of some or all of their ordinary shares on the grounds of national security or conflict of interest
- A provisions whereby at least the Non-executive Chairman or Chief Executive Officer must be a British citizen.

The Special Share carries no financial and economic value and the Special Shareholder is not entitled to vote at a general meeting of the Company. At any time the Special Shareholder may require QinetiQ to redeem the share at par and, if wound up, the Special Shareholder would be entitled to be repaid at its nominal value before other shareholders. Any variation of the rights attached to the Special Share requires the written approval of the MOD. Further details can be found in note 26 on page 133.

## Restrictions on the transfer of shares

As detailed above, the special share requires certain persons with an interest in QinetiQ's shares that exceed certain prescribed thresholds to dispose of some or all of their ordinary shares on the grounds of national security or conflict of interest.

## Employee share schemes

The QinetiQ Group plc Employee Benefit Trust (the Trust) holds shares in connection with QinetiQ's employee share schemes, excluding the Share Incentive Plan. As at 31 March 2020, the Trust held 595,063 ordinary shares of 1p each (the Trust Shares). The Trustees of the Trust have agreed to waive their entitlement to dividends payable on the Trust Shares. The Trust holds further ordinary shares in respect of deferred shares held on behalf of participants in the Company's Deferred Annual Bonus Plan. Dividends received by the Trust in respect of the deferred shares are paid direct to the Plan participants on receipt and are not retained in the Trust.

Equiniti Share Plan Trustees Limited acts as Trustee in respect of all ordinary shares held by employees under the QinetiQ Group plc Share Incentive Plan (the Plan). Equiniti Share Plan Trustees Limited will vote on all resolutions proposed at general meetings in accordance with voting instructions received from participants in the Plan.

## Corporate sponsored nominee

In circumstances where ordinary shares are held by the corporate sponsored nominee service, Equiniti Corporate Nominees Limited will vote on all resolutions proposed at general meetings in accordance with voting instructions received from shareholders using such corporate nominee service.

## Major shareholdings

In accordance with DTR 5, the Company has been notified of the following from holders representing 3% or more of the issued ordinary share capital of the Company:

Name of shareholder	At 31 March 2020 % of issued share capital*	At 14 May 2020* % of issued share capital
Schroders	9.62%	9.62%
Majedie Asset Management Limited	5.03%	5.03%
Silchester International	4.96%	4.96%
Investec	4.95%	4.95%
Standard Life Aberdeen plc	4.81%	4.81%
Norges Bank	4.02%	3.99%

\* As notified by the shareholder and based on the issued ordinary share capital at the time of the notification.

## Employees

The Group is committed to the fair treatment of people with disabilities in relation to applications, training, promotion and career development. If an existing employee becomes disabled, the Company makes every effort to enable them to continue their employment and career development, and to arrange appropriate training, wherever practical.

## Directors' interests in contracts

At the date of this report, there is no contract or arrangement with the Company or any of its subsidiaries that is significant in relation to the business of the Group as a whole in which a Director of the Company is materially interested.

## Indemnities

The Company has entered into indemnity deeds with all its current Directors containing qualifying indemnity provisions, as defined in Section 234 of the Companies Act 2006, under which the Company has agreed to indemnify each Director in respect of certain liabilities, which may be attached to them as Directors or as former Directors of the Company or any of its subsidiaries. All such indemnity provisions are in force as at the date of this Directors' report. The Directors of QinetiQ Pension Scheme Trustee Limited, a Group company and the Trustee of the QinetiQ Pension Scheme (the Scheme), benefit from an indemnity contained in the rules of the Scheme. The indemnity would be provided out of the Scheme assets.

# Directors' report continued

## Change of control – significant agreements

The following significant agreements contain provisions entitling the counterparties to require prior approval, exercise termination, alteration or other similar rights in the event of a change of control of the Company, or if the Company ceases to be a UK company:

- The Combined Aerial Target Service contract is a 20-year contract awarded to QinetiQ by the MOD on 14 December 2006. The terms of this contract require QinetiQ Limited to remain a UK company which is incorporated under the laws of any part of the UK, or an overseas company registered in the UK, and that at least 50% of the Board of Directors are UK nationals. The terms also contain change of control conditions and restricted share transfer conditions which require prior approval from HM Government if there is a material change in the ownership of QinetiQ Limited's share capital, unless the change relates to shares listed on a regulated market; 'material' is defined as being 10% or more of the share capital. In addition, there are restrictions on transfers of shares to persons from countries appearing on the restricted list as issued by HM Government.
- The Long Term Partnering Agreement (LTPA) is a 25-year contract, which QinetiQ Limited signed on 28 February 2003, to provide test, evaluation and training services to the MOD. This contract contains conditions under which the prior approval of HM Government is required if the contractor, QinetiQ Limited, ceases to be a subsidiary of the QinetiQ Group, except where such change in control is permitted under the Shareholders Agreement to which the MOD is a party.
- The Company is party to a £275m multi-currency revolving credit facility, provided by a consortium of banks, that expires on 27 September 2024, with an option to extend to a final maturity to 27 September 2025. Under the terms of the facility, in the event of a change of control of the Company, any lender may give notice to cancel its commitment under the facility and require all outstanding amounts to be repaid.

The Directors' contracts contain no provisions for compensation for loss of office on a change of control of the Company.

## Disclosures in accordance with Listing Rule 9.8.4

There are no matters requiring disclosure under the FCA's Listing Rule 9.8.4, other than details of long-term incentive schemes, which are explained further on page 98.

## Articles of Association

Changes to the Articles must be submitted to shareholders for approval. Save in respect of the rights attaching to the Special Share, the Company has not adopted any special rules relating to the appointment and replacement of Directors or the amendment of the Company's Articles of Association, other than as provided under UK corporate law.

## Appointment and replacement of Directors

According to the Articles of Association, all Directors are subject to election by shareholders at the first AGM following their appointment, and to re-election thereafter at intervals of no more than three years. In line with best practice reflected in the Code, however, the Company requires each serving member of the Board to be put forward for election or re-election on an annual basis at each AGM.

## Powers of the Directors: allotment/purchase of own shares

At the Company's AGM held in July 2019, the shareholders passed resolutions which authorised the Directors to allot relevant securities up to an aggregate nominal value of £3,786,037 (£1,893,019 pursuant only to a rights issue), to disapply pre-emption rights (up to 5% of the issued ordinary share capital) and to purchase ordinary shares (up to 10% of the issued ordinary share capital). The authorities will remain valid until the 2020 AGM.

Resolutions in respect of the allotment of relevant securities, the disapplication of pre-exemption rights and the purchase of own shares will be laid before the 2020 AGM.

## Annual General Meeting

The Company's AGM will be held on Tuesday 14 July 2020 at 11.00am at Cody Technology Park, Ively Road, Farnborough, Hampshire GU14 0LX.

## Independent auditor

PwC has expressed its willingness to continue in office as independent auditor and a resolution to re-appoint them will be proposed at the AGM.

## Statement of Directors' responsibilities

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 'Reduced Disclosure Framework', and applicable law). 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 Company and of the profit or loss of the Group and Company for that period. In preparing the financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently
- State whether applicable IFRSs as adopted by the European Union have been followed for the Group financial statements and United Kingdom Accounting Standards, comprising FRS 101, have been followed for the Company financial statements, subject to any material departures disclosed and explained in the financial statements
- Make judgments and accounting estimates that are reasonable and prudent
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and company will continue in business.

The Directors are also responsible for safeguarding the assets of the Group and Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

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

### Directors' confirmations

The Directors consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group and Company's position and performance, business model and strategy.

Each of the Directors, whose names and functions are listed on pages 60 and 61 confirm that, to the best of their knowledge:

- The Company's financial statements, which have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 'Reduced Disclosure Framework', and applicable law), give a true and fair view of the assets, liabilities, financial position and profit of the Company
- The Group financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group
- The Directors' report includes a fair review of the development

and performance of the business and the position of the Group and Company, together with a description of the principal risks and uncertainties that it faces

- In the case of each Director in office at the date the Directors' report is approved
- So far as the Director is aware, there is no relevant audit information of which the Group and Company's auditors are unaware
- They have taken all the steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Group and Company's auditors are aware of that information.

### Scope of the reporting in this Annual Report

The Board has prepared a Strategic report which provides an overview of the development and performance of the Group's business in the year ended 31 March 2020.

For the purposes of DTR 4.1.5R(2) and DTR 4.1.8 the Directors' report, the Directors confirm that, so far as they are aware, there is no relevant audit information of which the Company's auditor is unaware, and that they have taken all steps that they ought to have taken as Directors to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

By order of the Board.

**Jon Messent**

**Company Secretary and Group General Counsel**

21 May 2020

# Independent auditors' report to the members of QinetiQ Group plc

## Report on the audit of the financial statements

### Opinion

In our opinion:

- QinetiQ Group plc's Group financial statements and Company financial statements (the 'financial statements') give a true and fair view of the state of the Group's and of the Company's affairs as at 31 March 2020 and of the Group's profit and cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 'Reduced Disclosure Framework', and applicable law); 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.

We have audited the financial statements, included within the Annual Report and Accounts (the 'Annual Report'), which comprise: the Consolidated and Company balance sheets at 31 March 2020; the Consolidated income statement and Consolidated comprehensive income statement, the Consolidated cash flow statement, and the Consolidated and Company statements of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ('ISAs (UK)') and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Independence

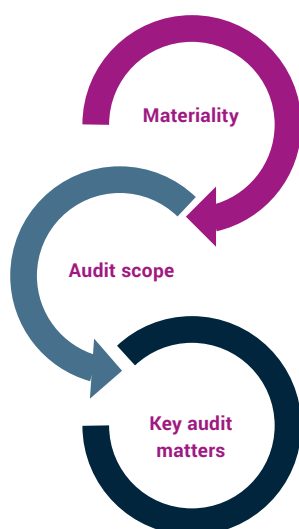
We remained independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Company.

Other than those disclosed in note 8 to the financial statements, we have provided no non-audit services to the Group or the Company in the period from 1 April 2019 to 31 March 2020.

### Our audit approach

#### Overview



- Overall Group materiality: £6.2 million (2019: £6.1 million), based on 5% of underlying profit before tax.
- Overall Company materiality: £4.8 million (2019: £4.8 million), based on 1% of total assets.
- We conducted full scope audit work in the UK over QinetiQ Limited, the main trading entity of the Group which provided significant coverage over all financial statement balances, except inventory. We performed a full scope financial statement line item audit over inventory balances at Foster Miller Inc. (QNA) and QinetiQ Target Systems Limited.
- We performed procedures over accounts receivable and accounts payable in Manufacturing Techniques Inc. (MTEQ).
- We performed procedures over revenue and associated balances in QNA.
- We performed procedures over goodwill, intangible assets, share-based payments, pensions, the implementation of IFRS 16, taxation and testing of the consolidation at a Group level.
- Long-term contract accounting
- Provisions and contingent liabilities
- Impairment of goodwill and acquired intangibles
- Accounting for tax research and development expenditure credits
- Acquisition accounting
- Impact of COVID-19

### **The scope of our audit**

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

### **Capability of the audit in detecting irregularities, including fraud**

Based on our understanding of the Group and industry, we identified that the principal risks of non-compliance with laws and regulations related to relevant tax legislation, Single Source Contracting Regulations, the Health and Safety Executive and anti-bribery and corruption legislation, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006.

We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries to increase revenue or reduce expenditure, and management bias in accounting estimates. The Group engagement team shared this risk assessment with the component auditors so that they could include appropriate audit procedures in response to such risks in their work. Audit procedures performed by the Group engagement team and/or component auditors included:

- Discussions with management at multiple levels across the business, internal audit and the Group's legal counsel throughout the year, as well as at year end. These discussions have included consideration of known or suspected instances of non-compliance with laws and regulation and fraud;
- Evaluation of management's controls designed to prevent and detect irregularities, in particular their anti-bribery controls;
- Assessment of matters reported on the Group's whistleblowing helpline and the results of management's investigation of such matters;
- Reviewing correspondence with and reports to relevant regulatory authorities;
- Challenging assumptions and judgements made by management in their significant accounting estimates, in particular in relation to long-term contract accounting and the impairment of goodwill and intangible fixed assets (see related key audit matter below);
- Identifying and testing journal entries, in particular any journal entries posted with unusual account combinations or posted by senior management; and
- Incorporating elements of unpredictability into the audit procedures performed.

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

### **Key audit matters**

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, 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. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.



# Independent auditors' report to the members of QinetiQ Group plc continued

## Key audit matter

### Long-term contract accounting

Refer to page 73 (Report of the Audit Committee) and page 162 (note 35, Significant accounting policies – Revenue from contracts with customers) and page 128 (note 2, Revenue from contracts with customers and other income).

QinetiQ Group plc has a large number of contracts which span multiple periods and are accounted for on a percentage of completion (POC) basis in accordance with IFRS 15.

Long term contracting accounting requires a number of judgements and management estimates to be made, particularly in calculating the forecast costs to complete the contract. These judgements drive the revenue and profit recognition, and together with cash paid by the customer, impact the balance sheet position at the year end.

Onerous contract provisions are recorded where there is an expectation that a contract will be loss-making, and judgement is applied to determine the magnitude of any provision. Particular focus is given to contracts which are technologically challenging.

## How our audit addressed the key audit matter

We evaluated the contract governance policies and controls in place within the business, and tested the design and operating effectiveness of key controls in place over long-term contracts.

We performed risk assessment procedures over the portfolio of contracts to identify higher-risk contracts. These higher-risk contracts were selected for detailed contract reviews. These detailed reviews involved meeting with key financial and non-financial personnel to discuss contract performance, as well as obtaining evidence to support contract financials. Specifically, our procedures included the following:

- We assessed the basis of revenue recognition to ensure it is in line with applicable accounting standards
- We agreed overall anticipated revenue to the underlying contract and validated a sample of customer invoices through to cash receipt
- We recalculated revenue recognised and agreed both revenue, costs and associated balance sheet positions to the underlying general ledger
- We obtained evidence to corroborate management estimates and judgements, particularly around costs to complete and risk contingencies. Where necessary, we obtained correspondence with the customer to evidence progress made on the contract during the year and remaining obligations
- We validated costs incurred and allocated to contracts during the year to supporting documentation on a company-wide basis

For remaining untested low-risk contracts, we selected a sample and performed testing over revenue, agreeing to supporting documentation including customer contracts and validating a sample of customer invoices to cash receipts.

We agreed contract loss provisions recorded based on the overall outcome anticipated on the contract through a combination of the procedures above.

Additional testing was performed, where not sufficiently covered by the above, over amounts recoverable under contract and billed in advance balance sheet positions. These have been sample tested and agreed to supporting documentation.

No material exceptions were found.

### Provisions and contingent liabilities

Refer to page 73 (Report of the Audit Committee) and page 162 (note 35, Significant accounting policies – Other payables, provisions and contingent liabilities), page 143 (note 21, Provisions) and page 160 (note 30, Contingent liabilities and assets).

QinetiQ Group plc holds provisions in respect of legal, regulatory and environmental issues. (Note: Project and contract related provisions are covered within the 'long-term contract accounting' matter above).

The Group operates in regulated environments and a failure to comply with particular regulations could result in fines and/or penalties. There is judgement required in determining the significance of any instances of potential non-compliance and potential liability based on management's assessment of the most likely outcome.

The financial statements should disclose any contingent liabilities in respect of contractual, regulatory or legal issues which have not been provided for on the basis that they are not considered to qualify for recognition as provisions

We have assessed management's processes and controls over legal and regulatory claims and issues and made enquiries with in-house legal counsel.

We tested the appropriateness of management's assumptions by reference to third party evidence for key provisions recorded at the year end and movements in the year. In doing this, we concluded on whether our understanding of the business gained throughout the audit process corroborated the provisions recorded.

We challenged management's estimate of the most likely outcomes by critically evaluating the range of possible outcomes to determine if the amounts provided are appropriate.

We assessed the adequacy of the Group's financial statement disclosures and adherence to accounting standards.

We found that the judgements formed by management were within an acceptable range and disclosures made in the financial statements are materially correct.

**Key audit matter****How our audit addressed the key audit matter****Impairment of goodwill and acquired intangibles**

Refer to page 73 (Report of the Audit Committee), page 162 (note 35, Significant accounting policies – Business combinations and related goodwill), page 136 (note 12, Goodwill) and page 138 (note 13, Intangible assets).

The business has a material amount of acquired intangible assets and goodwill, including for recent acquisitions. There is an increased risk of impairment where the post-acquisition performance of businesses acquired is behind expectations from the time of the original acquisition.

Management perform a discounted cash flow analysis based on the Board approved five year budget plans to assess whether the goodwill and intangible assets are supported by future cash projections.

Impairment charges have been recognised in the QinetiQ Germany and Advisory Services CGUs during the year.

We have tested the principles and mathematical integrity of the Group's discounted cash flow model used to assess goodwill and indefinite-lived intangible assets for potential impairment. With the assistance of our valuation specialists, we assessed the growth and discount rates used in this impairment calculation, by comparing the Group's assumptions to external data. We concluded that the Group's assumptions were appropriate.

We have understood the rationale for the model used, the term of which is consistent with the internal budgeting and forecasting process and the long-term viability assessment, and agreed that this has been appropriately approved by the Board.

We challenged the cash flow projections used within the model by reference to current level of sales and analysis of management's historic forecasting accuracy. We have held discussions with financial and non-financial personnel, corroborating explanations to supporting documentation, including third party evidence, where possible.

We tested the sensitivity of the impairment calculation to changes in the underlying assumptions and concluded that there is sufficient headroom within the model such that no further impairments are required.

Where impairment charges have been recognised, we have challenged the basis and accuracy of the impairment, and have ensured that sufficient and appropriate disclosure is made in the financial statements.

We assessed whether the Group's disclosures regarding sensitivity of the outcome of the impairment assessment to changes in key assumptions properly reflected the risks inherent in the valuation of goodwill.

Through review of the impairment assessment performed by management and the disclosures made, we did not identify any material misstatements.

**Accounting for tax research and development expenditure credits**

Refer to page 162 (note 35, Significant accounting policies – Taxation), page 133 (note 9, Taxation).

The Group has determined that it is appropriate to account for the UK's Research and Development Expenditure Credit ('RDEC') under IAS 12, rather than as a government grant within IAS 20.

Measurement of current tax includes RDEC and requires judgements as to the probable amount of tax payable after the preparation of tax filings and potential challenge by relevant tax authorities.

We have reviewed management's accounting policy for RDEC and disclosure (note 9, Taxation) of its impact on the Group's underlying effective tax rate. Management has made a judgement as to whether RDEC should be accounted for under IAS 12 or IAS 20 and we consider the disclosures made sufficient to enable a user of the accounts to identify and understand the impact of management's accounting policy.

We have used our tax specialists to challenge the appropriateness of management's assumptions and estimates in relation to tax positions, including RDEC, by critically assessing the range of possible outcomes. We obtained the latest correspondence with the relevant tax authorities to corroborate management's conclusions.

We found that judgements made by management in regards to RDEC were within an acceptable range.

We have reviewed the disclosures made in respect of tax, in particular around estimates and uncertainties and are satisfied that the disclosures made are appropriate.

**Acquisition accounting**

Refer to page 73 (Report of the Audit Committee), page 162 (note 35, Significant accounting policies – Business combinations and related goodwill), and page 134 (note 11, Business Combinations).

QinetiQ Group plc has completed two acquisitions in the year; Manufacturing Techniques Inc. and Newman & Spurr Consultancy.

Business combinations are inherently of greater risk as they are one-off and unique in nature. Management have applied key judgements, including assessing the fair value of assets and liabilities acquired.

A material amount of goodwill has resulted from these transactions, creating a risk that this may be impaired if it is unsupported by the forecast performance of the businesses acquired.

We have obtained and reviewed the purchase agreements to ensure that all terms have been considered and accounted for appropriately.

We used our internal valuation experts to assess the appropriateness of the fair value of acquired intangibles and other assets and liabilities, as calculated by management's experts.

We agreed consideration paid to supporting documents and ensured that the resulting goodwill is calculated accurately and supported by the expected future performance of the acquired businesses.

We obtained supporting evidence over Accounts Receivable and Accounts Payable balances at MTEQ at the acquisition date.

We reviewed the disclosures made in respect of acquisitions, in particular around estimates and uncertainties, and are satisfied that the disclosures made are appropriate.



# Independent auditors' report to the members of QinetiQ Group plc continued

## Key audit matter

### Impact of COVID-19

Refer to page 73 (Report of the Audit Committee) and page 10 (Chief Executive's statement) and page 36 (Principal risks).

QinetiQ Group plc continue to deliver customer contracts and consider the impact of COVID-19 to be limited.

Management have taken precautionary action in implementing a series of temporary measures, including a reduction in senior salaries and Board fees, in addition to postponing the decision on the dividend. Measures to temporarily close sites and furlough workers have also been taken to respond to the short-term impact of the pandemic.

Forecasts for FY21 and beyond have been revisited to ensure that any necessary revisions to the year end balance sheet are made. The impairment to QinetiQ Germany's Goodwill arose as a result of this reforecasting exercise and is detailed in that Key Audit Matter above.

Whilst management consider the Group to remain resilient, attributed to a strong order book and net cash position at the year end, a range of possible outcomes continues to be modelled depending on the duration and extent of measures such as social distancing and restrictions on international travel.

The third party engaged by management to value pension assets have included a material valuation uncertainty clause in their report. This clause highlights that there is less certainty attached to the valuation as a result of the COVID-19 pandemic. This represents a significant estimation uncertainty in relation to the valuation of pension assets.

## How our audit addressed the key audit matter

We have discussed the impact of COVID-19 in each meeting held with management at multiple levels across the Group.

Our audit work over long term contracts described above included obtaining an understanding of COVID-19 risks on each contract and agreeing that risk assumptions within the contract accounting were supportable to corroboratory evidence.

We have evaluated and challenged management's revised forecasts and agreed these to supporting documentation and correspondence with customers where applicable. The revised forecasts, and assumptions that underpin them, are supportable.

We have reviewed the disclosures made in respect of COVID-19 and are satisfied that they are sufficient and consistent with procedures performed. In particular, we considered the adequacy of the disclosures made in notes 36 (Critical accounting estimates and judgements) and 28 (Post-retirement benefits) to the financial statements, which explain that there is significant estimation uncertainty in relation to the valuation of the following pension assets included in the balance sheet as at 31 March 2020; the property portfolio of £167.0m and the unquoted equities of £47.3m. We obtained management's assessment and gathered sufficient appropriate audit evidence around the valuation in the statement of financial position and the sufficiency of the disclosures made.

We determined that there were no key audit matters applicable to the Company to communicate in our report.

## How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the Group and the Company, the accounting processes and controls, and the industry in which they operate.

The only financially significant component within the Group is QinetiQ Limited. The audit of this entity's complete financial information was performed by the Group audit team in the UK. This provided sufficient coverage over all financial statement balances, except inventory. We performed additional audit procedures over inventory balances at two further entities to ensure sufficient coverage over that financial statement line item. One entity was located within the UK and work was performed by the Group audit team. The other entity was located in the US and work was performed by our local PwC component audit team.

We performed additional procedures over revenue and associated financial statement balances at Foster Miller Inc., located in the US which was performed by our local PwC component audit team.

Additional procedures were also performed by the Group audit team over accounts receivable and accounts payable balances within Manufacturing Techniques Inc.

In addition to the above, we performed analytical procedures on the remaining entities to understand key balances and transactions in the year and performed additional procedures on any unusual balances identified.

The audit procedures performed over the complete financial information of QinetiQ Limited, accounted for 69% of total Group revenue and 90% of underlying profit before taxation.

To supplement our audit work on QinetiQ Limited, we performed audit procedures over: Inventory in two other locations, Accounts Receivable and Accounts Payable in MTEQ and Revenue and associated balance sheet accounts within QNA. This, along with work performed at Group level, obtained coverage of 77% of total Group Revenue and 86% of total Group assets.

The combination of the work referred to above, together with additional procedures performed at Group level, including testing of significant journals posted within the consolidation and significant adjustments made to the financial statements, gave us the evidence we needed for our opinion on the financial statements as a whole.

### How we tailored the audit scope continued

Only one component auditor, located in the US, was involved in the audit as all other audit procedures were performed by the Group audit team. The US business operates under a Proxy Board which is required to carry on business with the US Department of Defence. This Proxy Board places certain restrictions on access to, and communication of, information outside of the US borders. We planned our audit to ensure US personnel completed the audit work within the US and obtained approvals for transfer of information in advance of undertaking the audit work. The Group engagement leader discussed and agreed the audit plan with our US component audit team, in addition to agreeing the format and content of communications. We determined the level of involvement we needed to have in the audit work at this reporting entity to be able to conclude whether sufficient appropriate evidence had been obtained as a basis for our opinion on the financial statements as a whole. As the procedures performed by this component were limited to revenue and associated balances; and inventory only, this included discussions with the component team and attending the audit close meeting by video conference call, at which the outcome of all audit findings was discussed. The Group audit team have reviewed the working papers of the US component team and are comfortable that sufficient and appropriate procedures have been performed.

The Company audit was performed by the Group audit team. Audit procedures were performed over the complete financial information and disclosures for statutory audit purposes only. Audit work over the Company was not required for the Group audit as all significant balances within the Company are eliminated on consolidation.

### Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Company financial statements
<b>Overall materiality</b>	£6.2 million (2019: £6.1 million).	£4.8 million (2019: £4.8 million).
<b>How we determined it</b>	5% of underlying profit before tax.	1% of total assets.
<b>Rationale for benchmark applied</b>	Based on the benchmarks used in the Annual Report and Accounts, underlying profit before tax is one of the primary measures used by the shareholders in assessing the performance of the Group, and is a generally accepted auditing benchmark. It is considered appropriate to exclude specific adjusting items due to the nature of these balances as disclosed in note 4 to the Financial Statements.	We believe that total assets is the primary measure used by the shareholders in assessing the performance of this entity, and is a generally accepted auditing benchmark for non-trading entities. This materiality relates to the audit for the statutory entity only, as the Company was not in scope for the Group audit.

For each component in the scope of our Group audit, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £3.0 million and £5.9 million. Certain components were audited to a local statutory audit materiality that was also less than our overall Group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £300,000 (Group audit) (2019: £300,000) and £240,000 (Company audit) (2019: £240,000) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

In addition, we agreed with the Audit Committee that we would report to them misstatements identified during our audit of the Directors' Remuneration Report above £1,000, as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

### Going concern

In accordance with ISAs (UK) we report as follows:

Reporting obligation	Outcome
We are required to report if we have anything material to add or draw attention to in respect of the Directors' statement in the financial statements about whether the Directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the Directors' identification of any material uncertainties to the Group's and the company's ability to continue as a going concern over a period of at least 12 months from the date of approval of the financial statements.	We have nothing material to add or to draw attention to. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's and company's ability to continue as a going concern.
We are required to report if the Directors' statement relating to Going Concern in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.	We have nothing to report.

# Independent auditors' report to the members of QinetiQ Group plc continued

## Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The Directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, the Companies Act 2006 (CA06), ISAs (UK) and the Listing Rules of the Financial Conduct Authority (FCA) require us also to report certain opinions and matters as described below (required by ISAs (UK) unless otherwise stated).

## Strategic Report and Directors' report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' report for the year ended 31 March 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the Group and company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' report. (CA06)

## The Directors' assessment of the prospects of the Group and of the principal risks that would threaten the solvency or liquidity of the Group

We have nothing material to add or draw attention to regarding:

- The Directors' confirmation on page 113 of the Annual Report that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.
- The disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.
- The Directors' explanation on page 37 of the Annual Report as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We have nothing to report having performed a review of the Directors' statement that they have carried out a robust assessment of the principal risks facing the Group and statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the UK Corporate Governance Code (the 'Code'); and considering whether the statements are consistent with the knowledge and understanding of the Group and Company and their environment obtained in the course of the audit. (Listing Rules)

## Other Code Provisions

We have nothing to report in respect of our responsibility to report when:

- The statement given by the Directors, on page 113, that they consider the Annual Report taken as a whole to be fair, balanced and understandable, and provides the information necessary for the members to assess the Group's and Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and Company obtained in the course of performing our audit.
- The section of the Annual Report on page 72 describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.
- The Directors' statement relating to the company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified, under the Listing Rules, for review by the auditors.

### Directors' Remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006. (CA06)

### Responsibilities for the financial statements and the audit

#### Responsibilities of the Directors for the financial statements

As explained more fully in the Statement of Directors' Responsibilities set out on page 112, the Directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The Directors are also 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.

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

#### Auditors' responsibilities for the audit of the financial statements

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

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities). This description forms part of our auditors' report.

#### Use of this report

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### Other required reporting

#### Companies Act 2006 exception reporting

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

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

We have no exceptions to report arising from this responsibility.

#### Appointment

Following the recommendation of the Audit Committee, we were appointed by the members on 22 June 2017 to audit the financial statements for the year ended 31 March 2018 and subsequent financial periods. The period of total uninterrupted engagement is three years, covering the years ended 31 March 2018 to 31 March 2020.

#### Julian Gray

##### Senior Statutory Auditor

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Southampton

21 May 2020