

Code Principle D – Remuneration

Directors' Remuneration Report (DRR)

Chairman's statement



Michael Harper

Remuneration Committee Chairman

Committee Members

Lynn Brubaker, Admiral Sir James Burnell-Nugent, Mark Elliott, Ian Mason, Paul Murray and Susan Searle.

Chair's statement; pages 68 to 69.

At a glance; pages 70 to 71.

Remuneration Policy; pages 72 to 81.

Annual Report on Remuneration; pages 82 to 91.

This report complies with the Large and Medium-sized Companies and Groups (Accounting and Reports) (Amendment) Regulations 2013.

During 2017 the Committee met five times (detailed summary of attendance and activities are provided on pages 46 and 84).

Dear Shareholder

On behalf of the Board, I am pleased to present the Directors' remuneration report for the financial year ending 31 March 2017.

As the Chairman has outlined in his statement on page 4, the Board has been encouraged by the progress made by the CEO and his new Executive Committee during the year and by the momentum the CEO in particular has given to the development and implementation of our new growth strategy. The progress is evident from the growth in our share price and our improved total shareholder return performance.

Overall, the Remuneration Committee believes that good progress has been made during the year with increased orders and profitability. Overall, the annual contribution to the Bonus Banking Plan pool remains consistent with 2016 – see page 71.

The business context in 2017

Governments across the globe are increasingly seeking to protect their citizens against a variety of security threats. Our expertise in science and technology is particularly relevant in this environment and we play a vital role in linking different technologies and making connections across supply chains and internationally. The implementation of our new strategy, which represents significant change in direction and approach in the complex market of defence is challenging and will take time.

The essence of the business strategy is to grow the Company sustainably over the next five years through transformation which continues at pace, partnering with our customers and investing in organic growth. This organic investment includes internal research and development, complemented by bolt-on acquisitions where there is a strong strategic fit.

Short-term operational excellence is critical and the Remuneration Committee has spent a great deal of time during the year considering the incentive arrangements of the Executive Directors and the top 200 leaders in the Company with a view to ensuring the right balance between rewarding short-term performance and long-term growth. A sharp focus on annual performance will continue to be critical to delivering sustained, longer-term shareholder value.

The new Directors' Remuneration Policy

At the heart of the new policy, the Remuneration Committee is proposing a new approach to incentives which balances reward for incremental annual performance and long-term sustainable shareholder value creation as measured by share price appreciation and a progressive dividend policy. It is the Committee's view that the new five-year strategy requires a bespoke and innovative approach to remuneration.

The approach is designed to:

- Provide a clear link to strategy implementation
- Link short-term and sustained long-term performance; and
- Align the interests of our shareholders and leadership team.

The proposed incentive arrangements are built on the key performance indicators and performance targets which are integral to the five-year Integrated Strategic Business Plan.

During the year we embarked on an extensive consultation exercise with our largest shareholders and their representatives and we have listened carefully to the views we have received. The proposals which we are asking shareholders to vote on at the Annual General Meeting incorporate several design features which some of our shareholders requested during the engagement process. In summary the new policy:

- Reduces the total incentive opportunity from 425% to 325% of salary;
- Reduces the maximum award under the Bonus Banking Plan from 225% to 200% of salary. As now, half the award is deferred into shares and delivered over a four-year period;
- Introduces a new annual Deferred Share Plan equal to 125% of salary all of which is deferred into equity and subject to a three-year performance underpin with a further two-year holding period. This will be used in place of the performance share plan;
- Increases the minimum shareholding requirement for the CEO to 300% of salary and 200% for the CFO from 200% and 150% of salary respectively; and
- Reduces the pension contribution for new Executive Directors to 15% of salary from 25% of salary.

There are no other material changes to the Directors' Remuneration Policy.

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A number of checks and balances have been incorporated into the incentive arrangements to ensure that they will not reward short-term performance which is not sustained over the longer-term.
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Aligning the interests of our shareholders and QinetiQ's leadership team

The Remuneration Committee has sought to ensure that the new approach to incentives aligns the interests of our shareholders with those of the top 200 leaders in QinetiQ. A number of checks and balances have been incorporated into the incentive arrangements to ensure that they will not reward short-term performance which is not sustained over the longer term.

The key features of the arrangements which prevent this are:

- The measurement of multi-year performance in respect of shares awarded under the Bonus Banking Plan through the annual forfeiture mechanism;
- The mix of cash and shares awarded in the year is heavily weighted towards shares (circa 70% equity at maximum);
- The long-term performance underpin which will determine whether the Deferred Share Plan shares vest in full at the end of three years;
- The additional 'holding period' in respect of the Deferred Share Plan shares which may only be traded five years after the initial award;
- The stretch of the performance targets – so the performance targets for the Deferred Share Plan are based on our strategic growth plan;
- The transparent disclosure of the performance measures and targets; and
- Increased share ownership requirements.

In summary, the proposed incentive arrangement comprise two elements: the existing Bonus Banking Plan (Element A) and a new Deferred Share Plan (Element B) which replaces the Performance Share Plan. The Bonus Banking Plan (Element A) targets are based on the annual budget whilst the Deferred Share Plan (Element B) targets are based on strategic growth measures. For 2018, the performance measure for the Deferred Share Plan (Element B) is based on improving underlying profit over the previous years outturn with a stretching maximum.

We are aware that the use of operational financial measures and non-financial measures which drive long-term shareholder value is somewhat different from the more standard measures such as Earnings

per Share and Total Shareholder Return performance measures. The design of the incentive arrangements are based on annual and multi-year performance assessment. We believe that we have succeeded in developing arrangements which will reward both short-term performance and sustained, long-term shareholder value.

Employee engagement and reward

All QinetiQ's employees are key to the delivery of the strategy. The CEO and the Group HR Director have introduced regular consultations with our Employee Engagement Group on reward matters including Executive Directors' pay. I have met the Chair of the Employee Engagement Group and it is our intention to meet again prior to the AGM and at appropriate intervals thereafter.

Conclusion

The Committee is presenting a revised Remuneration Policy for shareholder approval at the 2017 AGM and is included in full on pages 72-81. It is also available to view in full on the Company's website www.QinetiQ.com. Further details on the new Deferred Share Plan (Element B) are set out in the Notice of the Annual General Meeting together with a summary description of the Plan's terms and conditions.

I hope that we can rely on your vote in favour of the Annual Report on Remuneration and Remuneration Policy at the AGM on 19 July 2017. I am very grateful for the time shareholders and their representative bodies have given us throughout the consultation process. If you would like to discuss any aspect of this report, I would be happy to hear from you. You may contact me through Jon Messent, Company Secretary and Group General Counsel.

Michael Harper

Remuneration Committee Chairman
25 May 2017

Directors' Remuneration Report continued

At a glance

“
...a year of immense
change delivered
with pace and
determination...
”

How have we performed against our corporate performance objectives?

Embedding our strategy, in tandem with transforming our Company through reorganisation and people development, has seen a year of immense change delivered with pace and determination across the Group.

The diverse challenges and opportunities we face in our markets, our unique heritage, and the deep transformation our organisation is working through, means that we continue to evolve our strategy in a very deliberate way.

Exceeding targets on orders and achieving stretch on operating profit and cash flow is regarded by the Committee as a good result in such a challenging year. The Committee believe that incentivising strategic and operational objectives, which support the financial KPIs, has ensured the Company has progressed both in terms of what was delivered but also how it was delivered.

The collective objectives have seen the CEO, supported by an engaged Executive Committee and Leadership Community, lead on communicating our vision and purpose. The CEO has been visible to both customers and employees alike and he has been a personal sponsor of the Leadership Development Programme which every member of the Executive Committee and Leadership Community has undertaken with hugely positive results. The CEO has also worked very closely with the Board in developing an Integrated Strategic Business Plan which provides the challenge and direction over the next five years.

We set five collective objectives, summarised below, based on securing contracts in certain markets and transforming the organisation. Of the five collective objectives, two were achieved in full, two partially achieved and one not achieved.

The Group Chairman takes responsibility for setting the personal objectives of the CEO and the two critical objectives, summarised below, relate to the development of the five-year Integrated Strategic Business Plan and Leadership Development. The Board is pleased with the excellent progress made against these two objectives.

The following table highlights the performance and remuneration outcomes for the year ended 31 March 2017 with more detail provided in Part 3 of the Remuneration Report.

Annual Incentive	Weighting (%)	Target performance	Stretch performance	Actual performance (excluding acquisitions)	% of maximum reward received
QinetiQ orders*	25	£600.0m	£750.0m	£671.4m	73.8%
QinetiQ underlying operating profit*	25	£105.0m	£115.0m	£115.1m	100.0%
QinetiQ underlying operating cash flow* (Excluding LTPA and MSCA capital Expenditure)	25	£80.0m	£96.0m	£100.0m	100.0%
Collective Objectives:					
Strategic					
– Lead and modernise the UK Defence 'Test & Evaluation Enterprise'					
– Build the Company internationally	12.5	60%	100%	65%	56.3%
– Innovate for customer advantage					
Operational					
– Transformation programme					
– Organisation development					
CEO Personal Objectives:					
Growth:					
– Develop a five-year Integrated Strategic Business Plan	12.5	60%	100%	90%	87.5%
Leadership:					
– Develop Leadership Community competence					

David Smith did not participate in the 2017 Bonus Banking Plan following his recruitment on 1 March 2017.

Long-term incentive

Neither of the Executive Directors were participants in the Performance Share Plan awards granted in 2014 and therefore no long-term incentives with a performance period to 31 March 2017 are due to vest for the Executive Directors.

* Definitions of the Group's 'Alternative performance measures' can be found in the glossary on page 151.

Share price growth

22.4%
over the last 12 months

How does reward earned in 2017 relate to Company performance?

Underlying EPS has grown by 11.0% in 2017 against a 10.6% reported increase in CEO annual variable reward. The CEO's 2016 annual variable reward was pro-rated for his hire date of 27 April 2015 therefore a like-for-like annual comparison is 2.7%. Results for 2017 represent a strong alignment between performance and reward over the last 12 months.

2017 Actual	1,105	EPS 18.1p
2016 Full Year Equivalent	1,076	EPS 16.3p
2016 Actual	999	EPS 16.3p

- Bonus Banking Plan Annual Contribution (£'000)

The share price has grown by 22.4% over the last 12 months benefiting both shareholders and Bonus Banking Plan participants alike. The Bonus Banking Plan annual contribution is added to the existing pool.

The pool has grown in value reflecting the growth in share price, building close alignment between Executive Directors and shareholders. Half of the restated pool is paid as cash with the remaining half deferred until the end of 2018 when it will be paid in shares. The following chart summarises the 2017 breakdown and detailed calculations are provided on page 87.

2017 Bonus Banking Pool Build-Up	538	60	12	1,105	1,715
2017 Bonus Banking Pool Cash Payment and Retained Equity Value	857.5			857.5	1,715

- Bonus Banking Pool Opening Equity Value (£'000)
- Increase in Equity Value (£'000)
- Dividend Equivalent Payment (£'000)
- Bonus Banking Pool Annual Contribution (£'000)
- 2017 Annual Payment (£'000)
- Bonus Banking Pool Closing Equity Value (£'000)

How does the reward earned in 2017 align with current policy?

CEO remuneration is above target performance and in line with our financial results achieved in challenging operating conditions. The Bonus Banking Plan annual contribution for 2017 is £1,104,687, half of which is treated as equity.

CEO (£'000)

Minimum	714			714
Target	714	320	632	1,666
Maximum	714	639		1,776
Actual	714	552.5	552.5	1,819

- Fixed
- Linked to Annual Performance
- Linked to Performance over more than 1 year

Executive Director Shareholding

The following charts show the relatively small shareholdings of both Executive Directors due to their short length of service. One of the objectives of the new Incentive Plan is to facilitate the rapid build-up of material shareholdings by the Executive Directors provided performance is delivered.

CEO shareholding as a percentage of salary

Shareholding requirement	300
Value of beneficially Owned shares & Deferred shares	10
Value of Conditional Shares Subject to performance conditions	399

CFO shareholding as a percentage of salary

Shareholding requirement	200
Value of Beneficially Owned shares & Deferred shares	0
Value of Conditional Shares Subject to performance conditions	0

Principles of the proposed Remuneration Policy

Incentivising sustained performance and growth, the key policy principles are highlighted below.

Continuity and effectiveness

Base salary

Robust and transparent governance with a clear link to pay conditions across the Group.

Incentives

Clear link to growth and transformation underpinned by substantial deferral in equity and risk of forfeiture ensuring a focus on long-term sustainable performance.

Rewarding long-term sustainable value while still driving immediate business objectives.

Performance related reward

Incentives

Pay mix focuses on variable pay and correlates reward opportunity with business performance. In turn maximising shareholder value through measurement in terms of financial and non-financial KPIs.

Alignment

Incentives

Reflecting shareholder value creation, incentives retain and lock-in new executive team by incentivising what is right for the Company while ensuring quick alignment through the build-up and retention of earned equity.

Shareholding requirements

Alignment of the new executive team with the shareholder experience over the period.

Directors' Remuneration Report continued

Part 2: Remuneration Policy

“ The policy will be put forward for binding vote at the AGM on 19 July 2017 and will be effective from that date. ”

Introduction

The Directors' Remuneration Policy was last approved in 2014 and the Company therefore seeks approval for the new policy at the AGM on 19 July 2017.

Scope of policy

The policy applies to Executive Directors, the Group Chairman and Non-executive Directors. Reference may also be made to the Executive Committee who, while not Directors, fall within the Committee's remit, although the policy is not binding for these individuals.

Duration of policy

The policy will be put forward for binding vote at the AGM on 19 July 2017 and will be effective from that date. The Policy is expected to remain in effect until the 2020 AGM.

Discretion

The Committee has discretion in several areas of policy as set out in this report. The Committee may also exercise operational and administrative discretions under relevant plan rules as set out in those rules. In addition, the Committee has the discretion to amend the Remuneration Policy with regard to minor or administrative matters where it would be, in the opinion of the Committee, disproportionate to seek or await shareholder approval and commits to communicating to shareholders when discretion is used.

Key changes in the Directors' Remuneration Policy

The Committee conducted an extensive review of the Remuneration Policy taking into account the following factors:

- The Company vision-led strategy launched at the beginning of FY17 aiming to establish the conditions for growth;
- The new executive team, including both Executive Directors and Executive Committee members, established to deliver the strategy; and
- The current suitability of the incentive arrangements for the Group incorporating insight from our Leadership Community and Employee Engagement Group.

This has resulted in the Committee proposing to introduce new incentive arrangements (collectively the Incentive Plan), if approved by shareholders, made up of two elements:

- Bonus Banking Plan (Element A) with no change to the current terms and conditions other than a reduction in the maximum opportunity from 225% to 200% of salary

- Deferred Share Plan (Element B) to be used in place of the current Performance Share Plan – maximum opportunity is reduced from 200% (current maximum granted to CEO in 2016 for two years) to 125% of salary.

Awards under the Deferred Share Plan (Element B) will be earned based on challenging strategic financial growth objectives set by the Committee each year in line with the Company's Integrated Strategic Business Plan.

Shares earned under the Deferred Share Plan (Element B) are subject to a three-year vesting period, during which the participant must remain employed by the Company, and also cannot be sold for five years from the date of award irrespective of employment status.

The rationale for the change to incentive provision is to:

- provide a simple cohesive design, that incentivises delivery of the Integrated Strategic Business Plan;
- recognise that the Integrated Strategic Business Plan will evolve, therefore providing the Board with the opportunity to manage the incentives annually to ensure the evolution continues to be incentivised;
- reward participants as shareholders by the build-up of a long-term retained shareholding; and
- ensure a focus on long-term sustainable performance through the deferral in equity. Based on the maximum incentive opportunity of 325%, half of the Bonus Banking Plan (Element A) opportunity (100%) and all of the Deferred Share Plan (Element B) opportunity (125%) is treated as equity.

There will be an increase in minimum shareholding requirement for the CEO to 300% of salary (previously 200% of salary) and for the CFO 200% of salary (previously 150% of salary). This increases the alignment of Executive Directors' remuneration with shareholder value.

The pension contribution for any new Executive Director will be reduced to a maximum of 15% of salary. The change will bring pension provision for Executive Directors more closely in line with the provision for the broader employee base.

Otherwise, the operation of the policy is in line with the previous policy in force.

Executive Directors' Remuneration Policy

The Executive Directors' Remuneration Policy is put forward for approval at the AGM on 19 July 2017. This policy covers the three year period commencing 1 April 2017 and complies with the Large and Medium-sized Companies and Groups (Accounting and Reports) (Amendment) Regulations 2013.

Element	Purpose and link to strategy	Operation and performance measures	Maximum opportunity
Base salary	To attract and retain the talent needed to lead our business.	<p>An Executive Director's basic salary is set on appointment and reviewed annually or when there is a change in position or responsibility.</p> <p>When determining an appropriate level of salary, the Committee considers:</p> <ul style="list-style-type: none"> - general salary rises to employees; - remuneration practices within the Group; - any change in scope, role and responsibilities; - the general performance of the Group; - the experience of the relevant Director; - the economic environment; and - when the Committee determines a benchmarking exercise is appropriate salaries within the ranges paid by the companies in the comparator groups used for remuneration benchmarking. <p>Individuals who are recruited or promoted to the Board may, on occasion, have their salaries set below the targeted policy level until they become established in their role. In such cases subsequent increases in salary may be higher than the general rises for employees until the target positioning is achieved.</p>	<p>Typically, the base salaries of Executive Directors in post at the start of the policy period and who remain in the same role throughout the policy period will be increased by a similar percentage to the average annual percentage increase in salaries of all other employees in the Group. The exceptions to this rule may be where:</p> <ul style="list-style-type: none"> - an individual is below market level and a decision is taken to increase base pay to reflect proven competence in the role; or - there is a material increase in scope or responsibility to the Executive Director's role. <p>The Committee ensures that maximum salary levels are positioned in line with companies of a similar size to QinetiQ and validated against other companies in the industry, so that they are competitive against the market.</p> <p>The Committee intends to review the comparators periodically and may add or remove companies from the group as it considers appropriate. Any changes to the comparator groups will be set out in the section headed Implementation of Remuneration Policy, in the following financial year.</p>
Pension	To ensure that Executive Directors' total remuneration remains attractive and competitive.	<p>The Company provides a pension contribution allowance in line with practice relative to its comparators to enable the Company to recruit and retain Executive Directors with the experience and expertise to deliver the Group's strategy.</p> <p>This allowance will be a non-consolidated allowance and will not impact any incentive calculations.</p>	<p>The maximum policy pension contribution allowance will be reduced to 20% for existing Executive Directors in line with current provision; however, any new Executive Directors will have a maximum contribution of 15%.</p> <p>The Company will set out in the section headed Implementation of Remuneration Policy, in the following financial year the pension contributions for that year for each of the Executive Directors.</p>
Benefits	To ensure that Executive Directors' total remuneration remains attractive and competitive.	<p>Benefits include car allowance, health insurance, life assurance, income protection and membership of the Group's employee Share Incentive Plan which is open to all UK employees (the Executive Directors will also be eligible to participate in any other all employee plan operated by the Company from time to time).</p> <p>The Committee recognises the need to maintain suitable flexibility in the benefits provided to ensure it is able to support the objective of attracting and retaining personnel in order to deliver the Group strategy. Additional benefits may therefore be offered such as relocation allowances on recruitment.</p>	<p>The maximum is the cost of providing the relevant benefits.</p>

Directors' Remuneration Report continued

Part 2: Remuneration Policy continued

Element	Purpose and link to strategy	Operation and performance measures	Maximum opportunity
Incentive Plan	<p>The Incentive Plan provides a significant incentive to the Executive Directors linked to achievement of delivering goals that are closely aligned with the Company's strategy and the creation of value for shareholders.</p> <p>In particular, the Incentive Plan supports the Company's objectives by:</p> <ul style="list-style-type: none"> – allowing the setting of annual targets based on the businesses' strategic objectives at that time, meaning that a wider range of performance metrics can be used that are relevant and suitably stretching whilst also providing sufficient incentive linked to potential to be achievable; and – providing substantial deferral in shares and ongoing adjustment by requiring a threshold level of performance to be achieved during the deferral period. Amounts deferred in shares are also forfeitable on a director's voluntary cessation of employment which provides an effective lock-in. 	<p>An award under the Incentive Plan is subject to satisfying financial and strategic/operational performance/personal performance conditions and targets measured over a period of one financial year.</p> <p>A minimum of 50% of the incentive shall be based on financial performance measures.</p> <p>The Incentive Plan consists of two elements (Element A and Element B).</p> <p>Bonus Banking Plan (Element A). Annual Company contributions will be earned based on the satisfaction of the performance conditions. Contributions will be made for three years with payments made over four years. 50% of the value of a participant's bonus account will be paid out annually for three years with 100% of the residual value paid out at the end of year four. 50% of the unpaid balance of a participant's bonus account will be at risk of annual forfeiture.</p> <p>Deferred Share Plan (Element B). Deferred share-based element earned based on the satisfaction of pre-grant annual performance assessment, which is subject to a three-year vesting period and a further two-year holding period. A minimum 50% (Remuneration Committee have discretion to increase subject to performance) of the unvested award will be at risk forfeiture after three years.</p> <p>Malus and clawback provision apply to the Incentive Plan (both Elements).</p> <p>The Committee has discretion to provide dividend equivalents on Element A and Element B shares.</p> <p>The Committee is of the opinion that given the commercial sensitivity arising in relation to the detailed financial targets used for the incentive, disclosing precise targets for the Incentive Plan in advance would not be in shareholder interests. Targets, performance achieved and awards made will be published at the end of the annual performance period so shareholders can fully assess the basis for any pay-outs under the Plan.</p>	<p>Maximum 325% of salary (200% of salary under Element A and 125% of salary under Element B).</p> <p>Bonus Banking Plan (Element A) Maximum = 200% of salary. Target = 80%–120% of salary. Threshold = 0% of salary.</p> <p>Deferred Share Plan (Element B) Maximum = 125% of salary. Target = 30%-75% of salary. Threshold = 0% of salary.</p>

Element	Purpose and link to strategy	Operation and performance measures	Maximum opportunity
Incentive Plan continued		<p>In exceptional circumstances the Committee retains the discretion to:</p> <p>Change the performance measures and targets and the weighting attached to the performance measures and targets part way through a performance year if there is a significant and material event which causes the Committee to believe the original measures, weightings and targets are no longer appropriate; for example adjustments for:</p> <ul style="list-style-type: none"> – Acquisitions and disposals; – Restructuring costs; – Business structure changes; – Restated corporate allocations; – Foreign currency exchange rates; and – Board approved budget adjustments. <p>Make downward or upward adjustments to the amount of incentive earned resulting from the application of the performance measures, if the Committee believe that the incentive outcomes are not a fair and accurate reflection of business performance. Any adjustments or discretion applied by the Committee will be fully disclosed in the following year's Directors' remuneration report.</p>	
Minimum shareholding requirements	To align Executive Directors' interests with those of shareholders through the build-up and retention of a personal holding in QinetiQ shares.	<p>Executives have five years to accumulate the required shareholding.</p> <p>300% of base salary for the CEO.</p> <p>200% of base salary for the CFO.</p>	<p>The Committee has adopted formal shareholding requirements that will encourage the Executive Directors to build up over a five-year period and then subsequently hold a shareholding equivalent to a percentage of base salary. Adherence to these guidelines is a condition of continued participation in the equity incentive arrangements. This policy ensures that the interests of Executive Directors and those of shareholders are closely aligned.</p> <p>In addition, Executive Directors will be required to retain 50% of the post-tax amount of vested shares from the Company incentive plans until the minimum shareholding requirement is met and maintained.</p> <p>The Committee retains the discretion to increase the shareholding requirements.</p>

Elements of existing policy that will continue to apply

Element	Purpose and Link to strategy	Operation and performance measures	Maximum opportunity
Bonus Banking Plan and Performance Share Plan (PSP)	To align Executive Directors' interests with those of shareholders.	<p>The outstanding awards under the Bonus Banking Plan and PSP will continue to form part of the Remuneration Policy until vesting.</p> <p>Details on how these plans operate can be found in the Directors' remuneration report for the year of grant.</p> <p>These plans vest on terms set out in the Plan rules which have previously been approved by shareholders.</p>	<p>Bonus Banking Plan – Number of shares in participants' bonus pool as at 31 March 2017.</p> <p>Performance Share Plan – Number of shares outstanding as detailed in this report.</p>

Directors' Remuneration Report continued

Part 2: Remuneration Policy continued

Notes to the policy tables

Performance measures and targets

The performance measures and targets, financial and non-financial, are determined annually based on the Company's strategy. The Committee is of the opinion that the specific performance targets for the Incentive Plan are commercially sensitive and that it would be detrimental to the interests of the Company to disclose them. The targets will be disclosed after the end of the relevant financial year in that year's remuneration report.

However, the Committee is of the opinion that certain elements of the collective objectives may remain commercially sensitive beyond the end of the relevant financial year and will therefore be disclosed once they cease to be commercially sensitive which is anticipated to be within two years of the relevant financial year.

Remuneration policy for all employees

All employees of QinetiQ are entitled to base salary, benefits and pension.

The link between performance and reward cascades down from the Executive incentive plans with the Leadership and Business Development Communities typically invited to participate in the Company's formal annual incentive arrangements. All other employees may receive a discretionary bonus based on Company and individual performance. Participation in long-term incentive plans is available to Executive Directors, Executive Committee members, Leadership Community and selected other employees. Share ownership is further encouraged via the QinetiQ Share Incentive Plan.

Recruitment policy

The Company's principle is that the remuneration of any new recruit will be assessed in line with the same principles as for the current Executive Directors. The Committee is mindful that it wishes to avoid paying more than it considers necessary to secure a preferred candidate with the appropriate calibre and experience needed for the role. In setting the remuneration for new recruits, the Committee will have regard to guidelines and shareholder sentiment regarding one-off or enhanced short-term or long-term incentive payments as well as giving consideration for the appropriateness of any award. The Company's detailed policy when setting remuneration for the appointment of new Directors is summarised in the table below:

Remuneration element	Recruitment policy
Salary, benefits and pension	These will be set in line with the policy for existing Executive Directors.
Incentive Plan	Maximum annual participation will be set in line with the Company's policy for existing Executive Directors and will not exceed 325% of salary.
Maximum variable remuneration	The maximum variable remuneration which may be granted is 325% of salary (excluding any buy-outs).
'Buy Out' of incentives forfeited on cessation of employment	<p>Where the Committee determines that the individual circumstances of recruitment justifies the provision of a buyout, the equivalent value of any incentives that will be forfeited on cessation of an Executive Director's previous employment will be calculated taking into account the following:</p> <ul style="list-style-type: none"> - The proportion of the performance period completed on the date of the Executive Director's cessation of employment; - The performance conditions attached to the vesting of these incentives and the likelihood of them being satisfied; and - Any other terms and condition having a material effect on their value ('Lapsed value'). <p>The Committee may then grant up to the same value as the lapsed value, where possible, under the Company's incentive plan. To the extent that it was not possible or practical to provide the buyout within the terms of the Company's existing incentive plan, a bespoke arrangement would be used.</p>
Relocation policies	In instances where the new Executive Director is required to relocate or spend significant time away from their normal residence, the Company may provide one-off compensation to reflect the cost of relocation for the Executive Director. The level of the relocation package will be assessed on a case-by-case basis but will take into consideration any cost of living differences/housing allowance and schooling.

Where an existing employee is promoted to the Board, the policy set out above would apply from the date of promotion but there would be no retrospective application of the policy in relation to subsisting incentive awards or remuneration arrangements. Accordingly, prevailing elements of the remuneration package for an existing employee would be honoured and form part of the ongoing remuneration of the person concerned. These would be disclosed to shareholders in the remuneration report for the relevant financial year.

Loss of office and change of control policy

When determining any loss of office payment for a departing Director the Committee will always seek to minimise the cost to the Company while complying with the contractual terms and seeking to reflect the circumstances in place at the time. The Committee reserves the right to make additional payments where such 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 settlement or compromise of any claim arising in connection with the termination of an Executive Director's office or employment.

Remuneration element	Approach	Application of Committee discretion
Salary and benefits	<p>In the event of termination by the Company, there will be no compensation for loss of office due to misconduct or normal resignation.</p> <p>In other circumstances, Executive Directors may be entitled to receive compensation for loss of office which will be a maximum of 12 months' salary.</p> <p>Such payments will be equivalent to the monthly salary and benefits that the Executive Director would have received if still in employment with the Company. These will be paid over the notice period. Executive Directors will be expected to mitigate their loss within a twelve month period of their departure from the Company.</p>	The Company has discretion to make a lump sum payment in lieu.
Pension	Pension contributions or payments in lieu of pension contribution will be made during the notice period.	The Company has discretion to make a lump sum payment in lieu.
Bonus Banking Plan (Element A of the Incentive Plan)	<p>For the year of cessation Good leavers: Performance conditions will be measured at the measurement date. The Company bonus contribution will normally be pro-rated for the period worked during the financial year.</p> <p>Other leavers: No Company bonus contribution payable for year of cessation.</p> <p>Deferred balances in participant's Plan Account Good leavers: The balance in the participants' Plan account will be payable on cessation of employment.</p> <p>Other leavers: The balance in the Participants' Plan account will be forfeited on cessation of employment.</p>	<p>For the year of cessation Discretion: the Remuneration Committee has the following elements of discretion:</p> <ul style="list-style-type: none"> - To determine that an Executive Director is a good leaver. It is the Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders; and - To determine whether to pro-rate the Company bonus contribution to time. The Remuneration Committee's normal policy is that it will pro-rate for time. It is the Remuneration Committee's intention to only use discretion to not pro-rate in circumstances where there is an appropriate business case which will be explained in full to shareholders. <p>Deferred balances in participant's Plan Account Discretion: the Remuneration Committee has the following elements of discretion:</p> <ul style="list-style-type: none"> - To determine that an Executive Director is a good leaver. It is the Remuneration Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders; - To determine whether the payment of the balance of the participant's Plan Account should be in cash or shares or a combination of both; - To determine whether to pro-rate the balance of the participant's Plan Account payable on cessation. The Committee's normal policy is that it will not pro-rate. The Remuneration Committee will determine whether to pro-rate based on the circumstances of the Executive Directors's departure.

Directors' Remuneration Report continued

Part 2: Remuneration Policy continued

Remuneration element	Approach	Application of Committee discretion
Bonus Banking Plan (Element A of the Incentive Plan) (change of control)	<p>For the year of the change of control Performance conditions will be measured at the date of the change of control. The Company bonus contribution will normally be pro-rated to the date of the change of control.</p> <p>Deferred balances in participant's Plan Account The balance in the participant's Plan Account will be payable on the change of control.</p>	<p>For the year of the change of control Discretion: the Remuneration Committee has the following element of discretion:-</p> <ul style="list-style-type: none"> – to pro-rate the Company bonus contribution to time. The Remuneration Committee's normal policy is that it will pro-rate for time. It is the Remuneration Committee's intention to only use discretion to not pro-rate in circumstances where there is an appropriate business case which will be explained in full to shareholders. <p>Deferred balances in participant's Plan Account Discretion: the Remuneration Committee has the following elements of discretion:</p> <ul style="list-style-type: none"> – to determine whether the payment of the balance of the participant's Plan Account should be in cash or shares or a combination of both; – to determine whether to pro-rate the balance of the participant's Plan Account payable on change of control. The Committee's normal policy is that it will not pro-rate. The Remuneration Committee will determine whether to pro-rate based on the circumstances of change of control.
Deferred Share Plan (Element B of the Incentive Plan) (cessation of employment)	<p>For the year of cessation Good leavers: Performance conditions will be measured at the measurement date. The Deferred Share Plan (Element B) award will normally be pro-rated for the period worked during the financial year.</p> <p>Other leavers: No Deferred Share Plan (Element B) award for year of cessation.</p> <p>Subsisting Element B awards Good leavers: Deferred Share Plan (Element B) awards will vest on their original vesting dates and remain subject to the sale restrictions.</p> <p>Other leavers: Deferred Share Plan (Element B) awards will be forfeited on cessation of employment.</p>	<p>For the year of cessation Discretion: the Remuneration Committee has the following elements of discretion:-</p> <ul style="list-style-type: none"> – to determine that an Executive Director is a good leaver. It is the Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders; – to determine whether to pro-rate the Company award to time. The Remuneration Committee's normal policy is that it will pro-rate for time. It is the Remuneration Committee's intention to only use discretion to not pro-rate in circumstances where there is an appropriate business case which will be explained in full to shareholders; and – to determine whether the Deferred Share Plan (Element B) award will vest on the date of cessation or the original vesting date. The Remuneration Committee will make its determination based amongst other factors on the reason for the cessation of employment; and to determine whether to provide the Deferred Share Plan (Element B) award in the form of cash or shares.

Remuneration element	Approach	Application of Committee discretion
Deferred Share Plan (Element B of the Incentive Plan) (cessation of employment) continued		Subsisting Deferred Share Plan (Element B) awards Discretion: the Remuneration Committee has the following elements of discretion: <ul style="list-style-type: none"> – To determine that an Executive Director is a good leaver. It is the Remuneration Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders; – To determine whether to pro-rate the Deferred Share Plan (Element B) award to the date of cessation. The Committee's normal policy is that it will pro-rate. It is the Remuneration Committee's intention to only use discretion to not pro-rate in circumstances where there is an appropriate business case which will be explained in full to shareholders; – To determine whether the Deferred Share Plan (Element B) award will vest on the date of cessation or the original vesting date. The Remuneration Committee will make its determination based amongst other factors on the reason for the cessation of employment.
Deferred Share Plan (Element B of the Incentive Plan) (Change of Control)	For the year of the change of control Performance conditions will be measured at the date of the change of control. The Element B award will normally be pro-rated to the date of the change of control. Subsisting Element B awards The awards will vest on the date of the change of control and the sale restrictions will fall away.	For the year of the change of control Discretion: the Remuneration Committee has the following element of discretion:– <ul style="list-style-type: none"> – To determine whether to pro-rate the Deferred Share Plan (Element B) award to time. The Remuneration Committee's normal policy is that it will pro-rate for time. It is the Remuneration Committee's intention to only use discretion to not pro-rate in circumstances where there is an appropriate business case which will be explained in full to shareholders. Subsisting Deferred Share Plan (Element B) awards Discretion: the Remuneration Committee has the following elements of discretion: <ul style="list-style-type: none"> – To determine whether the satisfaction of Deferred Share Plan (Element B) awards should be in cash or shares or a combination of both; and – To determine whether to pro-rate Deferred Share Plan (Element B) awards on change of control. The Committee's normal policy is that it will not pro-rate. The Remuneration Committee will determine whether to pro-rate based on the circumstances of change of control.
Other contractual obligations	There are no other contractual provisions other than those set out above agreed that could impact quantum of the payment.	None.

A good leaver is a person whose cessation of employment is for one of the following reasons:

- Death;
- Ill-health;
- Injury or disability;
- Redundancy;
- Retirement;
- Employing company ceasing to be a Group company;
- Transfer of employment to a company which is not a Group company; and
- Where the person is designated a good leaver at the discretion of the Committee (as described above).

A person who ceases employment in circumstances other than those set out above is designated as an 'other leaver'.

Directors' Remuneration Report continued

Part 2: Remuneration Policy continued

Malus and clawback

Malus provisions apply to both the Bonus Banking Plan (Element A) and the Deferred Share Plan (Element B). Malus is the adjustment of Element A bonus contributions or the balance in a participant's bonus account or unvested Deferred Share Plan (Element B) awards because of the occurrence of one or more circumstances. The adjustment may result in the value being reduced to nil.

Clawback is the recovery of payments made under the Bonus Banking Plan (Element A) or vested Deferred Share Plan (Element B) awards as a result of the occurrence of one or more circumstances. Clawback may apply to all or part of a participant's payment under the Deferred Share Plan (Element A) or Deferred Share Plan (Element B) award and may be effected, among other means, by requiring the transfer of shares, payment of cash or reduction of awards or bonuses.

The circumstances in which malus and clawback could apply are as follows:

- Discovery of a material misstatement resulting in an adjustment in the audited accounts of the Group or any Group company;
- The assessment of any performance condition or condition in respect of a payment or award under the Incentive Plan was based on error, or inaccurate or misleading information;
- The discovery that any information used to determine the Bonus Banking Plan (Element A) or Deferred Share Plan (Element B) award was based on error, or inaccurate or misleading information;
- Action or conduct of a participant which amounts to fraud or gross misconduct; or
- Events or the behaviour of a participant have led to the censure of a Group company by a regulatory authority or have had a significant detrimental impact on the reputation of any Group company provided that the Board is satisfied that the relevant participant was responsible for the censure or reputational damage and that the censure or reputational damage is attributable to the participant.

The following table sets out the periods during which malus and clawback may be effected.

	Bonus Banking Plan (Element A)	Deferred Share Plan (Element B)
Malus	Up to the date of a payment.	Any time prior to vesting.
Clawback	Three years post the date of any payment.	Three years from the date of vesting.

Pay and performance scenario analysis

The proposed Executive Remuneration Policy is illustrated in the following charts showing what each Director could expect to receive in FY18 under different performance scenarios, based on the following definitions:

Scenario	Fixed	Linked to annual performance	Linked to performance over more than 1 year
Stretch		50% of Element A Opportunity (100% of salary)	50% of Element A opportunity (100% of salary)
	FY18 base salary	50% of Element B (62.5% of salary)	50% of Element B (62.5% of salary)
Target	Car allowance	25% of Element A opportunity (50% of salary)	25% of Element A opportunity (50% of salary)
	Pension allowance	17.5% of Element B (21.875% of salary)	17.5% of Element B (21.875% of salary)
	Benefits		
Minimum		No variable pay	No variable pay

CEO (£'000)

Stretch	28%	36%	36%	2,587
Target	46%	27%	27%	1,547
Minimum			100%	722

- Fixed
- Linked to annual performance
- Linked to performance over more than 1 year

CFO (£'000)

Stretch	28%	36%	36%	1,984
Target	46%	27%	27%	1,187
Minimum			100%	554

- Fixed
- Linked to annual performance
- Linked to performance over more than 1 year

Based on the maximum incentive opportunity of 325%, half of the Bonus Banking Plan (Element A) opportunity (100%) and all of the Deferred Share Plan (Element B) opportunity (125%) is treated as equity. At both target and stretch performance 69% of variable pay is treated as equity.

Policy for Non-executive Directors

The Company's policy when setting fees for the appointment of new Non-executive Directors is to apply the policy which applies to current Non-executive Directors.

Element	Purpose and link to strategy	Operation and performance measures	Maximum opportunity
Non-executive Directors			
Fees	To attract and retain Non-executive Directors of the calibre required to assist the Company in setting and delivering its strategy.	<p>The Executive Directors and the Group Chairman are responsible for setting the remuneration of the Non-executive Directors. The Board, minus the Chairman, is responsible for setting the Chairman's fees.</p> <p>Non-executive Directors are paid an annual fee and additional fees for chairmanship of committees, and the Company retains the flexibility to pay fees for the membership of committees. The Chairman does not receive any additional fees for membership of committees.</p> <p>Fees are reviewed annually based on equivalent roles in the comparator group used to review salaries paid to the Executive Directors.</p> <p>An annual accommodation allowance may be payable to the Group Chairman and as deemed appropriate for individuals who are not UK resident.</p> <p>Excluding the Group Chairman, an additional fee is payable to those Non-executive Directors attending meetings outside of their country of residence.</p> <p>Non-executive Directors and the Group Chairman do not participate in any variable remuneration or benefits arrangements.</p>	<p>The fees for Non-executive Directors and the Group Chairman are broadly set at a competitive level against the comparator group.</p> <p>In general the level of fee increase for the Non-executive Directors and the Group Chairman will be set taking account of any change in responsibility and the general rise in salaries across employees.</p> <p>The Company will pay reasonable expenses incurred by the Non-executive Directors and Group Chairman and may settle any tax incurred in relation to these.</p>

Consideration of shareholder and employee views

The Chair of the Committee and the Group Chairman consult with key shareholders on remuneration matters from time to time, and particularly where changes to the Remuneration Policy are under consideration. The Chair reports any concerns expressed by shareholders to the Committee and these are taken into account as the Committee develops and implements its policy. Any comments received from shareholders outside these consultation exercises are also reported to the Committee, and the Committee takes account of general views on remuneration expressed by shareholders or representative bodies.

The Committee consulted with its principal shareholders in relation to the proposal to revise the policy and took into account views expressed during the consultation when agreeing the final design. The Remuneration Committee is grateful for shareholders' comments and engagement during the consultation process. At the end of this process, the Remuneration Committee was pleased that the majority of the shareholders consulted expressed support for the policy.

The Committee has not formally consulted with employees and has not used any specific all-employee comparison metrics in forming this policy. However, the Committee has regularly consulted with the Company's Employee Engagement Group on other reward matters.

Directors' Remuneration Report continued

Part 3: Annual Report on Remuneration

Introduction

The Remuneration Committee presents the Annual Remuneration Report showing how the Remuneration Policy has been implemented for the year ended 31 March 2017.

The Committee presents the Annual Report on Remuneration to shareholders at the AGM on 19 July 2017. This report was compiled in accordance with Schedule 8 of the Large and Medium-sized Companies and Group (Accounts and Reports) Regulations 2013 as well as the Companies Act 2006.

Remuneration Committee Structure

The Committee is chaired by Michael Harper, and is composed of the members set out on page 68.

Effectiveness review

In 2017, the effectiveness review was undertaken internally, and it rated the effectiveness of the Committee highly overall. Considerations for 2017 include continuing the productive dialogue with the Executive team and, subject to policy approval, ensuring incentive targets are stretching enough in the context of the strategy, as it plays out.

Consideration by the Directors of matters relating to Directors' remuneration

Members of the Committee are appointed by the Board. The Committee comprises at least three members (not counting the Group Chairman), all of whom are independent Non-executive Directors. The Group Chairman of the Board also serves on the Committee as an additional member as he was considered independent on appointment as Chairman.

Only members of the Committee have the right to attend Committee meetings. However, external advisors and other internal advisors such as the Chief Executive Officer and the Group Human Resources Director are invited to attend for all or part of any meeting, as and when appropriate.

The Board appoints the Committee Chairman who is an independent, Non-executive Director. In the absence of the Committee Chairman and/or an appointed deputy, the remaining members present shall elect one of themselves to chair the meeting who would qualify under these terms of reference to be appointed to that position by the Board. The Chairman of the Board is not permitted to be Chairman of the Committee.

The full terms of reference of the Committee can be found on the QinetiQ website (www.QinetiQ.com).

Service Contracts/Letters of Appointment

The Company's policy is that Executive Directors have rolling contracts which are terminable by either party giving 12 months' notice. Non-executive Directors do not have service contracts but are appointed under letters of appointment. All service contracts and letters of appointment are available for viewing at the Company's registered office and at the AGM. Non-executive Directors typically serve two three-year terms but may be invited by the Board to serve for an additional period (see table in the Nominations Committee report on page 53).

Non-executive Director	Date appointed	Arrangement	Notice period
Lynn Brubaker	27 January 2016	Initial term of three years from date of appointment until the conclusion of the Annual General Meeting approximately three years from that date, subject to annual reappointment at the AGM.	1 Month
Admiral Sir James Burnell-Nugent	10 April 2010	Initial term of three years from date of appointment, subject to annual reappointment at the AGM.	–
Mark Elliott	01 June 2009	Initial term of three years from date of appointment, subject to annual reappointment at the AGM.	–
Michael Harper	22 November 2011	Initial term of three years from date of appointment, subject to annual reappointment at the AGM.	–
Ian Mason	04 June 2014	Initial term of three years from date of appointment until the conclusion of the Annual General Meeting approximately three years from that date, subject to annual reappointment at the AGM.	1 Month
Paul Murray	25 October 2010	Initial term of three years from date of appointment, subject to annual reappointment at the AGM.	–
Susan Searle	14 March 2014	Initial term of three years from date of appointment until the conclusion of the Annual General Meeting approximately three years from that date, subject to annual reappointment at the AGM.	–
David Smith	01 March 2017	Service Contract	12 Months
Steve Wadey	27 April 2015	Service Contract	12 Months

The Committee has appointed PwC, an independent firm of remuneration consultants, to provide advice on market practice, corporate governance and institutional stakeholder views. Fees paid during the year for these services were £111,500 which included advice relating to the policy and shareholder consultation.

PwC provided the following additional services during the year:

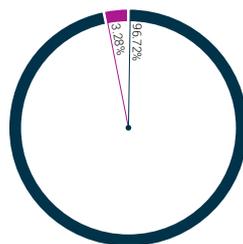
- Implementation support for the Company on Executive reward plans;
- Consultancy and advice to Group Tax; and
- Consultancy and advice in relation to Group Pensions.

The Committee is satisfied the scale and nature of this work does not impact on the objectivity and independence of the advice it receives from PwC.

Following the appointment of PwC as Independent Auditor the Committee can no longer retain PwC as advisors. The Committee undertook a thorough review and has appointed FIT Remuneration Consultants as advisors from 1 April 2017.

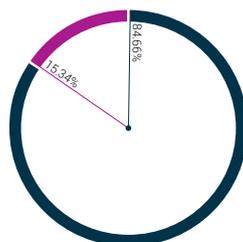
Statement of voting

Remuneration Report – 2016



Votes for	404,652,873 (96.72%)
Votes against	13,714,402 (3.28%)
Total votes cast	418,367,275 (71.86% share capital)
Abstained	1,781,755

Remuneration Policy – 2014



Votes for	422,740,088 (84.66%)
Votes against	76,602,719 (15.34%)
Total votes cast	499,342,807 (76.68% share capital)
Abstained	4,877,598

As in previous years, details on the voting on all resolutions at the 2017 AGM will be announced via the RNS and posted on the QinetiQ website following the AGM.

Directors' Remuneration Report continued

Part 3: Annual Report on Remuneration continued

Remuneration Committee meetings, activities and decisions 2017**Executive Directors changes during 2017**

David Mellors (CFO) resigned from the Company on 31 December 2016 and was replaced by David Smith on 1 March 2017. Following David Mellors' decision to leave the Committee agreed that all shares subject to performance conditions would lapse and that there would be no annual variable reward paid under the Bonus Banking Plan. However, given that David Mellors had built up equity in the Bonus Banking Plan when he made a positive contribution to stabilising the business through CEO change and transition to his successor, the Committee felt it was important that he stay incentivised during his notice period, therefore the decision was taken for David to remain eligible to receive the balance of his accrued and earned Bonus Banking Plan account. Details can be found on page 87.

Performance condition adjustments during 2017

In March 2015 the Committee agreed a set of adjustment principles to enable consistent and fair review in the event of an accounting decision impacting on incentives.

Underlying Operating Profit in 2017 included a credit of £5.2m following the LTPA contract amendment in December 2016. The contract amendment will see QinetiQ procure a new fleet of aircraft for the Empire Test Pilots' School and QinetiQ is, as a result, released from the commitment to fulfill the previously expected level of servicing obligations of the existing fleet. The Committee, following review with the Audit Committee, viewed this as neutral for the purposes of remuneration as the original charges reduced profit, and therefore incentive outturns, in prior years.

As in 2015 and 2016, the Committee again adjusted the performance conditions for the Performance Share Plan and Deferred Annual Bonus Matching Plan to reflect continuing operations and share buyback.

Neither Executive Director participated in the long-term incentives impacted by these changes owing to their respective hire dates with only the CEO participating in the annual incentive. The annual incentive paid to the CEO was £1,104,687 (86.4% of maximum) as detailed on page 86.

The following table provides a summary of all the key activities during the year. There was full attendance at each meeting except for March 2017 when Ian Mason was unable to be present.

	Base salary	Incentives	Equity	Governance	Resourcing
May 2016	Executive Remuneration market review	FY16 final results	2013 PSP/DAB vesting approval	Approve Directors' Remuneration Report	Iain Farley recruitment
July 2016	Executive Director and Executive Committee salary review			Shareholder feedback on Directors' Remuneration Report	David Mellors resignation
November 2016	Trends in Executive Remuneration Non-executive Group Chairman fees	FY17 half year forecast Draft Executive incentive design	Review of Executive Team shareholdings	Draft Executive Remuneration Policy review	David Smith recruitment
January 2017				Shareholder consultation arrangements	Miles Adcock resignation
March 2017		FY17 provisional results FY18 target setting	2014 PSP/DAB provisional vesting	Draft Directors' Remuneration Report Review of Committee remit and effectiveness	

Executive Director single figure remuneration

The auditor is required to report on the information in this table. Executive Director remuneration is shown as a single figure to provide an annual comparison between the actual remuneration for the performance year ended 31 March 2017 and the preceding year.

Element of remuneration (£'000)

Executive Director	Salary/Fees (£'000)		Benefits (£'000)		Annual Incentives (£'000)		Long-Term Incentives (£'000)		Pension (£'000)		Single Figure (£'000)	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Steve Wadey	568	520	33	31	1,105	999	–	–	113	104	1,819	1,654
David Mellors	332	456	21	26	645	850	–	–	66	91	1,064	1,423
David Smith	40	–	3	–	–	–	–	–	15	–	58	–

Additional supporting information for each Executive Director

To support the single figure, this section documents each element of remuneration and how the figure was calculated for the performance year ended 31 March 2017.

Salary/fees

The increase in the CEO's base salary reflects his first full year in post and a 2.5% (£14,000) per annum increase effective from 1 July 2016, in line with the typical 2016 salary increase across the Group.

The new CFO has commenced employment on the same base salary as his predecessor (£440,000).

Benefits

Benefits comprise of car allowance, healthcare, life assurance and income protection

Annual incentive

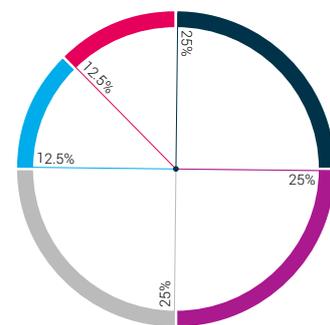
For the year ended 31 March 2017 achievement of on-target performance provides a payment equal to 112.5% of base salary, rising on a linear scale to 225% of base salary for achievement of stretch performance.

For FY17 and FY16, the scheme begins to pay out once threshold performance measures have been achieved. For the year ended 31 March 2017, financial performance measures make up 75% of the annual incentive opportunity with collective objectives and personal objectives accounting for the remaining 25%. For the year ended 31 March 2016, financial

performance measures and personal objectives were weighted at 80%/20% of the annual incentive opportunity.

The CEO/CFO were measured against the targets as shown below:

% of base salary



- Orders
- Underlying Operating Profit
- Underlying Cash Flow
- Collective Objectives
- Personal Objectives

Directors' Remuneration Report continued

Part 3: Annual Report on Remuneration continued

The auditor is required to report on the information in this table which summarises the key steps in the calculation of the annual incentive. Definitions of underlying measures of performance can be found in the glossary on page 157.

CEO/CFO financial performance measures	Weighting (%)	Threshold	Target	Stretch	Actual (excluding acquisitions)	% of maximum reward achieved	Plan contribution
Orders	25	£540.0m	£600.0m	£750.0m	£671.4m	73.8	235,846
Underlying operating profit	25	£95.0m	£105.0m	£115.0m	£115.1m	100.0	319,574
Underlying cash flow (Excluding LTPA and MSCA Capital Expenditure)	25	£72.0m	£80.0m	£96.0m	£100.0m	100.0	319,754
Collective objectives	12.5	40%	60%	100%	65%	56.3	89,880
CEO personal objectives	12.5	40%	60%	100%	90%	87.5	139,813
Overall result						86.4	1,104,687

Collective Objectives

At the beginning of the performance period five collective objectives were set by the Remuneration Committee and communicated to the Executive Directors, Executive Committee and Leadership Community. Three of the objectives focus on delivering our strategy and the remaining two focused on operational transformation so that we are organised effectively to succeed.

Lead and modernise the UK Defence 'Test & Evaluation enterprise'

The objective provided a focus on securing agreements for the modernisation of Boscombe Down and provision of future Test and Evaluation needs with key prime contractors. The objective was partially met.

Build the Company internationally

Significant progress was made, due to circumstances outside our control, the specifics of the objective were not delivered but remain live and therefore continue to be commercially sensitive and not disclosed. The objective was judged to be not delivered.

Innovate for customer advantage

The objective provided a focus on investing in new product capability opportunities. A number of these delivered contracts during the year but remain commercially sensitive and are not disclosed. The objective was measured as partially met.

Transformation programme

The objective provided a focus on generating a five-year Integrated Strategic Business Plan and delivering recurring savings of £20m for future growth investment. The objective was successfully met.

Organisation development

The objective focussed on establishing a matrix organisation, designed to support our new business model and strategy, and completion of the Leadership Development Programme for over 200 of our senior leaders. The objective was successfully met.

Personal objectives

At the beginning of the performance period two personal objectives were set by the Group Chairman and communicated to the CEO.

Growth

The objective provided a focus on developing a five-year business plan, generating a pipeline of potential acquisitions and building shareholder confidence. The five-year plan has been approved by the Board and the pipeline for potential acquisitions has already produced two successes via QinetiQ Target Systems and RubiKon Group Pty Limited. Positive shareholder feedback has shown that confidence is growing therefore the objective is judged to have been met.

Leadership

The objective provided a focus on forming the business leadership into an inspired, self-motivated winning group. Progress was to be shared with the Board at two reviews incorporating a clear focus on succession planning. Through organisation redesign, focused recruitment and development interventions and culture programmes the progress made has been positively received by the Board. The objective is judged to have been met.

The Bonus Banking Plan operates as follows:

- The Plan operates on a fixed four-year cycle. Year one of the Plan commenced on 1 April 2014, year two commenced 1 April 2015, year three commenced 1 April 2016, and year four commenced on 1 April 2017.
- Performance conditions are set at the beginning of each Plan year.
- At the end of each of the first three Plan years the performance against targets is assessed and the level of the incentive earned is determined and paid into the Plan account.
- At the end of each of the first three Plan years, 50% of the account balance will be paid and the balance retained and held in the Plan as notional shares.
- At the end of the fourth year, any remaining balance in the Plan account is paid out in shares.

The auditor is required to report on the information in this table. The measurement date for the CEO is 31 March 2017 and the Bonus Banking Plan annual contribution for 2017 is as reported in the single figure. Through the operation of the Plan the CEO received a cash payment of £857,475. The CEO retains 305,913 notional shares in his plan account.

	Notional shares on account at beginning of plan year 3 (31 March 2016)	30 Day average share price as at measurement Date (£)	Share value as at measurement date (£)	Bonus plan contribution for plan year 3 (£)	Dividend equivalent payment (£) (5.8p)	Bonus pool total value as at measurement date (£)	Gross cash payment for plan year 3 (£)	Bonus pool total value following cash payment (£)	Notional shares on account at beginning of plan year 4 (31 March 2017)
CEO	213,304	2.803	597,891	1,104,687	12,372	1,714,950	857,475	857,475	305,913
CFO	311,153	2.523	785,163	-	-	785,163	785,163	-	-

David Mellors resignation (measurement date 31 December 2016)

Following David Mellors' resignation, he was ineligible to receive the annual contribution due from the Bonus Banking Plan. However he retained the balance in his Bonus Banking Account.

Forfeiture

The CEO retained notional shares in his Plan account of which 50% were subject to forfeiture. Forfeiture would have been enacted if Group Underlying Operating Profit was less than £85.0m for FY17. FY17 Group Underlying Operating Profit was £115.1m (excluding contribution from acquisitions) therefore no notional shares were forfeited.

Discretion

For the year ended 31 March 2017, no discretion was applied to the calculated results; therefore, £1,104,687 has been reported in the single figure calculation.

For the year ended 31 March 2016, financial targets were exceeded providing a contribution of 85.4% of base salary for the CEO and 82.9% of base salary for the CFO. £999,117 and £849,917 has been reported in the single figure table. No discretion was applied to these contributions.

Long-term incentive summary

Deferred Annual Bonus Matching Plan

Following David Mellor's resignation any award due under the 2014 Deferred Annual Bonus Matching Award lapsed. The CEO did not participate in this award.

Performance Share Plan

Following David Mellor's resignation any award due under the 2014 Performance Share Plan lapsed. The CEO did not participate in this award.

A figure of zero has been reported in the single figure for Steve Wadey, David Mellors and David Smith respectively.

Long-term incentive plan results

The 2014 Performance Share Plan achieved 50.3% vesting and the 2014 Deferred Annual Bonus Matching Plan achieved 41.4% vesting.

Scheme interests awarded during the financial year ended 31 March 2017

The auditor is required to report on the information in this table. Performance conditions under the PSP are; EPS growth between 3% – 10% per annum; and TSR performance between median and upper quartile when compared to the FTSE250. The following awards were made to Executive Directors.

	Plan name	Performance measure	Grant date	Award as percentage of salary	Face value of award (£'000)	Share price at date of grant (£)	No. of shares granted	Performance period from – to	Percentage of award vesting at threshold
CEO	PSP 2016	EPS	1 Jul 16	95.0%	534	2.24	238,095	1 Apr 16 31 Mar 19	25%
CEO	PSP 2016	TSR	1 Jul 16	95.0%	534	2.24	238,095	1 Apr 16 31 Mar 19	30%

Between the approval date and grant date share price movement resulted in a revised award as a percentage of salary.

Pension

No Directors participate in the QinetiQ Pension Scheme. Pension figure represents cash in lieu of pension equating to 20% of base salary for both years.

The auditor is required to report on the information shown here over payments to past Directors.

Payments to past Directors and payment for loss of office

No payments were made to past Directors and no payments were made for loss of office.

Directors' Remuneration Report continued

Part 3: Annual Report on Remuneration continued

Single figure remuneration for each Non-executive Director

The auditor is required to report on the information in this table. Non-executive Director remuneration is shown as a single figure to provide an annual comparison between the actual remuneration awarded during the financial year ended 31 March 2017 and the preceding year.

Non-executive Director	Salary/fees (£'000)		Benefits (£'000)		Committee Chair fees (£'000)		US/UK attendance fee (£'000)		Single figure (£'000)	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Lynn Brubaker	46	8	–	–	–	–	15	3	61	11
Admiral Sir James Burnell-Nugent	46	45	–	–	9	9	2	–	57	54
Mark Elliott	238	236	75	75	–	–	–	–	313	311
Michael Harper	46	45	–	–	19	19	2	–	67	64
Ian Mason	46	45	–	–	–	–	–	–	46	45
Paul Murray	46	45	–	–	9	9	2	–	56	54
Susan Searle	46	45	–	–	–	–	2	–	48	45

Mark Elliott and Lynn Brubaker are US residents, therefore Mark is entitled to an accommodation allowance of £75,000 and Lynn is entitled to receive a \$4,000 fee for attending UK meetings. UK-based Non-executive Directors are entitled to receive a £2,500 fee for attending US meetings.

Statement of Directors' shareholding and share interests

The auditor is required to report on the information in this table. Set out below are the Directors' shareholdings as at 31 March 2017.

In relation to the revised Executive Shareholding Policy adopted on 1 April 2017 the Company requires Executive Directors to hold shares equivalent to 300% (CEO) and 200% (CFO) of base salary.

The CEO does not currently meet the minimum shareholding requirement; with a current holding equivalent to 10% of base salary using a share price of £2.726 (three-month average to 31 March 2017). This reflects his recent appointment as CEO and the lack of any opportunity for share-based awards to vest.

The CFO does not currently meet the minimum shareholding requirement; with a current holding equivalent to 0% of base salary using a share price of £2.726 (three-month average to 31 March 2017). This reflects his recent appointment as CFO and the lack of any opportunity for share-based awards to vest.

	Shares beneficially owned	Shares subject to performance conditions	Shares not subject to performance conditions	Total shares held at 23 May 2017
Steve Wadey	21,925	839,826	–	861,751
David Smith	–	–	–	–
Mark Elliott	125,000	–	–	125,000
Michael Harper	30,000	–	–	30,000
Admiral Sir James Burnell-Nugent	11,419	–	–	11,419
Paul Murray	74,942	–	–	74,942
Susan Searle	17,500	–	–	17,500
Ian Mason	10,000	–	–	10,000
Lynn Brubaker	12,000	–	–	12,000

Shares beneficially owned comprise shares held under the Share Incentive Plan (including matched shares) and shares owned by the Executive and any connected persons.

Shares subject to performance conditions comprise awards made under the Performance Share Plan for 2016 and 2015.

Total scheme interests summary

The auditor is required to report on the information in this table. Total scheme interests, including those awarded during the financial year ended 31 March 2017, are as follows.

Steve Wadey

Plan name	Date of grant	Number 1 April 2016	Granted in year (maximum potential of awards)	Exercised/ vested in year	Lapsed in year	Number 31 March 2017	Market price on date of grant	Earliest vest date	Latest vest date
PSP 2015	28 Jul 15	363,636	–	–	–	363,636	231.0	28 Jul 18	28 Jul 18
PSP 2016	1 Jul 16	–	476,190	–	–	476,190	224.4	1 Jul 19	1 Jul 19
		363,636	476,190	–	–	839,826			

David Mellors

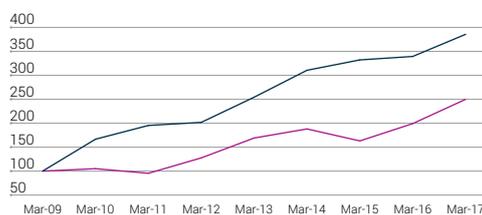
Plan name	Date of grant	Number 1 April 2016	Granted in year (maximum potential of awards)	Exercised/ vested in year	Lapsed in year	Number 31 March 2017	Market price on date of grant	Earliest vest date	Latest vest date
PSP 2013	28 Jun 13	300,000	–	–	300,000	–	180.4	28 Jun 16	28 Jun 16
DAB Match 2013	28 Jun 13	157,196	–	–	157,196	–	180.4	28 Jun 16	28 Jun 16
PSP 2014	28 May 14	293,550	–	–	293,550	–	200.0	28 May 17	28 May 17
DAB Match 2014	1 Jul 14	108,779	–	–	108,779	–	207.7	1 Jul 14	1 Jul 17
PSP 2015	28 Jul 15	285,714	–	–	285,714	–	231.0	28 Jul 18	28 Jul 18
		1,145,239	–	–	1,145,239	–			

PSP awards are subject to two equally weighted performance conditions; EPS growth between 3% – 10% per annum; and TSR performance between median and upper quartile when compared to the FTSE250. DAB Match is subject to the same EPS condition as the PSP. The price of a QinetiQ share at 31 March 2017 was 279.0p. The highest and lowest prices of a QinetiQ share during the year ended 31 March 2017 were 217.5p and 285.0p. There have been no changes to the interests shown above between 31 March 2017 and 23 May 2017.

Performance review

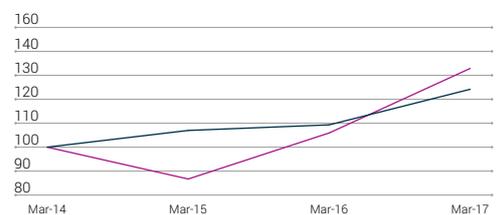
The eight-year and three-year charts show the Company's Total Shareholder Return over the period from 31 March 2009 to 31 March 2017 and 31 March 2014 to 31 March 2017 compared with the FTSE 250 (excluding investment trusts) over the same period based on spot values. The Committee has chosen to demonstrate the Company's performance against these indices as it is an appropriate sector comparison within the index in which the Company is listed. This comparator group is also used to measure TSR performance in the PSP.

Eight-year comparator chart



- QinetiQ
- FTSE 250 (excluding investment trusts)

Three-year comparator chart



- QinetiQ
- FTSE 250 (excluding investment trusts)

Directors' Remuneration Report continued

Part 3: Annual Report on Remuneration continued

CEO remuneration

The table below shows the CEO's remuneration over the same performance period as the Total Shareholder Return chart (31 March 2009 to 31 March 2017):

Year ended 31 March	Salary/fees	Single figure	Annual Bonus (% of maximum)	Long-Term Incentives (% of maximum vesting)
2017 Steve Wadey	568,132	1,819,177	86.42%	–
2016 Steve Wadey	520,219	1,654,546	85.36%	–
2016 David Mellors	455,885	1,423,382	82.86%	–
2015 David Mellors	501,227	1,725,960	88.55%	13.91%
2015 Leo Quinn	469,776	673,979	–	–
2014 Leo Quinn	610,844	2,177,742	76.97%	15.43%
2013 Leo Quinn	593,050	3,992,001	100.00%	40.27%
2012 Leo Quinn	580,000	1,495,284	100.00%	–
2011 Leo Quinn	580,000	1,327,156	100.00%	–
2010 Leo Quinn	217,872	886,564	–	–
2010 Graham Love	266,667	1,246,320	–	–

Percentage change in CEO remuneration

The following table compares change in CEO remuneration with an employee comparator group (averaged per capita). The comparison group (4,000 employees) represents the UK principal businesses in service between 1 April 2016 and 31 March 2017. For comparison purposes, the CEO's full year equivalent figures have been used for 2016 (CEO joined on 27 April 2015).

	CEO			Comparison group		
	2017	2016	% change	2017	2016	% change
Base salary	£568,132	£560,000	1.5%	£39,694	£38,591	2.9%
Benefits	£32,725	£34,939	-6.3%	£1,138	£1,173	-3.1%
Annual bonus	£1,104,687	£1,075,520	2.7%	£1,506	£912	65.1%

Remuneration Policy for all employees

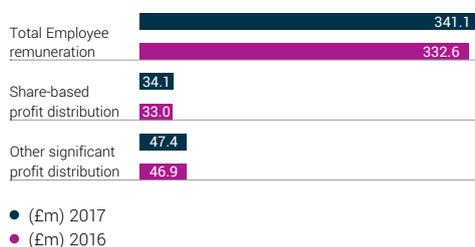
All employees of QinetiQ are entitled to base salary, benefits and pension. UK and Australia based employees are entitled to participate in the QinetiQ Share Incentive Plan. The maximum incentive opportunity available is based on the seniority and responsibility of the role. Participation in the PSP is available to Executive Directors; senior managers and selected employees throughout the organisation are also invited to participate. The Committee is advised of the general reward policy for other employees and of any significant changes proposed.

Gender related pay

QinetiQ is subject to gender pay reporting and will be publicising information during the coming year.

Relative importance of spend on pay

The graph below shows actual spend on all employee remuneration, shareholder dividends and buybacks and any other significant use of profit and cash within the previous two financial years.



Implementation of policy for the year ending 31 March 2018

Salary/fees

Non-executive Director fees were last increased on 1 July 2015, resulting in an increase in base fees from £43,000 to £46,000 per annum. Non-executive Director fees will be reviewed again in July 2017. The Non-executive Group Chairman's fees were last increased on 1 December 2016 resulting in an increase to £242,000. Salaries and fees are reviewed in line with Policy.

Executive Directors are permitted to accept one external non-executive director position with the Board's approval. Any fees received in respect of these appointments may be retained by the Executive Director.

The CEO does not hold any non-executive directorships in other companies. David Smith was appointed non-executive director of Motability Operations Group plc on 1 July 2010. Non-executive director fees, as reported in the 2016 Motability Operations Group plc annual report were £43,000 per annum.

	Fees effective as at 1 April 2017 £
Non-executive Group Chairman	£242,000
Accommodation allowance for Non-executive Group Chairman	£75,000
Basic fee for UK Non-executive Director	£46,000
Additional fee for chairing a Committee	£9,000
Additional fee to Deputy Chairman/Senior Independent Non-executive Director	£10,000
Additional fee for attendance at a Board meeting held in US by UK resident Non-executive Director	£2,500
Additional fee for attendance at a Board meeting held in UK by US resident Non-executive Director	\$4,000

Incentives for Executives

The table below shows the measures and relative weighting for Bonus Banking Plan (Element A) for the CEO and CFO:

	Performance measure (excluding 2018 acquisitions)	Relative weighting (%)
Bonus Banking Plan (Element A) (target performance 100% of base salary, stretch performance 200% of base salary)	Underlying Operating Profit	25.0%
	Underlying Net Cash from Operations (Pre-Capex)	25.0%
	Orders	25.0%
	Collective Objectives	12.5%
	Personal Objectives	12.5%

Details of specific performance targets for the Bonus Banking Plan have not been provided as they are deemed commercially sensitive. They will be disclosed retrospectively in next year's Annual Report on Remuneration.

The Deferred Share Plan (Element B) will award a maximum of 125% of base salary for achieving Stretch performance with 35% of maximum payable at Target performance. The 2018 performance measure will be Underlying Operating Profit but with different performance targets compared to the Bonus Banking Plan. Awards will be made in July 2018 based on 2018 performance. Details of specific performance targets for the Deferred Share Plan (Element B) have not been provided as they are deemed commercially sensitive. They will be disclosed retrospectively in next year's Annual Report on Remuneration.

Michael Harper

Remuneration Committee Chairman
25 May 2017