General Dynamics United Kingdom Limited

Annual report and financial statements

Registered number 1911653
31 December 2016

Contents

Directors' Report	1
Strategic Report	4
Statement of directors' responsibilities in respect of the Directors' report and the Strategic report and the financial statements	5
Independent auditor's report to the members of General Dynamics United Kingdom Limited	6
Income statement	7
Balance sheet	8
Other Comprehensive Income	9
Statement of Changes in Equity	9
Notes	10

Directors' Report

The directors present their annual report and the audited financial statements for the year ended 31 December 2016.

Principal Activities

General Dynamics United Kingdom ("GDUK") specialises primarily in the design, delivery and through-life support of solutions in the Command, Control, Communications, Computing and Information (C4I) domain and armoured vehicles; most notably the AJAX programme.

C4I (Command, Control, Communications, Computing and Information) is the delivery of vital information via the integration of technology and networks. This information is used to observe and act decisively in the field of battlespace management. GDUK delivers Bowman, one of the world's most advanced battlefield communication systems, to the UK MoD.

GDUK are contracted for the Demonstration, Production and Extended Support Phases of the AJAX programme for the UK Army. AJAX will offer unparalleled protection, weight and agility for a vehicle of its class, along with the most advanced Intelligence, Surveillance, Target Acquisition and Reconnaissance (ISTAR) capabilities on the AJAX variant platform. In service, users will benefit from the key advantages of the AJAX common base platform approach, including a lower cost of ownership and smaller logistics footprint thanks to the commonality of its components across the fleet.

GDUK also performs Long Term Evolution (LTE) Research and Development, and provides a range of best-in-class avionics products including tactical processors, ground to air data links, weapon management computers and secure data recorders. This wealth of experience in the avionics business has made GDUK a key supplier to programmes such as Typhoon and Wildcat.

Research and development

The Company has a policy of selective investment in the design and development of new technologies and capabilities that support our business.

Our major areas of interest include the development of open systems architectures, modelling and simulation. . Work continues to maximise leverage from available technologies from within the larger General Dynamics Corporation.

We continue to use our EDGE UK® facility to source potential solutions and thereby help provide Small and Medium Enterprises with new business opportunities.

Results and proposed dividend

Profit after taxation for the year ended 31 December 2016 was £66.8m compared to £56.5m for the year ended 31 December 2015. The directors paid a dividend of £120m for the year (*2015: £0m*).

Directors' Report *(continued)*

Directors

The directors who held office during the year were as follows:

Sir A T Cahn
Lord P K Levene of Portsoken (Chairman)
C Marzilli
G L Whited

Corporate Responsibility

During 2016, the Company continued to build on its solid progress and actively ensured delivery of our stakeholder commitments. Our website explains to stakeholders the Company policies, strategies and business progress, and is updated on a regular basis. Employees receive frequent updates on our progress and the latest Company initiatives through the weekly e-newsletter, which they all receive.

The Company strives to maintain the highest standards of ethical conduct and corporate responsibility. Our employees receive annual training on this subject, and support mechanisms are in place for employees through an information telephone line. By operating proactive policies, the Company manages its customer and supplier relationships responsibly.

The Company is committed to the Armed Forces Corporate Covenant. We support service leavers by attending Transition Fairs designed to promote employment opportunities, contribute to military thought leadership and support employees that wish to serve in the Reserves and undertake military training.

The single greatest contribution to the communities in which the Company operates is the sustained wealth created by providing hundreds of highly skilled jobs. Charitable donations and community involvement are encouraged across all of our sites and employees are supported by well-developed policies and practices.

Employees' involvement

Effective training and development of a highly skilled workforce is considered key to future business success. The Company also supports the employment and retention of disabled persons. In the event of members of staff becoming disabled every effort is made to ensure that their employment within the Company continues either in their current job or in a suitable alternative. The Company would endeavour to make any reasonable adjustments for disabled employees to fulfil their job role responsibility. It is the Company's policy to support disabled employees in all aspects of their training, development and promotion where it benefits the employee and the Company.

A comprehensive employee communications programme is active which includes bi-annual all-employee briefings in addition to monthly 'flow-down' meetings and the weekly e-bulletin, Dynamics Extra. Topics covered include market forecasts, product development, facilities and benefit changes and Company financial status.

The Company encourages participation and involvement in matters which affect their interests as employees. Encouragement is given to employees to provide feedback using organisation wide questionnaires with the aim of achieving a common awareness on all aspects affecting the performance of the Company.

Political and charitable contributions

The company made no political contributions during the year (*2015: £nil*). Donations to local community charities amounted to £26,663 in 2016 (*2015:* £73,116).

Directors' Report *(continued)*

Disclosure of information to auditor

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

Auditor

Pursuant to Section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office.

By Order of the Board

Lord P K Levene of Portsoken
Director

22/6/17

21 Holborn Viaduct
London
EC1A 2DY
22 JUNE 2017

Strategic Report

Business Review

The year ended 31 December 2016 has been a positive year with both turnover and profit above target. Total turnover increased by 28% to £565m in 2016 compared to 2015. Turnover was better than GDUK management expectations, driven by meeting programme deliverables earlier and additional volume across multiple programmes. Total operating profit increased by £10.2m to a profit of £79.0m in 2016 compared to profit of £68.8m in 2015. Our operating earnings as a percentage of sales slightly decreased to 14% in 2016 from 16% in 2015. Additional earnings were largely driven by increased volume and maintaining a low cost base following saving initiatives in prior years.

Performance against top level strategic objectives was above expectations. Our goal to grow our order book through UK MoD orders performed above expectations as GDUK was awarded a contract to provide in-service support for the AJAX fleet until 2024. In addition, the company has opened a new Armoured Fighting Vehicle (AFV) Assembly, Integration and Testing (AIT) facility in Merthyr, South Wales.

The AJAX programme achieved key milestones in 2016 including completing Test Rigs 6 & 7 for Mine Test, Unmanned Live Fire 1 & 2 and Training Preliminary Design alongside completion of Production Vehicle 1 Hull and Initial Office Build out at Merthyr AJAX continues to be the UK Army's highest Land Equipment Priority, is fully funded and will form the heart of the new Strike Brigades concept.

Support to the deployed Bowman Communications System remains a strategic goal as an enabler to win the award of the Design and Development phase of Morpheus, the Bowman successor program. The Morpheus Assessment Phase activity concluded that the optimal way to deliver the right capability to the user in a timely manner was through MoD working with GDUK to open the tactical architecture to enable a technical and commercial level playing field. Existing Bowman Programmes are operating to plan.

As a result of the events in North Africa GDUK received a Letter of Credit claim for the non-completion of a contract with the government of Libya in 2013. The value of the claim was £15m and was paid (despite GDUK's protest) via established bonds. In response, GDUK initiated arbitration proceedings in Switzerland against the State of Libya to recover the bond monies as well as damages for breach of contract permitted under Swiss law. The arbitration hearings were completed in December 2014 and, in January 2016, found in favour of GDUK. A Petition confirming foreign arbitral award was served on the Libyan Ministry of Defence in April 2016. In June 2016 GDUK filed a return of service with U.S. District Court of Columbia and subsequent default against respondent Libya. GDUK were awarded the default in October 2016 and have received the clerk's certificate certifying the judgement is final. The claim is shown in trade debtors' amounts falling due over one year as we anticipate a drawn out recovery process.

Business performance is assessed using several key performance indicators in addition to the traditional financial measures. These are focused on delivery performance in development and production, staff turnover, the success rate of new business pursuits and measures of cost effectiveness and productivity. Variance analysis is performed monthly.

Company risks and opportunities are reviewed regularly by the executive management at the individual programme and the enterprise levels. The major risk to the business associated with strategic, financial, or significant operating initiatives is securing the funds following the award of the Libyan bond claim.

Lord P K Levene of Portsoken
Director

21 Holborn Viaduct
London
EC1A 2DY
22 JUNE 2017

Statement of directors' responsibilities in respect of the Directors' report and the Strategic report and the financial statements

The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 101 Reduced Disclosure Framework.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

KPMG
1 Forest Gate
Brighton Road
Crawley
RH11 9PT

Independent auditor's report to the members of General Dynamics United Kingdom Limited

We have audited the financial statements of General Dynamics United Kingdom Limited for the year ended 31 December 2016 set out on pages 10 to 36. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice), including FRS 101 *Reduced Disclosure Framework.*

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

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's web-site at www.frc.org.uk/auditscopeukprivate

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report and the Strategic Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and from reading the Strategic report and the Directors' report:

- We have not identified material misstatements in those reports; and
- In our opinion, those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

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

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

Steve Masters (Senior Statutory Auditor)
For and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
1 Forest Gate
Brighton Road
Crawley
RH11 9PT
22 June 2017

Income statement

for the year ended 31 December 2016

	Note	2016 £000	2015 £000
Turnover	2	**565,405**	439,995
Cost of sales		**(447,433)**	(345,422)
Gross profit		**117,972**	94,573
Administrative expenses	6	**(38,998)**	(25,790)
Operating profit		**78,974**	68,783
Interest receivable and similar income	4	**531**	1,001
Interest payable and similar charges	5	**(24)**	(4)
Profit on ordinary activities before taxation	6	**79,481**	69,780
Tax on profit on ordinary activities	8	**(13,711)**	(13,318)
Retained profit for the financial year		**65,770**	56,462

The profit for the year and the preceding year arises entirely from continuing operations.

There is no material difference between the results reported in the profit and loss account and the results on an unmodified historical cost basis.

The notes on pages 10 to 36 form part of these financial statements.

Balance sheet

At 31 December 2016

	Note	2016 £000	2015 £000
Fixed assets			
Goodwill	9	**2,400**	17,141
Intangible assets	9	**6,186**	6,669
Tangible assets	10	**24,919**	19,860
		33,505	43,670
Current assets			
Stock and work in progress	11	**41**	240
Debtors	12	**329,174**	313,461
Other financial assets	15	**7,971**	421
Cash at bank		**470**	-
		337,656	314,122
Creditors: amounts falling due within one year	13	**(151,257)**	(102,367)
Other financial liabilities	15	**-**	(11,020)
Net current assets		**186,399**	200,735
Debtors: amounts falling due after more than one year	12	**15,678**	15,678
Other financial assets	15	**12,667**	968
Total assets less current liabilities		**248,249**	261,051
Creditors: amounts falling due after more than one year	14	**(7,829)**	(155)
Other financial liabilities	15	**-**	(55,315)
Provisions for liabilities and charges	17	**(9,921)**	(5,483)
Net assets including pension liability		**230,499**	200,098
Capital and reserves			
Called up share capital	18	**9,262**	9,262
Capital redemption reserve		**88**	88
Other reserves		**1**	1
Cashflow hedge reserve		**20,638**	(64,946)
Profit and loss account		**200,510**	255,693
Equity Shareholders' funds		**230,499**	200,098

These financial statements were approved by the board of directors on 22 JUNE 2017 and were signed on its behalf by:

Lord P K Levene of Portsoken
Director

The notes on pages 10 to 36 form part of these financial statements.

Other Comprehensive Income

	2016 £000	2015 £000
Profit for the financial year	**65,770**	56,462
Actuarial gain/(loss) recognised on the pension scheme	**(3,624)**	4,649
Movement on deferred tax relating to actuarial gain on the pension scheme	**616**	(837)
Reversal of deferred tax on de-recognition of pension surplus	**(616)**	837
De-recognition of pension surplus	**3,381**	(5,499)
Total comprehensive income for the year	**65,527**	55,612

Statement of Changes in Equity

	Called up Share Capital £000	Capital redemption reserve £000	Other reserves £000	Cash flow hedge reserve £000	Profit and loss account £000	Total £000
Balance at 1 January 2016	**9,262**	**88**	**1**	**(64,946)**	**255,693**	**200,098**
Retained profit for the year	-	-	-	-	65,770	65,770
Actuarial loss on pension schemes	-	-	-	-	(3,624)	(3,624)
IFRS 2 share based payment charges	-	-	-	-	(710)	(710)
IAS 19 (derecognition of pensions surplus)	-	-	-	-	3,381	3,381
Fair value of cashflow hedges	-	-	-	85,584		85,584
Dividend paid	-	-	-	-	(120,000)	(120,000)
At 31 December 2016	**9,262**	**88**	**1**	**20,638**	**200,510**	**230,499**

	Called up Share Capital £000	Capital redemption reserve £000	Other reserves £000	Cash flow hedge reserve £000	Profit and loss account £000	Total £000
Balance at 1 January 2015	**9,262**	**88**	**1**	**(31,392)**	**200,389**	**178,348**
Retained profit for the year	-	-	-		56,462	56,462
Actuarial gain on pension schemes	-	-	-		4,649	4,649
IFRS 2 share based payment charges	-	-	-		(308)	(308)
IAS 19 (derecognition of pensions surplus)	-	-	-		(5,499)	(5,499)
Fair value of cashflow hedges	-	-	-	(33,554)	-	(33,554)
At 31 December 2015	**9,262**	**88**	**1**	**(64,946)**	**255,693**	**200,098**

Notes

(forming part of the financial statements)

1 Accounting policies

General Dynamics United Kingdom Limited (the "Company") is a company incorporated and domiciled in the UK.

Basis of Preparation

These financial statements were prepared in accordance with Financial Reporting Standard 101 *Reduced Disclosure Framework ("FRS 101").* The amendments to FRS 101 (2014/15 Cycle) issued in July 2015 and effective immediately have been applied.
In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs"), but makes amendments where necessary in order to comply with Companies Act 2006 and has set out below where advantage of the FRS 101 disclosure exemptions has been taken.

The Company's ultimate parent undertaking, General Dynamics Corporation includes the Company in its consolidated financial statements. The consolidated financial statements of General Dynamics Corporation are prepared in accordance with US GAAP and International Financial Reporting Standards and are available to the public and may be obtained from 2941 Fairview Park Drive, Suite 100, Falls Church, VA 22042.

In these financial statements, the company has applied the exemptions available under FRS 101 in respect of the following disclosures:

- Cash Flow Statement and related notes;
- Disclosures in respect of transactions with wholly owned subsidiaries;
- Disclosures in respect of capital management; and
- Disclosures in respect of the compensation of Key Management Personnel.

As the consolidated financial statements of General Dynamics Corporation include the equivalent disclosures, the Company has also taken the exemptions under FRS 101 available in respect of the following disclosures:

- IFRS 2 Share Based Payments in respect of group settled share based payments, excluding the Save As You Earn scheme;
- Certain disclosures required by IAS 36 Impairment of assets in respect of the impairment of goodwill and indefinite life intangible assets; and
- Certain disclosures required by IFRS 13 Fair Value Measurement and the disclosures required by IFRS 7 Financial Instrument Disclosures.

The Company proposes to continue to adopt the reduced disclosure framework of FRS 101 in its next financial statements.

Notes *(continued)*

1 Accounting policies *(continued)*

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these financial statements and in preparing an opening FRS 101 IFRS balance sheet at 1 January 2014 for the purposes of the transition to FRS 101.

Going Concern

The directors have assessed the Company's financial resources and forecasts and based on this review have concluded that it is appropriate to continue to adopt the going concern basis of accounting in preparing these financial statements.

Intangible assets

(i) Goodwill

Goodwill represents the future economic benefits arising from assets acquired in a business combination that are not individually identified and separately recognised. Such benefits include future synergies expected from the combination and intangible assets not meeting the criteria for separate recognition. Goodwill is carried at cost less accumulated impairment losses. Goodwill is not amortised and is tested annually for impairment at country level, representing the lowest level at which it is monitored for internal management purposes, by assessing the recoverable amount of each cash generating unit or groups of cash generating units to which the goodwill relates. The recoverable amount is assessed by reference to the net present value of expected future pre-tax cash-flows ('value-in-use') or fair value less costs to sell if higher. The discount rate applied is based upon the Group's weighted average cost of capital with appropriate adjustments for the risks associated with the relevant cash generating unit or groups of cash generating units. When the recoverable amount of the goodwill is less than its carrying amount, an impairment loss is recognised immediately in the income statement which cannot be subsequently reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

(ii) Customer relationships

Customer relationships represent the future economic benefits arising from specific supplier or customer lists, or are party to supplier or customer relationships that are valuable. Customer relationships are held at cost less any provisions for impairment, with impairment reviews being performed annually. Amortisation commences when the Customer Relationship assets are available and is over the estimated useful life of 8 years.

(iii) Other Intangibles

The other Intangibles are a Royalty-Fee licence for relief from royalty, and backlog. Royalty-Fee licence relief and backlog are held at cost less any provisions for impairment, with impairment reviews being performed annually. Amortisation commences when the Royalty-Fee licence relief and backlog assets are available and is over the estimated useful life of 8 years.

(iv) Computer software

Where software is not an integral part of a related item of computer hardware, it is classified as an intangible asset. Costs that are directly associated with the acquisition or production of identifiable software products controlled by the Group, which are expected to generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Capitalised costs include those of software licences and development, including costs of employees, consultants and an appropriate portion of relevant overheads. Costs that are directly associated with identifying, sourcing, evaluating or maintaining computer software are recognised as an expense as incurred. Software under development is held at cost less any provisions for impairment, with impairment reviews being performed annually. Amortisation commences when the software assets are available for use and is over their estimated useful lives of three to four years.

Notes *(continued)*

1 Accounting policies *(continued)*

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses.
Where parts of an item of tangible fixed assets have different useful lives, they are accounted for as separate items of tangible fixed assets.

Leases in which the Company assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Where land and buildings are held under leases the accounting treatment of the land is considered separately from that of the buildings. Leased assets acquired by way of finance lease are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and less accumulated impairment losses. Lease payments are accounted for as described below.

Depreciation is charged to the profit and loss account on a straight-line basis over the estimated useful lives of each part of an item of tangible fixed assets. Leased assets are depreciated over the shorter of the lease term and their useful lives. Land is not depreciated. The estimated useful lives are as follows:

Freehold Buildings:	50 years
Leasehold Land and Buildings:	Life span of lease
Plant, Machinery and Motor Vehicles:	4-8 years
Finance Lease Plant and Machinery:	3-5 years

Fixed asset investments

Investments in subsidiaries are carried at cost less provision for impairment (if any).

Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the profit and loss account except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is recognised directly in equity or other comprehensive income.

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

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised.

Notes *(continued)*

1 Accounting policies *(continued)*

Stocks and work in progress

Stocks are stated at the lower of cost and net realisable value. Cost is based on the first-in first-out principle and includes expenditure incurred in acquiring the stocks, production or conversion costs and other costs in bringing them to their existing location and condition. In the case of manufactured stocks and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

Long Term Contracts

The majority of projects at GDUK are long-term development or support contracts spanning multiple financial years and are accounted for under IAS11. Contract revenue and margin is recognised in line with the effort expended in the performance of these programmes. This is known as the percentage-of-completion method, and is the preferred method of revenue recognition for the corporation. Percentage-of-completion is measured on a cost input basis with revenue being recognised in the period in which products are delivered or services are rendered to the customer, provided that entitlement to receive payment from the customer has been established and the revenue has been earned. The level of effort expended is derived from the actual project cost for each contract each period.

Each project has a Programme Finance Status Report (PFSR) which will highlight the "to-go" or prospective booking rate for that project. A comprehensive Estimate at Completion (EAC) is completed at least once during every 12 months which reviews all costs incurred, costs to go and risks. If an increase is expected in out-turn profits on a project then a change in the to-go (prospective) booking rate for that project will be put forward for approval.

Short Term Contracts

On short term contracts turnover represents amounts invoiced during the year net of Value Added Tax. A short term contract is a contract that is started and completed within the same financial year.

Foreign Currencies

Transactions in foreign currencies are translated to the Company's functional currencies at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined. Foreign exchange differences arising on translation are recognised in the profit and loss account.

Warranties

Provision is made for the estimated cost of work to be performed under warranty on products sold before the balance sheet date.

Research and Development

Expenditure on research activities is recognised in the profit and loss account as an expense as incurred. Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the Company intends and has the technical ability and sufficient resources to complete development, future economic benefits are probable and if the Company can measure reliably the expenditure attributable to the intangible asset during its development. Development activities involve a plan or design for the production of new or substantially improved products or processes. The expenditure capitalised includes the cost of materials, direct labour and an appropriate proportion of overheads and capitalised borrowing costs. Other development expenditure is recognised in the profit and loss account as an expense as incurred. Capitalised development expenditure is stated at cost less accumulated amortisation and less accumulated impairment losses.

Notes (continued)

1 Accounting policies *(continued)*

Leases

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents are charged as expenses in the periods in which they are incurred. Payments (excluding costs for services and insurance) made under operating leases are recognised in the profit and loss account on a straight-line basis over the term of the lease. Lease incentives received are recognised in the profit and loss account as an integral part of the total lease expense.

Employee Benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an expense in the profit and loss account in the periods during which services are rendered by employees.

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Company's net obligation in respect of defined benefit pension plans and other post employment benefits is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets (at bid price) are deducted. The Company determines the net interest on the net defined benefit liability/(asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability/(asset).

The discount rate is the yield at the reporting date on bonds that have a credit rating of at least AA that have maturity dates approximating the terms of the Company's obligations and that are denominated in the currency in which the benefits are expected to be paid.

Remeasurements arising from defined benefit plans comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest). The Company recognises them immediately in other comprehensive income and all other expenses related to defined benefit plans in employee benefit expenses in profit or loss.

The calculation of the defined benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Company, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of any minimum funding requirements.

Retirement Plans.

Our Company sponsors a hybrid arrangement that includes both a defined contribution section and a defined benefit section. The defined benefit section was closed from 6th April 1997, at which time members ceased to accrue benefits on a defined benefit basis. The assets of the scheme are held separately from the assets of the Company.

The defined benefit section costs and obligations depend on several assumptions and estimates. The key assumptions include mortality and interest rates used to discount estimated future liabilities and projected long-term rates of return on plan assets. We determine the long-term expected rate of return on cash by reference to bank base rates, the long-term return on bonds by reference to UK long dated government and corporate bond yields, and the long-term rate of return on equities based on the rate of return on bonds allowing for forward-looking returns.

These retirement plan estimates are based on our best judgement, including consideration of current and future market conditions. In the event any of the assumptions change, pension and post-retirement benefit cost could increase or decrease. In line with the requirements of the Scheme regulator any shortfall in asset value in the actuarial valuation for the defined benefit section are met by the company over an agreed period. For additional information on the Pension Scheme, see note 21 of the Annual report and financial statements.

Notes *(continued)*

1 Accounting policies *(continued)*

Employee Benefits (continued)

Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

Termination benefits

Termination benefits are recognised as an expense when the company is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised as an expense if the company has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

Employee share schemes

The share option programme allows employees to acquire shares in the Company. The fair value of options granted after 7 November 2002 and those not yet vested as at the effective date of FRS 20, is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using a Black - Scholes option pricing model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where variations are due only to share prices not achieving the threshold for vesting.

For cash settled share based payment transactions, the fair value of the amount payable to the employee is recognised as an expense with a corresponding increase in liabilities. The fair value is initially measured at grant date and spread over the period during which the employees become unconditionally entitled to payment. The fair value is measured based on an option pricing model taking into account the terms and conditions upon which the instruments were granted. The liability is revalued at each balance sheet date and settlement date with any changes to fair value being recognised in the profit and loss account.

Classification of financial instruments issued by the Company

Following the adoption of IAS 32, financial instruments issued by the Company are treated as equity only to the extent that they meet the following two conditions:

(a) they include no contractual obligations upon the company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the company; and
(b) where the instrument will or may be settled in the company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the company's own equity instruments or is a derivative that will be settled by the company's exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities, trade and other debtors, cash and cash equivalents, loans and borrowings, and trade and other creditors.

Notes *(continued)*

1 Accounting policies *(continued)*

Trade and other debtors and creditors

Trade and other debtors are recognised initially at fair value. Subsequent to initial recognition they are measured at amortised cost using the effective interest method, less any impairment losses.

Trade and other creditors are recognised initially at fair value. Subsequent to initial recognition they are measured at amortised cost using the effective interest method.

Investments in debt and equity securities

Ordinary shares are stated at cost less impairment. Financial instruments held for trading, or designated upon initial recognition or at the IAS 39 transition date if later are stated at fair value, with any resultant gain or loss recognised in profit or loss.

Other investments in debt and equity securities held by the Company are classified as being available-for-sale and are stated at fair value, with any resultant gain or loss being recognised directly in equity (in the fair value reserve), except for impairment losses and, in the case of monetary items such as debt securities, foreign exchange gains and losses. When these investments are derecognised, the cumulative gain or loss previously recognised directly in equity is recognised in profit or loss. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss.

Investments in jointly controlled entities and subsidiaries are carried at cost less impairment.

Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost using the effective interest method, less any impairment losses.

Derivative financial instruments

Derivative financial instruments are recognised at fair value. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see below).

Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in the hedging reserve. Any ineffective portion of the hedge is recognised immediately in the profit and loss account.

Notes *(continued)*

2 Turnover

Turnover has been wholly derived from the operation of design, production and support of armoured vehicles, avionic, communications and associated electronic equipment, which originates in the United Kingdom. The analysis of turnover by geographical destination is as follows:

	2016	2015
	£000	£000
United Kingdom	**555,774**	424,263
Europe	**6,069**	7,394
North America	**1,420**	3,252
Rest of the World	**2,142**	5,086
	565,405	439,995

3 Staff numbers and costs

The average number of persons employed by the Company (including directors) during the year, analysed by category, was as follows:

	2016	2015
	Number of employees	
Administration	**151**	137
Production	**707**	647
	858	784

The aggregate payroll costs of these persons were as follows:

	2016	2015
	£000	£000
Wages and salaries	**41,621**	38,229
Social security costs	**4,902**	4,408
Other pension costs (see note 21)	**6,327**	5,278
	52,850	47,915

Notes *(continued)*

4 Other interest receivable and similar income

	2016 £000	2015 £000
Bank interest	**288**	1,001
Pension interest	**243**	-
	531	1,001

5 Interest payable and similar charges

	2016 £000	2015 £000
On all other loan interest payable	**24**	4
	24	4

6 Profit/(loss) on ordinary activities before taxation

	2016 £000	2015 £000
The profit/(loss) on ordinary activities before taxation is stated after charging/(crediting):		
Operating leases		
- Land and buildings	**801**	884
- Motor vehicles	**83**	53
Research and development	**566**	1,225
Depreciation of owned fixed assets	**1,231**	1,437
Depreciation of leased assets	**226**	275
Goodwill impairment	**14,140**	-
Intangible amortisation	**2,400**	2,400
Grants received	**(176)**	443
Exchange loss	**(10,075)**	(619)
IFRS 2 share based payment charges	**(710)**	(308)
Loss on disposal of fixed assets	**-**	11
Restructuring charge	**121**	-
Auditor's Remuneration		
Audit of these Financial Statements	**213**	210
Taxation compliance	**92**	75

The restructuring costs were due to the exit of various properties and redundancy costs.

Notes *(continued)*

7 Directors' remuneration

	2016 £000	2015 £000
Directors' emoluments	**262**	241
Company contributions to money purchase pension schemes	**11**	10

Two Directors exercised share options of the ultimate parent company in the year *(2015: 2)*. The above amounts do not include any gains made on the exercise of share options. Gains made on the exercise of share options by these Directors were £412,314, *(2015:£206,486)*. These shares had an average market price of £129.53, *(2015:£95.17)*.

Two of the director's emoluments represent the intercompany recharge of their salary for time spent on affairs of the company.

Pensions

The number of Directors who were members of pension schemes was as follows:

	2016 Number	2015 Number
Money purchase scheme	**2**	2

Highest paid director

The above amounts for remuneration include the following in respect of the highest paid Director:

	2016 £000	2015 £000
Directors' emoluments	**84**	84
Company contributions to money purchase pension schemes	**0**	0

No Director had a direct or indirect interest in any transaction, arrangement or agreement, which in the opinion of the other Directors requires disclosure under the provisions of the Companies Act 2006.

Notes *(continued)*

8 Taxation

	2016 £000	2015 £000
UK deferred tax (see note 17)	**892**	699
UK current tax	**15,058**	12,300
Adjustments in respect of prior periods	**(2,239)**	319
Income statement	**13,711**	13,318

Reconciliation of effective tax rate	2016 £000	2015 £000
Profit for year	**65,770**	56,462
Total tax expense	**13,711**	13,318
Profit excluding taxation	**79,481**	69,780
Tax using the Corporate tax rate of 20% (2015:20¼%)	**15,896**	14,130
Non-deductible expenses	**(2,453)**	363
Tax exempt revenues	**(706)**	(2,514)
Capital allowances for year in excess of depreciation	**2,320**	321
Under/(over) provided in prior years	**(2,238)**	319
Deferred tax	**892**	699
Total tax expense	**13,711**	13,318

Reductions in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) and 18% (effective from 1 April 2020) were substantively enacted on 26 October 2015. A further reduction to the UK Corporation tax rate was announced in the 2016 Budget to further reduce the tax rate to 17% (to be effective from 1 April 2020). This will reduce the company's future current tax charge accordingly. The deferred tax asset at 31 December 2016 has been calculated on the rate of 17%.

Notes *(continued)*

9 Intangible assets

	Goodwill £000	Customer relationships £000	Other £000	Software £000	Total £000
Cost at 1 January 2016	**17,141**	**14,200**	**1,820**	**3,172**	**36,333**
Additions	-	-	-	2,334	2,334
Total Cost at 31 December 2016	**17,141**	**14,200**	**1,820**	**5,506**	**38,667**
Accumulated amortisation at 1 January 2016	**-**	**9,799**	**1,270**	**1,454**	**12,523**
Amortisation charge for the year	-	1,775	228	814	2,817
Impairment loss recognised	14,741	-	-	-	14,741
Amortisation at 31 December 2016	**14,741**	**11,574**	**1,498**	**2,268**	**30,081**
Net book value at 31 December 2016	**2,400**	**2,626**	**322**	**3,238**	**8,586**
Net book value at 31 December 2015	17,141	4,401	550	1,718	23,810

The net book value of Goodwill has been reduced by recognising an impairment loss of £14,741 as a result of our review of the Company's future UK MoD ISTAR programmes.

	Goodwill £000	Customer relationships £000	Other £000	Software £000	Total £000
Cost at 1 January 2015	**17,141**	**14,200**	**1,820**	**3,172**	**36,333**
Additions	-	-	-	-	-
Total Cost at 31 December 2015	**17,141**	**14,200**	**1,820**	**3,172**	**36,333**
Accumulated amortisation at 1 January 2015 (restated)	**-**	**8,024**	**1,043**	**1,057**	**10,124**
Amortisation charge for the year	-	1,775	228	397	2,400
Amortisation at 31 December 2015	**-**	**9,799**	**1,270**	**1,454**	**12,523**
Net book value at 31 December 2015	**17,141**	**4,401**	**550**	**1,718**	**23,810**
Net book value at 31 December 2014	17,141	6,176	777	2,115	26,209

Notes *(continued)*

9 Intangible assets *(continued)*

Key impairment assumptions

Management approved forecasts were used covering a period of 5 years. The discounted cash-flow rate used was 10%.

Intangibles and investments

Investment entity	Holding company	Share capital	Proportion held	Loss in year £000
General Dynamics Informations Systems and Technology Arabia Company	General Dynamics UK Ltd	SAR12,000,000	49%	-

All investments have been written down to zero in prior years.

Notes *(continued)*

10 Tangible fixed assets

	Premises land and buildings	Short leasehold land and buildings	Plant, machinery and motor vehicles	Total
Cost	**£000**	**£000**	**£000**	**£000**
At 1 January 2016	13,449	6,041	37,548	57,038
Additions	-	141	6,356	6,497
Transfers	5,543	-	(5,543)	-
At 31 December 2016	**18,992**	**6,182**	**38,361**	**63,535**
Depreciation				
At 1 January 2016	3,291	5,926	27,961	37,178
Charge for year	335	64	1,039	1,438
Disposals				
At 31 December 2016	**3,626**	**5,990**	**29,000**	**38,616**
Net book value				
At 31 December 2016	**15,366**	**192**	**9,361**	**24,919**
At 31 December 2015	10,158	116	9,586	19,860

The net book value of plant and machinery and motor vehicles above includes a net book value of £325,000 (*2015: £357,000*) in respect of assets held under finance leases. Depreciation charged in the year on these assets was £226,000 (*2015: £275,000*).

	Premises land and buildings	Short leasehold land and buildings	Plant machinery and motor vehicles	Total
Cost	**£000**	**£000**	**£000**	**£000**
At 1 January 2015	13,520	6,079	30,392	49,991
Additions	156	-	7,222	7,378
Disposals	(227)	(38)	(67)	(332)
At 31 December 2015	**13,449**	**6,041**	**37,547**	**57,037**
Depreciation				
At 1 January 2015	3,163	5,909	26,711	35,783
Charge for year	353	44	1,315	1,712
Disposals	(225)	(27)	(65)	(317)
At 31 December 2015	**3,291**	**5,926**	**27,961**	**37,178**
Net book value				
At 31 December 2015	**10,158**	**116**	**9,586**	**19,860**
At 31 December 2014	10,357	170	3,681	16,323

Notes *(continued)*

11 Stocks and work in progress

	2016 £000	2015 £000
Raw materials and consumables	**41**	240

12 Debtors

	2016 £000	2015 £000
Amounts falling due within one year:		
Amounts owed by fellow subsidiary	**109,480**	136,190
Amounts recoverable on contracts	**198,650**	155,335
Trade debtors	**6,885**	9,020
Prepayments and other debtors	**14,159**	11,780
Deferred tax asset (note 17)	**-**	10
Taxation	**-**	1,126
Total amounts falling due within one year	**329,174**	313,461
Trade debtor amounts greater than one year	**15,678**	15,678
Total debtors	**344,852**	329,139

13 Creditors: amounts falling due within one year

	2016 £000	2015 £000
Obligations under finance leases (see note 16)	**214**	216
Payments on account on long term contracts	**50,472**	30,399
Trade creditors	**39,377**	6,650
Bank overdraft	**-**	56
Amounts owed to group companies	**-**	16,380
Taxation and social security	**23,112**	9,274
Deferred tax liability (note 17)	**882**	-
Accruals and deferred income	**36,825**	39,017
Intercompany amount owed to subsidiary	**375**	375
	151,257	102,367

Notes *(continued)*

14 Creditors: amounts falling due after more than one year

	2016 £000	2015 £000
Obligations under finance leases (see note 16)	129	155
Welsh Development Agency grant	7,700	-
	7,829	155

The £7.7m Welsh Development Grant was received in the year in order to help fund the development of the Merthyr Tydfil site. The grant is repayable in equal instalments over 7 years.

15 Other financial asset and liabilities

	2016		2015	
	Assets £000	Liabilities £000	Assets £000	Liabilities £000
Current				
Cashflow hedges – foreign exchange contracts	7,971	-	421	(11,020)
Non-current				
Cashflow hedges – foreign exchange contracts	12,667	-	968	(55,315)
	20,638	-	1,389	(66,335)

The Company is exposed to market risk, primarily from foreign currency exchange rates. It may use derivative financial instruments to hedge some of these risks as described below. It does not use derivatives for trading or speculative purposes.

The foreign currency exchange rate risk relates to receipts from customers, payments to suppliers and inter-company transactions denominated in foreign currencies. To the extent possible, the Company include terms in our contracts that are designed to protect us from this risk. Otherwise, it enters into derivative financial instruments, principally foreign currency forward purchase and sale contracts, designed to offset and minimise our risk. It recognises derivative financial instruments on the Balance Sheets at fair value.

The Company records changes in the fair value of derivative financial instruments in operating costs and expenses in the Statements of Earnings or in other comprehensive income within the Statements of Comprehensive Income depending on whether the derivative is designated and qualifies for hedge accounting. Gains and losses related to derivatives that qualify as cash flow hedges are deferred in other comprehensive income until the underlying transaction is reflected in earnings. The Company adjusts derivative financial instruments not designated as cash flow hedges to market value each period and record the gain or loss in the Statements of Earnings. The gains and losses on these instruments generally offset losses and gains on the assets, liabilities and other transactions being hedged. Gains and losses resulting from hedge ineffectiveness are recognised in the Statements of Earnings for all derivative financial instruments, regardless of designation.

Notes *(continued)*

16 Obligations under finance leases

The maturity of obligations under finance leases and hire purchase contracts is as follows:

	2016	2015
	£000	£000
Within one year	**214**	216
In the second to fifth years	**129**	155
	343	371

17 Provisions for liabilities and charges

	Deferred tax	**Warranty provision**	**Total**
	£000	**£000**	**£000**
At 1 January 2016	**(10)**	**5,483**	**5,473**
Profit and loss/Retained Earnings Adjustment	892	4,438	5,330
At 31 December 2016	**882**	**9,921**	**10,803**

The liability at 31 December 2016 is split as follows:

Debtors (see note 12)	882
Provision for liabilities and charges	9,921
	10,803

The elements of deferred taxation are as follows:

	2016	2015
	£000	£000
Difference between accumulated depreciation and capital allowances	**901**	(5)
Other timing differences	**(19)**	(5)
Deferred tax liability/(asset)	**882**	(10)

18 Share capital

The share capital of the Company comprises ordinary shares of 50p each.

	2016		2015	
	Number of Shares	**£000**	Number of Shares	£000
Allotted, called-up and fully paid	**18,523,150**	**9,262**	18,523,150	9,262

Notes *(continued)*

19 Financial commitments

a) Capital commitments at the end of the financial year, for which no provision has been made, are as follows:

	2016	2015
	£000	£000
Contracted	**86**	1,241
Authorised but not contracted	**368**	7,125

(b) Aggregate commitments under non-cancellable operating leases are as follows:

	2016		2015	
	Land and buildings	**Other**	Land and buildings	Other
	£000	**£000**	£000	£000
Operating leases which expire:				
Within one year	**801**	**108**	1,527	36
In the second to fifth years inclusive	**1,446**	**28**	1,868	6
Over five years	**5,184**	**-**	5,132	-
	7,431	**136**	8,527	42

20 Contingent liabilities

	2016	2015
	£000	£000
Performance guarantees	**264**	325
Offset bond (expressed in AED)	AED 4,416k	AED 4,416k

Performance guarantees in 2016 are made up of a deferment guarantee of £150,000 (*2015: £150,000*) and performance bonds of £114,000 (*2015: £175,000*).

Notes *(continued)*

21 Pension scheme

The Company sponsors the General Dynamics Retirement and Death Benefit Scheme ('the Scheme'). The Scheme is a hybrid arrangement which includes both a defined contribution section and a defined benefit section comprising of current and deferred pensioners. The defined benefit section of the Scheme was closed from 6 April 1997, at which time members ceased to accrue benefits on a defined benefit basis and were given the option to transfer their benefits to the defined contribution section of the Scheme. The assets of the Scheme are held separately from those of the Company, being invested with an external fund manager. The expenses of the Scheme are borne by the Company.

Defined contribution element

The pension cost for the year was £6,327,000, *(2015: £5,278,000)*. There were no outstanding or prepaid contributions at 31 December 2016 *(2015: £nil)*.

Defined Benefit Section

A full actuarial valuation of this scheme was carried out by a qualified independent actuary as at 5 April 2015. This has been updated on an approximate basis to 31 December 2016. The actuarial valuation resulted in an asset. This was based on assumptions taking a worst case scenario of all eligible employees retiring early.

The contributions made by the Company totalled £850,000 *(2015: £850,000)*. The pension costs for the year were £nil *(2015: £nil)* on the basis that the Directors consider it unlikely that all eligible employees will retire early and therefore the scheme is in balance.

Assumptions

The mortality assumptions utilised were PMA92 and PFA92, projected using the medium cohort mortality improvement rates.

The mortality assumptions adopted at 31 December 2016 imply the following life expectancies:

Male retiring at age 65 in 2016	22.2
Female retiring at age 65 in 2016	24.2
Male retiring at age 65 in 2036	23.9
Female retiring at age 65 in 2036	26.1

Notes *(continued)*

21 Pension scheme *(continued)*

Expected long term rates of return

The long-term expected rate of return on cash is determined by reference to bank base rates at the balance sheet dates. The long-term expected return on bonds is determined by reference to UK long dated government and corporate bond yields at the balance sheet date. The long-term expected rate of return on equities is based on the rate of return on bonds with an allowance for out-performance.

The expected long term rates of return applicable for each period are as follows:

	Period commencing 01/01/2016 % per annum	Period commencing 01/01/2015 % per annum
Equity	5.87%	6.61%
Bonds	2.70%	3.78%
Gilts	1.87%	2.61%
Property	5.37%	6.11%
Cash	2.70%	3.78%
Overall for scheme	4.10%	5.04%

The assets of the scheme have been taken at market value and the liabilities have been calculated using the following principal actuarial assumptions:

	2016	2015	2014
Revaluation rate for deferred pensioners	**2.55%**	2.12%	2.11%
Rate of increase in pensions in payment and deferred pensions	**2.55%**	2.12%	2.11%
Discount rate applied to scheme liabilities	**2.70%**	3.78%	3.51%
Inflation assumption	**3.45%**	3.02%	3.01%

In valuing the liabilities of the pension fund at 31 December 2016 mortality assumptions have been made as indicated above. If life expectancy had been changed to assume that all members of the fund lived for one year longer, the value of the reported liabilities at 31 December 2016 would have increased by £720,000 before deferred tax.

The table below sets out the fair value of assets, a breakdown of the assets into the main asset classes, the present value of the IAS 19 liabilities and the surplus of assets below the IAS 19 liabilities (which equals the gross pension asset).

Notes *(continued)*

21 Pension scheme *(continued)*

Scheme assets

The fair value of the Scheme's assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the Scheme's liabilities, which are derived from cash flow projections over long periods and therefore inherently uncertain, were:

	2016	2015
	£000	£000
Fair value of plan assets	**21,682**	19,882
Present value of funded deferred benefit obligations	**(18,223)**	(13,892)
Actuary contributions timing adjustment	**-**	-
Surplus	**3,459**	5,990
De-recognition of surplus	**(3,459)**	(5,990)
Net pension asset	**-**	-

The pension surplus of £3,459k has been de-recognised in accordance with IAS 19 as it is not recoverable.

Reconciliation of opening and closing balances of the present value of the scheme liabilities.

	2016	2015
	£000	£000
Scheme liabilities at start of year	**13,892**	18,254
Interest cost	**519**	635
Actuarial gains/(losses)	**4,112**	(4,665)
Benefits paid, death in service insurance premiums and expenses	**(380)**	(359)
Past service costs	**-**	-
Impact of Defined Benefits underpin member retirements	**80**	27
Scheme liabilities at end of year	**18,223**	13,892

Notes *(continued)*

21 Pension scheme *(continued)*

Reconciliation of opening and closing balances of the fair value of scheme assets

	2016 £000	2015 £000
Fair value of scheme assets at start of year	**19,882**	18,714
Expected return on scheme assets	**762**	666
Actuarial gains/(losses)	**488**	(16)
Contributions by employer	**850**	850
Benefits paid, death in service insurance premiums and expenses	**(380)**	(359)
Impact of Defined Benefits underpin member retirements	**80**	27
Fair value of scheme assets at end of year	**21,682**	19,882

Movement in the surplus during the year

	2016 £000	2015 £000
Surplus in the Scheme at 1 January	**5,990**	460
Contribution	**850**	850
Other finance expense	**243**	31
Actuarial (loss)/gain	**(3,624)**	4,649
Surplus in the Scheme at 31 December	**3,459**	5,990

Analysis of amounts included in other finance (expense)/income:

	2016 £000	2015 £000
Expected return on pension scheme assets	**762**	(666)
Interest on pension scheme liabilities	**(519)**	635
Past service costs		-
	243	(31)

Analysis of amount recognised in statement of total recognised gains and losses:

	2016 £000	2015 £000
Actual return less expected return on Scheme assets	**488**	(16)
Experience gains arising on Scheme liabilities	**1,055**	3,372
Changes in assumptions underlying the present value of Scheme liabilities	**(5,167)**	1,080
Changes in demographic assumptions underlying the present value of Scheme liabilities	**-**	213
De-recognition of pension surplus	**2,774**	(5,499)
	(850)	(850)

Notes *(continued)*

21 Pension scheme *(continued)*

The fair value of the plan assets and the return on those assets were as follows:

	2016	2015
	£000	£000
Equity	**5,941**	5,568
Bonds	**7,167**	6,100
Gilts	**3,695**	3,221
Property	**1,608**	1,568
Cash	**2**	73
Diversified growth	**3,269**	3,352
Total	**21,682**	19,882
Actual return on plan assets	**1,250**	650

A history of experience gains and losses at 31 December 2016 would have been as follows:

	2016	2015	2014	2013	2012
Difference between the expected and actual return on scheme assets:	**£000**	£000	£000	£000	£000
Amount	**488**	(16)	1,223	996	1,460
Percentage of scheme assets (at end of year)	**2%**	0%	7%	7%	11%
Experience losses on scheme liabilities:					
Amount	**1,055**	3,372	322	1,426	95
Percentage of present value of scheme liabilities (at end of year)	**5%**	17%	2%	10%	1%
Total amount recognised in statement of total recognised gains and losses:					
Amount	**(850)**	(850)	(850)	84	2,194
Percentage of present value of scheme liabilities (at end of year)	**5%**	4%	5%	1%	15%
	2016	2015	2014	2013	2012

History of plans

The history of the plans for the current and prior periods is as follows:

	2016	2015	2014	2013	2012
	£000	£000	£000	£000	£000
Present value of scheme liabilities	**(18,223)**	(13,892)	(18,254)	(14,155)	(14,679)
Fair value of scheme assets	**21,682**	19,882	18,714	15,760	13,804
Actuary contribution timing	**-**	-	-	53	-
Surplus/(deficit)	**3,459**	5,990	460	1,658	(875)

Notes *(continued)*

21 Pension scheme *(continued)*

The expected contribution to be paid to the scheme in the next financial year is £850,000.

The total amount recognised in the statement of total recognised gains and losses in respect of actuarial gains and losses is £3,624,000 (*2015: £ (4,649,000)*).

Cumulative actuarial gains and losses reported in the statement of total recognised gains and losses for accounting periods ending on or after 22 June 2002 and subsequently included by prior year adjustment under IAS 19, are £(7,284,000) (*2015:(£6,434,000)*).

22 Related party disclosures

The Company is controlled by its immediate parent undertaking General Dynamics Ltd. The ultimate controlling party is General Dynamics Corporation (See note 23).

23 Employee benefits

Share based payments

The Save As You Earn (SAYE) scheme is offered to all employees once a year and employees have the option of entering either a 3 year or 5 year scheme

The terms and conditions of grants are as follows:

Notes *(continued)*

23 Employee benefits *(continued)*

Share based payments *(continued)*

Grant date/ Employees entitled/ nature of scheme	Number of instruments		Vesting conditions	Contractual life of options
2011 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/11.	GDUK	7,174	5 years from start of contract	2017
2012 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/12.	GDUK	2,795	5 years from start of contract	2018
2013 Cash-settled 3 year SAYE award to employees. Granted by parent on 5/12/13.	GDUK	7,979	3 years from start of contract	2017
2013 Cash-settled 5 year SAYE award to employees. Granted by parent on 5/12/13.	GDUK	2,448	5 years from start of contract	2019
2014 Cash-settled 3 year SAYE award to employees. Granted by parent on 3/12/14.	GDUK	13,111	3 years from start of contract	2018
2014 Cash-settled 5 year SAYE award to employees. Granted by parent on 3/12/14.	GDUK	1,838	5 years from start of contract	2020
2015 Cash-settled 3 year SAYE award to employees. Granted by parent on 30/11/15.	GDUK	16,297	3 years from start of contract	2019
2015 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/15.	GDUK	2,961	5 years from start of contract	2021
2016 Cash-settled 3 year SAYE award to employees. Granted by parent on 30/11/16.	GDUK	16,689	3 years from start of contract	2020
2016 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/16.	GDUK	2,710	5 years from start of contract	2022

The number and weighted average exercise prices of SAYE share options are as follows:

	2016 **Weighted Average exercise price**	**2016** **Number of options**	2015 **Weighted Average exercise price**	2015 Number of options
	£		**£**	
Outstanding at the beginning of the year	**62.93**	**56,056**	**44.72**	69,694
Forfeited during the year	**71.41**	**(8,930)**	**50.85**	(4,436)
Exercised during the year	**92.07**	**(11,664)**	**90.31**	(28,460)
Granted during the year	**103.19**	**19,399**	**82.40**	19,258
Lapsed during the year	**-**	**-**	**-**	-
Outstanding at the end of the year	**81.44**	**54,861**	**62.93**	56,056
Exercisable at the end of the year	-	-	-	-

Notes *(continued)*

23 Employee benefits *(continued)*

Share based payments *(continued)*

The weighted average share price at the date of exercise of share options exercised during the period was £92.07 *(2015: £90.31).*

The options outstanding at the year-end have an exercise price in the range of £33.48 to £103.19 and a weighted average remaining contractual life of 2.8 years.

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured based on a Black Scholes model. Measurement inputs and assumptions are as follows:

	SAYE 3 year		SAYE 5 year	
	2016	2015	**2016**	2015
Fair value at grant date	35.0728	9.002	37.6981	12.5756
Weighted average share price	103.1855	82.3955	103.1855	82.3955
Exercise price	103.1855	82.3955	103.1855	82.3955
Expected volatility (expressed as % used in the modelling under Black Scholes model)	16.702	17.81	19.057	19.34
Option life (expressed as weighted average life used in the modelling under Black Scholes model)	39 months	39 months	63 months	63 months
Expected dividends	2.0%	2.0%	2.0%	2.0%
Risk-free interest rate (based on national government bonds)	0.976%	1.207%	1.247%	1.728%

The total expenses recognised for the year arising from share based payments are as follows:

	2016	2015
	£000	£000
Equity settled share based payments (Restricted Stock and EC options for which we have applied the exemption)	**95**	105
Cash settled share based payments (SAYE)	**111**	88
Total carrying amount of liabilities (SAYE)	**1,268**	1,041
Total intrinsic carrying amount of liabilities in respect of vested benefits	**-**	-

24 Ultimate parent company

The Company is a 100% owned subsidiary undertaking of General Dynamics Limited, a company incorporated in Great Britain. General Dynamics Corporation is the ultimate parent company incorporated in the USA.

The largest and smallest group in which the results of the Company are consolidated is that headed by General Dynamics Corporation, incorporated in the USA. The consolidated accounts of the group are available to the public and may be obtained from 2941 Fairview Park Drive, Suite 100, Falls Church, VA 22042 – 4513, USA.

Notes *(continued)*

25 Accounting Estimates and Judgements

Accounting estimates and judgements

The preparation of the consolidated financial statements in conformity with FRS101 requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. The reported amounts and note disclosures reflect management's best estimate of the most probable set of economic conditions and planned course of actions. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in these consolidated financial statements include:

Revenue recognition
These estimates are based on our best judgment at the time. As a significant change in one or more of these estimates could affect the profitability of our contracts, we review our performance monthly and update our contract-related estimates at least annually and often quarterly, as well as when required by specific events and circumstances. We recognize any changes in the estimated profit on contracts under the cumulative catch-up method. Under this method, the impact of a revision in estimate is recognized immediately as opposed to under the prospective method, where changes in estimates are recognised over the remaining life of the contract.

Allowance for doubtful accounts

In its determination of the valuation of trade and other receivables, including the allowance for doubtful accounts, management relies on current customer information, which include customer creditworthiness and past experiences, and its planned course of action as well as assumptions about business and economic conditions in the future period over which the receivables are collectible. If future collections differ from estimates, future earnings would be affected.