Ministry of Defence

DEFENCE SUPPORT GROUP

ANNUAL REPORT AND ACCOUNTS 2014/15

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Presented to Parliament pursuant to Section 4(6) of the Government Trading Funds Act 1973 as amended by the Government Trading Act 1990.

Ordered by the House of Commons to be printed 14th July 2015.

HC 228

This publication is available at www.gov.uk/government/publications

Any enquiries regarding this publication should be sent to us at **BSG, MOD Main Building, London SW1A 2HB.**

Print ISBN 9781474116657
Web ISBN 9781474116664

ID 130131504 07/15 50470 19585

Printed on paper containing 75% recycled fibre content minimum

Printed in the UK by the Williams Lea Group on behalf of the Controller of Her Majesty's Stationery Office

DEFENCE SUPPORT GROUP ANNUAL REPORT AND ACCOUNTS 2014/15

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INTRODUCTION FROM THE CHAIRMAN

This is my final introduction to the Defence Support Group's (DSG) Annual Report and Accounts as Chairman of its Trading Fund Board (TFB), a role that has given me a great opportunity to witness a business excel in its field supporting the UK's Armed Forces. My role as Chairman extended to supporting DSG's Chief Executive on the Ministerial Owner's Advisory Council (OAC), which held its final meeting in February 2015.

This final Annual Report and Accounts covers the 2014/15 financial year and provides a useful insight into DSG's trading performance during the past accounting year. It is commendable that the DSG employees remained focussed on delivering an outstanding service in a continued climate of uncertainty. The sale of DSG's Land business and retention of DSG's Electronics and Components Business Unit (ECBU) and the activities undertaken at DSG Stafford within MOD ownership understandably remained at the forefront in the minds of most employees, but this did not stop them producing an outstanding performance in the face of growing anxiety and concern for their futures and for this my fellow Non-Executive Directors and I offer our thanks and gratitude.

The announcement of the successful bidder and subsequent contract award to Babcock International Group finally ended what was a protracted sale process that started in 2010 following publication of the Strategic Defence and Security Review. DSG's Land business transferred into private sector ownership on 1 April 2015. This is the same date that DSG's ECBU began trading as the Defence Electronics and Components Agency (DECA), a new MOD Executive Agency with Trading Responsibilities.

Without any doubt the highlight for me in my role as Chairman was in learning of the self-less sacrifice and commitment of all the DSG employees who stepped up to the plate and deployed to the front line to deliver an outstanding service to our Armed Forces engaged in military combat. Leaving loved ones and friends behind is hard at any time but knowing you are going into a war zone takes great courage. This demonstrates clearly to me that DSG's employees can hold their heads high and take great pride in what they achieved while in Afghanistan.

In conclusion, I offer thanks to my fellow Directors for their valuable advice, expertise and support during my time as Chairman. These thanks extend to DSG's Chief Executive, Archie Hughes, his team of Executive Directors and the DSG senior management team who have shown great professionalism and commitment in a year of massive pressure to deliver a service while supporting their colleagues in MOD during the sale and separation process.

I will look back on my time with DSG with great pride in the knowledge that I hope the small part played by me contributed to DSG's success. I offer my sincere best wishes to all DSG's employees as they now go their separate ways on what I am sure will be journeys of discovery and great success.

Alex Jablonowski
Chairman
Defence Support Group
31st March 2015

STATEMENT BY THE CHIEF EXECUTIVE

This is the DSG seventh and final Annual Report and Accounts in MOD ownership. Since its creation in 2008, DSG has produced strong trading results every year and the reporting period 2014/15 is no exception. This is even more commendable having achieved these results in a challenging environment as MOD prepared DSG for sale. DSG's TFB Chairman along with the Non-Executive Directors were, once again, able to provide the DSG Management Board with advice, guidance and challenge using the skills and expertise developed in their various careers at senior management level in both the public and private sectors.

Parliament measures DSG's performance against four clear business measures set by Ministers. The first assesses Quality in both the Air and Land environments where DSG must achieve no more than one and fewer than four attributable major customer concerns respectively over the reporting period. The second area measures Delivery in Air and Land where DSG must achieve 96% delivery of all Air programmes; and 94% of the Land Critical Programme Lines in September and December respectively, and finish the year with 97% and 92% of all Land Load tasks. The third measure is in Efficiency and Transformation where DSG must support MOD's Business Strategy and Governance team and their appointed advisors in preparing DSG for sale in accordance with the DSG sale strategy and timetable. The final measure used to assess DSG's performance is Financial Performance and here DSG must deliver a minimum 5% return on capital employed. This year I can report that once again DSG achieved or exceeded all the targets set by Ministers.

Following several months of uncertainty and speculation, MOD announced in December 2014 that Babcock International Group was the successful preferred bidder for the DSG Land business with the sale contract valued at £140M signed in early January 2015. Preceding this announcement was the Ministerial statement ratifying the decision to retain DSG's ECBU together with activities undertaken at DSG Stafford in MOD ownership. This business became an Executive Agency with Trading Responsibilities of MOD, called the Defence Electronics and Components Agency (DECA) on 1 April 2015. DSG's Chief Operating Officer, Geraint Spearing, is the agency's new Chief Executive.

In September, the majority of DSG employees supporting operations in Camp Bastion began their withdrawal from deployment to return home to their families and workplaces. The past five years have witnessed DSG demonstrate a level of commitment and professionalism to its customers in a hostile and, at times, dangerous environment that have earned the respect and plaudits from senior Ministers and politicians as well as from the ones who matter most, the serving men and women of the UK's Armed Forces.

During our time in Afghanistan, DSG's employees established themselves as great ambassadors for DSG. They have shown a great fortitude and capability for hard work and long hours, which helped keep vital fighting equipment in a high state of readiness. This was, without doubt, a critical element to the success of operations and I know everyone in DSG shares my pride in what we have achieved since we arrived in Camp Bastion in 2010.

Almost 500 DSG employees volunteered for deployment duties, which represent 20% of the DSG workforce. An impressive result whichever way you look at it. We continued maintaining a small team in Afghanistan in the Equipment Regeneration Hub Forward facility through to March 2015 when they too returned home and DSG's presence in Afghanistan ended.

Words alone cannot express how proud I am of all that we have achieved in Camp Bastion and the debt of gratitude we owe to all those employees who contributed to the success of our involvement at the operational front line. We must also acknowledge and recognise the contributions made by all the DSG employees back home who stepped up to the plate and shouldered the burden of extra work by filling in for their deployed colleagues and managed to deliver a sterling operational performance that helped DSG post an excellent business performance this year.

I have said on many occasions and make no apology for repeating it here again that DSG's greatest asset without any doubt is its people. We have some of the best and most talented employees in their respective fields and I am sure it is this extraordinary capability that was of particular attraction to our new owner. We have a world-class workforce that our Armed Forces customers value greatly with a long and proud heritage in supporting our Servicemen and women. This alone will ensure the future success of DSG now and into the future.

A. Hughes

Archie Hughes
Chief Executive
31st March 2015

BOARD OF DIRECTORS

The DSG Board of Directors comprised:

Archie Hughes	Chief Executive
Steve Hall	Finance Director
Geraint Spearing	Chief Operating Officer (until Jun 14)*
Richard Atkinson	Commercial Director
Keith Norris	Strategy Director
Jane Williams	Human Resources Director
Alex Jablonowski	Chairman (Non-Executive Director)
Janet Baker	Non-Executive Director
David Barrass	Non-Executive Director
David English	MOD Non-Executive Director

*DSG did not appoint a Chief Operating Officer to replace Geraint Spearing, but appointed Dave Edmunds as the Head of Operations, reporting directly to the Chief Executive.

PERFORMANCE AGAINST INTERNAL BUSINESS MEASURES

In line with our core mission and vision, and in order to maintain Trading Fund efficiency, structural alignment with MOD planning assumptions and strategic priorities (including the announced intention to sell DSG), DSG agreed the internal business measures (IBMs) below in consultation with the MOD Owner and Customer focal points and our performance against them is as follows:

Business Measure 1: **Quality** Deliver an improved quality performance by: • Air - achieving no more than 1 attributable Major Customer Concern; and Land – achieving no more than 4 attributable Major Customer Concerns	**Achieved**
Business Measure 2: **Delivery** Meet delivery standards as agreed with the Customer as follows: • Air Business – achieve 96% delivery of Customer Programmes; and • Land Business – achieve: 94% (Sep 14 and Dec 14) and 97% (Mar 15) delivery on Critical Programme Lines; and 92% of all Land Load Tasks	**Achieved**
Business Measure 3: **Efficiency and Transformation** To support MOD's Business Strategy & Governance (BSG), and their appointed advisors, in preparing DSG for sale in accordance with the DSG sale strategy and timetable.	**Achieved**
Business Measure 4: **Financial Performance** Achieve at least a 5% Return On Capital Employed (ROCE).	**Achieved**

BUSINESS PERFORMANCE REVIEW

DSG's operating units produced a sound performance during 2014/15 in an environment of change and uncertainty coupled with challenging customer requirements.

DSG Donnington completed the modification work during the year on the first Warrior Capability Sustainment Programme (WCSP) prototype hull. This was a major milestone in the development of the vehicle and involved DSG working closely with Lockheed Martin, the prime contractor for delivery of the WCSP programme. The work undertaken by DSG Donnington staff was of the highest standard and allowed completion of complex installations for the first time.

During the year at DSG Bovington, the team faced many production and customer changes, but met its business plan and produced another strong performance.

DSG Warminster played an increasingly important role as it increased its responsibilities and grew its capabilities. The Warminster Business Unit played a significant role in DSG delivering the HXP capability at both this site and from the DSG HXP facilities at MOD Lyneham.

DSG's sites at Ashchurch, Catterick, Colchester, Kinnegar, Longmoor and Stirling all contributed to the overall performance of the business, with the priorities of customers changing during the year and primary focus for some of the sites in supporting the Vanguard programme.

For ECBU, which includes activities undertaken at DSG Stafford and other military locations around the country, the priority during the year was in preparing the separation of this business from the rest of DSG. During the year, the Minister responsible for DSG, Philip Dunne MP, announced that ECBU would become an Executive Agency of MOD from 1 April 2015 called DECA with Geraint Spearing, previously DSG's Chief Operating Officer, as its new Chief Executive.

Both ECBU and DSG Stafford have secured new contracts to work on a variety of projects during the year, which the business hopes will open up further opportunities in the future and expand the capabilities of the new Agency.

DSG's role in Camp Bastion came to a close during the year with the final DSG employees leaving operational theatre in March 2015. DSG's presence in Afghanistan supporting front-line operations was a complete success on every level. DSG's Minister went on record to say, "I am left in no doubt that DSG's significant contribution to the success of the Operation HERRICK campaign will set the standard and deliver the template for our future support of deployed operations in combat situations. As the Minister with responsibility for DSG, I am immensely proud of what you have all achieved both at home and overseas."

DSG Bastion contributed cost avoidance savings in excess of £120M to MOD since 2009 with over 2000 pieces of equipment regenerated and over 11,000 pieces of equipment calibrated. Almost 500 DSG employees volunteered to deploy over the course of the project with over 100 for two or more tours.

COMMERCIAL OVERVIEW

The primary focus for the team in the commercial function during the year was ensuring delivery of the existing in-year contractual obligations to an acceptable customer standard. In addition, the team worked alongside MOD to support the sale activities through to the announcement of Babcock International Group as the preferred bidder and eventual contact signing in 2015, which included determining the future workload on the Warrior platform in the coming year.

STRATEGIC OVERVIEW

During the year the Strategy team worked in embedding DSG within Army HQ's Fleet Management key workstreams as well as developing a programme of growth and consolidation against a number of key milestones and stretch targets. Some of the opportunities identified for future growth include expanding support with the provision of fleet management of the Land District Load for the Land Training Fleet (Warminster) and securing synergy benefits through integration of the Green and White fleets.

BUSINESS SUPPORT OVERVIEW

With vigilance and continued emphasis on safety in the workplace, DSG witnessed a fall in reportable incidents involving employees. DSG continued to monitor closely the working environment to ensure incidents continue to decrease. Environmental management was a high priority for DSG and the business can report it achieved its target reductions in areas such as CO2 Emissions, reductions in generated waste and reductions in domestic air travel.

SUSTAINABILITY REPORT

Greenhouse Gas Emissions Data

The sustainability element of this year's report concentrates on the performance of DSG against MOD measures and IBMs for Sustainability. Greenhouse Gas (GHG) emissions and generated waste are both set against 2009/2010 baselines. The Disposals Services Authority (DSA) waste is not included as DE&S accounted for it separately. The Business Travel Performance Target was against a 2011/2012 target, as it was the first year the data was considered robust, providing a suitable baseline from which to measure future performance.

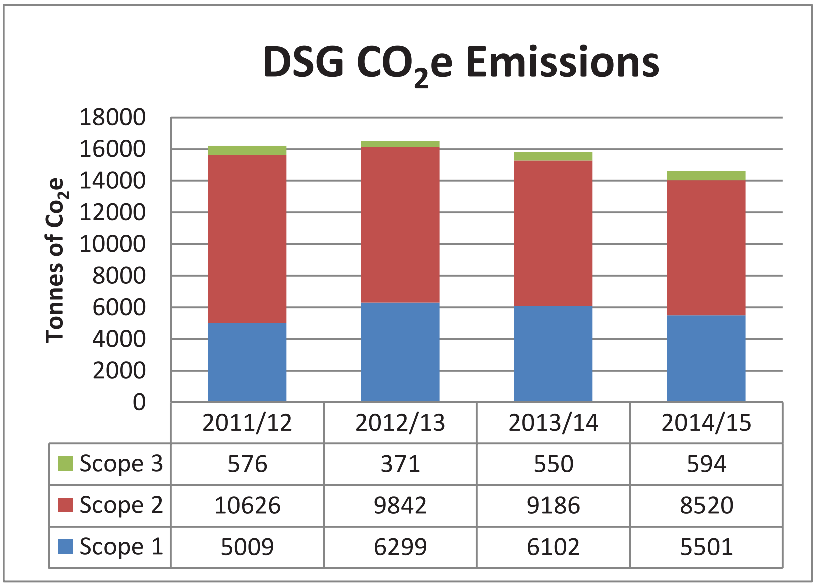
The 3 scopes of GHG emissions are:

- Scope 1 – Direct Greenhouse Gas Emissions (includes gas usage, fuel oil, LPG and fuel from vehicles owned and operated by DSG)
- Scope 2 – Energy Indirect Emissions (usage of electricity supplied to DSG)
- Scope 3 – Other Indirect Emissions (includes business travel by air, rail and hire/private car use)

The Table overleaf shows the breakdown of the various emissions by scope for this financial year. The target for the Emissions Reduction Measure was to reduce GHG emissions by 19% by 2015, against the 2009/10 baseline. At the end of this financial year, DSG exceeded the target and reduced its emissions by 38%. The graph below depicts the breakdown by scope.

GHG	FY2014/15		FY2013/14		FY2012/13		FY2011/12		FY2010/11	
	CO_2e Tonnes '000	£'000	CO_2e Tonnes '000	£'000	CO_2e Tonnes '000	£'000	CO_2e Tonnes '000	£'000	CO_2e Tonnes '000	£'000
Scope 1 – Direct GHG Emissions										
Natural Gas	4,605	352	4,949	971	5,062	628	4,213	1,299	NR	621
Fuel Oil/LPG	783	167	985	251	1,118	263	618	232	NR	188
DSG Fleet Vehicles	113	513	168	424	119	333	178	429	NR	308
Scope 2 – Energy Indirect Emissions										
Electricity	8,520	929	9,186	1,849	9,842	808	10,626	1,837	NR	1,883
Scope 3 – Official Business Travel Emissions										
Domestic Air Travel	72	65	45	103	26	112	45	177	NR	103
Rail Travel	5	55	4.6	48	1	39	1	42	NR	24
Hire/Private Car	517	367	500	499	344	350	530	286	NR	NR

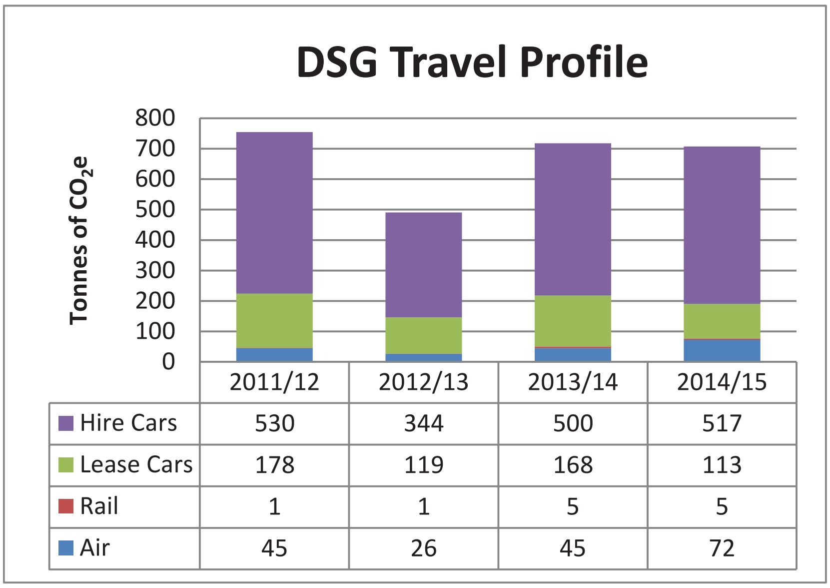
NR = Not Recorded



DSG CO2e Emissions by Scope

DSG Business Travel Profile

There has been a slight decrease in domestic travel this financial year; however meetings relating to MOD's sale of DSG increased the travel requirements to a higher level than usual. Video conference was used whenever practicable, and train usage has increased. The majority of domestic air travel was from Southampton to Edinburgh, essentially too far to drive, plus some long haul international activity has increased the CO_2e tonnage for this financial year. The total number of miles travelled by car this year was 2,112,812, this includes vehicles on long-term lease and short-term hires. There were 626 train journeys made this year compared to just fewer than 500 in the previous financial year. Air travel resulted in 394 domestic flights, which was below the target of 552 by the end of FY2014/15. The graph shows the CO2e breakdown by mode of travel.



	2011/12	2012/13	2013/14	2014/15
Hire Cars	530	344	500	517
Lease Cars	178	119	168	113
Rail	1	1	5	5
Air	45	26	45	72

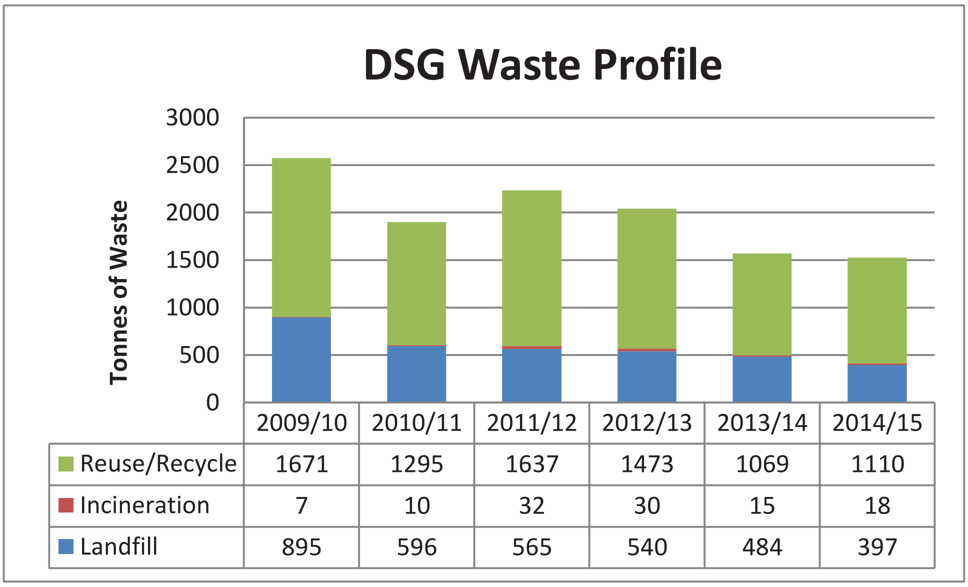
DSG CO2e Travel Profile

DSG Waste Profile

The DSG business performance target was a 25% reduction in waste generated through its operations by 2015 compared with the 2009/10 baseline year. In FY2014/15, DSG reduced its generated waste by 41%, exceeding the target. The reported data does not include material supplied through DE&S, which DSA collects and reports separately.

Although hazardous waste to landfill has increased, the recycling of hazardous waste also increased. The majority of non-hazardous recyclable was disposed of through DSA, i.e. product related waste such as metal, oils, etc. DSA took more waste types this year than any previous year. Financial data for waste disposal is not recorded, but by volume is shown overleaf:

Waste Category	FY2014/15	FY2013/14	FY2012/13	FY2011/12	FY2010/11	FY2009/10
	Tonnes	Tonnes	Tonnes	Tonnes	Tonnes	Tonnes
Hazardous						
Landfill	68	40.73	134.68	97.90	158.2	300.50
Incinerated	17	13.88	30.33	31.90	9.8	6.96
Reuse/Recycle	517	473.72	444.13	436.90	364.6	406.4
Non-Hazardous						
Landfill	329	443.17	405.17	467.00	437.5	594.46
Incinerated	0.9	1.18	0	0	0	0
Reuse/Recycle	593	595.37	1028.47	1,200.00	930.0	1264.6
Composted	0	0	0	0	0	0
Total Waste	**1525**	**1568.05**	**2,042.78**	**2,233.70**	**1900.10**	**2572.92**



DSG Waste Profile

PEOPLE

The Human Resources team's primary focus during the year was preparing DSG and its employees for sale and establishing the legislative processes and procedures required for a smooth transfer of employees to the new owner within the agreed timeframe. A period of industrial action by unions and their DSG membership in late 2014, which included Unite members taking strike action, further stretched the HR team's resources. However, after intense negotiations a settlement was reached in early 2015 that proved acceptable to all parties.

DSG's HR team supported the Transfer of Undertaking (Protected Employment) (TUPE) consultation between MOD and Babcock, which ensured we could keep employees fully informed as negotiations continued. A series of TUPE briefings for employees were rolled out across the DSG sites in order that employees could better understand their rights under the legislative process. Babcock's Lead-In Managing Director held a series of employee briefings across all the sites to introduce staff to the Babcock business and provide them with an overview of the new Babcock DSG Ltd organisation and its immediate plans for the future.

OFF PAYROLL APPOINTMENTS

The tables below provide information on DSG's most highly paid off-payroll appointments as required following the outcome of the Chief Secretary to the Treasury's Review of the Tax Arrangements of Senior Public Appointees (published on 23 May 2012).

For all off-payroll engagements as of 31 March 2015, for more than £220 per day and that last for longer than six months

	2014/15	**2013/14**
No. of existing engagements as of 31 March 2015	4	2
Of which...		
No. that have existed for less than one year at time of reporting.	2	1
No. that have existed for between one and two years at time of reporting.	1	1
No. that have existed for between two and three years at time of reporting.	1	0
No. that have existed for between three and four years at time of reporting.	0	0
No. that have existed for four or more years at time of reporting.	0	0

Assurance has been sought for all High-Paid Off-Payroll appointments that the individual appointees are paying the right amount of tax and National Insurance contributions.

For all new off-payroll engagements, or those that reached six months in duration, between 1 April 2014 and 31 March 2015, for more than £220 per day and that last for longer than six months

	2014/15	2013/14
No. of new engagements, or those that reached six months in duration, between 1 April 2014 and 31 March 2015	2	5
No. of the above which include contractual clauses giving the department the right to request assurance in relation to income tax and National Insurance obligations	2	5
No. for whom assurance has been requested	2	5
Of which...		
No. for whom assurance has been received	1	1
No. for whom assurance has not been received[1]	1	4
No. that have been terminated as a result of assurance not being received.	0	0

[1] This individual failed to respond prior to the year end and sale of the business to Babcock.

FINANCIAL PERFORMANCE REVIEW

Prior to the effect of the sale & disposal transactions on the accounts, DSG successfully completed its 7th year as a trading fund with a very satisfactory outcome of good profits for the year and a strong Statement of Financial Position at the year-end.

Overall, DSG's financial performance exceeded its plan with a Profit before Interest and Dividend of £14.6m.

Trading Results

DSG achieved a better than plan profit with below plan operating costs, which enabled the MOD customer to be given an unplanned price rebate of £1.9m. ROCE achieved was 8.79%.

There was significant Trade Union Industrial Action towards the end of 14/15. This was successfully resolved with no net impact on customers or outputs.

Cash Flow and Funding

The capital structure of DSG on formation was defined in the DSG Establishment as a Trading Fund Entry Terms document.

At 31st March 2015, DSG had repaid its Public Dividend Capital (PDC) of £23.3m and Government Loans, also valued at £23.3m.

Liquidity was strong throughout the year with a closing net cash position (pre-Sale) at 31st March 2015 of £19.0m.This balance was subsequently transferred to MOD post-Sale.

Capital Investment

Expenditure on capital projects amounted to £0.3m during the year.

Dividend

During the year, DSG paid MOD a dividend of £15m in respect of the year 2014/15.

Sale & Disposal Transactions

The Statement of Financial Position reflects the transfer of all DSG's assets and liabilities at year-end either to Babcock DSG, DECA or elsewhere in MOD and therefore shows nil balances.

Louise Tulett
Accounting Officer
23rd June 2015

DIRECTORS' REPORT

PENSION LIABILITIES

Details of the pension liabilities and their treatment is contained the Remuneration Report on Page 19 and in the notes to the accounts (para c of Note 5).

COMPANY DIRECTORSHIPS AND OTHER SIGNIFICANT INTERESTS HELD BY BOARD MEMBERS

No director of the DSG Board held any company directorships or other significant interests out with their DSG positions.

REMUNERATION PAID TO THE AUDITORS FOR NON-AUDIT WORK

DSG made no remuneration to the auditors for non-audit work in the financial year 2014/15.

SICKNESS ABSENCE

The total number of days lost due to sickness absence was 18,298, which equates to 6.78 days per employee. The comparative figures for FY13/14 were 26,994 and 10.11 respectively.

REPORTING OF PERSONAL DATA RELATED INCIDENTS

There are no reported personal data related incidents for the financial year 2014/15.

Louise Tulett
Accounting Officer
23rd June 2015

REMUNERATION REPORT

REMUNERATION COMMITTEE

The Remuneration Committee was a sub-Committee of the DSG Trading Fund Board (TFB) and existed to advise its owner, MOD, DSG's Chairman, Chief Executive and the TFB on matters relating to employee remuneration, and to ensure consistency with the Personnel Delegations held by the Chief Executive of DSG.

The remuneration of all DSG employees except senior civil servants (SCS) was set within the Civil Service Pay Guidance issued by HM Treasury annually.

The Remuneration Committee consisted of the independent NEDs of DSG's Board, an MOD representative and a representative from Human Resources to act as secretary. One of the NEDS acted as Chairman and other Executive Directors attended meetings to assist the committee in their deliberations as appropriate. The Committee met as required during the financial year and all recommendations arising from the meetings have been implemented.

The Committee made a positive input to the strategic direction of DSG pay settlements prior to sharing these with the Trades Unions. The terms of the DSG Corporate Bonus Scheme were agreed by the Remuneration Committee and endorsed by the TFB who then, having taken due consideration of the performance of the business, approved any bonus to be paid, the amount of which was presented to and endorsed by the DSG OAC.

REMUNERATION POLICY

The Finance Director, Chief Operating Officer and Human Resources Director were SCS. As such, their pay was set through recommendations made by the Review Body on Senior Salaries. The Review Body on Senior Salaries provides independent advice to the Prime Minister and the Secretary of State for Defence on the remuneration of the SCS taking account of evidence it receives about wider economic considerations and the affordability of its recommendations. Further information about the work of the Review Body can be found at https://www.gov.uk/government/organisations/office-of-manpower-economics.

All other employees had their remuneration determined by a process consistent with MOD and Treasury guidance.

The Chief Executive had delegated powers for the setting of terms and conditions of employment, including pay, for all DSG employees below SCS. The delegation required him to consult with MOD and HM Treasury before agreeing to any changes to pay and grading systems and arrangements. This was achieved through the business case and pay remit process whereby DSG pay proposals were submitted for MOD and HM Treasury approval before negotiation with staff representatives. The outcome of negotiations was reported back to HM Treasury through the annual outturn statement.

For the 2014/15 pay settlement year, all employees were awarded a pay increase of 1% which was consistent with Public Sector Pay Policy.

The DSG Pay and Grading Structure was approved by the DSG Board and Remuneration Committee and was designed to achieve the Corporate Business Strategy having due regard to the financial success of DSG, current Government and MOD policies and targets, and public sector pay guidance.

Performance Pay for staff was dependent firstly on DSG meeting agreed Internal Business Measures at a corporate level and then on individuals meeting agreed targets cascaded from the Corporate Plan. Achievement was determined by individual assessment within the line management chain. The DSG Board and Remuneration Committee may approve changes to pay and conditions of service prior to commencing the pay negotiating process with the Trades Unions.

All pay awards were subject to the satisfactory performance of the duties assigned.

SERVICE CONTRACTS OF DIRECTORS

Directors who were substantive members of the SCS hold appointments that are open-ended and made in accordance with the Constitutional Reform and Governance Act 2010 which requires Civil Service appointments to be on merit and based on fair and open competition. The Recruitment Principles published by the Civil Service Commission specify the circumstances when appointments may be made otherwise. Further information about the work of the Civil Service Commissioners can be found at www.civilservicecommission.org.uk. Members of the SCS recruited or promoted to the grade before 2 April 1990 have a 3 month notice period, members recruited or promoted to the grade after this time have a 1 month notice period.

Early termination of an Executive Director's appointment, other than for misconduct, would result in the individual receiving compensation as set out in the Civil Service Compensation Scheme. Details of the Civil Service Compensation Scheme can be found at http://www.civilservicepensionscheme.org.uk/

Archie Hughes was re-appointed on 1 August 2011 as Chief Executive on a fixed term contract which is due to expire in September 2015. Compensation for early termination, other than for misconduct, would be in accordance with the Civil Service Compensation Scheme. However, Archie Hughes transferred on TUPE terms on 31st March 2015 to DSG Babcock as the new owner of the Land business. The Chief Executive salary increases are determined by MOD centre and DSG is advised of any change accordingly.

Geraint Spearing was appointed CE Designate of the newly formed Defence Electronics and Components Agency on 1st June 2014. DSG did not appoint a Chief Operating Officer to replace Geraint Spearing, but appointed Dave Edmunds as the Head of Operations, reporting directly to the Chief Executive. On 31st March 2015, as part of the sale of DSG's Land business, Archie Hughes, Keith Norris and Richard Atkinson transferred to Babcock on TUPE terms. On the same date, Steve Hall and Jane Williams transferred to other roles in MOD.

MOD appointed the independent NEDs for a fixed term but not as civil servants, they are paid on a MOD administered payroll. Contracts may be terminated at one month's notice by either party or on dissolution of the Board unless found guilty of gross misconduct when termination would be immediate.

Remuneration for NEDs was set at a fixed annual rate determined by the Department's Permanent Under Secretary. Fees were set on the basis that the role should require around 40 days work per year. This excluded the NED representing the interests of the MOD's Finance Director whose services were not charged to DSG. NEDs were not involved in any discussion about their own remuneration and all payments made were non-pensionable. There were no compensation entitlements for early termination.

THE FOLLOWING INFORMATION IS SUBJECT TO AUDIT

REMUNERATION DETAILS OF DIRECTORS

Single Total Figure of Remuneration – Executive Directors									
		2014-15				2013-14			
		Salary and allowances[1 7]	Performance Bonus[2]	Pension Benefits[4]	Total	Salary and allowances[1]	Performance Bonus[2]	Pension Benefits[4]	Total
		£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Archie Hughes	Chief Executive	175-180	60-65	45-50	280-285	155-160	60-65	35-40	255-260
Steve Hall	Finance Director	75-80	0-5	5-10	85-90	70-75	-	10-15	85-90
Geraint Spearing[3]	Chief Operating Officer	85-90		15-20	100-105	79-80	0-5	(10)-(15)	70-75
Jane Williams	Human Resources Director	70-75		10-15	85-90	65-70	-	0-5	65-70
Keith Norris[5]	Strategy Director	85-90	10-15	10-15	115-120	70-75	5-10	0-5	75-80
Richard Atkinson[6]	Commercial Director	80-85	0-5	20-25	105-110	40-45	-	0-5	45-50

[1] Gross salary includes: salary; reserved rights to London Weighting or London allowances; recruitments and retention allowances; travel and subsistence allowances, compensation packages and any other allowance to the extent that it is subject to UK taxation.
[2] Performance Bonuses are considered as part of the overall performance appraisal process, the outcome of which is not usually known until after the publication of the Annual Accounts. The value reported for the Chief Executive reflects the estimated bonus in year for the individuals' performance for that same year which has been accrued at the maximum value payable whilst awaiting formal approval.

[3] Mr Spearing ceased to be Chief Operating Officer on 1st June 2014 on which date he was appointed to the position of Chief Executive (Designate) for the Electronics and Components Business Unit which is to be retained within MOD as a Trading Agency after the sale of DSG's Land business.
[4]The value of pension benefits accrued during the year is calculated as (the real increase in pension multiplied by 20) plus (the real increase in any lump sum) less (the contributions made by the individual). The real increases exclude increases due to inflation or any increase or decreases due to a transfer of pension rights.
[5] The bonus value for Keith Norris relates to both 13/14 and 14/15
[6] From 6th September 2013
[7] Following a review by HMRC during 2014/15 regular travel costs incurred by directors were considered to be benefits in kind and are included as such in Directors' remuneration for 2014/15. The change in treatment and reporting of these costs affects only 2014/15. No figures for these benefits in kind are included in Directors' remuneration for 2013/14 as they were included within travel and subsistence costs.

PENSION BENEFITS

	Accrued Pension at pension age as at 31/03/15 and related lump sum £'000	Real increase / (decrease) in pension and related lump sum at pension age £'000	CETV at 31/03/15 £'000	CETV at 31/03/14[1] £'000	Real increase / (decrease) in CETV £'000	Employee contribution to partnership pension account £'000
Archie Hughes	25-30	0-5	453	388	36	-
Steve Hall	20-25 Plus lump sum of 70-75	0-5 Plus lump sum of 0-5	417	393	3	-
Geraint Spearing	20-25 Plus lump sum of 70-75	0-5 Plus lump sum of 0-5	352	326	8	-
Jane Williams	30-35 Plus lump sum of 90-95	0-5 Plus lump sum of 0-5	630	587	13	-
Keith Norris	30-35 Plus lump sum of 95-100	0-5 Plus lump sum of 0-5	733	684	15	-
Richard Atkinson	10-15	0-5	176	145	18	-

[1]The figure may be different from the closing figure in the previous year's accounts. This is due to the CETV factors being updated to comply with The Occupational Pension Schemes (Transfer Values) (Amendment) Regulations 2008

PAY MULTIPLES

Reporting bodies are required to disclose the relationship between the remuneration of the highest paid Director in their organisation and the median remuneration of the organisation's workforce.

The banded remuneration of the highest-paid Director in DSG in the financial year 2014/15 was £235,000-240,000 (2013/14; £220,000 - £225,000). This was 10.3 times (2013/14 9.72 times) the median remuneration of the workforce, which was £22,873 (2013/14 £22,645).

No employees in either 2014/15 or 2013/14 received remuneration in excess of the highest-paid Director. Remuneration fell in ranges from £10,000 - £15,000 to £235,000 - £240,000 (2013/14; £10,000 - £15,000 to £220,000 - £235,000).

Total remuneration includes salary, non-consolidated performance-related pay and benefits-in-kind. It does not include severance payments, employer pension contributions and the cash equivalent transfer value of pensions.

CIVIL SERVICE PENSIONS

A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies.

The figures include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the Civil Service pension arrangements. They also include any additional pension benefit accrued to the member as a result of their buying additional pension benefits at their own cost. CETVs are calculated in accordance with The Occupational Pension Schemes (Transfer Values) (Amendment) Regulations 2008 and do not take account of any actual or potential reduction to benefits resulting from Lifetime Allowance Tax which may be due when pension benefits are taken.

The real increase in CETV represents the amount funded by the employer. It does not include the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

Further details relating to the Civil Service pension arrangements are in Note 5 to these accounts and at the website http://www.civilservicepensionscheme.org.uk/

None of the Directors had opted for a Partnership Account therefore there are no employer contributions to such accounts in respect of these Directors.

No other Director has received a payment for compensation for loss of office under the terms of an approved compensation scheme and no awards or compensation has been paid to former Directors.

None of the Directors had remuneration packages containing non-cash elements or other benefits-in-kind. No payments have been made to third parties for the services of a Director.

NON-EXECUTIVE DIRECTORS	**FEES 2014/15 £'000**	**FEES 2013/14 £'000**
Alex Jablonowski	20-25	20-25
David Barrass	15-20	15-20
Janet Baker[1]	10-15	15-20
David English[2]	-	

[1] Reflects NED fees for April – December 2014 only. After this time, the individual was appointed to a position in the Cabinet Office and was not entitled to receive separate remuneration from DSG but was remunerated in full by the Cabinet Office.

[2] This position has been appointed in conjunction with its responsibilities at MOD. It is not entitled to receive separate remuneration in undertaking its DSG duties but was remunerated in full by MOD.

APPROVAL

The Directors' Remuneration Report is approved.

Louise Tulett
Accounting Officer
23rd June 2015

STATEMENT OF ACCOUNTING OFFICER'S RESPONSIBILITIES

Under the Section 4(6) of the Government Trading Funds Act 1973, HM Treasury has directed DSG to prepare for each financial year a statement of accounts in the form and on the basis set out in the Accounts Direction. The accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of DSG and of its profit, changes in taxpayers' equity and cash flows for the financial year.

In preparing the accounts, the Accounting Officer (AO) is required to comply with the requirements of the *Government Financial Reporting Manual* and in particular to:

- observe the Accounts Direction issued by HM Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;

- make judgements and estimates on a reasonable basis;

- state whether applicable accounting standards as set out in the *Government Financial Reporting Manual* have been followed, and disclose and explain any material departures in the financial statements;

The AO of the Ministry of Defence designated the Chief Executive as AO of DSG for the entire year 2014/15, until the CE was transferred to Babcock as the new owner of the DSG Land Business on 31 March 2015. The AO of the MOD then designated the MOD's DG Finance as AO for the period from 1 April 2015 to oversee the final closure and accounts of DSG. The responsibilities of an AO, including responsibility for the propriety and regularity of the public finances for which the AO is answerable, for keeping proper records and for safeguarding DSG's assets, are set out in Managing Public Money published by HM Treasury.

As far as I am aware there is no relevant audit information of which DSG's auditors are unaware and as AO I have taken all the steps that ought to have been taken to make myself aware of any relevant audit information and to establish that DSG's auditors are aware of that information.

Louise Tulett
Accounting Officer
23rd June 2015

GOVERNANCE STATEMENT

SCOPE OF RESPONSIBILITY

With the sale of DSG's Land business to Babcock, Archie Hughes relinquished his responsibilities as Accounting Officer on 31st March 2015. I was appointed as Accounting Officer for the Trading Fund in succession to Archie with responsibility for the preparation of the final DSG Trading Fund Accounts for 2014-15. As Accounting Officer, I must be able to assure Parliament and the public of high standards of probity in the management of public funds, including the DSG Governance Statement.

The Annual Report and Accounts for 2014-15 as presented here have been produced under the guidance and oversight of the members of the Audit Committee.

In order to sign this statement I have sought assurance from the outgoing AO who has issued a statement to me confirming the actions he has taken before departing and he confirms were he remaining in office he would have been content to sign the annual financial statements. In addition before his departure he confirmed that he had sought assurance from the outgoing board and their direct reports which did not give rise to any significant issues. All risks associated with the sale have been identified and managed during the transition phase and a closure team managed by BSG have been appointed that will ensure closure in due time to enable the accounts to be finalised and signed in accordance with the timetable.

GOVERNANCE FRAMEWORK

From the reviews I have undertaken, and the assurance provided by the outgoing AO, I believe the Governance Structure and systems of Internal Control within DSG, to the extent that it is deemed relevant and practical, have followed the requirements of the Corporate Governance Code of Good Practice. The Governance Policy and Process were subject to review or Internal Audit on a frequent basis. The governance structure in place during 2014/15 was as follows:

- **Owners Advisory Council (OAC)**, chaired by the Min (DEST) as representative of our owners, was scheduled to meet up to 3 times a year to review DSG's performance.

- **Trading Fund Board (TFB)**, which was chaired by an independent NED and whose members comprise the four NEDs, one of whom was the representative of the shareholder, CE, FD and SD and was scheduled to meet 6 times a year. The main responsibilities were to review and manage the performance of DSG, review the Risk Management Policy and Process, the Corporate Risk Register, and to review the Information Asset Management Process.

- **Executive Management Board (XMB)**, which met every month and comprised the Executive directors of DSG and whose main responsibilities was to manage the performance of DSG against its targets and review and manage the Corporate Risk Register.

- **Audit Committee (AC)**, which was chaired by an independent NED with two other NEDs as members and Defence Internal Audit (DIA): NAO, FD and Head of Internal Audit (HIA) DSG were attendees and met at least four times a year. The AC was a sub-committee of the TFB. The role of the committee was to support the Board and to advise the AO on the adequacy and effectiveness of governance, risk and control arrangements within DSG.

- **Executive Governance Group,** the previous AO chaired the Executive Governance Group which included all XMB members and the HIA. The main responsibilities were to review the Governance Policy and Processes of DSG and manage the Internal Audit and Risk Management Policies and Processes.

Schedule of meetings and attendance during 2014/15:

Meeting	Members	No. of Members	Scheduled frequency	Meetings held	Attendance
OAC	Min (DEST), CDM, DGF, DES LE-Dir, BSG, DSG Exec Directors	8	Up to 3 times annually	2	66%
TFB	Independent NEDs, MOD NED, DSG CE, FD and SD	7	6	5	97%
XMB	Exec Directors	6	Monthly	10	86%
Remuneration Committee	Independent NEDs, DSG Executives	4	3	3	Full
Audit Committee	Independent NEDs, MOD NED, (NAO, DIA, DSG FD & HIA in attendance)	3	4	4	Full
Executive Governance Group	DSG Executive Directors & DSG HIA	7	4	4	96%

There were subsidiary committees that report to the XMB in respect of Compliance, Health & Safety, Environmental Control, Information Asset Management, Remuneration, Internal Audit and Risk Management (the following paragraphs cover the latter two in detail).

Minutes were taken at all of the meetings above and there was a requirement to report to the AO any significant issues/risks should they arise, demonstrate how they were being managed, assign owners, and enter on the appropriate risk register.

NEDs continued to make a valuable contribution to the board meetings and governance of DSG.

There was a register of member's interests maintained by the TFB Secretariat for the NEDs and this included the Executive Board members.

BOARD PERFORMANCE

The OAC met twice in the last twelve months, and the TFB, XMB and AC have met 5, 10 and 4 times respectively during the last year. The XMB and AC received regular reports from Compliance, Internal Audit, Security, Business Continuity, Risk Management and Finance. Specifically Compliance, Internal Audit and Risk Management provided reviews of any Corporate Governance issues that arose. All meetings were quorate and the Board Secretariat recorded minutes and actions.

The TFB reviews and assesses its own performance each year. Last year the TFB determined that it had performed satisfactorily. The TFB had reviewed the Corporate Governance Code of Good Practice; and believed there were no departures from this Code. During this assessment, TFB also reviewed the effectiveness of the AC and Remuneration Committee and found that they had also performed satisfactorily.

HIGHLIGHTS OF BOARD COMMITTEE REPORTS

The AC, Remuneration Committee, Risk Management and Compliance Meeting minutes were circulated to the Executive Board along with any relevant reports. Significant items from these meetings were:

Audit Committee

- The AC has been proactive in reviewing the Internal Audit activities and attending to process improvements for both Internal Audit and Risk Management; approving the annual internal audit plan and monitoring its progress during the year; and approving the terms of reference of the Risk Management Committee.
- The principal audits carried out in year were:
  - IBMs – DIA carried out the review, which confirmed that DSG had met its targets for 2013/14, MOD confirmed that there was no requirement for 2014/15.
  - Business Continuity – to ensure that the BCP activity is up to date and plans are effective and tested - Substantial Assurance
  - Maintaining Control of the Business – to ensure that robust financial plans, forecasting and performance monitoring are in place and are effective in maintaining control of the business in accordance with the Corporate Strategic Plan – Full Assurance
  - Compliance Failure – To ensure that DSG policies and business processes, relating to HSEP compliance, are aligned with appropriate MOD policy and are fitting for the DSG environment – Substantial Assurance.
  - Sale of DSG – Impact on DSG Business Plan – To ensure that DSG have adequate and appropriate Governance in place to manage the activities of the sale of DSG, and which may affect the achievement of the DSG business plan - Substantial Assurance
  - Major Security Breach – DSG's assets are safeguarded from unauthorised access or disclosure – This was awarded NO Assurance by DIA, however the DSG board and AC have reviewed the report and agree with HIA that this audit should be reassessed as Limited Assurance and

this has been done. There are however some significant issues to address relating to adherence to policies and processes.
    - ECBU Separation - To ensure that DSG have adequate and appropriate governance in place to manage the project to separate the Electronic Components Business Unit (ECBU but to become Defence Electronics and Components Agency [DECA] from 1 April 2015) from the DSG Land business being sold – Substantial Assurance.
    - Vehicle Management – Management of vehicles - to ensure the effective, safe and efficient use of vehicles – follow up audit from Limited Assurance last year – satisfactory progress.
    - In addition DSG internal auditors have carried out compliance audits across all sites during the year with no significant findings or non-conformances still outstanding.

The AC and the Executive Governance Meeting paid particular attention to the Limited Assurance from the vehicle management audit. There were 25 recommendations which required substantial review across all sites, all recommendations have now been implemented; the follow up audit by DIA established that satisfactory progress had been made. Also following the poor result for the Major Security Breach audit the AC has expressed its concern given the current security status in the UK.

- The AC approved the Annual Report and Accounts for 2013/14 with no significant issues raised and the accounts for 2014/15 will be reviewed at the June Committee meeting.
- The AC reviewed and amended its TOR, as it does each year and prepared a report on its own effectiveness to the AO. The report highlighted the principal activities of the Committee which included:
    - Approval of the Annual Report & Accounts
    - In-depth review of the recommendations from Internal Audit reports with special emphasis on the improvements to the vehicle management audit.
    - There has been substantial attention paid to the activities surrounding the sale of DSG's Land business, with special attention to the financial transactions required to reflect the closure of DSG.

The Audit Committee has been retained in full for the final AC meeting in June 2015 for the purpose of reviewing and approving these accounts.

Remuneration Committee

The Committee has met as required during the year and its core activity has been to approve the policy in relation to the remuneration of DSG employees. In addition, the Committee approved targets and payments for XMB members. The Committee also reviewed the people management and succession planning processes within the business.

Risk Management

Both the TFB and XMB carried out in-depth reviews of the Corporate Risk Register and approved new risks relating to the proposed sale of DSG's Land business, industrial action, vehicle inspections and driving safely.

Compliance Meeting

This met 4 times and issued a report to the XMB and AC primarily dealing with quality issues, including Health & Safety (Reporting of Injuries, Diseases and Dangerous Occurrences Regulations (RIDDOR) and accident data), results from Compliance audits, customer and supplier concerns, and data on other operational issues. There were no Air or Land major attributable customer concerns and there has been a steady reduction in numbers of incidents, which is an improvement from last year.

CORPORATE GOVERNANCE

The structure of Corporate Governance in DSG has been effective and was regularly reviewed both internally and periodically, externally. In the Board's opinion DSG, to the extent that it is deemed relevant and practical, has followed the Code's requirements.

INFORMATION REPORTING

The Integrated Business Reporting (IBR) Department controlled IBR, which aimed to handle all data requirements supplied to the Board to assist in decision-making. DSG enhanced this by consolidating into one enterprise resource planning system, Baan. The TFB, XMB and senior management reviewed reports generated on a regular basis. Both the TFB and XMB expressed their satisfaction with the levels of data generated to assist management decision-making. There was frequent review by the Board of the quality and suitability of the data and reports generated in order to optimise the effectiveness and suitability for use and management action.

RISK MANAGEMENT

The ethos of Risk Management in DSG during the last year has been continuous improvement to consolidate the good work done in previous years and concentrate on embedding risk management culture throughout the organisation. In addition, there has been increased focus on Project Risk Management in support of bids and proposals.

The DSG XMB accepted that some degree of business risk is inevitable, being a normal part of the operation of an organisation. Within the in-depth reviews of the Corporate Risk Register, the XMB has demonstrated its tolerance with the different categories of risk and through its Directors has given guidance to the functional heads for the functional and site risk registers. The same approach was adopted in respect of new business, key projects and business plans. Decisions on risk levels were communicated to those responsible for managing those risks or risk areas.

Risk Management in DSG was structured as follows:

- Corporate Risk Register – owned and reviewed by the TFB and reviewed regularly by the XMB. Risks included are those identified as affecting DSG as a whole and requiring Board members to manage them. The key risks identified within this register were:
    - Business restructuring - as a result of changing customer requirements
    - Material supply & provisioning – delays in purchasing/sourcing spares impacts delivery timescales
    - Industrial Action – continuing industrial action will impact delivery of output
    - Sale of DSG's Land business – the risks of adverse effects on core functions and the delivery of the business plan have now been closed. The only risk remaining is related to the agreement of working capital.
    - Compliance failure – failure to adhere to compliance measures could result in loss of accreditation from our reviewing bodies such as LRQA and UKAS
    - Loss of personal or key data
    - Loss of control of the business – failure to recognise that targets are not being met or over achieved
    - Inaccurate data – data not available or inaccurate
    - Failure to deliver the Business Continuity Plan
    - Vehicle inspections – failure to carry out vehicle inspections and thus release to service
    - Major security breach
    - Adverse customer perception/opinion of DSG
    - Future business strategy – failure to secure strategic development opportunities for DSG.
    - Unable to maintain profitability - failure to achieve Cost Reduction Programme
    - Key staff – loss of key individuals
    - Future competence requirements – alignment of competence to future demand opportunities

- Functional Risk Registers – owned by Board members or Heads of Site and cover all the functions in DSG. Risks were identified as those not affecting DSG as a whole and included risks that have been downgraded due to mitigation actions.

- Site Risk Registers – these were owned and managed by Heads of Sites and were reviewed regularly at Senior Management Team meetings.

- Project Risk Registers – were required for all major projects and proposals.

- Information Asset Management Risk – was managed by HR and reviewed regularly.

The Risk Management Process operated as follows during 2014/15:

- TFB – owns the Corporate Risk Register and was responsible for ensuring mitigation is in place and reviewing the actions of the XMB.

- XMB – carry out more frequent in-depth reviews of the corporate risks and recommend downgrading or approving and accepting upgrades of risks.

- AC – Approves the Risk Policy and Process and, through HIA, receives regular updates to incorporate central government advice and recommendations; and ensures recommendations from Internal Audit activity are implemented promptly.

- Risk Management Committee – met at least 4 times a year, managed the policy and process for the AC and has recently reviewed its TOR, which the AC approved. The chair was the FD or his delegated deputy and members were Board directors or their deputies and functional heads. Proposals for upgrading or downgrading of risks were normally handled through this committee who would make the recommendations.

- Risk Coordinators Committee – met at least 4 times a year, handled the management of the site registers and managed the software package, Active Risk Manager (ARM). It is here that risks were identified for possible elevation through the Risk Management Committee if considered serious or becoming significant across most sites.

FRAUD AND INFORMATION ASSURANCE

DSG has ensured that all its Information Asset Owners (IAO) have undertaken assessments to the required levels. The HR function maintained the Risk Register. There have been no breaches of the Information Management Asset Process and no loss of corporate data.

There have been no reported incidents of Fraud during the year.

HEALTH & SAFETY

The Major RIDDOR's reported have reduced from three in 2013/14 to two for this reporting year (both in March 2015) reported incidents being one finger amputation and one fractured ribs. There has been no statistically significant increase in RIDDOR reportable events this financial year (17 compared with 22 in 13/14), whilst reported incidents (non-RIDDOR) have reduced by 13% in comparison to 2013/14. There have been no significant environmental incidents on any of the DSG sites.

SUMMARY

The HIA issued his annual statement, which is a comprehensive view of the overall level of Assurance of DSG and includes the evaluation of reports from compliance on incidents involving individuals, Health & Safety, Quality and HR; and the overall opinion is that DSG has been making steady progress and improvement. As a result the HIA has recommended an overall level of assurance as Substantial and the AC have agreed and accepted this.

The main area of control weakness identified during the year, and as a result added to the Corporate Risk Register, emerged from the vehicle management audit from 2013/14. The principal issue related to a gap in driving qualification skills, licence and competences not being defined and assessed. A new risk has also been identified in year in relation to sites being unable to fully comply with JSP930 Volume 3 (Mandatory Equipment Inspection Facilities Policy) requirements. Appropriate mitigating actions and controls have been taken and we currently await further key stakeholder engagement and direction in relation to a potential future licensing scheme and full compliance with JSP930 requirements.

In addition, the report of the Major Security Breach audit instigated significant discussion at the AC and as a result it was agreed that the level of assurance should be increased to Limited from the DIA assessment of No Assurance. However this was caveated in that the AC made it clear that the recommendations had to be introduced and proven and Babcock had to be made aware of the contents and findings of the report in order that they can compare this with their own processes and check for any weaknesses. The AC also considered whether there was a major risk of a security breach; the only significant issues raised were actually outside DSG control and were dealt with once we were alerted to the situation. The conclusion was that the risk of a major security breach was not high as the sites have still dealt with any incidents that have arisen. In addition all the recommendations have now been implemented and closed and this further reduces any residual risk.

Louise Tulett
Accounting Officer
23rd June 2015

THE CERTIFICATE AND REPORT OF THE COMPTROLLER AND AUDITOR GENERAL TO THE HOUSES OF PARLIAMENT

I certify that I have audited the financial statements of the Defence Support Group for the year ended 31 March 2015 under the Government Trading Funds Act 1973. The financial statements comprise: Statement of Comprehensive Income, Statement of Financial Position, Statement of Cash Flows, Statement of Changes in Taxpayers' Equity; and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

RESPECTIVE RESPONSIBILITIES OF THE ACCOUNTING OFFICER AND AUDITOR

As explained more fully in the Statement of Accounting Officer's Responsibilities, the Accounting Officer is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit, certify and report on the financial statements in accordance with the Government Trading Funds Act 1973. I conducted my audit in accordance with International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Defence Support Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Defence Support Group; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies, I consider the implications for my certificate.

I am required to obtain evidence sufficient to give reasonable assurance that the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities, which govern them.

OPINION ON REGULARITY

In my opinion, in all material respects the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

OPINION ON FINANCIAL STATEMENTS

In my opinion:
• the financial statements give a true and fair view of the state of the Defence Support Group's affairs as at 31 March 2015 and of its loss for the year then ended; and
• The financial statements have been properly prepared in accordance with the Government Trading Funds Act 1973 and HM Treasury directions issued thereunder.

EMPHASIS OF MATTER – GOING CONCERN

Without qualifying my opinion, I draw attention to the disclosures made in Note 1 to the financial statements. The Ministry of Defence sold the majority of the DSG business to Babcock International in March 2015 and the remainder was transferred to the Department itself. The Trading Fund ceased to operate after the 31 March 2015. As a consequence of this, the accounts have been prepared on a basis other than going concern. Details of the movements of DSG's assets and liabilities are shown in Note 3 to the financial statements.

OPINION ON OTHER MATTERS

In my opinion:
• The part of the Remuneration Report to be audited has been properly prepared in accordance with HM Treasury directions made under the Government Trading Funds Act 1973; and
• The information given in the Strategic Report and the Directors Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

MATTERS ON WHICH I REPORT BY EXCEPTION

I have nothing to report in respect of the following matters which I report to you if, in my opinion:
• adequate accounting records have not been kept or returns adequate for my audit have not been received from branches not visited by my staff; or
• the financial statements and the part of the Remuneration Report to be audited are not in agreement with the accounting records and returns; or
• I have not received all of the information and explanations I require for my audit; or
• the Governance Statement does not reflect compliance with HM Treasury's guidance.

REPORT

I have no observations to make on these financial statements.

Sir Amyas C E Morse
Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP
7 July 2015

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 March 2015

	Note	2014/15	2013/14
		£'000	£'000
Turnover	2	175,757	179,478
Cost of sales	3	(148,659)	(153,568)
Gross profit		**27,098**	**25,910**
Operating expenses	3	(12,460)	(10,294)
Operating profit		**14,638**	**15,616**
Profit on ordinary activities before interest and costs on closure		**14,638**	**15,616**
Costs on closure	3.1	**(128,049)**	**0**
Interest receivable		235	347
Interest payable	4	(536)	(1,129)
(Loss)/Profit for the year before dividend		**(113,712)**	**14,834**
Dividend Payable		(15,000)	(7,000)
Net Income after interest and dividend		**(128,712)**	**7,834**
OTHER COMPREHENSIVE INCOME/(EXPENDITURE)			
Items that will not be reclassified to profit or loss			
Net gain/(loss) on revaluation of Property Plant & equipment		1,312	1,754
Total comprehensive Income/ (Expenditure) for the year		**(127,400)**	**9,588**
Return on capital employed (ROCE)		**8.79%**	**9.04%**

The notes on pages 41 to 64 form part of these accounts.

STATEMENT OF FINANCIAL POSITION AS AT 31 MARCH 2015

	Note	31 March 2015 pre Sale and separation £'000	Effect of Sale and Separation £'000	31 March 2015 £'000	31 March 2014 £'000
Non Current Assets					
Non current assets					
Property, Plant and Equipment	7	79,177	(79,177)	-	82,508
Total Non Current Assets		**79,177**	**(79,177)**	**-**	**82,508**
Current assets					
Inventories and work in progress	8	31,146	(31,146)	-	26,150
Trade and other receivables	9	27,837	(27,837)	-	31,692
Cash and cash equivalents	10	18,982	(18,982)	-	67,173
Total current assets		**77,965**	**(77,965)**	**-**	**125,015**
Total Assets		**157,142**	**(157,142)**	**-**	**207,523**
Current liabilities					
Trade and other payables	11	(28,612)	28,612	-	(33,301)
Loans	12	-	-	-	(1,663)
Provisions	13	(481)	481	-	(200)
Total current liabilities		**(29,093)**	**29,093**	**-**	**(35,164)**
Non Current liabilities					
Loans	12	-	-	-	(21,635)
Total non current liabilities		**0**			**(21,635)**
Net Assets		**128,049**	**(128,049)**	**-**	**150,724**
Financed by:					
Capital and reserves					
Public dividend capital		0	-		23,324
Revaluation reserve		68,325	(68,325)	-	67,414
Retained earnings		59,724	(59,724)	-	59,986
Taxpayers' equity		**128,049**	**(128,049)**	**-**	**150,724**

The notes on pages 41 to 64 form part of these accounts.

Louise Tulett
Accounting Officer
23rd June 2015

These accounts have been authorised for issue by the Accounting Officer on the same date as the Comptroller and Auditor General's Audit Certificate.

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 MARCH 2015

	Note	2014/15 £'000	2013/14 £'000
Cash flows from operating activities			
Operating profit	statement of comprehensive income	14,638	15,616
Adjustments for:			
Losses on disposals of non-current assets	7	79,204	24
Permanent Diminution and Reclassification of non current assets	7	29	8
Depreciation charges	7	4,907	4,855
Decrease / (increase) in inventories	8	26,150	(4,966)
(Increase) / decrease in receivables	9	31,692	3,660
(Decrease) / increase in payables	11	(33,301)	2,806
(Decrease) in provisions for liabilities and charges	13	(200)	(1,063)
Non cash movement in assets as a result of Sale and separation	3.1	(109,067)	-
Net cash inflow from operating activities		**14,052**	**20,940**
Cash flows from investing activities			
Payments to aquire property plant and equipment	14a	(320)	(1,040)
Interest received	14a	235	347
Net cash (outflow) from investing activities		**(85)**	**(693)**
Cash flows from financing activities			
Repayment of public Dividend capital		(23,324)	-
Decrease in borrowings	14a	(23,298)	(1,663)
Dividends paid	statement of comprehensive income	(15,000)	(14,000)
Interest paid	14a	(536)	(1,129)
Cash balance transferred to MOD		(18,982)	
Net cash (outflow) from financing activities		**(81,140)**	**(16,792)**
(Decrease) / increase in cash and cash equivalents	14c	**(67,173)**	**3,455**
Cash and cash equivalents at start of year	14b	67,173	63,718
Cash and cash equivalents at end of year	14b	-	67,173

The notes on pages 41 to 64 form part of these accounts.

STATEMENT OF CHANGES IN TAXPAYERS' EQUITY FOR THE YEAR ENDED 31ST MARCH 2015

	Public Dividend Capital	Revaluation Reserve	Retained Earnings	Total Equity
	£'000	£'000	£'000	£'000
Taxpayers' equity at 31st March 2013	**23,324**	**66,088**	**51,724**	**141,136**
Comprehensive income for the year	-	1,754	7,834	9,588
Realised element of revaluation reserve	-	(428)	428	-
Taxpayers' equity at 31st March 2014	**23,324**	**67,414**	**59,986**	**150,724**
Recognised in Statement of Comprehensive income for the year	-	1,312	(128,712)	**(127,400)**
Repaid during year	(23,324)			**(23,324)**
Realised element of revaluation reserve in year		(401)	401	
Realised element of revaluation reserve on sale and separation	-	(68,325)	68,325	**0**
Taxpayers' equity at 31st March 2015	0	0	0	0

The notes on pages 41 to 64 form part of these accounts.

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2015

1 Accounting policies

Basis of accounting

The accounts have been prepared in accordance with the Government Financial Reporting Manual (FReM) for 2014/15 and the Accounts Direction, both issued by HM Treasury. The accounting policies contained in the FReM apply International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector context. Where the FReM permits a choice of accounting policy, the accounting policy which was judged to be most appropriate to the particular circumstances of DSG for the purpose of giving a true and fair view was selected.The particular policies adopted by DSG are described below. They have been applied consistently in dealing with items considered material in relation to the accounts.

In autumn 2010 the MOD's Strategic Defence and Security Review (SDSR) announced that DSG would be one of the MOD owned assets which would be offered for sale. The Sale was completed on 31 March 2015 also, as part of the process, DSG's existing Electonics and Components business has separated from the rest of the business and remains in MOD ownership forming a new MOD Executive Agency called DECA. The rest of the business was transferred to DSG Land Equipment Support Ltd (DLES), a company wholly owned by MOD in preparation for sale.
As a result of of the Sale and separation process all of DSG's assets and liabilities were either transferred to DLES , transferred to DECA or transferred to MOD . No consideration was received by DSG as a result of these transfers.

After the sale DSG ceased to exist as a Trading fund. The Accounting Officer formed the view that in these circumstances it was not appropriate to continue to adopt the going concern basis in preparing the Annual Report and Accounts. The net book values of all assets and liabilities have been reduced to nil as a result of the sale and separation and there are no assets or liabilities shown in the Statement of Financial Position.

These accounts are prepared on a basis other than going concern.

Absorbtion accounting

The sale and transfer of DSG's assets are condidered to be transfers of function and as such are required by the FreM to be accounted for under absorbtion accounting. Under absorbtion accounting net assets are transferred at their carrying value with the value of the assets shown as a non operating loss. There is no requirement to restate prior year comparatives.

Accounting convention

These accounts have been prepared in accordance with the accruals concept and the historical cost convention, modified to account for the revaluation of land and buildings and other non current assets, at current costs or value to the business.

Turnover

Turnover comprises the invoiced and accrued value of services (excluding VAT and other sales taxes) and is recognised in line with the underlying sales contract which may result in turnover and costs recognised prior to job completion.

Property, plant and equipment

Basis of Valuation

Property Plant and Equipment are carried at fair value. A professional quinquennial valuation, in accordance with the Royal Institute of Chartered Surveyors Appraisal and Valuation Standards Red Book, was carried out by GVA Grimley Ltd as at 31st March 2011 and covered all classes of non current assets. Due to the nature of the business assets a market valuation is difficult to determine therefore the basis of valuation applied is generally Depreciated Replacement Cost (DRC) or Existing Use where DRC is not appropriate.

Property, Plant and Equipment is revalued in the years between professional valuations, using the Corporate Financial Controller (CFC) Modified Historic Cost Accounting (MHCA) indices produced by the Defence Analytical Services Agency (DASA), and is carried at valuation as at the end of the accounting period.

Basis of Recognition

Expenditure on plant, equipment, computers and transport equipment was periodically reviewed and capitalised where the useful life exceeds one year and the cost of acquisition exceeds the threshold of £10,000 excluding VAT. The value of capitalised plant, equipment and transport equipment was reviewed annually and adjustments made using the CFC MHCA Index in the relevant periods.

Individual items valued at less than the threshold were ordinarily capitalised only if they constituted integral parts of a composite or grouped asset that was in total valued greater than a threshold of £25,000. A composite or grouped asset was intended only to encompass items that are purchased to operate together rather than bulk purchases of items that could, or would ordinarily, operate in an individual capacity.

Non current assets were recognised initially as Assets in the Course of Construction which were not depreciated. At the point that an asset became fully available for use, it was recategorised appropriately and depreciation commenced.

Land and buildings

Where DSG bore the risks and rewards of using Departmental Estate, such estate was treated as an asset of the Trading Fund although legal ownership rested with the Secretary of State for Defence.

Depreciation

Freehold land was not depreciated. Depreciation on buildings, plant and equipment, transport equipment and IT equipment was calculated to reflect the consumption of economic benefit of assets by equal instalments over their estimated useful lives. The lives of the assets were periodically reviewed with reference to obsolescence and continued asset useage. Although DSG ceased to exist after 31st March 2015 the assets will continue in use either within MOD or by the buyers of DLES.

The depreciation rates applied to the main categories of assets were based on the following initial estimates of useful life:

Buildings - Not exceeding sixty years

Plant & Equipment - Between three and twenty years

Transport Equipment - Between three and twenty years

IT Equipment - Between three and ten years

Where an impairment loss has occurred with reference to the existing use of an asset, a discount rate of 3.5% has been applied to the cashflows.

Pension costs

Past and present employees are covered by the provisions of the Principal Civil Service Pension Scheme (PCSPS) and Armed Forces Pension Schemes (AFPS) which is non-contributory and unfunded. Although the scheme is a defined benefit scheme, liability for payment of future benefits is a charge to the PCSPS or AFPS appropriately. The cost of pension cover provided is by payments of charges (Accrued Superannuation Liability Charges - ASLC) based on a percentage of salary. Salaries include gross salary, certain performance bonuses and recruitment and retention allowances. It does not include the estimated monetary value of benefits in kind. Payments are made at contribution rates determined by the Government Actuary's Department.

Foreign exchange

All foreign denominated transactions were translated at the average exchange rate for the previous month, being a proxy rate for that ruling at the time of the transaction. At 31 March balances were translated into sterling at a year end spot rate. Foreign exchange differences were taken directly to the Statement of Comprehensive Income.

Inventories

Inventory was valued on a first in first out basis (FIFO) and at the lower of cost or net realisable value. Following periodic reviews, inventory was written down to address obsolescence, surpluses and defective items using two main criteria based on redundancy and technical validity.

Redundant inventory was written down to its net recoverable value and disposed of. Items that were technically valid but for which DSG had no current forecast requirement were also written down to their net recoverable amount and disposed of unless a justification was made for retention due to a definable imminant contractual requirement.

Where provision was made it was based on 100% provision against the value of the appropriate items. This calculation could include any significant surplus inventories based on projected consumption using historical trends and review by management.

Work in progress

Work in progress was valued on the basis of direct labour, where this was applicable to the contract, and indirect production support, plus those business overheads that were directly related to normal levels of production activity. For spares inclusive contracts, the cost of the spares consumed was also included in the WIP valuation. The value was reviewed monthly to reflect the lower of cost or net realisable value and the rates used to value WIP were reviewed at least annually.

Long term contracts

Long term contract (LTC) balances were stated at costs incurred (net of amounts transferred to cost of sales), after deducting related payments on account. Profit on individual long term contracts was taken only when their outcome could be foreseen with reasonable certainty, based on the lower of the percentage margin earned to date and that prudently forecast at completion, taking account of agreed claims. Turnover on long term contracts is ascertained in a manner appropriate to the stage of completion of the contract.

Provisions

At the point any contract is foreseen to become loss making a provision was be made for the future losses identified. Other provisions represent liabilities of uncertain timing or amount. Provisions were discounted where the effect of the discount would be material.

Provision for bad and doubtful debts

DSG made provision for bad and doubtful debts as soon as they are deemed to be irrecoverable based on analysis and reviews of aged receivables.

Operating leases

Rentals under operating leases were charged to the Statement of Comprehensive Income as incurred.

There were no finance leases.

Return on capital employed

The return on capital employed was expressed as the profit before interest for the year calculated as a percentage of the average capital employed during the year. Capital employed comprises the total net assets (non-current assets at net book value, plus current assets, less current liabilities, less non current liabilities) and adding back the short and long term loans provided from government sources.

Value Added Tax

DSG had a single registration for VAT with HM Revenue & Customs and accounts for VAT on an accruals basis.

Employee Benefits

DSG accrued for untaken employee leave entitlement at the end of the financial year. For permanent employees the leave year runs to 30th April and employees were able to carry forwards an element of entitlement at the end of the financial year. These amounts fall due within one year and the value of the liability was calculated using records of actual untaken leave and average pay rates to comply with IAS 19.

Significant Accounting Judgements and Estimates

DSG management made judgements and assumptions concerning the future that impacted on the application of policies and reported amounts. The resulting accounting estimates calculated using these judgements and assumptions, by definition, seldom equalled the related actual results but were based on historical experience and expectations of future events. The risk generated by these judgements and estimates was therefore materially only cost related and is mitigated as far as is practical. The judgements and key sources of estimation uncertainty that have a significant effect on the amounts recognised in the financial statements are discussed below.

Provisions

Provisions have been made for obsolete stock, expected future legal / employment tribunal costs and other relevant events. These provisions were estimates and the actual costs and timing of future cash flows are dependent on future events. Any difference between expectations and the actual future liability will be accounted for in the period when such determination is made.

Accounting accruals

Accruals for the costs of goods and services received were recognised based on the best information available at the reporting date. Any difference between accounting accruals and the actual liability when presented will be accounted for in the period when such determination is made.

CFC Indexation Rates and Quinquennial Non Current Asset Review

Indices were provided by the Corporate Financial Controller (CFC) for revaluing non current assets under the Modified Historic Cost Accounting (MHCA) regime. Whilst these indices predict a valuation as at the end of the accounting period they also include corrections for previous periods. In these accounts, DSG has applied the professional external revaluations of its non current assets from GVA Grimley at as 31 March 2011.

Impairment of Assets

On an Annual basis DSG reviwed its assets for any indication that an asset may be impaired (I.e.that its carrying amount may be higher than its recoverable amount). If any asset was found to be impaired its value was reduced to its recoverable amount.

2 (a)Turnover and segmental analysis

Turnover is stated net of trade discounts, provisions, VAT and similar taxes. There were no acquisitions and the majority of turnover arose from UK sources.

Where the substance of the transaction is such that DSG effectively operates as an agent, turnover represents the net revenue receivable and due to DSG in accordance with contractual terms.

Although substantially all turnover relates to the same class of business, the repair, overhaul and maintenance of equipment, DSG is able to analyse its operating profit by activity depending on the type of equipment platform being worked on. The major segments are Land platforms, Air and Electronic platforms and specialist procurement and supply operation carried out by the Land Supply business.

Analysis of turnover and operating profit by segment

2014/15	Land	Air and Electronics	Land Supply	Total
	£'000	£'000	£'000	£'000
Turnover (i)	136,818	26,011	12,928	175,757
Cost of Sales	116,733	21,243	10,683	148,659
Administrative Expenses	9,068	2,597	795	12,460
Operating profit	**11,017**	**2,171**	**1,450**	**14,638**

(i) Within turnover £175.241K relates to MoD customers.

2013/14	Land	Air and Electronics	Land Supply	Total
	£'000	£'000	£'000	£'000
Turnover (i)	139,494	27,794	12,190	179,478
Cost of Sales	123,215	20,701	9,652	153,568
Administrative Expenses	7,403	1,943	948	10,294
Operating profit	**8,876**	**5,150**	**1,590**	**15,616**

(i) Within turnover £179,117 k relates to MoD customers.

2 (b) Business Separation of ECBU

In autumn 2010 the MOD's Strategic Defence and Security Review (SDSR) announced that DSG would be one of the MOD owned assets which would be offered for sale. The sale was completed on 31 March 2015 and as part of the process, DSG's existing Electonics and Components business has separated from the rest of the business and has remained in MOD ownership.

The Profit on ordinary activities before interest for the Electronics and Components business to be separated is shown below:

	2014/15	**2013/14**
	£'000	£'000
Turnover	26,011	27,794
Cost of sales	(21,243)	(20,701)
Gross profit	**4,768**	**7,093**
Operating expenses	(2,597)	(1,943)
Operating profit	**2,171**	**5,150**
Profit on ordinary activities before interest and dividend	**2,171**	**5,150**

3 Cost of sales and operating expenses.

	Note	2014/15	2013/14
		£'000	£'000
Cost of sales:			
Staff costs	5b	83,333	87,298
Supplies and services consumed		50,882	52,804
Accommodation costs		3,605	3,873
Depreciation and impairment		4,811	4,757
Cost reimbursement (i)		(247)	(248)
Other administration costs	6	6,275	5,084
Total cost of sales		**148,659**	**153,568**
Operating expenses:			
Staff costs	5b	9,691	8,215
Supplies and services consumed		(214)	(261)
Accommodation costs		213	125
Depreciation and impairment		124	106
Cost reimbursement (i)		(1)	0
Other administration costs	6	2,647	2,109
Total operating expenses		**12,460**	**10,294**
Cost of sales & operating expenses:			
Staff costs	5b	93,024	95,513
Supplies and services consumed		50,668	52,543
Accommodation costs		3,818	3,998
Depreciation and impairment		4,935	4,863
Cost reimbursement (i)		(248)	(248)
Other administration costs	6	8,922	7,193
Total cost of sales & operating expenses		**161,119**	**163,862**

(i) Cost reimbursement primarily relates to various facility management and other costs recharged to units lodging on DSG sites of £248k (2013/14 £248k). These reimbursements are shown as a separate line to assist visibility.

3.1 a) Costs arising from sale and separation

	Note	2014/15	2013/14
		£'000	£'000
(Losses) on disposal of Property plant and equipment	7	(79,177)	-
Gains/(Losses) on disposal of net current assets and liabilities:			-
Inventory	8	(31,146)	-
Receivables	9	(27,837)	-
Payables		28,612	-
Cash	10	(18,982)	-
Provisions	13	481	-
Net loss on disposal of assets and liabilities		(128,049)	
Total costs on closure		**(128,049)**	**-**

The DSG land business was transferred, on 31 March 2015, from DSG to an off the shelf incorporated entity - DSG Land Equipment Support Ltd (DLES) a company wholly owned by the MOD. The Department then immediately (31 March 2015) sold its entire shareholding in the company to Babcock Land Limited and received £140M in cash as consideration

3.1 b) Movement of Trading Fund assets and liabilities

	SoFP before Sale and Separation	Transferred to DLES Ltd	Transferred to DECA	Transferred to MOD	Balance at 31st March 2015	Loss/(Gain) arising from transfers
	£'000	£'000	£'000	£'000	£'000	£'000
Non Current Assets	79,177	(2,488)	(11,629)	(65,060)	-	79,177
Property , plant & equipment						
Current Assets						
Inventory	31,146	(30,580)	(566)		-	31,146
Trade and other receivables	27,837	(23,419)	(4,520)	102	-	27,837
Cash and cash equlvalents	18,982			(18,982)	-	18,982
Total current assets	77,965	(53,999)	(5,086)	(18,880)	-	77,965
Total assets	157,142	(56,487)	(16,715)	(83,940)	-	157,142
Current Liabilities						
Trade and other payables	(28,612)	12,782	5,709	10,121	-	(28,612)
Provisions	(481)		481			(481)
Total current liabilities	(29,093)	12,782	6,190	10,121	-	(29,093)
Net assets	128,049	(43,705)	(10,525)	(73,819)	-	128,049

DSG Land Equipment Support Ltd (DLES) was formed by MOD to receive the assets to be sold to the buyer of the DSG business. These assets were transferred into DLES which was then sold to the buyer.

DECA did not exist until 1st April 2015 so the assets to be transferred to DECA were transferred to MOD on 31st March 2015 and then transferred to DECA on 1st April 2015.

The sale agreement allowed for adjustment to the proceeds of £140 M received by the MOD to reflect the extent to which the value of the business assets transferred to Babcock Land Limited differed from that assumed at the time the price was agreed. This aspect of the sale is still subject to negotiation. The amounts shown above reflect the values recorded in the DSG accounts before the sale and separation. Under Absorption Accounting, the carrying value of the assets and liabilities of the combining bodies or functions are not adjusted to fair value on consolidation. Therefore the values shown for amounts transferred to DLES are not intended to reflect the outcome of these negotiations, although depending on the final outcome there may be some amendments to the classification of transfers.

4 Interest payable and similar charges

	2014/15	2013/14
	£'000	£'000
On loans wholly repayable within five years	536	1,129
On loans not wholly repayable within five years	-	-
	536	**1,129**

5 Staff numbers and costs

(a) Staff numbers	2014/15	2013/14
	Number of employees	Number of employees
The average number of persons employed during the year was:		
Senior Management	6	6
Service personnel	1	1
Civilian personnel	2,400	2,403
Agency staff	291	256
	2,698	**2,666**

(b) Payroll costs

	£'000	£'000
in Cost of sales:		
Salaries, wages and allowances	60,685	64,453
Social security	4,389	4,878
Pension costs	10,200	10,364
Agency Staff	8,059	7,603
	83,333	**87,298**
in Operating expenses:		
Salaries, wages and allowances	7,589	6,391
Social security	744	547
Pension costs	900	899
Agency Staff	458	378
	9,691	**8,215**
Total:		
Salaries, wages and allowances	68,274	70,844
Social security	5,133	5,425
Pension costs	11,100	11,263
Agency Staff	8,517	7,981
Total payroll costs	**93,024**	**95,513**

5 Staff numbers and costs (Continued)

(c) Pension benefits are provided through the Civil Service pension arrangements. From 30 July 2007, civil servants may be in one of four defined benefit schemes; either a final salary scheme (classic, premium or classic plus); or a whole career scheme (nuvos). These statutory arrangements are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under classic, premium, classic plus and nuvos are increased annually in line with Pensions Increase legislation. Members joining from October 2002 may opt for either the appropriate defined benefit arrangement or a 'money purchase' stakeholder pension with an employer contribution (partnership pension account).

Employee contributions are salary-related and range between 1.5% and 6.85% of pensionable earnings for classic and 3.5% and 8.85% for premium, classic plus and nuvos. Benefits in classic accrue at the rate of 1/80th of final pensionable earnings for each year of service. In addition, a lump sum equivalent to three years initial pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike classic, there is no automatic lump sum. classic plus is essentially a hybrid with benefits for service before 1 October 2002 calculated broadly as per classic and benefits for service from October 2002 worked out as in premium. In nuvos a member builds up a pension based on his pensionable earnings during their period of scheme membership. At the end of the scheme year (31 March) the member's earned pension account is credited with 2.3% of their pensionable earnings in that scheme year and the accrued pension is uprated in line with Pensions Increase legislation. In all cases members may opt to give up (commute) pension for a lump sum up to the limits set by the Finance Act 2004.

The partnership pension account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3% and 12.5% (depending on the age of the member) into a stakeholder pension product chosen by the employee from a panel of providers. The employee does not have to contribute, but where they do make contributions, the employer will match these up to a limit of 3% of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8% of pensionable salary to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement).

The accrued pension quoted is the pension the member is entitled to receive when they reach pension age, or immediately on ceasing to be an active member of the scheme if they are already at or over pension age. Pension age is 60 for members of classic, premium and classic plus and 65 for members of nuvos.

Further details about the Civil Service pension arrangements can be found at the website www.civilservicepensionscheme.org.uk. New Career Average pension arrangements will be introduced from 1st April 2015 and the majority of classic , premium , classic plus and nuvos members will join the new scheme. Further details of this new scheme are available at http://www.civilservicepensionscheme.org.uk/members/the-new-pension-scheme-alpha/

The Principal Civil Service Pension Scheme (PCSPS) is an unfunded multi employer defined benefit scheme and it is not possible to separately identify DSG's share of the underlying assets and liabilities. A full actuarial valuation was carried out as at 31 March 2007. Details can be found in the resource accounts of the Cabinet Office: Civil Superannuation (www.civilservice-pensions.gov.uk).

For 2014/15 employers' contributions of £11,037,593 were payable to the PCSPS (2013/14 £11,232,525) at one of four rates in the range 16.7% to 24.3% of pensionable pay, based on salary bands. The Scheme Actuary reviews employer contributions usually every four years following a full scheme valuation. The contribution rates are set to meet the cost of the benefits accruing during 2014/15 to be paid when the member retires and not the benefits paid during this period to existing pensioners.

For 2014/15 employers' contributions of £53,295 were paid to one or more of a panel of four appointed stakeholder pension providers (2013/14 £43,915). In addition, employer contributions of £3,464 were payable to the PCSPS to cover the cost of the future provision of lump sum benefits on death in service and ill health retirement of these employees (2013/14 £1,959). Contributions due to the partnership pension providers at the statement of financial position date were £5,677 (2013/14: £4,723) .

5 employees retired early on ill-health grounds; the total additional accrued pension liabilities in the year amounted to £2,896 (2013/14 2 persons - additional pension liabilities amounted to £4,678).

5 Staff numbers and costs (Continued)

(d) Reporting of Civil Service and other compensation schemes - exit packages

Exit costs are accounted for in full in the year of departure except for the annual compensation costs of certain packages which fall into future years and are accounted for in the year of payment.

Comparative data shown in brackets for 2013/14.

Exit package cost band	**Number of Agreed Departures**	
<£10,000	0	(2)
£10,000 - £25,000	1	(8)
£25,000 - £50,000	0	(11)
£50,000 - £100,000	0	(1)
£100,000- £150,000	0	0
Total number of exit packages for in year departures	1	(22)
Total cost of in year departures £'000	1,658	(4,188)

There were no compulsory redundancies in 2014/15 (and none in 2013/14)

Redundancy and other departure costs have been paid in accordance with the provisions of the Civil Service Compensation Scheme, a statutory scheme made under the Superannuation Act 1972. Exit costs are funded directly by the MOD and are therefore not accounted for within DSG.

Where early retirements have been agreed, the additional costs are met by DSG and not by the Civil Service pension scheme. Ill-health retirement costs are met by the pension scheme and are not included in the table.

The total cost includes £1,640k for pre 1 April 2014 leavers which will fall into financial year 2014/15 (£3,610k for pre 1 April 2013 leavers costs falling into 2013/14).

6 Other administration costs

	2014/15	2013/14
	£'000	£'000
in Cost of sales:		
Travel and subsistence, including vehicle hire	1,983	1,999
IT and telecommunications	3,356	2,746
Training, recruitment and consultancy	848	711
Insurance	16	44
Other expenses	195	(216)
Movement in Provisions	(123)	(200)
	6,275	**5,084**
in Operating expenses:		
Auditors' remuneration	83	83
Travel and subsistence, including vehicle hire	415	449
IT and telecommunications	243	203
Training, recruitment and consultancy	166	65
Insurance	875	940
Other expenses	450	368
Losses/ (Gains) on Foreign Exchange	-	-
Movement in Provisions	415	1
	2,647	**2,109**
Total:		
Auditors' remuneration	83	83
Travel and subsistence, including vehicle hire	2,398	2,448
IT and telecommunications	3,599	2,949
Training, recruitment and consultancy	1,014	776
Insurance	891	984
Other expenses	645	152
Gains on Foreign Exchange	-	-
Movement in Provisions	292	(199)
Total of Other administration costs	**8,922**	**7,193**

7 Property Plant and Equipment

The movements in each class of assets during 2014/15 were:

	Land	Buildings	Plant & Machinery	Transport Equipment	IT	Assets in Course of Construction	Total Tangible
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Cost or valuation:							
At 31 March 2014	21,946	70,576	4,439	182	618	52	97,813
Additions	-	26	76	-	80	138	320
Donations	-	-	-	-	-	-	-
Disposals	-	(111)	(46)	-	(9)	-	(166)
Transferred to Defence Land Equipment Support Ltd			(3,595)	(174)	(541)		(4,310)
Transferred to DECA	(3,631)	(11,503)	(415)	(10)	(126)	(72)	(15,757)
Transferred to MOD	(18,315)	(60,327)	(715)		(27)	(66)	(79,450)
Impairment / Reversal of Impairment	-	-	(29)	-	-	-	(29)
Reclassification	-	-	52	-	-	(52)	-
Revaluation	-	1,339	233	2	5	-	1,579
At 31 March 2015	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Depreciation:							
At 31 March 2014	-	13,554	1,401	101	249	-	15,305
Depreciation charged during the year	-	4,356	434	23	94	-	4,907
Disposals	-	(111)	(25)	-	(3)	-	(139)
Impairment	-	-	-	-	-	-	-
Transferred to Defence Land Equipment Support Ltd			(1,399)	(119)	(302)		(1,820)
Transferred to DECA	-	(3,873)	(218)	(6)	(31)	-	(4,128)
Transferred to MOD		(14,162)	(222)		(8)		(14,392)
Revaluation	-	236	29	1	1	-	267
At 31 March 2015	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Net book value							
At 31 March 2015	**-**	**-**	**-**	**-**	**-**	**-**	**-**
At 31 March 2014	21,946	57,022	3,038	81	369	52	82,508

In addition to the above movements assets known as Customer Supplied Items (CSI's) which had previously been in MOD ownership but used by DSG were transferred to DSG on 31st March 2015 and immediately transferred to DLES Ltd.

7 Property Plant and Equipment (continued)

The movements in each class of assets during 2013/14 were:

	Land	Buildings	Plant & Machinery	Transport Equipment	IT	Assets in Course of Construction	Total Tangible
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Cost or valuation:							
At 31 March 2013	21,946	68,014	3,708	197	521	442	94,828
Additions	-	512	476	-	-	52	1,040
Donations	-	-	-	-	-	-	-
Disposals	-	-	(29)	(16)	(38)	-	(83)
Impairment / Reversal of Impairment (i)	-	-	(8)	-	-	-	(8)
Reclassification	-	115	261	-	66	(442)	-
Revaluation	-	1,935	31	1	69	-	2,036
At 31 March 2014	**21,946**	**70,576**	**4,439**	**182**	**618**	**52**	**97,813**
Depreciation:							
At 31 March 2013	-	8,966	998	82	181	-	10,227
Depreciation charged during the year	-	4,321	417	25	92	-	4,855
Disposals	-	-	(13)	(6)	(40)	-	(59)
Impairment	-	-	-	-	-	-	-
Reclassification	-	-	-	-	-	-	-
Revaluation	-	267	(1)	-	16	-	282
At 31 March 2014	**-**	**13,554**	**1,401**	**101**	**249**	**-**	**15,305**
Net book value							
At 31 March 2014	**21,946**	**57,022**	**3,038**	**81**	**369**	**52**	**82,508**
At 31 March 2013	**21,946**	**59,048**	**2,710**	**115**	**340**	**442**	**84,601**
Asset Financing:							
Owned	21,946	54,853	3,038	81	369	52	80,339
Donated	-	2,169	-	-	-	-	2,169
NBV as at 31 March 2015	**21,946**	**57,022**	**3,038**	**81**	**369**	**52**	**82,508**

8 Inventories and work in progress

	31 March 2015		31 March 2014	
	£'000	£'000	£'000	£'000
Gross Inventories	17,260		15,077	
Less inventory provision	(10)		(184)	
		17,250		14,893
Work in progress - net costs incurred		13,896		11,257
Total inventory & WIP before sale and separation		**31,146**		**26,150**
Transferred to Defence Land Equipment Support Ltd		(30,580)		-
Transferred to DECA		(566)		
		-		26,150

During 2014/15, inventory with a value of £22.158m was charged to cost of sales along with the creation of an in year provision of £0.260m which £0.01m remained at year end. Inventory with a value of £0.377m was written off against previously created provisions. During the same period, £9.377m of work in progress was expensed to cost of sales.

9 Receivables and prepayments

	31 Mar '15	31 Mar '14
	£'000	£'000
Trade and sundry invoiced receivables	25,376	29,010
Other receivables	172	778
Bad debt provision	-	(25)
Prepayments and accrued income	2,289	1,929
Total receivables before sale and separation	**27,837**	**31,692**
Transferred to Defence Land Equipment Support Ltd	(23,419)	-
Transferred to DECA	(4,520)	-
Transferred to MOD	102	-
	-	31,692

Current assets are further analysed by debtor category as noted below:

	31 Mar '15	31 Mar '14
	£'000	£'000
Other central government bodies	25,067	27,641
Bodies external to government	2,770	4,051
	27,837	31,692

All the above balances fall due within 1 year.

Aged Trade and Sundry Invoiced Receivables Analysis	Not Yet Due	30 to 60 Days	60 to 90 Days	90 to 120 Days	120 Days +	Total
	£'000	£'000	£'000	£'000	£'000	£'000
At 31 March 2015	21,817	1,881	750	476	452	25,376
At 31 March 2014	23,282	4,347	495	65	821	29,010

10 Cash at bank and in hand

	31 March 2015	31 March 2014
	£'000	£'000
Cash on short term deposit and at bank (i) (ii)	18,982	67,172
Cash in hand	-	1
Total cash before sale and separation	**18,982**	**67,173**
Transferred to MOD	(18,982)	-
	-	67,173

11 Payables

Amounts falling due within one year:	31 March 2015	31 March 2014
	£'000	£'000
Trade payables	1,387	1,260
Taxation and social security	2,695	1,636
Value Added Tax	6,038	6,520
Accruals	11,336	16,111
Deferred income	4,042	4,417
Sundry payables	3,114	3,357
Total payables before sale and separation	**28,612**	**33,301**
Transferred to Defence Land Equipment Support Ltd	(12,782)	-
Transferred to DECA	(5,709)	-
Transferred to MOD	(10,121)	-
	-	**33,301**

Payables are further analysed by creditor category as below:	31 March 2015	31 March 2014
	£'000	£'000
Other central government bodies	13,014	21,204
Bodies external to government	15,598	12,097
	28,612	33,301

12 Short term and long term loans

	31 March 2015	31 March 2014
	£'000	£'000
Current portion of long term borrowings	0	1,663
Loan repayments due within 2 and 5 years	0	6,658
Loan repayments due after 5 years	0	14,977
	0	**23,298**

The outstanding loan balance was repaid during the year in preparation for sale.

13 Provisions for liabilities and charges

	Provision for closure costs	Other	Total
	£'000	£'000	£'000
Balance at 1 April 2014	0	200	200
Increase / (decrease) in provisions	415	(97)	318
Utilised in year	0	(37)	(37)
Balance at 31 March 2015 before sale and separation	**415**	**66**	**481**
Transferred to MOD	-	-	-
Transferred to DECA	(415)	(66)	(481)
Transferred to Defence Land Equipment Support Ltd	-	-	-
Balance at 31 March 2015	-	-	-

The balance on other provisions at 31st March was required to meet a variety of obligations, mainly to provide replacement stock for parts supplied by a customer. This balance was transferred to DECA.

During the year an obligation to replace a number of Government Furnished Assets was resolved and the provision relating to this obligation was released.

14 Cash flow statement note

	2014/15	2013/14
	£'000	£'000
(a) Detailed analysis of gross cash flows		
Returns on investments and servicing of finance		
Interest received	235	347
Interest paid	(536)	(1,129)
	(301)	**(782)**
Capital expenditure		
Non current assets in the course of construction	(138)	(52)
Purchase of non current assets	(182)	(988)
	(320)	**(1,040)**
Financing		
With the MoD:		
Decrease in borrowings	(23,298)	(1,663)
	(23,298)	**(1,663)**

(b) Analysis of changes in net funds/(debt)

	At 31 March 2014	Cashflow	At 31 March 2015
	£'000	£'000	£'000
Cash at bank and in hand	67,173	(67,173)	-
Debt due within one year	(1,663)	1,663	-
Debt due after one year	(21,635)	21,635	-
Total	**43,875**	**(43,875)**	**-**

(c) Analysis of changes in cash and cash equivalents

	£'000
Balance at 31st March 2014	**67,173**
Net change in cash and cash equivalent balances	(67,173)
Balance at 31st March 2015	**-**

15 Operating leases

Operating Lease payments recognised as expenses in the period were:

	2014/15	2013/14
	£'000	£'000
Leases of other Land and Buildings	-	15
Leases of vehicles & Other Equipment (i)	377	371
Total operating leases paid	**377**	**386**

(i) Contained within note 6 - Vehicle hire and Other expenses and within note 3 - Supplies and services consumed

None of these payments were contingent rents or sublease payments.

Future minimum lease payments under non-cancellable operating leases are due as follows:

	31 March 2015	31 March 2014
	£'000	£'000
Not later than one year	-	165
Later than one year and not later than five years	-	16
Later than five years	-	-
	-	**181**

None of DSG's leasing arrangements have renewal or purchase options, rentals are payable on fixed installments over the duration of the lease.

There are no restrictions imposed by lease arrangements on dividends or further debt.

All of DSG's Operating Leases have either been terminated at the end of 2014/15 or have the obligations under them transferred to other parties. DSG has no future obligations under leases.

Future minimum lease payments under non-cancellable operating leases where DSG is acting as lessor are:

	31 March 2015	31 March 2014
	£'000	£'000
Receivable within one year	-	325
Receivable after one year	-	-
	-	**325**

This relates to a short term lease on facilities at the Sealand site.

There are no finance leases.

16 Commitments, Contingent Assets and Liabilities

DSG had no capital commitments as at 31st March 2015 and none were transferred.

There are no contingent assets at 31 March 2015 (nil at 31 March 2014).

There are no Contingent Liabilities at 31st March 2015

Any liabilities concerning environmental pollution are considered to be pre-Trading Fund events and the liability therefore falls to the MOD.

17 Financial Instruments

DSG's treasury operations were governed under the Government Trading Funds Act 1973(a) as supplemented by DSG's Framework Document and were conducted within a framework of policies, mandates and delegations authorised at the top level by the Board and regularly reviewed. DSG's financial instruments comprised cash deposits, debtors, creditors and loans. DSG used forward foreign currency sales and purchase contracts as derivative instruments when required for risk management purposes only, although none have been utilised during 2014/15 (nil during 2013/14). The main purpose of these financial instruments was to finance DSG's operations and DSG had limited powers to borrow or invest surplus funds. The main risks that would arise from the financial instruments were foreign currency, liquidity and interest rate risks. DSG's policies for managing these risks were set to achieve compliance with the regulatory framework including the rules contained within Managing Public Money.

Interest Rate Risk

DSG’s funding was determined by fixed rate Government loans. There were no floating rate liabilities and DSG had only one loan which was repaid during the year.

Currency Risk

DSG conducted business in Sterling, US Dollars, Euros and Swedish Krone and was therefore subject to foreign exchange risk. At 31 March liabilities existed of SKr93k . An adverse movement in foreign currency exchange rates of 10% for this currency would give rise to additional liabilities of £1k.

DSG managed this risk by natural hedging and entering into forward foreign exchange contracts where amounts were material. DSG policy required that transactions were translated at the prior month average rate and year end foreign denominated net assets were translated at a year end spot rate.

All liabilities in foreign currencies were transferred to DLES Ltd at 31st March 2015.

Liquidity Risk

Current liquidity throughout the year was strong. Cash at bank was available on demand and short term investments were conducted through the Lloyds Bank plc Money Market.

Counterparty / Credit Risk

DSG’s approachwas to minimise counter-party risk by aiming only to enter into contracts with institutions with long term credit ratings of AA or better.

Capital Management

The financial strategy of DSG supported its aim of sustaining its manufacturing capability and achieving the return on capital objectives set by its owner. The key elements of the strategy were:

- Sufficient flexibility for the funding of necessary capital expenditure and working capital required for any expansion of the business.
- Avoidance of risk and compliance with HM Treasury policies
- Funding of dividend payments as agreed with the owner.
- Funding of loan repayment schedules.

The Capital structure of DSG was based on management’s judgement of the balancing of all the elements of its financial strategy in order to meet its day-to-day and strategic needs. DSG together with its owner considered the amount of Public Dividend Capital in proportion to loans and retained earnings and manages the capital structure, making adjustments to it if necessary in the light of changes in economic conditions and risk characteristics of the underlying assets.

DSG was not subject to covenants in any of its financing agreements.

Categories of Financial Instruments
Financial Assets

	At 31 March 2015	At 31 March 2014
	£'000	£'000
Trade, sundry and other debtors	25,376	29,788
Cash on short term deposit, at bank and in hand	18,982	67,173
	44,358	96,961
Transferred to Defence Land Equipment Support Ltd	(22,460)	-
Transferred to DECA	(2,916)	-
Transferred to MOD	(18,982)	-
	-	96,961

Financial Liabilities

	At 31 March 2015	At 31 March 2014
	£'000	£'000
Trade and other payables	13,232	17,190
Ministry of Defence loans	-	23,298
	13,232	40,488
Transferred to Defence Land Equipment Support Ltd	(3,062)	-
Transferred to DECA	(161)	-
Transferred to MOD	(10,009)	-
	-	40,488

DSG did not retain any assets classed as held to maturity investments or available for sale financial assets, or any financial assets or liabilities held for trading. For all assets and liabilities, amortised cost was a proxy for fair value due to the short term nature of the instrument.

Embedded Derivatives
In accordance with IAS 39 - Financial instruments: Recognition and measurement, DSG has reviewed all material contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard. No instances were found that required embedded derivatives to be recognised at their fair value separately from the non-derivative host contract. For the contracts reviewed, the economic characteristics and risks were closely related to those of the host contract.

18 Related parties

The Ministry of Defence (MOD) was a related party and has a representative on the DSG Board. During the year, DSG has had material transactions with the Department and with other entities for which MOD is the parent department. None of the DSG Board members or key managerial staff have declared any related party interests which may conflict with their management responsibilities.

19 Events After The Reporting Period

Following the end of the reporting period DSG ceased to exist as a Trading Fund as all of its assets and liabilities were disposed of as disclosed in these accounts. These accounts have been authorised for issue by the Accounting Officer on the same date as the Comptroller and Auditor Generals audit certificate.

As explained in note 3, the sale agreement allowed for adjustment to the proceeds of £140M received by the MOD to reflect the extent to which the value of the business assets transferred to Babcock Land Limited differed from that assumed at the time the price was agreed. This aspect of the sale is still subject to negotiation.

20 Losses and special payments

During the year DSG made ex-gratia payments of £500 per head to staff which totalled £1,209K. There were no other material losses or special payments.

21 Auditors

The Trading Fund Act 1973 requires DSG’s Annual Report and Accounts to be audited by the Comptroller and Auditor General. DSG’s auditor is the National Audit Office (NAO). The cost of this audit is £83,000 (2013/14 £83,000).

22 Third Party Assets

In connection with contracts held with the Jordan Armed Forces, DSG held in its name a bank account, controlled by a member of the Jordan Armed Forces, with a balance of £557k as at 31 March 2015 (£743k as at 31 March 2014).

Responsibilty for this account passed to the MOD on 31st March 2015.

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ISBN 978-1-4741-1665-7