

Audit Committee report



Jeff Perrin
Independent Non-executive Director
and Senior Independent Director

Auditor's remuneration

	2022 £'000	2021 ¹ £'000
Fees payable to the Company's auditor for the audit of the Company and consolidated accounts	78	77
Fees payable to the Company's auditor for the audit of the Company's subsidiaries	289	282
Total audit fees	367	359
Other accounting services	—	7
Interim review fee	48	53
Total non-audit fees	48	60
Total fees paid to the auditor and its associates	415	419
Charged to profit for the year	415	419

1. The 2021 figures include cost overruns of £54,000.

Introduction

Up until 31 August 2021, the Audit Committee comprised two independent Non-executive Directors. From 1 September 2021 the Audit Committee membership was increased to three independent Non-executive Directors following the appointment of Beatrice Nicholas. The Audit Committee is scheduled to meet at least three times a year. It is the Audit Committee's role to provide formal and transparent arrangements for considering how to apply financial reporting under IFRS, the Companies Act 2006, risk and the internal control requirements of the QCA Corporate Governance Code and to maintain an appropriate relationship with the independent auditor of the Group.

The Audit Committee is responsible for ensuring that the Group's risks are understood, managed and mitigated as far as practicable.

Jeff Perrin is Chair of the Audit Committee, being a qualified Chartered Certified Accountant and having experience of the defence industry in this and previous roles. The current terms of reference of the Audit Committee were reviewed and updated in October 2019.

A review is expected in the coming year to address changes in reporting, including Task Force on Climate-related Disclosure, which will apply to the Group from 1 May 2022.

Consideration of the financial statements

In making its recommendation that the financial statements be approved by the Board, the Audit Committee has taken account of the following significant issues and judgement areas:

Areas of judgement

Revenue and profit recognition on fixed-price contracts

The judgement applied in recognising revenue on a contract over time as performance obligations are completed is in respect of the input costs incurred and the attributable margin. The latter is particularly a judgement in respect of estimating the cost to complete on a particular contract and the remaining risk and associated contingency. This cost contingency takes account of the stage that the contract has reached and any judgement and uncertainty remaining to deliver the remainder of the contract. It is usual for these cost contingencies to reduce as the contract progresses and risk and uncertainty reduce.

Recoverability of trade and other receivables

Judgement is applied in determining whether any of the Group's trade and other receivables require a bad debt provision to be recognised. This takes account of the nature of our customers, many of whom are ultimately governments, our historical experience and the commercial terms we have in place to protect the recoverability of our receivables.

Goodwill

The Group has recognised goodwill and other intangible assets in respect of the acquisitions of Chess, MASS, SEA, MCL, EID and ELAC. The other intangible assets are in respect of contracts acquired, intellectual property rights and specific opportunities and, in each case, are amortised over the expected life of the earnings associated with the other intangible assets acquired. The goodwill, which is not subject to amortisation but to at least annual impairment testing, arises from the intangible elements of the acquired businesses for which either the value or life is not readily derived. This includes, but is not limited to, reputation, customer relations, contacts and market synergies with existing Group members. The goodwill relating to the acquisitions of Chess, MASS, SEA, MCL, EID and ELAC has been tested for impairment as at 30 April 2022; this is an area of judgement. In each case there was no impairment. The Group's 2022 post-tax WACC of 10.8% is higher than the 2021 equivalent of 7.6%, which reflects higher interest rates and higher volatility in respect of Cohort plc's shares. These post-tax WACC amounts are equivalent to a pre-tax WACC of 16.2% (2021: 10.4%).

Sensitivity was applied to the impairment tests to deliver a material impairment of goodwill as reported in note 9.

Provisions

The Group makes estimates of provisions for existing commitments arising from past events. In estimating these provisions, the Group makes judgements as to the quantity and likelihood of the liability arising. Certain provisions require more judgement than others. In particular, warranty provisions and contract loss provisions have to take account of future outcomes arising from past deliveries of products and services. In estimating these provisions, the Group makes use of management experience, precedents and specific contract and customer issues.



Audit Committee report continued

Consideration of the financial statements continued

Alternative performance measures (APMs)

The Group reports a number of APMs which are not in accordance with the reporting requirements of IFRS. The Audit Committee has reviewed these during the year ended 30 April 2022 to ensure they are appropriate and that in each case:

- ▶ the reason for their use is clearly explained;
- ▶ they are reconciled to the equivalent IFRS figure; and
- ▶ they are not given prominence over the equivalent IFRS figure.

The most important APMs reported by the Group are as follows:

Adjusted operating profit

This is used by the Group to report what the Board considers is its trading profit in a consistent manner, year on year, to provide the readers of the accounts with a consistent comparative. This is derived from the operating profit as reported under IFRS by excluding amortisation of other intangible assets, all of which arises on the acquisition of subsidiaries; research and development expenditure credits (RDEC), which were prior to the 2019 Annual Report and Accounts shown in the reported tax figure; exceptional items, including costs of acquisitions and reorganisations; and foreign exchange movements from non-trading activities, including marking forward exchange contracts to market.

The reconciliation of operating profit (IFRS) to adjusted operating profit is shown in the Consolidated income statement for the Group and in note 1 to the accounts for the Group's subsidiaries. The following table shows the Group's adjusted operating profit compared with operating profit for the last five years:

	2022 £m	2021 £m	2020 £m	2019 £m	2018 £m
Adjusted operating profit	15.5	18.6	18.2	16.2	15.2
Operating profit (IFRS)	11.1	7.8	10.7	5.9	10.3

The main difference between the two figures is the amortisation of other intangible assets value which arises on the acquisition of businesses.

It is the Board's opinion that the trading performance of the Group is better reflected by the adjusted operating profit.

Adjusted earnings per share

This is based upon the adjusted operating profit after taking account of tax applying to adjusted operating profit and interest, to enable the Group to report an earnings per share figure based upon what the Board considers is a more appropriate and comparable earnings basis.

This is reconciled to the headline (IFRS) earnings per share in note 8 to the accounts.

Independent auditor

The independent auditor liaises with the Audit Committee regarding work to be undertaken and complies with the Ethical Standards for Auditors issued by the Auditing Practices Board. Prior to commencing its audit work, the independent auditor confirmed in writing the nature of any non-audit work carried out on behalf of the Group and the safeguards in place to ensure its independence and objectivity. Any in-year proposals for non-audit work are subject to prior approval by the Audit Committee.

The independent auditor presented its audit plan to the Audit Committee prior to the Audit Committee meeting held in March 2022. The plan was reviewed and approved at that meeting with specific areas of focus by the independent auditor discussed in detail for the ensuing audit.

The independent auditor (RSM UK Audit LLP) was appointed in November 2019.

The analysis of RSM UK Audit LLP (2021: RSM UK Audit LLP) remuneration is shown in the table above. The payments made to RSM UK Audit LLP in 2021 include additional fees incurred as part of that audit.

Fees payable to RSM UK Audit LLP and its associates for non-audit services to the Company are not required to be disclosed because the consolidated financial statements are required to disclose such fees on a consolidated basis only.

Jeff Perrin

Chair of the Audit Committee