Directors, Secretary and Advisers

Chairman	G G Gray
Directors	K S Beeston E Bryan R H B Jones* G Rodgers G L Sturgess* R D White I M Williams
Secretary	C R Hyman
Registered Office	Dolphin House Windmill Road Sunbury-on-Thames Middlesex TW16 7HT
Auditors	Deloitte & Touche Chartered Accountants Hill House 1 Little New Street London EC4A 3TR
Principal Bankers	Barclays Bank PLC 54 Lombard Street London EC3V 9EX National Westminster Bank Plc 1 Princes Street London EC2R 8PB
Merchant Bankers	Lazard Brothers & Co. Limited 21 Moorfields London EC2P 2HT
Stockbrokers	Cazenove & Co. 12 Tokenhouse Yard London EC2R 7AN
Solicitors	Allen & Overy One New Change London EC4M 9QQ
Registrar	Lloyds TSB Registrars The Causeway Worthing West Sussex BN99 6DA

*Non-executive

Corporate Governance

The Board has evaluated the Hampel Committee's Principles of Good Governance and Code of Best Practice ("the Combined Code"), and supports the principles set out in the Combined Code. The Board has applied the principles set out in the Combined Code in the manner set out in this report.

With the exception of the items set out in the following paragraphs, the Company was in full compliance, throughout the 1998 accounting period, with the provisions set out in section 1 of the Combined Code on Corporate Governance issued by The London Stock Exchange.

The Company's Articles of Association do not require Executive Directors to retire by rotation and, consequently, those Directors have not previously submitted themselves for re-election other than at the Annual General Meeting ("AGM") following the date of appointment. Principle A.6 of the Combined Code provides that each Director submit himself for re-election at regular intervals and at least every three years. The Board has resolved to recommend the adoption of new Articles of Association, and in support of this principle, the new Articles of Association will require all Directors of the Company to retire by rotation at least every three years. The new Articles of Association will be submitted for approval and adoption at an Extraordinary General Meeting to be held immediately after the 1999 AGM. In support of best practice, Richard White, Kevin Beeston and Gary Sturgess will voluntarily present themselves for re-election at this year's AGM.

Provision B.1.7 of the Combined Code recommends that an objective be set by companies to reduce contractual notice periods to one year or less. After careful evaluation by the Remuneration Committee, it has been agreed that the contribution made to the development of the Company by Directors, together with the diversity and complexity of the business, warranted the maintenance of a two year contractual notice period to ensure retention, and recruitment, of the services of Directors by the Group.

Throughout 1998, there were two Non-executive Directors who are independent of the management and business of the Group and are highly regarded by the Executive Directors. Under Provision A.3.1 of the Combined Code, it is recommended that Non-executive Directors should comprise at least one third of the Board. In addition, Provision D.3.1 of the Combined Code recommends that at least three Non-executive Directors be members of the Audit Committee. Accordingly, the Board has resolved to appoint a further Non-executive Director to the Board and Audit Committee in support of these provisions, and expects to make such an appointment in the near future.

The Nomination Committee has a formal and transparent procedure in place for the appointment of new Directors. Under Provision A.5.1 of the Combined Code, the majority of this Committee should be Non-executive Directors. The Committee currently comprises an equal number of Executive and Non-executive Directors.

The Board

The Board currently comprises eight Directors:

Kevin Beeston	Finance Director
Everton Bryan	Executive Director
George Gray	Chairman
Rhidian Jones	Senior Non-executive Director
Gerrard Rodgers	Executive Director
Gary Sturgess	Non-executive Director
Richard White	Chief Executive
Iestyn Williams	Executive Director

Short profiles of each Director are set out on page 7.

The Directors meet formally and informally to discuss matters specifically reserved for decision by the Board. Timely information is obtained by the Directors to enable effective independent judgement in decision making. Where required, a Director may seek independent professional advice at the expense of the Company.

Members of the Board have access to the advice and services of the Company Secretary, and may also address specific issues to the Senior Non-executive Director.

In 1998, the Board established a Training and Development Committee. The Committee has been tasked with designing beneficial training programmes for Directors in their respective fields of responsibility, including relevant programmes for new Directors.

The Board encourages dialogue with its shareholders, and regular meetings are held with institutional investors.

Board Committees

The Board has formally constituted, with written terms of reference, the Audit, Remuneration and Nomination Committees.

The Audit Committee comprises both Non-executive Directors, and examines any matters relating to the financial affairs of the Group. Such matters include reviews of the Company's Annual Accounts, internal control procedures, accounting policies, compliance with accounting standards, as well as the independence, objectivity and cost effectiveness of the Group's auditors.

Corporate Governance

The Committee is chaired by Rhidian Jones and meets at least twice each year. The Group's auditors attend these meetings on request, without the presence of Executive Directors where required. Where deemed appropriate, the Committee may also invite the Finance Director to attend the whole or a part of any meeting.

The Minutes of each meeting are formally brought to the Board's attention at Board Meetings.

The Remuneration Committee comprises both Non-executive Directors, and determines all aspects of the Executive Directors' remuneration as well as their terms and conditions of employment.

The Committee is chaired by Gary Sturgess, and its report is set out on pages 10 to 12.

George Gray chairs the Nomination Committee, and its other members are Richard White, Gary Sturgess and Rhidian Jones. The Committee members consider proposed appointments to the Board.

The Committee may consult with other Board members before submitting proposals for approval by the Board.

The Chairmen of the Audit, Remuneration and Nomination Committees will be available to answer questions at the AGM.

Going concern

Following a review of the Group's financial results and forecasts, as well as holding discussions with relevant individuals, the Board has a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Consequently, the going concern basis continues to be adopted in preparing the Annual Accounts.

Internal controls

The Board is vested with the responsibility of ensuring that the Group's system of internal control safeguard the Group's assets, and result in reliable information being used in the Group's business and publications.

Any system of internal control has inherent limitations, and it is acknowledged that even the most effective system can only provide reasonable, as opposed to absolute, assurance against misstatement or loss.

In the opinion of the Board, internal reviews carried out to date have not revealed any significant matters that indicate that the internal controls used in the Group's business lack effectiveness.

Serco Group plc is dedicated to the highest standards achievable in its worldwide operations.

To meet its objectives, the Group operates through a number of clearly defined business units, each with its own senior management team. The senior management team of each unit reports to members of the Board and is responsible for ensuring that the performance of that business meets Group objectives.

The Board has also identified a number of key support activities that are subject to separate regular reporting to the Board. These support activities include treasury and pension management, risk and insurance matters, Health and Safety, quality assurance, as well as the reports of the Audit Committee.

Key financial, operational and compliance procedures used by the Group are described in the following paragraphs.

Executive Directors agree marketing and sales targets with each business unit on an annual basis. Progress against these targets is reviewed regularly.

Financial targets are also agreed between senior management of business units and Executive Directors on an annual basis. These include profit and loss, balance sheet and cashflow forecasts that are reviewed against actual performance on a regular basis. Where required, forecasts for the current year are updated.

Budgets, which are agreed between a budget holder and the senior management teams of business units or executive management, are reviewed regularly and, where applicable, re-forecast. This system of control enables the monitoring of annual sales and costs of individual contracts and cost centres.

The Group has a clearly defined framework for reviewing and approving major capital projects and expenditure. Appropriate authorisation levels requiring approval from the business unit management team or, where appropriate, Board members are in place.

Business unit management teams or, where applicable Board members, review bid documents, tenders and pricing prior to their submission to customers. There are formal sign-off processes to ensure that appropriate authority levels are observed.

Corporate Governance

Business unit management teams or Board members also review contract documents, to ensure that the terms and conditions contained in these are acceptable to the Group.

External audit firms are appointed by the Company to perform an internal audit programme on behalf of the Group, reporting on selected aspects of the Group's system of internal controls, such as those outlined in the above paragraphs. The internal audit programme has not identified any material issues.

Risk management

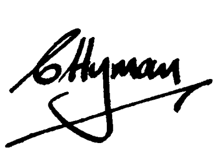
Board members and business unit management teams are responsible for the identification, evaluation and mitigation of key risks applicable to their area of business.

Risks may arise from time to time due to a variety of internal or external sources, as well as breakdown in controls, disruption to information systems, competition, regulatory changes or natural catastrophes.

Each business unit management team is required to certify, on an annual basis, that it has discovered no weaknesses in internal controls that resulted in material losses, uncertainties or contingencies.

Two key risks for many businesses are the impact of European Monetary Union ("EMU") and Year 2000 compliance. These matters are being addressed by working parties throughout the Group, which are headed by Board members and senior management teams, in order that issues and solutions are identified at an early stage. The Company's approach to EMU and Year 2000 is set out in more detail in the Directors' Report.

Approved by the Board of Directors and signed on behalf of the Board:



Christopher R Hyman
Secretary

Dolphin House
Windmill Road
Sunbury-on-Thames
Middlesex TW16 7HT

3 March 1999

Directors' Report

Directors' Report to be presented to the Twelfth Annual General Meeting of the Shareholders

The Directors herewith present the Annual Accounts for the year ended 31 December 1998.

Activities

The activities of Serco Group plc are those of a holding company. Its subsidiary companies and joint venture undertakings provide a wide range of facilities management and systems engineering services.

Review of developments

A review of developments during 1998, the position at the end of that year and the likely future developments in the business of the Group are included in the Chairman's Statement and the Review of 1998 on pages 1 to 24 of the Annual Review and Summary Financial Statement ('Annual Review').

Results

The Consolidated Profit and Loss Account of Serco Group plc and its subsidiaries for the year ended 31 December 1998 is set out on page 15. A review of the Group's activities in 1998 is given on pages 6 to 24 of the Annual Review. These activities will continue in 1999. The Directors are confident that 1999 will be another satisfactory year.

Dividends and transfers to reserves

An interim dividend of 2.3p (1997 - 2.0p) net per Ordinary Share was paid on 16 October 1998. The Directors recommend that a final dividend in respect of the year ended 31 December 1998 of 5.1p (1997 - 4.4p) net per Ordinary Share be paid in April 1999. After dividends, retained profits of £12,532,000 will be transferred to reserves.

Share capital

The increase in the issued Ordinary Share Capital during the period is explained in Note 20 to the Accounts set out on pages 43 and 44.

Special business at the Twelfth Annual General Meeting

Shareholders are invited to renew the Directors' general authorities to allot equity securities and other relevant securities in certain circumstances as set out in the Notice of the Annual General Meeting on pages 58 and 59. The Directors consider that in order to retain some flexibility, the renewal of these authorities is in the best interests of the Company and the shareholders as a whole.

In addition, shareholders are invited to grant to the Company power to make market purchases of its own shares in accordance with the provisions of, and limitations set out in the Companies Act 1985 and The Listing Rules of The London Stock Exchange. The Directors consider that this power will, again, provide flexibility to the Company. The Directors have no immediate intention of exercising the authority. Any such exercise would only take place after careful consideration and to the extent that the Directors believe that a purchase would be in the best interests of the Company, and would result in an expected increase in earnings per Ordinary Share.

As mentioned in the Corporate Governance report, the Directors propose to adopt new Articles of Association for the Company. Further details are set out in the circular accompanying the Annual Review.

The Directors recommend that the shareholders vote in favour of Resolutions 1 to 9 set out in the said Notice. The Notes to the Notice of the Twelfth Annual General Meeting on page 60 set out further information regarding the resolutions to be proposed as the special business to be conducted at that Meeting.

Supplier payment policy

Serco Group plc requires its business units to determine terms and conditions of payment for the supply of capital and revenue items just as keenly as they negotiate prices and other commercial matters.

Suppliers are made aware of the agreed terms and how any disputes are to be settled and payment is to be made in accordance with those terms. The Group's average creditor payment days in 1998 was 36 days (1997 - 37 days) (Company – 30 days (1997 - 35 days)).

Directors' Report

Health and Safety
The Board is committed to ensuring high standards of workplace Health and Safety for its employees, customers and others affected by the Group's activities. The Health and Safety functions in the Group continue to provide advice, guidance and support to Group businesses and employees. Performance is monitored and reviewed on a regular basis.

Environment
The Group and its constituent businesses recognise their responsibilities for the environment. The possible effects of the Group's business on the environment are given due consideration when decisions are taken in such areas as energy use and the minimisation of waste.

Substantial interests
As at the close of business on 12 February 1999 (being the latest practical date prior to the printing of the Directors' Report), the Company had received notifications, pursuant to the Companies Act 1985 (as amended by the Disclosure of Interest in Shares (Amendment) Regulations 1993) of the following 'notifiable interests'. A notifiable interest is an interest of 3% or more of the voting share capital of the Company or, in the case of persons authorised to manage investments belonging to another, 10% or more:

Smith Barney Inc.	3.78%
Standard Life Assurance Company	3.99%
Legal & General Investment Management	4.02%
Putnam Investments	5.94%

Employee policies
The Board is committed to maintaining a working environment where staff are individually valued and recognised.

Managers are tasked with developing employees' awareness of factors affecting the business and matters concerning them as employees and noting employees' views so that they can be taken into account when making decisions which may affect them or the business. Regular meetings are held with employee representatives where trade unions or staff associations are recognised or where works councils are constituted.

The Board understands its responsibility to encourage and assist in the employment, training, promotion and personal career development of disabled people. The Group gives proper consideration to applications for employment received from the disabled and offers employment when suitable opportunities arise. If employees become disabled during their service with the Group, wherever practicable, arrangements are made to continue their employment and training.

Charitable and political contributions
During the year the Group has made contributions amounting to £52,000 (1997 – £60,000) to United Kingdom charitable organisations. No contributions were made for political purposes (1997 – £nil).

European Monetary Union
In 1997 a Euro Committee was set up comprising senior management and external advisers. This Committee managed the training and development of staff and review and upgrading of systems which ensured that there was a smooth transition to the introduction of the Euro on 1 January 1999. All operating units which trade with relevant countries are continually addressing the Euro's gradual implementation. The Committee meets quarterly and discussions are held regularly with external advisers to ensure that the Company is in a position to deal with any issues which may arise.

Year 2000
The Board has appointed one of its members with specific responsibility for Year 2000 issues. The Director responsible for the Year 2000 project has formulated procedures to ensure that the Group is in a position to solve all material issues and test solutions relating to Year 2000 risks well in advance. The Board receives regular reports on progress made and believes that it has appropriate procedures in place and will deal promptly with any issues as they arise.

The Group does not expect to spend a material amount in resolving Year 2000 issues. This information is gained from risk assessments carried out at each of the Group's subsidiaries, which is evaluated and challenged by a worldwide project team on an ongoing basis.

Liability insurance for Company Officers
As permitted by the Companies Act 1985, the Group has maintained insurance cover for the Directors and Officers against liabilities in relation to their responsibilities as Directors and Officers.

Directors
The following Directors served during the year:

K S Beeston F.C.M.A.	
E Bryan B.A. (Hons) A.C.A.	
G G Gray B.Sc Ph.D C.Eng F.I.Mech.E	(Chairman)
R H B Jones M.A. F.C.I.S. F.I.Mgt.	(Senior Non-executive)
G Rodgers	
G L Sturgess Llb	
R D White B.Sc (Hons)	
I M Williams B.A.	

Particulars of Directors' interests in the shares of Serco Group plc are disclosed in Note 3 to the Accounts.

The Directors did not have any material interests in any contract of any company within the Group, during or at the end of the year, other than service contracts and in relation to directors' liability insurance.

Directors' Report

Director profiles

Kevin Stanley Beeston F.C.M.A. (36)
Finance Director
Kevin Beeston joined Serco in 1985 as a Financial Analyst. He held a number of financial positions before being appointed Finance Director of International Aeradio Limited upon its acquisition by Serco in 1992 and subsequently became Managing Director. From 1994 he held the position of Chief Executive of Serco International Limited and in 1996 he was appointed Finance Director of Serco Group plc.

Everton Bryan B.A. (Hons) A.C.A. (39)
Executive Director
Everton Bryan joined Serco in 1991 as Group Financial Controller and has since held a number of senior positions. He was Managing Director of Serco Limited, the Group's largest operating subsidiary from 1995 until January 1998 when he was appointed President of Serco North America which is based in New Jersey, USA. He was appointed Director of Serco Group plc in 1996.

George Gowans Gray B.Sc Ph.D C.Eng F.I.Mech.E (61)
Chairman
George Gray joined RCA Group in 1964 as a spacecraft systems engineer. He was appointed a Director of RCA Limited and Managing Director of its services contracting division in 1974 and has thus led the business during its principal growth years. He was appointed Chairman of Serco Group plc on completion of the management buy-out from RCA in 1987. He is also a Non-executive Director of Misys plc.

Rhidian Huw Brynmor Jones M.A. F.C.I.S. F.I.Mgt. (55)
Non-executive Director
Rhidian Jones is a partner at Nabarro Nathanson, Solicitors, specialising in corporate finance, and has practical experience of commerce and industry, having worked in management for ten years. He previously served as a Non-executive Director of the Company from 1987 until 1994, and was reappointed in 1996. He is also a Non-executive Director of the Britannia Building Society.

Gerrard Rodgers (50)
Executive Director
Gerry Rodgers joined RCA in 1970. He held the position of Chairman and Chief Executive of Serco Services Limited from April 1993 until November 1995 when he was appointed Managing Director of Serco Systems Limited. In 1997 he was appointed to the Board of Serco Group plc with responsibility for IT and Innovation.

Gary Leon Sturgess Llb (45)
Non-executive Director
Gary Sturgess was Cabinet Secretary and Director General of the Cabinet Office in the NSW State Government in Australia from 1988 until 1992. He is now the principal of Sturgess Australia, a business specialising in strategic policy advice to government and the private sector. He has served as a Non-executive Director of Serco Group plc since 1994.

Richard David White B.Sc (Hons) (49)
Chief Executive
Richard White joined RCA in 1970 and since that date has worked in both operational and marketing roles. He has been responsible, in particular, for developing the marketing philosophy and operational strategy of the business. He was appointed Director responsible for government services in 1984. He was appointed Managing Director of Serco Group plc on completion of the management buy-out from RCA in 1987, and was subsequently designated as Chief Executive.

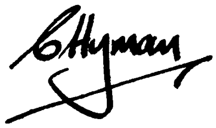
Iestyn Milton Williams B.A. (47)
Executive Director
Iestyn Williams joined RCA in 1978, working in the personnel function. He was appointed Director of Personnel in 1984 and Personnel Director of Serco Group plc on completion of the management buy-out from RCA in 1987. He was appointed President of Serco North America in 1996 and was based in New Jersey, USA. He returned to the United Kingdom in 1998 and is currently responsible for the Group's business in Europe and for developing new initiatives in Change Management and Contract Support.

Directors' Report

Auditors

Deloitte & Touche have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

Approved by the Board of Directors and signed on behalf of the Board:



Christopher R Hyman
Secretary

Dolphin House
Windmill Road
Sunbury-on-Thames
Middlesex TW16 7HT

3 March 1999

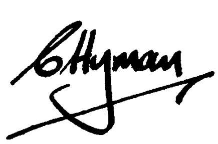
Directors' Responsibilities

Company Law requires the Directors to prepare Accounts and Notes for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and of the profit or loss of the Group for that period. In preparing those Accounts and Notes, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed; and
- prepare the Accounts and Notes on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the Accounts and Notes comply with the Companies Act 1985. They are also responsible for the Company's system of internal control and for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Approved by the Board of Directors and signed on behalf of the Board:



Christopher R Hyman
Secretary

Dolphin House
Windmill Road
Sunbury-on-Thames
Middlesex TW16 7HT

3 March 1999

Remuneration Report

The Remuneration Committee ("the Committee") advises the Board on all aspects of the Executive Directors' remuneration as well as their terms and conditions of employment.

Membership and Remit

The Committee is made up solely of the Non-executive Directors of the Company, its members being Gary Sturgess (Chairman) and Rhidian Jones.

The remit of the Committee is to define, on behalf of the Board, the remuneration policy for Executive Directors and to determine the specific remuneration, benefits and terms of employment of each Executive Director, including pension rights and compensation payments. It consults with the Group Chairman and Group Chief Executive and receives advice from external consultants specialising in executive remuneration. The Committee has written Terms of Reference and meets as required and in any event at least three times a year.

In determining the remuneration policy, the Committee has given full consideration to the provisions on Executive Directors' remuneration as set out in the Hampel Committee's Principles of Good Governance and Code of Best Practice. The Committee's Chairman attends the Annual General Meeting to respond to shareholders' questions on Executive Directors' remuneration.

Policy

It is the responsibility of the Board to attract, retain and motivate an executive team to deliver enhanced shareholder value for the Company on a consistent long term basis, by matching the remuneration strategy with the corporate strategy. To meet this aim, the Committee retains the help of external remuneration specialists. The Committee has considered the totality of the remuneration for Executive Directors and where necessary has adjusted individual elements to ensure that the needs of the Group, its shareholders and the individual Executive Directors are met. The diversity of the Group's activities, its market position and the rate of growth make it difficult to determine a clear group of comparator companies for bench-marking purposes. However, the Committee reviews levels of remuneration in listed companies of similar size, growth rate and international diversity, as well as current best practice for salary, benefits, pensions and incentive arrangements once every three years. The next review is currently in progress. In the intervening years, the Committee determines salary increases having regard to the average earnings index except for circumstances where the Committee deems another basis appropriate.

The Committee has agreed on the existing remuneration package which has the following components for all Executive Directors:

- a base salary;
- long term share incentives; and
- retirement and other benefits.

Annual bonuses are not normally awarded, but the Committee decided to award a bonus to one Director in recognition of outstanding performance.

Base salary and benefits

Annual remuneration of the Executive Directors, listed individually, is set out in Note 3 to the Accounts on page 26. Included within 'Benefits' for each Executive Director is a non-contributory private healthcare scheme. Each of the Executive Directors will continue to receive this benefit for a period of five years following retirement.

Long Term Incentives

The existing Serco Group plc 1998 Executive Option Plan ("the Plan") was approved by shareholders at the Annual General Meeting on 3 April 1998. The Plan was designed to align the interests of executives with those of the shareholders, as well as providing a competitive and market related package to attract, motivate and retain Executive Directors and other senior executives in the Group. In designing the Plan, the Group's culture, as well as changes in tax and accounting treatment of share option plans, were considered.

Remuneration Report

At the time the Plan was approved by the shareholders, the Company also established the Serco Group plc Employee Share Ownership Trust ("the Trust") for the purpose (amongst other things) of acquiring and holding shares in the Company to satisfy awards made under the Plan. The Trust may be financed by voluntary contributions or loans made from time to time by the Company and other Group companies or by a third party loan with a guarantee given by the Company or a Group Company. Shares may be acquired by the trustee either by purchase in the market or by subscription for new shares (at par or greater).

Under the Plan, market value options are granted to participants at the beginning of a three year award period. For each grant period, performance targets are set which have to be achieved before a participant may exercise an option.

The performance target for the current awards under the Plan is based on earnings per share ("EPS") growth over the award period. If annual EPS growth is less than 10% per annum over a three year performance period, no option can be exercised. If annual EPS growth is at least 15% per annum, an option can be exercised in full. If a growth rate of 10% is achieved, a participant becomes entitled to exercise 50% of the options granted. For EPS growth between 10% and 15%, the percentage of the option grant that can be exercised increases proportionately.

Since the implementation of the Plan on 3 April 1998, the participants in the Plan are no longer eligible to receive share options or awards under any other plan. Benefits under the Plan are not pensionable. Details of Directors' options granted under the Plan, and share options and awards granted under previous arrangements, have been disclosed in Note 3 to the Annual Accounts on pages 27 to 29.

Retirement and other benefits

The Executive Directors receive pensions and life assurance benefits consistent with those provided by other leading companies. The final salary scheme to which they belong is approved by the Inland Revenue and is described in Note 34 to the Annual Accounts. Associated benefits include a lump sum in the case of death in service and dependants' pensions.

One of the Executive Directors joined the Company after 1989 and is therefore subject to the Inland Revenue earnings cap which limits the amount of pensionable salary within an approved scheme. In the case of that Director, the Company provides appropriate benefits outside the scheme in relation to that part of his salary that exceeds the cap. Details of individual accrued pension benefits are set out in a table in Note 3 on page 30. Directors' accrued pension benefits have been disclosed in accordance with the requirements of The London Stock Exchange Listing Rules and the Companies Act.

The normal retirement age of the Executive Directors is sixty, although retirement is permissible from the age of fifty. In the event of early retirement, a pension is payable subject to the actuarial reductions determined in the scheme.

Service contracts

The Executive Directors' service contracts have a rolling notice period of two years. Copies are available for inspection prior to and during the Annual General Meeting. In view of the diversity of the Group's activities, its market position and rate of growth, the Committee considers a two year notice period to be reasonable and proper.

Remuneration Report

Non-executive Directors

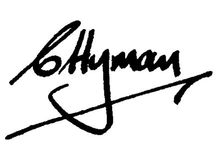
The Non-executive Directors of the Company have no personal financial interests in the matters determined by the Committee, no potential conflicts of interest arising from cross-directorships and no involvement in the day-to-day running of the Group.

Non-executive Directors are paid Directors' fees and reimbursed all necessary and reasonable expenses incurred in the performance of their duties. Non-executive Directors do not participate in the Company's share incentive or pension plans.

Non-executive Directors have a three year letter of engagement. Re-appointment is not automatic and Non-executive Directors are required to stand for re-election by shareholders on a rotating basis as set out in the Company's Articles of Association, but otherwise such appointments may be terminated upon three months written notice.

The Executive Directors determine the specific fees and terms of engagement of each Non-executive Director.

By order of the Board:



Christopher R Hyman
Secretary

Dolphin House
Windmill Road
Sunbury-on-Thames
Middlesex
TW16 7HT

3 March 1999

Auditors' Report

Auditors' report to the members of Serco Group plc

We have audited the financial statements on pages 14 to 57 which have been prepared under the accounting policies set out on pages 20 and 21.

Respective responsibilities of Directors and Auditors

The Directors are responsible for preparing the Annual Accounts as described on page 9 of the financial statements. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board, the Listing Rules of The London Stock Exchange, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding Directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We review whether the report on pages 2 to 4 reflects the compliance with those provisions of the Combined Code specified for our review by The London Stock Exchange, and we report if it does not. We are not required to form an opinion on the effectiveness of the Corporate Governance procedures or the Group's internal controls. We draw attention to the fact that the Directors' review of the system of internal controls has been undertaken before formal guidance has been issued as to the scope of such a review and the procedures to be undertaken and may not, therefore, constitute a review for the purposes of the Combined Code as ultimately interpreted.

We read the other information contained in the Annual Accounts, including the Corporate Governance report, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 1998 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche

Deloitte & Touche
Chartered Accountants and Registered Auditors

Hill House
1 Little New Street
London EC4A 3TR

3 March 1999

Explanatory Notes to the Consolidated Profit and Loss Account

Introduction
During 1998 there have been a number of new Financial Reporting Standards ("FRS") issued, which have resulted in significant changes to the presentation of the 1998 Consolidated Profit and Loss Account, the key aspects of which are noted below:-

Turnover
In accordance with FRS 9 - Associates and Joint Ventures, the Group's share of turnover from joint venture activities has been reported in addition to turnover from subsidiaries. The Group turnover of £574 million (1997 - £489 million) is stated excluding £113 million (1997 - £83 million) relating to the Group's share of joint ventures.

Goodwill amortisation
In accordance with FRS 10 - Goodwill and Intangible Assets, goodwill arising on acquisitions is to be amortised over 20 years. Goodwill amortised of £823,000, on acquisitions made in 1998, has been charged to profit. There was no comparable charge in 1997.

Share of operating profit and interest in joint ventures
Total profit earned from joint ventures is now disclosed gross, in accordance with FRS 9, by the addition of the "share of operating profit in joint ventures" and the "share of interest payable/receivable in joint ventures". "Share of interest payable in joint ventures" represents Serco's share of the interest payable by the joint venture on its debt. Such debt is largely the result of Private Finance Initiative ("PFI") activities and is non-recourse to Serco Group plc and the resulting interest charge is excluded from the definition of interest cover which prevails in the Group's banking covenants.

Group interest cover in 1998 was 14.7 times, excluding the effects of goodwill amortisation and net share of interest payable in joint ventures.

Realisation of PFI investment and reorganisation expenses
In accordance with FRS 3 - Reporting Financial Performance, the following items have been highlighted:-

Realisation of PFI investment
The sale of the Group's equity holding in FBS Limited, a Special Purpose Company established to procure helicopters for the Defence Helicopter Flying School, realised a profit of £4.6 million in the year.

Reorganisation expenses
The reorganisation expenses of £4.4 million relate to redundancy and dispersal costs, and costs of non-renewal of certain contracts resulting from significant restructuring of the Group's business.

Consolidated Profit and Loss Account

For the year ended 31 December 1998

	Note	1998 £'000	Restated 1997 £'000
Turnover: Group and share of joint ventures - continuing operations	2	**687,760**	571,636
Less: share of joint ventures	2	**(113,471)**	(82,618)
Group turnover	2	**574,289**	489,018
Cost of sales		**(499,052)**	(426,424)
Gross profit		**75,237**	62,594
Administrative expenses		**(51,865)**	(44,515)
Amortisation of goodwill		**(823)**	–
Other administrative expenses		**(51,042)**	(44,515)
Operating profit - continuing operations		**23,372**	18,079
Share of operating profit in joint ventures		**6,315**	6,556
Realisation of PFI investment		**4,602**	–
Reorganisation expenses		**(4,440)**	–
Interest receivable	4	**2,840**	982
Group		**2,764**	832
Share of joint ventures		**76**	150
Interest payable and similar charges	5	**(7,070)**	(3,605)
Group		**(4,852)**	(2,780)
Share of joint ventures		**(2,218)**	(825)
Profit on ordinary activities before taxation	6	**25,619**	22,012
Taxation on profit on ordinary activities	7	**(8,199)**	(7,479)
Profit on ordinary activities after taxation		**17,420**	14,533
Dividends	8	**(4,888)**	(3,910)
Retained profit for the financial year	24	**12,532**	10,623
Earnings per Ordinary Share of 2p each:	9		
Basic earnings per share, after amortisation of goodwill		**27.4p**	23.9p
Basic earnings per share, before amortisation of goodwill		**28.7p**	23.9p
Fully diluted earnings per share, after amortisation of goodwill		**27.0p**	23.7p
Fully diluted earnings per share, before amortisation of goodwill		**28.3p**	23.7p

Consolidated Balance Sheet At 31 December 1998

	Note	1998 £'000	Restated 1997 £'000
Fixed assets			
Intangible asset: Goodwill	10	**23,332**	–
Tangible assets	11	**23,962**	28,994
Investments in joint ventures	12	**10,617**	8,813
Share of gross assets		**128,524**	78,262
Share of gross liabilities		**(117,907)**	(69,449)
		57,911	37,807
Current assets			
Stocks	*13*	**9,127**	8,099
Debtors: Amounts due within one year	*14*	**119,757**	114,379
Debtors: Amounts due after more than one year	*14*	**37,608**	22,135
Cash at bank and in hand		**53,474**	19,618
		219,966	164,231
Creditors: Amounts falling due within one year			
Bank loans and overdrafts		**9,483**	2,009
Trade creditors		**48,768**	42,708
Other creditors including taxation and social security	*15*	**33,334**	29,093
Accruals and deferred income		**58,137**	45,113
Proposed dividend	*8*	**3,279**	2,693
		153,001	121,616
Net current assets		**66,965**	42,615
Total assets less current liabilities		**124,876**	80,422
Creditors: Amounts falling due after more than one year	*16*	**48,957**	49,020
Provisions for liabilities and charges	*17*	**3,726**	4,722
		72,193	26,680
Capital and reserves			
Called up share capital	*20*	**1,285**	1,224
Share premium account	*21*	**57,195**	23,977
Capital redemption reserve		**143**	143
Other reserve – shares to be issued	*22*	**3,078**	3,078
Profit and loss account	*24*	**10,492**	(1,742)
Equity shareholders' funds	*19*	**72,193**	26,680

These Accounts and Notes were approved by the Board of Directors on 3 March 1999 and signed on behalf of the Board:

G G Gray *Chairman* **K S Beeston** *Finance Director*

Balance Sheet At 31 December 1998

	Note	1998 £'000	1997 £'000
Fixed assets			
Tangible assets	*11*	**479**	246
Investments	*12*	**27,664**	34,153
		28,143	34,399
Current assets			
Amounts owed by subsidiary companies due within one year		**17,518**	17,882
Amounts owed by subsidiary companies due after more than one year		**45,160**	10,431
Debtors	*14*	**6,588**	2,097
Cash at bank and in hand		**43,219**	32,018
		112,485	62,428
Creditors: Amounts falling due within one year			
Trade creditors		**418**	427
Other creditors including taxation and social security	*15*	**4,152**	1,746
Accruals and deferred income		**7,259**	4,771
Proposed dividend	*8*	**3,279**	2,693
		15,108	9,637
Net current assets		**97,377**	52,791
Total assets less current liabilities		**125,520**	87,190
Creditors: Amounts falling due after more than one year	*16*	**41,430**	41,449
		84,090	45,741
Capital and reserves			
Called up share capital	*20*	**1,285**	1,224
Share premium account	*21*	**57,195**	23,977
Capital redemption reserve		**143**	143
Other reserve – shares to be issued	*22*	**3,078**	3,078
Profit and loss account	*24*	**22,389**	17,319
Equity shareholders' funds		**84,090**	45,741

These Accounts and Notes were approved by the Board of Directors on 3 March 1999 and signed on behalf of the Board:

G G Gray *Chairman* **K S Beeston** *Finance Director*

Consolidated Cash Flow Statement For the year ended 31 December 1998

	Note	1998 £'000	Restated 1997 £'000
Net cash inflow from operating activities	25	**30,032**	6,229
Dividends received from joint ventures		**1,023**	1,210
Returns on investment and servicing of finance			
Interest received		**2,764**	832
Interest paid		**(4,852)**	(2,780)
Net cash outflow from returns on investments and servicing of finance		**(2,088)**	(1,948)
Taxation			
UK corporation tax paid		**(3,258)**	(3,499)
Overseas tax paid		**(1,146)**	(910)
Tax paid		**(4,404)**	(4,409)
Capital expenditure and financial investment			
Purchase of tangible fixed assets		**(8,379)**	(6,807)
Sale of tangible fixed assets		**7,902**	1,478
Long term loans made to joint ventures	33	**(7,786)**	(8,067)
Net short term cashflows with joint ventures		**3,374**	3,861
Reorganisation costs		**(4,440)**	–
Net cash outflow from capital expenditure and financial investment		**(9,329)**	(9,535)
Acquisitions and disposals			
Purchase of subsidiary undertakings	29	**(20,138)**	(10,247)
Net cash acquired with subsidiary undertakings	30	**1,853**	2,311
Subscription for shares in joint ventures	12	**(922)**	(2,242)
Purchase of businesses		**–**	(116)
Proceeds from disposal of PFI investment	12	**3,350**	–
Net cash outflow from acquisitions and disposals		**(15,857)**	(10,294)
Equity dividends paid			
Dividends paid		**(4,302)**	(3,527)
Net cash outflow from equity dividends paid		**(4,302)**	(3,527)
Net cash outflow before financing		**(4,925)**	(22,274)
Financing			
Issue of Ordinary Share Capital		**33,279**	137
Debt due within one year:			
Increase in other loans		**19**	6
Debt due beyond one year:			
Increase in bank loans		**–**	37,746
Increase in other loans		**113**	1,077
Capital element of finance lease repayments		**(2,104)**	(2,731)
Net cash inflow from financing		**31,307**	36,235
Increase in cash		**26,382**	13,961
Balance at 1 January		**17,609**	3,648
Balance at 31 December		**43,991**	17,609

Consolidated Statement of Recognised Gains and Losses
For the year ended 31 December 1998

	1998 £'000	1997 £'000
Profit on ordinary activities after taxation	**17,420**	14,533
Currency translation differences on foreign currency net investments	**(298)**	(2,486)
Total recognised gains and losses relating to the year	**17,122**	12,047

Notes to the Accounts For the year ended 31 December 1998

1. *Accounting policies*

These Accounts have been prepared in accordance with applicable accounting standards. The particular accounting policies adopted are described below:

Accounting convention

These Accounts have been prepared under the historical cost convention.

Basis of consolidation

The Group Accounts consolidate the Accounts of the Company, its subsidiaries and joint ventures made up to 31 December of each year, for the periods they are owned by Serco Group plc.

Depreciation

Depreciation is provided on a straight-line basis at rates which, in the opinion of the Directors, reduce the assets to their residual value over their estimated useful lives.

The principal annual rates used are:

Freehold buildings	2.5%
Short leasehold building improvements	The higher of 10% or rate produced by lease term
Machinery	15% – 20%
Motor vehicles	18% – 50%
Furniture	10%
Office machines	20% – 33%
Leased equipment	The higher of the rate produced by either lease term or useful life

Stocks

Stocks are stated at the lower of cost and net realisable value. Cost includes an appropriate proportion of direct material and labour.

Long term contracts

Long term contract balances represent costs incurred on specific contracts, net of amounts transferred to cost of sales in respect of work recorded as turnover by reference to the value of the work carried out to date. No profit is recognised until the contract has advanced to a stage where the total profit can be assessed with reasonable certainty. Advance payments are included in creditors to the extent that they exceed the related work in progress.

Deferred taxation

Deferred taxation is provided at the anticipated tax rates on timing differences arising from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the accounts, to the extent that it is probable that a liability or asset will crystallise in the future.

Notes to the Accounts For the year ended 31 December 1998

Fixed asset investments: Subsidiaries
Investments held as fixed assets are stated at cost less provision for any permanent diminution in value.

Fixed asset investments: Joint Ventures
In the consolidated accounts, investments in joint ventures are accounted for using the gross equity method of accounting in accordance with Financial Reporting Standard 9 ("FRS 9") - Associates and Joint Ventures. All of the Group's associated undertakings have been reclassified as joint ventures as defined by FRS 9. To assist in the understanding of the accounts, the appropriate comparative balances have been restated in accordance with FRS 9.

The Group consolidated Profit and Loss Account includes the Group's share of joint ventures' operating profits and interest, and the attributable taxation. In the consolidated Balance Sheet, the investments in the joint ventures are shown as the Group's share of the net assets of the joint ventures. The share of net assets is split between gross assets and liabilities.

Goodwill
Goodwill arising on acquisitions during 1998 has been capitalised in the balance sheet in accordance with Financial Reporting Standard 10 ("FRS 10") - Goodwill and Intangible Assets. Amortisation of goodwill is provided on a straight line basis over a period of 20 years, which, in the opinion of the Directors is a period not exceeding the economic useful life of the asset.

Goodwill eliminated against reserves in prior periods and shown as a separate goodwill write off reserve has been reclassified to the profit and loss account reserve in the current year in accordance with FRS 10.

Basis of translation of foreign currencies
Transactions of UK companies denominated in foreign currencies are translated into Sterling at the rate ruling at the date of the transaction. Amounts receivable and payable in foreign currencies at the balance sheet date are translated at the rates ruling at that date and any differences arising are taken to the profit and loss account.

The Accounts of overseas subsidiary companies and associated undertakings are translated into Sterling at the closing rates of exchange at the balance sheet date and the difference arising from the translation of the opening net investment and matched long term foreign currency borrowings is taken directly to reserves. The profit and loss account is translated using average exchange rates.

Pension costs: Defined benefit schemes
Retirement benefits to employees of Group companies are funded by contributions from Group companies and employees. Payments are made to trust funds which are financially separate from the Group in accordance with periodic calculations by consulting actuaries. The expected cost to the Group of providing defined benefit pensions is charged to the profit and loss account so as to spread the cost of pensions over the service lives of employees in the schemes, in such a way that the cost is a substantially level percentage of payroll cost, with experience surpluses and deficits being amortised on a straight line basis.

Turnover
Turnover represents net sales of goods and services sold to third parties.

Leases
Assets obtained under finance leases are capitalised at their fair value on acquisition and depreciated over the shorter of their estimated useful lives or lease term. The finance charges are allocated over the period of the lease in proportion to the capital element outstanding. Rentals on assets under operating leases are charged to the profit and loss account in equal annual amounts.

Contract termination provisions
Contract termination provisions are recognised for those employees where there is a statutory or contractual obligation.

Notes to the Accounts For the year ended 31 December 1998

2. Segmental Report

Classes of Business

1998	Facilities Management £'000	Systems Engineering £'000	Total £'000
Turnover			
Total sales – Group and share of joint ventures	619,055	68,705	687,760
Less: share of joint ventures	(113,471)	–	(113,471)
Group turnover – sales to third parties	505,584	68,705	574,289
Profit before taxation			
Segment profit	30,175	5,819	35,994
Segment profit before common costs, joint ventures, goodwill, exceptional items, interest and taxation	30,175	5,819	35,994
Common costs			(11,799)
Amortisation of goodwill			(823)
Operating profit			23,372
Share of operating profit of joint ventures	6,315	–	6,315
Realisation of PFI investment			4,602
Reorganisation expenses			(4,440)
Net interest – Group			(2,088)
– share of joint ventures			(2,142)
Group profit before taxation			25,619
Net assets			
Segment net assets	43,349	5,896	49,245
Group share of the net assets of joint ventures	10,617	–	10,617
Net assets before unallocated assets	53,966	5,896	59,862
Unallocated assets			12,331
Total net assets			72,193

Notes to the Accounts For the year ended 31 December 1998

Classes of Business

1997 restated	Facilities Management £'000	Systems Engineering £'000	Total £'000
Turnover			
Total sales – Group and share of joint ventures	500,569	71,067	571,636
Less: share of joint ventures	(82,618)	–	(82,618)
Group turnover – sales to third parties	417,951	71,067	489,018
Profit before taxation			
Segment profit	23,700	6,053	29,753
Segment profit before common costs, joint ventures, interest and taxation	23,700	6,053	29,753
Common costs			(11,674)
Operating profit			18,079
Share of operating profit of joint ventures	6,556	–	6,556
Net interest – Group			(1,948)
– share of joint ventures			(675)
Group profit before taxation			22,012
Net assets			
Segment net assets	4,892	4,785	9,677
Group share of the net assets of joint ventures	8,813	–	8,813
Net assets before unallocated assets	13,705	4,785	18,490
Unallocated assets			8,190
Total net assets			26,680

Notes to the Accounts For the year ended 31 December 1998

2. Segmental Report (continued)

Geographical Segments

1998	United Kingdom £'000	Rest of Europe £'000	Asia Pacific £'000	Other £'000	Total £'000
Turnover					
Turnover by destination:					
Total sales – Group and share of joint ventures	442,857	45,960	126,921	72,022	687,760
Less: share of joint ventures	(53,678)	(3,301)	(36,241)	(20,251)	(113,471)
Group turnover – sales to third parties	389,179	42,659	90,680	51,771	574,289
Turnover by origin:					
Total sales – Group and share of joint ventures	448,906	42,711	125,809	70,334	687,760
Less: share of joint ventures	(53,678)	(3,301)	(36,241)	(20,251)	(113,471)
Group turnover – sales to third parties	395,228	39,410	89,568	50,083	574,289
Profit before taxation					
Segment profit	19,106	4,975	7,800	4,113	35,994
Segment profit before common costs, joint ventures, goodwill, exceptional items, interest and taxation	19,106	4,975	7,800	4,113	35,994
Common costs					(11,799)
Amortisation of goodwill					(823)
Operating profit					23,372
Share of operating profit/(loss) of joint ventures	7,459	(105)	(2,104)	1,065	6,315
Realisation of PFI investment					4,602
Reorganisation expenses					(4,440)
Net interest – Group					(2,088)
– share of joint ventures					(2,142)
Group profit before taxation					25,619
Net assets					
Segment net assets	28,664	3,506	14,645	2,430	49,245
Group share of the net assets of joint ventures	7,807	4	(38)	2,844	10,617
Net assets before unallocated assets	36,471	3,510	14,607	5,274	59,862
Unallocated assets					12,331
Total net assets					72,193

Notes to the Accounts For the year ended 31 December 1998

Geographical Segments **1997 restated**	**United Kingdom £'000**	**Rest of Europe £'000**	**Asia Pacific £'000**	**Other £'000**	**Total £'000**
Turnover					
Turnover by destination:					
Total sales – Group and share of joint ventures	375,424	28,097	117,640	50,475	571,636
Less: share of joint ventures	(26,479)	(3,023)	(34,596)	(18,520)	(82,618)
Group turnover – sales to third parties	348,945	25,074	83,044	31,955	489,018
Turnover by origin:					
Total sales – Group and share of joint ventures	371,593	27,840	123,571	48,632	571,636
Less: share of joint ventures	(26,479)	(3,023)	(34,596)	(18,520)	(82,618)
Group turnover – sales to third parties	345,114	24,817	88,975	30,112	489,018
Profit before taxation					
Segment profit	17,073	4,270	4,350	4,060	29,753
Segment profit before common costs, joint ventures, interest and taxation	17,073	4,270	4,350	4,060	29,753
Common costs					(11,674)
Operating profit					18,079
Share of operating profit of joint ventures	4,317	98	1,774	367	6,556
Net interest – Group					(1,948)
– share of joint ventures					(675)
Group profit before taxation					22,012
Net assets					
Segment net assets	7,707	2,075	(615)	510	9,677
Group share of the net assets of joint ventures	3,673	347	2,843	1,950	8,813
Net assets before unallocated assets	11,380	2,422	2,228	2,460	18,490
Unallocated assets					8,190
Total net assets					26,680

Notes to the Accounts For the year ended 31 December 1998

3. Information regarding Directors & employees

	1998 £'000	1997 £'000
a) Directors' remuneration:		
Fees as Directors	**79**	58
Other emoluments	**1,307**	1,073
Total remuneration excluding pensions	**1,386**	1,131

"Other emoluments" in 1997 has been adjusted to exclude the basic salary and benefits of D Perkins, who retired in October 1997 (total £82,000).

The total of the remuneration of Directors is made up of the following:

	Salary £	Fees £	Benefits £	Total Remuneration excluding pensions 1998 £	Total Remuneration excluding pensions 1997 £
K S Beeston	**215,300**	–	**1,429**	**216,729**	176,710
E Bryan	**247,999**	–	**3,974**	**251,973**	175,698
G G Gray (Chairman)	**141,438**	–	**1,367**	**142,805**	154,096
R H B Jones	–	**36,000**	–	**36,000**	25,000
G Rodgers	**185,300**	–	**1,147**	**186,447**	18,563
G L Sturgess	–	**43,353**	–	**43,353**	32,899
R D White	**298,500**	–	**1,319**	**299,819**	288,218
I M Williams	**207,867**	–	**1,351**	**209,218**	260,066
Total	**1,296,404**	**79,353**	**10,587**	**1,386,344**	1,131,250

Included in the salary of K Beeston is a bonus of £30,000 which was paid in May 1998.
E Bryan replaced I Williams as President of Serco North America from January 1998, and each Director's remuneration for 1998 and 1997 respectively included a relocation allowance.

Notes to the Accounts For the year ended 31 December 1998

b) The Directors' interests, as defined by the Companies Act 1985, in the shares of Serco Group plc (including the percentages held of the issued share capital of the Company) were as follows:

	Ordinary shares of 2p each fully paid			
	1 January 1998		**31 December 1998**	
	Shares	%	**Shares**	**%**
K S Beeston	10,130	0.02%	**10,130**	**0.02%**
E Bryan	–	–	**–**	**–**
G G Gray	524,908	0.86%	**424,908**	**0.66%**
R H B Jones	7,750	0.01%	**7,750**	**0.01%**
G Rodgers	10,000	0.02%	**12,500**	**0.02%**
G L Sturgess	–	–	**–**	**–**
R D White	539,682	0.88%	**369,502**	**0.57%**
I M Williams	626,945	1.02%	**476,945**	**0.74%**

The above shareholdings include the Directors' personal holdings, as well as those of their spouses and trusts of which a Director and his family are beneficiaries or potential beneficiaries.
There were no non-beneficial interests.
There has been no change in these interests since the end of the financial year.

c) Senior Staff Share Option Scheme

The following options over the Ordinary Share Capital of the Company granted under the Senior Staff Share Option Scheme were outstanding at 1 January 1998 and 31 December 1998:

	Balance at 1/1/98 and 31/12/98	Date from which exercisable	Expiry date	Exercise price £
K S Beeston	–	–	–	–
E Bryan	**10,000**	16/10/1998	16/10/2005	3.69
G G Gray	–	–	–	–
R H B Jones	–	–	–	–
G Rodgers	–	–	–	–
G L Sturgess	–	–	–	–
R D White	–	–	–	–
I M Williams	–	–	–	–

No share options under this scheme were granted or exercised during the year or since the end of the financial year.

The share price at 31 December 1998 was £11.51½ and ranged from £7.82 to £14.47 during the year.

Notes to the Accounts For the year ended 31 December 1998

3. Information regarding Directors & employees (continued)

d) Serco Group plc 1996 Long Term Incentive Scheme

The following options over the Ordinary Share Capital of the Company granted under the Serco Group plc 1996 Long Term Incentive Scheme were outstanding at 1 January 1998 and 31 December 1998:

		Numbers of options at 1 January 1998 & 31 December 1998	Exercise price	End of performance period	Date of expiry of option
K S Beeston	3 year Award	19,701	Nil	01/01/1999	01/01/2003
	Additional Award	9,851	Nil	01/01/1999	01/01/2003
	3 year Award	12,240	Nil	01/01/2000	01/01/2004
	Additional Award	6,120	Nil	01/01/1999	01/01/2004
E Bryan	3 year Award	19,701	Nil	01/01/1999	01/01/2003
	Additional Award	9,851	Nil	01/01/1999	01/01/2003
	3 year Award	12,240	Nil	01/01/2000	01/01/2004
	Additional Award	6,120	Nil	01/01/1999	01/01/2004
G G Gray	Additional Award	14,096	Nil	01/01/1999	01/01/2003
R H B Jones		–	–	–	–
G Rodgers	3 year Award*	19,701	Nil	01/01/1999	01/01/2003
	Additional Award*	9,851	Nil	01/01/1999	01/01/2003
	3 year Award	12,240	Nil	01/01/2000	01/01/2004
	Additional Award	6,120	Nil	01/01/1999	01/01/2004
G L Sturgess		–	–	–	–
R D White	3 year Award	31,114	Nil	01/01/1999	01/01/2003
	Additional Award	15,557	Nil	01/01/1999	01/01/2003
	3 year Award	20,772	Nil	01/01/2000	01/01/2004
	Additional Award	10,386	Nil	01/01/1999	01/01/2004
I M Williams	3 year Award	26,155	Nil	01/01/1999	01/01/2003
	Additional Award	13,077	Nil	01/01/1999	01/01/2003
	3 year Award	14,466	Nil	01/01/2000	01/01/2004
	Additional Award	7,233	Nil	01/01/1999	01/01/2004

No options were granted or exercised during the year or since the end of the financial year.

The options granted set out above have been made in accordance with the rules of the scheme. The performance period and, in the case of additional awards the further restricted period, expire at the dates shown above, but any vesting of awards is conditional upon the performance criteria of the scheme being met.

The performance target is based on earnings per share ("EPS") growth over the award period. The EPS growth has to be at least 35% over the three years before any shares are allotted. If a growth rate of 35% over the three years is achieved, a participant becomes entitled to 35% of his annualised salary to be paid out in shares. If EPS growth exceeds 35% the entitlement is equivalent to the percentage growth in EPS as a percentage of salary, but is capped at 50%.

Options may not be exercised until the Remuneration Committee has determined the extent to which an award has vested (which may not in any case occur until after the auditors have signed the Annual Accounts following the end of the performance period).

* Contractual commitments were made to G Rodgers in 1996, that he would receive benefits similar to those under the Serco Group plc 1996 Long Term Incentive Scheme. In recognition of that commitment, the Remuneration Committee intends to grant these awards on 3 March 1999.

Notes to the Accounts For the year ended 31 December 1998

e) Serco Group plc 1998 Executive Option Plan

During the period, options over the Ordinary Share Capital of the Company were granted under the Serco Group plc 1998 Executive Option Plan to the following Directors:

		Number of options at 1 January 1998	Options granted during period	Numbers of options at 31 December 1998	Exercise price £	Date from which exercisable	Date of expiry of option
K S Beeston	Approved	–	2,298	2,298	13.05	21/05/2001	20/05/2008
	Unapproved	–	11,487	11,487	13.05	21/05/2001	20/05/2005
E Bryan	Approved	–	2,298	2,298	13.05	21/05/2001	20/05/2008
	Unapproved	–	11,487	11,487	13.05	21/05/2001	20/05/2005
G G Gray		–	–	–	–	–	–
R H B Jones		–	–	–	–	–	–
G Rodgers	Approved	–	2,298	2,298	13.05	21/05/2001	20/05/2008
	Unapproved	–	11,487	11,487	13.05	21/05/2001	20/05/2005
G L Sturgess		–	–	–	–	–	–
R D White	Approved	–	2,298	2,298	13.05	21/05/2001	20/05/2008
	Unapproved	–	19,908	19,908	13.05	21/05/2001	20/05/2005
I M Williams	Approved	–	2,298	2,298	13.05	21/05/2001	20/05/2008
	Unapproved	–	13,165	13,165	13.05	21/05/2001	20/05/2005

No options were exercised during the year or since the end of the financial year.

The awards set out above have been made in accordance with the rules of the Serco Group plc 1998 Executive Option Plan and accordingly, the exercise of options is conditional upon the performance criteria of the plan being met. Details of the performance criteria in respect of the above awards are set out in the Remuneration Report on page 11.

Notes to the Accounts For the year ended 31 December 1998

3. Information regarding Directors & employees (continued)

f) Accrued pension benefits

	Increase in pension during the year (ii)	Transfer value of increase (iii)	Total accrued pension at year end (i)
K S Beeston	£10,831	£54,358	£42,472 p.a.
E Bryan	£2,070	£9,921	£16,745 p.a.
G G Gray	Nil	Nil	£140,967 p.a.
G Rodgers	£16,581	£177,980	£68,352 p.a.
R D White	£13,458	£131,591	£119,312 p.a.
I M Williams	£3,726	£27,083	£94,719 p.a.

E Bryan received additional benefit from a supplementary arrangement whereby the Company contributes 15% of that remuneration in excess of the Permitted Maximum under the Inland Revenue approved pension scheme into a Funded Unapproved Retirement Benefit Scheme.

Notes to pension benefits:

(i) The total accrued pension shown is that which would be paid annually on retirement, based on service to the end of the year.

(ii) The increase in accrued pension during the year excludes any increase for inflation.

(iii) The transfer value of the increase in accrued pension has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11, less Directors' contributions.

(iv) Members have the option to pay Additional Voluntary Contributions; neither the contributions nor the resulting benefits are included in the above table.

(v) Transfer values disclosed do not represent the sum paid or payable to the individual Director. Instead, they represent a potential liability of the pension scheme.

g) Directors' interests in contracts and other transactions with Group companies:
None of the Directors have a material interest in any contract with Group companies other than service contracts and in relation to Directors' liability insurance.

h) Employee costs

	1998 £'000	1997 £'000
Employee costs including Directors:		
Wages and salaries	**288,067**	244,791
Social security costs	**22,076**	16,883
Other pension costs (Note 34)	**14,875**	9,058
Long Term Incentive Scheme costs	**1,050**	700
	326,068	271,432

i) Number of persons employed by Serco Group plc and its subsidiaries

	1998 Number	1997 Number
Average number of persons employed in the provision of services:		
Facilities Management	**16,360**	14,723
Systems Engineering	**1,153**	1,189
Non-specific	**97**	87
	17,610	15,999

Notes to the Accounts For the year ended 31 December 1998

4. Interest receivable

	1998 £'000	1997 £'000
Group		
Short term deposits	**2,141**	178
Loans to joint ventures	**623**	654
Total Group	**2,764**	832
Share of joint ventures interest	**76**	150
	2,840	982

5. Interest payable and similar charges

	1998 £'000	1997 £'000
On liabilities repayable within five years:		
Group bank loans and overdrafts	**1,820**	2,610
Share of joint ventures interest	**194**	–
	2,014	2,610
On liabilities repayable after five years:		
Group bank loans and overdrafts	**3,032**	170
Share of joint ventures interest	**2,024**	825
	5,056	995
	7,070	3,605

6. Profit on ordinary activities before taxation

	1998 £'000	1997 £'000
Profit on ordinary activities before taxation is after charging:		
Rentals under operating leases:		
Land and buildings	**6,436**	4,909
Plant and machinery	**16,317**	15,824
Depreciation on tangible assets:		
Owned	**6,257**	5,257
Held under finance leases	**1,839**	1,782
Finance lease interest on operational assets	**428**	425
Amortisation of goodwill	**823**	–
Auditors' remuneration:		
Deloitte & Touche	**411**	436
Other auditors	**24**	88
Other fees paid to auditors	**742**	537

Notes to the Accounts For the year ended 31 December 1998

7. Taxation on profit on ordinary activities

	1998 £'000	1997 £'000
The taxation charge on the results of the year is made up as follows:		
United Kingdom corporation taxation at 31%		
(1997 – 33% to 31 March 1997 and 31% from 1 April 1997 onwards) based on the profit for the year	**2,796**	3,207
Overseas taxation	**1,840**	923
Deferred taxation	**1,429**	1,079
Adjustment in respect of prior years:		
United Kingdom corporation taxation	**(1,015)**	(89)
Overseas taxation	**91**	(286)
Deferred taxation	**26**	(130)
Share of joint ventures taxation charge	**3,032**	2,775
	8,199	7,479

The effective tax charge for the year is higher than the United Kingdom corporation tax rate principally as a result of higher rates of overseas taxation, losses accruing overseas that are not available for relief and disallowed expenditure.

The above 1998 tax charge includes the following amounts attributable to exceptional items:

	1998 £'000	1997 £'000
Realisation of PFI investment	**(791)**	–
Reorganisation expenses	**1,376**	–
	585	–

8. Dividends

	1998 £'000	1997 £'000
Interim dividend of 2.3p per share on 64,238,968 Ordinary Shares (1997 – 2.0p on 60,849,335 Ordinary Shares) of 2p each fully paid – paid 16 October 1998	**1,477**	1,217
Proposed final dividend of 5.1p per share on 64,291,629 Ordinary Shares (1997 – 4.4 p on 61,200,513 Ordinary Shares) of 2p each fully paid – proposed payment in April 1999	**3,279**	2,693
	4,756	3,910
1997 final dividend of 4.4p on 3,000,000 shares relating to March 1998 share placement	**132**	–
	4,888	3,910

Notes to the Accounts For the year ended 31 December 1998

9. Earnings per Ordinary Share

1998 fully diluted earnings per Ordinary Share after goodwill has been calculated in accordance with Financial Reporting Standard 14 ("FRS 14") – Earnings per share and 1997 fully diluted earnings per Ordinary Share has been restated for the effects of FRS 14.

Earnings per share is shown both before and after goodwill to assist in the understanding of the impact of FRS 14 on the Group Accounts.

The calculation of basic earnings per Ordinary Share after goodwill is based on profits of £17,420,000 for the year ended 31 December 1998 (1997 – £14,533,000) and the weighted average number of 63,662,797 (1997 – 60,839,106) Ordinary Shares of 2p each in issue during the year.

The calculation of basic earnings per Ordinary Share before goodwill is based on profits of £18,243,000 (adjusted for the effect of goodwill amortisation of £823,000) for the year ended 31 December 1998 (1997 - £14,533,000) and the weighted average number of 63,662,797 (1997 - 60,839,106) Ordinary Shares of 2p each in issue during the year.

The calculation of fully diluted earnings per Ordinary Share after goodwill is based on adjusted profits for the year of £17,420,000 (1997 – £14,533,000 restated) and the weighted average number of 64,474,738 (1997 – 61,430,804 restated) Ordinary Shares of 2p each assuming that the options are all exercised.

The calculation of fully diluted earnings per Ordinary Share before goodwill is based on adjusted profits of £18,243,000 (adjusted for the effect of goodwill amortisation of £823,000) for the year ended 31 December 1998 (1997 - £14,533,000 restated) and the weighted average number of 64,474,738 (1997 - 61,430,804 restated) Ordinary Shares of 2p each assuming that the options are all exercised.

10. Intangible asset: Goodwill

	Group £'000
Balance at 1 January 1998	–
Goodwill capitalised on acquisitions in 1998 (see Notes 12 and 29)	24,155
Amortisation during the year	(823)
Balance at 31 December 1998	**23,332**

Notes to the Accounts For the year ended 31 December 1998

11. Tangible assets

The cost of assets held by the Group under finance leases at 31 December 1998 was £10,503,000 (1997 – £9,034,000). The accumulated depreciation provided for those assets at 31 December 1998 was £4,788,000 (1997 – £3,813,000).

Group	Freehold Land & Buildings £'000	Short Leasehold Building Improvements £'000	Machinery, Motor Vehicles, Furniture & Equipment £'000	Total £'000
Cost:				
At 1 January 1998	10,237	2,429	43,506	56,172
Subsidiaries acquired	183	333	2,604	3,120
Reclassifications	655	391	(1,046)	–
Capital expenditure	449	1,322	8,493	10,264
Disposals	(7,319)	(362)	(4,302)	(11,983)
Foreign exchange differences	(4)	(51)	(565)	(620)
At 31 December 1998	**4,201**	**4,062**	**48,690**	**56,953**
Accumulated depreciation:				
At 1 January 1998	398	917	25,863	27,178
Subsidiaries acquired	36	261	1,354	1,651
Reclassifications	(13)	108	(95)	–
Provided during the year	153	523	7,420	8,096
Disposals	(116)	(293)	(3,326)	(3,735)
Foreign exchange differences	–	(6)	(193)	(199)
At 31 December 1998	**458**	**1,510**	**31,023**	**32,991**
Net book value:				
At 31 December 1998	**3,743**	**2,552**	**17,667**	**23,962**
At 31 December 1997	9,839	1,512	17,643	28,994

Notes to the Accounts For the year ended 31 December 1998

Company	Short Leasehold Building Improvements £'000	Machinery, Motor Vehicles, Furniture & Equipment £'000	Total £'000
Cost:			
At 1 January 1998	96	437	533
Transfers from subsidiary undertakings	–	669	669
Reclassifications	(49)	49	–
Capital expenditure	142	138	280
At 31 December 1998	**189**	**1,293**	**1,482**
Accumulated depreciation:			
At 1 January 1998	44	243	287
Transfers from subsidiary undertakings	–	442	442
Provided during the year	26	248	274
At 31 December 1998	**70**	**933**	**1,003**
Net book value:			
At 31 December 1998	**119**	**360**	**479**
At 31 December 1997	52	194	246

Notes to the Accounts For the year ended 31 December 1998

12. Investments held as fixed assets

	Company £'000
a) Shares in subsidiary companies at cost:	
At 1 January 1998	34,153
Transfer of shares in Docklands Railway Management Limited to Serco Limited	(6,489)
At 31 December 1998	**27,664**

b) Group investments in joint ventures and other undertakings:

	Group £'000
At 1 January 1998	8,813
Dividends received	(1,023)
Acquisitions/disposals	1,984
Foreign exchange translation difference	(298)
Retained profits	1,141
At 31 December 1998	**10,617**

c) A list of the principal undertakings of Serco Group plc is shown in Note 35. All the subsidiaries of the Group have been consolidated.

d) At 31 December 1998, Group companies had branches in Abu Dhabi, Bahrain, Chile, Dubai, Luxembourg, the Philippines, Ras Al Khaimah, Sharjah and Spain.

e) All the subsidiaries of Serco Group plc (including the branches) and the associated undertakings are engaged in the provision of services.

	1998 £'000	1997 £'000
f) The aggregate of the Group's share in the assets and liabilities of joint ventures is:		
Share of fixed assets	**47,035**	49,888
Share of current assets	**81,489**	28,374
	128,524	78,262
Share of liabilities due within one year or less	**32,892**	19,356
Share of liabilities due after more than one year	**85,015**	50,093
	117,907	69,449
Share of net assets	**10,617**	8,813

Notes to the Accounts For the year ended 31 December 1998

g) Acquisitions:
(i) JL Associates, Inc. ("JLA")

All the issued share capital of JLA was acquired by Serco Group Inc. on 29 May 1998 for a cash consideration of £6,762,000 with an additional consideration of £751,333 being held in escrow until 24 April 1999 which is contingent upon the agreement of prior year tax liabilities. This acquisition has been accounted for by the acquisition accounting method.

The fair value of assets and liabilities are considered to be the same as the book value. The goodwill arising on consolidation of £10,800,000 is being carried forward as an intangible asset and will be amortised over 20 years.

Net liabilities acquired:	£'000	Discharged by:	£'000
Tangible assets	653	Cash paid	6,762
Stocks	151	Acquisition costs	436
Debtors	2,846		
Creditors	(7,252)		
Net liabilities acquired	(3,602)		
Goodwill	10,800		
	7,198		7,198

Notes to the Accounts For the year ended 31 December 1998

12. Investments held as fixed assets (continued)

(ii) Serco Newsec AB

The remaining 50% of the shares of Serco Newsec AB were acquired by Serco Limited on 24 July 1998 for a cash consideration of £3,676,507. This acquisition has been accounted for by the acquisition method of accounting.

The fair value of the assets and liabilities acquired are considered to be the same as the book values. The goodwill arising on consolidation of £3,529,484 is being carried forward as an intangible asset and will be amortised over 20 years.

Net assets acquired:	£'000	Discharged by:	£'000
Tangible assets	432	Cash paid	3,677
Stocks	12	Acquisition costs	16
Debtors	1,169		
Cash	1,644		
Creditors	(2,903)		
Net assets acquired	354		
Investment in Serco Newsec AB as a joint venture at the date of acquisition	(190)		
Goodwill	3,529		
	3,693		3,693

(iii) Tecnodata

100% of the issued share capital of Tecnodata Italia s.r.l. and Tecnodata Computer Services (UK) Ltd were acquired by Serco Limited and one of its subsidiaries on 5 February 1998 for a consideration of £9,000,000 of which £8,000,000 was paid on completion, with deferred consideration of £1,000,000 held in escrow and being payable over the next five years. This acquisition has been accounted for by the acquisition method of accounting.

The fair value of the assets and liabilities are considered to be the same as the book values. The goodwill arising on consolidation of £9,825,908 is being carried forward as an intangible asset and will be amortised over 20 years.

Net liabilities acquired:	£'000	Discharged by:	£'000
Tangible assets	384	Cash paid	9,000
Debtors	1,983	Acquisition costs	247
Cash	323		
Creditors	(3,155)		
Overdraft	(114)		
Net liabilities acquired	(579)		
Goodwill	9,826		
	9,247		9,247

Notes to the Accounts For the year ended 31 December 1998

(iv) Subscriptions for shares in joint ventures

During the year the Group made subscriptions in six joint ventures all of which have been accounted for by the gross equity method of accounting, the details of each are as follows:

50% of the Ordinary Share Capital of Defence Management (Holdings) Ltd was subscribed for by Serco Investments Ltd on 4 June 1998, the date of incorporation, for a cash consideration of £176,500.

50% of the Ordinary Share Capital of Laser Teddington (Holdings) Ltd was subscribed for by Serco Investments Ltd on 29 September 1998, the date of incorporation, for total cash consideration of £249,217.

50% of the Ordinary Share Capital of Pucklechurch Custodial (Holdings) Ltd was subscribed for by Serco Investments Ltd on 13 July 1998, the date of incorporation, for a cash consideration of £100,000.

50% of the Ordinary Share Capital of Medomsley Training Services Ltd was subscribed for by Serco Investments Ltd on 3 November 1998, the date of incorporation, for a cash consideration of £100,000.

An additional shareholding was subscribed for in Great Southern Railways Pty Ltd by Serco Asia Pacific Pty Ltd for a cash consideration of £230,000 which increased the Group's shareholding from 47.59% to 49.24% of the Ordinary Share Capital.

5% of the Ordinary Share Capital of Octagon Healthcare (Holdings) Limited was subscribed for by Serco Investments Ltd on 26 February 1998, the date of incorporation, for a cash consideration of £66,250.

h) Disposals

FBS Limited

The Group's 33% equity holding in FBS Limited, was sold on 12 June 1998 for a cash consideration of £3,440,000, with associated disposal costs of £90,000. The Group's share of the net liabilities of FBS Limited at the date of disposal was £1,252,000 generating a profit on sale of £4,602,000.

13. Stocks

	Group	
	1998	1997
	£'000	£'000
Service spares	**4,967**	4,716
Long term contract balances	**4,160**	3,383
	9,127	8,099

Notes to the Accounts For the year ended 31 December 1998

14. Debtors

		Group		Company	
		1998 £'000	1997 £'000	**1998 £'000**	1997 £'000
a)	Amounts recoverable within one year:				
	Amounts recoverable on contracts	**99,737**	94,108	**–**	–
	Other debtors	**7,938**	8,066	**6,397**	2,097
	Prepayments and accrued income	**10,774**	10,821	**191**	–
	Amounts owed by joint ventures	**1,308**	1,384	**–**	–
		119,757	114,379	**6,588**	2,097
b)	Amounts recoverable after more than one year:				
	Amounts recoverable on contracts	**9,600**	4,192	**–**	–
	Other debtors	**3,376**	1,844	**–**	–
	Pensions prepayment (Note 34)	**8,779**	8,032	**–**	–
	Amounts owed by joint ventures	**15,853**	8,067	**–**	–
		37,608	22,135	**–**	–
	Total debtors	**157,365**	136,514	**6,588**	2,097

Included in trade creditors is an amount of £17,447,000 (1997 – £14,087,000) and in accruals an amount of £2,857,000 (1997 – £897,000) in respect of items procured on behalf of customers. These are partly offset by an amount of £18,173,000 (1997 – £12,640,000) in amounts recoverable on contracts. There are no amounts included in the profit and loss account in respect of such procured items.

15. Other creditors including taxation and social security

	Group		Company	
	1998 £'000	1997 £'000	**1998 £'000**	1997 £'000
Obligations under finance leases	**1,897**	1,940	**30**	30
Corporation tax	**4,894**	4,799	**551**	660
Advance corporation tax on dividends	**214**	1,001	**214**	978
Other taxes and social security costs	**22,565**	20,608	**357**	78
Amounts owed to joint ventures	**3,000**	–	**3,000**	–
Other loans	**764**	745	**–**	–
	33,334	29,093	**4,152**	1,746

Notes to the Accounts For the year ended 31 December 1998

16. Creditors: Amounts falling due after more than one year

	Group		Company	
	1998 £'000	1997 £'000	**1998 £'000**	1997 £'000
a) Amounts falling due after more than one year:				
Bank loans and overdrafts	**50,903**	43,429	**41,420**	41,420
Obligations under finance leases	**5,310**	5,529	**40**	59
Other loans	**4,888**	4,756	**–**	–
Total loans	**61,101**	53,714	**41,460**	41,479
Less: amounts included in creditors falling due within one year	**12,144**	4,694	**30**	30
Amounts falling due after more than one year	**48,957**	49,020	**41,430**	41,449
b) Analysis of loan repayments:				
Bank loans and overdrafts:				
Within one year or on demand	**9,483**	2,009	**–**	–
After five years	**41,420**	41,420	**41,420**	41,420
Obligations under finance leases:				
Within one year or on demand	**1,897**	1,940	**30**	30
Between one and two years	**1,449**	2,293	**10**	29
Between two and five years	**1,809**	1,291	**–**	–
After five years	**155**	5	**–**	–
Other loans:				
Within one year or on demand	**764**	745	**–**	–
Between one and two years	**664**	1,386	**–**	–
Between two and five years	**1,120**	669	**–**	–
After five years	**2,340**	1,956	**–**	–
	61,101	53,714	**41,460**	41,479

c) All loans are unsecured.

d) Finance lease obligations are secured by retention of title to the relevant vehicles and equipment.

e) Treasury and Financial Policies

Financing activities including debt, interest costs and foreign exchange matters are managed by the Group. The Group uses financial instruments to manage its interest rate and foreign exchange exposures. All transactions in derivatives are undertaken to manage the risks arising from the underlying operations. As a matter of policy, the Group does not undertake speculative financial transactions.

The Board reviews and agrees policies for managing the interest rate and foreign exchange risks on a regular basis.

Notes to the Accounts For the year ended 31 December 1998

16. Creditors: Amounts falling due after more than one year (continued)

Financing and Interest Rate Management

The Group finances part of its operations by a mixture of bank borrowings and private placement debt. The Group had £10 million committed and £80 million uncommitted bank borrowing facilities unutilised at 31 December 1998. In December 1997, Serco raised USD 70 million in the US Private Placement market, most of the proceeds being swapped into Sterling at a fixed rate of interest of 7.56%. The USD 70 million is repayable in a 'bullet' payment in December 2007. The Group borrows in the desired currencies at both fixed and floating rates of interest and then uses interest rate swaps to generate the desired interest rate profile.

Foreign Exchange Management

It is Group policy to reduce material transaction exposures by matching the currencies of its borrowings, after currency swaps, to the currencies of its earnings.

The Group companies face some currency transaction exposures. It is Group policy that material exposures are hedged through the use of forward contracts or options.

17. Provisions for liabilities and charges

Group	Balance 1 January 1998 £'000	Usage £'000	Charged/(Credited) to the Profit & Loss Account £'000	**Balance 31 December 1998 £'000**
Contract termination	1,749	(1,315)	(434)	**–**
Pensions provision	702	–	(702)	**–**
Deferred taxation	2,271	–	1,455	**3,726**
	4,722	(1,315)	319	**3,726**

18. Deferred taxation

	Group **1998 £'000**	1997 £'000
The amounts of deferred taxation provided in the accounts are:		
Overseas timing differences	**582**	–
Other timing differences	**3,144**	2,271
	3,726	2,271
Potential amounts of deferred taxation for which no credit has been taken:		
Depreciation in advance of capital allowances	**(701)**	(369)
Overseas timing differences	**(341)**	(722)
Other timing differences	**(772)**	(733)
	(1,814)	(1,824)

Notes to the Accounts For the year ended 31 December 1998

19. Reconciliation of movements in shareholders' funds

	1998 £'000	1997 £'000
Profit on ordinary activities after taxation	**17,420**	14,533
Dividends	**(4,888)**	(3,910)
	12,532	10,623
Currency translation differences on foreign currency net investments	**(298)**	(2,486)
New capital subscribed	**33,279**	2,901
Shares to be issued	**–**	3,078
Goodwill written off	**–**	(13,711)
Net increase in shareholders' funds	**45,513**	405
Opening shareholders' funds	**26,680**	26,275
Closing shareholders' funds	**72,193**	26,680

20. Called up share capital

		1998 £'000	1997 £'000
a)	Authorised 100,000,000 (1997 – 100,000,000) Ordinary Shares of 2p each	**2,000**	2,000
b)	Called up, allotted and fully paid: 64,291,629 (1997 – 61,200,513) Ordinary Shares of 2p each	**1,285**	1,224

c) Ordinary Shares of 2p each allotted in the year:

During the year 79,116 Ordinary Shares of 2p each were allotted to the holders of options or their personal representatives. 14,500 of these were allotted at £2.20, 35,000 at £3.69 and 29,616 at £4.61.

3,000,000 Ordinary Shares of 2p each were allotted as a result of a Share Placement on the 4 March 1998 at a price of £11.10 each. The aggregate nominal value of the shares placed was £60,000 and the total consideration received was £33,300,000.

12,000 Ordinary Shares of 2p each were allotted to the Company's Employee Benefit Trust for a consideration of £141,997 to enable the satisfaction of awards granted under the rules of the 'Serco Group plc 1996 Long Term Incentive Scheme'.

d) Options in respect of Ordinary Shares of 2p each:

i) On 10 September 1993, 70,000 options in respect of Ordinary Shares of 2p each were granted, of these there remain 41,500 options which are exercisable at any time up to 10 September 2003 at a price of £2.20 each.

ii) On 16 October 1995, 80,000 options in respect of Ordinary Shares of 2p each were granted, of these 5,000 options have lapsed and there remain 35,000 options which are exercisable at any time between 16 October 1998 and 16 October 2005 at a price of £3.69 each.

iii) In January 1996, 172,180 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1996 Long Term Incentive Scheme', the details of which are set out in Note 3(d).

iv) On 28 February 1996, 10,000 options in respect of Ordinary Shares of 2p each were granted which are exercisable at any time between 28 February 1999 and 28 February 2006 at a price of £4.30 each.

v) The Company operates a Sharesave Scheme whereby eligible employees are granted options to apply for shares as part of a save-as-you-earn contract. 543,133 options were held by employees on 31 December 1998 which were granted on 28 August 1996. The options are exercisable between 1 November 1999 and 1 April 2000 at a price of £4.61 each provided the requirements of the Scheme are met.

Notes to the Accounts For the year ended 31 December 1998

20. Called up share capital (continued)

vi) In January 1997, 239,937 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1996 Long Term Incentive Scheme', the details of which are set out in Note 3(d).
At 31 December 1998 there remained 218,937 options which are exercisable in accordance with the rules of the Scheme. 12,000 options have been exercised during the year.

vii) On 19 December 1997, a put and call option in respect of 366,405 Ordinary Shares of 2p each was granted as deferred consideration on the acquisition of Docklands Railway Management Limited. The option is exercisable at any time between 1 March 1999 and 1 August 1999 at a price of £8.40 per share.

viii) On 20 May 1998, 553,824 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan', the details of which are set out in Note 3(e).

ix) On 4 September 1998, 3,067 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan', the details of which are set out in Note 3(e).

e) The market price of Serco Group plc Ordinary Shares of 2p each as at 31 December 1998 was £11.51½ and ranged from £7.82 to £14.47 during the year.

21. Share premium account

	£'000
Balance at 1 January 1998	23,977
Share premium on share placement (net of costs)	32,780
Share premium on issue of shares upon exercise of options	438
Balance at 31 December 1998	**57,195**

22. Other reserve – shares to be issued

	£'000
Balance at 1 January 1998 and 31 December 1998	**3,078**

This reserve represents deferred consideration of Serco Group plc shares on the acquisition of Docklands Railway Management Limited in 1997.

23. Goodwill written off

	£'000
Balance at 1 January 1998	41,578
Transfer to profit and loss account reserve	(41,578)
Restated balance at 1 January 1998	**–**

24. Profit and loss account

	£'000
Group	
Balance at 1 January 1998	39,836
Transfer from goodwill written off in previous years	(41,578)
Restated balance at 1 January 1998	(1,742)
Retained profit transferred to reserves	12,532
Foreign exchange translation differences	(298)
Balance at 31 December 1998	**10,492**

Notes to the Accounts For the year ended 31 December 1998

Company
As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the Parent Company is not presented as part of these accounts. The consolidated profit for the financial year includes the Parent Company profit of £11,282,000 which includes dividends of £17,515,000 received from subsidiary companies.

A final ordinary dividend of £3,279,000 is proposed which together with the interim dividend of £1,479,000 and the payment in relation to the 1997 final dividend caused by the movement in number of shares of £135,000, leaves a profit of £6,389,000 which has been added to reserves brought forward of £17,319,000 along with a foreign exchange movement of £1,319,000 resulting in reserves carried forward of £22,389,000.

25. Reconciliation of operating profit to net cash inflow from operating activities

	1998 £'000	Restated 1997 £'000
Operating profit	**23,372**	18,079
Depreciation	**8,096**	7,039
Goodwill amortisation	**823**	–
Loss on sale of tangible assets	**346**	35
Increase in stocks	**(865)**	(1,227)
Increase in debtors	**(7,143)**	(28,542)
Increase in creditors	**7,854**	13,974
Decrease in provisions	**(2,451)**	(3,129)
Net cash inflow from operating activities	**30,032**	6,229

26. Analysis of net debt

	Balance 1 January 1998 £'000	Cash Flow £'000	Other non-cash changes £'000	**Balance 31 December 1998 £'000**
Cash at bank and in hand	19,618	33,856	–	**53,474**
Overdrafts	(2,009)	(7,474)	–	**(9,483)**
Cash net of overdrafts	17,609	26,382	–	**43,991**
Bank loans due after more than one year	(41,420)	–	–	**(41,420)**
Cash net of overdrafts and bank loans	(23,811)	26,382	–	**2,571**
Other loans due after more than one year	(4,011)	(113)	–	**(4,124)**
Other loans due within one year	(745)	(19)	–	**(764)**
Finance leases	(5,529)	2,104	(1,885)	**(5,310)**
Net debt	(34,096)	28,354	(1,885)	**(7,627)**

Notes to the Accounts For the year ended 31 December 1998

27. Reconciliation of increase in cash to movement in net debt

	1998 £'000	1997 £'000
Increase in cash	**26,382**	13,961
Cash outflow/(inflow) from debt and lease financing	**1,972**	(36,098)
Change in net debt resulting from cash flows	**28,354**	(22,137)
Deferred consideration on acquisition	**–**	(606)
New finance leases	**(1,885)**	(3,024)
Movement in net debt in the period	**26,469**	(25,767)
Net debt at 1 January	**(34,096)**	(8,329)
Net debt at 31 December	**(7,627)**	(34,096)

28. Major non-cash transactions

During the year the Group entered into finance lease arrangements in respect of assets with a total capital value at the inception of the leases of £1,885,000 (1997 – £3,024,000).

29. Purchase of subsidiary undertakings

Net (liabilities)/assets acquired:	1998 £'000	1997 £'000
Tangible fixed assets	**1,469**	724
Stock	**163**	2,479
Debtors	**5,998**	6,418
Cash at bank and in hand	**1,967**	2,599
Creditors	**(13,310)**	(8,729)
Bank overdraft	**(114)**	(288)
Net (liabilities)/assets	**(3,827)**	3,203
Investment in associate at date of acquisition	**(190)**	(219)
Goodwill (see Note 10)	**24,155**	13,711
	20,138	16,695
Satisfied by:		
Cash paid in current year	**20,138**	10,247
Shares allotted	**–**	2,764
Deferred consideration – cash	**–**	606
Deferred consideration – shares	**–**	3,078
	20,138	16,695

Notes to the Accounts For the year ended 31 December 1998

30. Analysis of the net outflow of cash in respect of the purchase of subsidiary undertakings

	1998 £'000	1997 £'000
Cash consideration	**20,138**	10,247
Cash at bank and in hand acquired	**(1,967)**	(2,599)
Bank overdrafts of acquired subsidiary undertakings	**114**	288
Net outflow of cash in respect of the purchase of subsidiaries	**18,285**	7,936

31. Contingent liabilities

The Group has given indemnities to banks totalling £17,331,000 in respect of performance bonds in the normal course of business.
In addition the Group has given financial guarantees in respect of a lease security to a subsidiary and equity contributions to associates of £13,651,000.

32. Capital and other commitments

	Group		Company	
	1998 £'000	1997 £'000	1998 £'000	1997 £'000
Capital expenditure contracted but not provided	**2,637**	980	**–**	–

During the year ending 31 December 1999 the Group is to make the following payments in respect of operating leases:

	Land and Buildings £'000	Other £'000
Leases which expire:		
Within one year	908	3,347
Between one and five years	3,538	16,985
After five years	1,466	12
	5,912	20,344

Notes to the Accounts For the year ended 31 December 1998

33. Related parties

Directors

The Directors of Serco Group plc had no material transactions with the Group during the year other than as a result of service agreements. Details of the Directors' remuneration is disclosed in Note 3.

Joint ventures

The following material transactions took place between the Group and its joint ventures during 1998:

	1998 £'000	1997 £'000
Net loans during the year	**(5,563)**	(5,248)
Net purchase of goods or services	**(2,084)**	(1,866)
Royalties and management fees received	**744**	1,057
Dividends received	**1,023**	1,210
	(5,880)	(4,847)

The following receivable balances relating to joint ventures were included in the Group balance sheet:

	1998 £'000	1997 £'000
Amounts due within one year:		
Loans	**1,120**	343
Trading balance	**2**	–
Royalties and management fees received	**56**	692
Dividends	**130**	349
	1,308	1,384
Amounts due after more than one year:		
Loans	**15,853**	8,067

The following payable balances relating to joint ventures were included in the Group balance sheet:

	1998 £'000	1997 £'000
Amounts payable within one year:		
Loans	**3,000**	–

Details of Group investments in joint ventures and other undertakings are given in Note 35. No amounts were written off during the period.

Notes to the Accounts For the year ended 31 December 1998

34. Pension schemes

The net pension charge for the year ended 31 December 1998 was £14,875,000 (1997 – £9,058,000).

The Group paid employer contributions of £3,179,000 (1997 – £870,000) into other UK defined contribution and foreign state pension schemes.

The other main Group operated pension schemes were as follows:

a) Serco Pension and Life Assurance Scheme

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 6 April 1997.

The projected unit method was adopted for the actuarial valuation of the Scheme for accounting purposes. The main actuarial assumptions used in the valuation for accounting purposes this year were:

Investment yield	9.5% p.a.
Salary growth	7.5% p.a.
Price inflation	5.0% p.a.
Equity dividend growth	5.0% p.a.
Pension increases	Nil, except as required by legislation

The Scheme is assessed to be fully funded on a current funding level basis based on a market value of assets of £76,829,000 at 6 April 1997. Liabilities for this purpose are calculated using the basis for determining individual cash equivalents for active members and deferred pensioners and by estimating the cost of purchasing annuity policies for pensioners.

The actuarial value of the assets represented 100% of the ongoing liabilities of the Scheme. Variations from the normal cost are amortised for accounting purposes over a fifteen year period as a constant monetary amount.

Employer pension contributions paid into the Scheme during the year were £4,355,000 (1997 – £3,589,000), of which £619,000 related to special contributions in respect of a discretionary increase to pensions in payment awarded during the year.

At 31 December 1998 a prepayment of £248,000 (1997 – £702,000 provision) in respect of the Scheme was included in the balance sheet, whilst £3,405,000 was charged to the 1998 Profit and Loss Account, in respect of the Scheme.

Notes to the Accounts For the year ended 31 December 1998

34. Pension schemes (continued)

b) The Serco-IAL Pension Scheme

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 31 March 1998. On the assumptions adopted for accounting purposes and based on a market value of assets of £97,316,000 at 31 March 1998, the actuarial value of the assets represented 117% of the ongoing past service liabilities of the Scheme as at that date.

For accounting purposes, the projected unit method has been adopted and the main actuarial assumptions used are:

Investment yield	8.50% p.a.
Salary growth	6.00% p.a.
Equity dividend growth	5.50% p.a.
Pension increases (Part 4 and 6 members)	3.75% p.a.
Pension increases (others)	4.00% p.a.

The past service surplus as at 31 March 1998 is being amortised for accounting purposes over a nine year period as a constant monetary amount.

No employer pension contributions were paid into the Scheme during the year.

An amount of £154,000 (1997 – £2,665,000) has been credited to the 1998 profit and loss account in respect of the Scheme and a prepayment of £7,885,000 (1997 – £7,731,000) has been included in the balance sheet as at 31 December 1998.

Notes to the Accounts For the year ended 31 December 1998

c) Serco Services Pension Scheme

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 1 September 1996.

The projected unit method was adopted for the actuarial valuation of the Scheme for accounting purposes. The main actuarial assumptions used in the valuation for accounting purposes this year were:

Investment yield	9.5% p.a.
Salary growth	7.5% p.a.
Price inflation	5.0% p.a.
Equity dividend growth	5.0% p.a.
Pension increases	5.0% p.a.

The Scheme is assessed to be fully funded on a current funding level basis based on a market value of assets of £7,193,517 at 1 September 1996. Liabilities for this purpose are calculated using the basis for determining individual cash equivalents for active members and deferred pensioners and by estimating the cost of purchasing annuity policies for pensioners.

The actuarial value of the assets represented 118% of the ongoing liabilities of the Scheme. Variations from the normal cost are amortised for accounting purposes over a sixteen year period as a percentage of salaries.

Employer pension contributions paid into the Scheme during the year were £348,000 (1997 – £449,000).

At 31 December 1998 there was a prepayment of £396,000 (1997 – £269,000) in respect of the Scheme in the balance sheet whilst £221,000 (1997 – £327,000) was charged to the 1998 profit and loss account, in respect of the Scheme.

Notes to the Accounts For the year ended 31 December 1998

34. Pension schemes (continued)

d) Serco Superannuation Fund

This is a combined defined benefit and defined contribution scheme which was established in Australia on 1 April 1993 to provide equivalent benefits for Members transferring from the AWA Defence Industries Superannuation Fund, a defined benefit scheme, and the AWA Group Superannuation Fund (1987), a defined contribution scheme.

Actuarial assessments covering expenses and contributions relating to the defined benefit element of the Scheme are carried out by independent qualified actuaries with the last such valuation being carried out as at 31 December 1997. The Attained Age Method was used for the actuarial valuation of the Scheme as at 31 December 1997. This method was chosen to produce a level Employer contribution rate as a proportion of Members' salaries over the expected future working lives of the existing Members, as the defined benefit element of the Scheme was closed to new Members with effect from 1 April 1993.

The main actuarial assumptions used in the actuarial valuation for accounting purposes this year were:

Average long term interest rate (net of investment and administration expenses and investment tax)	9.5%
Average long term allowance for salaries increases	7.5%

The defined benefit element of the Scheme is assessed to be fully funded on a current funding level basis based on a market value of assets of £1,054,000 (A$2,860,000) at 31 December 1997 with a ratio of market value of assets to current funding level liabilities of 121%.

The actuarial value of assets of the defined benefit element of the Scheme represented 112% of its ongoing liabilities at 31 December 1997.
The pension cost calculated under the Attained Age Method will amortise the above surplus over the expected future working lives of the existing Members which have an average value of 11 years.

Employer pension contributions paid into the Scheme during the year were as follows:

		1998 £'000	**1998 A$'000**
Defined benefit element	Regular cost	**96**	**261**
	Variation cost	**(9)**	**(24)**
		87	**237**
Defined contribution element		**1,852**	**5,025**
Total		**1,939**	**5,262**

		1997 £'000	1997 A$'000
Defined benefit element	Regular cost	121	268
	Variation cost	(11)	(24)
		110	244
Defined contribution element		1,860	4,108
Total		1,970	4,352

Notes to the Accounts For the year ended 31 December 1998

e) Serco Alternative Pension Scheme 1994

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 6 April 1997.

The projected unit method was adopted for the actuarial valuation of the Scheme. The main actuarial assumptions used in the valuation for accounting purposes this year were:

Investment yield	9.5% p.a.
Salary growth	7.5% p.a.
Price inflation	5.0% p.a.
Equity dividend growth	5.0% p.a.
Pension increases	5.0% p.a.

The Scheme is assessed to be fully funded on a current funding level basis based on a market value of assets of £6,678,000 at 6 April 1997 and after allowing for subsequent bulk transfer payments totalling £5,600,000. Liabilities for this purpose are calculated using the basis for determining individual cash equivalents for active members and deferred pensioners and by estimating the cost of purchasing annuity policies for pensioners.

The actuarial value of the assets represent 102% of the ongoing liabilities of the Scheme. Variations from the normal cost are amortised for accounting purposes over a fifteen year period as a constant monetary amount.

Employer pension contributions paid into the Scheme during the year were £3,802,000 (1997 – £5,500,000), of which £399,000 was to finance benefit enhancements. At 31 December 1998 a prepayment of £250,000 (1997 - £33,000) in respect of the Scheme was included in the balance sheet, whilst £3,585,000 was charged to the 1998 profit and loss account in respect of the Scheme.

Notes to the Accounts For the year ended 31 December 1998

34. Pension schemes (continued)

f) The NPL Management Limited Pension Scheme

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 1 October 1995.

The projected unit method was adopted for the actuarial valuation of the Scheme. The main actuarial assumptions used in the valuation for accounting purposes this year were:

Investment yield	9.5% p.a.
Salary growth	7.0% p.a. (plus promotional scale)
Price inflation	5.0% p.a.
Pension increases	5.0% p.a.

The Scheme had no assets at its inception and members have the option as to whether to transfer their pension rights from previous arrangements into the Scheme. Transfer payments totalling £7,268,135 have been paid into the Scheme to date. Hence, it is assumed to be fully funded on a current funding level basis at 1 October 1995.

There is no surplus or deficiency to be amortised.

Employer pension contributions paid into the Scheme during the year were £1,607,000 (1997 – £1,663,000).

g) The Serco Shared Cost Section of the Railways Pension Scheme

The Serco Shared Cost Section of the Scheme was established on 6 January 1997 after the acquisition of Nationwide Fire Services from the British Railways Board.

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 6 January 1997.

The attained age method was adopted for the actuarial valuation of the Scheme. The main actuarial assumptions used in the valuation for accounting purposes were:

Investment yield	8.5%
Salary growth	6.5%
Price inflation	4.5%
Pension increases	4.5%

As at 6 January 1997 the actuarial value of the assets represented 115% of the ongoing liabilities of the Scheme. Although a surplus was revealed, the subsequent acquisition of Railtest and compulsory transfers as a result of TUPE mean that the current funding position is not clear. A triennial actuarial valuation of the Scheme as at 31 December 1998 is currently taking place with the results due in late summer 1999.

Employer pension contributions paid into the Scheme and charged to the profit and loss account during the year were £203,000.

Notes to the Accounts For the year ended 31 December 1998

h) Serco Metrolink Pension Scheme

This is a pre-funded defined benefits scheme established on 1 September 1991. On 27 May 1997 Serco Metrolink Limited replaced Greater Manchester Metro Limited as the Principal Employer of the Scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries with the last such review being carried out as at 1 September 1995.

The projected unit method was adopted for the actuarial valuation of the Scheme for accounting purposes. The main actuarial assumptions used in the valuation for accounting purposes this year were:

Investment yield	9.0% p.a.
Salary growth	7.0% p.a.
Price inflation	5.0% p.a.
Equity dividend growth	5.0% p.a.
Pension increases	4.0% p.a.

The Scheme is assessed to be fully funded on a current funding level basis at 1 September 1995. Liabilities for this purpose were calculated using the basis for determining individual cash equivalents for active members and deferred pensioners and by estimating the cost of purchasing annuity policies for pensioners.

As at 1 September 1995 the actuarial value of the assets represented 126% of the ongoing liabilities of the Scheme based on the assumptions used for the formal triennial valuation. No allowance for any surplus has been made for this accounting year pending the results of the actuarial valuation as at 1 September 1998 because the surplus existing at 1 September 1995 was utilised by way of a temporary suspension of employer and member contributions during 1996.

Employer pension contributions paid into the Scheme during the year and charged to the profit and loss account totalled £205,000.

Notes to the Accounts For the year ended 31 December 1998

34. Pension schemes (continued)

i) Docklands Light Railway Pension Scheme

Docklands Railway Management Limited became a participating employer in the Scheme on 6 April 1997. The Scheme is a pre-funded defined benefit scheme, with Docklands Light Railway Limited being the Principal Employer.

The funding policy is to contribute such variable amounts, on the advice of the Scheme Actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 1 April 1996.

The projected unit method was adopted for the actuarial valuation of the Scheme for accounting purposes. The main actuarial assumptions used in the valuation for accounting purposes this year were:

Investment yield	8.5% p.a.
Salary growth	6.5% p.a.
Price inflation	4.75% p.a.
Equity dividend growth	4.0% p.a.
Pension increases	4.75% p.a. for Pre 1/4/1989 joiners
	4.25% p.a. for Post 1/4/1989 joiners

The Scheme is assessed to be fully funded on a current funding level basis based on a market value of assets of £9,639,000 at 1 April 1996. Liabilities for this purpose are calculated using the basis for determining individual cash equivalents for active members and deferred pensioners and by estimating the cost of purchasing annuity policies for pensioners.

The actuarial value of the assets represented 100% of the ongoing liabilities of the Scheme. Variations from the normal cost are amortised for accounting purposes over the future working lifetime of current active members as a percentage of salaries.

Employer pension contributions paid into the Scheme and charged to the profit and loss account totalled £685,000 (1997 – £51,000).

Notes to the Accounts For the year ended 31 December 1998

35. List of principal undertakings

The companies listed below are, in the opinion of the Directors, the principal undertakings of Serco Group plc. The percentage of equity capital directly or indirectly held by Serco Group plc is shown. The companies are incorporated and principally operate in the countries designated below.

Principal subsidiaries

United Kingdom	
Serco Limited*	100%
Serco Contracting Limited	100%
Serco Denholm Limited	90%
Serco Europe Limited	100%
Serco-IAL Limited	100%
Serco International Limited	100%
Serco Maintenance Services Limited	100%
Serco Railtest Limited	100%
Sercoserve Limited	100%
Serco Services Ireland Limited	100%
Serco Systems Limited*	100%
Serco Test Technology Limited	100%
Serco Overseas Investments Limited*	100%
Serco Project Development Limited*	100%
Serco Research & Development Limited*	100%
Serco Insurance Co Limited*	100%
NPL Management Limited*	100%
Docklands Railway Management Limited	100%
Serco Investments Limited*	100%
Tecnodata Computer Services (UK) Limited	100%
Community Leisure Management Ltd	100%
Rest of Europe	
France	
Serco France Sarl	100%
Germany	
Serco Services GmbH	100%
Serco GmbH	100%
Italy	
Serco Servizi s.r.l.	100%
Tecnodata Italia s.r.l.	100%
The Netherlands	
Serco Facilities Management BV	100%
Serco International BV	100%
Serco Investments BV	100%
Sweden	
Serco Newsec AB	100%
Belgium	
Serco Belgium S.A.	100%
Serco Facilities Management S.A.	100%
Asia Pacific	
Australia	
Serco Systems Pty Limited	100%
Serco Asia Pacific Pty Limited	100%
Serco Australia Pty Limited	100%
Serco Water (WA) Pty Limited	100%
Serco Superannuation Pty Limited	100%
New Zealand	
Serco Group NZ Limited	100%
Other	
Canada	
Serco Facilities Management, Inc.	100%
Serco Aviation Services, Inc.	100%
USA	
Serco, Inc.	100%
Serco Management Services, Inc.	100%
Barton ATC, Inc.	100%
Barton ATC International, Inc.	100%
JL Associates, Inc.	100%

Joint venture undertakings

United Kingdom	
Premier Prison Services Limited	50%
Lowdham Grange Prison Services Limited	50%
Kilmarnock Prison Services (Holdings) Limited	50%
Serco Gulf Engineering Limited	50%
FRA Serco Limited	50%
Defence Management (Holdings) Limited	50%
Medomsley Training Services Limited	50%
Pucklechurch Custodial (Holdings) Limited	50%
Laser Teddington (Holdings) Limited	50%
Altram (Manchester) Limited	26%
Asia Pacific	
Australia	
Defence Martime Service Pty Limited	50%
InfoDirect Pty Limited	50%
Serco-Gardner Merchant Pty Limited	50%
Great Southern Railways Pty Limited	49%
New Zealand	
Serco Viatech Limited	50%
Serco Project Engineering Ltd	50%
Serco Gardner Merchant NZ	50%
Hong Kong	
Serco Guardian (FM) Limited	50%
Other	
Bahrain	
Aeradio Technical Services WLL	49%
Dubai	
International Aeradio (Emirates) LLC	49%
Indian Ocean	
Diego Garcia	20%
Johnston Atoll, Pacific Ocean	
Kalama Services	38%
Malaysia	
Serco Minda SDN	49%
Saudi Arabia	
Key Communications Development Co Limited	N/A
Singapore	
JBS Singapore Pte Limited	20%
Serco Guthrie Pte Ltd	50%
USA	
Baker Serco Wright Patterson	49%

*Directly held by Serco Group plc.

Notice of Annual General Meeting

Notice is hereby given that the Twelfth Annual General Meeting of Serco Group plc will be held at the National Physical Laboratory, Teddington, Middlesex, TW11 0LW at 10.00am on Thursday 1 April 1999 to consider and, if thought fit, pass the following resolutions, of which numbers 1 to 7 (inclusive) will be proposed as ordinary resolutions and numbers 8 and 9 will be proposed as special resolutions:

1. To receive and adopt the Annual Accounts and the Annual Review and Summary Financial Statement for the year ended 31 December 1998, together with the reports of the Directors and Auditors thereon.

2. To declare a final dividend for 1998.

3. To re-elect R White as an Executive Director.

4. To re-elect K Beeston as an Executive Director.

5. To re-elect G Sturgess as a Non-executive Director.

6. To re-appoint Deloitte & Touche, Chartered Accountants, as the auditors of the Company and to authorise the Directors to fix the auditors' remuneration.

7. That the Directors be and they are hereby generally and unconditionally authorised in accordance with Section 80 of the Companies Act 1985 to exercise all powers of the Company to allot, grant options over, offer or otherwise deal with or dispose of relevant securities (as defined in Section 80(2) of the said Act) of the Company provided that this authority shall:

a) be in substitution for any authority in accordance with the said Section 80 which may have been given to the Directors before the date hereof;

b) be limited to the allotment of such relevant securities up to an aggregate nominal value of £424,408; and

c) unless previously revoked or varied, shall expire on the date of the next Annual General Meeting of the Company or the date being fifteen months after the passing of this Resolution, whichever is the earlier, but so that the Company may at any time before the authority shall expire make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities in pursuance of such an offer or agreement as if the authority conferred hereby had not expired.

8. That, subject to Resolution 7 being passed and pursuant to and in accordance with the authority thereby granted, the Directors be and they are hereby authorised in accordance with Section 95 of the Companies Act 1985 to allot equity securities (as defined in Section 94(2) of the said Act) of the Company as if Section 89(1) of the said Act did not apply to such allotment, provided that this authority shall be limited:

a) to the allotment (otherwise than pursuant to sub-paragraph (b) below) of equity securities which are, or are to be, wholly paid in cash up to an aggregate nominal value of £64,304; and

b) to the allotment of equity securities in connection with a rights issue in favour of shareholders where the equity securities respectively attributable to the interests of the shareholders are proportionate (as nearly as may be) to the respective numbers of ordinary shares of 2p each in the Company held by them but subject to such exclusions or other arrangements as the Directors may deem necessary or expedient to deal with fractional entitlements or legal or practical problems under the laws of, or requirements of any recognised body, in any territory;

Notice of Annual General Meeting

and unless previously revoked or varied, shall expire on the date of the next Annual General Meeting of the Company or the date being fifteen months after the passing of this Resolution, whichever is the earlier, but so that the Company may at any time before the authority shall expire make an offer or agreement which would or might require equity securities to be allotted after such expiry and the Directors may allot equity securities in pursuance of such an offer or agreement as if the authority conferred hereby had not expired.

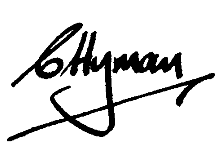
9. That, in accordance with Article 10 of the Company's Articles of Association and the Companies Act 1985, the Company be and it is hereby authorised to make market purchases (within the meaning of Section 163(3) of the Companies Act 1985) of its ordinary shares of 2p each upon or subject to the following conditions:

a) the maximum number of ordinary shares of 2p each in the Company which may be purchased is 6,430,422;

b) the maximum price at which ordinary shares may be purchased shall be 5% above the average of the middle market quotations for the ordinary shares as taken from The London Stock Exchange Daily Official List for the five business days preceding the date of purchase and the minimum price shall be 2p being the nominal value of the ordinary shares (in both cases exclusive of expenses); and

c) this authority shall expire on the date of the next Annual General Meeting or the date being fifteen months after the passing of this Resolution, whichever is the earlier save that the Company may, before such expiry, enter into a contract of purchase under which such purchase may be completed or executed wholly or partly after the expiration of this authority.

By order of the Board:



Christopher R Hyman
Secretary

Dolphin House
Windmill Road
Sunbury-on-Thames
Middlesex TW16 7HT

3 March 1999

Notes to Annual General Meeting

1. A member entitled to attend and vote at this meeting is entitled to appoint a proxy or proxies to attend and vote instead of him or her. A proxy need not be a member of the Company. Proxy forms must be lodged together with the power of attorney or other authority (if any) under which it is signed or a notarially certified copy of such power or authority at the Registrars' office at Lloyds TSB Registrars, The Causeway, Worthing, West Sussex, BN99 6DA not later than 48 hours before the time fixed for the meeting. In the case of a corporation being the relevant registered holder of shares, a proxy must be executed under its seal or under the hand of an officer, attorney or other person authorised to sign the same.

2. The Register of Directors' Interests in the Company and copies of all Directors' service contracts with the Company and its subsidiaries are available for inspection at the Company's registered office, Dolphin House, Windmill Road, Sunbury-on-Thames, Middlesex TW16 7HT during usual business hours on any weekday (public holidays excluded); and, at the place of the Annual General Meeting for a period of fifteen minutes immediately before the Annual General Meeting until the conclusion of that meeting.

3. Resolutions 7, 8 and 9 to be proposed deal with the following matters:

Resolution 7 – Authority to Allot Shares
It is proposed to renew the authority of the Directors in relation to the allotment of unissued and uncommitted shares in the capital of the Company. The authority is limited to 21,220,394 ordinary shares of 2p each (being £424,408 in nominal value), representing approximately 33% of the total issued ordinary share capital of the Company as at 12 February 1999. The authority will expire upon the earlier of the date of the next Annual General Meeting or the date being fifteen months following the passing of the resolution.

Resolution 8 – Disapplication of Pre-emption Rights
It is proposed to renew the authority of the Directors to allot equity securities for cash without first being required to offer such securities to existing shareholders. This authority relates to 3,215,211 ordinary shares of 2p each (being £64,304 in nominal value), representing 5% of the issued ordinary share capital of the Company as at 12 February 1999. The authority will expire upon the earlier of the date of the next Annual General Meeting or the date being fifteen months following the passing of the resolution.

Resolution 9 – Authority to Purchase Own Shares
Resolution 9 provides authority for the Company to make purchases on a recognised investment exchange of up to 10% of the Company's own issued ordinary shares. Any shares purchased by the Company shall be cancelled and the issued share capital reduced accordingly. The authorised share capital of the Company would remain the same. The Directors believe that the ability of the Company to buy its own ordinary shares is advantageous to both the Company and its shareholders. Any exercise of such authority would only take place after careful consideration and to the extent that the Directors believe that a purchase would be in the best interests of the Company and would result in an expected increase in earnings per ordinary share.

The Directors have no present intention of exercising the authorities proposed under Resolutions 7, 8 and 9.