Mears Group PLC
Annual report and accounts 2016

Helping clients in new ways

MEARS

We carry out
6,000
repairs a day

Find out more about our Housing business on **page 4**

Mears today employs over 15,000 people, providing services in every region of the UK. In partnership with our Housing clients, we maintain, repair and upgrade the homes of hundreds of thousands of people in communities from remote rural villages to large inner city estates. Mears has extended its activities to provide broader housing solutions to solve the challenge posed by the lack of affordable housing. Our Care teams provide support to around 20,000 people a year, enabling older and disabled people to continue living in their own homes. We focus on long-term outcomes for people, rather than short-term solutions and invest in innovations that make a positive impact on people's quality of life and on their communities' social, economic and environmental wellbeing

by helping clients in new ways...

Check out what we are up to on our website, www.mearsgroup.co.uk, and connect with us on social media

- Mears Group
- @mearsgroup
- Mears Group PLC

We provide care to more than

20,000

elderly and disabled people

Find out more about our Care business on **page 5**

Contents

Our year in brief

Mears is a market leader in providing housing management and maintenance services to the affordable housing sector and a major presence in the homecare and support market.

Key highlights

- Group revenue of £940.1m (2015: £881.1m), reflecting strong organic growth in Housing following a record year for new contract bidding in 2015.
- Group profit before tax and before acquisition intangible amortisation of £40.1m (2015: £36.8m).
- Housing revenue of £787.5m (2015: £735.1m), reflecting strong organic growth underpinned by the growth in Housing Management.
- Housing operating margin of 5.6% (2015: 5.8%) reflects some dilution from the record number of new contract mobilisations.
- Service quality remains our key differentiator; the proportion of customers rating our service as 'excellent' was maintained at the record level of 91% (2015: 91%).
- Care revenue increased by 5% to £152.6m (2015: £146.0m), reflecting the full-year impact of the acquisition of Care at Home from Care UK.
- Rationalisation of our Care business – closure of circa 20% of Care branches and redirection of activities towards maintaining a portfolio of good quality contracts that can provide clear and sustainable margins with more sophisticated clients.
- Care operating results reflect the cost of care rationalisation. Excellent progress made in securing charge rate increases following the introduction of the National Living Wage.
- EBITDA cash conversion of 70% (2015: 99%) is below our historic norm. Average net debt of £85m (2015: £68m) and net debt at 31 December 2016 of £12.4m (2015: net cash of £0.8m), reflecting the working capital expansion required to fund organic growth, a changing sales mix and an outflow of £10m relating to deferred consideration payable in respect of the acquisition of Omega.
- Total dividend increased by 6% to 11.70p per share (2015: 11.00p), reflecting the Board's confidence in the underlying performance of the Group and the future.
- New contract wins of circa £500m (2015: £1 billion); Housing awards of over £250m with a conversion rate of 39% (2015: £900m and 49%); and Care awards of over £200m with a conversion rate of 74% (2015: £80m and 63%).
- Order book at £3.1 billion (2015: £3.5 billion) and a solid pipeline of new opportunities.
- Visibility of 94% of consensus forecast revenue for 2017 and in excess of 82% for 2018 (2015: 96% and 83% respectively at the turn of the year).

Group revenue

£940.1m +7%

2016	£940.1m
2015	£881.1m
2014	£838.7m

Group operating profit*

£41.9m +8%

2016	£41.9m
2015	£38.7m
2014	£43.3m

Dividend per share

11.70p +6%

2016	11.70p
2015	11.00p
2014	10.00p

Normalised diluted earnings per share**

30.36p +9%

2016	30.36p
2015	27.94p
2014	32.20p

* Operating profit before amortisation of acquisition intangibles (see note 1 to the financial statements).

** On continuing operations, see note 9 to the financial statements.

Our business

We focus on long-term outcomes and positive social, economic and environmental impact.

Our vision

Mears' vision is to make a positive difference to the communities we serve. We do this by improving homes, improving communities and improving lives. Our approach is based on the development of outstanding partnerships with employees, clients, tenants, customers, their families and the wider community.

Our values

- We value our customers and communities, putting the needs of our customers at the heart of everything we do.
- We value teamwork, supporting each other, sharing ideas and never excluding others.
- We value personal responsibility, setting and achieving consistently high standards in our work and our conduct and never adopting a negative attitude.
- We value innovation, being inventive in our approach and never allowing conventional thinking or bureaucracy to get in the way.

Our key strengths

Differentiated service delivery

In order for customers to recommend us, we must deliver excellent service. We randomly conduct around 80,000 Housing customer surveys each year.

Customer excellence rating

91%

Strategic relationships

We listen carefully to the needs of our clients and their tenants. As our clients' needs have changed, we have developed a broader service offering which has increased the depth of our client partnerships.

Value of new contracts mobilised in 2016

£1bn

Strong financial management

We operate in a high volume, low value and low margin environment where we have delivered consistent financial results over an extended period of time. This is achieved through works management systems, conservative accounting policies and a culture of giving attention to detail.

Normalised EPS

+9%

Social value

We aim to lead the way with social value in the markets where we operate, delivering meaningful outcomes through positive community engagement projects and effective measurement.

Net social impact in 2016

£3,555,877

Find out more about our business model on **page 10**

Find out more about our strategic objectives on **page 12**

Find out more about our social values on **page 36**

Our business continued

Housing

We repair and maintain around 15% of the Social Homes in the UK and we are increasingly focused on providing broader affordable housing solutions.

The Housing division made excellent progress in 2016

Our broader service offering, incorporating our new homes capability, alongside housing management and maintenance, supports our involvement in new partnering models as they emerge alongside traditional outsourcing contracts.

We have broadened the services we offer across the sphere of affordable housing. In particular, our acquisition of Omega in 2014 has unlocked a large number of new housing management opportunities. We will look to make further acquisitions to reinforce our market-leading position.

Our clients are increasingly looking for partners who can operate strategically as well as operationally across a range of housing services. Mears has extended its core reactive and planned maintenance offering to include housing management to support clients in delivering more integrated solutions, aligned to their strategic challenges.

In focus

- Milton Keynes regeneration page 28
- Empty Homes – improving neighbourhoods page 27

Our services

- Repairs and maintenance
- Planned and cyclical maintenance
- Estate management
- Asset management
- Income management
- Emergency accommodation

Our customers

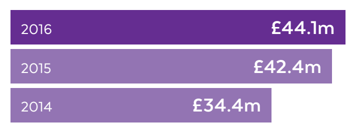
- Local Authorities
- Registered Social Landlords
- Private landlords
- Tenants and service users
- Community groups

Revenue

£787.5m +7%

Operating profit

£44.1m +4%



Operating margin

5.6%

See note 1 to the financial statements.

We repair and maintain over

700,000

homes nationwide

Read about our Housing division on **page 24**

Care

We provide personal care to over 20,000 elderly and disabled people.

The Care division made good progress in a challenging period

We are continuing to see the emergence of new commissioning models that are long-term partnering orientated, focused on improving quality and cost over time and combining services into an integrated approach to achieve better outcomes for users at less overall cost to the public purse.

Whilst there has been no shortage of demand for care work, our barrier has been recruiting sufficient numbers of good quality carers. However, we believe the current funding pressure will be the catalyst for change as will the impact of the National Living Wage on the underlying cost of care.

We have a comprehensive range of domiciliary care and complex care services enhanced by the ability to deliver a range of housing adaptations and assistive technology such as telecare. We deliver broad solutions to the independent living challenges faced by so many elderly people, as well as younger people with physical or mental disabilities.

In focus

→ Wiltshire Help to Live at Home page 29

Our services

→ Independent living services

→ Aids and adaption

→ Complex care

→ Assistive technology (telecare)

→ Live-in care

→ Extra care

Our customers

→ Local Authorities

→ NHS

→ Charities

→ Community groups

Revenue

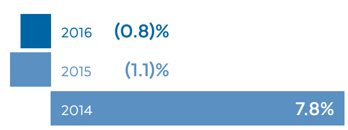
£152.6m +5%

Operating profit

£(1.2)m +25%

Operating margin

(0.8)%



See note 1 to the financial statements.

Our staff volunteered over
20,000
hours last year

Read about our Care division on **page 28**

Chairman's statement

I continue to be impressed at the strong growth being delivered by our Housing Management business.

Summary

- This has been the busiest year on record, with nine new Housing contracts successfully mobilised
- We secured a new contract with Milton Keynes Council, representing one of the single largest contracts ever awarded to Mears
- During the year we took the decision to exit from in excess of 20% of our existing care contracts where the pricing, longevity and spend certainty did not allow us to deliver a high quality service at sustainable margins
- Our aim to make sure jobs and opportunities are open to everyone has been enhanced by our continued Social Mobility Champion status

I am delighted to report a year of solid progress, particularly within our Housing division, where we have continued to extend our services from our traditional maintenance base to a broader affordable housing offering. The year was the busiest on record for new contract mobilisations, with nine new Housing contracts successfully mobilised.

A particular highlight for the year was Mears' success in securing and mobilising a new partnership with Milton Keynes Council, which represents one of the single largest contracts ever awarded to Mears. The contract initially saw the commencement of repairs and maintenance services to nearly 11,500 homes. The scope of works quickly expanded with Mears engaged to develop 80 new homes. In addition, a number of temporary accommodation solutions are being developed through the joint venture partnership. We anticipate seeing further new client opportunities, similar to Milton Keynes, which bring together all elements of our Housing service offering.

Our Housing Management business continues to deliver strong growth. Since Mears extended its services to housing management, accelerated by the acquisition of Omega in 2014, the Group has successfully grown the business from around 2,000 homes under full management to a figure in excess of 9,000. This remains an exciting area for us given the urgency for our clients to find solutions to address the homelessness issue, and the pipeline remains buoyant. We are bringing a number of new innovative service models to this area which I look forward to reporting on in the future.

We firmly believe in our long-term Care strategy and that Mears is best placed to benefit from the inevitable market evolution. During the year we took the decision to exit from around 20% of our existing contracts where the pricing, longevity and certainty of spend did not allow us to deliver a high quality service at sustainable margins.

I am pleased to report a solid financial performance for the year to 31 December 2016. Group revenue amounted to £940.1m (2015: £881.1m), with this organic growth being driven by our Housing business. Group profit margin edged upwards to 4.26% (2015: 4.17%) with profit before tax and, before acquired intangible amortisation increasing by 9% to £40.1m (2015: £36.8m). Normalised diluted earnings mirrored the increase in operating profits, increasing by 9% to 30.36p (2015: 27.94p). Our performance by operating division is discussed in greater detail in the Review of Operations.

The order book sits at £3.1 billion, edging back from the record high of £3.5 billion reported at the end of 2015. Importantly, revenue visibility for 2017 at the turn of the year stood at 93%, which is just below our key performance target of 95%. Revenue visibility for 2017 has subsequently increased to 94%. Revenue visibility for 2018 is 82%, in line with our expectations.

Cash generated from continuing operations as a proportion of EBITDA was 70% (2015: 99%) and there was net debt at the year end of £12.4m (2015: net funds of £0.8m). Average daily net debt for the year increased to £85.0m (2015: £68.0m) reflecting the working capital expansion required to fund the strong organic growth this year together with the £10m of deferred consideration payable in respect of the acquisition of Omega. We have a robust cash management culture and, whilst I have no concerns in respect of falling short of our cash target in 2016, we fully understand the importance placed by our investors on this metric.

Dividend

The Board remains confident in the future opportunities in our growth markets and consequently it expects to continue following a progressive dividend policy. The Board has recommended a final dividend of 8.40p per share which, when combined with the interim dividend, gives a total dividend for the year of 11.70p (2015: 11.00p), a 6% increase, reflecting the Board's confidence in the underlying performance of the Group. The dividend is payable, subject to shareholder approval, on 6 July 2017 to shareholders on the register on 16 June 2017. The Board regularly reviews the Group's dividend policy to maximise returns to shareholders whilst maintaining a prudent capital structure and retaining the ability to invest for growth.

Corporate governance and risk management

The Board continues to set itself high standards of corporate governance. Our Corporate Governance Report issued within our Annual Report details how we approach governance and the areas of focus for the Board in 2016 and into the future. In line with good practice, we have reviewed and updated the Group's risk register. The Senior Management Team plays a central role in reviewing and challenging the Group's risks. The Group risk team presented risk management training modules to all levels of management via the Group development programme, to reinforce our strong risk management ethos.

During 2016 the Group has continued to enhance its risk and control environment. A number of new assurance provider functions have been created, including an IT security governance team to provide extra focus on the increasing challenges of cyber-security.

Board evaluation and effectiveness

Performance evaluation of the Board, its Committees and individual Directors takes place on an annual basis. The Directors were asked for their views on a broad range of areas including Group strategy, independence, experience and effectiveness and the interaction between Board members. It is vital that as a Board we have the right mix of skills, experience and diversity, ensuring that Board members have sufficient knowledge of the Company whilst maintaining their independence and objectivity. I am fortunate as Chairman to be able to call upon a Board with a broad range of expertise and specialist knowledge.

During the year, a number of our Non-Executive Directors reached nine years' service on the Board, and as such are not offering themselves for re-election. I would like to thank David Hosein and Mike Rogers for their significant contribution to the Group.

It was also with deep regret that we announced the passing of Rory Macnamara, who had been a Director since June 2010 and chaired our Nomination Committee. Rory will be greatly missed by the Board for his strong technical contribution, and as a trusted colleague.

UK exit from the European Union

While uncertainty is never positive for business, Mears does not envisage any significant negative impact from an EU exit. It was disappointing that the Government's domestic policy agenda took a back-seat through much of 2016 as the referendum took centre stage. It is pleasing now that since the turn of the year, significant momentum is building in respect of both Housing and Care policy.

Social value

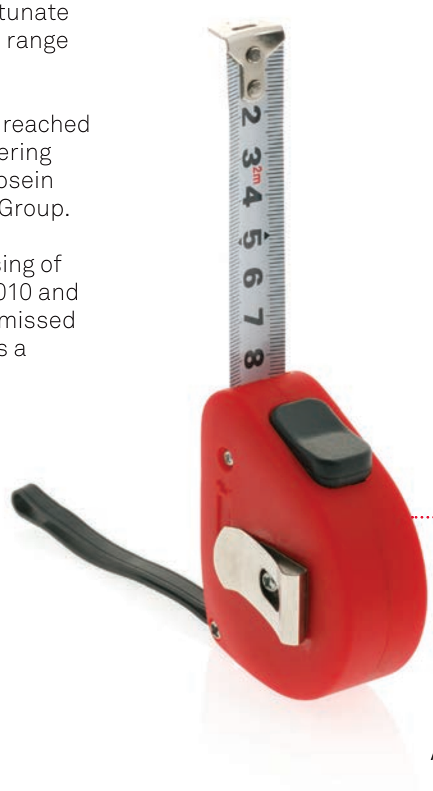
At the heart of Mears lies a strong sense of responsibility towards improving people's lives. We aim to lead the way with social value in the markets where we operate, delivering lasting and meaningful outcomes. During the year we conducted a review of our social value strategy, identifying our key priorities to ensure that we effectively engage with communities and deliver social value on the ground throughout the business, with an effective measurement of the social impact that is created.

We continued to secure Social Mobility Champion status from the Department of Business, Energy & Industrial Strategy. Social mobility is about creating opportunities for young people from disadvantaged backgrounds. At Mears, we aim to make sure jobs and opportunities are open to everyone.

Our people

I commend our employees for their commitment and energy throughout another significant period for the Group and I continue to be impressed by their quality, professionalism and loyalty. Mears has a diverse workforce of circa 15,000 staff including 400 apprentices; the vast majority of our employees live in the areas in which they work.

I look forward to reporting news of our further success during the coming year.



Read more in the governance section on **page 45**

Chief Executive's strategy overview

David Miles
Chief Executive Officer

I am more confident than ever in the quality of our leadership team and our front line people.

Summary

- Our strategy to broaden our service offering in Housing has created a significant sustainable competitive advantage for Mears
- We firmly believe in our long-term Care strategy and that Mears is best placed to benefit from the inevitable market evolution
- We continue to perform well against all of our strategic priorities and are better placed than ever to meet growing client opportunities
- Our commitments to our workforce have never been greater and have included significant investment in training and championing improvements in the pay and conditions of care workers

The 2016 year saw the largest number of new contract mobilisations in our history. Positively, we performed strongly during this period in terms of both delivering excellent customer service whilst also putting in place robust structures and processes that ensure that these contracts deliver both operationally and financially in the future.

Within our Housing division, we have continued to extend our services from our traditional maintenance base to a broader affordable housing offering. Our strategy to broaden our service offering in Housing has created a significant sustainable competitive advantage for Mears. We expect our Housing business to continue to grow through further contract wins. Whilst we are the market leader, we deliver maintenance services to around 15% of the UK's social housing, which provides us with significant headroom for growth. Furthermore, our Housing Management capabilities offer material growth opportunities, as the demand for affordable housing requires that housing providers work harder and smarter to increase the supply of suitable housing through innovation and partnership. We believe the Housing division is well positioned to deliver strong organic growth. Where appropriate, we will continue to make the right acquisitions to develop the breadth and depth of our services.

Our guidance remains unchanged in Housing. We remain on track to deliver annual revenue growth of 5–10% per annum over the medium term and the strong revenue visibility underpins the Board's confidence. We believe we can maintain our Housing margin at its historic normalised range of 5.7–6.0%, assisted by the shifting sales mix towards housing management services, which typically generate a higher operating margin.

We firmly believe in our long-term Care strategy and that Mears is best placed to benefit from the inevitable market evolution. The reduction in revenues, following our exit from around 20% of our existing contracts, has allowed the business to focus on operational quality and switch focus to those strategically important clients which we believe have potential to develop into partnerships and where we are able to deliver a high quality service at sustainable margins. We believe the margin generated by this division can reach similar levels to those of Housing in the medium to long term, however the short term remains more challenging.

Continued funding issues in the care market will create a catalyst for change. Whilst we do not see a strong prospect of immediate fundamental change, we are clear in our view that, increasingly, commissioners will have to look to rebalance their contract estate, focusing on working with fewer, better run, service delivery partners. Moreover, further opportunities will result from localised health related outsourcing. Our market-leading approach to service quality and innovation puts us in a strong position, and as the care market evolves, we expect to benefit disproportionately.

Our dedication to providing our clients with first class service and value remains undiminished and is key to how we manage the business.

Q&A with CEO David Miles

Our client partnerships have never been stronger and are increasingly based on clients purchasing a broader range of services.

How have you performed against your strategic priorities?

We continue to perform well against all of our strategic priorities and are better placed than ever to meet growing client opportunities. We are particularly pleased that 2016 saw the largest number of contract mobilisations ever and that these all went well, giving us a really positive platform for future development. Our client partnerships have never been stronger and are increasingly based on them purchasing a broader range of services from us. Our business has been built on high levels of customer service and 2016 saw another good performance in all areas of our business. I am more confident than ever in the quality of our leadership team and our front line people, given our increasing investment in training and development, backed up by technology enabling us to better deliver and to gain real-time feedback on our performance.

Why has there been such significant growth in housing management services?

In a short space of time, we have become a leading housing management services provider in the UK. There is a huge demand for services that help address the shortage of suitable affordable accommodation. Mears has created a range of innovative solutions that enable homelessness to be addressed cost effectively and for the long term. We are now managing over 9,000 homes nationally, helping Councils reduce their costs and at the same time giving often vulnerable people a decent and stable home environment. This capability has developed following the acquisition of the Omega business in 2014. Since then we have significantly grown the business, invested in structure and expanded our footprint to many places outside of the South East.

Mears has withdrawn from some care contracts. Why is this and will there be more?

We remain optimistic for the long-term prospects for homecare. The decision to withdraw from a contract is only made if a Council is not prepared to pay a rate that allows us to meet our pay obligations to our workforce and our service requirements to our customers. Unfortunately there are some Councils that commission care services at rates that do not allow either of the above and we have decided it is the responsible thing to not deliver homecare in these areas. We continue to lead the market on outcome-based partnering contracts and this is where we will focus our energies going forward. Whilst it is likely that we will withdraw from further contracts, where certain Councils do not feel an obligation to reflect the Living Wage within their costs of care, there are an increasing number of care commissioners who are acting responsibly and balancing their own tight budgets with a realistic understanding of the cost of delivering care. We also expect Government to go further in terms of investment in Social Care. Recent announcements mean that Councils can raise additional funding to support these services in 2017 but Mears and others are of course encouraging the Government to put in place more long-term financing solutions, which we believe must and will happen.

What do you see as the key opportunities for 2017?

There continues to be a good pipeline of opportunities for housing repairs and maintenance services and our leadership position has never been stronger but, in addition, I would highlight three particular areas for 2017. Firstly, Housing Management will continue to see good growth and we expect to see more integrated multi-service contracts, such as the one we have in Milton Keynes. Secondly, given the positive mobilisations in 2016, we do expect these contracts to develop strongly in 2017. Thirdly, given the pressures on the care system, we are seeing more Councils considering outcome-based partnering contracts, this being an area where Mears has also established a leadership position.

How has the Social Value Act impacted on Mears' approach to sustainability and supporting local communities?

Acting responsibly, both nationally and within local communities, has always been a fundamental part of the Mears approach. Our Sustainability Strategy has five guiding principles: long-term customer relationships, excellent employee experience, awareness of the environment, being responsible leaders and ensuring a diverse and inclusive approach to our business. In 2016, we introduced a Social Value Group into Mears with three independent experts. Their role has been to challenge Mears to do more building on its solid foundations (see their report on page 42). We make specific social value commitments to each of our clients, whether this be investment in apprenticeships or using our skills to improve important local facilities for the benefit of the communities in which we operate. Our new Geo-Stat tool allows us to target interventions to specific areas of greatest need, for example where there is an area with a high level of worklessness and social isolation. Our commitments to our workforce have never been greater and have included significant investment in training, championing improvements in care worker pay and conditions and taking a national lead in encouraging more women to consider the building trade for their career.

Read about our strategic priorities on **page 12**

Business model

We focus on long-term outcomes and positive social, economic and environmental impact.

Key resources and relationships

Outstanding partnerships

We work with Local Authority, Housing Association and care commissioner clients. Our end service users are the recipients of housing services and care in the home.

Exceptional people

We recognise our staff as our greatest asset. Mears employees are skilled in delivering an excellent service whilst showing a strong customer service ethos and an empathy for our service users.

Market-leading technology

Our performance is built on a bedrock of first class IT platforms giving market-leading capability and driving innovation.

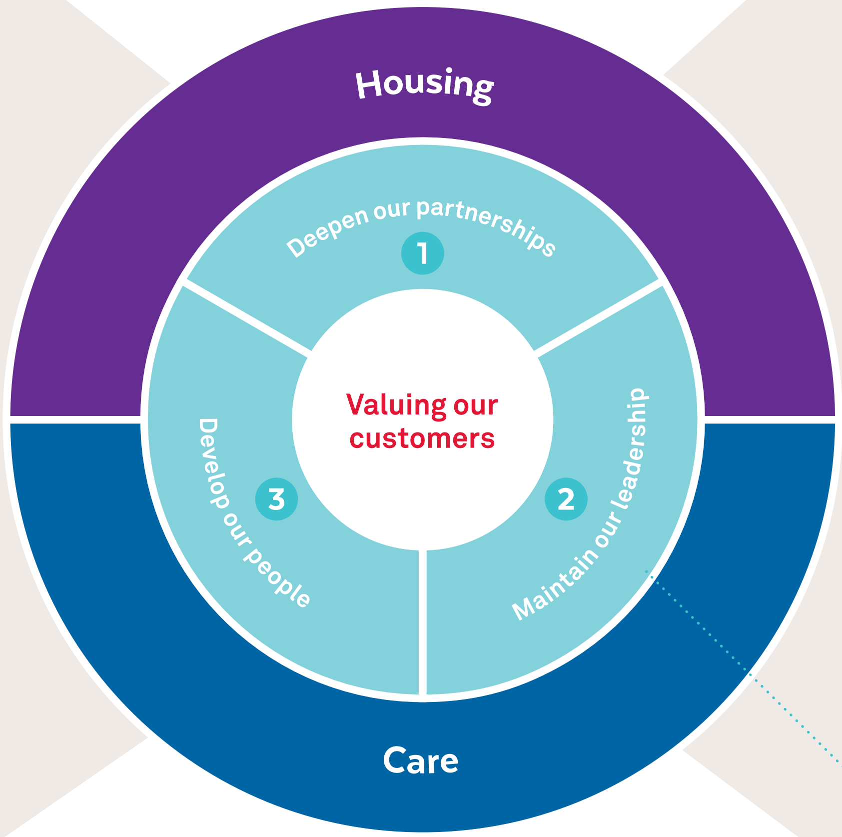
Supply chain partners

We choose suppliers who share our values and meet our standards. We work closely with suppliers to develop innovative services and integrate them with our core systems.

Financial stability

We receive funding through shareholder capital, retained profits, debt and cash generation to run our business and fund its activities.

What we do



How we generate revenue

Mears' revenue is generated from payments from its Local Authority, Housing Association and NHS Trust clients in respect of its Housing and Care services. Whilst the end service users are at the centre of our business model, they do not pay for the service directly.

Read about our revenue breakdown in more detail in the Review of Operations on **page 24**

How are we maintaining our leadership position

How we measure ourselves

We measure ourselves with a suite of KPIs focused upon financial and non-financial measures, mindful of there being multiple stakeholders.

Read more about our key performance indicators on **page 14**

How we reward for our value creation

Our remuneration policy creates an alignment between the creation of value and the remuneration of our Executive Directors and employees.

Read more about our Remuneration Policy on **page 63**

Link to strategy

Our strategic goals sit at the heart of our business model and dictate how we respond to changes taking place in the markets we serve.

Read more about our strategic priorities on **page 12**

Why clients and users choose us

Service delivery
Our service delivery is our key differentiator. We invest heavily in training our people and we are committed to providing them with the skills and equipment to deliver great service. We measure our performance to drive further improvements.

Innovation
The challenge of delivering service improvements at lower cost requires innovative thinking. We create and lead best practice in our markets.

Responsibility, transparency and accountability
Operating our business safely, responsibly and in compliance with regulations is paramount. We have a number of open book arrangements and our clients rightly require a high level of financial visibility.

Social value
Mears defines its responsibilities to society to include social, economic and environmental impact. It takes a proactive approach to these responsibilities and recognises that highlighting the positive difference this makes in communities enthuses staff, motivates customers and clients, creates substantial environmental and social benefits and builds competitive advantage for Mears. This is why Mears refers to its social and environmental activities as "Social Value" – because through these activities it is creating value for Mears and the wider communities in which it operates.

How we create value

Shareholders
We generated a normalised diluted EPS of 30.36p and the proposed dividend for the year increased by 6% to 11.70p per share.

Customers
We maintain over 700,000 homes in the UK amounting to around 6,000 repairs per day. Mears has extended its activities to provide solutions to resolve the challenges of homelessness. Our Care division provides care and support to around 20,000 people, enabling older and disabled people to continue living in their own homes for longer.

Communities
At the heart of Mears lies a strong sense of responsibility towards improving people's lives. We employee over 15,000 people, including around 400 apprentices. We are proud of our Social Mobility Champion status, creating opportunities and enabling people to develop new skills within some of the most disadvantaged and marginalised communities in the UK. Every branch of Mears makes a social value pledge, which focuses on specific activities to improve its local community in at least one of our social value priorities.

Government
In 2016, we paid £4.9m in corporation tax, £78m in payroll taxes and £46m in indirect taxes. In addition, through the services we provide to the public sector, we are delivering significant cost savings and better value to Local Authorities and the NHS.

How we develop our people
Mears is committed to training. We employ over 400 apprentices and provide a number of alternative training solutions for upskilling employees and the professional development of Mears' managers. We are proud to have been appointed as one of only twelve Government Social Mobility Champions working in some of the most marginalised communities in the UK.

Read about our new Rotherham Training Academy on **page 31**

How we manage ourselves

Corporate governance
We are committed to the highest standards of corporate governance, ensuring the safeguard of stakeholders' interests and the long-term success and sustainability of our business.

Read more in the Corporate Governance section on **page 48**

Risk management
Effective risk management is central to the continuing success of Mears. The Board of Directors has ultimate responsibility for ensuring that risk is effectively managed across the Group.

Read more about our risk management and principal risks on **page 18**

Values
Our organisational values shape the way we do business with all stakeholders.

Read more about our social value priorities on **page 36**

Our strategic priorities

Our strategy is to be the market leader in transforming Housing and Care environments.

1 Deepening our client partnerships in both core markets

Performance in 2016

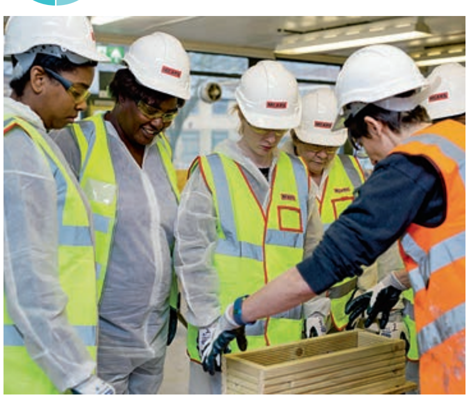
- Record year of new contract mobilisations, in particular our Milton Keynes partnership and Key Worker Housing contract
- Retention of key client relationships in 2016 including Sedgefield and Manchester
- Successful development and introduction of new innovative service offerings such as our partnership with London Borough of Bromley (read more about this on page 25)
- Mears was awarded further contracts by Wiltshire Council following service failure by other care providers. We now deliver around 75% of Local Authority funded care in Wiltshire
- We undertook hundreds of local community projects with our staff and our supply partners often volunteering their time and resources for the benefit of local communities

2 Maintaining quality leadership

Performance in 2016

- 91% of our customers rated our service as excellent
- Re-accreditation with Customer Service Excellence including the Community Engagement standard
- Contractor accreditation for the fifth year running for TPAS (Tenant Participation Advisory Service) for our approach to tenant and customer engagement
- In Care, we have delivered strong regulatory performance in our key Scottish market. Our performance in England has been less consistent, with processes and controls at times falling short of our high expectations
- Increasing commitment by Mears to deliver social value to our clients and communities (read more about this on page 36)

3 Developing our people



Performance in 2016

- During 2016, we opened two new bespoke academies in Rotherham and Brentwood
- We employ 400 apprentices and have been named a Top 100 Apprentice Employer
- We have continued to secure Social Mobility Champion status. Social mobility is about giving young people equal chances in life, regardless of their social background
- Successful delivery of a range of upskilling and professional development for Mears managers and employees together with programmes for young and/or unemployed people from our communities
- In 2016, Mears once again retained its Investors in People (IIP) accreditation

Find out more about our KPIs on **page 14**

Find out more about our risks on **page 18**

Focus in 2017
- Maximise growing opportunities in our Housing Management business
- Focus on Local Authorities adopting partnership-based and outcome-based commissioning in Care
- Continue to raise client awareness of Mears' wide range of services across Housing and Care

Link to KPIs
- Housing new contract success rate
- Order book growth
- Revenue secured
- Revenue growth

Link to risks
- Reputation
- Business continuity

Focus in 2017
- Improve use of technology to improve the way that services are delivered for our customers
- Focus on care quality through better care worker recruitment and retention and continued development of care managers
- Continue to deliver strong regulatory performance in our Scottish Care operation. Improve the consistency of our English Care delivery
- Continue to drive social value, addressing community issues around social mobility, social isolation and fuel poverty

Link to KPIs
- Housing new contract success rate
- Order book growth
- Customer complaints
- Excellent service rating

Link to risks
- Health and safety
- Business continuity
- People
- Reputation

Focus in 2017
- The expansion of our apprenticeship programme in Housing and Care
- The integration of apprenticeships and other qualifications for Care staff
- Management of the CITB levy together with the introduction of the Apprenticeship Levy
- Increased focus on succession planning
- Increased commitment to enhance the terms and conditions of our employees, in particular of carers where the valuable role they play remains undervalued

Link to KPIs
- Housing new contract success rate
- Order book growth
- Revenue secured
- Revenue growth
- Carer churn

Link to risks
- Health and safety
- People

How have we performed?

Our KPIs are our most important measures to monitor our business and to ensure that we are on target to deliver our strategic priorities. Service delivery remains our key differentiator. Our strong contract bidding and financial performance are direct outputs for delivering great service.

Great service delivery

"Excellent" service rating (Housing)

Definition

In order for customers to recommend us, we must deliver excellent service. We randomly conduct around 80,000 customer surveys per year.

Results from the year

91%

We are delighted that our service delivery has remained at the high levels reached in the last two years. Strong performance will ensure competitiveness as we continue to be ranked above our peers.

How we performed

2016 target

91%

On target

2017 target

91%

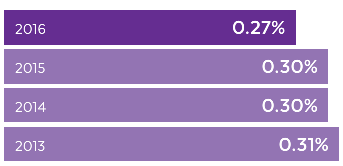
Customer complaints (Housing)

Definition

Incidents resulting from poor service result in a complaint. We are committed to dealing with all complaints on an individual basis.

Results from the year

0.27%



We are committed to providing our colleagues with the skills and equipment to deliver great service. We seek to identify trends in order to improve our overall service quality.

How we performed

2016 target

<0.30%

Out performance

2017 target

<0.27%

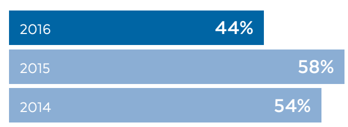
Carer churn (Care)

Definition

The carer churn figure is calculated as the total number of leavers during the year as a proportion of the average carer headcount. Carer churn data is only available from 2014.

Results from the year

44%



There has been some improvement in carer churn rates. We have increased carer pay rates across the business and focused on those Care contracts which provide a better mix of longevity, spend certainty and price, which allows us to offer carers more attractive terms and conditions.

How we performed

2016 target

30%

Under performance

2017 target

30%

Strong contract bidding

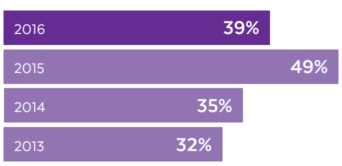
New contract success (Housing)

Definition

Contract success is measured by results of tender by contract value. We typically tender around £1 billion of new opportunities each year. The average contract length is around six years. In order to achieve our organic growth forecasts, we monitor the proportion of new contracts secured as a proportion of total tendered works.

Results from the year

39%



The strategy established two years ago was to provide a broader service offering which includes housing management. We are pleased with our bidding success in 2016, with over £250m of new orders secured. However, the total value of tenders submitted was lower than expected.

How we performed

2016 target

33%

Out performance

2017 target

33%

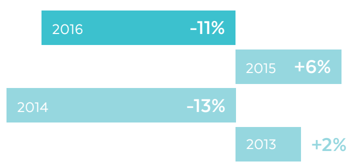
Order book growth (Group)

Definition

Contracts with our clients are long term. Housing contracts average six years and Care contracts average around three years. We only account for contractually secured orders. We anticipate a solid period of new contract bidding in 2017, but would be satisfied to maintain the order book at current levels.

Results from the year

-11%



Following our excellent period of new contract success in 2015, our order book had increased by 6% to £3.5 billion. It was not surprising to see some reduction in 2016, falling to £3.1 billion.

How we performed

2016 target

+6%

Under performance

2017 target

+0%

Secured revenue (Group)

Definition

Secured revenue measures how much revenue is secured in respect of our revenue forecast for the following year. This performance measure is taken at the beginning of each financial year. Government procurement policy means tenders take around twelve months from advertisement to contract award.

Results from the year

93%

We have fallen narrowly short at 93% visibility of 2017 revenues. The time lag in securing and mobilising new works means that it is important that the Group secures the remaining 7% early in 2017. We are in a strong position to achieve forecast revenue.

How we performed

2016 target

95%

Under performance

2017 target

95%

How have we performed? continued

Financial KPIs are critical to measuring and understanding our financial health.

Financial performance

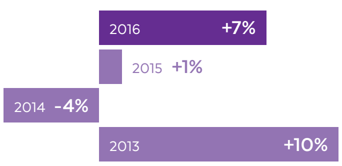
Revenue growth (Housing)

Definition

Revenue represents the amounts due for services provided during the year. In order to measure organic growth, we deduct incremental revenue arising from acquisitions. We believe that organic growth gives a better indication of business performance, as it is a purer aggregation of market growth, success in new contract bidding and contract retention.

Results from the year

+7%



We are pleased to have achieved this target, driven by a very successful new contract success rate in 2015. We continue to invest in our people and systems to provide capacity to achieve our target.

How we performed

2016 target

+6%

Out performance

2017 target

5%

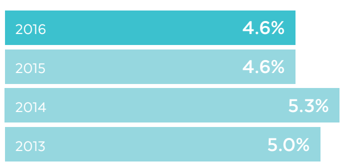
Operating margin (Group)

Definition

Operating margin is the KPI used to measure and understand the profitability of our activities. This KPI is used to continually monitor our costs to ensure services are being delivered efficiently.

Results from the year

4.6%



The Group's operating margin has been diluted in both 2016 and 2015 by the performance of Care. The Housing margin was strong, despite the diluting impact of new mobilisations.

How we performed

2016 target

>5.1%

Under performance

2017 target

>5.1%

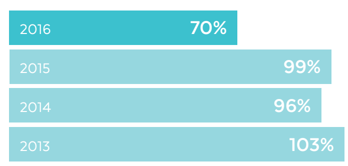
Profit to cash conversion (Group)

Definition

This is a working capital management KPI, which remains the cornerstone of our business. The key measure is cash inflow from operating activities as a proportion of EBITDA. Whilst we internally target 100%, our external target allows some leniency reflecting an increased working capital requirement to fund organic growth.

Results from the year

70%



The solid organic growth delivered in 2016 resulted in some working capital expansion and the increase in trade receivables. The Group also reported a reduction in trade payables due to a changing sales mix. Management is disappointed with this outcome.

How we performed

2016 target

90%

Under performance

2017 target

90%

Read more about our Housing operations on **page 24**

Read more about our Care operations on **page 28**

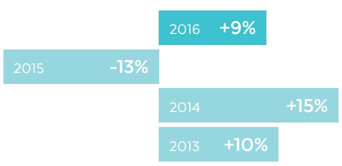
Normalised diluted EPS
(Group)

Definition

Normalised earnings are stated before exceptional costs and exclude the amortisation of acquisition intangibles together with an adjustment to reflect a full tax charge.

Results from the year

+9%



Our headline EPS increased by 9%, mirroring the increase in profits. However, EPS of 30.36p still sits below the equivalent figure of 32.20p reported in 2014 due to the poor trading results delivered by the Care division. We are working hard to improve that position.

How we performed

2016 target

>10-15%

Under performance

2017 target

>10%

Health & safety

Accident frequency rate
(Group)

Definition

Providing our employees with a safe working environment remains paramount. Our accident frequency rate (AFR) is calculated as the number of reportable incidents divided by the number of hours worked, multiplied by 100,000.

Results from the year

0.16

We are pleased to have maintained our accident record at low levels. Mears delivers much of its health and safety training through its in-house registered training provider, which is a key factor in achieving year-on-year improvement.

How we performed

2016 target

<0.17

Out performance

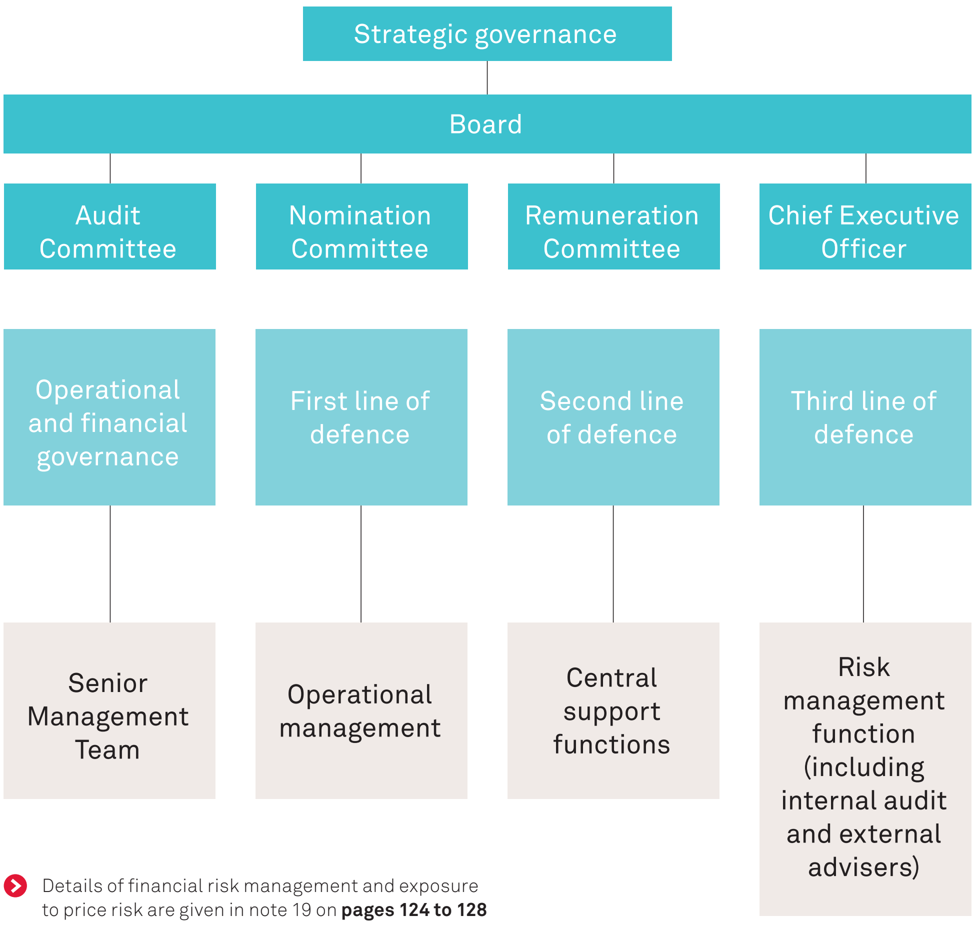
2017 target

<0.16

Risk management and principal risks

Effective management of risks and opportunities is essential to the delivery of the Group's strategic objectives, the achievement of sustainable shareholder value and maintaining good standards of corporate governance.

Risk management process



Details of financial risk management and exposure to price risk are given in note 19 on **pages 124 to 128**

The Senior Management Team

The Senior Management Team reviews and identifies the key risks which may impact upon the achievement of the Group's strategic goals and will consider how these risks are developing with changes in the operations, markets and the regulatory environment.

The nature of the risk is reviewed, including the possible triggering events and the aggregated impacts, before setting appropriate mitigation strategies directed at the causes and consequences of each risk. The risk is assessed in relation to the likelihood of occurrence and the potential impact of the risk upon the business, and assessed against a matrix scoring system which is then used to escalate risks within the Group as appropriate. The Senior Management Team has responsibility for managing the Group's key risks.

The Board

The Board has overall responsibility for determining the nature and extent of risk it is willing to take within the agreed strategy, and ensuring that risks are managed effectively across the Group.

Risk is a regular agenda item at Board meetings and is closely aligned to strategy review.

The Board also reviews reports on the effectiveness of the systems and processes of risk management and internal control.

The Audit Committee

The Audit Committee monitors the Group's key risks identified by the risk assessment processes and reports findings to the Board. It also has delegated responsibility for reviewing in detail the effectiveness of the Group's system of internal control policies, and procedures for the identification, assessment and reporting of risk.

Risk management function

The Group risk function headed by the Group's Chief Risk Officer supports the risk management process by providing guidance and support to management. Group risk also acts as the central point for the coordination and initial review of risk assessment and risk monitoring procedures. To ensure our risk management process continues to drive improvement, the Group risk function monitors the ongoing status and progress of mitigation plans on a quarterly basis.

The Group outsources elements of internal audit and cyber-security, to external advisers.

The control environment is underpinned by a detailed scheme of delegated responsibilities that defines processes and procedures for the approval process in respect of decision making. This ensures that decisions within the organisation are made by the appropriate level of management.

Risk management approach

The Group's approach to risk management is targeted at early identification of risks and mitigation of those risks to reduce their likelihood and impact.

The Group is committed to protection of its assets through an effective risk management process, supported by insurance where appropriate. Examples of assets within scope include human, intellectual, physical property and financial resources.

Reporting within the Group is structured so that key issues can be escalated rapidly through the management team to the Board where appropriate. Risks are continually monitored, contingency plans are provided and this information is reported through established procedures. There is extensive fieldwork undertaken by risk auditors incorporating systems review, branch visits and cross business surveillance.

The internal control approach is designed to manage rather than eliminate the risk of failure and thus can only provide a reasonable, rather than absolute, assurance against material misstatement or loss.

Risk management process

The responsibility for risk identification, analysis, evaluation and mitigation rests with the line management of the businesses. They are also responsible for reporting and monitoring key risks in accordance with established processes under the Group operational policies.

Identified risks are documented in risk registers showing: the risks that have been identified; characteristics of the risks; consequences of the risks; the basis for determining the mitigation strategy; and what reviews and monitoring are necessary. The person(s) accountable for assessing and monitoring each risk is noted.

We continue to drive improvements in our risk management process. We also review our business model, core markets and business processes to ensure that we have properly identified all risks. We continually review our mitigating actions to ensure that they are sufficient to minimise our residual risk.

Key financial and non-financial risks identified by the business from the risk assessment processes are collated and reviewed by the Audit Committee. The financial and non-financial risk registers are reviewed to monitor the status and progression of mitigation plans; the key risks are reported to the Board on a regular basis.

Principal risks

The Board has carried out a robust assessment of the principal risks facing the Group, including those that threaten the business model, strategy, future performance, solvency and liquidity. Risks have been identified as principal based on the likelihood of occurrence and the severity of the impact on the Group, and have been identified through the application of policies and processes previously outlined.

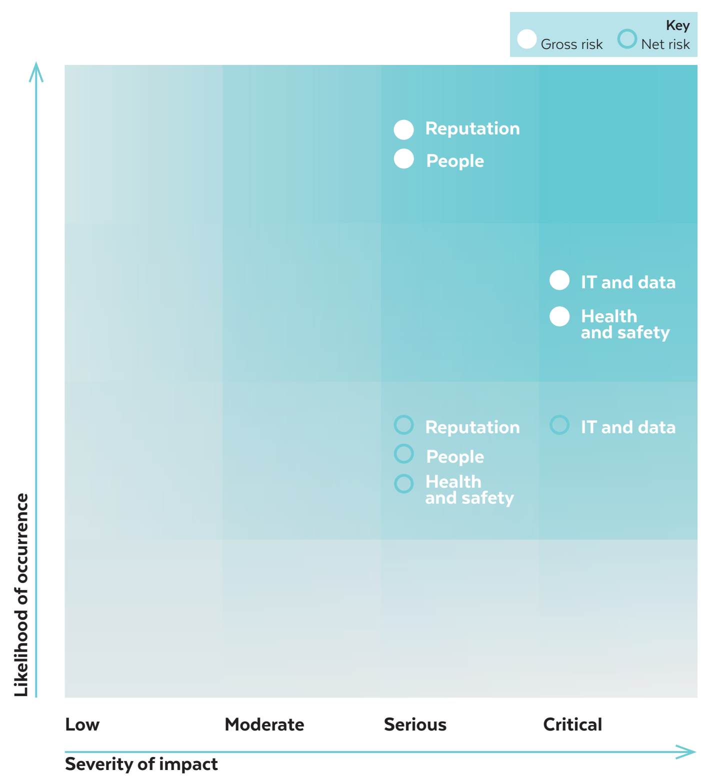
The Board is keen to simplify the reporting of risks, to ensure the risks disclosed to shareholders are those that are considered as business critical or potentially catastrophic. Therefore no additional risks have been disclosed in this Annual Report. These business-as-usual risks are monitored by divisional management.

Prioritising our risks

The Group's risk register rates risks on a matrix scoring system based on their likelihood and potential severity. This severity can be measured using financial, life and limb, customer service, growth, regulatory compliance and reputational criteria. Therefore, Mears measures more than simply the financial impact of the risk. These scores are used to escalate risks and to drive the mitigation plans.

Read more in the Corporate governance section on **page 48**

Read more in the Report of the Audit Committee on **page 56**



Risk management and principal risks continued

Risks are identified as principal based on the likelihood of occurrence and the potential impact on the Group. The Group's principal risks are identified below, together with how we mitigate those risks.

Key risk movements

Each principal risk is considered in the context of how it relates to achievement of the Group's strategic objectives. The risk discussion includes assessment of gross risk and net risk. Gross risk reflects the exposure and risk landscape before considering the mitigations in place, with net risk being the residual risk after mitigations. The gross risk movement from the prior year for each principal risk has been assessed and is presented below:

Mitigations in place supporting the management of the risk to a net risk position are also described for each principal risk.

Reputation

No change

Definition

We recognise that significant commercial value is attributable to the Mears brand.

Poor service delivery would damage our reputation. Both our housing and care markets are close-knit communities where examples of poor performance are quickly communicated widely.

Furthermore, in Care we deliver services to people who are elderly and vulnerable. A service delivery failure within our Care division could result in the physical harm or, in the most extreme cases, death of a service user.

In the environment of caring for vulnerable people, there is a risk of isolated incidents of abuse and neglect which rightly receive significant press coverage with the inevitable reputational damage.

KPIs associated with risk:

- 'Excellent' service rating
- Customer complaints
- Net carer recruitment and retention

Mitigation

- In-house IT system developed to provide operational management with a real-time dashboard of service delivery indicators.
- Internal auditing of KPI reporting including 'mystery shoppers'.
- Strict process in place for vetting and approval of subcontractors.
- We drive a culture of putting our customers first; this is continually reinforced within internal communications.
- Well communicated policy for dealing with press enquiries and incident management.
- Care risk plans for dealing with vulnerable customers.
- Compliance management of bribery and corruption legislation and whistleblowing policy.
- We induct and train all new starters. This induction ensures that all employees understand our values and it reinforces the Group's culture.
- We ensure that staff are properly trained for their roles. We ensure that we deliver relevant training and implement best practice.

People

Decreased gross risk exposure

Definition

The Group employs over 15,000 employees who are critical to the success of our contract performance. Attracting and maintaining good relations with employees and the investment in their training and development is essential to the efficiency and sustainability of the Group's operations. Delivery of strategic objectives increases our ability to attract, motivate and retain talent.

In addition, the Care division is facing a challenging environment where the ability to recruit and retain carers is restricting performance.

KPIs associated with risk:

- 'Excellent' service rating
- Customer complaints
- Carer net recruitment and retention

Mitigation

- We induct and train all new starters. This induction ensures that all new employees understand our strategy, vision and values. All Care staff have access to NVQ training.
- We regularly review and benchmark our remuneration packages to ensure that they remain competitive.
- In Care, we are investing in an innovative recruitment process to ensure an increase in the volume and quality of carers. Local Care branches are targeted on a monthly basis in the areas of recruitment and retention.
- At the senior end of the business, we have increased our focus on succession planning and increased our investment in senior management development. Our Senior Leadership programme has identified a cross-section of the Group's brightest talent that we would envisage will play central roles in our future business.
- The investment in an in-house dedicated training division to provide a range of employee development services through two academies in Rotherham and Brentwood.
- An annual appraisal process is completed for all employees to ensure that all people receive feedback in respect of their performance and to identify future training and development requirements. We hold a national accreditation as an Investor in People.
- We are continually looking to improve our position as an employer of choice by improving the level of engagement with our employees through formal communications, awards to recognise success, local events and family fun days.
- We are continually monitoring our future skills requirements.
- We regularly undertake employee surveys to gauge employee satisfaction and engagement, and any barriers to high level performance.

Health and safety

Increased gross risk exposure

Definition

Prevention of injury or loss of life for both employees and customers is of utmost importance. In addition, it is vital to maintaining the confidence our customers and clients have in our business.

KPIs associated with risk:

- Accident frequency rates
- Reportable incidents
- Customer complaints
- 'Excellent' service rating

Mitigation

- Significant investment in the centralised health, safety and environment (HSE) function to maintain consistency and quality.
- We have comprehensive safe systems of work which are well communicated through a robust and coordinated internal training regime.
- We have robust processes for inducting new staff to ensure importance of health and safety is emphasised together with detailed method statements for working safely.
- Regular HSE training and updates are held, predominantly delivered by the internal function.
- Independent review of health and safety cases by insurers where recommendations of change are implemented.
- Internal Health and Safety auditing takes place using third party validation.
- Annual Group Health and Safety strategy and plan are produced.

IT and data

Increased gross risk exposure

Definition

A major incident or catastrophic event could impact on the Group's ability to trade. In addition, it is essential that the security of customer, employee and Company confidential data is maintained. A major breach of information security could have a major negative financial and reputational impact on the business. The risk landscape of IT and data is constantly increasing with deliberate acts of cyber crime becoming more sophisticated and frequent across all markets.

Mitigation

- The Business Continuity Plan is constantly reviewed and frequently tested to ensure it is fit for purpose.
- Business continuity and IT disaster recovery management resource is convened at short notice to manage the response and any associated risk to the Group.
- Various information security policies and standards are in place with a focus on network security, access controls, encryption, system security, data protection and information handling.
- Information security penetration is externally tested to identify improvement recommendations which are then implemented.
- Data Security Committee in place to monitor and review both physical data security and IT data security.

Viability statement

The Group has a broad spread of customers – our largest client constitutes less than 7% of Group revenues which, while significant, would, in the event of its loss, not impact on the Group's wider viability.

Business planning and financial viability

In accordance with C.2.2 of the UK Corporate Governance Code 2014, the Directors have assessed the viability of the Group over a five-year period. A period of five years has been chosen as it reflects the average contract length of five years. Whilst the Group holds contracts which extend beyond this time horizon, a period of greater than five years is considered too long, given the inherent uncertainties involved.

The Board considered its key risks. The principal risks are set out on pages 18 to 23 and the most relevant of these risks to viability were considered to be:

- a service delivery failure, possibly resulting in the death or harm of a service user, with significant negative publicity and long-term reputation damage;
- deterioration in carer churn rates and poor recruitment practices resulting in a material reduction in carer numbers, sales volumes and profitability;
- a health and safety failure resulting in serious personal injury or death of an employee or service user, leading to significant financial penalties and significant reputation damage; and
- a failure in our IT systems, impacting upon our ability to deliver our services. We provide services to vulnerable people and even a short period of downtime could cause severe reputation damage. A serious system failure could have significant impact on invoicing our customers and collecting cash.

A financial model has been built on a contract-by-contract basis for the next twelve months and extended on a business-by-business basis for the following four years. The five-year plan considers cash flows as well as financial covenants. Consideration was given to a number of key assumptions, namely future revenue growth, operating margins and working capital management. The assumptions set were considered conservative given the focus of the model is in respect of underperformance. Sensitivity analysis was undertaken to stress test the resilience of the Group and its business model to the potential impact of the Group's principal risks, or a combination of those risks. The Board overlaid the potential impact of the principal risks which could affect solvency or liquidity in 'severe but plausible' scenarios.

Two scenarios were modelled. The first scenario assumed a significant business failure within the Housing division. The model assumed a 6% per annum compound reduction in revenues for each year within the five-year plan, a total reduction of 22%. This was combined with a 1% deterioration in the Housing gross margin which, when combined with an under-recovery in central support overheads, resulted in a reduction in Group net profit margin from 4.3% to 3.0% in year five of the model.

The second scenario assumed a similar failure within the Care division. The model assumed a 15% per annum compound reduction in revenues for each year within the five-year plan, a total reduction of 50%. This was combined with a 2% deterioration in the Care gross margin which resulted in a Care operating loss of £4.3m in year five of the model but no reduction in Group net profit margin in the reducing materiality of Care in this scenario.

Both scenarios showed that the Group would remain viable even in the event of a severe business failure over an extended period. No mitigating actions were included within either scenario, which was considered conservative albeit not entirely realistic.

Whilst the Group's continuing operations are entirely based in the UK, the large network of branches does reduce the risk of serious business interruption. In addition, the Group has a broad spread of customers – our largest client constitutes less than 7% of Group revenues which, while significant, would, in the event of its loss, not impact on the Group's wider viability.

The Board has recently completed an 'amend and extend' of the Group's revolving credit facility which now runs to July 2020. The Board has considered the Group's ability to renew the existing debt facilities in July 2020 and believes that the Group has a high level of comfort that replacement sources of funding will be available at that time.

The Board also considered the impact of Brexit on the business activities and does not envisage any significant negative effect impacting on the Group's viability.

The Board accepts that uncertainty of results increases as the projections cover a five-year period. However, the Board concluded that there was a reasonable expectation that the Group will continue in operation and would be able to continue to meet liabilities as they fall due over the five-year period of business planning.

Key risks impacting upon viability and delivery of our strategic priorities

Reputation

Service quality remains our key differentiator and underpins our future viability.

→ **Customer excellence rating**

91%

(2015: 91%)

People

We have over 15,000 employees; the majority of these are interacting with our customers on a daily basis. It is this day-to-day contact which is fundamental in delivering a differentiated service and high levels of satisfaction. It is imperative to Mears' viability that the Group's strategic goals are well communicated and understood by all employees.

→ **Customer complaints**

0.27%

(2015: 0.30%)

Health and safety

Mears' services and operations involve a series of high risk activities, ranging from dealing with vulnerable customers in need of care, to our building related services, such as working at height and working with gas and electricity.

→ **Accident frequency rate**

0.16

(2015: 0.17)

The Board reviewed the Group's viability in terms of both its financial viability and its ability to achieve its strategic goals.

Our strategic priorities **page 12**

Effective risk management underpins the Group's long-term viability.

Risk management and principal risks **page 18**

Review of operations

Summary

→ The Housing business has continued to deliver excellent financial performance.

→ We have positioned ourselves to provide a broader service offering to a market where we are seeing an increasing blurring of the boundaries around social, affordable and private rented housing.

→ The Group has made significant progress in rebalancing its portfolio of Care contracts to focus upon those which have a better mix of longevity, spend certainty and price.

→ In Care, whilst we have become increasingly selective in new contract bidding, it is pleasing that we have enjoyed a particularly buoyant period for winning new work.

	2016			2015		
Operating segments	**Housing £m**	**Care £m**	**Total £m**	Housing £m	Care £m	Total £m
Revenue	**787.5**	**152.6**	**940.1**	735.1	146.0	881.1
Operating result*	**44.1**	**(1.2)**	**42.9**	42.4	(1.6)	40.8
Operating margin*	**5.60%**	**(0.79%)**	**4.56%**	5.77%	(1.10%)	4.63%

* Pre amortisation of acquisition intangibles and long-term incentive plans.

Housing

Mears has quickly become the leading provider of housing management services to the public sector, delivering a range of innovative and unique solutions.

The Board is very pleased with the progress made by our Housing division, where we have positioned ourselves to provide a broader service offering to a market where we are seeing an increasing blurring of the boundaries around social, affordable and private rented housing. Whilst we have increased the depth and breadth of our capabilities, we place particular emphasis upon ensuring that our wide spectrum of core skills is delivered from the individual operating unit, which is important given the increasingly complex housing challenges being faced by our clients.

The Housing business has continued to deliver excellent financial performance with revenues of £787.5m (2015: £735.1m), an increase of 7% reflecting a particularly busy period of new contract mobilisations. Our operating margin of 5.6% (2015: 5.8%) reflects some dilution given this high number of new contract mobilisations. Typically, the Group anticipates a lower margin from a new contract during its mobilisation phase, being a time when the primary focus is in investing resources to establish excellent customer service. Having reported an operating margin of below 5.0% in the first half year, it is pleasing that operating margins normalised during the second half of the year.

The Housing division has secured new contracts of over £250m, with a contract win rate on competitively tendered works of 39% (by value) (2015: £900m and 49%). Following a significant period of new contract awards in 2015, in the past year we have focused our attention upon existing contract renewals, notably Sedgefield and Manchester, both of which I am pleased to confirm have chosen to continue their existing relationship with Mears. We were also successful in extending our relationship with Gateshead, although the maintenance will now follow an insourcing solution.

Whilst we focus upon a single Housing division, the following provides a breakdown of the revenue streams:

	2016 £m	2015 £m
Maintenance	**602.0**	589.0
Regeneration	**86.0**	98.4
Housing Management	**99.5**	47.7
Total Housing revenues	**787.5**	735.1

Maintenance

The Housing division saw maintenance revenues increase to £602.0m (2015: £589.0m). Organic growth of 2% underplays the level of activity in this area. Whilst our historic record of contract renewals is strong, we were disappointed to report, in early 2016, the loss of our flagship contract with Birmingham City Council following a competitive retender, a contract with annual revenues of some £28m. However, it was pleasing to report overall growth in 2016 despite the loss of such a significant contract. The majority of new contract awards commenced in April 2016 and as such only nine months' trading is reflected in the 2016 trading numbers. Notable contract activities include:

→ Mears forming a new joint venture with Milton Keynes Council called YourMK, focusing upon the regeneration of key areas in Milton Keynes. The contract, which mobilised in April 2016, initially delivered repairs and maintenance services to nearly 11,500 homes but has since enjoyed a significant extension to the scope of works. This contract is valued at £250m.

→ Mears' success in resecuring its Sedgefield contract, delivering responsive and planned maintenance to approximately 8,500 homes, which is valued at £110m over the ten-year contract term. This is a contract renewal, with the original contract having been awarded in 2008.

→ Mears being re-awarded with a multi-service contract with Manchester City Council on its own behalf and on behalf of Northwards Housing. The contract is for day-to-day repairs and maintenance including void property and general building works to Northwards Housing managed stock and leasehold properties and to Manchester City Council managed hostels, shared houses and residential dwellings. The contract is valued at £31m over its initial four-year term with potential to increase to £78m, subject to extension, over its full ten-year term.

Revenue

£787.5m +7%

2016	£787.5m
2015	£735.1m
2014	£714.7m

Operating profit

£44.1m +4%

2016	£44.1m
2015	£42.4m
2014	£34.4m

Operating margin

5.6%

2016	5.6%
2015	5.8%
2014	4.8%

See note 1 to the financial statements.

CASE STUDY: HOUSING

Joint venture tackles homelessness

Homelessness is a growing problem, especially in London, and increasingly councils are looking for innovative ways to fulfil their duties to vulnerable households.

More than 1,000 households in Bromley are in temporary accommodation – in many cases this means costly B&Bs, as there is not enough suitable accommodation to meet demand.

A new joint venture between the London Borough of Bromley and Mears, named More Homes Bromley, will see Mears purchase and refurbish 400 properties to the Decent Homes standard and manage them on behalf of the council.

The £80m landmark venture is funded by BAE Systems Pension Funds.

Investors gain a return on their investment while the Council stands to save substantially on B&B costs over the long term.

Review of operations continued

Regeneration

The Housing division saw capital work revenues reduce to £86.0m (2015: £98.4m). Whilst the level of spend on one-off refurbishment projects has reduced, we are seeing a high number of new development opportunities with existing customers. During the last twelve months, Mears has broadened its service capability to include the provision of new build services through our supply-chain partnerships, primarily targeting our existing Housing clients. Mears is not a property developer or general builder; rather, we will use our entire portfolio of services to provide a more integrated solution which enhances our focus on managing assets for the benefit of owners and client public sector bodies. We see this as a growth area for our Housing division; however, during this transitional period, the new development opportunities have not generated sufficient revenues to replace the reduction of refurbishment works. Notable contracts secured during the period include the following:

- → Further to the long-term maintenance works that we are delivering for our Welwyn and Hatfield Council client, we have been engaged to develop 29 affordable rented homes on a brownfield site. The works are valued at £5.6m and the contract is due to complete at the end of 2017. Mears will take over the long-term maintenance of these new homes, giving a seamless solution to the housing requirements of Welwyn and Hatfield Council.
- → Mears' success in securing the joint venture with Milton Keynes Council, which saw the commencement of repairs and maintenance services in April 2016, has already seen the scope of works expanding. Mears has been engaged to develop 80 new homes spread across seven infill sites around the city. These homes will be for affordable rent, once finished, with a contract value of approximately £11m. Site work commenced during the first quarter of 2017 and will complete in early 2018.

Housing Management

The Housing division saw Housing Management revenues more than double to £99.5m (2015: £47.7m). This business stream is seeing significant growth opportunities with an annual revenue run rate now at around £120m. Mears has quickly become the leading provider of housing management services to the public sector, delivering a range of innovative and unique solutions. The innovative nature of these propositions has meant that much of the work has been secured without the requirement for an extended, competitive tender process. We expect this to be a continuing trend.

- → Mears mobilised a Key Worker Housing contract providing a full housing management service throughout the UK. This includes sourcing properties, managing the application and allocation process as well as the subsequent day-to-day administration. The contract, which fully mobilised in April 2016, is valued at over £160m over the initial three-year term.
- → Mears has been engaged by the London Borough of Bromley (Bromley) to arrange the purchase and refurbishment of 400 homes currently under private ownership. The key aim is to provide Bromley with an alternative, affordable housing supply to replace the significant bed and breakfast accommodation costs currently incurred by Bromley. Mears has engaged funding partners to finance the purchase of properties on behalf of the client. We will then carry out refurbishment works and act as managing agent for the portfolio. The contract will be operated by Bromley and Mears for up to 40 years and is valued at circa £50m. The operation mobilised in February 2016, and the purchase and refurbishment phase will continue over a period of 24 months. This is typical of a number of opportunities within the pipeline.
- → Mears has entered into a contract with Safe Haven, a charity which acquires homes to use as temporary accommodation for the London Borough of Ealing. Safe Haven owns around 200 homes with a clear plan to increase this number to 400. Mears is engaged, over an initial 20-year term, to carry out all housing management services, including an initial refurbishment programme, so that the homes will now be a long-term affordable housing provision.

Our strategy

We have maintained a consistent strategy across Housing over a long period:

1 Focus on delivering a high level of customer service

We have continued to maintain high levels of customer satisfaction. Over 90% of tenants regard our services as excellent.

2 Drive innovation to provide better outcomes for tenants

Successful development and introduction of new partnership models such as our joint ventures with Milton Keynes Council and the London Borough of Bromley.

Our service delivery is supported by our internally developed IT systems underpinning our capabilities and driving innovation.

3 Evolve the breadth and depth of our service offering

We have, over recent years, extended our Housing offering from our original maintenance offering to full maintenance, regeneration and housing management capability. In addition, Mears provides solutions for clients who wish to insource their maintenance services.

- Mears, through its Registered Provider of Social Housing, and HB Villages are working in partnership to create a new supply of purpose-built accommodation for the Care sector. The objective is for HB Villages to develop and fund the new housing with Mears providing long-term tenancy and asset management services to the residents. The first scheme in Northampton is for an 80-home extra care complex, with Mears providing both housing management and care services.
- Mears completed a transaction with Chapter 1 Housing Association for the management of 900 homes in the South and West of England. Following a strategic review by Chapter 1, this form of private sector leased property for homeless families was considered non-core, and they searched for a partner that could ensure a continuity of a quality service. This arrangement also introduced Mears to a further twelve Local Authorities and Mears will look to extend its service offering to those new customer relationships.

CASE STUDY: HOUSING

Empty homes – improving neighbourhoods

With a severe shortage of affordable homes in the UK, empty properties represent a significant waste of resources and a missed opportunity for meeting the housing needs of communities across the country.

Bringing long-term empty properties and redundant commercial buildings back into use is much more cost effective than building new properties to tackle the shortage of affordable homes, and also improves neighbourhoods.

Mears works with several Local Authorities in London, Luton and the South East to revitalise empty properties and provide ongoing management and maintenance.

In the London Borough of Newham, Mears was selected as the preferred partner to refurbish, let and manage 185 flats and houses in 2011, this has risen to over 270 properties. The annual savings to Newham are expected to be in the region of £1.5m.

Mears has also worked with:

- London Borough of Hounslow – 40 unit hostel
- London Borough of Sutton – 40 self-contained units
- Luton Borough Council – 54 Room Hostel
- Rushmoor Borough council – 45 self-contained units

Other customers include London Borough of Enfield, Circle Housing Group and East Thames Housing Association.

4 Focus on building sustainable, long-term partnerships

During 2016, we retained a number of key client relationships including Sedgefield and Manchester.

Our broader service offering is enabling us to generate multiple revenue streams from single client relationships.

5 Invest in the workforce to ensure that it is both motivated and well trained

We invest in extensive training and development of staff at all levels. We have recently opened National Training Academies in both Rotherham and Brentwood. We are one of only twelve UK companies who have been recognised by the Government as a Social Mobility Champion. This is for our work in creating opportunities for people from disadvantaged backgrounds. We employ over 400 apprentices.

6 Primarily focus upon organic growth

Given our broad capabilities, our primary focus is on organic growth. We continue to consider bolt-on acquisitions to reinforce our leadership position.

Review of operations continued

CASE STUDY: HOUSING

YourMK joint venture partnership

YourMK, the partnership between Milton Keynes Council and Mears, came into existence on 1 April 2016. YourMK is responsible for the strategic asset management of around 11,500 council-owned properties and leading the regeneration programme in Milton Keynes.

Since April, the operational team has completed around 25,000 jobs, with 99% completed within the 28-day target. They have reduced the void turnaround from 16 days to ten, and achieved an average customer satisfaction score of 96.5%.

In addition, YourMK is leading the affordable housing building programme for Milton Keynes Council and is currently working with Mears on five sites, with potential for considerably more in the pipeline.

The five-year business plan – detailing where regeneration and related work will begin, plus the planned works programme aligned to the business plan – will be published in spring 2017.

Completed over
25,000
jobs, with over 99% completed within the 28-day target

Customer satisfaction score
>95%

Care

The Group has made significant progress in rebalancing its portfolio of Care contracts to focus upon those which have a better mix of longevity, spend certainty and price.

Revenues for the Care division were £152.6m (2015: £146.0m), reflecting the full-year impact of the Care at Home acquisition. The Care division reported a loss of £1.2m (2015: £1.6m), broadly in line with management expectations and reflecting the continued challenges of homecare and the additional costs incurred in restructuring our Care activities.

The Group has made significant progress in rebalancing its portfolio of Care contracts to focus upon those which have a better mix of longevity, certainty of spend and price. The Group entered 2016 with the imminent introduction of the National Living Wage (NLW) hanging over the Care sector with an increase in the National Minimum Wage from £6.70 to £7.20 per hour from April 2016. In addition, the Scottish Living Wage (SLW) signposted an increase from £6.70 to an enhanced £8.25 per hour, which further impacted on around 25% of our Care operations. Whilst the majority of care providers were very supportive of the principle of paying carers a rate that is more reflective of the crucial role that they deliver, the additional pressure on clients' already overstretched budgets brought significant uncertainty as to how this additional cost would be funded. The Government has continued to provide some short-term relief, allowing Local Authorities to levy a new social care precept of up to 2% on Council tax, with the money raised to be spent exclusively on adult social care. In addition, the Spring Budget 2017 committed a further £1 billion of additional funding to 2017/18 that will go some way to preventing an immediate collapse but does not represent a long-term solution.

During the second half of 2015, and running into 2016, we carried out a detailed review, on a contract-by-contract basis, of charge rates and care worker pay rates. The process placed particular focus upon managing the impact of the NLW and also identifying more effective solutions to the sourcing and retention of sufficient, good quality, care workers. Pleasingly a large number of care commissioners have shown a deeper understanding of the true underlying cost of delivering care. This has resulted in an increasing acceptance that the NLW only really represents a legal minimum, and that one cannot expect to recruit individuals to deliver homecare, and to accept the responsibilities that go with this role, at this minimum rate. It remains a key part of our long-term strategy to see care workers properly recognised as the skilled workers they undoubtedly are.

In aggregate, Mears enjoyed an increase in charge rates of circa 7% within England and Wales and around 15% in Scotland, which is generally in line with the increase in our carer payroll cost and is better than the average increase given to providers across the sector. The outcome of our review has highlighted those care commissioners who we believe, in the medium term, have little desire to change their commissioning strategies and where there is little likelihood of contract pricing that will allow providers to deliver care responsibly. This outcome led us to carry out a substantial restructuring of our Care division, which has seen a reduction in our Care activities by some 20%, a significant proportion of which arose within the North of England, which has the lowest charge rates and more traditional procurement methods. The initial round of branch closures was substantially completed in 2016. Further refining has taken place since the end of the year, seeing Mears withdraw from Northern Ireland and a number of Midlands-based contracts.

CASE STUDY: CARE

Help to live at home

Mears' partnership with Wiltshire Council to deliver the innovative Help to Live at Home care service has extended to cover six of the county's eight areas.

The new contract is worth £80m over four years, with the option to extend for a further two years.

Help to Live at Home takes a different approach to homecare, getting away from the traditional 'time and task' model, focusing instead on what people want from their care based on outcomes.

Outcomes-based commissioning aims to help people regain independence and prevent them from needing longer-term care.

In the first three months of operating the new areas, Mears was able to grow the amount of work delivered by 17%, helping to reduce the rising pressures on health and social care.

Mears already successfully runs the service in the South of the region and the new contract extends the service in the East, West and much of the North of the county.

New contract value

£80m

over four years

Revenue

£152.6m +5%

2016	£152.6m
2015	£146.0m
2014	£124.0m

Operating profit

£(1.2)m +25%

2016	£(1.2)m
2015	£(1.6)m
2014	£9.6m

Operating margin

(0.8)%

2016	(0.8)%
2015	(1.1)%
2014	7.8%

See note 1 to the financial statements.

Review of operations continued

A summary of the changing volumes and charge rates as a result of the refocusing of our Care activities is detailed below:

	Hours per week	Annualised revenue £m	Charge rate per hour £
As at 1 January 2016*	216,000	148.1	13.19
Contract closures	(48,200)		
Material new contract awards	9,100		
Other net volume decrease	(15,500)		
As at 31 December 2016	**161,400**	**126.2**	**15.04**

* Includes contracts under notice of termination as at balance sheet date.

Whilst we have experienced significant downsizing in certain geographic areas, we are experiencing a solid pipeline of good quality bidding opportunities. In addition there are growth opportunities with the majority of our remaining clients.

Whilst we have become increasingly selective in new contract bidding, it is pleasing that we have enjoyed a particularly buoyant period for winning new work, securing over £200m of contract wins at a win rate of 74% by value (2015: £80m and 63%). More importantly, the quality of the new orders secured is much improved, enjoying a significantly higher charge rate, which enables us to reflect this within our carer pay and conditions. The average contract lengths of these latest awards has increased to in excess of five years and the number of providers reduced significantly, which reflects the trends which we anticipated and should in the future result in a better quality of earnings from our Care activities. Notable wins include:

- a contract with Devon County Council for the provision of homecare services. The contract is for an initial five-year period with an option to extend for a further two years and is worth over £100m. Mears is acting as the lead provider partner in four geographic areas across the South of Devon and is responsible for organising and delivering personal care services in that area, predominantly coordinating and supporting the local SME providers. The contract commenced in July 2016;
- further contracts by Wiltshire Council, as lead provider within zones in the North and West regions of the county, to add to our existing work in the South and East. The new contract, which is valued at around £85m over its six-year term, means Mears is the prime provider for the significant majority of this work across the county, doubling its previous value of work. The new contract commenced in August 2016;
- the renewal of our existing Care contract with the London Borough of Richmond, a client with whom we have enjoyed a long-standing relationship. The new contract, which commenced in July 2016, is for six years and will see us doubling our sales volume; and
- being re-awarded its existing Care contract with Aberdeenshire Council, delivering a wide spectrum of homecare and supported living services to people with complex needs, including autism and mental health. The contract has increased our provision to 4,000 hours of support per week.

The main limitation to achieving growth in Care and to delivering a consistent, good quality service, remains the sourcing and retention of sufficient care workers of good quality. Whilst we have experienced some improvement in carer turnover during the year, with churn rates falling by 14%, this still remains at unsustainable levels. We remain committed to driving improvement to the conditions of care workers, including better financial rewards and incentives and a more formalised career pathway.

Our annual survey of staff also showed a significant increase in job satisfaction, reflecting the effort we have put into making Mears the place to work for care staff interested in developing a career in the sector.

We are pleased to see the various UK regulators implementing tougher standards around quality, which will play to our strengths. We are particularly pleased with our regulatory performance in our key Scottish market and, while we have seen some pressure points in England, our processes and controls continue to improve.

Our strategy

We have maintained a consistent strategy across Care over a long period:

1 Focus on delivering a high level of customer service

We achieved Customer Service Excellence accreditation for our Care division, which adds to our existing accreditation for housing services.

We have delivered excellent regulatory compliance in Scotland. We are working hard to improve the consistency of our service delivery in England.

2 Drive innovation to provide better outcomes for service users

Our Wiltshire contract is very much the flagship for the development of outcome-based working, as opposed to the traditional care focus on task and time. Within Wiltshire, all care plans are written based upon achieving specific outcomes for individual service users. We anticipate more clients commissioning care in this way.

3 Evolve the breadth and depth of our service offering

Increasing integration of NHS and social services is growing the number of people with more complex conditions who need care at home. Complex care covers services such as spinal injury treatment, head injury treatment, end of life care, dementia care and learning disability support.

There has never been greater stakeholder pressure to increase funding into social care, including from organisations such as the NHS, which has really been feeling the impact of the underfunded social care system. Mears is playing its part in encouraging additional investment to be made and the additional funding secured from the Spring Budget 2017 and Council tax increases is positive. Mears is widely recognised now as the organisation in homecare that is doing the most to drive change, which we believe is a real positive for the long-term development of our business.

CASE STUDY: HOUSING

National Training Academy

Mears opened our new national Training Academy at the New York Stadium in Rotherham, running courses on plumbing, electrics, roofing, carpentry, joinery, plastering and painting and decorating.

The Training Academy delivers accredited apprenticeships for those starting a career in construction or repairs and maintenance, as well as providing training for those currently working in the trades.

The Training Academy is our national training facility which also operates a training academy in Brentwood, Essex.

The Training Academy also supports unemployed young people and adults of all ages and sexes to gain skills for employment. This includes a new business and management school and, in the future will offer purpose-designed courses and services to our clients.

During 2016, Mears recruited over

100

new apprentices

4 Focus on building sustainable, long-term partnerships

We are increasingly selective in bidding for new contract opportunities. Our recent success in being awarded five-year contracts with both Devon County Council and Wiltshire Council is reward for this. These contracts are secured at rates which allow us to recruit a workforce delivering high quality care.

5 Invest in the workforce to ensure that it is both motivated and well trained

We have agreed new minimum pay levels for our staff which are set ahead of NLW. We are also investing further in training and a range of other benefits. We believe this investment is fundamental in helping reduce the staff churn rate.

It is central to our strategy that care workers are properly recognised as the skilled workers they are.

6 Focus upon organic growth

With the current challenges in Care, we are entirely focused upon developing our Care offering organically. Whilst we continue to have aspirations to grow the business, our focus in the short term will be on quality and we may see some reduction in size.

Financial review

Andrew Smith
Finance Director

We operate in a high volume, low value and low margin environment where we have delivered consistent financial results over an extended period of time.

Summary

Earnings

The normalised diluted EPS, which allows for the potential dilutive impact of outstanding share options, increased by 9% to 30.36p (2015: 27.94p).

Dividend

The Board has recommended a final dividend of 8.40p per share which, when combined with the interim dividend, gives a total dividend for the year of 11.70p (2015: 11.00p), a 6% increase, reflecting the Board's confidence in the underlying performance of the Group.

Cash

The efficiency with which the Group manages working capital remains a cornerstone of our business. The Group's conversion of EBITDA to cash in the year was below target at 70% (2015: 99%). The solid organic growth delivered in 2016 resulted in some working capital expansion and the increase in trade receivables reflects this.

Group revenue
£940.1m
(2015: £881.1m)

Dividend per share
11.70p
(2015: 11.0p)

Group operating profit*
£41.9m
(2015: £38.7m)

Cash conversion
70%
(2015: 99%)

* Before acquisition intangible amortisation.

This provides further key information in respect of the financial performance and financial position of the Group to the extent that this is not already covered within the Review of Operations.

Acquisitions

Having completed a number of significant acquisitions in recent years, notably the Care at Home division of Care UK in 2015 and the Omega Group in 2014, the past year was focused upon consolidation and organic growth with no new acquisitions completed in the period.

Contingent consideration of £10.0m was paid during the year, relating to the previous acquisition of Omega. A further payment of £5.0m has been paid in the early part of 2017. The Directors believe it is highly probable that the full contingent consideration will be paid, with the final instalment of £5.0m therefore anticipated in January 2018.

The acquisition of Omega included an interest in 50% of the share capital of three jointly owned entities. During 2015, the Group increased its holding to 75% in the year for a cash consideration of £6.1m. Mears has agreed a forward purchase agreement to acquire the remaining 25% for consideration of £6.1m in January 2018.

Discontinued activities

In November 2013, the Group completed the disposal of the entire share capital of Haydon Mechanical and Electrical Limited ('Haydon UK'). As part of that disposal, the Group retained the beneficial interest in 49% of the share capital of an investment in a company registered in the United Arab Emirates, Haydon Mechanical and Electrical Company LLC (Haydon LLC). This beneficial interest was retained due to a number of performance guarantees in place at the time of the disposal which would unwind as the underlying contracts were completed. During the year, the Group reduced its interest to 1% of the share capital in return for a nominal consideration. At 31 December 2016, a balance of £3.3m was due from Haydon LLC to the Group. Upon the remaining guarantees being satisfied and the outstanding debtor settled, the Group is in the process of transferring the remaining share to the local management.

In the year, the Group made a full provision against all remaining amounts due from Haydon UK. This was balanced with an operating profit generated by Haydon LLC in the period leading up to its disposal. Accordingly, the net impact on the profit for the year was zero.

Amortisation of acquisition intangibles

A charge for amortisation of acquisition intangibles of £10.7m (2015: £10.8m) arose in the year. This charge relates to a number of acquisitions in both Housing and Care over recent years. The remaining unamortised value of £19.7m (2015: £26.8m), predominantly relating to order book and customer relationships, will be written off over their estimated lives.

Net finance charge

A net finance charge of £1.8m has been recognised in the year (2015: £1.9m). The finance cost in respect of bank borrowings was £2.8m (2015: £2.7m), reflecting a slightly higher average debt level.

The Group held two interest rate swaps covering 2016. The first fixed at a rate of 1.92% on £27.5m of borrowings and expired in August 2016. The second, which ran throughout the year, fixed at a rate of 1.85% on £30.0m of borrowings. The remaining debt bore a variable LIBOR rate. The Group pays a margin over and above LIBOR which is subject to a ratchet mechanism and which, during the year, was typically in the region of 1.5% above LIBOR.

The Group entered into further interest rate swaps impacting upon future periods. One swap, which commenced in January 2017, fixed the rate for a period of four years at 0.83% on £40.0m of borrowings.

The net finance costs also include a net credit generated from defined benefit pension accounting of £0.9m (2015: £0.7m).

Tax expense

	2016 £m	2015 £m
Current tax recognised in income statement	**4.7**	5.1
Deferred tax recognised in income statement	**(1.0)**	(1.3)
Total tax expenses recognised in income statement*	**3.7**	3.8
Profit before tax and before amortisation of acquired intangibles	**40.1**	36.8
Profit before tax	**29.4**	25.9
Effective current tax rate	**16.0%**	19.7%

* Continuing activities.

The Group complies with all relevant tax laws and regulations regarding the payment of tax and the provision of information to tax authorities. Mears does not undertake any aggressive tax planning or schemes that utilise low tax regimes in other jurisdictions for the purposes of tax avoidance. Mears seeks to maintain an open and honest relationship with the tax authorities and benefits from an HMRC 'low risk' status.

The headline UK corporation tax rate for the year was 20.0% (2015: 20.3%). The total tax charge for the year on continuing operations was £3.7m (2015: £3.8m) resulting in an effective total tax rate of 11.6% (2015: 14.7%). The key reconciling items to the headline rate were the utilisation of brought forward losses relating to previous acquisitions, an annual corporation tax deduction in respect of share options and adjustments in respect of the prior year estimated tax charge.

Total tax includes deferred tax, which is an estimate of the tax due on any differences between the carrying value and the tax base of assets or liabilities. The current tax charge excludes deferred tax and is therefore affected by both permanent and temporary differences in the recognition of items for tax and accounting purposes.

The current tax charge for the year on continuing operations was £4.7m (2015: £5.1m), which represents an effective tax rate of 16.0% (2015: 19.7%). For both the years, the key reconciling items to the headline rate were permanent differences on the amortisation of acquisition intangibles and the utilisation of brought forward tax losses primarily associated with the Morrison business.

Earnings per share (EPS)

	2016 p	2015 p	Change %
Diluted earnings per share*	**23.41**	20.10	+16%
Normalised diluted earnings per share**	**30.36**	27.94	+9%
Dividend per share	**11.70**	11.00	+6%

* Continuing activities.

** Continuing activities before acquired intangible amortisation with an adjustment to reflect a full tax charge.

The normalised diluted EPS, which allows for the potential dilutive impact of outstanding share options, increased by 9% to 30.36p (2015: 27.94p). Normalised earnings are based upon continuing activities and exclude the amortisation of acquisition intangibles together with an adjustment to reflect a full tax charge of 18% (2015: 18%). We believe that this normalised diluted EPS measure better allows the assessment of operational performance, the analysis of trends over time, the comparison of different businesses and the projection of future performance.

Read the Report of the Audit Committee on **page 56**

View the primary statements on **page 100**

Financial review continued

Cash performance

	2016 £m	2015 £m
Operating profit*	**41.9**	38.7
Depreciation and amortisation	**7.4**	6.3
EBITDA	**49.3**	45.0
Cash inflow from operating activities	**34.5**	44.5
EBITDA to cash conversion	**70%**	99%
Net (debt)/cash at balance sheet date	**(12.4)**	0.8
Average net debt in year**	**85.0**	68.0

* Before amortisation of acquisition intangibles.

** Average debt represents a 366-day mean.

The efficiency with which the Group manages working capital remains a cornerstone of our business. The Group's conversion of EBITDA to cash in the year was below target at 70% (2015: 99%), reflecting the organic growth delivered in 2016 resulting in some working capital expansion and the increase in trade receivables reflects this. The Group saw a reduction in trade payables and its associated cash outflow, impacted by a changing sales mix. The Group continues to drive a cash culture internally, which is so important in a high volume, low value and public sector environment. A cash conversion target of in excess of 90% remains the key performance measure and one which historically the Group historically has an excellent track record of delivering.

Balance sheet

	2016 £m	2015 £m
Goodwill and intangible assets	**219.6**	224.9
Property, plant and equipment	**20.3**	18.4
Inventories	**11.2**	9.0
Trade receivables	**157.2**	146.9
Trade payables	**(186.6)**	(188.5)
Net (debt)/cash	**(12.4)**	0.8
Deferred consideration	**(16.5)**	(20.9)
Cash flow hedge	**0.4**	(0.9)
Pension	**8.5**	4.0
Taxation	**(3.0)**	(2.1)
Net assets	**198.7**	191.6

Goodwill and intangible assets

The carrying value of identifiable acquisition intangibles at 31 December 2016 was £19.8m (2015: £26.8m), which predominantly relates to order book and customer relationships valued on acquisition. The carrying value will be amortised over its useful economic life, with over half of this value being expensed over the next two years. The net movement in the year comprised an increase of £3.7m relating to the finalisation of the fair value adjustments made in respect of the Care at Home acquisition completed in 2015 together with a reduction of £10.7m relating to amounts amortised and charged to the Income Statement during the year.

The carrying value of goodwill of £193.7m (2015: £193.1m) is not amortised but is reviewed for impairment on an annual basis or more frequently where there is an indication of impairment. The headroom between the goodwill carrying value of the Care division has been low for a number of years. The Board has carried out a detailed impairment review and was encouraged that the improved financial and non-finance performance, driven by the Care rationalisation, has resulted in a significant improvement in this headroom.

In addition, intangible assets includes the capitalisation of expenditure incurred in developing the in-house IT platform. Additions in the year amounted to £2.9m (2015: £3.0m) with a carrying value of £6.1m (2015: £5.1m), which is amortised over four years.

Tangible fixed assets

The Group capital expenditure of £7.4m (2015: £6.2m) relates to IT hardware, other office equipment and the refurbishment of new office premises. The level of capital expenditure in respect of property, plant and equipment in any single year has a close correlation to the number of new contracts mobilised in that period. As detailed within the Review of Operations, 2016 was a record year in respect of new contract mobilisations.

The majority of plant utilised by our operational teams is subject to short-term hire and motor vehicles are subject to operating leases and hence neither are included within capital expenditure or recognised as an asset within the balance sheet. Similarly, the Housing Management business has a large number of short-term property leases which are similarly not carried on the balance sheet. The new accounting standard IFRS 16 'Leases' requires lessees to recognise assets and liabilities for all leases, subject to materiality, and is effective for the Group's 2019 year end. A detailed analysis is being prepared during the course of 2017 to properly understand the impact of this new standard. The Directors' current expectation is that the accounting methodology will have a material impact upon the balance sheet but is not expected to have a material impact upon the profit before tax. The Group's bank facility agreement, and associated covenants, will not be impacted by these changes.

Working capital and net debt

Trade receivables and inventories increased to £168.4m (2015: £155.9m), which reflects the working capital expansion required to fund the organic growth delivered in the year. Trade payables reported a reduction to £186.6m (2015: £188.5m), reflecting a shift in the sales mix in favour of Housing Management, which carries a lower level of trade payables compared to the Housing maintenance activities.

Our net debt position at 31 December 2016 was £12.4m (2015: net cash of £0.8m). The Group seeks to minimise its trade receivables at both its June and December period ends, resulting in an atypical low net debt balance. A far more important metric is the Group's daily net debt balance, which provides a better indication of working capital management. The average net debt over the year was £85m, which represents an increase compared to the prior year, having funded both acquisitions and organic growth.

During the year, the Group completed an 'amend and extend' to its revolving capital facility which extended the expiry date from July 2018 to July 2020. The total commitment under the facility increased from £120m to £140m. The revised facility enjoys a reduction to the interest cost, with the margin payable over and above LIBOR, which is subject to a ratchet mechanism, reducing from a range of 150–250bps to 120–220bps. The Group continues to maintain a strong relationship with both of its bankers, Barclays and HSBC, and meets with them regularly.

Pensions

	2016		
	Group schemes £m	**Other schemes £m**	**Total £m**
Scheme assets	**149.5**	**406.9**	**556.5**
Scheme liabilities	**(137.7)**	**(410.3)**	**(548.0)**
Net asset/(liability)	**11.8**	**(3.3)**	**8.5**
Current service cost	**2.1**	**4.4**	**6.5**

	2015		
	Group schemes £m	Other schemes £m	Total £m
Scheme assets	116.5	332.7	449.2
Scheme liabilities	(111.3)	(333.8)	(445.1)
Net asset/(liability)	5.2	(1.1)	4.1
Current service cost	2.1	5.5	7.7

The Group participates in two principal Group pension schemes (2015: two) together with a further 33 (2015: 30) individual defined benefit schemes where the Group has received Admitted Body status in a Local Government Pension Scheme. At the point of tendering for new contract opportunities, the Group seeks to minimise its exposure to future changes in the required pension contribution rates and to future liabilities resulting from scheme deficits.

Whilst the aggregate of all the schemes reports a net asset position, the Group is mindful of managing its risks in this area. Under IAS 19, pension scheme liability values are driven by changes in the net discount rate, which is the yield on high quality corporate bonds less the long-term rate of expected price inflation. Following the result of the EU referendum, an increasingly volatile macro-economic environment has resulted in a downward move in the net discount rate. This has led to a significant increase in pension liabilities. Positively, the pension schemes are reporting strong increases in their scheme assets which have, in aggregate, exceeded the increase in the associated defined benefit obligation. Overall, the Group has reported an increase in its pension net asset from £4.1m to £8.5m.

However, one significant negative resulting from the changing assumptions is the charge to the income statement, being the current service cost. The pension charge to the income statement for 2017, which is fixed at the start of the year using the assumptions set at December 2016, is £9.0m, increasing from £6.5m. This element of pension accounting is a non-cash item. Typically cost recovery for pension costs within the underlying customer contracts is aligned to employers' contributions which are, in the short term at least, unchanged.

Guidance for 2017

The 93% visibility of consensus forecast revenues secured for 2017 at the turn of the year fell marginally short of the 95% target. Revenue visibility for 2017 has subsequently increased to 94%. The Group targets annual revenue growth in Housing of 5% to 10% per annum, and our expectation for growth in 2017, given the small short-fall on the headline visibility measure, would be at the bottom end of that range.

Our Housing margin has historically been in the range of 5.6%–5.9%. The lower number of new contract mobilisations in 2017 will remove some of the margin dilution experienced in 2016. The shifting sales mix towards Housing Management services, which typically generate a higher operating margin, also provides an opportunity for margins to improve slightly. On the downside, the increase in pension service costs, following a reduction in the associated net discount rate, will reduce Housing profits by circa £2.5m.

In Care, the Group is focused on achieving good levels of service at sustainable margins and there is less ambition for achieving revenue growth. During 2016, the Group took the decision to exit from around 20 of its Care contracts and a number of these closures have continued into 2017. However, a number of key new contract wins have also delivered some strong organic growth. The Group has previously made commitments on its Care margins, with the expectation that over time a margin can be delivered in Care that is similar to those delivered in Housing. In 2017, we expect Care performance to be in line with that trajectory and return to profit.

We will continue to manage working capital to a high standard, targeting EBITDA to cash conversion in excess of 90%.

Social value

At the heart of Mears lies a strong sense of responsibility towards improving people's lives. We are committed to achieving this by ensuring everyone we work with creates greater value and receives wider benefits from an integrated social value approach.

We aim to lead the way with social value in the markets where we operate, delivering lasting and meaningful outcomes through positive community engagement projects and effective measurement.

The concept of social value has long been embedded in Mears. We already have a strong reputation for delivering some great long-term community and legacy projects. To maintain the focus on delivering excellence in social value, responding to the changing requirements of the Social Value Act of 2012, Mears conducted a review of our social value strategy. We needed to demystify social value by exploring the key challenges that social housing and service providers face in meeting the requirements of the Act. The review identified four key social value priorities. These have become the focus areas against which all of our community and engagement activities are considered and measured.

Mears has a strong belief and culture that we have a responsibility to contribute to the needs of our wider society. So, further to understanding the outcomes of the legislation, the challenge we approached and delivered, with our social value commitments, was to develop a strategy and framework of practical approaches to effectively engage with communities and deliver social value on the ground throughout the business, with an effective measurement of the social impact that is created.

Net social impact
£3,555,877
in the year

Read the Independent Committee Members' Report on Mears' Social Value Activities on **page 42**

Thought leadership approach

Mears has taken an active approach to initiate thought leadership campaigns, to drive the agenda for social value in our markets.

Mears has continued to lead thinking across the housing and care sectors. We have produced a report with the think tank ResPublica looking at factors influencing regeneration programmes and highlighting our work with Milton Keynes Council.

Mears has also once again championed the case nationally for greater focus and investment in homecare and this subject has now risen significantly as an area of national debate. We will continue to champion the cause of care workers and service users.

Social value board: our key influencers

To support our approach to developing and continually improving our social value framework, the social value board was created. Our social value board will ensure we take a strategic approach to corporate social responsibility and embed it into each aspect and area of our operations. The board will provide validation and challenge, ensuring a continuous improvement focus to our social value delivery.

To help us realise our vision, we have appointed three external experts to lead the board, who are all experts in the field.

Hazel Blears

The former Secretary of State for Communities and Local Government and Minister for Health championed the Social Value Act through Parliament.

Richard Kennedy

Richard is chair of the board for Social Value UK and co-chair of Social Value International.

Dr Greg Lavery

Greg is a global expert in sustainability with 18 years' experience of implementing carbon reduction and money-saving waste management strategies across the world. Greg has spoken internationally on low carbon and sustainability.

Mears' four social value priorities

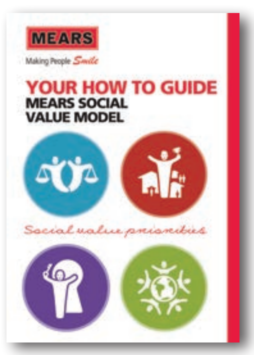
Championing local
Improving the wellbeing of the people and communities we serve

Creating chances
Providing career, skills and employment opportunities

Fair for all
Reducing prejudice, improving understanding of differences and supporting social inclusion

Healthy planet
Making a positive contribution to our planet

Delivering solutions for local activities
The introduction of an annual social value calendar delivers national themes and awareness for local activity, focusing on the four key social value priorities. This has enabled the branches to design and deliver local activities, which supports the overall strategy and the delivery of the branch social value plan.



Measuring our success
It's vital to know if what we're doing really does make a difference. The only way to do that is by measuring – but how can you measure social impact? It's a tough challenge, particularly when social impacts can be hard (such as new jobs created) and soft (something as simple and yet profound as increased happiness). Our approach is based on evaluating wellbeing. A bespoke social value calculator enables Mears to measure our impacts and outcomes.

Embedding the commitment and approach with accreditation success
To ensure we always strive to improve, we open ourselves to an annual programme of accreditations. These external assessments tell us if we're reaching what we aim to achieve.

We're delighted to say that 2016 brought great success. Mears was accredited by G4S (on behalf of CSE) for customer service excellence, including community engagement, and by TPAS for our approach to tenant and customer engagement. We also continued to secure Social Mobility Champion status from the Department for Business Innovation and Skills.

Social mobility is about giving young people equal chances in life, regardless of where they were born, the school they go to, or the jobs their parents do. At Mears, we aim to make sure jobs and opportunities are open to everyone and we want to inspire other businesses to follow suit.

Social Mobility Champion

"The Social Mobility Champions have risen to the challenge set by Government and shown genuine commitment to bringing about positive change.

They have gone beyond just volunteering in schools or changing the way they advertise jobs; they have made social mobility a core part of their corporate strategy."

Nick Boles, Skills Minister

Social value continued

Focus on championing local:

Improving the wellbeing of people and the communities we serve

Working with partners and clients is key to identifying the local social value projects for the business to get involved in. Through the development of branch social value plans, which are measured to establish social impact, we can really push the boundaries to deliver the social value commitments in our communities locally. The local approach, whilst utilising the benefit of national partners, really makes a difference and we urge all business units and branches to develop their plans, to talk to their partners and clients, to work together, utilising our commitment of volunteers from the business, and to make a real POSITIVE difference to enable the individuals and the communities in which we operate to flourish and thrive.

Total number of projects in the year to date

496

Total volunteering hours

58,650

Doing the right thing #BetterBusiness

Delivering our social value plans: in practice

We plan to make it easy for everyone in Mears to get behind our goal, by creating awareness and understanding and providing the framework and tools needed for success. The social value strategy and framework of tools have been cascaded to all key stakeholders in the business, utilising new methods of communication such as webinars, in addition to the traditional briefings and approach.

Every branch of Mears makes a social value pledge, which focuses on specific activities to improve its local community in at least one of these areas. All branches are measured on a social value plan.

Insight into focusing on the right projects in the right locations…

We have developed a bespoke market-leading online portal that gives our colleagues an insight into local demographics and helps identify areas of deprivation. This enables users throughout the business to drill down into a local area and find out more information about the demographics of an area, including layer crime statistics, depravation information and isolation data, along with health and environmental data.

This allows us to target intervention and outreach to the most disadvantaged groups, focus on the right outcomes and make targeted social value decisions.

Further development of this solution will allow insight into specific housing stock locations, aligned to our client business, to fully support the collaborative approach to targeting the right outcomes in the right locations.

Focus on fair for all:

Targeting under-represented groups

Mears commits to a fully structured approach to target groups that are under-represented in the building and construction sector such as females, black and minority ethnic groups (BME) groups and those with disabilities in the area. To achieve this objective we conducted a focused recruitment campaign to target particular groups and organised a series of events to support the campaign.

One area of particular focus is to encourage more women into the trades and management. Mears has a funded partnership with the CITB. This has the aim of increasing the number of female trade apprentices and operatives in the social housing business maintenance sector. Through a targeted and curriculum-based approach to working with schools and colleges, we provide a focused approach to supporting local schools and college sessions.

Leading the way in fair for all in the care market

Our Care division has experienced a challenging market environment this year. The sector has been under severe funding pressure. We have focused on those strategically important clients which we believe have potential to develop into partnerships where we are able to deliver a high quality service.

We take a responsible and ethical approach to paying our carers and have endeavour to influence clients in this area.

We are fully supportive of the new National Living Wage legislation, which we believe is really important in attracting a workforce capable of delivering to the growing demands of the care market. Given our focus on quality, we will only bid for opportunities where we can pay our workforce at a level that will not only meet legal minimum requirements but will ensure we have the workforce to deliver the high quality service that is at the heart of our strategy.

Continued funding issues in the care market will create a catalyst for change, as will the consequences of implementing the National Living Wage, and Mears will proactively engage in this challenge to shape the service, supporting the fair for all focus.

In focus: addressing training needs of hard-to-reach groups through collaborative working

Through our contract with Manchester City Council, and working with our partners Yes Manchester and The Skills Company, we held a pilot Pre-recruitment Programme to target candidates out of reach of the employment market. They included a diverse mix of individuals representing the hard-to-reach groups, including persons with mental health issues and an ex-offender.

The pilot was a great success and we directly recruited six out of the eight candidates for the Mears National Apprenticeship Programme and all of them are currently working towards NVQ Levels 2 and 3 in a range of trade and technical specialisms.

One of the barriers that we encountered in formulating the Pre-recruitment Programme related to the issue of candidates being disqualified from receiving Universal Credit during the six weeks of training. To overcome this The Skills Company negotiated a special arrangement with JobCentre Plus so that candidates could continue to receive their benefits.

One of the critical factors contributing to the success of the Pre-recruitment Programme has been the time taken to communicate and explain the training in detail at the outset. This has ensured that candidates fully understand the programme objectives, what is entailed, what is required from them and the possibility of an apprenticeship at the end of the training.

One trainee maintenance operative got her opportunity through Yes Manchester which helped her to secure a six-week traineeship on the pre-recruitment Programme.

After completing the traineeship, she was offered a place on our apprenticeship programme as a maintenance trainee and is currently working towards her NVQ. Our trainee said:

> "This has been life changing for me. Instead of jobs with no future and suffering from stress, I am now doing something I enjoy. It's really boosted my confidence and had a positive effect on my health and wellbeing."

Number of work placement opportunities offered to young people from lower socioeconomic groups between January and December 2016

350+

Focus on creating chances:

Mears is investing in the future through training and skills

The Academies are dedicated to improving the skills of employees and the employability of people within the communities we serve.

During 2016 Mears opened two brand new, bespoke Academies in Rotherham, South Yorkshire, and Brentwood, Essex.

The Academies are fully equipped and accredited to deliver practical training and apprenticeships across the trades, and have IT suites and modern classroom facilities. Our flagship Rotherham Academy houses our national gas training centre, accredited by BPEC, to train operatives to the standard required for registration with Gas Safe.

Across the Group, we employ 400 apprentices and have been named as a Top 100 Apprentice Employer by the National Apprenticeship Service in recognition of the positive experience apprentices have with us. Mears runs Study Programmes for young people as a precursor to apprenticeships and an alternative to school or college. Around 20 16 to 19-year-olds participate in the programme at any point in time.

Transforming lives is at the heart of what we strive to achieve. Through our genuine commitment to social value and providing training opportunities to local people in the areas we operate, Mears is in a unique position to make a real, sustainable and long-term difference to the lives of local people. Mears has an impressive training track record as we currently employ around 400 apprentices nationally, with a clear commitment to working with our clients and partners, which will support the transformation of lives through greater access to a wide range of training opportunities.

During 2017 we will bring together the delivery of qualifications and apprenticeships to Care staff under the umbrella of one national service provider, primarily to improve quality and standards as well as the experience of the learner.

Number of employees involved in delivering social value projects

7,000+

Number of apprentices on structured apprenticeship framework

400+

Rotherham careers event brings employment opportunities

Mears brought together local businesses and organisations to showcase employment and training opportunities at the annual Local Employment Advisory Forum (LEAF) event in Rotherham, with over 1,429 attending, and supported by 65 local businesses, with over 500 current vacancies to showcase employment and training opportunities in the area, as well as providing advice on how to gain the skills needed by employers.

The event was sponsored by Mears and Rotherham Council, delivered in partnership with Jobcentre Plus.

Focus on creating chances: providing career, skills and employment opportunities

Our approach is to target excluded and hard-to-reach groups, entering partnerships at a national and regional level with organisations.

Creating chances is about having a workforce drawn from local communities, thus creating opportunities for careers and enabling people to develop new and existing skills.

Number of school students who attended careers talks and engagement projects

8,500

Number of schools engaged in our projects

90+

Focus on healthy planet:

A successful partnership with Network Waste has helped Mears to achieve 90% recycling rates and more than a 10% reduction in waste costs.

We are committed to being a good corporate citizen in all our dealings with customers, colleagues, suppliers and in the communities where we work. To ensure a consistent approach throughout our supply chain, we expect our suppliers to have or adopt similar business principles to our own. We are working towards a set of social values where suppliers will be required to acknowledge the significance of social, environmental and ethical matters in their conduct, and work towards improving quality standards.

We are committed to minimising the environmental impact of our activities and our success to date has been externally recognised through our accreditations to the Carbon Footprint Status and Green Accord Premier Status. We are also members of the Sustainable Homes Index for Tomorrow (SHIFT) and a member of the FTSE4Good Index, the leading global responsible investment index which is designed to measure the performance of companies that meet globally recognised corporate responsibility standards.

In line with our environmental accreditations, we actively measure all carbon emissions and waste to identify improvement opportunities and set clear targets for reduction.

Our environment proposals are aligned with the social value priorities and are designed to ensure that our commitments can be clearly evidenced and measured through the tangible outcomes we will demonstrate:

→ **Reduce waste and increase recycling rates** using a national waste strategy, site waste management plans and our partnership with Network Waste.

→ **Reduce fleet emissions** using a recently upgraded green fleet, GPS tracker systems and Smarter Driver Training.

→ **Reduce the carbon footprint of our activities** using a mixture of Company-wide measures and bespoke initiatives tailored to the priorities of the partnership.

→ **Produce a SMART plan** to manage and measure our environmental commitments against the environmental priorities identified.

Focus on health and safety

It was another positive year for the Mears safety and quality in 2016. We have reduced accident rates by over 10% and achieved RoSPA President's Award (14 consecutive Golds), for our continued commitment to accident and ill-health prevention.

We successfully continued our certification to ISO 9001, ISO 14001 and OHSAS 18001. We also attained a diversion from landfill of over 94% of our waste.

Having gained approval as a CITB Training Provider we now have 14 registered instructors available to deliver the full suite of CITB Site Safety schemes.

In 2017 we will continue to challenge our standards and look to continuously improve the safety environment for all of our employees.

In focus: working with social enterprise to reuse materials

We engage and collaborate with social enterprises to facilitate the reuse of various items we come across whilst undertaking our services. We have worked with a number of social enterprises such as Electronics Recycling (Relectricals) and Mustard Tree, which is a Manchester-based social enterprise working to tackle homelessness and provide employment opportunities. This approach, whilst supporting our wider social value objectives, ensures that any reusable items are reused/recycled and waste to landfill is minimised.

relectricals

Mustard Tree
Combatting Poverty – Preventing Homelessness

Independent Committee members' report on Mears' social value activities

Authored by the independent members of the Mears Social Value Committee:

- Dr Greg Lavery
- Richard Kennedy
- Rt Hon Hazel Blears

Read our Social Value key influencers on **page 36**

How corporate social responsibility/ social value is done at Mears

Mears defines its responsibilities to society to include its social, economic and environmental impact. It takes a proactive approach to these responsibilities and recognises that highlighting the positive difference this makes in communities enthuses staff, motivates customers and clients, creates substantial environmental and social benefits and builds competitive advantage for Mears. This is why Mears refers to its social and environmental activities as 'Social Value' – because through these activities it is creating value for Mears and the wider communities in which it operates.

Social Value in Mears is delivered by staff, often on a daily basis alongside their job. Social Value is overseen by Mears' Social Value Committee, headed by Director Alan Long and comprising senior executives from within the business as well as independent external experts.

Mears has chosen four strategic pillars of Social Value to focus its efforts where it can create the greatest impact in a way which is most relevant to the business. These are:

- Championing Local: improving the wellbeing of people and the communities they serve;
- Fair for All: reducing prejudice, improving understanding of differences and supporting social inclusion;
- Creating Chances: providing career, skills and employment opportunities; and
- Healthy Planet: making a positive contribution to our planet.

The 'Red Thread' defines the culture of the organisation and expected behaviours. This culture sets the aspirations and standards of the Company, which, together with the four themes above, provide the parameters within which staff focus their efforts to create Social Value.

Delivery and creation of Social Value is site and staff specific, with a vast range of activities occurring that are all chosen for their local relevance.

Strengths and weaknesses of Mears' approach to social value

Narrowing the scope of such a broad topic of Social Value, through the four themes, is considered prudent, enabling the organisation/staff to focus on a few priorities that deliver the most impact.

Allowing a wide range of activities under these themes empowers teams/staff to address local issues where the needs are greatest. This has the added benefit of creating bespoke and well researched action plans that are attractive to clients because they add value beyond the contracted services which Mears provides, while also addressing local issues.

However, these bespoke local solutions mean that Mears is currently not easily able to present a simple story of its activities to external observers, which makes it difficult to capture the full impact of its work.

Key achievements of the Social Value Committee in the last year

The importance of managers in the creation of Social Value was identified. This starts with creating consequences for and addressing poor management and recognising that improvement requires management training. Positive leadership which drives Social Value should be rewarded. These key points have been addressed through manager training in people management as well as through management personnel changes.

HR practices and policies have been reviewed and compared with best practice, leading to:

- a review of the salary banding structure, bonus scheme and process for annual pay awards (consistently administered);
- a review of the gender gap and actions taken to address this with a particular focus on ensuring a more equal representation of females at the operative level;
- the development of a reward and consequence model; and
- a review of the appraisal system.

The staff satisfaction survey was reviewed and actions were identified to improve Mears' performance.

Mears' collaboration with and expectations of suppliers were examined with the specific focus of driving Social Value through Mears' procurement.

A series of metrics related to Social Value has been created, enabling Mears to measure performance and progress.

Areas for further improvement

Find better ways to extract Social Value through pre-competitive collaboration with key suppliers and subcontractors. Examples could include:

- transport collaboration to reduce both environmental impacts and costs;
- more creative ways to train future leaders of Mears, such as exchanges/secondments with other friendly organisations, such as Travis Perkins;
- sharing Mears' Social Value lessons with suppliers and subcontractors to lead change throughout the sector; and
- setting targets for suppliers around employment opportunities and local sourcing.

Mears can further integrate its Social Value work into its value proposition for clients to aid with market differentiation and competitive advantage. For example, substantial work is being done by the Care division tackling loneliness, supporting those with dementia, facilitating timely discharge from hospital, and providing support at home and in the community. All of these have clear and measurable cost advantages in savings to the healthcare system as well as improvements in wellbeing for those with health conditions and their carers and families. Articulating this value and building it into client discussions, bids and reports is a logical, if not easy, next step.

Mears is currently missing the marketing benefits of its Social Value activities due to the perceived difficulty in communicating the diverse range of its actions as well as the general sense of humility within the business. It is recommended that Mears recognise and communicate its local and tailored approach, giving examples from real projects to illustrate it. Mears should be communicating that it is committed to addressing the most important issues where it is able to have an impact in each community where it operates. No two communities are the same, so Mears develops bespoke programmes for each. This is an easy-to-communicate message that is attractive to clients and accurately represents Mears' value-adding approach.

There could be opportunities to reduce the environmental impact of Mears' activity through smart procurement, for example using sustainable office refurbishment options to address the second biggest concern from staff in the recent staff satisfaction survey (i.e. office conditions).

Environmental performance and improvements have not yet been discussed by the Social Value Committee, nor have the business opportunities related to environmental sustainability and resource efficiency.

The work of the Social Value Committee continues, with a range of aspects of the business not yet reviewed. As a result, this report should be read as an interim document as part of a work in progress.

Overall assessment compared to most companies and leading companies

The independent Social Value Committee members commend Mears on its wide range of Social Value initiatives in all regions that demonstrate strong community focus and excellent social and environmental behaviours from management and staff.

The level of local consultation to unearth and identify community needs and build them into bids is ahead of current mainstream business practices and is strongly focused on creating maximum Social Value while contributing to winning contracts. This is an excellent alignment that creates a win-win situation for all parties.

Mears is also a leader in engaging its front line staff with practical Social Value projects to which they willingly contribute.

In 2016 Mears demonstrated sector leadership by enacting the Living Wage and remaining uncompromising on staff working hours throughout its challenging price renegotiations with clients. Further, Mears has been courageous and outspoken on this important issue, leading the care sector. An example of this is Mears walking away from contracts where clients were unwilling to pay for the Living Wage and appropriate travel time. The long-term approach of Mears will benefit all in the sector.

Mears is a modest company which has not captured many of the marketing benefits offered by Social Value creation. In this respect it lags behind many sustainability leaders. Addressing this issue should improve bid success rates and profitability for Mears, as well as building staff pride.

The Strategic Report was approved by the Board of Directors on 27 March 2017 and signed on its behalf by

D J Miles
Chief Executive Officer
david.miles@mearsgroup.co.uk

Corporate governance

Introduction to corporate governance

Code compliance

We apply the provisions of the UK Corporate Governance Code 2014 (the 'Code'). The Directors confirm that the Group has complied with all provisions set out in the Code during the year ended 31 December 2016.

Dear shareholder,

We seek to create a working culture where honesty, openness and fairness are valued.

We seek to maintain high standards of corporate governance as this will help to facilitate the success of the Company and sustain this over time. An important distinction between the management, led by David Miles, Chief Executive Officer, and the Board is that the management is responsible for running the business while the Board, acting under my leadership, provides constructive challenge to management, which is necessary to create accountability and drive performance. This results in an environment that creates and preserves value for shareholders.

It is vital that, as a Board, we have the right mix of skills, experience and diversity, ensuring that Board members have sufficient knowledge of the Company whilst maintaining their independence and objectivity. I am fortunate as Chairman to be able to call upon a Board with a broad range of expertise and specialisms. It was with deep regret that we announced the passing of Rory Macnamara, who had been a Director since June 2010 and chaired our Nomination Committee. Rory will be greatly missed by the Board for his strong technical contribution, and as a trusted colleague. Julia Unwin has agreed to become the replacement Chair of the Nomination Committee.

During the year, a number of our Non-Executive Directors have reached nine years' service, and as such are not offering themselves for re-election. I would like to thank David Hosein and Mike Rogers for their significant contribution to the Group. Peter Dicks has also now reached nine years' service. However, given the unexpected loss of Rory Macnamara, I have asked Peter to remain on the Board as Senior Independent Non-Executive Director for a further year to provide continuity and stability.

We take succession at Board and senior management level very seriously. We believe we have a good record of resourcing the needs of our business along with developing our own people in line with our desired culture. Since the year end, we have identified two new recruits to the Board. I am delighted to propose to shareholders that they approve the appointment of Roy Irwin and Jason Burt as Directors at the 2017 AGM. I believe that we have achieved a good balance with the right skills and experience which will add considerably to Board discussions. We will keep the Board composition under continuous review and I would expect the Group to make further Non-Executive Director appointments during 2017 to bring additional skills and even further diversity to the Board.

During 2016, the Board visited two of our largest operations in Gateshead, which is the hub for a number of significant Housing contracts, and our newly opened Rotherham Training Academy. Such visits are essential to enable the Non-Executive Directors to understand better the day-to-day functioning of our business.

We will not compromise on our governance principles. The Board is committed to maintaining the Group's operations in accordance with the highest standards of corporate governance as set out in the UK Corporate Governance Code issued in 2014 and has complied with all Code principles and relevant provisions throughout the year.

We continue to engage with our shareholders and explain our business model and key priorities to ensure that we deliver our strategic goals and value to all our stakeholders.

R Holt
Chairman
bob.holt@mearsgroup.co.uk
27 March 2017

Your Board

Bob Holt OBE
Non-Executive Chairman

Age: 62

Tenure: 20 years

Skills and experience:

Bob had a controlling interest in Mears at the time of flotation in October 1996. He has a background in developing support service businesses. He has operated in the service sector since 1981, initially in a financial capacity then moving into general management.

Principal external appointments:

Chairman, Lakehouse PLC

Chairman, Totally PLC

Chairman, DX Group PLC

David J Miles
Chief Executive Officer

Age: 50

Tenure: 20 years (10 years on the Board)

Skills and experience:

David joined Mears in 1996 and, prior to his appointment to the Board in January 2007, was Managing Director of the Mears Social Housing division. Prior to joining Mears, David held a senior position with the Mitie Group. His background is in electrical engineering.

Principal external appointments:

None

Andrew C M Smith
Finance Director

Age: 44

Tenure: 17 years (10 years on the Board)

Skills and experience:

Andrew joined Mears in 1999 and, prior to his appointment to the Board, was Finance Director covering the Group's subsidiaries. Andrew qualified as a Chartered Accountant in 1994 and worked in professional practice prior to joining Mears.

Principal external appointments:

None

Alan Long
Executive Director

Age: 54

Tenure: 11 years (7 years on the Board)

Skills and experience:

Alan joined Mears in 2005 and, prior to his appointment to the Board in August 2009, was Managing Director of the Group's Care division, having previously held the position of Group Sales and Marketing Director. Prior to joining Mears, Alan held senior roles at Britannia Building Society, Mars and Smith & Nephew.

Principal external appointments:

None

Julia Unwin CBE
Non-Executive Director

Age: 60

Tenure: 1 year

Skills and experience:

Julia is former Chief Executive of the Joseph Rowntree Foundation and the Joseph Rowntree Housing Trust. She has significant experience in the housing and care sectors, having been a member of the Housing Corporation Board for ten years.

Principal external appointments:

Yorkshire Water Services Limited

Non-Executive proposed appointments to be confirmed at the 2017 AGM

Jason Burt
Non-Executive Director

Age: 51

Skills and experience:

Jason Burt was a senior partner at Plexus Law, specialising in complex employers' and public liability claims. His appointment will further integrate health and safety into the Group's governance structures, driving good working and health and safety practices. Jason will chair a newly formed Health, Safety and Environment core group and be a member of the Audit and Risk Committee.

Principal external appointments:

None

Roy Irwin
Non-Executive Director

Age: 62

Skills and experience:

Roy Irwin has significant experience in the social housing sector, having lately been Chief Inspector for the Audit Commission following a career of over 30 years in public sector housing. Since 2013, Roy has held the position of Non-Executive Chairman of Plexus and Omega Housing, being Mears' registered providers of social housing with the Homes and Communities Agency.

Principal external appointments:

None

Rory Macnamara
It was with deep regret that the Group announced the passing of Rory Macnamara, who served as a Director throughout the year until the date of his death, 17 December 2016.

Peter F Dicks
Non-Executive Deputy Chairman and Senior Independent Director

Age: 74

Tenure: 9 years

Skills and experience:

Peter has been active in the venture capital and investment fields for a number of years. He is currently a Director of a number of companies. He joined Mears in 2008 and is Chairman of the Remuneration Committee.

Principal external appointments:

Chairman,
Miton UK MicroCap Trust plc

Geraint Davies CBE
Non-Executive Director

Age: 62

Tenure: 1 year

Skills and experience:

Geraint is a fellow member of the Institute of Chartered Accountants in England and Wales. He was previously a partner for a leading professional practice for over 25 years. His commercial experience includes working with Registered Social Landlords and a number of organisations in the healthcare sector.

Principal external appointments:

Cardiff International Airport Limited

David L Hosein*
Non-Executive Director

Age: 53

Tenure: 9 years

Skills and experience:

David has over 17 years' consulting experience, the last five of which have been at OC&C Strategy Consultants Limited where he is a partner. David has worked extensively in the support services sector for corporate and private equity clients. Previously, he was a partner in Arthur Andersen. He joined Mears in 2008.

Principal external appointments:

Partner, OC&C

Michael G Rogers*
Non-Executive Director

Age: 75

Tenure: 9 years

Skills and experience:

Michael founded Careforce in 1999 and has over 30 years' experience in healthcare services and care provision. In 1976 he joined Nestor Medical Group Limited as Managing Director and went on to become Chief Executive of Nestor Healthcare Group plc from 1986 to 1996. From 1996 to 1999 he worked as a consultant to a number of healthcare related organisations.

Principal external appointments:

Non-Executive Director,
Totally PLC

* Not standing for re-election.

Ben Westran
Company Secretary

Age: 40

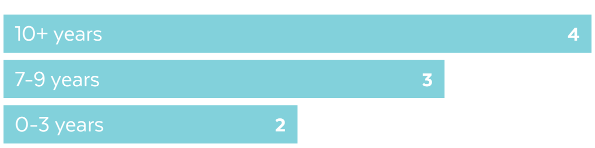
Tenure: 13 years

Skills and experience:

Ben is a Chartered Accountant and, prior to his appointment as Company Secretary, was Group Financial Controller and Director of a number of the Group's subsidiaries. Ben joined the Group in 2004 having previously worked in professional practice.

Key:
R Remuneration Committee
A Audit Committee
N Nomination Committee
◯ Chairman
S Senior Independent Non-Executive Director

Length of tenure of Board



Non-Executive/Executive Directors

Corporate governance report
Leadership

How the Board operates

The Board leads and provides strategic direction to the Group and carries ultimate responsibility for management of the Group's activities and financial performance. The Board acknowledges accountability to shareholders for proper conduct of the business, and responsibility for the long-term success of the Group, having regard to the interests of all stakeholders.

The Board's prime objective is to ensure the ongoing commercial and financial success of the Group. The Board provides entrepreneurial leadership of the Group within a sound and prudent risk management framework using effective internal control systems which enable risk to be assessed and managed. The Board sets the Group's strategic objectives, and the nature and extent of principal risks it is willing to take in achieving these strategic objectives, and ensures that the necessary financial and human resources are in place for the Group to meet these objectives. The Board sets the Group's values and standards and ensures that the Group's obligations to its shareholders and others are understood and met.

The Group's business model and strategic priorities can be found on pages 10 and 11 and 12 to 13.

The Board maintains and regularly reviews a full list of matters and decisions that are reserved to, and can only be approved by, the Board. These are reviewed annually and include but are not limited to:

- Group strategy and operating plans;
- corporate governance and risk management;
- the approval of budgets;
- changes to the Group's debt and equity funding;
- appointment, termination and remuneration of Directors and the Company Secretary;
- financial reporting and audit, including interim and full-year results announcements and dividends;
- approving significant acquisitions and disposals; and
- values and ethics.

The day-to-day running of the business is delegated to the Executive Directors through Divisional Boards, which comprise the Chief Executive Officer, the Finance Director and the Executive Director together with other senior divisional team members.

It is through the Divisional Boards that the operational and financial business of the Group is delivered. The Housing and Care Boards meet monthly and the key matters considered include:

- financial performance and actual performance in comparison to forecast;
- review of quarterly revised forecasts;
- monitoring strategic developments;
- business development and review of active tenders and opportunity pipeline;
- monitoring service delivery performance measures and driving improvement;
- values and culture and driving consistency and best practice together with employee engagement; and
- health, safety and environment.

The Board delegates certain responsibilities to its three principal Committees.

- The Audit Committee ensures the integrity of financial information, the effectiveness of the financial controls and the internal control and risk management systems.
- The Nomination Committee recommends the appointment of Directors and conducts a review of succession planning at Board and Operating Board levels.
- The Remuneration Committee sets the remuneration policy for Executive Directors and determines their individual remuneration arrangements.

The Chairman of each Committee briefs the Board at each meeting on the principal items that were discussed, decisions made and key issues. The activities of these Committees are discussed in more detail later in this report.

Each Committee comprises Non-Executive Directors only, as required by the UK Corporate Governance Code 2014. The Chair of each Committee is present at the AGM to answer questions from shareholders.

Corporate governance framework

Responsibility for good governance lies with the Board. There is a strong and effective governance system in place throughout the Group which ensures that integrity and good ethical conduct are the foundations of our decision making.

The governance framework extends to operational activities, as outlined in the risk management process on pages 18 to 23.

The Chairman

Key responsibilities:

- is responsible for the leadership of the Board and ensuring its effectiveness;
- sets the Board's agenda and ensures adequate time is available for discussion of all agenda items;
- ensures all discussion is in the context of the long-term success of the Group;
- promotes a culture of openness and debate by facilitating the effective contribution of Non-Executive Directors;
- ensures that the Directors receive accurate, timely and clear information; and
- is responsible for designing a rigorous annual evaluation of the performance of the Board and individual Directors.

The Board

Audit Committee

Key objective: The Audit Committee is responsible for effective corporate governance in respect of financial reporting, agreeing the scope of the external audit, the setting of the auditor's remuneration and reviewing the effectiveness of the Group's internal controls, risk management and internal audit processes.

Read the Report of the Audit Committee on **page 56**

Remuneration Committee

Key objective: The Remuneration Committee is responsible for setting, reviewing and recommending the remuneration policy and strategy in respect of Executive remuneration.

Read the Report of the Remuneration Committee on **page 61**

Nomination Committee

Key objective: The Nomination Committee is responsible for ensuring that the Board comprises a high level and range of business experience, skills and diversity to enable the Group to be managed effectively.

Read the Report of the Nomination Committee on **page 54**

The Chief Executive Officer

Key responsibilities:

- manages the day-to-day business operations of the Group;
- ensures that the appropriate standards of corporate governance permeate throughout the organisation;
- recommends key strategies and is responsible for execution of those agreed by the Board;
- takes a leading role in the relationship with all external agencies and in promoting Mears Group PLC; and
- directs the risk profile of the Group in line with the risk appetite and categories of risk identified and accepted by the Board.

Read the Review of Operations on **page 24**

Divisional Boards

Key objective: The Housing and Care Divisional Boards are the principal forum through which the operational and financial business of the Group is delivered.

Corporate governance report continued
Leadership

Board composition and meetings in 2016

	Board		Strategy days		Audit		Nomination		Remuneration	
Number of meetings	Potential	Actual	Potential	Actual	Potential	Actual	Potential	Actual	Potential	Actual
R Holt	6	6	1	1	—	—	—	—	—	—
D J Miles	6	6	1	1	5	5	—	—	—	—
A C M Smith	6	6	1	1	5	5	—	—	—	—
A Long	6	6	1	1	—	—	—	—	—	—
M G Rogers	6	6	1	1	—	—	—	—	2	2
P F Dicks	6	6	1	1	5	5	1	1	2	2
D L Hosein	6	6	1	1	—	—	1	1	—	—
R Macnamara	6	4	1	1	5	4	1	1	2	1
G Davies	6	6	1	1	5	5	—	—	—	—
J Unwin	2	2	1	1	—	—	—	—	—	—

During the year, the Board had a total of eight Directors, all of whom, with the exception of Rory Macnamara, served throughout the year. Rory Macnamara died on 17 December 2016.

The table above shows the attendance of Directors at scheduled Board and Committee meetings. The Board scheduled seven meetings during the year including one strategy day. Additional ad hoc meetings or conference calls were also organised pertaining to specific matters which required Directors' involvement between the scheduled meetings.

The Board comprises the Chairman, the Chief Executive Officer, the Finance Director, the Executive Director and six Non-Executive Directors. Peter Dicks was the Senior Independent Non-Executive Director throughout the period. The Directors' biographical details are set out on page 46. These indicate the respective backgrounds and range of business experiences which enable the Board to operate effectively. Their differing mix of skills and business experience is a major contribution to the proper functioning of the Board and its Committees, ensuring that matters are challenged and there is constructive debate.

In addition to the meetings scheduled, the Chairman and the Non-Executive Directors met without the presence of the Executive Directors, and the Non-Executive Directors met without the presence of the Executive Directors and the Chairman.

The Chairman and the Chief Executive Officer

The roles of the Chairman and the Chief Executive Officer are separate and clearly defined. Nonetheless, they maintain a close working relationship to ensure integrity of the Board's decision-making process and successful delivery of the Group's strategic priorities.

The roles of the Chairman and the Chief Executive Officer are clearly established, set out in writing and agreed by the Board.

Bob Holt is Non-Executive Chairman. The Chairman creates and manages the constructive dialogue between the Executive and Non-Executive Directors. He works with the Company Secretary to ensure appropriate matters are discussed during Board meetings. David Miles is the Chief Executive Officer. He has the responsibility for leading the Executive Directors and the senior team in the day-to-day management of the business and ensures effective implementation of Group strategy.

Non-Executive Directors and independence of our Board

At the date of this Annual Report, the Group has a Non-Executive Chairman and five Non-Executive Directors. The Non-Executive Directors constructively challenge and develop proposals on strategy and scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They determine appropriate levels of remuneration of Executive Directors and have a prime role in appointing and, where necessary, removing Executive Directors.

Peter Dicks was the Senior Independent Non-Executive Director throughout 2016. Peter is not intending to stand for re-election at the 2018 AGM having reached nine years' service. The Senior Independent Non-Executive Director, if required, will deputise for the Chairman. He is available to talk to shareholders if they have issues or concerns.

In addition to planned Board meetings, the Chairman meets with the Non-Executive Directors to discuss, on a less formal basis, Group performance, strategy, governance and Board succession plans. The Executive Directors do not attend these meetings.

The Chairman, having started the year fulfilling an Executive role, is not considered independent.

The Board considers all other Non-Executive Directors who served during the year to be independent in terms of judgement and character and free from any relationship that might materially interfere with the exercise of independent judgement. Independence of long-serving Independent Non-Executive Directors has been determined as part of the Board appraisal, where conduct and communications recorded from meetings were assessed.

All Directors act in what they consider to be the best interests of the Company, consistent with their statutory duties. The Code suggests that the length of tenure is a factor to consider when determining independence. The Nomination Committee is responsible for the progressive refreshing of the Board's membership. The terms of reference of Non-Executive Directors are reviewed annually as part of the Board performance evaluation.

Activities of the Board during the year

Board discussion during 2016 to deliver strategic priorities

Strategy

- Discussed strategy and performance of both operating segments

Financial performance

- Approval of 2016 budget
- Reviewed performance by business segment
- Approval of 2015 Annual Report and dividend
- Approval of announcement of final results for 2015
- Approval of amend and extend to revolving debt facility
- Approval of interest rate and fuel hedging instruments

Deliver our strategic priorities

1. Deepening our client partnerships in both core markets
2. Maintain quality leadership
3. Develop our people

Read about our strategic priorities on **page 12**

Corporate governance and risk management

- Reviewed and considered matters discussed at Audit Committee meetings
- Selection and appointment of new Non-Executive Directors

Values and ethics

- Review of social mobility plan
- Red Thread
- Review of output from employee satisfaction survey
- Visited our new Rotherham Training Academy

Stakeholder engagement

- Engaged with private shareholders at AGM
- Reviewed and considered investor feedback following final and interim results investor roadshows

Corporate governance report continued
Effectiveness

Board performance evaluation overview

The performance evaluation process included:

- a review of the areas of Board roles and responsibility;
- an internally facilitated review by the Chairman, which included meeting with all Board members individually;
- the structure and composition of the Board and its Committees and the performance of the Committees;
- the quantity, quality and scope of information provided to the Board;
- an assessment of the appropriateness of Directors' terms of reference;
- the content of Board meetings and presentations to meetings; and
- the openness of communications between the Board members and Executive Management.

Board performance

The Chairman is responsible for ensuring Directors are properly briefed on issues to be discussed at Board meetings and that they have full and timely access to relevant information, including minutes of previous Board and Committee meetings. Timely access to information is a priority in order for Directors to be able to consider and present their own challenges to each meeting. The quality and timeliness of information provided to Directors was included as part of the Board evaluation. The findings were that information provided to Directors was thorough and relevant, and in all instances provided suitably in advance.

Director induction and development

The Group's policy is to provide appropriate training to its Directors. Training takes into account each individual's qualifications and experience and includes environmental, social and governance training, tailored to individual requirements as appropriate. The Chairman regularly meets with each Director to review and agree any training and development needs.

All Directors have access to the Company Secretary, who is responsible for ensuring that Board procedures and applicable rules and regulations are observed. All Directors also have unfettered access to the Group's operations and staff. In accordance with Board policy, following her appointment, Julia Unwin received a full, formal and tailored induction relating to all of the Group's activities upon joining the Board.

Board appraisal

Performance evaluation of the Board, its Committees and individual Directors takes place on an annual basis. The 2016 Board performance evaluation was internally facilitated.

The Chairman met with all Board members individually and asked for their views on a broad range of areas including Group strategy, independence, experience, effectiveness, shareholders and the interaction between Board members. Each Board member provided feedback and key observations on the Board's effectiveness as well as suggestions for further enhancement. The performance of the Chairman was reviewed separately in a process led by the Senior Independent Director. The Chairman reviewed the range of feedback provided and identified some broad themes. Some recommendations were proposed which have been implemented, but the overall conclusion was that the Board is working effectively.

An externally facilitated performance evaluation will be conducted during 2017 in line with the requirements of the Code.

Your Board has due regard for the benefits of diversity in its membership, including gender, and strives to maintain the right balance. It comprises individuals with deep knowledge and experience in core and diverse business sectors within local, international and global markets, bringing a wide range of perspectives to the business. This diversity ensures thorough challenge during discussions which results in effectiveness in all aspects of the Board.

Re-election of Directors

To promote good governance, and in accordance with the requirements of the Code, each of the current Directors will offer themselves for re-election annually. Following the evaluation of the Board's performance during the year, it is confirmed that the performance of each of the Non-Executive Directors continues to be effective and that they are considered to demonstrate appropriate commitment to the role.

Indemnifications of Directors

In accordance with our Articles of Association and to the extent permitted by the laws of England and Wales, Directors are granted an indemnity from the Company in respect of liabilities incurred as a result of their position in office. However, our indemnity does not cover Directors or officers in the event of being proven of acting dishonestly or fraudulently.

Shareholder engagement

Principal methods of communication with investors

- Annual Report and Accounts
- Interim statements
- Trading updates
- Quarterly newsletters
- Group website (www.mearsgroup.co.uk)

Investor relations

The Company is committed to maintaining good communications with investors. Normal shareholder contact is the responsibility of the Executive Directors, who respond on a daily basis to queries from institutional and private investors. The Chairman, the Senior Independent Director and other Non-Executive Directors are available to shareholders to discuss any matters they wish to raise. The Directors regularly meet shareholders at operational locations, which both parties find more rewarding as it provides greater insight into the business and its processes. All Directors are available at each AGM and shareholder participation is encouraged.

The Board is committed to maintaining regular contact through the provision of the Annual Report, regular Interim Reports and regular trading updates. This information can be found on the Group's website (www.mearsgroup.co.uk).

There is an active programme of communication with existing and potential shareholders. There is increased dialogue with institutional investors following the publication of final and interim results, which is facilitated through a series of formal presentations.

The Group regularly receives and responds to questions raised by small private shareholders through the investor enquiry portal within the Group's website. In addition, a number of private shareholders attend the Company's AGM.

Feedback from communications with major shareholders and other investors, where necessary, is discussed at each Board meeting. In addition, analyst views are shared prior to Board meetings enabling an opportunity for discussion and challenge. Shareholders are given access to other members of the Senior Management Team, giving an insight into the strength of the Senior Management Team.

The feedback from this year's shareholder dialogue gave consistent support for the Group's Housing strategy, particularly the recent development in Housing Management. The shareholder feedback in respect of Care was less consistent and the Board welcomes this challenge. Succession planning has been identified as a key area for the Group ensuring that there is less reliance on the Group Chief Executive.

The Group has more regular contact with its banking partners, Barclays and HSBC, and the Group values this close relationship.

P F Dicks
Senior Independent Non-Executive Director
peter.dicks@mearsgroup.co.uk
27 March 2017

Q1 2016

Investor meetings prior to the close period.

Following release of final results for 2015, investor roadshow spanning six days, meeting with both 'buy' and 'sell' side.

Q2 2016

Regular update meetings with existing and prospective shareholders.

AGM held in June 2016, providing an opportunity to meet a number of private investors.

Q3 2016

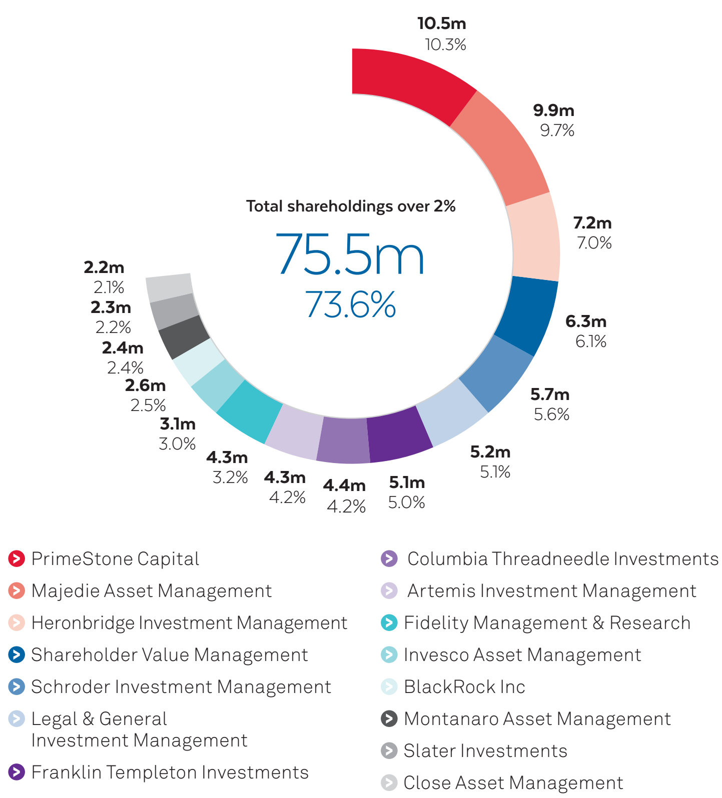
Following release of interim results for 2015, investor roadshow spanning five days, meeting with both 'buy' and 'sell' side.

Q4 2016

Regular update meetings with existing and prospective shareholders.

Investor lunch providing cross-section of fund managers to meet the key management beneath the PLC Board.

Shareholder consultation in respect of setting the remuneration policy for approval at the 2017 AGM.



Report of the Nomination Committee

Introduction

The Nomination Committee ensures there is an effective balance of skills and experience for Board discussions. Succession and diversity are key aspects of our agenda to ensure the Board is continually challenged.

It was with great sadness that, in December 2016, we learnt of the death of Rory Macnamara who had been Chair of the Nomination Committee for the past six years. The Committee had already commenced a process to identify new Non-Executive Directors with the right balance of skills and experience to succeed retiring Non-Executive Directors, and on my appointment as Chair in February 2017 I was delighted to propose the appointment of Roy Irwin and Jason Burt. Together these appointments bring significant and valuable experience. Roy Irwin deepens our understanding of local authorities, and Housing Associations, through a career spent in the housing environment. Jason Burt brings great knowledge of the health and safety operating environment, and his appointment underlines our commitment to outstanding performance in this area. Subject to the approval of shareholders at the 2017 AGM, Roy Irwin and Jason Burt will be formally appointed as Non-Executive Directors.

During the year, the Committee considered the membership of each Board Committee and updated its succession plans for Executive and Non-Executive Directors and senior management. The Committee will search actively for additional Non-Executive Directors who can further enhance the quality of the Board and anticipates the appointment of a further Non-Executive Director during 2017.

Mears has a diverse workforce of around 15,000 employees, including 400 apprentices. The Company believes in promoting diversity at all levels of the organisation. Diversity and respect for all are core to our induction programmes. It will be an important part of my new role to ensure the Group makes further progress in respect of diversity across the Group, including at Board level. During the year, the Group retained its status as one of the Government's Social Mobility Champions. Social mobility is about giving young people equal chances in life, regardless of where they were born, the school they attend or the jobs of their parents. The Government initiative began during 2015 and Mears was one of just twelve UK companies awarded the status of Social Mobility Champion; we have pledged to lead by example – encouraging behavioural change in our business to ensure jobs and opportunities are open to everyone. The benefits of diversity are appropriately balanced with their capabilities, values and approach.

"There is a formal, rigorous and transparent procedure for the appointment of new Directors to the Board. The search for Board candidates is conducted, and appointments are made, on merit, against objective criteria and with due regard to the benefits of diversity on the Board, including gender."

Role of the Committee

The Nomination Committee's responsibilities include:

- keeping under review the composition of the Board and succession to it and succession planning for senior management positions within the Group;
- making recommendations to the Board concerning appointments to the Board, whether of Executive or Non-Executive Directors, having regard to the balance of skills, knowledge, experience and diversity of the Board;
- reviewing the length of service of Non-Executive Directors to ensure a progressive refreshing of the Board, whilst retaining the correct level of experience;
- making recommendations to the Board concerning the re-appointment of any Non-Executive Director at the conclusion of his/her specified term and the re-election of any Director by shareholders under the retirement provisions of the Company's Articles of Association;
- managing a formal, rigorous and transparent procedure for any appointments of new Directors to the Board;
- prior to the appointment of a Director, requiring that the proposed appointee discloses any other business interests that may result in a conflict of interest and reports any future business interests that could result in a conflict of interest; and
- ensuring that, on appointment to the Board, Non-Executive Directors receive a formal letter of appointment setting out clearly what is expected of them in terms of time commitment, Committee service and involvement outside Board meetings.

Committee meetings

Given three Non-Executive Directors reached nine years' service, and can no longer be considered independent, this year has been a particularly active one in terms of ensuring the Board secures new Non-Executive appointments whilst maintaining the right mix of skills and experience. The Committee formally met once during the year with all members of the Committee present at the meeting. In addition to its formal meeting, there was regular contact between Committee members as well as ad hoc meetings with other Board members and management, when deemed necessary by the Committee Chairman, particularly relating to the search process for the new Non-Executive Directors. The Committee considered the balance of skills, experience and diversity of the Board.

The Board acknowledges that diversity extends beyond the boardroom and supports the management effort to build a diverse organisation. The Company believes in promoting diversity at all levels of the organisation; at present 23% of our senior managers are female. The Board is confident that this will increase over time. It is the aspiration of the Board for the diversity in membership to mirror the diversity in our Senior Management Team. Currently 9% of Board members are female (2015: 9%). When considering the optimum composition of the Board, the benefits of diversity are appropriately balanced with their skills, knowledge, experience and approach.

J Unwin
Nomination Committee Chairman
julia.unwin@mearsgroup.co.uk
27 March 2017

Report of the Audit Committee
Accountability


Geraint Davies
Audit Committee Chairman

Introduction

The Audit Committee assists the Board in fulfilling its oversight responsibilities regarding, in particular, the Company's financial and corporate reporting, risk management and internal controls, and the independence and effectiveness of the external auditor.

This report sets out how the Committee has discharged its responsibilities during the year. The Board is required to ensure that the Annual Report is fair, balanced, concise and understandable, and the Committee assists in considering this. This report also sets out, in relation to the financial statements, the significant issues considered and how these were addressed.

I have spent considerable time during my first year as Chairman of the Audit Committee meeting the divisional senior management and I have had a number of detailed review meetings with the Group's Chief Risk Officer (CRO) during which I have obtained a high degree of comfort around the risk management and control environment of the Group. With this being my first full year as Audit Committee Chairman, I believe that I have added fresh challenge and value to what is already a robust process.

The work of the Committee is far-ranging. However, without attempting to summarise here, I would draw attention to the following:

In relation to financial reporting, the two primary significant judgements relate to the carrying value of goodwill and revenue recognition. Both of these have a high level of materiality and also carry a significant level of judgement. In reaching its conclusions, the Audit Committee has had detailed discussions with management and also gained assurance from the procedures carried out by Grant Thornton when testing both areas. In addition to these two, the Audit Committee has included defined benefit pension valuations as a third key estimate. Whilst the valuations are prepared by qualified actuaries providing a high level of comfort as to the reasonableness of the carrying value, the Audit Committee is mindful that in today's volatile economic environment, assumptions around discount rates and corporate bond rates have become unpredictable and can result in a material change in the carrying value of pension assets and liabilities over a short time period.

In relation to risk management and internal control, we focused on financial controls and updating and reviewing the risk register which enables the review of the internal audit plan and the internal audit findings which are produced by our internal audit team led by the CRO. Principal risks are generated from our risk register; further information relating to principal risks can be found on pages 18 to 23. In relation to risk management, the Senior Management Team plays a central role in safeguarding against risk. The Group's risk personnel present risk management training modules to ensure operations are conducted with a strong risk management ethos and I attended and presented at a senior management development event.

In relation to the independence and effectiveness of the external auditor, the Committee continues to review the external audit engagement on an annual basis having carried out a tender exercise in 2013. The review process includes reviewing reports produced by the external auditor, and Committee discussion around the sophistication and appropriateness of audit procedures and approach. The tender process resulted in the re-appointment of Grant Thornton UK LLP, which has been the Group's external auditor since 1996.

The Senior Statutory Auditor, Simon Lowe, will rotate off the Mears audit, in accordance with the Ethical Standards, at the end of the 2016 audit process and a new person will be introduced to this role. The Audit Committee anticipates carrying out an audit tender in 2018.

Role of the Committee

The Committee has access to the financial expertise of the Group and its auditor and, if required, can seek further professional advice at the expense of the Group.

The key responsibilities of the Committee are to:

- → consider the appointment of the external auditor, its reports to the Committee and its independence, including an assessment of its appropriateness to conduct any non-audit work;
- → review the financial statements and announcements relating to the financial performance of the Company;
- → review the internal audit programme and ensure that the internal audit function is adequately resourced and has appropriate standing within the Company;
- → discuss with the external auditor the nature and scope of the audit;
- → review, and challenge where necessary, the actions and judgements of management, in relation to the interim and annual financial statements before submission to the Board;
- → formally review the effectiveness of the external and internal audit processes;
- → consider management's response to any major external or internal audit recommendations;
- → review the Company's plans for business continuity;
- → review the Company's plans for prevention and detection of fraud, bribery and corruption;
- → review the effectiveness of the whistleblowing arrangements; and
- → report to the Board on how it has discharged its responsibilities.

The Committee's terms of reference are available on the Company's website and on request from the Company Secretary.

The Committee comprises financially literate members with the requisite ability and experience to enable it to discharge its responsibilities. With the very sad and untimely death of Rory Macnamara, who had sat on the Committee for six years, I am working with the Chair of the Nomination Committee to find a replacement with suitable recent and relevant financial experience.

Committee meetings

The Committee met five times during the year with attendance by all members. These meetings were also attended by the Group Chief Executive Officer, the Group Finance Director and the Chief Risk Officer as required by invitation from the Chairman of the Audit Committee. The external auditor, Grant Thornton UK LLP, was invited to all meetings. There was also significant dialogue outside formal meetings between Committee members, Executive Directors and the external auditor particularly during the audit process and the preparation of the Annual Report. The Audit Committee Chairman meets with the external auditor regularly throughout the year.

Main activities of the Committee during the year

Financial and business reporting

The Audit Committee shares the responsibility with the Board for reviewing the appropriateness of the Annual Report and half-year announcements, to ensure that they properly reflect the Group's business model, strategic priorities, key risks and financial and non-financial performance. Consideration is given to the reasonableness of the accounting policies, adherence to accounting standards and sufficiency and clarity of the information disclosed.

The primary areas of judgement considered by the Committee in relation to the 2016 accounts, and how these were addressed, were:

Carrying value of goodwill

For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows; these are termed as cash-generating units (CGUs). Due to the Board successfully integrating the newly acquired Care business into the existing Care business, there have been two CGUs identified: Social Housing and Care. Determining whether goodwill is impaired requires an estimate of the value in use of each of the CGUs to which goodwill has been allocated. The value-in-use calculation involves an estimate of the future cash flows of the CGU and also the selection of an appropriate discount rate to calculate present values. Future cash flows are estimated using the current one-year budget, extrapolated for five years to December 2021 using specific rates with a general terminal growth rate being used thereafter. This has been derived from the extensive business planning process described in greater detail within note 10 on pages 114 to 117 of the Annual Report. Estimated growth rates over each period are based on past experience and knowledge of the individual sector's markets. The Directors consider that the estimates and judgements involved in determining the value in use of the Care CGU goodwill are the most significant to the Group and they have therefore utilised the services of an external consultant to assist with this impairment review. The value in use is most sensitive to changes in the terminal growth rate, the explicit growth rate during the forecast period and the discount rate. The sensitivity to changes in these estimations is detailed in note 10. The Audit Committee takes reassurance from the previous year's impairment review, where the key assumptions have subsequently been found to have been reasonably conservative and that the actual results in the subsequent year have delivered better outcomes than anticipated. The headroom in the period, being the excess between value in use compared to carrying value, has increased which gives the Audit Committee further reassurance although the Committee remains mindful that there is still significant uncertainty in the Care sector and key assumptions could change and materially impact upon the carrying value of the Care business.

Report of the Audit Committee continued

Main activities of the Committee during the year continued

Financial and business reporting continued

Carrying value of goodwill continued

The Audit Committee addressed this area of judgement by reviewing the key assumptions proposed by management, notably forecast growth rate, discount rate, terminal growth rate and carer recruitment and retention rates. Given the importance of these assumptions, the Committee also reviewed reports prepared by a third party valuation expert, PwC, which provided validation to the management proposals:

- the Committee reviewed the asset valuation report prepared by PwC on behalf of management to discuss the report in detail. The Committee gave particular focus to the sensitivity analysis which showed the level of changes in key value-in-use calculation assumptions that would be required before triggering any impairment;
- the Committee reviewed the disclosure in the notes to the financial statements; and
- this area represented a prime area of audit focus and Grant Thornton UK LLP provided detailed feedback to the Committee.

Revenue recognition

Revenue is recognised when the outcome of a job or contract can be estimated reliably; revenue associated with the transaction is recognised by reference to the stage of completion of work at the balance sheet date. The outcome of the transaction is deemed to be able to be estimated reliably when all the following conditions are satisfied:

- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the entity;
- the stage of completion of the transaction at the balance sheet date can be measured reliably; and
- the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

Full provision is made for future losses on all contracts in the year in which the loss is first foreseen.

The Audit Committee addressed this area of judgement in the following ways:

- the Committee reviewed the key judgements report prepared by management which provided a detailed explanation in respect of the valuation of unbilled works and the recognition of revenues;
- the Committee took comfort from the contract management system which is central in generating the valuation of works (both billed and unbilled) and the integrated process that follows to ensure an accurate cut-off so that revenue is appropriately matched to cost. Grant Thornton tested these systems during its audit fieldwork and provided feedback to the Committee on this crucial area; and
- this area represented a prime area of external audit focus. Grant Thornton UK LLP carried out both controls-based and substantive testing of the amounts recoverable on contracts, adopting a blend of risk-based and random sampling approaches to testing, and provided detailed feedback to the Committee in this area. Grant Thornton's comments can be seen on page 82.

Defined benefit pension valuation

A number of key estimates have been made, which are given below and which are largely dependent on factors outside the control of the Group:

- inflation rates;
- mortality;
- discount rate; and
- salary and pension increases.

Details of the particular estimates used are included in the pensions note (note 24) on pages 131 to 135.

Where the Group has a contractual right to recover the costs of making good any deficit pension scheme, the fair value of that asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. The Directors have made judgements in respect of whether any of the deficit is as a result of such situations.

The right to recover costs is also limited to situations where the cap on contributions payable by the Group is not set so as to contribute to reducing the deficit in the scheme. The Directors, in conjunction with the scheme actuaries, have made judgements in respect of the predicted future service cost and contributions to the scheme to reflect this in the fair value of the asset recognised.

The Audit Committee addressed this area of judgement in the following ways:

- the Committee reviewed the key assumptions proposed by management, notably assumptions in respect of discount rate, RPI, CPI and future salary increases. Given the materiality of this area, the Committee reviewed a report prepared by Ernst & Young LLP which validated the assumptions set by management and provided a comparison with other quoted companies;
- the Committee reviewed the accounting treatment of pension related transactions. Full disclosure has been provided within the pensions note (note 24) on pages 131 to 135; and
- given the technical nature of this area, the Committee placed reliance upon the actuarial reports prepared by the respective scheme actuaries in respect of each of the defined benefit pension schemes.

Internal control and risk management

With respect to its oversight of risk management and internal controls, the Board reviewed and discussed a wide range of matters with management, internal audit and external audit, as appropriate. This extends to cover all material controls, including operational, compliance and financial controls and risk management systems. The Directors are satisfied that procedures are in place to ensure that the Group complies with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting (the Risk Guidance) published by the Financial Reporting Council in September 2014.

The Board has delegated some of these responsibilities to the Audit Committee which has reviewed the effectiveness of the system of internal control and ensured that any remedial action has been or is being taken on any identified weaknesses. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss. It includes all controls including financial, operational and compliance controls and risk management procedures.

The Group has an ongoing process for identifying, evaluating and managing the significant risks faced by the Group. The Group endeavours to ensure that the appropriate controls, systems and training are in place and has established procedures for all business units to operate appropriate and effective risk management.

The processes used to assess the effectiveness of the internal control systems are ongoing, allowing a cumulative assessment to be made, and include the following:

- → delegation of day-to-day management to operational management within clearly defined systems of control, including:
  - → the identification of levels of authority within clearly identified organisational reporting structures;
  - → the identification and appraisal of financial risks both formally, within the annual process of preparing business plans and budgets, and informally, through close monitoring of operations;
  - → a comprehensive financial reporting system within which actual results are compared with approved budgets, quarterly reforecasts and previous years' figures on a monthly basis and reviewed at both local and Group level; and
  - → an investment evaluation procedure to ensure an appropriate level of approval for all capital and revenue expenditure;
- → discussion and approval by the Board of the Group's strategic directions, plans and objectives and the risks to achieving them, combined with regular reviews by management of the risks to achieving objectives and actions being taken to mitigate them;
- → review and approval by the Board of annual budgets, combined with regular operational and financial reviews of performance against budget, prior year results and regular forecasts by management and the Board;
- → regular reviews by the Board and the Audit Committee of identified fraudulent activity and actions being taken to remedy any control weaknesses;
- → regular reviews by management and the Audit Committee of the scope and results of internal and external audit work across the Group and the implementation of recommendations;
- → consideration by the Board and by the Audit Committee of the major risks facing the Group and of the procedures in place to manage them and to ensure controls react to changes in the Group's overall risk profile. These include health and safety, people, legal compliance, quality assurance, insurance and security, and reputational, social, ethical and environmental risks;
- → discussion relating to a presentation from the IT Director on cyber-security, including an assessment of vulnerabilities and the programmes being implemented to protect the Group against this evolving and potentially catastrophic risk;
- → consideration and discussion relating to regular updates from the Finance Director regarding developments within the finance function; and
- → review of the Group's treasury policies with the Finance Director and Head of Treasury in order to ensure best practice is being adhered to.

The Board has reviewed these procedures and considers them appropriate given the nature of the Group's operations. The Chief Risk Officer (CRO) and the Finance Director presented a report on the robustness of the internal controls for the year and an internal audit plan for 2017. The Committee has concluded that the system of internal control and risk management is embedded into the operations of the Group and the actions taken to mitigate any weaknesses are carefully monitored.

The key controls in place are:

- → a defined organisational structure and an appropriate level of delegated responsibility to operational management;
- → authorisation limits for financial and non-financial transactions;
- → written operational procedures;
- → a robust system of financial budgeting and forecasting;
- → a robust system of financial reporting with actual results compared to budget and forecast results; and
- → regular reporting of operational performance and risks to the Board.

Report of the Audit Committee continued

Main activities of the Committee during the year continued

Internal control and risk management continued

In 2014 a review of internal controls was performed by independent internal audit outsourced partners KPMG. This work was commissioned on a risk-based approach and was performed to provide the Committee with independent assurance over the quality of risk management and strength of internal controls. The procedures performed by KPMG were undertaken within inherently risky areas that would affect KPI performance. This assignment was finalised during 2015 and the independent view of internal controls was that controls were generally adequate, though improvements were suggested. The improvements have been implemented. In line with the Audit Plan for 2017, the Committee anticipates refreshing and extending this review during the course of the coming year.

The Company has in place internal control and risk management systems in relation to the Company's financial reporting process and the Group's process for the preparation of consolidated accounts. The consolidated financial statements are produced by the Group finance function, which is responsible for the review and compilation of reports and financial results from each of the operating subsidiaries in accordance with the Group reporting procedures. The consolidated financial statements are supported by detailed working papers. The Audit Committee is responsible for overseeing and monitoring these processes, which are designed to ensure that the Company complies with relevant regulatory reporting and filing requirements. As at the end of the period covered by this report, the Audit Committee, with the participation of the Chief Executive Officer and the Finance Director, evaluated the effectiveness of the design and operation of disclosure controls and procedures designed to ensure that information required to be disclosed in financial reports is recorded, processed, summarised and reported within specified time periods.

The Committee carried out a review of its effectiveness with input from Committee and Board members, management and the external auditor. The review concluded that the Audit Committee members had sufficient expertise and committed time to discharge their responsibilities.

External audit related services

The Committee is also responsible for monitoring and reviewing the performance, independence and objectivity of Grant Thornton UK LLP, the external auditor. The external auditor has also confirmed that it has complied with relevant UK independence standards. It is expected that the formal rotation of the current lead audit partner will be effective from the audit of the financial statements for 2017.

During the year the Financial Reporting Council (FRC) undertook an audit quality review of the Grant Thornton statutory audit of 2015. The results were discussed separately by me with both the FRC and Grant Thornton. The Audit Committee was pleased with the positive outcome and two minor amendments have been made to the audit process for the current year.

The Company has adopted a strict policy of prohibiting the external auditor from carrying out non-audit services, in order to safeguard audit objectivity and independence. The Committee is responsible for approval of all non-audit services provided by Grant Thornton; however, this is considered to be in exceptional circumstances only. In such an exceptional event, the Audit Committee would approve only where the Company would be disadvantaged by engaging an alternative provider, for instance where Grant Thornton possesses a detailed knowledge of the structure of the business or an understanding of the markets that the Group operates in.

During 2016, Mears was delighted to retain its accreditation with Investors in People (IIP). This followed a four-week assessment programme which involved external assessors visiting 16 branches and interviewing around 300 employees. IIP in the South of England is delivered by Grant Thornton under licence from the UK Commission for Employment and Skills. Whilst Mears played no part in the selection of Grant Thornton as its external assessor, the fee of £45,000 paid to Grant Thornton for this assessment is required to be disclosed within non-audit services. Other than in respect of this IIP assessment, there were no fees paid to Grant Thornton during the year in respect of non-audit services. In the comparative 2015 year, fees relating to non-audit services amounted to £0.03m, being 7% of total fees.

G Davies
Audit Committee Chairman
geraint.davies@mearsgroup.co.uk
27 March 2017

Report of the Remuneration Committee

Dear shareholder,

On behalf of the Board, I am pleased to present the report on Directors' remuneration for 2016.

You will have read earlier in the Annual Report that 2016 has been a solid year of further progress for the Company. During the last twelve months, the Company has continued to make significant progress in a number of areas including:

- achieving a broader housing service offering;
- an important step forward with the award of the long-term joint venture partnership with Milton Keynes Council;
- an order book standing at £3.1 billion with solid visibility for 93% of 2016 consensus revenues reflecting strong progress in positioning the business for the future; and
- continued financial discipline evidenced by conservative accounting policies and a track record of strong cash management.

Despite progress made during the year that ensures that the Group is well positioned, the external operating environment around the Care business remains challenging, impacting earnings for the year. As a result, there will be no contribution to the Management Incentive Plan (MIP) in 2016. Details of our performance against MIP targets are as follows.

Performance measures*	Threshold	Maximum	Actual
EPS growth	8%	13%	5%
TSR growth	10%	20%	3%
Cash conversion (underpin)	80%	80%	70%
ROCE (underpin)	10%	10%	18%

* See pages 73 and 74 for definitions of performance measures and actual remuneration outcomes.

Review of remuneration policy

The Company's remuneration policy was last approved at the 2014 AGM and as such is due for renewal at the 2017 AGM. During the year, the Committee undertook an in-depth review of the current policy to ensure that we have in place a forward-looking policy that supports the evolving business strategy, striking a balance between short-term corporate success and long-term value creation ensuring there is no payment for failure.

In making its review, the Remuneration Committee also considered the goals it would like the remuneration policy to support. These are set out below:

- ensuring that Executive remuneration is linked to performance and sustained achievement of annual financial, strategic and operational objectives which lead to the creation of long-term shareholder value;
- providing greater alignment between Executives' interests and those of shareholders;
- awareness of the need for more fairness in pay outcomes across the wider workforce;
- maintaining flexibility, in recognition of the uncertain business environment, while making sure that remuneration outcomes are aligned to long-term shareholder interests by ensuring a significant proportion of any incentive payout is linked to the achievement of hard financial targets; and

Report of the Remuneration Committee continued

"The Company's remuneration structure has been designed to support the evolving business strategy and foster a pay for performance culture, helping us achieve our corporate goals."

Review of remuneration policy continued

→ shareholder support for the rationale and structure of Executive remuneration of our key Executives who are critical to executing the business strategy.

Following the review, the Committee determined that it wanted to retain the simplified salary and single 'deferred annual bonus' style incentive arrangement but that it needed to make a number of key changes primarily targeted at further strengthening the alignment of Executive pay with the interests of shareholders. These changes are designed to bring parts of the structure into line with best practice corporate governance whilst recognising certain aspects of the industry in which our employees operate.

The Company is proposing to introduce a new incentive arrangement, the Executive Incentive Plan (EIP), which will replace the current Management Incentive Plan (MIP). The EIP, which will be split into two parts, simplifies the current annual incentive arrangement through the removal of the bonus banking construct and the cash payment mechanism. Significantly, under the EIP, annual award levels will be reduced from 250% to 200% of salary, paid in shares with no element of cash bonus. This reduction in incentive value has been largely driven by the Executive team, which is mindful of the pay structure of the wider workforce and wants to implement a greater fairness in pay structure. The Remuneration Committee is comfortable that this reduction in award levels does not present a retention risk as the proposed structure is designed to enable management to build up a meaningful level of equity in the business over the next five years.

Of the reduced annual award level of 200% of salary, 100% of salary will be granted in deferred shares to ensure that the management team is locked in over the next five years. This element of the award will feature a financial underpin relating to earnings growth. Management is therefore provided with the opportunity to build up a meaningful stake in the business which ensures simple alignment with the long-term sustainable performance of the business. Furthermore, the high probability of payout of this element provides an enhanced lock in mechanism to reflect the reduction in award levels.

The other 100% of salary will be granted as a 'performance on grant' type share award and will be granted based on the successful achievement of a range of annual performance measures which support the business strategy on a rolling basis. Amounts earned will vest over a three to five-year period on the same basis as the deferred share award. The Committee believes that it is important that shares start to vest at the three-year point rather than a longer period in order to ensure strong alignment with the interests of shareholders and the tenure of the management team.

The EIP has been designed to ensure that it is fully aligned with the strategic priorities of the Group and provides a holistic assessment of overall corporate performance. The deferred share element featuring an EPS underpin provides a simple alignment with the long-term sustainable performance of the business by ensuring that management can build up and retain a meaningful shareholding in the Company.

The performance element of the EIP focuses on those metrics which will drive long-term value creation on a rolling basis from both:

→ a financial and operational perspective – growing earnings (EPS) and the quality of those earnings (ROCE) from both an organic and non-organic perspective balanced with strong cash and balance sheet management (cash conversion); and

→ a strategic perspective – strong customer service and our good health and safety record which helps win new contracts with end users and support new innovative operating models.

Specific targets will be set on an annual basis taking account of both the short and medium-term business plan to ensure that the targets are sufficiently stretching and in the best interest of the shareholders. The Committee is mindful to ensure that there is no payment for poor performance and will therefore ensure that it reviews all incentive awards prior to grant and will exercise discretion to moderate the total annual incentive outcomes if necessary, to ensure that they balance management performance and the shareholder experience in any given financial year.

Other remuneration and related issues

The Remuneration Committee is acutely aware of the sensitivity around increasing pay levels in excess of the general workforce increase but believes that this is necessary to retain individuals as part of an overall remuneration strategy in which overall levels of remuneration remain conservative and a high proportion of total pay is delivered in long-term equity. As such it should be noted, that even after the proposed increases, the remuneration of the Executive Directors will be some of the lowest in the sector.

Furthermore, the shareholding requirement will be increased over time to 400% of salary to reflect the new share award structure. This will ensure that the Executive Directors build up a meaningful shareholding in the Company so that their interests are directly aligned with those of shareholders in line with investor sentiment.

2017 AGM

The Committee wishes to thank those shareholders who have actively engaged in helping the Committee shape a new remuneration policy. We have taken feedback into account and believe we have a structure that will both retain and motivate management, while being sensitive to the external and internal operating environment.

The Directors' remuneration policy will be subject to a binding shareholder vote, and the Annual Report on Remuneration along with this statement will be subject to an advisory shareholder vote at the forthcoming AGM on 7 June 2017.

I hope that you find the information in this report helpful and I look forward to your support at the forthcoming AGM. I am always happy to hear from the Company's shareholders and you can contact me direct, or via the Company Secretary, Ben Westran, if you have any questions on this report or more generally in relation to the Company's remuneration.

P F Dicks
Remuneration Committee Chairman
peter.dicks@mearsgroup.co.uk
27 March 2017

Remuneration policy

Directors' remuneration policy

Remuneration policy and philosophy

Remuneration policy	How is this achieved?
A simple and transparent remuneration structure that retains and motivates Executives while being sympathetic to Mears' operating environment from both an external and internal perspective.	→ Conservative levels of fixed remuneration balanced with one annual incentive strongly linked to performance. → The performance element of the annual incentive incorporates robust financial, operational and strategic KPIs that are aligned with an evolving business strategy in an uncertain economic environment. → All incentive payments are deferred into equity over a five-year period ensuring clear alignment with shareholders' interests and 'at-risk' remuneration.
A proportion of each Executive's total compensation should be linked to performance related pay and the provision of equity.	→ All incentive payments are delivered in 'deferred' shares. At stretching performance, around one third of the Executive Directors' total remuneration is based on the achievement of key corporate metrics that are aligned to the Company's long-term strategy.
There should be a commitment to fostering a performance culture that aligns an individual's rewards with the key corporate metrics that drive shareholder value creation.	→ The performance measures used in the Executive Incentive Plan are directly aligned with our corporate goals and as such ensure that there is no payment for poor performance. → The Committee will ensure that the remuneration package does not lead to irresponsible behaviour and that it takes appropriate account of risk.

Executive Directors

The table below sets out the key elements of the policy for Executive Directors:

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Base salary			
The purpose of the base salary is to: → help recruit and retain key individuals; → reflect the individual's experience, role and contribution within the Group; and → ensure fair reward for 'doing the job'.	The Committee reviews base salaries annually in April. The Committee will retain the discretion to increase an individual's salary where there is a significant difference between current levels and a market competitive rate. When determining base salaries and whether to increase levels the Committee will take the following into consideration: → the performance of the individual Executive Director; → the individual Executive Director's experience and responsibilities; → the impact on fixed costs of any increase; → pay and conditions throughout the Group; and → the economic environment. When setting the salary levels for the Executive Directors, in addition to the factors summarised above, salary levels paid by companies of a similar size and complexity to Mears are taken into account.	The annual increase will not exceed 10% of annual base salary. The Committee is guided by the general increase for the broader employee population but may decide to award a lower increase for Executive Directors or indeed exceed this to recognise, for example, an increase in the scale, scope or responsibility of the role and/or to take into account relevant market movements. The Company will set out in the section headed Implementation of Remuneration Policy, in the following financial year, the salaries for that year for each of the Executive Directors.	Not applicable.

Remuneration policy continued

Directors' remuneration policy continued

Executive Directors continued

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Other benefits			
To provide benefits that are valued by the recipient and are appropriately competitive.	The Executive Directors receive additional benefits including a company-provided car or an allowance in lieu, life assurance and private medical insurance. Other benefits may be provided where appropriate. Benefits in kind are not pensionable.	Benefit values vary year on year depending on premiums and the maximum potential value is the cost of these provisions.	Not applicable.
Pension			
To provide a framework to save for retirement that is appropriately competitive.	All Executive Directors receive a contribution into their respective defined contribution plans, which are subject to periodic review to ensure that they remain in line with rates applicable in the market. Only the base salary is pensionable.	The Executive Directors receive a contribution of 15% of salary.	Not applicable.
Executive Incentive Plan (EIP)			
To provide a link between reward and corporate performance in order to appropriately retain and motivate the Executive Directors and senior management who are critical to executing the business strategy. To align the interests of Executive Directors and senior management more closely with shareholders over the longer term and provide a greater exposure to share price movements over this period.	Annual awards of nil-cost options will be made based on the achievement of annual performance measures. Awards will be made in two parts: → 50% of the maximum award will be granted in deferred shares ("Part A"); and → 50% of the maximum award will be granted based on the achievement of a range of annual performance measures ("Part B"). Both awards will vest 60% after three years, with a further 20% after four years and the remaining 20% after five years. The Committee may award dividends/dividend equivalents on shares to the extent that the shares vest. In exceptional circumstances (such as recruitment) the Committee retains the discretion to provide an element of the award in cash. Further details of the operation of the EIP, including the performance measures for 2017, are set out on pages 76 and 77.	Annual awards made to Executive Directors will be capped at a maximum of 200% of salary. For Part A of the award, 100% will vest if the EPS metric is met in full. For Part B of the award: → 20% of the award will vest for threshold performance; and → 100% of the award will vest for maximum performance. There is straight-line vesting between these points.	The performance measure for Part A will be earnings per share. The performance measures for Part B of the 2017 awards are as follows: earnings per share (EPS), return on capital employed (ROCE), cash conversion, customer satisfaction and health and safety. The Remuneration Committee has discretion to set performance measures and weightings on an annual basis, with performance measures for the next financial year set out in the Statement of Implementation on pages 76 to 78. The EIP contains malus (up to date of vesting) and clawback (two years post vesting) provisions.

Directors' remuneration policy continued

Executive Directors continued

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
All-employee share plans			
Encourages employees to own shares in order to increase alignment over the longer term.	All employees are eligible to participate in the Company's Share Incentive Plan (SIP) and Sharesave Plan. Under the terms of the Sharesave Plan all employees can apply for three or five-year options to acquire the Company's shares priced at a discount of up to 20%. Under the terms of the SIP the Company can choose to offer free shares, partnership shares, matching shares (up to two for one on any partnership shares purchased) and/or dividend shares. In addition the Company operates a discretionary unapproved share plan and a Company Share Option Plan (CSOP). No awards to Executive Directors are proposed under these plans.	Under the SIP, Sharesave and CSOP, the maximum amount is equal to the regulatory limits set from time to time.	Not applicable.
Shareholding requirement			
Secures a long-term locked-in alignment between the Executive Directors and shareholders, ensuring that they build up and maintain a minimum level of shareholding throughout their employment with the Company.	The shareholding requirement will operate in the following manner: → only shares unconditionally owned by the Executive Director will count against the requirement; and → shares can be built up over a five-year period from implementation of the policy through the vesting and retention of share awards and/or MIP/EIP payments.	Minimum shareholding requirement is 400% of salary.	Not applicable.
Provisions of previous policy that will continue to apply			
Management Incentive Plan (MIP)	Participants have a plan account into which annual contributions by Mears are made. No further contributions are due to be made under the new policy. Each year participants are entitled to withdraw up to 50% of the plan account balance in cash or shares with the remaining 50% deferred in shares. 50% of the plan account is at risk of forfeiture each year if minimum levels of performance are not met. 2017 is the final year of the MIP. No further contributions will be made; however, the final balance of a participant's plan account is due to be paid out in shares. The Committee has determined that this final payment will be deferred into shares which vest in annual instalments (rather than a single payment) over 2017–2019. Further details of the operation of the MIP, including the performance measures for 2016, are set out on page 73.	No further contributions can be made to participants' plan accounts under the MIP.	Not applicable.

Remuneration policy continued

Directors' remuneration policy continued

Notes to the future policy table

Changes to remuneration policy from previous policy

The Management Incentive Plan (MIP) has been replaced by the EIP as the Company's variable incentive arrangement. The EIP retains the single 'deferred annual bonus' style of the MIP but has a small number of key changes which are designed to further strengthen the alignment of the Executives' pay with the interests of shareholders.

- Under the EIP, awards will be made 100% in shares rather than split between cash and shares.
- An element of deferral has been retained with awards vesting 60% after three years, 20% after four years and 20% after five years. This compares to the MIP, which had a decreasing length of holding period as the plan progressed.
- Maximum award levels have been reduced from 250% of salary to 200% of salary. Of this, 100% of salary will be granted as deferred shares. The remaining 100% of salary will be awarded based on the successful achievement of a range of annual performance measures, as per the previous construct.
- Strategic and operational performance measures have been introduced to sit alongside the previous EPS and TSR measures.
- Malus and clawback provisions have been introduced in line with UK corporate governance best practice.

Deferred awards under the MIP will continue to vest though the payment schedule, which has been increased to four years from two to provide further alignment between Executive Directors and shareholders. See page 73 for further details.

In addition to the all-employee Sharesave Plan, the Company is intending to introduce the Mears Share Incentive Plan (SIP).

The previous Share Plan will not continue to operate for Executive Directors under the new policy. All awards under this incentive have now vested.

Reasons for selecting performance measures

The Committee wanted to ensure that the performance measures selected provide a holistic assessment of overall corporate performance and tie in to the non-financial objectives that the Company embraces throughout the organisation.

EPS growth has been selected as it provides direct alignment to the Company's strategic objectives over the long term and is also transparent, fully understood by participants and an externally audited metric over which they have line of sight.

The use of ROCE and cash conversion (previously incorporated as underpins) ensures that quality of earning is protected and the Company maintains strong working capital management.

Customer satisfaction and health and safety performance conditions are included as these are key KPIs that the Company focuses on and by performing strongly in these areas, it will help win new contracts with end users and support new innovative operating models.

Targets are calibrated to reflect the Committee's assessment of good to exceptional performance and taking into account internal budgets and the current economic environment.

Differences in remuneration policy for all employees

The Company sets terms and conditions for employees which reflect the different legislative and labour market conditions that operate in each of our jurisdictions. We will always meet or exceed national minimum standards for terms and conditions of employment in each of our business areas. Pay arrangements in our businesses also reflect local performance with personal increases based on achievement, individually assessed. Mears believes in the value of continuous improvement, both for the individual and for the Company.

In general, all employees receive base salary, benefits and pension, and are eligible to participate in the Company's share plans. Share awards and bonus plans are cascaded down below Executive level to senior management, aligning the Senior Management Team to deliver value for the Group.

The remuneration of the Executive Directors and Senior Executives is more heavily weighted towards variable pay than for other employees with a large proportion of their overall package dependent on successful and sustained execution of the business strategy over the longer term.

Committee discretions

The Committee will operate the EIP and MIP according to their respective rules. The Committee retains discretion, consistent with market practice, in a number of regards to the operation and administration of these plans. These include, but are not limited to, the following:

- the participants;
- the timing of grant of an award;
- the size of an award;
- the determination of vesting;
- discretion required when dealing with a change of control or restructuring of the Group;
- determination of the treatment of leavers based on the rules of the plan and the appropriate treatment chosen;
- adjustments required in certain circumstances (e.g. rights issues, corporate restructuring events and special dividends);
- the annual review of performance measures and weighting for the EIP and exercise conditions (if any) for the EIP and the MIP; and
- in exceptional circumstances the payment of a proportion of the EIP in cash.

These discretions, which in certain circumstances can be operated in both an upward and downward manner, are consistent with market practice and are deemed necessary for the proper and fair operation of the schemes in order to achieve their original purpose. It is the Committee's policy, however, that there should be no element of reward for poor performance and any upward discretion will only be applied in exceptional circumstances.

Directors' remuneration policy continued

Illustrations of application of remuneration policy

We estimate that the level of remuneration received by each Executive Director for the first full year in which the policy applies will be, indicatively, at three different levels of performance:

- minimum performance includes where only fixed pay (salary, benefits and pension);
- on-target performance includes Part A of the EIP and 60% of Part B of the EIP; and
- maximum performance includes the maximum opportunity under the EIP.

Fixed pay is base salary for 2017 plus the value of pension and other benefits.

The charts demonstrate the balance between fixed and variable pay for minimum, threshold and maximum performance for Executive Directors' remuneration in 2017 in line with the relevant policy.

Approach to recruitment remuneration

In the event that the Company recruits a new Executive Director (either from within the organisation or externally), when determining appropriate remuneration arrangements, the Committee will take into consideration all relevant factors (including but not limited to quantum, the type of remuneration being offered and the jurisdiction the candidate was recruited from) to ensure that arrangements are in the best interests of both the Company and its shareholders without paying more than is necessary to recruit an Executive of the required calibre.

The Committee would generally seek to align the remuneration of any new Executive Director following the same principles as for the current Executive Directors (set out in the table on page 70).

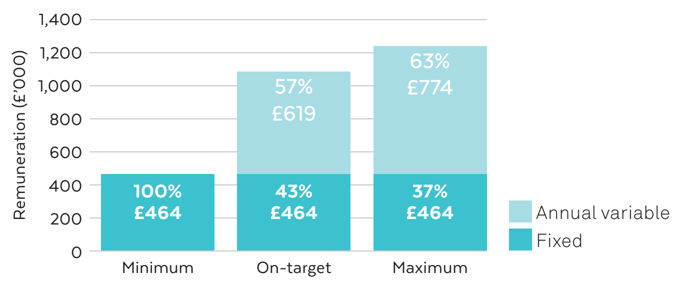
The elements that would be considered by the Company for inclusion in the remuneration package for a new Director are in line with those offered to existing Directors (see policy table on pages 63 to 65 for more details):

- salary and benefits including defined contribution pension participation or a salary supplement in lieu of pension provision;
- participation in the EIP of up to 200% of salary;
- participation in all-employee share plans operating at that time; and
- costs relating to but not limited to relocation, legal, financial, tax and visa advice and pre-employment medical checks.

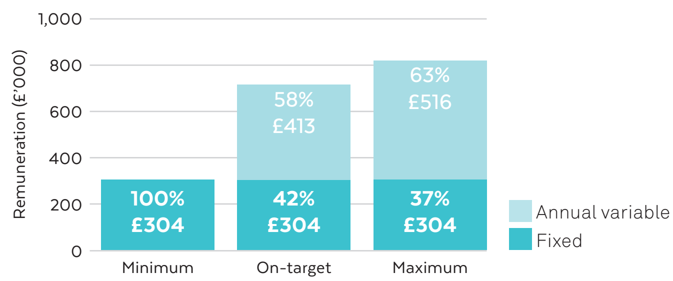
The maximum variable remuneration will be 200% of salary.

The Committee may make awards on appointing an Executive Director to 'buy out' remuneration arrangements forfeited on leaving a previous employer. Awards made by way of compensation for forfeited awards would be made on a comparable basis, taking account of performance achieved (or likely to be achieved), the proportion of the performance period remaining and the form of the award. Compensation could be in cash or shares.

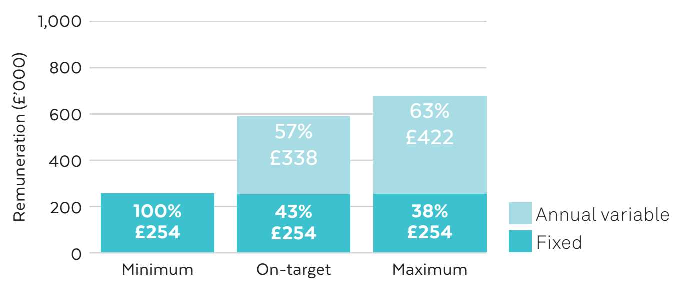
D J Miles



A C M Smith



A Long



Remuneration policy continued

Directors' remuneration policy continued

Approach to recruitment remuneration continued

The Committee's policy is for all Executive Directors to have rolling service contracts with a notice period of twelve months, unless on an exceptional basis to complete an external recruitment successfully, when a longer initial period reducing to twelve months may be used.

Service contracts and payment for loss of office

Director	Date of contract/ letter of appointment	Notice period by Company or Director
Executive		
D J Miles	June 2008	12 months
A C M Smith	June 2008	12 months
A Long	August 2009	12 months
Chairman/Non-Executive		
R Holt	June 2015	Rolling 6-month appointment
D L Hosein	June 2008	Rolling 6-month appointment
M G Rogers	June 2008	Rolling 6-month appointment
P F Dicks	June 2008	Rolling 6-month appointment
R Macnamara	June 2010	Rolling 6-month appointment
G Davies	October 2015	Rolling 6-month appointment
J Unwin	January 2016	Rolling 6-month appointment
J Burt	February 2017	Rolling 6-month appointment
R Irwin	February 2017	Rolling 6-month appointment

All Executive Directors' contracts are rolling and, therefore, will continue unless terminated by written notice. In the event of the termination of an Executive Director's contract, salary and benefits will be payable during the notice period. There will, however, be no automatic entitlement to bonus payments or share incentive grants during the period of notice.

The rules of the EIP and the MIP set out what happens to awards if a participant ceases to be an employee or Director of Mears before the end of the vesting period. Generally, any outstanding share awards will lapse on such cessation, except in certain circumstances.

If the Executive Director ceases to be an employee or Director as a result of death, injury, ill health, redundancy, retirement, the sale of the business or company that employs the individual or any other reason at the discretion of the Committee, then they will be treated as a 'good leaver' under the plan rules.

Under the EIP, a proportion of a good leaver's award will vest on cessation of employment by reference to the time elapsed from grant to cessation. The Committee has discretion to determine the period during which the good leaver may exercise their award after cessation.

On a change of control, all awards under the EIP will vest immediately.

Under the MIP, a good leaver's accumulated plan account (as measured at the date of cessation of employment) will be paid to them. For other leavers, any amounts not vested will lapse. On a change of control, the accumulated plan accounts of all participants (as measured at the date of change of control) will be paid to them.

Directors' remuneration policy continued

Chairman and Non-Executive Directors

The Board as a whole is responsible for setting the remuneration of the Non-Executive Directors, other than the Chairman whose remuneration is determined by the Committee and recommended to the Board.

The table below sets out the key elements of the policy for the Chairman and Non-Executive Directors.

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessments
To provide compensation that attracts individuals with appropriate knowledge and experience.	Fee levels are reviewed periodically taking into account independent advice and the time commitment required of Non-Executive Directors. The fees paid to the Chairman and the fees of the other Non-Executive Directors aim to be competitive with other listed companies which the Committee (in the case of the Chairman) and the Board (in respect of the Non-Executive Directors) consider to be of equivalent size and complexity. Non-Executive Directors receive a base fee and additional fees for the role of Senior Independent Director or membership and/or chairmanship of certain Committees. The Chairman receives a single fee and does not receive any additional fees for membership and/or chairmanship of Committees. Non-Executive Directors also receive reimbursement of reasonable expenses (and any tax thereon) incurred through undertaking their duties and/or Company business.	Any increase in Non-Executive Director base fees or additional Committee/membership fees (if introduced) may be above the level awarded to other employees, given that they may only be reviewed periodically and may need to reflect any changes to time commitments or responsibilities. The maximum potential value of any benefits provided is the cost of these provisions. The Company will pay reasonable expenses incurred by Non-Executive Directors. Current fee levels are set out in the Statement of Implementation on page 76.	Non-Executive Director fees are not performance related. Non-Executive Directors do not receive any variable remuneration element.

Remuneration policy continued

Directors' remuneration policy continued

Other Non-Executive appointments

Executive Directors have an obligation to inform the Board, specifically the Remuneration Committee, of any Non-Executive positions held or being contemplated and of the associated remuneration package. The Remuneration Committee will consider the merits of each case and carefully consider the work and time commitment required to fulfil the Non-Executive duties and the potential benefit to the Group and then determine whether the remuneration should be retained by the Executive or passed over to the Group.

Consideration of employment conditions elsewhere in the Company in developing policy

In setting the remuneration policy for Executive Directors, the Remuneration Committee takes into account Group and business unit performance including both financial performance and safety improvements in the year. Due to the wide variety of labour market conditions and the markets in which we operate, pay rates are not normally considered when considering Executive Director base pay reviews. The Remuneration Committee reviews and notes the salaries of Senior Executives within the Group.

The Committee has not expressly sought the views of employees and no remuneration comparison measurements were used when drawing up the Directors' remuneration policy. Through the Board, however, the Committee is updated as to employee views on remuneration generally.

Consideration of shareholder views

The Committee is committed to an ongoing dialogue with shareholders and seeks shareholder views when any significant changes are being made to remuneration arrangements. We remain sensitive to the views of shareholders and sought to consult many of our largest shareholders regarding the changes we are proposing to the remuneration policy.

As a result of the feedback received, the Committee made a number of changes to the initial design to ensure that the new incentives are delivering the necessary lock-in and motivation to deliver long-term shareholder value, particularly given the reduction in total share-based incentive levels from 250% to 200%.

The Company will continue to monitor shareholder comments and retain an open dialogue as necessary.

Annual remuneration report 2016

Annual report on remuneration

This section of the Remuneration Report contains details of how the Company's remuneration policy for Directors was implemented during the financial year.

Single total figure of remuneration (audited)

Executive Directors

The remuneration of Executive Directors showing the breakdown between elements and comparative figures is shown below. Figures provided have been calculated in accordance with the regulations.

Executive Director (£'000)	Year	Salary	Taxable benefits	Pension	Annual incentives	Total remuneration
D J Miles	**2016**	**363**	**19**	**54**	**—**	**436**
	2015	363	19	54	—	436
A C M Smith	**2016**	**242**	**7**	**36**	**—**	**285**
	2015	242	7	36	—	285
A Long	**2016**	**198**	**11**	**30**	**—**	**239**
	2015	198	11	30	—	239

Annual report on remuneration continued

Single total figure of remuneration (audited) continued

Non-Executive Directors

The remuneration of Non-Executive Directors showing the breakdown between elements and comparative figures is shown below. Figures provided have been calculated in accordance with the regulations.

Chairman and Non-Executive Director (£'000)	Year	Basic fees	Additional fees	Other	Total fees
R Holt	**2016**	**250**	**—**	**95**[1]	**345**
	2015	250	—	95	345
D L Hosein	**2016**	**45**	**—**	**—**	**45**
	2015	45	—	—	45
M G Rogers	**2016**	**45**	**—**	**—**	**45**
	2015	45	—	3	48
P F Dicks	**2016**	**45**	**—**	**—**	**45**
	2015	45	—	—	45
D Marston	**2016**	**—**	**—**	**—**	**—**
	2015	22	—	—	22
R Macnamara	**2016**	**45**	**—**	**—**	**45**
	2015	45	—	—	45
G Davies	**2016**	**45**	**—**	**—**	**45**
	2015	11	—	—	11
J Unwin	**2016**	**45**	**—**	**—**	**45**
	2015	—	—	—	—

1. From the 2017 AGM, R Holt will receive no benefits.

Annual remuneration report 2016 continued

Annual report on remuneration continued

Additional details in respect of single total figure table (audited)

The outcome of the MIP for the year ended 31 December 2016, being year four on the schematic, is set out on page 73. The following schematic illustrates the operation of the MIP:

Annual report on remuneration continued

Additional details in respect of single total figure table (audited) continued

The performance measures and targets for the MIP for the year ended 31 December 2016 are detailed below:

Description	Weighting	Calculation	Targets
Earnings per share (EPS)	80%	→ Growth in diluted EPS. Diluted EPS is stated before exceptional costs, share-based payments, costs relating to the MIP and amortisation of acquisition intangibles and is adjusted for a normalised tax charge from 1 January 2016 to 31 December 2016. → Base figure of 29.58p to be used.	→ Threshold: 8% EPS growth leads to 20% maximum contribution. → Maximum: 13% EPS growth leads to 100% maximum contribution. → Straight-line contribution between 8% and 13% growth.
Absolute total shareholder return (TSR)	20%	→ Growth in absolute TSR from 1 January 2016 to 31 December 2016 (using an average period of 30 days for both dates). → Starting share price is £4.47.	→ Threshold: 10% TSR growth leads to 20% maximum contribution. → Maximum: 15% TSR growth leads to 100% maximum contribution. → Straight-line contribution between 10% and 15% growth.
Cash conversion (underpin)	N/A	→ Cash inflow from operating activities as a proportion of operating profit before acquisition intangible amortisation measured at 31 December 2016.	→ A threshold level of cash conversion of 80% must be achieved. → If this threshold level is not achieved, 50% of any annual contribution in relation to EPS will be forfeited.
Return on capital employed (ROCE) (underpin)	N/A	→ Operating profit before acquisition intangible amortisation and exceptional costs/(total assets – current liabilities less all balances relating to bank borrowings and overdrafts classified within non-current liabilities) at 31 December 2016.	→ A threshold level of ROCE of 10% must be achieved. → If this threshold level is not achieved, 50% of any annual contribution in relation to EPS will be forfeited.

The actual performance achievement is summarised below:

Performance measures	Actual	% of target satisfied
EPS growth	5%	0%
TSR growth	3%	0%
Cash conversion (underpin)	82%	Yes
ROCE (underpin)	18%	Yes

The Remuneration Committee was also satisfied that a minimum level of corporate performance had been exceeded and so no forfeiture of the accumulated plan account was necessary.

Annual remuneration report 2016 continued

Annual report on remuneration continued

Additional details in respect of single total figure table (audited) continued

The value of plan accounts following the contribution for the year is set out below:

	D J Miles	A C M Smith	A Long
2015 closing balance brought forward (shares)	207,998	138,665	113,453
2015 closing balance brought forward (£)[1]	948,469	632,313	517,347
2016 contribution (£)	—	—	—
% of salary	—	—	—
2016 plan account balance (£)	948,469	632,313	517,347
2016 plan account balance (shares)[1]	207,998	138,665	113,453
2016 account balance to be withdrawn in shares (£)	474,235	316,157	258,674
2016 account plan balance converted into deferred shares, vesting over 2017 and 2019 (shares)	103,999	69,333	56,727

1. Using share price as at 31 December 2016 = 456p.

As set out in the policy, it is proposed that, following the withdrawal of 50% of the 2016 plan account balance in shares, the remaining balance will be converted into deferred shares, with vesting in annual instalments over 2017 to 2019. The Committee believes that the change to the timings of payments and 100% use of shares will provide further alignment between Executive Directors and shareholders. The deferred shares remain subject to continued employment and as such only the portion vesting each year will be included in the single figure table.

Statement of Directors' shareholding and share interests (audited)

Directors' share interests are set out below:

		Share interests		
		Conditional unvested	Vested but unexercised	
Director	Number of beneficially owned shares	Share awards/ options	Options	Total interests held at year end
D J Miles	175,020	103,999	164,729	443,748
A C M Smith	110,000	69,333	69,333	248,666
A Long	36,230	56,727	56,727	149,684
R Holt	—	—	150,000	150,000
D L Hosein	—	—	—	—
M G Rogers	40,000	—	—	40,000
P F Dicks	39,541	—	—	39,541
G Davies	2,500	—	—	2,500
J Unwin	—	—	—	—
J Burt	—	—	—	—
R Irwin	—	—	—	—

On 29 April 2016 the following Directors and connected persons exercised options over shares received pursuant to the Mears Group PLC Share Plan (2013):

Director	Date of transaction	Number of options exercised and sold	Option price	Sale price per share	Gain on exercise
D J Miles	29 April 2016	203,367	1p per share	£4.00	811,434
A C M Smith	29 April 2016	135,578	1p per share	£4.00	540,956
A Long	29 April 2016	110,927	1p per share	£4.00	442,599

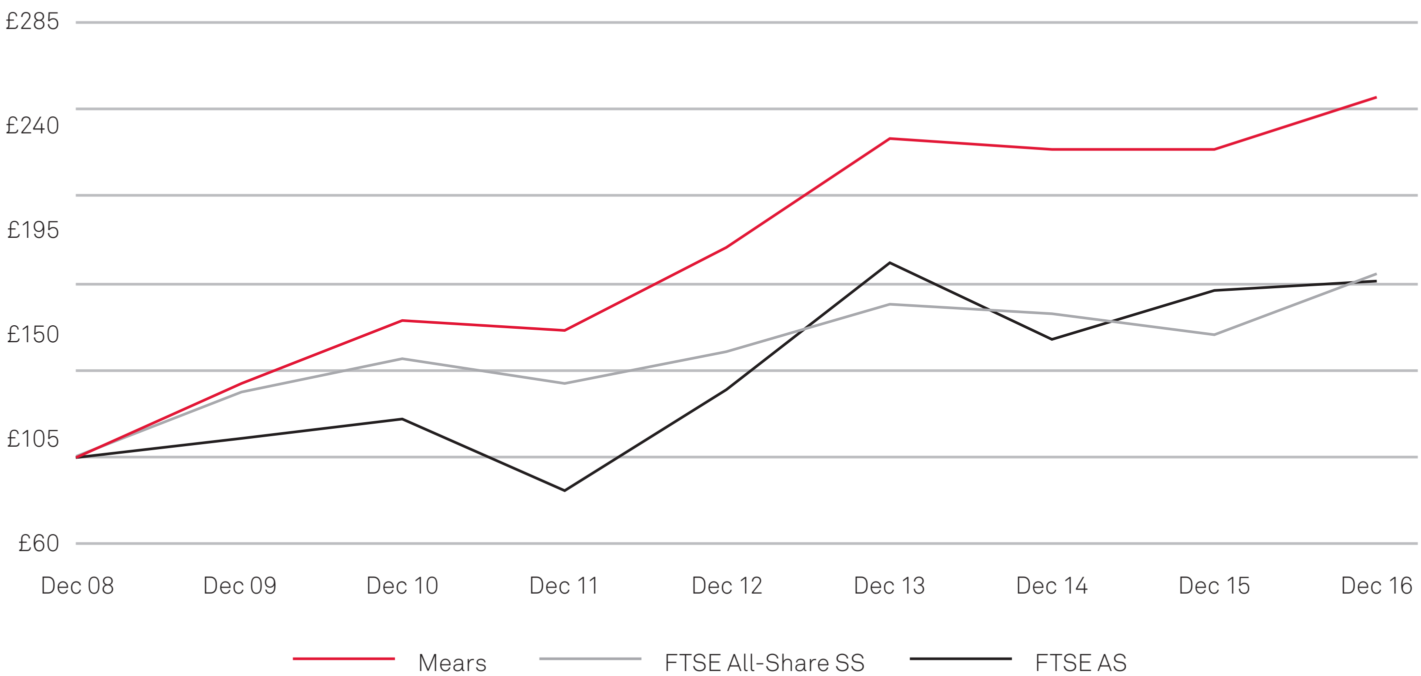
Annual report on remuneration continued

Shareholder dilution

In accordance with the Association of British Insurers' guidelines, the Company can issue a maximum of 10% of its issued share capital in a rolling ten-year period to employees under all its share plans. In addition, of this 10% the Company can issue 5% to satisfy awards under discretionary or Executive plans. The Company operates all its share plans within these guidelines.

Performance graph and table (unaudited)

The graph below shows the Group's performance, measured by TSR, compared with the constituents of the FTSE All-Share support service sector over the last eight years. The Index is the most relevant to compare the Group's performance against its peers.



The table below shows the Chief Executive Officer's remuneration package over the past eight years, together with incentive payout/vesting as compared to the maximum opportunity.

Year	Name	Single figure of total remuneration (£'000)	Bonus payout (as % maximum opportunity)	Long-term incentive accrual rate (as % maximum opportunity)
2016	D J Miles	436	—	—
2015	D J Miles	436	—	20%
2014	D J Miles	412	—	35%
2013	D J Miles	825	—	100%
2012	D J Miles	409	—	—
2011	D J Miles	384	—	—
2010	D J Miles	270	—	—
	R Holt	600	—	—
2009	R Holt	1,095	100%	—

Annual remuneration report 2016 continued

Annual report on remuneration continued

Percentage change in Chief Executive Officer's remuneration

The table below compares the percentage change in the salary of the Chief Executive Officer with that of the wider employee population.

	Remuneration		
	Salary entitlement	Benefits	Bonus/ incentives
Chief Executive Officer	5%	0%	0%
Office salaries	1%	—	—

Relative importance of spend on pay

The table below sets out the relative importance of spend on pay in the financial year and previous financial year compared with other disbursements from profit.

Significant distributions	**Disbursements from profit in financial year 2016 £'000**	Disbursements from profit in previous financial year 2015 £'000	% change
Total Directors' pay	**1,530**	1,858	1%
Profit distributed by way of dividend	**11,483**	10,445	10%
Underlying profit before tax	**40,062**	36,757	9%

Statement of implementation of remuneration policy in the following financial year

Executive Directors

Salary

The salary entitlements for the forthcoming year are set out below:

Executive Director	**2017 £**	2016 £	% change
D J Miles	**386,817**	381,100	1.5%
A C M Smith	**257,912**	254,100	1.5%
A Long	**211,019**	207,900	1.5%

Pension

Details of pension contributions for the year ended 31 December 2016 are set out below:

Executive Director	Pension
D J Miles	15%
A C M Smith	15%
A Long	15%

EIP

As set out in the policy table, the EIP is split into two parts: the deferred share award and the performance share award. Set out below is the maximum opportunity of each part for the year ended 31 December 2017:

Part A – Deferred share award (% of salary)	Part B – Performance share award (% of salary)
100%	100%

Statement of implementation of remuneration policy in the following financial year continued

Executive Directors continued

EIP continued

For the 2017 EIP, the performance share award threshold level of vesting is 20% for each measure. The measures and weightings are set out below:

Condition		Weighting	Payout range (threshold to maximum opportunity)
Earnings per share (EPS)		40%	20%–100%
ROCE		40%	20%–100%
EBITDA cash conversion			20%–100%
Other	Customer satisfaction	20%	20%–100%
	Health and safety		20%–100%

In setting these targets, the Committee is taking under consideration (amongst other items):

- the Company's business plan;
- consensus forecasts for the Company; and
- alignment with the Company's business strategy.

Non-Executive Directors

The following table sets out the fee rates for the Non-Executive Directors:

	2017	2016	% change
Chairman fee	**250,000**	—	N/A
Base fee	**50,000**	45,000	11
Committee Chairman fee	**15,000**	—	N/A
Committee membership fee	**5,000**	—	N/A

It should be noted that the Chairman no longer receives any benefits from the date of the 2017 AGM. For 2016 the benefits amounted to £95,000.

Role of the Committee and activities

The Committee determines the total individual remuneration packages of each Executive Director of the Group and certain other senior employees (and any exit terms) and recommends to the Board the framework and broad policies of the Group in relation to Senior Executive remuneration. The Committee determines the targets for all of the Group's performance related remuneration and exercises the Board's powers in relation to all of the Group's share and incentive plans.

There is a formal and transparent procedure for developing policy on Executive remuneration and for determining the remuneration of individual Directors.

The Remuneration Committee is responsible for:

- determining and agreeing with the Board the broad remuneration policy for:
  - the Chairman, the Executive Directors and senior management; and
  - the Executive Directors' remuneration and other benefits and terms of employment, including performance related bonuses and share options; and
- approving the service agreements of each Executive Director, including termination arrangements.

No Director is involved in determining his/her own remuneration.

Annual remuneration report 2016 continued

Statement of implementation of remuneration policy in the following financial year continued

Annual overview

The Committee has continued to work to build investor confidence with regard to its Executive remuneration policies and remains committed to the following actions:

→ improving the level of openness and transparency in remuneration reporting through a detailed Annual Remuneration Report;

→ operating a structured incentive arrangement with clear financial performance targets for each year;

→ undertaking a regular review of the remuneration policies for Executive Directors and other Senior Executives within the Group to ensure that they remain appropriate to retain and motivate such individuals;

→ considering pay policies within the Group as a whole when determining Executive Directors' remuneration packages;

→ encouraging Executive Directors and Senior Executives to build up a meaningful shareholding in the Company to more closely align the interests of shareholders and Executives; and

→ being kept fully aware and informed on developments and best practice in the field of remuneration and corporate governance from external advisers, institutional shareholders and their representative bodies.

Notwithstanding the above, the Committee recognises that the success of the Group is dependent upon the efforts of key individuals and that they should be fairly rewarded for their efforts and contributions in making Mears the success it is.

Advisers to the Committee

In 2016, the Committee continued to engage PwC and received wholly independent advice on Executive compensation. PwC is a member of the Remuneration Consultants Group and complies with its code of conduct that sets out guidelines to ensure that its advice is independent and free of undue influence. Fees paid to PwC in respect of these services in the year ended 31 December 2016 were £30,000.

Statement of voting at general meeting

The table below shows the historic voting outcomes in respect of the remuneration policy and Annual Remuneration Report.

Item	Votes for	%	Votes against	%	Votes withheld
To approve the Directors' Remuneration Report (2016)	84,285,932	97.924	1,740,944	2.023	45,779
To approve the remuneration policy (2014)	73,134,765	90.863	7,350,317	9.132	3,688

The total number of ordinary shares eligible to vote at the 2016 AGM was 102,526,212. Every shareholder has one vote for every ordinary share held.

Report of the Directors

The Directors present their report together with the consolidated financial statements for the year ended 31 December 2016.

Principal activities

The principal activities of the Group are the provision of a range of outsourced services to the public and private sectors. The principal activity of the Company is to act as a holding company.

Business review

The Company is required to set out a fair review of the business of the Group during the reporting period. The information that fulfils this requirement can be found in the Strategic Report, Review of Operations and Financial Review. The results of the Group can be found within the Consolidated Income Statement. Information required to be disclosed in respect of emissions and future developments is included within the Strategic Report.

Dividend

The final dividend in respect of 2015 of 7.90p per share was paid in July 2016. An interim dividend in respect of 2016 of 3.30p was paid to shareholders in November 2016. The Directors recommend a final dividend of 8.40p per share for payment on 4 July 2017 to shareholders on the Register of Members on 16 June 2017. This has not been included within the consolidated financial statements as no obligation existed at 31 December 2016.

Corporate governance

Details of the Group's corporate governance are set out on pages 48 to 53.

Key performance indicators (KPIs)

We focus on a range of key indicators to assess our performance. Our performance indicators are both financial and non-financial and ensure that the Group targets its resources around its customers, employees, operations and finance. Collectively they form an integral part of the way that we manage the business to deliver our strategic goals. Our primary performance indicators are detailed on pages 14 to 17.

Directors

The present membership of the Board is set out with the biographical detail on page 46.

In line with current practice, all of the Directors will retire and, being eligible, offer themselves for re-election at the AGM in June 2017.

The beneficial interests of the Directors in the shares of the Company at 31 December 2016 and 31 December 2015 are detailed within the Remuneration Report on page 74.

The process governing the appointment and replacement of Directors is detailed within the Report of the Nomination Committee on pages 54 and 55.

Amendment to Articles of Association

The Company's Articles of Association can be amended only by a special resolution of the members, requiring a majority of not less than 75% of such members voting in person or by proxy.

Appointment of Directors

Directors are appointed by ordinary resolution, or the existing Directors may appoint a person as a Director to either fill a vacancy or as an additional Director provided that the number of Directors does not exceed the maximum permissible. Any person appointed by the Directors must retire at the next AGM but will be eligible for re-election at that meeting.

Share capital authorisations

The 2016 AGM held in June 2016 authorised:

- the Directors to allot shares within defined limits. The Companies Act 2006 requires directors to seek this authority and, following changes to FSA rules and institutional guidelines, the authority was limited to one third of the issued share capital, a total of £340,000 plus an additional one third of issued share capital of £340,000 that can only be used for a rights issue or similar fund raising;
- the Directors to issue shares for cash on a non pre-emptive basis. This authority was limited to 10% of the issued share capital of £104,000 and is required to facilitate technical matters such as dealing with fractional entitlements or possibly a small placing; and
- the convening of general meetings (other than an AGM) on 14 days' notice. This results from a European Union directive that became effective on 3 August 2010 and will override Section 307 of the Companies Act 2006 where the requirement to give 21 days' notice for certain meetings has been amended.

Further details of these authorisations are available in the notes to the 2016 Notice of AGM. Shareholders are also referred to the 2017 Notice of AGM, which contains similar provisions in respect of the Company's equity share capital as detailed below.

AGM

The 2017 AGM will be held at the offices of Buchanan, 107 Cheapside, London EC2V 6DN on 7 June 2017 at 9.30am and a formal Notice of Meeting and Form of Proxy are enclosed. The ordinary business to be conducted will include the re-appointment of all Directors. The special business will comprise the following resolutions:

- to authorise the Directors to allot shares within defined limits. The Companies Act 2006 requires Directors to seek this authority and, following changes to FSA rules and institutional guidelines, the authority, as in previous years, will be limited to one third of the issued share capital, plus an additional one third of issued share capital that can only be used for a rights issue or similar fund raising;
- to authorise the Directors to issue shares for cash on a non pre-emptive basis. This authority is limited to 10% of the issued share capital and is required to facilitate technical matters such as dealing with fractional entitlements or possibly a small placing;
- to authorise the convening of general meetings (other than an AGM) on 14 days' notice. This results from a European Union directive that became effective on 3 August 2010 and will override Section 307 of the Companies Act 2006 where the requirement to give 21 days' notice for certain meetings has been amended; and
- to approve the amended rules of the Mears All-Employee Share Plan in the form produced to the meeting and the Directors be authorised to do all things necessary in order to adopt and carry the amended scheme into effect.

Report of the Directors continued

Principal risks and uncertainties

Risk is an accepted part of doing business. The Group's financial risk management is based upon sound economic objectives and good corporate practice. The Board has overall responsibility for risk management and internal control within the context of achieving the Group's objectives. Our process for identifying and managing risks is set out in more detail within the Corporate Governance Statement. The key risks and mitigating factors are set out on pages 18 to 23. Details of financial risk management and exposure to price risk, credit risk and liquidity risk are given in note 19 on pages 124 to 128.

Contracts of significance

The Group is party to significant contracts within each segment of its business. The Directors do not consider that any one of those contracts is essential in its own right to the continuation of the Group's activities.

Payment policy

The Company acts purely as a holding company and as such is non-trading. Accordingly, no payment policy has been defined. However, the policy for Group trading companies is to set the terms of payment with suppliers when entering into a transaction and to ensure suppliers are aware of these terms. Group trade creditors during the year amounted to 61 days (2015: 57 days) of average supplies for the year.

Capital structure

The Group is financed through both equity share capital and debt. Details of changes to the Company's share capital are given in note 21 to the financial statements. The Company has a single class of shares – ordinary 1p shares – with no right to any fixed income and with each share carrying the right to one vote at the general meetings of the Company. Under the Company's Articles of Association, holders of ordinary shares are entitled to participate in any dividends pro-rata to their holding. The Board may propose and pay interim dividends and recommend a final dividend for approval by the shareholders at the AGM. A final dividend may be declared by the shareholders in a general meeting by ordinary resolution but such dividend cannot exceed the amount recommended by the Board.

Substantial shareholdings

As at 28 February 2017 the Company has been notified of, or is aware of, the shareholders holding 2% or more of the issued share capital of the Company, as detailed in the table adjacent.

Fund manager	City	Number (m)	%
PrimeStone Capital	London	10.5	10.3
Majedie Asset Management	London	9.9	9.7
Heronbridge Investment Management	Bath	7.2	7.0
Shareholder Value Management	Frankfurt	6.3	6.1
Schroder Investment Management	London	5.7	5.6
Legal & General Investment Management	London	5.2	5.1
Franklin Templeton Investments	London	5.1	5.0
Columbia Threadneedle Investments	London	4.4	4.2
Artemis Investment Management	Edinburgh	4.3	4.2
Fidelity Management & Research	Boston	4.3	4.2
Invesco Perpetual Asset Management	Henley-on-Thames	3.1	3.0
BlackRock Inc	London	2.6	2.5
Montanaro Asset Management	London	2.4	2.4
Slater Investments	London	2.3	2.2
Close Asset Management	London	2.2	2.1

Disabled employees

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Group continues and that appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Employee information and consultation

The Group has received recognition under the 'Investors in People' award. The Group continues to involve its staff in the future development of the business. Information is provided to employees through a daily news email, a quarterly newsletter posted out to all staff, the Group website and the intranet to ensure that employees are kept well informed of the performance and objectives of the Group.

CREST

CREST is the computerised system for the settlement of share dealings on the London Stock Exchange. CREST reduces the amount of documentation required and also makes the trading of shares faster and more secure. CREST enables shares to be held in an electronic form instead of the traditional share certificates. CREST is voluntary and shareholders can keep their share certificates if they wish. This may be preferable for shareholders who do not trade in shares on a frequent basis.

Auditor

Grant Thornton UK LLP offers itself for re-appointment as auditor in accordance with Section 489 of the Companies Act 2006.

By order of the Board

B Westran
Company Secretary
ben.westran@mearsgroup.co.uk
27 March 2017

Statement of Directors' responsibilities

In respect of the Directors' Report and financial statements

The Directors are responsible for preparing the Annual Report, the Remuneration Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors are required to prepare Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and have elected to prepare the Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice including FRS 102 'The Financial Reporting Standard Applicable in the UK and the Republic of Ireland' (United Kingdom Accounting Standards and Applicable Law). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs and profit or loss of the Group and the Company for that period. In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and the Company and enable them to ensure that the financial statements and Remuneration Report comply with the Companies Act 2006 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that:

- so far as each Director is aware there is no relevant audit information of which the Company's auditor is unaware; and
- the Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

To the best of my knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Annual Report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The Directors are responsible for preparing the Annual Report in accordance with applicable law and regulations. The Board considers the Annual Report and Accounts, taken as a whole, as fair, balanced and understandable and that it provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

Going concern

We principally operate in robust defensive markets, Social Housing and Care, where spend is largely non-discretionary and our contracts tend to be long-term partnerships.

The Group had net debt of £12.4m at 31 December 2016. The core debt required to satisfy the day-to-day requirements of the business is in the region of £85m. This represents significant headroom against the £140m unsecured revolving credit facility, with an additional accordion mechanism allowing the facility to be increased to a maximum of £200m, maturing in July 2020.

After reviewing the Group's and Company's budget for the next financial year and longer-term plans, the Directors consider that, as at the date of approving the financial statements, it is appropriate to adopt the going concern basis in preparing the financial statements.

On behalf of the Board

A C M Smith
Finance Director
andrew.smith@mearsgroup.co.uk
27 March 2017

Independent auditor's report

To the members of Mears Group PLC

Our opinion on the financial statements is unmodified

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2016 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Parent Company financial statements have been properly prepared in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) including FRS 102 'The Financial Reporting Standard Applicable in the UK and Republic of Ireland'; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Who we are reporting to

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

What we have audited

Mears Group PLC's financial statements for the year ended 31 December 2016 comprise the Group principal accounting policies, the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement, the Consolidated Statement of Changes in Equity, the related Group notes, the Company principal accounting policies, the Parent Company Balance Sheet, the Parent Company Statement of Changes in Equity and the related Company notes.

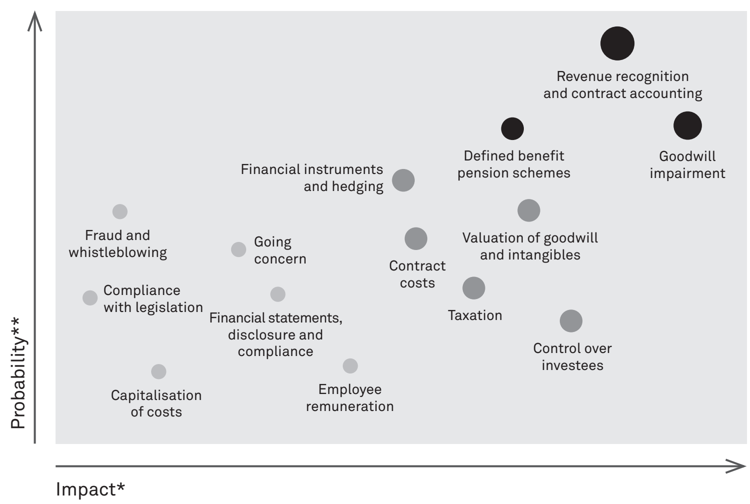
The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the Parent Company financial statements is United Kingdom Generally Accepted Accounting Practice including FRS 102 'The Financial Reporting Standard Applicable in the UK and Republic of Ireland'.

Overview of our audit approach

- the key audit risks were identified as: revenue recognition and contract accounting, goodwill impairment, and defined benefit pension schemes;
- overall Group materiality was set at £2.1m, which represents 4.8% of the Group's earnings before interest, tax and amortisation; and
- we performed full scope audits at three companies and specific audit procedures over certain balances and transactions at six further companies to gain sufficient, appropriate audit evidence over all material balances at both divisional and Group levels.

Our assessment of risk

At the outset of our audit we identified the risks and matters that would need to be considered in dispensing our duties and then updated them as the audit progressed. These were first presented to the Audit Committee on 2 December 2015 and then as part of our concluding procedures on 3 March 2016. The following graph illustrates the risks identified by us and our assessment of the impact of them on our audit approach.



* Impact that the identified risk would have on the Group's financial statements.

** Probability that the identified risk could occur during the year if not properly controlled.

Key

- Significant risks
- Other risks
- Other areas of focus

Our assessment of risk continued

In arriving at our opinions set out in this report, we highlight the following risks that, in our judgement, had the greatest effect on our audit:

Audit risk	How we responded to the risk
Revenue recognition and contract accounting	**Our audit work included but was not restricted to:**
Refer to pages 92 to 94. Revenue is recognised throughout the Group as the fair value of consideration receivable in respect of the performance of contracts and the provision of services. Provision is made for expected contract losses as soon as they are foreseen. Determining the amount of revenue to be recognised, requires management to make significant judgements and estimates as to the stage of completion, the costs to complete, the impact of any changes in scope of work and the recoverability of work-in-progress and receivables balances. We therefore identified revenue recognition and contract accounting as a significant risk.	→ an evaluation of the methodology by which the Directors determine the amount of revenue and profit to recognise based on each type of contract as disclosed in the accounting policies. This included assessing whether the accounting policies adopted by the Directors are in accordance with the requirements of International Accounting Standard (IAS) 11 "Construction Contracts", IAS 18 "Revenue" and IFRIC 12 "Service Concession Arrangements", and whether management accounted for revenue in accordance with the accounting policies; → testing key controls, where applicable, over the recognition of revenue and the allocation of costs to the contracts, including invoicing, cost approval and cost allocation; → judgementally selecting contracts by reference to materiality and other risk factors including loss making contracts and contracts with significant aged work-in-progress and receivables balances; → selecting a samples of contract balances, accrued income and revenue transactions, including contract invoicing, care invoicing and rental and rebates income, to ensure coverage across the Group; → assessing, for the selected items and samples, whether the revenue and profit recognised are in accordance with the Group's accounting policies by agreeing inputs to contract terms, re-performing management's calculations and assessing management's assumptions and assertions underpinning their forecasts for contracts' future performance by reference to supporting documentation, such as contract KPIs, historical performance against forecasts and discussions with key operations personnel; → reviewing contracts that are loss making or at risk of incurring future losses during the remaining life of the contract and challenging management's assumptions and assertions relating to the future results of those contracts by reference to supporting evidence such as management's plans to return the contract to profit, forecast models, previous history of turning around loss making contracts and correspondence with clients where appropriate. We also visited a number of sites during the year in order to further understand the operations; and → investigating the recoverability of receivables, accrued income and work-in-progress balances by reference to post balance sheet cash collection, certifications performed by the Group or external Quantity Surveyors, reviewing the quality of supporting evidence, including internal and external legal opinions, expert valuer reports and correspondence with customers, and examining the Group's historical experience of recovery.

Independent auditor's report continued
To the members of Mears Group PLC

Our assessment of risk continued

Audit risk	How we responded to the risk
Goodwill impairment	**Our audit work included but was not restricted to:**
Refer to pages 90 and 91. The Directors are required to make an annual assessment to determine whether the carrying value of goodwill of £193.7m is impaired. Past experience has indicated that there is significant headroom in the goodwill balance relating to the Housing division cash-generating unit (CGU) but limited headroom in the goodwill balance relating to the Care division CGU, which accounts for £99.6m of the carried goodwill. The process for assessing whether an impairment exists under IAS 36 'Impairment of Assets' is complex. The process of determining the value in use, through forecasting cash flows related to CGUs and the determination of the appropriate discount rate and other assumptions to be applied, can be highly judgemental and can significantly impact the results of the impairment review. We therefore identified the impairment review of goodwill undertaken by management in relation to the Care division as a significant risk.	→ obtaining management's discounted cash flow forecast for the Care division used in the impairment review and comparing it to our understanding of the division and recalculating the arithmetical accuracy of those calculations; → testing and challenging the assumptions utilised in the impairment models, including the ability for the Group to recruit and retain the appropriate levels of carers, the rate at which the Group can pass National Living Wage increases on to customers, the rate at which the Group can increase its contracted hours and the discount rates and terminal values used; → we involved our specialist valuation team to consider whether the market level assumptions used were appropriate to the Care division's circumstances and where possible, benchmarked these assumptions against available industry data; and → testing the accuracy of management's forecasting through a comparison of budget to actual data and historical variance trends and reviewing the cash flows for exceptional or unusual items or assumptions.
Defined benefit pensions schemes	**Our audit work included but was not restricted to:**
Refer to page 95. The Group operates two defined benefit pension schemes and is admitted body of a number of other defined benefit pension schemes. At 31 December 2016 the defined benefit pension schemes had a combined net surplus of £24.2m, of which £8.5m is recognised in the financial statements as recoverable. The gross value of the pension assets and obligations which form the net surplus amounted to £572.2m and £548.0m respectively. The measurement of the obligations in accordance with IAS 19 (revised) "Employee Benefits" involves significant judgement and their valuation is subject to complex actuarial assumptions. Small variations in those actuarial assumptions can lead to a materially different value of pension liabilities being recognised within the Group financial statements. We therefore identified the valuation of the defined benefit pension schemes obligations as a significant risk.	→ utilising the expertise of our actuarial specialists in order to review the appropriateness of the assumptions used in the calculation of the obligations and testing the appropriateness of the valuation methodologies and their inherent actuarial assumptions by benchmarking key assumptions such as discount rates, wages and salary growth rates and mortality rates to available market data; → testing the accuracy of underlying membership data utilised by the Group's actuaries for the purpose of calculating the scheme liabilities by selecting a sample of employees and agreeing key standing data such as date of birth, gender and date of membership to underlying records; → directly confirming the existence and valuation of pension scheme assets with asset managers for Group schemes and analysing the movements on assets for a sample of admitted body schemes; and → considering the appropriateness of the recognition of any scheme surpluses by reviewing scheme rules to assess whether the Group will benefit from any future refund or reduction in future contributions as a result of such surpluses.

Our application of materiality and an overview of the scope of our audit

Materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality in determining the nature, timing and extent of our audit work and in evaluating the results of that work.

We determined materiality for the audit of the Group financial statements as a whole to be £2.1m (2015: £1.7m), which is 4.80% (2015: 4.75%) of the Group's earnings before, interest, tax and amortisation. This benchmark is considered the most appropriate because it is the key financial measure by which management assess the performance of the Group and is used to report to investors on the financial performance of the Group.

Materiality for the current year is higher than the level that we determined for the year ended 31 December 2015 as a result of higher earnings before, interest, tax and amortisation of the Group in the year.

We use a different level of materiality, performance materiality, to drive the extent of our testing and this was set at 75% of financial statement materiality for the audit of the Group financial statements. We also determine a lower level of specific materiality for certain areas such as Directors' remuneration and related party transactions.

We determined the threshold at which we will communicate misstatements to the Audit Committee to be £105,000. In addition we communicate misstatements below that threshold that, in our view, warrant reporting on qualitative grounds.

Overview of the scope of our audit

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

We conducted our audit in accordance with International Standards on Auditing (ISAs) (UK and Ireland). Our responsibilities under those standards are further described in the 'Responsibilities for the financial statements and the audit' section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Group in accordance with the Auditing Practices Board's Ethical Standards for Auditors, and we have fulfilled our other ethical responsibilities in accordance with those Ethical Standards.

Our audit approach was based on a thorough understanding of the Group's business and is risk-based. In order to address the risks described above as identified during our planning procedures, we performed a full scope audit of the financial statements of the Parent Company, Mears Group PLC, and of the Group's operations throughout the United Kingdom.

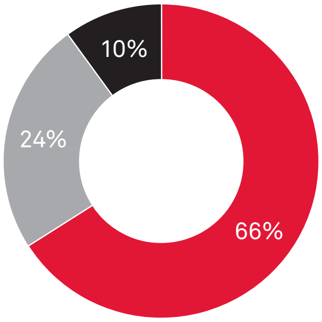
The companies of the Group were evaluated by the Group audit team based on a measure of materiality considered as a percentage of total Group assets, revenues and profit before taxes, to assess the significance of the component and to determine the planned audit response. For those components that we determined to be significant components, either a full scope approach or specific procedures in relation to specific balances and transactions were carried out. This approach was determined based on their relative materiality to the Group and our assessment of audit risk.

The Group's companies vary significantly in size. We performed full scope audits at three companies. Specific audit procedures over certain balances and transactions were performed on a further six companies, to give appropriate coverage of all material balances at both divisional and Group levels. Together, the reporting units subject to audit procedures, being full scope and specific procedures, were responsible for 90% of the Group's revenues, 89% of the Group's earnings before, interest, tax and amortisation and 88% of Group's total assets.

For significant components requiring a full scope approach an interim visit was conducted before the year end to undertake substantive procedures in advance of the final visit and to evaluate the Group's internal control environment including its IT systems. We then evaluated and tested controls over the financial reporting systems identified as part of our risk assessment, reviewed the accounts production process and addressed critical accounting matters. We sought wherever possible, to rely on the effectiveness of the Group's internal controls which allows us to reduce substantive testing. We then undertook substantive testing on significant transactions and material account balances, including the procedures outlined above in relation to the key risks. For the components where specific procedures were carried out a similar testing strategy was applied, focused on the significant transactions and material account balances.

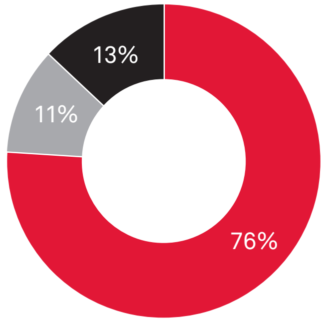
The remaining non-significant components of the Group were subject to analytical procedures over their financial performance and position after taking into account the risks identified above and the significance of the component to the Group. The charts on page 86 summarise the extent of our audit approach.

Independent auditor's report continued
To the members of Mears Group PLC



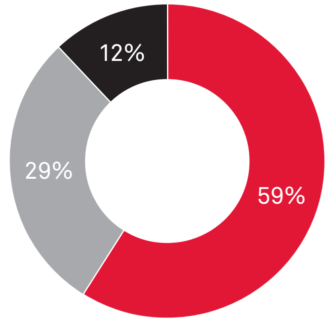
Revenue

- Full scope
- Specific procedures
- Analytical



EBITA

- Full scope
- Specific procedures
- Analytical



Total assets

- Full scope
- Specific procedures
- Analytical

Other reporting required by regulations

Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

Matter on which we are required to report under the Companies Act

In the light of the knowledge and understanding of the Group and the Parent Company and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic Report or the Directors' Report.

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report to you if, in our opinion:

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

Under the Listing Rules, we are required to review:

- the Directors' statements in relation to going concern and longer-term viability, set out on pages 22 and 23 respectively; and
- the part of the Corporate Governance Statement relating to the Company's compliance with the provisions of the UK Corporate Governance Code specified for our review.

Matters on which we are required to report by exception continued

Under the ISAs (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- otherwise misleading.

In particular, we are required to report to you if:

- we have identified any inconsistencies between our knowledge acquired during the audit and the Directors' statement that they consider the Annual Report is fair, balanced and understandable; or
- the Annual Report does not appropriately disclose those matters that were communicated to the Audit Committee which we consider should have been disclosed.

We have nothing to report in respect of any of the above matters.

We also confirm that we do not have anything material to add or to draw attention to in relation to:

- the Directors' confirmation in the annual report that they have carried out a robust assessment of the principal risks facing the Group including those that would threaten its business model, future performance, solvency or liquidity;
- the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated;
- the Directors' statement in the financial statements about whether they have considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the Group's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements; and
- the Directors' explanation in the Annual Report as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Responsibilities for the financial statements and the audit

What the Directors are responsible for:

As explained more fully in the Statement of Directors' responsibilities set out on page 81, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

What we are responsible for:

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Simon Lowe
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
London
27 March 2017

Principal accounting policies – Group

Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with IFRS as adopted by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS and therefore the Group financial statements comply with Article 4 of the EU International Accounting Standards Regulations. The financial statements are prepared under the historical cost convention as modified by the revaluation of derivative financial instruments and share-based payments.

The accounting policies remain unchanged from the previous year except for the modification of a number of standards with effect from 1 January 2016. Changes include Disclosure Initiative (Amendments to IAS 1), Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11), Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28), Investment Entities: Applying the Consolidation Exception (Amendments to IFRS 10, IFRS 12 and IAS 28) and Annual Improvements 2012–2014 (which made amendments to IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations', IFRS 7 'Financial Instruments: Disclosures', IAS 19 'Employee Benefits' and IAS 34 'Interim Financial Reporting'). The adoption of these amendments had no material effect on the Group's financial statements.

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and judgements that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the year. Although these estimates are based on the Directors' best knowledge of the amounts, actual results may ultimately differ from those estimates. The most significant estimates made by the Directors in these financial statements are set out in 'Use of judgements and estimates' on pages 98 and 99.

Mears Group PLC is incorporated and domiciled in England and Wales (registration number 3232863). Its registered office and principal place of business is 1390 Montpellier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH. Mears Group PLC's shares are listed on the London Stock Exchange.

The Directors consider that as at the date of approving the financial statements, there is a reasonable expectation that the Group and the Company have adequate resources to continue in operational existence for the foreseeable future. For this reason, the Directors continue to adopt the going concern basis in preparing the financial statements. The Directors have discussed the principal risks and uncertainties of the business in the Risk Management section on pages 18 to 23.

Basis of consolidation

The Consolidated Balance Sheet includes the assets and liabilities of the Company and its subsidiaries and is made up to 31 December 2016. Entities over which the Group has the ability to exercise control over financial and operating policies are accounted for as subsidiaries. Control is achieved where the Company has existing rights that give it the current ability to direct the activities that affect the Company's returns and exposure or rights to variable returns from the entity. Interests acquired in entities are consolidated from the effective date of acquisition and interests sold are consolidated up to the date of disposal.

All significant intercompany transactions and balances between Group enterprises, including unrealised profits arising from intra-group transactions, are eliminated on consolidation; no profit is taken on sales between Group companies.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling shareholders' share of changes in equity since the date of the combination. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interest having a deficit balance.

A joint venture is a joint arrangement whereby the parties that have joint control have the rights to the net assets of the arrangement. Investments in joint ventures are accounted for using the equity method of accounting. Under this method, the Group's share of post-acquisition profits or losses is recognised in the Consolidated Income Statement; the cost of the investment in a given joint venture, together with the Group's share of that entity's post-acquisition changes to shareholders' funds, is included in investments within the Consolidated Balance Sheet.

Business combinations

Business combinations are accounted for using the acquisition method. The acquisition method involves the recognition at fair value of all identifiable assets and liabilities, including contingent liabilities of the subsidiary at the acquisition date, regardless of whether or not they were recorded in the financial statements of the subsidiary prior to acquisition. On initial recognition, the assets and liabilities of the subsidiary are included in the Consolidated Balance Sheet at their fair values, which are also used as the bases for subsequent measurement in accordance with the Group accounting policies. Goodwill is stated after separating out identifiable intangible assets. Goodwill represents the excess of acquisition cost over the fair value of the Group's share of the identifiable net assets of the acquired subsidiary at the date of acquisition.

Where applicable the consideration for an acquisition includes any assets or liabilities arising from a contingent consideration arrangement, measured at fair value at the acquisition date. Subsequent changes in such fair values are adjusted against the cost of acquisition where they result from additional information obtained up to one year from the acquisition date about facts and circumstances that existed at the acquisition date. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are recognised in accordance with IAS 39 in the Consolidated Income Statement.

Costs relating to acquisitions in the year have been expensed.

For transactions with non-controlling parties that do not result in a change of control, the difference between the fair value of the consideration paid and the amount by which the non-controlling interest is adjusted is recognised in equity.

Any business combinations prior to 1 January 2010 were accounted for in accordance with the standards in place at the time, which differ in the following respects: transaction costs directly attributable to the acquisition formed part of the acquisition costs; contingent consideration was recognised if, and only if, the Group had a present obligation, the economic outflow was more likely than not and a reliable estimate was determinable; and subsequent adjustments to the contingent consideration were recognised as part of goodwill.

Property, plant and equipment

Items of property, plant and equipment are stated at historical cost, net of depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow into the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the Income Statement during the financial period in which they are incurred.

Freehold land is not depreciated. Depreciation on other assets is calculated to write down the cost less estimated residual value over their estimated useful economic lives. The rates generally applicable are:

Freehold buildings	–	2% p.a., straight line
Leasehold improvements	–	over the period of the lease, straight line
Plant and machinery	–	25% p.a., reducing balance
Fixtures, fittings and equipment	–	25% p.a., reducing balance
Motor vehicles	–	25% p.a., reducing balance

Residual values are reviewed annually and updated if appropriate. The carrying value is reviewed for impairment in the period if events or changes in circumstances indicate the carrying value may not be recoverable. An asset's carrying value is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within administrative expenses in the Income Statement.

Principal accounting policies – Group continued

Intangible assets

In accordance with IFRS 3 (Revised) 'Business Combinations', an intangible asset acquired in a business combination is deemed to have a cost to the Group of its fair value at the acquisition date. The fair value of the intangible asset reflects market expectations about the probability that the future economic benefits embodied in the asset will flow to the Group. Where an intangible asset might be separable, but only together with a related tangible or intangible asset, the group of assets is recognised as a single asset separately from goodwill where the individual fair values of the assets in the Group are not reliably measurable. Where the individual fair values of the complementary assets are reliably measurable, the Group recognises them as a single asset provided the individual assets have similar useful lives. Intangible assets are amortised over the useful economic life of those assets.

Development costs incurred on software development are capitalised when all the following conditions are satisfied:

- completion of the software module is technically feasible so that it will be available for use;
- the Group intends to complete the development of the module and use it;
- the software will be used in generating probable future economic benefits;
- there are adequate technical, financial and other resources to complete the development and to use the software; and
- the expenditure attributable to the software during its development can be measured reliably.

Costs incurred making intellectual property available for use (including any associated borrowing costs) are capitalised when all of the following conditions are satisfied:

- completion of the data set is technically feasible so that it will be available for use;
- the Group intends to complete the preparation of the data and use it;
- the data will be used in generating probable future economic benefits;
- there are adequate technical, financial and other resources to complete the data set and to use it; and
- the expenditure attributable to the intellectual property during its development can be measured reliably.

Development costs not meeting the criteria for capitalisation are expensed as incurred. Careful judgement by management is applied when deciding whether the recognition requirements for development costs have been met. This is necessary as the economic success of any development is uncertain and may be subject to future technical problems at the time of recognition. Judgements are based on the information available at each balance sheet date. In addition, all internal activities related to the research and development of new software are continually monitored by management.

The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Directly attributable costs include employee costs incurred on software development.

Amortisation commences upon completion of the asset and is shown within other administrative expenses. Until the asset is available for use on completion of the project, the assets are subject to impairment testing only. Development expenditure is amortised over the period expected to benefit.

The identifiable intangible assets and associated periods of amortisation are as follows:

Order book	–	over the period of the order book, typically three years
Client relationships	–	over the period expected to benefit, typically five years
Development expenditure	–	20 to 25% p.a., straight line
Intellectual property	–	over the period of usefulness of the intellectual property, typically five years

Goodwill

Goodwill arises on the acquisition of subsidiaries and represents any excess of the cost of the acquired entity over the Group's interest in the fair value of the entity's identifiable assets and liabilities acquired and is capitalised as a separate item. Goodwill is recognised as an intangible asset.

Under the business combinations exemption of IFRS 1, goodwill previously written off directly to reserves under UK GAAP is not recycled to the Income Statement on calculating a gain or loss on disposal.

Impairment

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows: cash-generating units (CGUs). As a result, some assets are tested individually for impairment and some are tested at CGU level. Goodwill is allocated to those CGUs that are expected to benefit from synergies of the related business combination and represent the lowest level within the Group at which management monitors the related cash flows.

Goodwill or CGUs that include goodwill and those intangible assets not yet available for use are tested for impairment at least annually. All other individual assets or CGUs are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised in the Income Statement for the amount by which the asset or CGU's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of fair value, reflecting market conditions less costs to sell, and value in use based on an internal discounted cash flow evaluation. Impairment losses recognised for CGUs, to which goodwill has been allocated, are credited initially to the carrying amount of goodwill. Any remaining impairment loss is charged pro-rata to the other assets in the CGU. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognised may no longer exist.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is the actual purchase price of materials.

Work in progress

Work in progress is included in inventories after deducting any foreseeable losses and payments on account not matched with revenue. Work in progress represents costs incurred on contracts that cannot be matched with contract work accounted for as revenue. Work in progress is stated at the lower of cost and net realisable value. Cost comprises materials, direct labour and any subcontracted work that has been incurred in bringing the inventories and work in progress to their present location and condition.

Amounts recoverable on contracts

Amounts recoverable on contracts are included in trade and other receivables and represent revenue recognised in excess of payments on account.

Accounting for taxes

Income tax comprises current and deferred taxation.

Current tax assets and/or liabilities comprise those obligations to, or claims from, fiscal authorities that are unpaid at the balance sheet date. They are calculated according to the tax rates and tax laws applicable to the accounting periods to which they relate, based on the taxable profit for the year.

Where an item of income or expense is recognised in the Income Statement, any related tax generated is recognised as a component of tax expense in the Income Statement. Where an item is recognised directly to equity or presented within the Consolidated Statement of Comprehensive Income, any related tax generated is treated similarly.

Deferred taxation is the tax expected to be repayable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and corresponding tax bases used in the computation of taxable profit and is accounted for using the balance sheet liability method.

Deferred taxation liabilities are generally recognised on all taxable temporary differences in full with no discounting. Deferred taxation assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. However, deferred tax is not provided on the initial recognition of goodwill, nor on the initial recognition of an asset or liability, unless the related transaction is a business combination or affects tax or accounting profit.

Deferred taxation is calculated using the tax rates and laws that are expected to apply in the period when the liability is settled or the asset is realised, provided they are enacted or substantively enacted at the balance sheet date. The carrying value of deferred taxation assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available against which taxable temporary differences can be utilised. Deferred tax is charged or credited to either the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income or equity to the extent that it relates to items charged or credited. Deferred tax relating to items charged or credited directly to equity is also credited or charged to equity.

Principal accounting policies – Group continued

Revenue

Revenue is measured in accordance with IAS 18 'Revenue' and IAS 11 'Construction Contracts' at the fair value of the consideration received or receivable, for goods and services provided in the normal course of business, net of rebates and discounts and after eliminating sales within the Group.

Housing

Revenue is recognised when the outcome of a job or contract can be estimated reliably; revenue associated with the transaction is recognised by reference to the stage of completion of work at the balance sheet date. The outcome of the transaction is deemed to be able to be estimated reliably when all the following conditions are satisfied:

- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the entity;
- the stage of completion of the transaction at the balance sheet date can be measured reliably; and
- the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

Whilst all Housing contracts can fit within the guidelines laid down for revenue recognition as detailed above, the alternative contractual pricing mechanisms do result in different methods of assessing the stage of completion. The Group has therefore recognised revenue dependent on the nature of transactions in line with IAS 18.

There are some contracts where we are entitled to a fee to reimburse the costs relating to a new contract start-up. This fee is sometimes paid on commencement or paid in instalments over an extended period. Where the contractual entitlement to this income crystallises upon commencement, the revenue is recognised. All costs relating to pre-commencement and mobilisation are written off as they are incurred.

There are numerous contractual pricing mechanisms but one can broadly divide these into five types.

Schedule of rates (SOR) contracts

There is an element of SOR in the majority of contracts. At tender stage we enter a price for each of the numerous tasks carried out in respect of property maintenance. Typically we price for uplift or a discount against a pre-priced schedule. This price will, in some cases, be an all-encompassing price for the cost of direct works, the local site overhead, central overhead and profit contribution. In other instances, the SOR tendered may only recover direct works with an alternative mechanism to recover the other elements. Wherever possible, we seek to identify all works tickets received individually and capture costs and billing at the individual work ticket level. In so doing, this allows revenue to be recognised with a high degree of accuracy. Typically, reactive maintenance works are invoiced within a month of completion; hence, the majority of revenue recognised has already been valued at the individual work ticket level and the significant majority has been subsequently settled. The only element of revenue or profit recognition that requires judgement is against those jobs that are part complete or those completed works that have not been subject to a final valuation.

For part completed works, consideration needs to be given as to whether the Group will recover the transaction costs incurred. Whether the outcome of the transaction can be estimated reliably needs to be considered contract by contract based on historic outcomes and knowledge of any events that may affect future job profitability. Where the outcome of the transaction cannot be estimated reliably, revenue is recognised only to the extent that the costs incurred are anticipated to be recovered. Where the outcome of the transaction can be estimated reliably, an element of anticipated profit is recognised within revenue to the extent that historic outcomes adjusted for knowledge of any events that may affect future job profitability support such recognition.

For completed but not yet priced works, the outcome of the individual valued work tickets is not reviewed individually for the purposes of profit and revenue recognition. However, given the high volume of historical data to provide an accurate indication of underlying contract margin at a particular site, the Group considers that the application of an anticipated profit margin on cost to all completed and unbilled works produces a reliable measure.

For completed and priced works, the likely outcome for the individual work ticket can be determined individually for the purposes of profit and revenue recognition. The Group considers that the recognition of the anticipated profit for the individual job within revenue is appropriate.

Full provision is made in respect of any job if a future loss is foreseen.

Revenue continued

Housing continued

Open book contracts

Typically the open book element of contracts relates to the local site overhead. A priced overhead model is usually provided to a client at tender stage and the client pays the Group a fixed sum for maintaining this local site. This is typically an agreed fixed price. Revenue is recognised in line with cost incurred and similarly the attributable profit recognised against that cost.

Any over or underspends are typically at the risk of the Group. The actual overhead spend is often subject to an open book review which is then used as the basis for agreeing future pricing.

On the rare occasions that a contract does recover costs under a pure 'cost plus' arrangement, revenue is recognised in line with cost incurred and similarly the attributable profit recognised against that cost.

Full provision is made in respect of any contract if a future loss is foreseen.

Lump sum contracts

This type of contract is becoming more commonplace. To avoid the onerous burden of administering a high volume, low value activity, the pricing mechanism is reduced to either a price per ticket or a price per property. Historically, many gas servicing and breakdown contracts have been procured on a lump sum basis. However, it is now becoming increasingly common within the reactive maintenance environment. There is typically an exclusions list for works that are not considered repairs and not deemed to fall within the lump sum price. It is normal for this excluded element of the works to be billed under an SOR arrangement.

For practical purposes, in the majority of lump sum contracts, revenue is recognised on a straight-line basis over the contract term. There is not a material impact of seasonality in a client's reactive maintenance spend (in terms of either volume or value of orders received). In terms of the lump sum element of the contract, the revenue is split evenly across the twelve-monthly reporting periods. No element of revenue is either advanced or deferred.

There are a small number of lump sum contracts where recognising revenue on a straight-line basis would be inappropriate. These are contracts where the phasing of the works over the contract term varies materially over the period of the contract and there is a mismatch between the delivery of works and the timing of invoicing against those works. For these contracts, the Group has historically reverted to recognising revenue based on the proportion of costs incurred to date compared with the estimated total costs of the contract.

Full provision is made in respect of any contract if a future loss is foreseen.

Rental income

Rental income relating to Housing Management activities is recognised in the Income Statement on a straight-line basis over the term of the lease.

Where initial costs are required to make good the housing to perform Housing Management activities, a straight-line basis of revenue recognition would not be appropriate. Where there are initial costs, revenue is recognised based on the proportion of costs incurred to date compared with the estimated total costs of the contract. Full provision is made in respect of any contract if a future loss is foreseen.

Construction contracts

Revenue reflects the contract activity during the year and is measured at the fair value of consideration received or receivable. When the outcome can be assessed reliably, contract revenue and associated costs are recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the balance sheet date. The stage of completion of the contract at the balance sheet date is usually assessed by comparing the proportion of costs incurred to estimated total contract costs. Where this is not representative, contract milestones are used as a basis of assessing the stage of completion. Where the outcome of a construction contract cannot be estimated reliably, revenue is recognised only to the extent that it is probable that contract costs incurred will be recoverable. Contract costs are recognised as an expense in the period in which they are incurred.

In the case of a fixed price contract, the outcome of a construction contract is deemed to be estimated reliably when all the following conditions are satisfied:

- it is probable that economic benefits associated with the contract will flow to the Group;
- both the contract costs to complete the contract and the stage of completion at the balance sheet date can be measured reliably; and
- the contract costs attributable to the contract can be clearly identified and measured reliably so that actual contract costs incurred can be compared with prior estimates.

Principal accounting policies – Group continued

Revenue continued

Housing continued

Construction contracts continued

The gross amount due from customers for contract work is presented as an asset for all contracts in progress for which costs incurred, plus recognised profits (less recognised losses), exceed progress billings. The gross amount due to customers for contract work is presented as a liability for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less losses).

Full provision is made for losses on all contracts in the year in which the future loss is first foreseen.

Care

Revenue is recognised when the actual care has been delivered and is generally based on a price per time period of care delivered. Revenue relating to care delivered and not invoiced is accrued and disclosed under trade and other receivables as amounts recoverable on contracts. Certain 'block' contracts guarantee a certain level of revenue. Revenue attributable to any unused capacity under block contracts, where the Group is able to invoice for contracted services not provided, is recognised when the recovery of income is considered virtually certain. There is minimal scope for judgement based on the care process.

The Group utilises rostering systems to manage care. These systems allow for planning a rota for each staff member, together with the corresponding pay and bill rates for the particular service type, length of service and time of delivery. These results are very accurate in the calculation of billable time, income and corresponding employee pay for a particular contract, branch or region.

Accrued income is determined by applying an average historical billing rate to the number of unbilled hours delivered at the balance sheet date. Variances are reviewed in the following month once actual billing is known. The rostering systems allow unbilled hours to be calculated based on planned, rostered and actual visits along with the corresponding pay and bill rates for the particular service type, length of service and time of delivery. These results are very accurate in the calculation of billable time, income and corresponding employee pay for a particular contract, branch or region.

Segment reporting

Segment information is presented in respect of the Group's operating segments based upon the format that the Group reports to its chief operating decision makers.

The Group considers that the chief operating decision makers are the Executive Directors and Senior Executives of the business.

Exceptional costs

Exceptional costs are disclosed on the face of the Consolidated Income Statement where these are material and considered necessary to explain the underlying financial performance of the Group. They are either one-off in nature or necessary elements of expenditure to derive future benefits for the Group which have not been capitalised in the Consolidated Balance Sheet.

Costs of restructure are only considered to be exceptional where the restructure is transformational and the resultant cost is significant.

Acquisition costs are only considered to be exceptional where the acquisition and the resultant cost are significant.

Employee benefits

Retirement benefit obligations

The Group operates both defined benefit and defined contribution pension schemes as follows:

i) Defined contribution pensions

A defined contribution plan is a pension plan under which the Group pays fixed contributions into an independent entity. The Group has no legal obligations to pay further contributions after payment of the fixed contribution.

The contributions recognised in respect of defined contribution plans are expensed as they fall due. Liabilities and assets may be recognised if underpayment or prepayment has occurred and are included in current liabilities or current assets as they are normally of a short-term nature.

The assets of the schemes are held separately from those of the Group in an independently administered fund.

Employee benefits continued

Retirement benefit obligations continued

ii) Defined benefit pensions

The Group contributes to defined benefit schemes which require contributions to be made to separately administered funds.

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligations for any benefits from this kind of pension plan remain with the Group, even if plan assets for funding the defined benefit plan have been set aside.

Scheme liabilities are measured using the projected unit funding method, applying the principal actuarial assumptions at the balance sheet date. Assets are measured at market value. In accordance with IFRIC 14, the asset that is recognised is restricted to the amount by which the IAS 19 (Revised) service cost is expected, over the lifetime of the scheme, to exceed funding contributions payable in respect of accruing benefits.

Where the Group has a contractual obligation to make good any deficit in its share of a Local Government Pension Scheme (LGPS) but also has the right to recover the costs of making good any deficit from the Group's client, the fair value of that guarantee asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. The right to recover costs is also limited to situations where the cap on employer contributions payable by the Group is not set so as to contribute to reducing the deficit in the scheme. Movements in the guarantee asset are taken to the Income Statement and to the Statement of Comprehensive Income to match the movement in pension assets and liabilities.

Actuarial gains and losses are taken to the Statement of Comprehensive Income as incurred. For this purpose, actuarial gains and losses comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

Other movements in the net surplus of deficit are recognised in the Income Statement, including the current service cost, any past service cost and the effect of curtailments or settlements. The net interest cost is also charged to the Income Statement. The amount charged to the Income Statement in respect of these plans in included within operating costs.

The Group's contributions to the scheme are paid in accordance with the rules of the schemes and the recommendations of the actuary.

Share-based employee remuneration

All share-based payment arrangements that were granted after 7 November 2002 and had not vested before 1 January 2005 are recognised in the consolidated financial statements in accordance with IFRS 2.

The Group operates equity-settled and cash-settled share-based remuneration plans for its employees. All employee services received in exchange for the grant of any share-based remuneration are measured at their fair values. These are indirectly determined by reference to the fair value (excluding the effect of non-market based vesting conditions) of the share options awarded. Their value is determined at the date of grant and is not subsequently remeasured unless the conditions on which the award was granted are modified. The fair value at the date of the grant is calculated using the Black Scholes option pricing model and the cost is recognised on a straight-line basis over the vesting period. Adjustments are made to reflect expected and actual forfeitures during the vesting period. For SAYE plans, employees are required to contribute towards the plan. This non-vesting condition is taken into account in calculating grant date fair value.

All share-based remuneration is ultimately recognised as an expense in the Income Statement. For equity-settled share-based payments there is a corresponding credit to the share-based payment reserve; for cash-settled share-based payments the Group recognises a liability at the balance sheet date.

Upon exercise of share options, the proceeds received net of any directly attributable transaction costs up to the nominal value of the shares issued are allocated to share capital, with any excess being recorded as share premium.

Principal accounting policies – Group continued

Leases

In accordance with IAS 17 'Leases', the economic ownership of a leased asset is transferred to the lessee if they bear substantially all the risks and rewards related to the ownership of the leased asset. The related asset is recognised at the time of inception of the lease at the fair value of the leased asset or, if lower, the present value of the lease payments plus incidental payments, if any, to be borne by the lessee. A corresponding amount is recognised as a finance leasing liability, irrespective of whether some of these lease payments are payable upfront at the date of inception of the lease.

Subsequent accounting for assets held under finance lease agreements, i.e. depreciation methods and useful lives, correspond to those applied to comparable acquired assets. The corresponding finance leasing liability is reduced by lease payments less finance charges, which are expensed to finance costs. Finance charges represent a constant periodic rate of interest on the outstanding balance of the finance lease liability.

All other leases are treated as operating leases. Payment on operating lease agreements is recognised as an expense on a straight-line basis over the lease term. Associated costs, such as maintenance and insurance, are expensed as incurred.

The Group does not act as a lessor.

Financial instruments

Financial assets and liabilities are recognised in the Balance Sheet when the Group becomes party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Group are as follows:

Financial assets

When financial assets are recognised initially under IAS 39 'Financial Instruments: Recognition and Measurement', they are measured at fair value, net of transaction costs other than for financial assets carried at fair value through the Income Statement.

The Group's financial assets are included in the Balance Sheet as current assets, except for those maturing more than twelve months after the balance sheet date, whereupon they are classified as non-current assets. The Group's financial assets comprise 'Trade and other receivables', 'Amounts recoverable on contracts' and 'Cash at bank and in hand' in the Balance Sheet.

Loans and receivables

Trade receivables, amounts recoverable on contracts and cash at bank and in hand are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Trade receivables and amounts recoverable on contracts are initially recorded at fair value net of transaction costs, being invoiced value less any provisional estimate for impairment should this be necessary due to a loss event. Trade receivables are subsequently remeasured at invoiced value, less an updated provision for impairment. Any change in their value through impairment or reversal of impairment is recognised in the Income Statement.

Provisions against trade receivables and amounts recoverable on contracts are made when objective evidence is received that the Group will not be able to collect all amounts due to it in accordance with the original terms of those receivables. The amount of the write down is determined as the difference between the asset's carrying amount and the present value of estimated future cash flows. Individually significant balances are reviewed separately for impairment based on the credit terms agreed with the customer. Other balances are grouped into credit risk categories and reviewed in aggregate.

Cash and cash equivalents include cash at bank and in hand and bank deposits available with no notice or less than three months' notice from inception that are subject to an insignificant risk of changes in value. Bank overdrafts are presented as current liabilities to the extent that there is no right of offset with cash balances.

Following initial recognition, financial assets are subsequently remeasured at amortised cost using the effective interest rate method.

Financial liabilities

The Group's financial liabilities are overdrafts, trade and other payables including contingent consideration, and interest rate swaps. They are included in the Balance Sheet line items 'Short-term borrowings and overdrafts', 'Trade and other payables', 'Financial liabilities' and 'Other liabilities'.

All interest related charges are recognised as an expense in 'Finance cost' in the Income Statement with the exception of those that are directly attributable to the construction of a qualifying asset which are capitalised as part of that asset.

Financial instruments continued

Financial liabilities continued

Bank and other borrowings are initially recognised at fair value net of transaction costs. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognised respectively in finance revenue and finance costs. Borrowing costs are recognised as an expense in the period in which they are incurred with the exception of those which are directly attributable to the construction of a qualifying asset which are capitalised as part of that asset.

Trade payables on normal terms are not interest bearing and are stated at their fair value on initial recognition and subsequently at amortised cost.

Contingent consideration is initially recognised at fair value and is subsequently measured at fair value through the Income Statement.

Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to interest rate risks arising from operational and financing activities.

Derivative financial instruments are recognised initially and subsequently at fair value, with mark-to-market movements recognised in the Income Statement except where cash flow hedge accounting is applied.

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for trading purposes.

Hedge accounting for interest rate swaps

Where an interest rate swap is designated as a hedge of the variability in cash flows of an existing or highly probable forecast loan interest payment, the effective part of any valuation gain or loss on the swap instrument is recognised in 'Other comprehensive income' in the hedging reserve. The cumulative gain or loss is removed from equity and recognised in the Income Statement at the same time as the hedged transaction. The ineffective part of any gain or loss is recognised in the Income Statement immediately.

When a hedging instrument or hedge relationship is terminated but the hedged transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer probable, the cumulative unrealised gain or loss recognised in equity is recognised in the Income Statement immediately.

Nature and purpose of each reserve in equity

Share capital is determined using the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Equity-settled shared-based employee remuneration is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The hedging reserve represents the effective part of any gain or loss on a cash flow hedge which has not been removed from equity and recognised in the Income Statement.

The merger reserve relates to the difference between the nominal value and total consideration in respect of the acquisition of Careforce Group plc, Supporta plc and Morrison Facilities Services Limited where the Company was entitled to the merger relief offered by the Companies Act.

Dividends

Dividend distributions payable to equity shareholders are included in 'Current financial liabilities' when the dividends are approved in a general meeting prior to the balance sheet date.

Principal accounting policies – Group continued

Use of judgements and estimates

The preparation of financial statements requires management to make estimates and judgements that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenditure during the reported period. The estimates and associated judgements are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying judgements are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

In the preparation of these consolidated financial statements, estimates and judgements have been made by management concerning the selection of useful lives of property, plant and equipment, provisions necessary for certain liabilities, when to recognise revenue on long-term contracts, actuarial judgements, discount rates used within impairment reviews, the underlying share price volatility for valuing equity-based payments and other similar evaluations. Actual amounts could differ from those estimates.

Critical judgements in applying the Group's accounting policies

Revenue recognition

Revenue is recognised based on the stage of completion of job or contract activity. As described in the Revenue section on pages 92 and 93, certain types of Housing pricing mechanisms and Care revenue require minimal judgement; however, Housing lump sum contracts and construction contracts do require judgements and estimates to be made to determine the stage of completion and the expected outcome for the individual contract.

Joint arrangements

The Group participates in a number of joint arrangements where control of the arrangement is shared with another party. A joint arrangement is classified as a joint operation or as a joint venture, depending on management's assessment of the legal form and substance of the arrangement.

The classification can have a material impact on the consolidated financial statements. The Group's share of assets, liabilities, revenue, expenses and cash flows of joint operations would be included in the consolidated financial statements on a line-by-line basis, whereas the Group's investment and share of results of joint ventures are shown within single line items in the Consolidated Balance Sheet and Consolidated Income Statement respectively.

Key sources of estimation uncertainty

Impairment of goodwill

Determining whether goodwill is impaired requires an estimate of the value in use of the CGUs to which goodwill has been allocated. The value-in-use calculation involves an estimate of the future cash flows of the CGUs and also the selection of appropriate discount rates to calculate present values. Future cash flows are estimated using the current one-year budget forecast, extrapolated for a future growth rate. The estimated growth rates are based on past experience and knowledge of the individual sector's markets. Changes in the estimated growth rate could result in variations to the carrying value of goodwill. The Directors consider that the estimates and judgements involved in determining the value in use of the Care CGU goodwill are the most significant and have therefore utilised the services of an external consultant to undertake this impairment review. The estimated cash flows and future growth rates are based on past experience and knowledge of the sector. The value in use is most sensitive to changes in the terminal growth rate, the explicit growth rate and the discount rate. The sensitivity to changes in these estimations is detailed in note 11.

Use of judgements and estimates continued

Key sources of estimation uncertainty continued

Defined benefit liabilities

A number of key estimates have been made, which are given below, which are largely dependent on factors outside the control of the Group:

- inflation rates;
- mortality;
- discount rate; and
- salary and pension increases.

Details of the particular estimates used are included in the pensions note. Sensitivity analysis for these key estimates is included in note 24.

Where the Group has a contractual obligation to make good any deficit in its share of an LGPS but also has the right to recover the costs of making good any deficit from the Group's client, the fair value of that asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. The Directors have made judgements in respect of whether any of the deficit is as a result of such situations.

The right to recover costs is also limited to situations where the cap on employer contributions to be suffered by the Group is not set so as to contribute to reducing the deficit in the scheme. The Directors, in conjunction with the scheme actuaries, have made judgements in respect of the predicted future service cost and contributions to the scheme to reflect this in the fair value of the asset recognised.

New standards and interpretations not yet applied

IFRS 9 'Financial Instruments' specifies how an entity should classify and measure financial assets, including some hybrid contracts. The Group is expected to apply this standard for the Group's 31 December 2018 financial statements.

IFRS 15 'Revenue from Contracts with Customers'. This standard introduces a new revenue recognition model that recognises revenue either at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognised. The Group is currently expected to apply this standard for the Group's 31 December 2018 financial statements. Management has started to assess the impact of this standard but is not yet in a position to provide quantified information.

IFRS 16 'Leases'. Under IFRS 16 lessees have to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for almost all lease contracts. This is a significant change compared to IAS 17 under which lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 contains an optional exemption for certain short-term leases and leases of low value assets. The Group is expected to apply this standard for the Group's 31 December 2019 financial statements, subject to endorsement by the EU. Management has started to assess the impact of this standard but is not yet in a position to provide quantified information.

A number of standards have been modified. These include Disclosure Initiative (Amendments to IAS 7), Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12) and Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2). None of these amendments are expected to have a material effect on the Group's Financial Statements.

Consolidated income statement

For the year ended 31 December 2016

	Note	2016 £'000	2015 £'000
Continuing operations			
Sales revenue	1	**940,100**	881,139
Cost of sales		**(695,206)**	(649,007)
Gross profit		**244,894**	232,132
Other administrative expenses		**(203,044)**	(193,470)
Amortisation of acquisition intangibles	11	**(10,690)**	(10,837)
Total administrative costs		**(213,734)**	(204,307)
Operating profit before amortisation of acquisition intangibles	1	**41,850**	38,662
Operating profit	1	**31,160**	27,825
Finance income	3	**1,152**	1,171
Finance costs	3	**(2,940)**	(3,076)
Profit for the year before tax and the amortisation of acquisition intangibles		**40,062**	36,757
Profit for the year before tax		**29,372**	25,920
Tax expense	6	**(3,676)**	(3,832)
Profit for the year from continuing operations		**25,696**	22,088
Discontinued operations			
Loss from discontinued operations	7	**—**	(7,964)
Tax income from discontinued operations	7	**—**	165
Loss for the year after tax from discontinued operations		**—**	(7,799)
Profit for the year from continuing and discontinued operations		**25,696**	14,289
Attributable to:			
Owners of the Parent		**21,526**	12,874
Non-controlling interest		**4,170**	1,415
Profit for the year		**25,696**	14,289
Earnings per share – from continuing operations			
Basic	9	**23.54p**	20.31p
Diluted	9	**23.41p**	20.10p
Earnings per share – from continuing and discontinued operations			
Basic	9	**21.03p**	12.65p
Diluted	9	**20.91p**	12.52p

The accompanying accounting policies and notes form an integral part of these financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2016

	Note	**2016 £'000**	2015 £'000
Profit for the year		**25,696**	14,289
Other comprehensive income/(expense):			
Which will be subsequently reclassified to the Income Statement:			
Cash flow hedges:			
– losses arising in the year	19	**(884)**	(72)
– reclassification to the Income Statement	19	**643**	559
Increase/(decrease) in deferred tax asset in respect of cash flow hedges	19	**39**	(97)
Which will not be subsequently reclassified to the Income Statement:			
Actuarial gain/(loss) on defined benefit pension scheme	24	**3,676**	(3,371)
(Decrease)/increase in deferred tax asset in respect of defined benefit pension schemes	20	**(804)**	675
Other comprehensive income/(expense) for the year		**2,670**	(2,306)
Total comprehensive income for the year		**28,366**	11,983

Attributable to:		
Owners of the Parent	**24,196**	10,568
Non-controlling interest	**4,170**	1,415
Total comprehensive income for the year	**28,366**	11,983

The accompanying accounting policies and notes form an integral part of these financial statements.

Consolidated balance sheet
As at 31 December 2016

	Note	2016 £'000	2015 £'000
Assets			
Non-current			
Goodwill	10	**193,712**	193,058
Intangible assets	11	**25,913**	31,851
Property, plant and equipment	12	**20,265**	18,436
Pension and other employee benefits	24	**15,992**	8,272
Financial assets	17	**677**	—
Deferred tax asset	20	**5,704**	6,584
		262,263	258,201
Current			
Assets included in disposal group classified as held for sale	7	**—**	13,255
Inventories	14	**11,234**	9,021
Trade and other receivables	15	**157,181**	146,879
Financial assets	17	**839**	—
Cash at bank and in hand	19	**52,904**	68,612
		222,158	237,767
Total assets		**484,421**	495,968
Equity			
Equity attributable to the shareholders of Mears Group PLC			
Called up share capital	21	**1,026**	1,019
Share premium account		**58,320**	58,124
Share-based payment reserve		**1,975**	1,651
Hedging reserve	19	**(774)**	(572)
Merger reserve		**46,214**	46,214
Retained earnings		**92,555**	86,438
Total equity attributable to the shareholders of Mears Group PLC		**199,316**	192,874
Non-controlling interest		**(642)**	(1,246)
Total equity		**198,674**	191,628
Liabilities			
Non-current			
Long-term borrowing and overdrafts	19	**60,000**	57,500
Pension and other employee benefits	24	**7,498**	4,224
Deferred tax liabilities	20	**7,120**	6,970
Financial liabilities	17	**612**	368
Other payables	18	**15,950**	15,396
		91,180	84,458
Current			
Liabilities included in disposal group classified as held for sale	7	**—**	13,255
Short-term borrowings and overdrafts	19	**5,278**	10,290
Trade and other payables	16	**187,264**	194,103
Financial liabilities	17	**478**	510
Current tax liabilities		**1,547**	1,724
Current liabilities		**194,567**	219,882
Total liabilities		**285,747**	304,340
Total equity and liabilities		**484,421**	495,968

The financial statements were approved and authorised for issue by the Board of Directors and were signed on its behalf on 27 March 2017.

D J Miles
Director

A C M Smith
Director

Company number: 03232863

The accompanying accounting policies and notes form an integral part of these financial statements.

Consolidated cash flow statement
For the year ended 31 December 2016

	Note	2016 £'000	2015 £'000
Operating activities			
Result for the year before tax		**29,372**	25,920
Adjustments	22	**20,438**	19,887
Change in inventories		**(2,213)**	(553)
Change in trade and other receivables		**(8,793)**	6,668
Change in trade and other payables		**(4,289)**	(7,458)
Cash inflow from operating activities of continuing operations before taxation		**34,515**	44,464
Taxes paid		**(4,877)**	(5,888)
Net cash inflow from operating activities of continuing operations		**29,638**	38,576
Net cash outflow from operating activities of discontinued operations		**(3,925)**	(4,503)
Net cash inflow from operating activities		**25,713**	34,073
Investing activities			
Additions to property, plant and equipment		**(10,029)**	(4,297)
Additions to other intangible assets		**(2,904)**	(2,978)
Proceeds from disposals of property, plant and equipment		**2**	86
Acquisition of subsidiary undertakings, net of cash		**(10,019)**	(17,590)
Loans made to other entities (non-controlled)		**(211)**	—
Interest received		**35**	158
Net cash outflow from investing activities		**(23,126)**	(24,621)
Financing activities			
Proceeds from share issue		**202**	1,418
Discharge of finance lease liability		**(661)**	(545)
Interest paid		**(2,822)**	(2,764)
Dividends paid – Mears Group shareholders		**(11,483)**	(10,445)
Dividends paid – non-controlling interests		**(1,019)**	(128)
Net cash outflow from financing activities		**(15,783)**	(12,464)
Cash and cash equivalents, beginning of year		**822**	3,834
Net decrease in cash and cash equivalents		**(13,196)**	(3,012)
Cash and cash equivalents, end of year		**(12,374)**	822

Cash and cash equivalents comprises the following:		
– cash at bank and in hand	**52,904**	68,612
– borrowings and overdrafts	**(65,278)**	(67,790)
Cash and cash equivalents	**(12,374)**	822

Cash conversion key performance indicator		
Cash inflow from operating activities of continuing operations	**34,515**	44,464
EBITDA for continuing operations	**49,260**	44,940
Conversion	**70.1%**	98.9%

The accompanying accounting policies and notes form an integral part of these financial statements.

Consolidated statement of changes in equity

For the year ended 31 December 2016

	Attributable to equity shareholders of the Company							
	Share capital £'000	Share premium account £'000	Share-based payment reserve £'000	Hedging reserve £'000	Merger reserve £'000	Retained earnings £'000	Non-controlling interest £'000	Total equity £'000
At 1 January 2015	1,011	56,714	1,653	(962)	46,214	92,179	(2,347)	194,462
Net result for the year	—	—	—	—	—	12,874	1,415	14,289
Other comprehensive income/(expense)	—	—	—	390	—	(2,696)	—	(2,306)
Total comprehensive income for the year	—	—	—	390	—	10,178	1,415	11,983
Deferred tax on share-based payments	—	—	—	—	—	(552)	—	(552)
Issue of shares	8	1,410	—	—	—	—	—	1,418
Share option charges	—	—	771	—	—	—	—	771
Exercise of share options	—	—	(773)	—	—	773	—	—
On acquisition	—	—	—	—	—	—	282	282
Transactions with non-controlling interests	—	—	—	—	—	(5,695)	(468)	(6,163)
Dividends	—	—	—	—	—	(10,445)	(128)	(10,573)
At 1 January 2016	1,019	58,124	1,651	(572)	46,214	86,438	(1,246)	191,628
Net result for the year	—	—	—	—	—	21,526	4,170	25,696
Other comprehensive income	—	—	—	(202)	—	2,872	—	2,670
Total comprehensive income for the year	—	—	—	(202)	—	24,398	4,170	28,366
Deferred tax on share-based payments	—	—	—	—	—	(635)	—	(635)
Issue of shares	7	196	—	—	—	—	—	203
Share option charges	—	—	324	—	—	—	—	324
On disposal	—	—	—	—	—	—	(2,570)	(2,570)
Transactions with non-controlling interests	—	—	—	—	—	(6,163)	23	(6,140)
Dividends	—	—	—	—	—	(11,483)	(1,019)	(12,502)
At 31 December 2016	**1,026**	**58,320**	**1,975**	**(774)**	**46,214**	**92,555**	**(642)**	**198,674**

The accompanying accounting policies and notes form an integral part of these financial statements.

Notes to the financial statements – Group

For the year ended 31 December 2016

1. Segment reporting

Segment information is presented in respect of the Group's operating segments. Segments are determined by reference to the internal reports reviewed by the Board.

The Group had two operating segments during the year:

- Housing – services within this sector comprise a full housing management service predominantly to Local Authorities and other Registered Social Landlords; and
- Care – services within this sector comprise personal care services to people in their own homes.

All of the Group's activities are carried out within the United Kingdom and the Group's principal reporting to its chief operating decision maker is not segmented by geography.

The principal financial measures used by the chief operating decision maker and the Board to review the performance of the operating segments are that of revenue growth and operating margins in both the core divisions of Housing and Care. The operating result utilised within the key performance measures is stated before amortisation of acquisition intangibles and costs relating to the long-term incentive plans.

	2016			2015		
Operating segments	Housing £'000	Care £'000	Total £'000	Housing £'000	Care £'000	Total £'000
Revenue	**787,530**	**152,570**	**940,100**	735,129	146,010	881,139
Operating result pre amortisation of acquisition intangibles and long-term incentive plans	**44,057**	**(1,199)**	**42,858**	42,413	(1,601)	40,812
Operating margin pre amortisation of acquisition intangibles and long-term incentive plans	**5.60%**	**(0.79%)**	**4.56%**	5.77%	(1.10%)	4.63%
Long-term incentive plans	**(1,008)**	**—**	**(1,008)**	(2,150)	—	(2,150)
Operating result pre amortisation of acquisition intangibles	**43,049**	**(1,199)**	**41,850**	40,263	(1,601)	38,662
Amortisation of acquisition intangibles			**(10,690)**			(10,837)
Operating result			**31,160**			27,825
Net finance costs			**(1,788)**			(1,905)
Tax expense			**(3,676)**			(3,832)
Profit for the year from continuing activities			**25,696**			22,088

All revenue and all non-current assets arise within the United Kingdom. All of the revenue reported is external to the Group. No revenue in respect of a single customer comprises more than 10% of the total revenue reported.

Notes to the financial statements – Group continued
For the year ended 31 December 2016

1. Segment reporting continued
In addition, the following disclosures have been provided in respect of segmental analysis required by IFRS 8 'Operating Segments':

	2016			2015		
Operating segments	**Housing £'000**	**Care £'000**	**Total £'000**	Housing £'000	Care £'000	Total £'000
Segment assets	**348,066**	**136,355**	**484,421**	359,578	136,390	495,968
Segment liabilities	**(214,339)**	**(71,408)**	**(285,747)**	(237,689)	(66,651)	(304,340)
Property, plant and equipment additions	**6,553**	**872**	**7,425**	5,388	829	6,217
Depreciation	**4,066**	**1,507**	**5,573**	3,710	1,253	4,963
Amortisation of acquisition intangibles	**6,878**	**3,812**	**10,690**	6,707	4,130	10,837
Amortisation of other intangibles	**1,837**	**—**	**1,837**	1,314	—	1,314

2. Operating costs
Operating costs, relating to continuing activities, include:

	2016 £'000	2015 £'000
Share-based payments	**324**	771
Long-term incentives	**684**	1,379
Depreciation	**5,573**	4,963
Amortisation of acquisition intangibles	**10,690**	10,837
Amortisation of other intangibles	**1,837**	1,314
Loss on disposal of property, plant and equipment	**48**	45
Hire of plant and machinery	**5,450**	5,727
Other operating lease rentals	**112,940**	65,461

Fees payable for audit and non-audit services during the year were as follows:

	2016 £'000	2015 £'000
Fees payable to the auditor for the audit of the Group's financial statements	**60**	60
Other fees payable to the auditor in respect of:		
– auditing of accounts of subsidiary undertakings pursuant to legislation	**331**	331
– taxation advice fees	**—**	21
– audit related advisory fees	**8**	8
– accreditation related assurance fees	**45**	—
Total auditor's remuneration	**444**	420

During 2016, Mears was delighted to retain its accreditation with Investors in People (IIP). This followed a four-week assessment programme which involved external assessors visiting 16 branches and interviewing around 300 employees. IIP in the South of England is delivered by Grant Thornton under licence from the UK Commission for Employment and Skills. Whilst Mears played no part in the selection of Grant Thornton as its external assessor, the fee of £0.05m was paid to Grant Thornton for this assessment and is included within accreditation related assurance services. The Group has a strict policy of prohibiting the external auditor from carrying out non-audit services in order to safeguard audit objectivity and independence.

3. Finance income and finance costs

	2016 £'000	2015 £'000
Interest charge on overdrafts and short-term loans	**(2,134)**	(2,136)
Interest charge on hedged items (effective hedges)	**(643)**	(559)
Other interest	**(26)**	(4)
Finance costs on bank loans, overdrafts and finance leases	**(2,803)**	(2,699)
Interest charge on defined benefit obligation	**(137)**	(252)
Unwinding of discounting	**—**	(125)
Total finance costs	**(2,940)**	(3,076)
Interest income resulting from short-term bank deposits	**19**	16
Interest income resulting from defined benefit asset	**1,085**	964
Unwinding of discounting	**40**	49
Other interest income	**8**	142
Finance income	**1,152**	1,171
Net finance charge	**(1,788)**	(1,905)
Gains and losses on hedged items recognised in other comprehensive income		
Losses arising in the year	**(884)**	(72)
Reclassification to the Income Statement	**643**	559
Changes in mark-to-market of interest rate swaps (effective hedges)	**241**	487

4. Employees

Staff costs during the year were as follows:

	2016 £'000	2015 £'000
Wages and salaries	**299,684**	291,542
Social security costs	**25,785**	22,310
Other pension costs	**9,292**	9,859
	334,761	323,711

Notes to the financial statements – Group continued
For the year ended 31 December 2016

4. Employees continued
The average number of employees of the Group during the year was:

	2016 Number	2015 Number
Site workers	**3,897**	3,900
Carers	**8,531**	7,318
Office and management	**3,291**	3,110
	15,719	14,328

Remuneration in respect of Directors was as follows:

	2016 £'000	2015 £'000
Emoluments	**1,334**	1,323
Gains made on the exercise of share options	**1,795**	—
Pension contributions to personal pension schemes	**195**	195
	3,324	1,518

During the year contributions were paid to personal pension schemes for four Directors (2015: four).

During the year three Directors (2015: none) exercised share options.

5. Share-based employee remuneration
As at 31 December 2016 the Group maintained seven share-based payment schemes for employee remuneration.

Details of the share options outstanding are as follows:

	2016		2015	
	Number '000	Weighted average exercise price p	Number '000	Weighted average exercise price p
Outstanding at 1 January	**3,102**	**255**	2,994	223
Granted	**—**	**—**	1,462	330
Forfeited/lapsed	**(488)**	**356**	(550)	394
Exercised	**(621)**	**33**	(804)	176
Outstanding at 31 December	**1,993**	**300**	3,102	255

The weighted average share price at the date of exercise for share options exercised during the period was 405p. At 31 December 2016, 0.4m options had vested and were still exercisable at prices between 1p and 300p. These options had a weighted average exercise price of 74p and a weighted average remaining contractual life of one year.

The fair values of options granted were determined using the Black Scholes option pricing model. Significant inputs into the calculation include the market price at the date of grant and exercise prices. Furthermore, the calculation takes into account the future dividend yield, the share price volatility rate and the risk-free interest rate.

5. Share-based employee remuneration continued

The underlying expected share price volatility was determined by reference to historical data. The Company expects the volatility of its share price to reduce as it matures. The risk-free interest rate was determined by the implied yield available on a zero-coupon Government bond at the date of grant. Adjustments are made to reflect expected and actual forfeitures during the vesting period due to failure to satisfy service conditions. In the case of the SAYE scheme the expected forfeitures take account of the requirement to save throughout the life of the scheme. There were no options granted during the year and 0.5m options lapsed during the year. The market price at 31 December 2016 was 456p and the range during 2016 was 353p to 483p.

All share-based employee remuneration will be settled in equity. The Group has no legal obligation to repurchase or settle the options.

The Group recognised the following expenses related to share-based payments:

	2016 £'000	2015 £'000
Giving rise to share-based payment reserve:		
– SAYE	**324**	113
– Share Plan	**—**	658
Giving rise to liabilities:		
– MIP	**684**	1,379
	1,008	2,150

In total, £0.3m of employee remuneration expense that gave rise to additional share-based payment reserves has been included in the Consolidated Income Statement for 2016 (2015: £0.8m). In total, £0.7m (2015: £1.4m) of liabilities were recognised due to cash-settled share-based payment transactions.

Approved share option plan

Options are exercisable at a price equal to the average quoted market price of the Company's shares on the three dealing days prior to the date of grant. The vesting period is three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Options are forfeited if the employee leaves Mears before the options vest. All options issued under this plan have vested or were forfeited.

Unapproved share option plan

Options are exercisable at nominal value. The vesting period is three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Options are forfeited if the employee leaves Mears before the options vest. With the introduction of the LTIP in 2008, the Remuneration Committee has decided that no further awards will be made under the unapproved share option plan. All options issued under this plan have vested or were forfeited.

Save As You Earn (SAYE) scheme

Options are available to all employees. Options are granted for a period of three years. Options are exercisable at a price based on the quoted market price of the Company's shares at the time of invitation, discounted by up to 20%. Options are forfeited if the employee leaves Mears Group before the options vest which impacts on the number of options expected to vest. If an employee stops saving but continues in employment, this is treated as a cancellation which results in an acceleration of the share-based payment charge.

Special Incentive Plan 2007 (SIP)

The SIP was introduced in 2007 to reward the then Chief Executive Officer, Bob Holt, with premium priced options linked to long-term performance. The terms and conditions were subsequently amended on 3 July 2009. If the options remain unexercised after a period of ten years from the date of grant, the options expire. There was a single award and no further awards will be made under this plan. All options issued under this plan have vested.

Notes to the financial statements – Group continued

For the year ended 31 December 2016

5. Share-based employee remuneration continued

The Mears Group PLC Long-term Incentive Plan (LTIP)

The LTIP was introduced in October 2008 following shareholder approval. The award of options is offered to a small number of key senior management. The principal terms of the LTIP are detailed below:

Principal terms of LTIP

Number of options	Maximum award limit under the plan will be 200% of salary p.a.
Exercise price	1p
Performance period	3 years
Performance conditions	There are two performance targets attaching to the LTIP Award.
	75% of the LTIP Award will relate to an EPS growth target. The other 25% of the LTIP Award relates to the Company's TSR against the return of the FTSE All-Share Support Services Sector.
Expiry conditions	Options are forfeited if the employee leaves the Group before the options have vested.

All options issued under this plan have vested or were forfeited.

Management Incentive Plan (MIP)

The MIP was introduced in June 2013 following shareholder approval. The award of options is offered to a small number of key senior management. The MIP is a share-based payment plan which is settled through a combination of cash and shares. Further details are provided on page 73 of the Remuneration Report.

6. Tax expense

Tax recognised in the Income Statement

	2016 £'000	2015 £'000
United Kingdom corporation tax	**5,672**	5,783
Adjustment in respect of previous periods	**(972)**	(642)
Total current tax recognised in Income Statement	**4,700**	5,141
Deferred taxation charge:		
– on defined benefit pension obligations	**146**	133
– on share-based payments	**(65)**	(151)
– on accelerated capital allowances	**194**	(232)
– on amortisation of acquisition intangibles	**(2,066)**	(2,130)
– on short-term temporary timing differences	**277**	(276)
– on corporate tax losses	**617**	1,609
– impact of change in statutory tax rates	**(19)**	—
Adjustment in respect of previous periods	**(108)**	(262)
Total deferred taxation recognised in Income Statement	**(1,024)**	(1,309)
Total tax expense recognised in Income Statement on continuing operations	**3,676**	3,832
Total tax credit recognised in Income Statement on discontinued operations	**—**	(165)
Total tax expense recognised in Income Statement	**3,676**	3,667

6. Tax expense continued

Tax recognised in the Income Statement continued

The charge for the year can be reconciled to the result for the year as follows:

	2016 £'000	2015 £'000
Result for the year before tax	**29,372**	17,956
Result for the year multiplied by standard rate of corporation tax in the United Kingdom for the period of 20.0% (2015: 20.25%)	**5,874**	3,636
Effect of:		
– expenses not deductible for tax purposes	**563**	1,412
– income not subject to tax	**(885)**	—
– tax relief on exercise of share options	**(463)**	(397)
– statutory tax rate changes	**(19)**	—
– temporary timing differences not previously recognised in deferred tax	**(15)**	(20)
– tax losses not previously recognised in deferred tax	**(299)**	(60)
– adjustment in respect of prior periods	**(1,080)**	(904)
Actual tax expense	**3,676**	3,667

Deferred tax is recognised on both temporary and permanent differences between the treatment of items for tax and accounting purposes. Deferred tax on the amortisation of acquisition intangibles is a permanent difference and arises because no tax relief is due on this kind of amortisation.

Tax losses generated in previous years which are expected to be utilised against future profits are recognised as a deferred tax asset and a subsequent charge arises as those losses are utilised. The majority of the charge of £0.6m (2015: charge of £1.6m) represents losses associated with previous acquisitions which were utilised in the year.

No deferred tax asset is recognised in respect of losses of £31.3m (2015: £32.9m) across several entities in the Group as it is not expected that they will be eligible to be utilised against profits in the future.

Deferred tax is also recognised on short-term temporary timing differences, primarily relating to provisions. These differences are expected to reverse in the following year and arise because tax relief is only available when the costs are incurred.

Capital allowances represent tax relief on the acquisition of property, plant and equipment and are spread over several years at rates set by legislation. These differ from depreciation which is an estimate of the use of an item of property, plant and equipment over its useful life. Deferred tax is recognised on the difference between the remaining value of such an asset for tax purposes and its carrying value in the accounts.

The following tax has been charged to other comprehensive income or equity during the year:

	2016 £'000	2015 £'000
Deferred tax recognised in other comprehensive income		
– on defined benefit pension obligations	**804**	(675)
– on cash flow hedges	**(39)**	97
Total deferred tax recognised in other comprehensive income	**765**	(578)
Deferred tax recognised directly in equity		
Deferred tax charge:		
– on share-based payments	**(635)**	(552)
Total deferred tax recognised in equity	**(635)**	(552)
Total tax		
Total current tax	**4,700**	4,976
Total deferred tax	**(894)**	(2,439)

Notes to the financial statements – Group continued
For the year ended 31 December 2016

7. Discontinued activities
On 21 November 2013, the Group completed the disposal of the entire share capital of Haydon Mechanical and Electrical Limited ('Haydon UK'). As part of that disposal, the Group retained the beneficial interest in 49% of the share capital of an investment in a company registered in the United Arab Emirates, Haydon Mechanical and Electrical Company LLC ('Haydon LLC'). This beneficial interest was retained due to a number of performance guarantees in place at the time of the disposal which unravel as underlying contracts complete. During the period the Group reduced its interest to 1% of the share capital, completing a disposal of 48% for a nominal consideration. Upon the remaining guarantees being satisfied and the outstanding debtor settled, it is the intention of the Group to transfer the remaining share to the local management.

As at 31 December 2016, the Group has performance guarantees of £13.7m outstanding and these are anticipated to reduce to £9.4m and £nil by December 2017 and 2018 respectively. These performance guarantees are disclosed as contingent liabilities in note 27.

At 31 December 2015, a balance of £2.0m was due from Haydon Mechanical & Electrical Limited to the Group. During the period the Group fully provided against this balance. The provision of £2.0m has been reported as a loss from discontinued activities. In addition, the Group paid £0.6m in respect of an indemnity provided under the share purchase agreement. The cost of £0.6m has been reported as a loss from discontinued activities and a cash outflow from discontinued activities.

The results of Haydon LLC up until the point of disposal, which have been aggregated into a single line within the Consolidated Income Statement, comprise sales revenue of £8.3m (2015: £38.5m), costs of sales of £5.2m (2015: £44.1m), administrative expenses of £0.6m (2015: £3.3m) and a tax credit of £nil (2015: £0.2m), equating to a profit on discontinued activities of £2.6m (2015: £6.9m loss). All of this profit has been attributed to the non-controlling interest.

At 31 December 2015, a balance of £nil was due from Haydon LLC to the Group. During the period, the Group provided additional financial support to Haydon LLC of £3.4m to fund ongoing losses in the company so as to mitigate its risk in respect of the performance guarantees. This is reported as a cash outflow from discontinued operations. The Directors consider this balance to be recoverable.

8. Dividends
The following dividends were paid on ordinary shares in the year:

	2016 £'000	2015 £'000
Final 2015 dividend of 7.90p (2015: final 2014 dividend of 7.15p) per share	**8,099**	7,286
Interim 2016 dividend of 3.30p (2015: interim 2015 dividend of 3.10p) per share	**3,384**	3,159
	11,483	10,445

The proposed final 2016 dividend of 8.40p per share has not been included within the consolidated financial statements as no obligation existed at 31 December 2016.

9. Earnings per share

	Basic (continuing)		Basic (discontinued)		Basic (continuing and discontinued)	
	2016 p	2015 p	**2016 p**	2015 p	**2016 p**	2015 p
Earnings per share	**23.54**	20.31	**(2.51)**	(7.66)	**21.03**	12.65
Effect of amortisation of acquisition intangibles	**10.44**	10.65	**—**	—	**10.44**	10.65
Effect of full tax adjustment	**(3.45)**	(2.73)	**—**	—	**(3.45)**	(2.73)
Normalised earnings per share	**30.53**	28.23	**(2.51)**	(7.66)	**28.02**	20.57

	Diluted (continuing)		Diluted (discontinued)		Diluted (continuing and discontinued)	
	2016 p	2015 p	**2016 p**	2015 p	**2016 p**	2015 p
Earnings per share	**23.41**	20.10	**(2.50)**	(7.58)	**20.91**	12.52
Effect of amortisation of acquisition intangibles	**10.39**	10.54	**—**	—	**10.39**	10.54
Effect of full tax adjustment	**(3.44)**	(2.70)	**—**	—	**(3.44)**	(2.70)
Normalised earnings per share	**30.36**	27.94	**(2.50)**	(7.58)	**27.86**	20.36

A normalised EPS is disclosed in order to show performance undistorted by amortisation of intangibles. The Group defines normalised earnings as excluding the amortisation of acquisition intangibles and exceptional costs and adjusted to reflect a full tax charge. The profit attributable to shareholders before and after adjustments for both basic and diluted EPS is:

	Normalised (continuing)		Normalised (discontinued)		Normalised (continuing and discontinued)	
	2016 £'000	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000
Profit/(loss) attributable to shareholders:	**24,096**	20,673	**(2,570)**	(7,799)	**21,526**	12,874
– amortisation of acquisition intangibles	**10,690**	10,837	**—**	—	**10,690**	10,837
– full tax adjustment	**(3,535)**	(2,784)	**—**	—	**(3,535)**	(2,784)
Normalised earnings	**31,251**	28,726	**(2,570)**	(7,799)	**28,681**	20,927

Notes to the financial statements – Group continued
For the year ended 31 December 2016

9. Earnings per share continued
The calculation of EPS is based on a weighted average of ordinary shares in issue during the year. The diluted EPS is based on a weighted average of ordinary shares calculated in accordance with IAS 33 'Earnings Per Share', which assumes that all dilutive options will be exercised. The additional normalised basic and diluted EPS use the same weighted average number of shares as the basic and diluted EPS.

	2016 Million	2015 Million
Weighted average number of shares in issue:	**102.35**	101.77
– dilutive effect of share options	**0.57**	1.06
Weighted average number of shares for calculating diluted earnings per share	**102.92**	102.83

10. Goodwill

	Goodwill arising on consolidation £'000	Purchased goodwill £'000	Total £'000
Gross carrying amount			
At 1 January 2015	191,597	406	192,003
Additions on acquisition	1,055	—	1,055
At 1 January 2016	192,652	406	193,058
Revisions	654	—	654
At 31 December 2016	**193,306**	**406**	**193,712**
Accumulated impairment losses			
At 1 January 2015, at 1 January 2016 and at 31 December 2016	—	—	—
Carrying amount			
At 31 December 2016	**193,306**	**406**	**193,712**
At 31 December 2015	192,652	406	193,058

Goodwill on consolidation arises on the excess of cost of acquisition over the fair value of the net assets acquired on purchase of a company.

Purchased goodwill arises on the excess of cost of acquisition over the fair value of the net assets acquired on the purchase of the trade and assets of a business by the Group.

Revisions to goodwill additions in prior years relate to liabilities not accrued at the time of the acquisition. These revisions are not considered sufficiently material to warrant restatement of the prior year balances.

Goodwill is not amortised but is reviewed for impairment on an annual basis or more frequently if there are any indications that goodwill may be impaired. Goodwill acquired in a business combination is allocated to groups of cash-generating units (CGUs) according to the level at which management monitors that goodwill. Goodwill is carried at cost less accumulated impairment losses.

10. Goodwill continued

The carrying value of goodwill is allocated to the following CGUs:

	Goodwill arising on consolidation £'000	Purchased goodwill £'000	Total £'000
Housing	93,655	406	94,061
Care	99,651	—	99,651
	193,306	406	193,712

An asset is impaired if its carrying value exceeds the unit's recoverable amount which is based upon value in use. At 31 December 2016 impairment reviews were performed by comparing the carrying value with the value in use for the CGUs to which goodwill has been allocated.

The Housing CGU's value in use is calculated from the Board-approved one-year budgeted cash flows and extrapolated cash flows for the next four years discounted at a post-tax discount rate of 8.0% over a five-year period with a terminal value. The impairment reviews incorporated a terminal growth assumption of 2.0%, in line with the UK long-term growth rate.

The Care CGU's value in use is calculated from a detailed business plan deriving cash flows over a five-year review period, discounted at a post-tax discount rate of 8.3% over a five-year period with a terminal value. The impairment review incorporated a terminal growth assumption of 2.5%, which, whilst marginally higher than the UK long-term growth rate of 2.0%, is supported by the underlying demographics underpinning strong organic growth in adult social care.

The estimated growth rates are based on knowledge of the individual CGU's sector and market and represent management's base level expectations for future growth, dependent on the CGU. Changes to revenue and direct costs are based on past experience and expectation of future changes within the markets of the CGUs. All CGUs have the same access to the Group's Treasury function and borrowing arrangements to finance their operations.

The rates used were as follows:

	Post-tax discount rate	Pre-tax discount rate	Volume growth rate (years 1-5)	Terminal growth rate
Housing	8.00%	9.10%	5.00%	2.00%
Care	8.30%	9.47%	2.91%	2.50%

Housing

The contracts awarded within the social housing area are significant in size and the contract terms typically average six years in duration. The record of Mears in retaining contracts on expiry is typically over 90%.

Budgeted operating profits during the budget period are estimated by reference to the operating margin achieved in the period leading up to the start of the budget period, flexed for known changes in either the pricing mechanism or the cost base at a contract level. There is no inclusion of any anticipated efficiency improvements which have not been formally committed to before the year end.

The Directors consider that reasonably possible changes in these key assumptions would not cause a CGU's carrying amount to exceed its recoverable amount.

Notes to the financial statements – Group continued
For the year ended 31 December 2016

10. Goodwill continued

Care

Management recognises that there remain significant difficulties within the homecare market, although the sector has seen some improvements over the last twelve months. The introduction of the National Living Wage proved a significant boost for providers, with a large number of Local Authorities materially increasing their charge rates, recognising that much of the cost increase in recent years has been absorbed by care providers. Providers have typically passed these rate increases onto their carers in full, adding some stability in a the sector where recruitment and retention represent a significant constraint. The care market in Scotland went further, with all Local Authorities adopting the Scottish Living Wage, a minimum pay rate of £8.25 per hour versus the statutory National Living Wage rate of £7.20.

Notwithstanding the improvements, market conditions remain challenging. The Directors note that, given these pressures, a number of competitors are withdrawing from the homecare market, which reflects the difficult conditions but could in part also provide some opportunity. Mears has increased carer pay rates significantly over the last three years, which has reduced margin but improved Mears' operating position. The Group continues to see significant new contract opportunities as well as opportunities to increase volumes of work with existing clients. Whilst there are still examples of poor commissioning practices, the Directors are confident there are sufficient new bidding opportunities to deliver against the Group's growth forecast.

As part of the annual impairment testing, management performed an extensive business planning process which involved a detailed review, on a contract-by-contract basis, of charge rates and carer pay rates. The process allowed management to appraise the performance of branches against objectives set, and further increased understanding of the main drivers behind negative carer recruitment and retention performance. Carer pay rates continue to be the principal barrier to successful recruitment and retention, but there are a number of factors around culture, working practices and recognition which impact upon maintaining a stable workforce.

The business plan identified a number of key factors, which are built in to the value-in-use calculation:

→ Mears has become increasingly selective, targeting those contracts where the pricing, longevity and spend certainty allow Mears to deliver a high quality service at sustainable margins. During the year, Mears was successful in maintaining its historical contract win rates, achieving this while securing an average charge rate over 25% higher than those rates tendered in 2015. As a result, management has made what is considered to be a conservative assumption, modelling an annual increase of 6,000 hours per week, which will be achieved through new contract bidding. This is well below the actual outcome achieved in 2016.

→ Recruitment and retention of quality care workers continue to be challenging. Retention methods implemented following the 2015 business planning process have been successful, resulting in reduced carer churn rates. However, recruitment remains challenging and this is expected to continue during the short term, whilst our whole contract portfolio aligns with our new contract bidding strategy. Mears recognises that traditional localised recruitment plays a vital role, aiding recruitment from the existing carer workforce pool. In an attempt to encourage new talent to the care at home market, Mears is utilising innovative recruitment tools to ensure breadth of coverage in attracting new care workers to the sector. Mears' internal recruitment plan anticipates modest growth during the medium and long term which, on average, equates to three additional carers per year per branch; this represents an increase of 300 carers per year on an existing workforce of 8,000 carers which is considered realistic. However, conservatively, the business plan underpinning the impairment review has stripped out this expected increase and assumes no growth as a result of improved recruitment and retention practices.

→ Mears is committed to leading the way with carer pay rates; the increase in the National Living Wage in April will further increase direct costs from 1 April 2017. Management will look to maintain a significant differential between Mears pay rates and the National Living Wage to ensure it remains the employer of choice in the homecare sector. Mears had a successful contract negotiation period following the initial introduction of the National Living Wage in April 2016, during which an average charge increase of 7% was secured. Given the Government has provided a clear indication of its intention to increase the National Living Wage to £9.00 per hour in 2020, the Directors have assumed an increase in carer pay rates of 5.0% per annum. The Directors are confident that charge rate increases will be received from clients to match the increase in the cost base. The percentage increase assumed for charge rates matches that of carer pay rates in each year throughout the business plan.

10. Goodwill continued

Care continued

Management considers that the Care value-in-use calculation is most sensitive to changes in the terminal growth rate, discount rate and EBITA margin. The table below shows the sensitivity of the headroom (£m) to simultaneous changes in the discount rate and the long-term growth rate.

	Discount rate						
Long-term growth rate	7.1%	7.5%	7.9%	8.3%	8.7%	9.1%	9.5%
1.3%	14.5	4.9	(3.6)	(11.0)	(17.7)	(23.6)	(29.0)
1.7%	23.7	12.3	3.3	(5.0)	(12.4)	(18.9)	(24.8)
2.1%	32.9	20.6	9.9	0.7	(7.5)	(14.7)	(21.0)
2.5%	43.6	29.6	17.5	**7.1**	(1.9)	(9.9)	(16.9)
2.9%	56.6	40.1	26.3	14.5	4.4	(4.5)	(12.2)
3.3%	72.3	52.7	36.6	23.1	11.6	1.7	(6.9)
3.7%	91.6	68.0	48.9	33.1	20.0	8.7	(0.9)

11. Other intangible assets

	Acquisition intangibles			Other intangibles			
	Client relationships £'000	Order book £'000	Total acquisition intangibles £'000	Development expenditure £'000	Intellectual property £'000	Total other intangibles £'000	Total intangibles £'000
Gross carrying amount							
At 1 January 2015	71,761	19,360	91,121	7,355	224	7,579	98,700
Acquired on acquisition	377	5,272	5,649	—	—	—	5,649
Additions	—	—	—	2,978	—	2,978	2,978
At 1 January 2016	72,138	24,632	96,770	10,333	224	10,557	107,327
Revisions	—	3,685	3,685	—	—	—	3,685
Additions	—	—	—	2,904	—	2,904	2,904
At 31 December 2016	**72,138**	**28,317**	**100,455**	**13,237**	**224**	**13,461**	**113,916**
Accumulated amortisation							
At 1 January 2015	41,352	17,812	59,164	3,937	224	4,161	63,325
Amortisation charge for period	7,679	3,158	10,837	1,314	—	1,314	12,151
At 1 January 2016	49,031	20,970	70,001	5,251	224	5,475	75,476
Amortisation charge for period	7,313	3,377	10,690	1,837	—	1,837	12,527
At 31 December 2016	**56,344**	**24,347**	**80,691**	**7,088**	**224**	**7,312**	**88,003**
Carrying amount							
At 31 December 2016	**15,794**	**3,970**	**19,764**	**6,149**	**—**	**6,149**	**25,913**
At 31 December 2015	23,107	3,662	26,769	5,082	—	5,082	31,851

Notes to the financial statements – Group continued
For the year ended 31 December 2016

11. Other intangible assets continued

Revisions to acquisition intangibles additions in prior years relate to liabilities not accrued at the time of the acquisition. These revisions are not considered sufficiently material to warrant restatement of the prior year balances.

Development expenditure is an internally developed intangible asset and relates largely to the development of the Group's Housing job management system, the Group's Care management system and the UK Planning Portal website. Development expenditure is amortised over its useful economic life of 5.0 years. The weighted average remaining economic life of the asset is 3.0 years (2015: 3.5 years).

Intellectual property is amortised over its useful economic life, typically 5.0 years.

Amortisation of development expenditure is included within other administrative expenses. Amortisation of acquisition intangibles is presented separately.

The value placed on the order book is based upon the cash flow projections over the contracts in place when a business is acquired. Due to uncertainties in trying to forecast revenues beyond the contract term, the Directors have taken a measure of conservatism and value contracts over the contractual term only. The value of the order book is amortised over its remaining life.

The value placed on the customer relationships is based upon the non-contractual expected cash inflows. These cash flow projections assume a customer attrition rate of 5% based upon three-year historic trends.

12. Property, plant and equipment

	Freehold property £'000	Leasehold improvements £'000	Plant and machinery £'000	Fixtures, fittings and equipment £'000	Motor vehicles £'000	Total £'000
Gross carrying amount						
At 1 January 2015	691	10,007	3,289	33,527	1,361	48,875
Acquired on acquisition	—	—	—	7,299	39	7,338
Additions	97	2,319	136	3,665	—	6,217
Disposals	—	(68)	(444)	(40)	(11)	(563)
At 1 January 2016	788	12,258	2,981	44,451	1,389	61,867
Acquired on acquisition	—	—	—	54	—	54
Additions	—	1,777	113	5,535	—	7,425
Disposals	—	(82)	(204)	(3,370)	(94)	(3,750)
At 31 December 2016	**788**	**13,953**	**2,890**	**46,670**	**1,295**	**65,596**
Depreciation						
At 1 January 2015	—	6,786	1,807	23,147	1,255	32,995
Acquired on acquisition	—	—	—	5,894	11	5,905
Provided in the year	—	996	372	3,538	57	4,963
Eliminated on disposals	—	(25)	(360)	(38)	(9)	(432)
At 1 January 2016	—	7,757	1,819	32,541	1,314	43,431
Acquired on acquisition	—	—	—	26	—	26
Provided in the year	—	1,202	310	4,040	21	5,573
Eliminated on disposals	—	(82)	(204)	(3,319)	(94)	(3,699)
At 31 December 2016	**—**	**8,877**	**1,925**	**33,288**	**1,241**	**45,331**
Carrying amount						
At 31 December 2016	**788**	**5,076**	**965**	**13,382**	**54**	**20,265**
At 31 December 2015	788	4,501	1,162	11,910	75	18,436

13. Investments

The subsidiary undertakings within the Group at 31 December 2016 are shown below:

	Proportion held	Country of registration	Nature of business
3c Asset Management Limited	100%	England and Wales	Maintenance services
Ardmore Homecare Limited	100%	England and Wales	Dormant
Careforce Group Plc	100%	England and Wales	Dormant
Careforce Services Limited	100%	England and Wales	Dormant
Coulter Estates Limited	100%	Scotland	Provision of care
Electrical Contracting Services (UK) Limited	100%	England and Wales	Dormant
Energy Insurance Services Limited	100%	England and Wales	Insurance services
Evolve Housing Limited	50%	England and Wales	Dormant
Heather Housing Limited	100%	England and Wales	Housing management services
Heatherpark Community Services Limited	100%	Scotland	Provision of care
Helcim Group Limited	100%	England and Wales	Dormant
Helcim Homes Limited	100%	England and Wales	Dormant
ILS Group Limited	100%	Scotland	Dormant
ILS Trustees Limited	100%	Scotland	Dormant
Independent Living Services (ILS) Limited	100%	Scotland	Provision of care
Insitu Care Limited	100%	England and Wales	Dormant
Jackson Lloyd Limited	100%	England and Wales	Dormant
Laidlaw Scott Limited	100%	Scotland	Dormant
Let to Birmingham Limited	100%	England and Wales	Housing management services
Manchester Working Limited	80%	England and Wales	Maintenance services
Mears 24/7 LLP	50%	England and Wales	Call centre services
Mears Building Contractors Limited	100%	England and Wales	Dormant
Mears Building Services Limited	100%	England and Wales	Dormant
Mears Care (Holdings) Limited	100%	England and Wales	Intermediate holding company
Mears Care (Northern Ireland) Limited	100%	Northern Ireland	Provision of care
Mears Care (Scotland) Limited	100%	Scotland	Provision of care
Mears Care Limited	100%	England and Wales	Provision of care
Mears Community Care Agency Limited	100%	England and Wales	Dormant
Mears Decorating Services Limited	100%	England and Wales	Dormant
Mears Energy Limited	100%	England and Wales	Dormant
Mears Estates Limited	100%	England and Wales	Grounds maintenance
Mears Facility Management Limited	100%	England and Wales	Dormant
Mears Home Improvement Limited	100%	England and Wales	Maintenance services
Mears Homecare Limited	100%	England and Wales	Provision of care
Mears Homes Limited	100%	England and Wales	Dormant
Mears Housing Management Limited	100%	England and Wales	Intermediate holding company

Notes to the financial statements – Group continued
For the year ended 31 December 2016

13. Investments continued

	Proportion held	Country of registration	Nature of business
Mears Insurance Company Limited	99.99%	Guernsey	Insurance services
Mears Learning Limited	90%	England and Wales	Training provider
Mears Lifetime Homes Limited	100%	England and Wales	Dormant
Mears Limited	100%	England and Wales	Maintenance services
Mears Mechanical & Electrical Limited	100%	England and Wales	Dormant
Mears Modular Homes Limited	100%	England and Wales	Dormant
Mears New Homes Limited	90%	England and Wales	House building
Mears Scotland (Housing) Limited	100%	Scotland	Dormant
Mears Scotland (Services) Limited	66.67%	Scotland	Maintenance services
Mears Scotland LLP	66.67%	Scotland	Maintenance services
Mears Social Housing Limited	100%	England and Wales	Dormant
Mears Wales Limited	100%	England and Wales	Dormant
Mears Window and Door Maintenance Limited	100%	England and Wales	Dormant
Morrison Facilities Services Limited	100%	Scotland	Maintenance services
Nurseplus Limited	100%	Scotland	Provision of care
O&T Developments Limited	75%	England and Wales	Housing management services
Omega Housing Limited	100%	England and Wales	Housing registered provider
Omega Lettings Limited	100%	England and Wales	Housing management services
Planning Portal Limited	75%	England and Wales	Dormant
Plexus UK (First Project) Limited	100%	England and Wales	Housing registered provider
Plexus UK (Systems) Limited	100%	England and Wales	Dormant
PortalPlanQuest Limited	75%	England and Wales	Professional services
Potton Road Management Company Limited	90%	England and Wales	Dormant
Powersave Limited	100%	England and Wales	Dormant
PS Business Services Limited	100%	Scotland	Dormant
PS Payroll Services Limited	100%	England and Wales	Dormant
R Carter and Son (Painting Contractors) Limited	100%	England and Wales	Dormant
Robert Hawkins (Contractors) Limited	100%	England and Wales	Dormant
Scion Group Limited	100%	England and Wales	Dormant
Scion Property Services Limited	100%	England and Wales	Dormant
Scion Technical Services Limited	100%	England and Wales	Maintenance services
Supporta Limited	100%	England and Wales	Dormant
Supporta Services Limited	100%	England and Wales	Dormant
Tando Homes Limited	75%	England and Wales	Housing management services
Tando Property Services Limited	75%	England and Wales	Housing management services
Terraquest Group Limited	100%	England and Wales	Dormant
Terraquest Limited	100%	England and Wales	Dormant
Terraquest Solutions Limited	100%	England and Wales	Professional services
West Haddon Management Company Limited	90%	England and Wales	Dormant
Zenon Property Services Limited	100%	England and Wales	Maintenance services

All subsidiary undertakings with the exception of Manchester Working Limited and Omega Housing Limited prepare accounts to 31 December. Manchester Working Limited prepares accounts to 31 March in line with the minority shareholder. Omega Housing Limited prepares accounts to 31 March in line with its historical accounting reference date.

13. Investments continued

At 1 January 2016 the Group reassessed the level of influence it held over Mears 24/7 LLP and concluded that the threshold for control had been met. In accordance with IFRS 10, the Group has accounted for this entity as a subsidiary from that date.

The Group includes two subsidiaries, Mears Scotland LLP and Manchester Working Limited, with material non-controlling interests. The table below sets out selected financial information in respect of those subsidiaries:

	2016 £'000	2015 £'000
Revenue and profits		
Revenue	**88,192**	84,452
Expenses and taxation	**(85,400)**	(83,473)
Profit for the year	**2,792**	979
Other comprehensive expense	**—**	—
Total comprehensive income	**2,792**	979
Profit/(loss) for the year allocated to non-controlling interests	**804**	(273)
Total comprehensive expense allocated to non-controlling interests	**—**	—
Net assets		
Non-current assets	**266**	295
Current assets	**25,333**	24,187
Current liabilities	**(27,719)**	(29,394)
Total assets less total liabilities	**(2,120)**	(4,912)
Equity shareholders' funds	**(729)**	(2,717)
Non-controlling interests	**(1,391)**	(2,195)
Total equity	**(2,120)**	(4,912)

The Group held investments in the following joint ventures at 31 December 2016:

	Proportion held	Country of registration	Nature of business
Asert LLP	50%	England and Wales	Dormant
More Homes Bromley LLP	50%	England and Wales	Housing management services
YourMK LLP	50%	England and Wales	Maintenance services

Notes to the financial statements – Group continued
For the year ended 31 December 2016

13. Investments continued

The following UK subsidiaries will take advantage of the audit exemption set out within Section 479A of the Companies Act 2006 for the year ending 31 December 2016:

	Registration number
3c Asset Management Limited	02859913
Coulter Estates Limited	SC148145
Heatherpark Community Services Limited	SC314108
ILS Group Limited	SC285635
Independent Living Services (ILS) Limited	SC184499
Let to Birmingham Limited	08757503
Mears Care (Holdings) Limited	03689426
Mears Estates Limited	03720903
Mears Home Improvement Limited	03716517
Mears Housing Management Limited	04726480
Scion Group Limited	03905442
Scion Technical Services Limited	03671450
Zenon Property Services Limited	07448134

14. Inventories

	2016 £'000	2015 £'000
Materials and consumables	**5,243**	4,979
Work in progress	**5,991**	4,042
	11,234	9,021

The Group consumed inventories totalling £695.2m during the year (2015: £649.0m). No items are being carried at fair value less costs to sell (2015: £nil).

15. Trade and other receivables

	2016 £'000	2015 £'000
Current assets:		
– trade receivables	**49,086**	47,364
– amounts recoverable on non-construction contracts	**98,405**	90,627
– prepayments and accrued income	**9,690**	8,888
Total trade and other receivables	**157,181**	146,879

Trade receivables are normally due within 30 to 60 days and do not bear any effective interest rate. All trade receivables and accrued income are subject to credit risk exposure. Housing customers are typically Local Authorities and Housing Associations where credit risk is minimal. Care customers are typically Local Authorities and NHS Trusts where credit risk is minimal.

The ageing analysis of trade receivables is as follows:

	2016 £'000	2015 £'000
Neither impaired nor past due	**46,032**	40,869
Less than three months past due but not impaired	**1,904**	4,008
More than three months past due but not impaired	**1,150**	2,487
Total trade and other receivables	**49,086**	47,364

16. Trade and other payables

	2016 £'000	2015 £'000
Trade payables	**111,490**	100,385
Accruals and deferred income	**45,571**	54,945
Social security and other taxes	**20,896**	23,669
Payments on account for non-construction contract work	**19**	140
Finance lease liabilities	**113**	386
Other creditors	**9,175**	14,578
	187,264	194,103

The fair value of trade payables has not been disclosed as, due to their short duration, management considers the carrying amounts recognised in the Balance Sheet to be a reasonable approximation of their fair value.

Included in other creditors is £5.0m (2015: £10.5m) relating to contingent consideration on acquisitions.

17. Financial assets and liabilities

	2016 £'000	2015 £'000
Current assets:		
– diesel hedge	**839**	—
Non-current assets:		
– diesel hedge	**677**	—
Total financial assets	**1,516**	—
Current liabilities:		
– interest rate swaps	**478**	510
Non-current liabilities:		
– interest rate swaps	**612**	368
Total financial liabilities	**1,090**	878

18. Long-term other liabilities

	2016 £'000	2015 £'000
Other creditors	**15,950**	15,396

Included in other creditors is £5.3m (2015: £10.4m) relating to contingent consideration on acquisitions and £6.2m relating to a forward purchase agreement in respect of 25% of Tando Property Services Limited, Tando Homes Limited and O&T Developments Limited.

Notes to the financial statements – Group continued
For the year ended 31 December 2016

19. Financial instruments
The Group uses a limited number of financial instruments comprising cash and liquid resources, borrowings, interest rate swaps and various items such as trade receivables and trade payables that arise directly from its operations. The main purpose of these financial instruments is to finance the Group's operations. The Group seeks to finance its operations through a combination of retained earnings and borrowings and investing surplus cash on deposit. The Group uses financial instruments to manage the interest rate risks arising from its operations and sources of finance but has no interests in the trade of financial instruments.

Categories of financial instruments

	2016 £'000	2015 £'000
Financial assets		
Fair value (level 2)		
Diesel hedge – ineffective	**1,516**	—
Amortised cost		
Trade receivables	**49,086**	47,364
Amounts recoverable on contracts	**98,405**	90,627
Cash at bank and in hand	**52,904**	68,612
	201,911	206,603
Financial liabilities		
Fair value (level 2)		
Interest rate swaps – effective	**(1,090)**	(878)
Fair value (level 3)		
Deferred and contingent consideration in respect of acquisitions	**(16,457)**	(20,861)
Amortised cost		
Bank borrowings and overdrafts	**(65,278)**	(67,790)
Trade payables	**(111,490)**	(100,385)
Accruals and deferred income	**(44,055)**	(54,945)
Other creditors	**(8,668)**	(9,113)
	(247,038)	(253,972)
	(45,127)	(47,369)

The IFRS 13 hierarchy level categorisation relates to the extent the fair value can be determined by reference to comparable market values. The classifications range from level 1, where instruments are quoted on an active market, through to level 3, where the assumptions used to arrive at fair value do not have comparable market data.

The fair values of diesel hedges and interest rate swaps have been calculated by a third party expert discounting estimated future cash flows on the basis of market expectations of future interest rates and the wholesale price of diesel (level 2).

The amount of contingent consideration payable is generally determined by future expected profits of the acquired businesses. The fair values of contingent consideration have been calculated by the Directors by reference to expected future income and expenditure in respect of the acquired businesses.

There have been no transfers between levels during the year.

Fair value information
The fair value of the Group's financial assets and liabilities is as disclosed above and approximates to the book value.

Financial risk management
The Group's activities expose it to a variety of financial risks: market risk (including interest rate risk and price risk); credit risk; and liquidity risk. The main risks faced by the Group relate to the availability of funds to meet business needs and the risk of credit default by customers. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

Risk management is carried out under policies and guidelines approved by the Board of Directors.

19. Financial instruments continued

Borrowing facilities

The Group's borrowing facilities are drawn on as required to manage its cash needs. Banking facilities are reviewed regularly and extended and replaced in advance of their expiry.

The Group had total borrowing facilities of £140.0m with Barclays Bank PLC and HSBC Bank plc, of which £65.0m was utilised at 31 December 2016.

The facilities comprise a committed four-year £130.0m revolving credit facility and an unsecured overdraft facility of £10.0m. The undrawn amounts at 31 December 2016 were a £65.0m revolving credit facility and an overdraft facility of £10.0m.

Interest rate risk management

The Group finances its operations through a mixture of retained profits and bank borrowings from major banking institutions at floating rates of interest based on LIBOR. The Group's exposure to interest rate fluctuations on borrowings is managed through the use of interest rate swaps; hence the fixed rate borrowings relate to floating rate loans where the interest rate has been fixed by a hedging arrangement. The fair value of interest rate exposure on financial liabilities of the Group as at 31 December 2016 was:

	Interest rate			
	Fixed £'000	Floating £'000	Zero £'000	Total £'000
Financial liabilities – 2016	**30,000**	**35,248**	**10,294**	**75,542**
Financial liabilities – 2015	57,500	10,290	20,861	88,651

The Group's policy is to accept a degree of interest rate risk, provided the effects of the various potential changes in rates remain within certain prescribed parameters.

Accordingly, at 31 December 2016 the Group had hedged the first £30.0m of the £140.0m total borrowing facilities by entering into an interest rate swap arrangement with Barclays Bank PLC. This consists of one £30.0m swap contract expiring in August 2018, with quarterly maturity, matching the underlying facility.

The maturity of the interest rate swap contracts is as follows:

	2016		2015	
	Nominal amount hedged £'000	**Average applicable interest rates %**	Nominal amount hedged £'000	Average applicable interest rates %
Within one year	**—**	**—**	27,500	1.92%
One to two years	**30,000**	**1.85%**	—	—
Two to five years	**—**	**—**	30,000	1.85%
More than five years	**—**	**—**	—	—

The Group has also entered into a further five interest rate swap arrangements with HSBC Bank PLC, three £10.0m swap contracts with a deferred start date of January 2017 expiring December 2020 at an applicable interest rate of 0.84% and two £15.0m swap contracts with a deferred start date of August 2018 expiring August 2021 at an applicable interest rate of 0.96%.

Effective interest rates

Interest rate swaps with fair value liabilities of £1.1m (2015: £0.9m) and average remaining lives of three years and seven months have been accounted for in financial liabilities.

The Group's overall average cost of debt, including effective interest rate swaps, is 2.6% as at 31 December 2016 (2015: 3.0%). Excluding these swaps the average is 1.9% (2015: 2.1%).

Cash flow hedging reserve

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Income Statement when the hedged item affects the Consolidated Income Statement.

Notes to the financial statements – Group continued
For the year ended 31 December 2016

19. Financial instruments continued

Cash flow hedging reserve continued

Movements during the year were:

	£'000
At 1 January 2015	(962)
Amounts transferred to the Consolidated Income Statement	559
Revaluations during the year	(72)
Deferred tax movement	(97)
At 1 January 2016	(572)
Amounts transferred to the Consolidated Income Statement	643
Revaluations during the year	(884)
Deferred tax movement	39
At 31 December 2016	**(774)**

At 31 December 2016 the Group had minimal exposure to movements in interest rates as the remaining interest rate risk was offset by the Group's cash and short-term deposits.

If the interest rates had been 0.5% higher or lower and all other variables were held constant, the Group's profit before taxation for the year ended 31 December 2016 and reserves would decrease or increase, respectively, by £0.2m (2015: £0.1m).

Liquidity risk management

The Group seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably.

Management monitors rolling forecasts of the Group's liquidity reserve (comprising undrawn borrowing facilities and cash and cash equivalents) on the basis of expected cash flows. This is generally carried out at a local level in the operating companies of the Group in accordance with the practice and limits set by the Group. These limits vary by location and take into account the liquidity and nature of the market in which the entity operates.

The quantum of committed borrowing facilities of the Group is regularly reviewed and is designed to exceed forecasted peak gross debt levels. For short-term working capital purposes, the Group utilises bank overdrafts as required. These facilities are regularly reviewed and are renegotiated ahead of their expiry date.

The table below shows the maturity profile of the Group's financial liabilities:

	Within 1 year £'000	1–2 years £'000	2–5 years £'000	Over 5 years £'000	Total £'000
2016					
Non-derivative financial liabilities					
Bank borrowings	**5,278**	**—**	**60,000**	**—**	**65,278**
Trade and other payables	**159,720**	**4,493**	**—**	**—**	**164,213**
Deferred and contingent consideration in respect of acquisitions	**5,000**	**11,457**	**—**	**—**	**16,457**
Derivative financial liabilities					
Interest rate swaps – effective	**478**	**375**	**226**	**11**	**1,090**
2015					
Non-derivative financial liabilities					
Bank borrowings	10,290	—	57,500	—	67,790
Trade and other payables	159,465	4,978	—	—	164,443
Deferred and contingent consideration in respect of acquisitions	10,443	10,418	—	—	20,861
Derivative financial liabilities					
Interest rate swaps – effective	510	210	158	—	878

The Group has disclosed core bank borrowings of £60.0m as due in two to five years. Whilst the amounts borrowed could be repaid each quarter, the Group's intention is to align core bank borrowings with its interest rate swaps.

19. Financial instruments continued

Credit risk management

The Group's credit risk is primarily attributable to its trade receivables, amounts recoverable on contracts and work in progress.

Trade receivables are normally due within 30 to 60 days. Trade and other receivables included in the Balance Sheet are stated net of a bad debt provision which has been estimated by management following a review of individual receivable accounts. There is no Group-wide rate of provision and provision made for debts that are overdue is based on prior default experience and known factors at the balance sheet date. Receivables are written off against the bad debt provision when management considers that the debt is no longer recoverable.

Housing customers are typically Local Authorities and Housing Associations. Care customers are typically Local Authorities and the NHS. The nature of both of these customers means that credit risk is minimal. Other trade receivables contain no specific concentration of credit risk as the amounts recognised represent a large number of receivables from various customers.

The Group continually monitors the position of major customers and incorporates this information into its credit risk controls. External credit ratings are obtained where appropriate.

Details of the ageing of trade receivables are shown in note 15.

Deferred and contingent consideration

The table below shows the movements in deferred and contingent consideration:

	Total £'000
At 1 January 2015	21,045
Increase due to new acquisitions in the year	123
Paid in respect of acquisitions	(7)
Released on reassessment	(425)
Unwinding of discounting	125
At 1 January 2016	20,861
Increase due to forward purchase agreement	6,163
Paid in respect of acquisitions	(10,019)
Released on reassessment	(548)
At 31 December 2016	**16,457**

Contingent consideration represents an estimate of future consideration likely to be payable in respect of acquisitions. Contingent consideration is discounted for the likelihood of payment and for the time value of money. Contingent consideration becomes payable based upon the profitability of acquired businesses or, in the case of one specific acquisition, the utilisation of certain timing differences in respect of corporation tax. The fair value of contingent consideration is estimated by forecasting future profits and utilising the forecast to determine the likely contingent consideration payable.

Information as to the likely timing of payments in respect of these provisions' financial liabilities is provided earlier within this note.

Notes to the financial statements – Group continued

For the year ended 31 December 2016

19. Financial instruments continued

Capital management

The Group's objectives when managing capital are:

- to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk; and
- to maintain an optimal capital structure to reduce the cost of capital.

The Group sets the amount of capital in proportion to risk. The Group manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The capital structure of the Group consists of net debt as disclosed below and equity as disclosed in the Consolidated Statement of Changes in Equity.

	2016 £'000	2015 £'000
Cash and cash equivalents is comprised as follows:		
– cash at bank and in hand	**52,904**	68,612
– bank borrowings and overdrafts	**(65,278)**	(67,790)
Cash and cash equivalents	**(12,374)**	822

20. Deferred taxation

Deferred tax is calculated on temporary differences under the liability method.

Deferred tax asset

The following deferred tax assets were recognised by the Group as at 31 December 2016:

	Pension scheme £'000	Share-based payments £'000	Cash flow hedges £'000	Tax losses £'000	Short-term temporary differences £'000	Total £'000
At 1 January 2015	1,675	1,311	257	4,358	972	8,573
Acquired on acquisition	—	—	—	—	178	178
(Debit)/credit to Consolidated Income Statement	(9)	151	—	(1,598)	759	(697)
Debit to Consolidated Statement of Changes in Equity	—	(552)	—	—	—	(552)
Debit to Consolidated Statement of Comprehensive Income	(821)	—	(97)	—	—	(918)
At 1 January 2016	845	910	160	2,760	1,909	6,584
Credit/(debit) to Consolidated Income Statement	72	65	—	(588)	(230)	(681)
Debit to Consolidated Statement of Changes in Equity	—	(635)	—	—	—	(635)
Credit/(debit) to Consolidated Statement of Comprehensive Income	596	—	(160)	—	—	436
At 31 December 2016	**1,513**	**340**	**—**	**2,172**	**1,679**	**5,704**

20. Deferred taxation continued

Deferred tax asset continued

In accordance with IFRS 2 'Share-based Payments', the Group has recognised an expense for the consumption of employee services received as consideration for share options granted. A tax deduction will not arise until the options are exercised. The tax deduction in future periods is dependent upon the Company's share price at the date of exercise. The estimated future tax deduction is based on the options' intrinsic value at the balance sheet date.

The cumulative amount credited to the Consolidated Income Statement is limited to the tax effect of the associated cumulative share-based payment expense. The excess has been credited directly to equity. This is presented in the Consolidated Statement of Comprehensive Income.

In addition to those recognised on the previous page, unused tax losses totalling £31.3m (2015: £32.9m) have not been recognised as the Directors do not consider that it is probable that they will be recovered.

The following deferred tax liabilities were recognised by the Group as at 31 December 2016:

Deferred tax liabilities

	Pension scheme £'000	Acquisition intangibles £'000	Cash flow hedges £'000	Total £'000
At 1 January 2015	3,026	6,392	—	9,418
Acquired on acquisition	—	1,054	—	1,054
Debit/(credit) to Consolidated Income Statement	124	(2,130)	—	(2,006)
Credit to Consolidated Statement of Comprehensive Income	(1,496)	—	—	(1,496)
At 1 January 2016	1,654	5,316	—	6,970
Acquired on acquisition	—	654	—	654
Debit/(credit) to Consolidated Income Statement	73	(2,066)	—	(1,993)
Debit to Consolidated Statement of Comprehensive Income	1,400	—	89	1,489
At 31 December 2016	**3,127**	**3,904**	**89**	**7,120**

Intangible assets acquired as part of a business combination are capitalised at fair value at the date of the acquisition and amortised over their useful economic lives. The UK tax regime calculates tax using the individual financial statements of the members of the Group and not the consolidated accounts. Hence, the tax base of acquisition intangible assets is £nil. The estimated tax effect of this £nil tax base is accounted for as a deferred tax liability which is released over the period of amortisation of the associated acquisition intangible asset.

Notes to the financial statements – Group continued
For the year ended 31 December 2016

21. Share capital and reserves

Classes of reserves

Share capital represents the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Share-based payment reserve represents employee remuneration which is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Statement of Comprehensive Income and recycled through the Consolidated Income Statement when the hedged item affects the Consolidated Income Statement.

The merger reserve relates to the difference between the nominal value and total consideration in respect of acquisitions, where the Company was entitled to the merger relief offered by the Companies Act.

Share capital

	2016 £'000	2015 £'000
Allotted, called up and fully paid		
At 1 January 101,938,335 (2015: 101,134,142) ordinary shares of 1p each	**1,019**	1,011
Issue of 621,464 (2015: 804,193) shares on exercise of share options	**7**	8
At 31 December 102,559,799 (2015: 101,938,335) ordinary shares of 1p each	**1,026**	1,019

During the year 621,464 (2015: 804,193) ordinary 1p shares were issued in respect of share options exercised. The difference between the nominal value of £0.007m and the total consideration of £0.2m has been credited to the share premium account.

22. Notes to the Consolidated Cash Flow Statement

The following non-operating cash flow adjustments have been made to the result for the year before tax:

	2016 £'000	2015 £'000
Depreciation	**5,573**	4,963
Loss on disposal of property, plant and equipment	**48**	45
Amortisation	**12,527**	12,151
Share-based payments	**324**	771
IAS 19 pension movement	**(770)**	(660)
Finance income	**(67)**	(158)
Finance cost	**2,803**	2,775
Total	**20,438**	19,887

23. Acquisitions

On 1 January 2016 the Group reassessed the level of influence it held over Mears 24/7 LLP and concluded that the threshold for control had been met and therefore, in accordance with IFRS 10, the Group has accounted for this entity as a subsidiary from that date.

The effect of this reassessment is an increase in trade assets of £0.8m and an increase in trade payables of £0.7m. In the period ended 31 December 2016, the acquisition contributed revenue of £3.0m and an operating profit of £0.1m.

Analysis of net outflow in respect of the purchase of the subsidiary undertakings:

	Total £'000
Cash payments in respect of prior year acquisitions	10,019

24. Pensions

Defined contribution schemes

The Group operates a defined contribution Group personal pension scheme for the benefit of certain employees. The Group contributes to personal pension schemes of certain Directors and senior employees. The Group operates a stakeholder pension plan available to all employees. During the year, the Group contributed £2.3m (2015: £2.3m) to these schemes.

IAS 19 'Employee Benefits'

The Group contributes to 35 (2015: 32) principal defined benefit schemes on behalf of a number of employees which require contributions to be made to separately administered funds.

These pension schemes are operated on behalf of Mears Limited, Mears Care Limited, Morrison Facilities Services Limited and their subsidiary undertakings. The assets of the schemes are administered by trustees in funds independent from the assets of the Group.

In certain cases, the Group will participate under Admitted Body status in the Local Government Pension Scheme. The Group will contribute for a finite period up until the end of the particular contract. The Group is required to pay regular contributions as detailed in the scheme's schedule of contributions. In some cases these contributions are capped and any excess can be recovered from the body from which the employees originally transferred. Where the Group has a contractual right to recover the costs of making good any deficit in the scheme from the Group's client, the fair value of that asset has been recognised within the Group's share of the scheme assets and disclosed on page 132. Certain judgements around the value of this asset have been made and are discussed in the judgements and estimates disclosure within the accounting policies.

The disclosures in respect of the two (2015: two) Group defined benefit schemes and the 33 (2015: 30) other defined benefit schemes in this note have been aggregated.

Costs and liabilities of the schemes are based on actuarial valuations. The latest full actuarial valuations for the schemes were updated to 31 December 2016 by qualified independent actuaries using the projected unit method.

The principal actuarial assumptions at the balance sheet date are as follows:

	2016	2015
Rate of increase of salaries – first year	**1.00%**	1.00%
Rate of increase of salaries – second year	**1.00%**	1.00%
Rate of increase of salaries – long term	**3.35%**	3.30%
Rate of increase for pensions in payment – based on CPI with a cap of 5%	**2.45%**	2.40%
Rate of increase for pensions in payment – based on RPI with a cap of 5%	**3.25%**	3.20%
Rate of increase for pensions in payment – based on CPI with a cap of 3%	**2.10%**	2.10%
Rate of increase for pensions in payment – based on RPI with a cap of 3%	**2.55%**	2.55%
Discount rate	**3.05%**	3.95%
Retail prices inflation	**3.35%**	3.30%
Consumer prices inflation	**2.45%**	2.40%
Life expectancy for a 65-year-old male	**23.9 years**	22.4 years
Life expectancy for a 65-year-old female	**26.4 years**	24.7 years

Notes to the financial statements – Group continued

For the year ended 31 December 2016

24. Pensions continued

IAS 19 'Employee Benefits' continued

The amounts recognised in the Consolidated Balance Sheet and major categories of plan assets are:

	2016			2015		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Equities – quoted	36,470	236,932	273,402	39,997	184,989	224,986
Equities – unquoted	—	20,368	20,368	—	24,047	24,047
Bonds – quoted	88,412	77,900	166,312	64,989	62,591	127,580
Bonds – unquoted	—	7,932	7,932	—	7,663	7,663
Guarantee	—	18,587	18,587	—	11,223	11,223
Property – quoted	2,004	10,201	12,205	—	6,010	6,010
Property – unquoted	—	15,884	15,884	122	16,671	16,793
Cash	22,643	34,887	57,530	11,404	39,496	50,900
Group's estimated asset share	149,529	422,691	572,220	116,512	352,690	469,202
Present value of funded scheme liabilities	(137,721)	(410,258)	(547,979)	(111,327)	(333,839)	(445,166)
Funded status	11,808	12,433	24,241	5,185	18,851	24,036
Scheme surpluses not recognised as assets	—	(15,747)	(15,747)	—	(19,988)	(19,988)
Pension asset/(liability)	11,808	(3,314)	8,494	5,185	(1,137)	4,048

The amounts recognised in the Income Statement are as follows:

	2016			2015		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Current service cost	2,062	4,370	6,432	2,143	5,521	7,664
Past service cost	—	70	70	—	39	39
Settlement and curtailment	—	169	169	—	—	—
Administration costs	196	114	310	197	119	316
Total operating charge	2,258	4,723	6,981	2,340	5,679	8,019
Net interest	(697)	(251)	(948)	(421)	(291)	(712)
Total charged to the result for the year	1,561	4,472	6,033	1,919	5,388	7,307

24. Pensions continued

IAS 19 'Employee Benefits' continued

Cumulative actuarial gains and losses recognised in equity are as follows:

	2016			2015		
	Group schemes £'000	**Other schemes £'000**	**Total £'000**	Group schemes £'000	Other schemes £'000	Total £'000
On TUPE transfer of employees	**—**	**—**	**—**	—	(223)	(223)
Return on plan assets below that recorded in net interest	**27,129**	**59,020**	**86,149**	(4,984)	(7,406)	(12,390)
Actuarial gain/(loss) arising from changes in demographic assumptions	**1,355**	**—**	**1,355**	(9,311)	(155)	(9,466)
Actuarial (loss)/gain arising from changes in financial assumptions	**(24,475)**	**(66,308)**	**(90,783)**	3,800	11,167	14,967
Actuarial gain arising from liability experience	**1,000**	**1,714**	**2,714**	5,193	819	6,012
Effects of limitation of recognisable surplus	**—**	**4,241**	**4,241**	—	(2,271)	(2,271)
Total gains and losses recognised in equity	**5,009**	**(1,333)**	**3,676**	(5,302)	1,931	(3,371)
At 1 January	**(10,738)**	**(5,602)**	**(16,340)**	(5,436)	(7,533)	(12,969)
Total at 31 December	**(5,729)**	**(6,935)**	**(12,664)**	(10,738)	(5,602)	(16,340)

Changes in the present value of the defined benefit obligations are as follows:

	2016			2015		
	Group schemes £'000	**Other schemes £'000**	**Total £'000**	Group schemes £'000	Other schemes £'000	Total £'000
Present value of obligations at 1 January	**111,327**	**333,839**	**445,166**	106,710	331,666	438,376
Current service cost	**2,062**	**4,370**	**6,432**	2,143	5,521	7,664
Past service cost	**—**	**70**	**70**	—	39	39
Scheme administration costs	**—**	**45**	**45**	—	55	55
Interest on obligations	**4,355**	**13,152**	**17,507**	4,027	12,703	16,730
Plan participants' contributions	**392**	**1,608**	**2,000**	426	2,007	2,433
Benefits paid	**(2,535)**	**(7,202)**	**(9,737)**	(2,297)	(6,663)	(8,960)
Contract transfer	**—**	**—**	**—**	—	342	342
Settlements	**—**	**(218)**	**(218)**	—	—	—
Actuarial (gain)/loss arising from changes in demographic assumptions	**(1,355)**	**—**	**(1,355)**	9,311	155	9,466
Actuarial loss/(gain) arising from changes in financial assumptions	**24,475**	**66,308**	**90,783**	(3,800)	(11,167)	(14,967)
Actuarial gain arising from liability experience	**(1,000)**	**(1,714)**	**(2,714)**	(5,193)	(819)	(6,012)
Present value of obligations at 31 December	**137,721**	**410,258**	**547,979**	111,327	333,839	445,166

Notes to the financial statements – Group continued
For the year ended 31 December 2016

24. Pensions continued
IAS 19 'Employee Benefits' continued

Changes in the fair value of the plan assets are as follows:

	2016			2015		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Fair value of plan assets at 1 January	116,512	352,690	469,202	115,818	347,034	462,852
Expected return on plan assets	5,052	13,403	18,455	4,448	12,994	17,442
Employer's contributions	3,175	3,628	6,803	3,298	4,669	7,967
Plan participants' contributions	392	1,608	2,000	426	2,007	2,433
Benefits paid	(2,535)	(7,202)	(9,737)	(2,297)	(6,663)	(8,960)
Scheme administration costs	(196)	(69)	(265)	(197)	(64)	(261)
Contract transfer	—	—	—	—	119	119
Settlements	—	(387)	(387)	—	—	—
Return on plan assets above/(below) that recorded in net interest	27,129	59,020	86,149	(4,984)	(7,406)	(12,390)
Fair value of plan assets at 31 December	149,529	422,691	572,220	116,512	352,690	469,202

History of experience gains and losses is as follows:

	Group schemes				
	2016 £'000	2015 £'000	2014 £'000	2013 £'000	2012 £'000
Fair value of scheme assets	149,529	116,512	115,818	98,910	89,737
Net present value of defined benefit obligations	(137,721)	(111,327)	(106,710)	(88,195)	(79,336)
Net surplus	11,808	5,185	9,108	10,715	10,401
Experience adjustments arising on scheme assets					
Amount	27,129	(4,984)	10,624	3,796	695
Percentage of scheme assets	18.1%	(4.3%)	9.2%	3.8%	0.8%
Experience adjustments arising on scheme liabilities					
Amount	(1,000)	(5,193)	(910)	(932)	—
Percentage of scheme liabilities	(0.7%)	(4.7%)	(0.9%)	(1.1%)	—

	Other schemes				
	2016 £'000	2015 £'000	2014 £'000	2013 £'000	2012 £'000
Fair value of scheme assets	422,691	352,690	347,034	324,723	286,328
Net present value of defined benefit obligations	(410,258)	(333,839)	(331,666)	(295,641)	(260,689)
Net surplus	12,433	18,851	15,368	29,082	25,639
Asset value not recognised as surplus	(15,747)	(19,988)	(17,717)	(31,173)	(27,758)
Net deficit	(3,314)	(1,137)	(2,349)	(2,091)	(2,119)
Experience adjustments arising on scheme assets					
Amount	59,020	(7,406)	22,125	25,805	3,991
Percentage of scheme assets	14.0%	(2.1%)	6.4%	7.9%	1.4%
Experience adjustments arising on scheme liabilities					
Amount	(1,714)	(819)	(9,828)	(518)	143
Percentage of scheme liabilities	(0.4%)	(0.2%)	(3.0%)	(0.2%)	0.1%

24. Pensions continued

IAS 19 'Employee Benefits' continued

Funding arrangements are agreed for each of the Group's defined benefit pension schemes with their respective trustees. The employer's contributions expected to be paid during the financial year ending 31 December 2017 amount to £6.6m.

Each of the schemes manage risks through a variety of methods and strategies to limit downside in falls in equity markets, movement in inflation and movement in interest rates.

The Group's defined benefit obligation is sensitive to changes in certain key assumptions. The sensitivity analysis below shows how a reasonably possible increase or decrease in a particular assumption, in isolation, results in an increase or decrease in the present value of the defined benefit obligation as at 31 December 2016.

	Decrease £'000	Increase £'000
Rate of inflation – decrease/increase by 0.1%	(2,362)	2,902
Rate of increase in salaries – decrease/increase by 0.1%	(274)	321
Discount rate – decrease/increase by 0.1%	4,509	(3,869)
Life expectancy – decrease/increase by 1 year	(5,871)	(6,631)

25. Operating lease commitments

Non-cancellable operating lease rentals payable were as follows:

	Land and buildings		Other	
	2016 £'000	2015 £'000	**2016 £'000**	2015 £'000
Payable				
Within one year	**44,917**	2,641	**15,456**	11,557
Between two and five years	**22,404**	6,864	**28,249**	17,136
After more than five years	**11,541**	3,090	**—**	—
	78,862	12,595	**43,705**	28,693

Operating lease payments represent rentals payable by the Group for certain of its office properties and housing management residential properties, the hire of vehicles and the hire of other equipment. These leases have durations ranging from one to 15 years. No arrangements have been entered into in respect of contingent rental payments.

26. Capital commitments

The acquisition of Omega included an interest in 50% of the share capital of three jointly owned companies. During 2015 the Group increased its holding to 75% and agreed a forward purchase agreement to acquire the remaining 25% for consideration of £6.1m in January 2018.

The Group had no capital commitments at 31 December 2016 or at 31 December 2015.

27. Contingent liabilities

The Group has guaranteed that it will complete certain Group contracts that it has commenced. At 31 December 2016 these guarantees amounted to £25.4m (2015: £22.4m).

As detailed in note 7, the Group has a facility in place guaranteeing the performance of a number of M&E projects in Haydon Mechanical and Electrical Company LLC. The guarantees will fall away as the underlying contracts are completed and the associated guarantees released. As at 31 December 2016, guarantees amounted to £13.7m (2015: £15.4m).

The Group had no other contingent liabilities at 31 December 2016 or at 31 December 2015.

Notes to the financial statements – Group continued
For the year ended 31 December 2016

28. Related party transactions
Identity of related parties
The Group has a related party relationship with its pension schemes, its subsidiaries and its Directors.

Pension schemes
Details of contributions to pension schemes are set out in note 24 to the financial statements.

Subsidiaries
The Group has a central treasury arrangement in which all subsidiaries participate. The Directors do not consider it meaningful to set out details of transfers made in respect of this treasury arrangement between companies, nor do they consider it meaningful to set out details of interest or dividend payments made within the Group.

Transactions with key management personnel
The Group has identified key management personnel as the Directors of Mears Group PLC.

Key management personnel held the following percentage of voting shares in Mears Group PLC:

	2016 %	2015 %
Directors	**0.4**	0.4

Key management personnel's compensation is as follows:

	2016 £'000	2015 £'000
Salaries including social security costs	**1,762**	1,513
Contributions to defined contribution pension schemes	**195**	195
Share-based payments	**150**	150
	2,107	1,858

Further details of Directors' remuneration are disclosed within the Remuneration Report.

Transactions with other related parties
During the year the Group made a loan to YourMK LLP, an entity in which the Group is a 50% member, totalling £0.2m (2015: £nil). At 31 December 2016, the Group was owed £0.2m (2015: £nil) by YourMK LLP.

Principal accounting policies – Company

Statement of compliance

Mears Group PLC is a public limited company incorporated in England and Wales. Its registered office is 1390 Montpellier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH.

Basis of preparation

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards, including FRS 102 and the Companies Act 2006. The financial statements have been prepared on the historical cost basis except for the modification to a fair value basis for certain financial instruments specified in the accounting policies below. The financial statements are presented in Sterling.

The Company has taken advantage of the exemption in Section 408 of the Companies Act from disclosing its individual profit and loss account.

The Company has taken advantage of the reduced disclosures for subsidiaries and the ultimate parent provided for in FRS 102 and has therefore not provided a Statement of Cash Flows or certain disclosures in respect of share-based payments.

The principal accounting policies of the Company are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated.

Goodwill

Goodwill representing the reallocation of amounts previously classed as investments upon the hive-across of trade and assets is capitalised and amortised on a straight-line basis over its estimated useful economic life.

Share-based employee remuneration

All share-based payment arrangements that were granted after 7 November 2002 are recognised in the financial statements.

The Group operates equity-settled and cash-settled share-based remuneration plans for its employees. All employee services received in exchange for the grant of any share-based remuneration are measured at their fair values. These are indirectly determined by reference to the fair value of the share options awarded. Their value is determined at the date of grant and is not subsequently remeasured unless the conditions on which the award was granted are modified. The fair value at the date of the grant is calculated using the Black Scholes option pricing model and the cost is recognised on a straight-line basis over the vesting period. Adjustments are made to reflect expected and actual forfeitures during the vesting period.

Share-based remuneration in respect of employees of the Company is ultimately recognised as an expense in the profit and loss account. For equity-settled share-based payments there is a corresponding credit to the share-based payment reserve; for cash-settled share-based payments the Company recognises a liability at the balance sheet date. The Company operates share-based remuneration plans for employees of subsidiaries using the Company's equity instruments. The fair value of the compensation given in respect of these share-based compensation plans less payments received from subsidiaries in respect of those share-based payments is recognised as a capital contribution.

Upon exercise of share options, the proceeds received net of any directly attributable transaction costs up to the nominal value of the shares issued are allocated to share capital with any excess being recorded as share premium.

Deferred taxation

Deferred tax is recognised on all timing differences where the transactions or events that give the Company an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred by the balance sheet date. Deferred tax assets are recognised where it is more likely than not that they will be recovered. Deferred tax is measured using rates of tax and laws that have been enacted or substantively enacted by the balance sheet date.

Principal accounting policies – Company continued

Retirement benefits

i) Defined contribution pension scheme

The pension costs charged against profits are the contributions payable to individual policies in respect of the accounting period.

ii) Defined benefit pensions

The Company contributes to defined benefit schemes which require contributions to be made to separately administered funds.

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligations for any benefits from this kind of pension plan remain with the Group, even if plan assets for funding the defined benefit plan have been set aside.

Scheme liabilities are measured using the projected unit funding method, applying the principal actuarial assumptions at the balance sheet date. Assets are measured at market value. The asset that is recognised is restricted to the amount by which the service cost is expected, over the lifetime of the scheme, to exceed funding contributions payable in respect of accruing benefits.

Actuarial gains and losses are taken to the Statement of Comprehensive Income as incurred. For this purpose, actuarial gains and losses comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

Other movements in the net surplus or deficit are recognised in the profit and loss account, including the current service cost, any past service cost and the effect of curtailments or settlements. The interest costs less the expected return on assets are also charged to the Income Statement. The amount charged to the Income Statement in respect of these plans is included within operating costs.

The Company's contributions to the schemes are paid in accordance with the rules of the schemes and the recommendations of the actuary.

Financial instruments

Financial assets and liabilities are recognised in the Balance Sheet when the Company becomes party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Company are as follows:

Financial assets

Basic financial assets, including trade and other receivables, amounts due to Group companies and cash and cash equivalents, are initially recognised at transaction price, unless the arrangement constitutes a financing transaction, where the transaction is measured at the present value of the future receipts discounted at a market rate of interest.

Such assets are subsequently carried at amortised cost using the effective interest method.

At the end of each reporting period financial assets measured at amortised cost are assessed for objective evidence of impairment. If an asset is impaired the impairment loss is the difference between the carrying amount and the present value of the estimated cash flows discounted at the asset's original effective interest rate. The impairment loss is recognised in profit or loss.

Financial assets are derecognised when (a) the contractual rights to the cash flows from the asset expire or are settled, or (b) substantially all the risks and rewards of the ownership of the asset are transferred to another party, or (c) despite having retained some significant risks and rewards of ownership, control of the asset has been transferred to another party which has the practical ability to unilaterally sell the asset to an unrelated third party without imposing additional restrictions.

Cash and cash equivalents include cash at bank and in hand and bank deposits available with no notice or less than three months' notice from inception that are subject to an insignificant risk of changes in value. Bank overdrafts are presented as current liabilities to the extent that there is no right of offset with cash balances.

Financial instruments continued

Financial liabilities

Basic financial liabilities, including trade and other payables, and amounts payable to Group companies that are classified as debt, are initially recognised at transaction price, unless the arrangement constitutes a financing transaction, where the debt instrument is measured at the present value of the future receipts discounted at a market rate of interest.

Bank borrowings are non-basic financial liabilities and are initially recognised at fair value, being the present value of future payments discounted at a market rate of interest. Bank borrowings are remeasured at fair value.

Derivatives, including interest rate swaps, are not basic financial instruments.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Changes in the fair value of derivatives are recognised in profit or loss in finance costs or finance income as appropriate, unless they are included in a hedging arrangement.

Financial liabilities are derecognised when the liability is extinguished, that is when the contractual obligation is discharged or cancelled or expires.

Offsetting

Financial assets and liabilities are offset and the net amounts presented in the financial statements when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

Hedge accounting for interest rate swaps

The Company applies hedge accounting for transactions entered into to manage the cash flow exposures of borrowings. Interest rate swaps are held to manage the interest rate exposures and are designated as cash flow hedges of floating rate borrowings.

Changes in the fair values of derivatives designated as cash flow hedges, and which are effective, are recognised directly in equity. Any ineffectiveness in the hedging relationship (being the excess of the cumulative change in fair value of the hedging instrument since inception of the hedge over the cumulative change in the fair value of the hedged item since inception of the hedge) is recognised in the Income Statement.

The gain or loss recognised in other comprehensive income is reclassified to the Income Statement when the hedge relationship ends. Hedge accounting is discontinued when the hedging instrument expires or no longer meets the hedging criteria, the forecast transaction is no longer highly probable, the hedged debt instrument is derecognised or the hedging instrument is terminated.

Parent Company balance sheet

As at 31 December 2016

	Note	2016 £'000	2015 £'000
Non-current assets			
Intangible assets: goodwill	5	**—**	—
Investments	6	**58,467**	58,467
		58,467	58,467
Current assets			
Debtors	7	**139,155**	135,827
Cash at bank and in hand		**—**	—
		139,155	135,827
Creditors: amounts falling due within one year	8	**(27,021)**	(32,879)
Net current assets		**112,134**	102,948
Total assets less current liabilities		**170,601**	161,415
Creditors: amounts falling due after more than one year	9	**(60,686)**	(57,961)
Provisions for liabilities			
Pension liability	14	**(4,184)**	(3,087)
		105,731	100,367
Capital and reserves			
Called up share capital	11	**1,026**	1,019
Share premium account		**58,320**	58,124
Share-based payment reserve		**1,975**	1,651
Hedging reserve		**(774)**	(572)
Profit and loss account		**45,184**	40,145
Shareholders' funds		**105,731**	100,367

The Parent Company has taken advantage of Section 408 of the Companies Act 2006 and has not included its own profit and loss account in these financial statements. The Group profit for the year includes a profit of £18.2m (2015: £12.9m) which is dealt with in the financial statements of the Company.

The financial statements were approved by the Board of Directors on 27 March 2017.

D J Miles
Director

A C M Smith
Director

Company number: 03232863

The accompanying accounting policies and notes form an integral part of these financial statements.

Parent Company statement of changes in equity
For the year ended 31 December 2016

	Share capital £'000	Share premium account £'000	Share-based payment reserve £'000	Hedging reserve £'000	Retained earnings £'000	Total £'000
At 1 January 2015	1,011	56,714	1,653	(962)	35,213	93,629
Net result for the year	—	—	—	—	12,862	12,862
Other comprehensive income	—	—	—	390	1,742	2,132
Total comprehensive income for the year	—	—	—	390	14,604	14,994
Issue of shares	8	1,410	—	—	—	1,418
Share option charges	—	—	771	—	—	771
Exercise of share options	—	—	(773)	—	773	—
Dividends	—	—	—	—	(10,445)	(10,445)
At 1 January 2016	1,019	58,124	1,651	(572)	40,145	100,367
Net result for the year	—	—	—	—	18,238	18,238
Other comprehensive expense	—	—	—	(202)	(1,716)	(1,918)
Total comprehensive (expense)/income for the year	—	—	—	(202)	16,522	16,320
Issue of shares	7	196	—	—	—	203
Share option charges	—	—	324	—	—	324
Dividends	—	—	—	—	(11,483)	(11,483)
At 31 December 2016	**1,026**	**58,320**	**1,975**	**(774)**	**45,184**	**105,731**

The accompanying accounting policies and notes form an integral part of these financial statements.

Notes to the financial statements – Company

For the year ended 31 December 2016

1. Result for the financial year

This result for the year is stated after charging auditor's remuneration of £60,000 relating to audit services.

2. Directors and employees

Employee benefits expense

All staff costs relate to Directors. Staff costs during the year were as follows:

	2016 £'000	2015 £'000
Wages and salaries	**1,334**	1,323
Social security costs	**428**	190
Other pension costs	**182**	195
	1,944	1,708

The average number of employees of the Company during the year was:

	2016 Number	2015 Number
Management	**9**	8

3. Share-based employee remuneration

As at 31 December 2016 the Group maintained seven share-based payment schemes for employee remuneration. The details of each scheme are included within note 5 to the consolidated financial statements.

All share-based employee remuneration will be settled in equity. The Group has no legal obligation to repurchase or settle the options.

In total, £0.2m of employee remuneration expense has been included in the Company's profit and loss account for 2016 (2015: £0.2m), which gave rise to additional paid-in capital.

4. Dividends

The following dividends were paid on ordinary shares in the year:

	2016 £'000	2015 £'000
Final 2015 dividend of 7.90p (2015: final 2014 dividend of 7.15p) per share	**8,099**	7,286
Interim 2016 dividend of 3.30p (2015: interim 2015 dividend of 3.10p) per share	**3,384**	3,159
	11,483	10,445

The proposed final 2016 dividend of 8.40p per share has not been included within the financial statements as no obligation existed at 31 December 2016.

5. Goodwill

	Goodwill £'000
Cost	
At 1 January 2016 and at 31 December 2016	6,196
Amortisation	
At 1 January 2016 and at 31 December 2016	6,196
Net book value	
At 31 December 2016	**—**
At 31 December 2015	—

6. Fixed asset investments

	Investment in subsidiary undertakings £'000
Cost	
At 1 January 2016 and at 31 December 2016	58,467

Details of the subsidiary undertakings of the Company are shown in note 13 to the consolidated financial statements.

7. Debtors

	2016 £'000	2015 £'000
Amounts owed by Group undertakings	**135,620**	131,951
Prepayments and accrued income	**1,073**	810
Other receivables	**—**	2,000
Corporation tax asset	**—**	12
Deferred tax asset	**946**	1,054
Diesel hedge	**1,516**	—
	139,155	135,827

The deferred tax asset above of £0.9m (2015: £1.1m) is due after more than one year. The recoverability of the deferred tax asset is dependent on future taxable profits. The Company expects to realise sufficient profits to enable the deferred tax asset to be recovered.

8. Creditors: amounts falling due within one year

	2016 £'000	2015 £'000
Bank loan	**5,000**	10,000
Bank overdraft	**19,146**	20,801
Interest rate swaps	**478**	510
Accruals	**1,623**	1,548
Corporation tax	**708**	—
Other payables	**66**	20
	27,021	32,879

9. Creditors: amounts falling due in more than one year

	2016 £'000	2015 £'000
Bank borrowings	**60,000**	57,500
Contingent consideration	**74**	93
Interest rate swaps	**612**	368
	60,686	57,961

The Company has disclosed core bank borrowings of £60.0m as due in two to five years. Whilst the amounts borrowed could be repaid each quarter, the Company's intention is to align core bank borrowings with its interest rate swaps.

Included in other creditors is £0.1m (2015: £0.1m) relating to deferred consideration on acquisitions.

Notes to the financial statements – Company continued
For the year ended 31 December 2016

10. Financial instruments
The Company has the following financial instruments:

	2016 £'000	2015 £'000
Financial assets that are debt instruments measured at amortised cost:		
– other receivables	—	2,000
Financial assets that are measured at fair value through profit and loss:		
– diesel hedge	1,516	—
Financial liabilities that are measured at fair value through profit and loss:		
– bank borrowings	(65,000)	(67,500)
Financial liabilities that are measured at fair value through other comprehensive income:		
– interest rate swaps	(1,090)	(878)
Financial liabilities that are measured at amortised cost:		
– accruals	(1,623)	(1,548)
– other payables	(66)	(20)
	(1,689)	(1,568)
Other financial liabilities that are measured at fair value:		
– contingent consideration	(74)	(93)

There have been no changes during the period or cumulatively in the fair value of bank borrowings attributable to changes in the credit risk of the instrument. The change attributable to changes in own credit risk is not material due to the short life of individual drawdowns within bank borrowings. The difference between the carrying amount and the amount expected to be paid at maturity is not material due to the short life of individual drawdowns within bank borrowings.

The Company pays a margin over and above LIBOR on bank borrowings. The margin is based on the ratio of Group consolidated net borrowings to Group consolidated adjusted EBITDA and could have varied between 1.2% and 2.2% during the year.

The Company has entered into interest rate swaps to receive interest at LIBOR and pay interest at fixed rates. At 31 December 2016, this consists of one £30.0m swap contract expiring in August 2018 with a fixed interest rate of 1.85%. The swap has quarterly maturity matching the underlying debt. The Company has also entered into three commodity price hedges in respect of the wholesale price of diesel covering the purchase of 6m litres of diesel per annum.

These instruments are used to mitigate the Company's exposure to any interest rate movements and diesel price movements. The fair value of the interest rate swaps is a liability of £1.1m (2015: £0.9m). The fair value of the commodity price hedge is an asset of £1.5m (2015: £nil).

During 2016, a hedging loss of £0.9m (2015: £0.07m) was recognised in other comprehensive income for changes in the fair value of the interest rate swap and £0.6m (2015: £0.6m) was reclassified from the hedge reserve to profit and loss.

The Company has also entered into a further five interest rate swap arrangements with HSBC Bank PLC, three £10.0m swap contracts with a deferred start date of January 2017 expiring December 2020 at an applicable interest rate of 0.84% and two £15.0m swap contracts with a deferred start date of August 2018 expiring August 2021 at an applicable interest rate of 0.96%.

The Company seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably.

Management monitors rolling forecasts of the Group and Company's liquidity reserve (comprising undrawn borrowing facilities and cash and cash equivalents) on the basis of expected cash flows. The quantum of committed borrowing facilities of the Group and Company is regularly reviewed and is designed to exceed forecasted peak gross debt levels. For short-term working capital purposes, the Group and Company utilise bank overdrafts as required. These facilities are regularly reviewed and are renegotiated ahead of their expiry date.

11. Share capital and reserves

	2016 £'000	2015 £'000
Allotted, called up and fully paid		
At 1 January 101,938,335 (2015: 101,134,142) ordinary shares of 1p each	**1,019**	1,011
Issue of 621,464 (2015: 804,193) shares on exercise of share options	**7**	8
At 31 December 102,559,799 (2015: 101,938,335) ordinary shares of 1p each	**1,026**	1,019

During the year, 621,464 (2015: 804,193) ordinary 1p shares were issued in respect of share options exercised. The difference between the nominal value of £0.007m and the total consideration of £0.2m has been credited to the share premium account.

Classes of reserves

Share capital represents the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Share-based payment reserve represents employee remuneration which is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, are accounted for through the Statement of Comprehensive Income and recycled through the Income Statement when the hedged item affects the Income Statement.

12. Capital commitments

The Company had no capital commitments at 31 December 2016 or at 31 December 2015.

13. Contingent liabilities

The Company has guaranteed that it will complete certain Group contracts that its subsidiaries have commenced. At 31 December 2016 these guarantees amounted to £25.4m (2015: £22.4m).

As detailed in note 7 of the Group financial statements, the Company has a facility in place guaranteeing the performance of a number of M&E projects in Haydon Mechanical and Electrical Company LLC. The guarantees will fall away as the underlying contracts are completed and the associated guarantees released. As at 31 December 2016, guarantees amounted to £13.7m (2015: £15.4m).

The Company had no other contingent liabilities at 31 December 2016 or at 31 December 2015.

14. Pensions

Defined contribution schemes

The Company contributes to personal pension schemes of the Directors.

Defined benefit scheme

The Company operates a defined benefit pension scheme for the benefit of certain employees of its subsidiary companies. The assets of the schemes are administered by trustees in a fund independent from the assets of the Company.

Costs and liabilities of the scheme are based on actuarial valuations. The actuarial valuations were reviewed and updated to 31 December 2016 by a qualified independent actuary using the projected unit method.

The principal actuarial assumptions at the balance sheet date are as follows:

	2016	2015
Rate of increase of salaries – first year	**1.00%**	1.00%
Rate of increase of salaries – second year	**1.00%**	1.00%
Rate of increase of salaries – long term	**3.35%**	3.30%
Rate of increase for pensions in payment – based on RPI with a cap of 5%	**3.25%**	3.20%
Rate of increase for pensions in payment – based on RPI with a cap of 3%	**2.55%**	2.55%
Discount rate	**3.05%**	3.95%
Retail prices inflation	**3.35%**	3.30%
Consumer prices inflation	**2.45%**	2.40%
Life expectancy for a 65-year-old male	**22.4 years**	22.6 years
Life expectancy for a 65-year-old female	**24.5 years**	24.7 years

Notes to the financial statements – Company continued

For the year ended 31 December 2016

14. Pensions continued

Defined benefit scheme continued

The amounts recognised in the Parent Company Balance Sheet and major categories of plan assets as a percentage of total plan assets are:

	2016 £'000	2015 £'000
Equities	**5,004**	11,341
Bonds	**9,470**	2,790
Cash	**2,679**	705
Group's estimated asset share	**17,153**	14,836
Present value of funded scheme liabilities	**(21,337)**	(17,923)
Funded status	**(4,184)**	(3,087)
Related deferred tax asset	**795**	617
Pension liability	**(3,389)**	(2,470)

The amounts recognised in the profit and loss account are as follows:

	2016 £'000	2015 £'000
Current service cost	**67**	140
Administration cost	**(42)**	42
Past service cost	**—**	—
Total operating charge	**25**	182
Net interest	**101**	183
Total charged to the result for the year	**126**	365

Changes in the present value of the defined benefit obligations are as follows:

	2016 £'000	2015 £'000
Present value of obligations at 1 January	**17,923**	19,771
Current service cost	**67**	140
Past service cost	**—**	—
Interest on obligations	**700**	747
Plan participants' contributions	**12**	27
Benefits paid	**(412)**	(451)
Actuarial gain arising from changes in demographic assumptions	**(232)**	(389)
Actuarial gain/(loss) arising from changes in financial assumptions	**3,509**	(656)
Actuarial loss arising from liability experience	**(230)**	(1,266)
Present value of obligations at 31 December	**21,337**	17,923

14. Pensions continued

Defined benefit scheme continued

Changes in the fair value of the plan assets are as follows:

	2016 £'000	2015 £'000
Fair value of plan assets at 1 January	**14,836**	13,748
Expected return on plan assets	**599**	564
Administration costs	**42**	(42)
Employer's contributions	**1,057**	1,124
Plan participants' contributions	**12**	27
Benefits paid	**(412)**	(451)
Return on plan assets above that recorded in net interest	**1,019**	(134)
Fair value of plan assets at 31 December	**17,153**	14,836

The movements in the net pension liability and the amount recognised in the Balance Sheet are as follows:

	2016 £'000	2015 £'000
Deficit in schemes at 1 January	**(3,087)**	(6,023)
Current service cost	**(67)**	(140)
Past service cost	**—**	—
Administration costs	**42**	(42)
Contributions	**1,057**	1,124
Other finance income	**(101)**	(183)
Actuarial gain arising from changes in demographic assumptions	**232**	389
Actuarial (loss)/gain arising from changes in financial assumptions	**(3,509)**	656
Actuarial loss arising from liability experience	**230**	1,266
Return on plan assets above that recorded in net interest	**1,019**	(134)
Deficit in schemes at 31 December	**(4,184)**	(3,087)

The employer's contributions expected to be paid during the financial year ending 31 December 2017 amount to £1.1m.

15. Related party transactions

Identity of related parties

The Group has a related party relationship with its pension schemes, its subsidiaries and its Directors.

Pension schemes

Details of contributions to pension schemes are set out in note 14 to the financial statements.

Subsidiaries

The Group has a central treasury arrangement in which all subsidiaries participate. The Directors do not consider it meaningful to set out details of transfers made in respect of this treasury arrangement between companies, nor do they consider it meaningful to set out details of interest or dividend payments made within the Group.

Transactions with key management personnel

The Group has identified key management personnel as the Directors of Mears Group PLC. Details of transactions are disclosed in note 28 to the consolidated financial statements.

Five-year record (unaudited)

Income Statement

	2016 £'000	2015 £'000	2014 £'000	2013 £'000	2012 £'000
Revenue by business segment					
Housing	**787,530**	735,129	714,733	742,479	504,686
Care	**152,570**	146,010	124,007	123,095	112,550
Continuing activities	**940,100**	881,139	838,740	865,574	617,236
Discontinued activities	**—**	—	—	32,632	62,289
Total sales revenue	**940,100**	881,139	834,740	898,206	679,525
Gross profit	**244,894**	232,132	225,041	227,960	184,305
Operating profit before acquisition intangible amortisation and exceptional costs	**41,850**	38,662	42,995	38,392	31,161
Exceptional items	**—**	—	—	(25,493)	(2,877)
Operating profit	**31,160**	27,825	30,667	2,039	20,323
Profit for the year before tax	**29,372**	25,920	29,677	277	18,199
PBT before acquisition intangible amortisation and exceptional costs	**40,062**	36,757	42,005	36,630	29,037
Earnings per share					
Basic	**23.54p**	20.31p	25.03p	(1.21)p	19.61p
Diluted	**23.41p**	20.10p	24.65p	(1.17)p	18.85p
Normalised	**30.36p**	27.94p	32.20p	28.06p	25.60p
Dividends per share	**11.70p**	11.00p	10.00p	8.80p	8.00p

Balance Sheet

	2016 £'000	2015 £'000	2014 £'000	2013 £'000	2012 £'000
Non-current assets	**262,263**	258,201	268,818	233,960	225,964
Current assets	**222,158**	237,767	217,718	241,697	249,719
Current liabilities	**(194,567)**	(219,882)	(190,040)	(222,506)	(231,934)
Non-current liabilities	**(91,180)**	(84,458)	(102,034)	(72,850)	(74,931)
Total equity	**198,674**	191,628	194,462	180,301	168,818
Cash and cash equivalents, end of year	**(12,374)**	822	3,834	(448)	(12,384)

Shareholder and corporate information

Financial calendar

Annual General Meeting

7 June 2017

Record date for final dividend

16 June 2017

Dividend warrants posted to shareholders

6 July 2017

Interim results announced

15 August 2017

Registered office

1390 Montpellier Court
Gloucester Business Park
Brockworth
Gloucester GL3 4AH

Tel: 01452 634600
www.mearsgroup.co.uk

Company registration number

3232863

Company Secretary

Ben Westran

1390 Montpellier Court
Gloucester Business Park
Brockworth
Gloucester GL3 4AH

Tel: 01452 634600

Bankers

Barclays Bank PLC

Wales and South West
Corporate Banking
4th Floor, Bridgewater House
Counterslip
Finzels Reach
Bristol BS1 6BX

Tel: 0800 285 1152

HSBC Bank plc

West & Wales
Corporate Banking Centre
3 Rivergate
Temple Quay
Bristol BS1 6ER

Tel: 0845 583 9796

Solicitors

BPE

St James' House
St James' Square
Cheltenham GL50 3PR

Tel: 01242 224433

Mishcon de Reya LLP

Africa House
70 Kingsway
London WC2B 6AH

Tel: 020 3321 7000

Travers Smith

10 Snow Hill
London EC1A 2AL

Tel: 020 7295 3000

Auditor

Grant Thornton UK LLP

Registered Auditor
Chartered Accountants
Hartwell House
55–61 Victoria Street
Bristol BS1 6FT

Tel: 0117 305 7600

Financial adviser

Investec Bank PLC

2 Gresham Street
London EC2V 7QP

Tel: 020 7597 2000

Registrar

Neville Registrars Ltd

Neville House
18 Laurel Lane
Halesowen
West Midlands B63 3DA

Tel: 0121 585 1131

Joint corporate brokers

Liberum Capital Limited

Ropemaker Place, Level 12
25 Ropemaker Street
London EC2Y 9LY

Tel: 020 7418 8900

Peel Hunt

Moor House
20 London Wall
London EC2Y 5ET

Tel: 020 7418 8900

Investor relations

Buchanan

107 Cheapside
London EC2V 6DN

Tel: 020 7466 5000

Internet

The Group operates a website which can be found at www.mearsgroup.co.uk. This site is regularly updated to provide information about the Group. In particular all of the Group's press releases and announcements can be found on the site.

Registrar

Any enquiries concerning your shareholding should be addressed to the Company's registrar. The registrar should be notified promptly of any change in a shareholder's address or other details.

Investor relations

Requests for further copies of the Annual Report and Accounts, or other investor relations enquiries, should be addressed to the registered office.

FSC www.fsc.org RECYCLED Paper made from recycled material FSC® C022913

CERTIFIED CARBON NEUTRAL® publication CarbonNeutral.com

The Group's commitment to environmental issues is reflected in this Annual Report which has been printed on Cocoon Offset which is made from 100% post-consumer fibres, FSC® certified and PCF (Process Chlorine Free). Printed in the UK by Pureprint Group using their environmental printing technology, and vegetable inks were used throughout. Pureprint Group is a CarbonNeutral® company. Both manufacturing mill and the printer are registered to the Environmental Management System ISO14001 and are Forest Stewardship Council® (FSC) chain-of-custody certified.

consultancy, design and production by designportfolio
design-portfolio.co.uk @WeAre_DP
Design Portfolio is committed to planting trees for every corporate communications project, in association with Trees for Cities.

Mears Group PLC
1390 Montpellier Court
Gloucester Business Park
Brockworth
Gloucester GL3 4AH

Tel: 01452 634 600
www.mearsgroup.co.uk