


2005/06 ANNUAL
REPORT & ACCOUNTS

ABRO 2005/06 ANNUAL REPORT & ACCOUNTS

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ABRO | Company Information

ABRO is a defence engineering business providing a range of customers with Fleet Management Services across a broad spectrum of vehicle and equipment types.

ABRO is a defence engineering business providing a range of customers with Fleet Management Services across a broad spectrum of vehicle and equipment types. These include:

- Military armoured vehicles
- Military non-armoured vehicles and plant
- Commercial and specialist vehicles
- Fleet management
- Electronics
- Optronics
- Test and measurement
- Small arms
- Major assemblies

With the largest service range of any equivalent company, and successful partnerships with major organisations, ABRO has provided an unrivalled repair, maintenance and re-manufacture service to the military customer since the early 20th century. Today it operates as a Government Trading Fund, fulfilling many commercial contracts ranging from total fleet management of large fleets of vehicles to the service and repair of assemblies and equipments such as small arms.

Its prime role is to continue to support the British Armed Forces, but further utilise its capabilities to fulfil commercial contracts.

At the heart of ABRO is a flexible workforce of more than 2100 people with a diverse skill base. With eleven strategically located sites throughout the UK, ABRO provides a comprehensive support network, in-barracks support, on-site servicing and repair, and mobile support teams which strengthen geographic coverage.

With an annual turnover of £137 million, in a typical year work is carried out on over 900 product lines of military and commercial vehicles and equipments, as well as completing in excess of 95,000 specific on-call repair tasks.

ABRO's aim is to further exploit its core capabilities and develop its sound reputation based on high quality, flexible, cost-effective resource solutions for all its customers.

ABRO | Chairman's Statement



The last year has proved a real challenge for ABRO with a requirement to meet frequent long and short term changes to demand for support from our main customer, particularly for armoured vehicles. Despite this difficult environment, relations with our customers have improved, our working capital is better managed and we have delivered four of the five Key Targets set by the Owner. On behalf of the Board I would like to extend our thanks to both management and all our employees for their significant efforts in this achievement. I would also wish to give recognition to Malcolm Westgate for his very competent tenure as Acting Chief Executive prior to the arrival of Peter Moore last August.

The future continues to be full of uncertainty for ABRO as the Ministry of Defence considers the optimum future delivery of support to its fleet of armoured vehicles and its intentions

for the ownership of the business. What is clear, however, is that to achieve a viable business, ABRO will need to build a contractual relationship with its customers that gives an adequate reward for the risks it is being asked to manage. In exchange ABRO needs to deliver quality, appropriate response times and value for money. This will necessitate a transformation in the fixed cost nature of ABRO's

operations, with far greater flexibility to respond to changing requirements. It will also mean that appropriate incentives need to be offered that reward the success of a partnership between ABRO, its management and employees.

Let us look forward to the future with confidence based on our ability to deliver the changes that meet our stakeholders' expectations.



A handwritten signature in cursive script that reads 'Michael Gates'.

Michael Gates
Chairman
3 July 2006

“On behalf of the Board I would like to extend our thanks to both management and all our employees for their significant efforts”

ABRO | Chief Executive's Overview



The demands on the business created by the need to respond to the modernisation of logistic support to the front line, created a difficult and volatile trading environment for ABRO.

Our first priority was to deliver the required output to the UK Armed Forces and this we have done, exceeding the sales output key target. The introduction of In-Barracks Support arrangements has enabled us to work closer with the Customer, providing an improved level of service and increasing the level of Land Activity. We have continued to build on the lean process improvements identified in the previous year for our armoured vehicle programmes, with a significant improvement in schedule adherence. Work has continued in Germany on the installation of the Bowman communications system and we secured a contract for an additional 1000 Land Rover fits during 2006. Under the

ABRO Fleet Services brand, we won the service support contract for BAA plc at Edinburgh Airport, and have been successfully down-selected to provide fleet management support to the City of York.

Despite these successes, traditional MoD repair programme activity continues to come under pressure with a planned reduction in overall levels. As a result in July 2005, the first of a two phase rationalisation programme was announced to reflect the downturn in workload and the need to increase the underlying efficiency of the business to protect our competitive position and modernise our service delivery footprint. We have successfully implemented Phase One of this programme, achieving our planned headcount reductions with the minimal use of compulsory redundancies.

Phase Two of this programme was announced in November 2005 and proposed the closure of our armoured vehicle and engine facilities at Donnington and consolidation of our armoured vehicle capability at Bovington. Rationalisation plans for our Land and wheeled vehicle business involved the closure and re-provision of our current facilities at Warminster and Colchester and an extension of in-barracks support, enabling engineering support services to be delivered closer to the customer. In addition there was significant rationalisation planned of the Head Office in Andover.

In March 2006, the MoD announced the extension of the depth repair programme for the FV430 armoured fighting vehicle resulting in a significant increase to the predicted workload for our armoured vehicle repair centre at Bovington. As a consequence, repair work on Warrior and Combat Vehicle Reconnaissance (Tracked) will remain at our Donnington facility for the medium term. However, proposals for rationalisation of our Land and wheeled vehicles business were confirmed with a headcount reduction of up to 339 by April 2008.



“In a changing, demanding and volatile market the need to improve the competitiveness of our business remains a key managerial target”

In a changing, demanding and volatile market, the need to improve the competitiveness of our business remains a key managerial target and we will therefore present revised rationalisation proposals for the armoured vehicle and related business units later in the year.

Against this background of uncertainty, the financial year ended well with us achieving a profit before interest of £5.0m and a ROCE of 6.8%.

Going forward, the key challenges that face us are: supporting the MoD Customer's aim of modernising support to our Armed Forces - balancing demands for better value and performance whilst continuing to deliver against key targets; ensuring that we meet the obligations placed upon us in the Defence Industrial Strategy; and playing an important role in the formulation and delivery of the MoD/BAe Logistic Support partnering agreement which will include wide ranging changes to the management of the armoured vehicle sector. We will also use our core skills to continue to develop new and profitable business in both the defence and other commercial markets.

Finally, I would like to express my personal thanks to each and every member of staff who have continued to provide our range of engineering services, often against tight deadlines and under extreme pressure. The challenges ahead of us remain demanding and success will be achieved by continuing to pull together



and work hard as a team. I look forward to us continuing to deliver a first class service to our Customers in the coming year.

Peter Moore
Chief Executive
3 July 2006

ABRO | Management Commentary

Business Activity

The UK MoD equipment support environment continues to reduce due to reductions in individual Integrated Project Team budgets. Business activity for the year remains dominated by traditional MoD work and comprises over 900 repair programmes and 95,000 repair tasks in support of field force units. In contrast ABRO continues to secure further growth in sales directly from the defence industry and through commercial fleet services activity.

Strategy

The major strategic focus has been determining ABRO's position in the maintenance repair and overhaul markets, transition to business units, closer relationships with industry and a major drive to improve customer satisfaction.

ABRO intends to ensure that current business remains broadly level. In order to achieve this it aims to position itself as the preferred supplier/partner for the key land systems original equipment manufacturers on all "future legacy" programmes, maintain contact with front line commands and ensure participation in urgent operational requirements. It will also broaden the business base to sustain critical mass in areas where capability will erode.

ABRO will continue to pursue its growth objectives in new markets.

Sales and Customer Development

Major successes in winning new contracts were dominated by defence industry work for the UK. This included Shielder vehicles being base overhauled, the conversion of MLRS platforms into recovery vehicles and 105mm light gun fleet brake modifications. An additional 35 FV430 armoured fighting vehicles were base overhauled as the result of a delay in the placement of the powertrain contract. Additional Land activity was undertaken through operational funding and defence modernisation in preparation for whole fleet management.

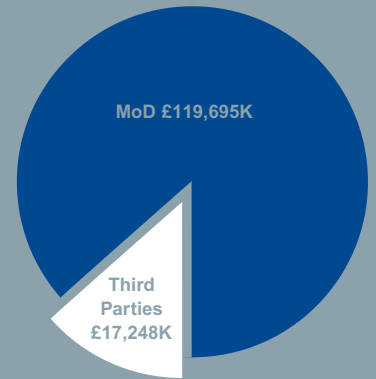
Under Project Hermes, work was secured to convert an initial 100 'general service' Land Rover vehicles to 'fit for radio' with a further 979 during 2006. A further 3,500 vehicles for Project Shoehorn were fitted with anti-roll bars to enable a weight increase to be achieved for the fitting of Bowman radios. This project involved units visiting ABRO workshops across the country, support provided in Germany, Canada and Cyprus and use of mobile support teams across the UK.

Additional activity included in-depth repair of 80 Drops vehicles, and a refurbishment programme for 300 Bedfords.

There was significant development of In-barracks support where ABRO employees undertake activity in REME workshops and work alongside REME soldiers. The added benefit of this initiative is that equipment availability for the end-user is increased in addition to improvements in the quality of training for the REME soldier.

Maintaining existing relationships with key customers and partners remains essential and ABRO is increasingly working with MoD and BAe in formulating a joint business plan which recognises the need for ABRO to retain its armoured fighting vehicle capability. Under the BAe partnering agreement development of a contract for the conversion of the FV430 Powertrain fleet to diesel engines and new transmissions is currently being negotiated.

ABRO Fleet Services won a contract for the servicing of BAA plc's, Edinburgh Airport Ltd's fleet of vehicles and ground handling equipment worth £1.5 million. Additionally, they have been down-selected to 'sole preferred partner status' by the City of York to fleet manage their range of vehicles and equipments.



Total Sales £136,943K

Financial Performance

Overview

ABRO successfully completed its 4th year in business as a Trading Fund within the UK MoD. The 2005/2006 year has been one of two halves; the first half under the cloud of reducing customer budgets and disappointing results, but the second half year seeing a strong business performance, improvement in order book which translated into good profits and a healthy balance sheet.

Operating Results

Sales were £137m (2005 - £151m) and exceeded the key target by £9m. The principal customer remains the MoD, who took £120m (87%) of sales.

Profit before interest was £5.0m (2005 loss £4.2m). This resulted in a return on capital employed of 6.8% (2005 - 5.3%), against a target of 3.5%.

Major improvements in inventory management saw positive results in 2005/2006 both to balance sheet and profits in contrast to the 2004/2005 results which suffered from weak material control and resulting in an escalation in stock holdings and the need to establish £10m in obsolete stock provisions. The improvements in inventory management also released excessive accruals for goods received of £3.7m and released value from stock disposals. The quinquennial revaluation of assets and the disposal of the Warminster site contributed to the loss on asset disposals of £1.2m in year. The net effect of these 'one off' adjustments was a £2.9m enhancement to profits (2005 - £10m loss).

Profit after interest was £4.5m (2005 - £5.3m loss) and a dividend of £12m was paid to the owner, the MoD.

Financing and Cash Flow

ABRO was launched with £32.3m of capital and reserves, £32.3m of long-term (fifteen year) loans and took on further financing in terms of a short-term (five year) loan of £15m and £10m of short-term borrowing (under one year). This produced a debt equity ratio at commencement of the Trading Fund of 1.8:1.

ABRO has since repaid in full its short-term borrowings and reduced long-term borrowings to £23.7m. In addition a £12m dividend has been paid to the Shareholder. The debt equity ratio has improved to 0.3:1.

The sale of the Warminster site was concluded on 31st March 2006 for the sum of £5.6m as part of a sale and lease back arrangement. The cash proceeds were received early in 2006/2007. The balance sheet was considerably strengthened during the year from improvement in materials management, reduction in inventories and improvement in debt collections. These enabled the £12m dividend to be paid whilst retaining cash balances at a £12m level.

Shareholder Value

ABRO has generated significant Shareholder value in its four years as a Trading Fund. Reductions of 23% in selling prices have been made to customers plus a three year standstill in prices (2004/2005 to 2006/2007).

Shareholders have benefited by a growth of £15.9m in retained earnings, £12m of dividends and £33m in reduction in borrowings.

Rationalisation

ABRO announced the intention to proceed with a two phase rationalisation programme. Under Phase One, 283.5 staff were released in 2005/06 with the cost of employee severance met by the MoD, and ABRO bearing the cost of site and facilities rationalisation. Phase Two proposals for rationalisation of the Land and wheeled vehicle business were confirmed, and the implementation will begin in 2006/2007. However, the decision by the MoD Customer to update and upgrade more armoured vehicles meant that the original proposals for rationalisation of ABRO's armoured vehicle and related business units had to be re-examined. These plans are expected to be developed further in 2006, and as plans have not yet matured into tangible programmes; no provision for site rationalisation has been made in the financial statements.

Capital Investment

Given the presence of a major rationalisation programme, new capital investment has been limited. New investment in 2005/2006 amounted to £1.2m.

Performance Against Key Targets 2005/06

The following five key targets were agreed with the Minister of State for the Armed Forces. Performance against each target has been subject to inspection by the National Audit Office.

Key Target 1: Financial Performance

To achieve at least a 3.5% Return on Capital Employed (ROCE). – Achieved.

Key Target 2: Turnover

To achieve a turnover figure of at least £128m in FY 2005/06. – Achieved.

Key Target 3: Schedule Adherence

To meet customer agreed targets for delivery schedules on MoD Critical programme lines. – Partially achieved.

Key Target 4: Efficiency

To achieve a value added per employee target of at least £38K. – Achieved.

Key Target 5: Winning Work

To maintain a closing order book of at least £141m for FY 2005/06. – Achieved.

ABRO Key Targets 2006/07

Background

As an established Trading Fund, ABRO has adopted commercially focused key targets for FY 2006/07 that are comparable to similar organisations within the private sector. ABRO are currently going through a considerable period of change and for consistency have elected to maintain the same key targets as for 2005/06. The exception being the inclusion of a Land measure within the Schedule Adherence Target.

ABRO | Management Commentary (continued)

Summary

Title	Target
Key Target 1: Financial Performance	To achieve at least a 3.5% Return on Capital Employed (ROCE)
Key Target 2: Turnover	To achieve a turnover figure of at least £134m
Key Target 3: Schedule Adherence	To meet Customer agreed targets for delivery schedules on Critical Programme lines and Land load tasks
Key Target 4: Efficiency	To achieve a value added per employee target of at least £39K
Key Target 5: Winning Work	To achieve a total closing order book of at least £150m

Reporting

Progress against Key Targets will be reviewed by the ABRO Trading Fund Board and reported to ABRO's Owner's Advisory Council. As part of their audit of the end of year accounts, ABRO's reported performance will be independently validated by the National Audit Office.

People

Employment Policies

ABRO continues to maintain the strong conviction that in order to remain competitive, the workforce must mirror the diversity of the communities within which it operates. It continues to pursue talented employees, without regard to ethnic background, religion, age, disability or gender, who will provide the expertise, passion, pace and imagination to drive the business forward to a prosperous future. It is ABRO's policy to provide equal employment opportunities and appropriate training and career development for any employees who are or have become disabled.

A 'Family Friendly' employer, ABRO offers various flexible working patterns, and assists employees with parental or other care responsibilities. Some sites provide access to workplace nurseries, providing day facilities for children aged between 3 months and 5 years.

Offering youth and adult apprenticeship schemes, the number of apprentices during the period increased from 89 to 112.

ABRO achieved Investors in People in 1999 and continues to maintain accreditation, the most recent being in January 2004. The commitment to continue to meet or exceed this standard is a key component for continuous improvement. ABRO will be re-assessed again in July 2007.

Employee Involvement

ABRO is committed to excellent working relations with the Trade Unions, through both formal consultation and the Whitley process and the more informal day to day contact at local and national levels. It also has in place partnering agreements with both the non-industrial and industrial Trade Unions. ABRO continues to seek to maximise communications at all levels in order to involve employees in the decision-making process of the business. Various methods include the in-house magazine, Insite, weekly cascade briefs, the Chief Executive's workshop tours, trade union consultation and training programmes aligned to business growth.

Occupational Risk & The Environment

ABRO is committed to meeting its obligations, responsibilities and adhering to all existing legislation on health, safety and environmental requirements.

Statistics show that positive action in encouraging all staff to take appropriate steps to reduce accidents has resulted in a decrease in the total number of incidents across the sites and these remain well below the HSE's national incidence rates.

Occupational health services are provided by three nurses currently employed by ABRO. They work to current legislation and provide cover to Donnington, Stirling, Catterick, Colchester and Warminster. Bovington is currently covered by a contract with the NHS Primary Care Trust.

ABRO is committed to compliance of the Environmental Protection Act and the Environment Act and with all other existing environmental legislation. Bovington maintains BSEN14001 certification and much work has been undertaken to conduct impact assessments at other sites. Whilst these assessments have concluded that significant improvement has been made, further progress is required prior to ABRO-wide status being achieved.

ABRO maintains BS EN ISO 9001:2000 certification.

ABRO | Report by the Comptroller and Auditor General on ABRO's Statement of Performance against 2005-2006 Key Performance Targets

The Chief Executive of ABRO has asked me to validate performance against the 2005-2006 Key Targets.

Respective responsibility of ABRO, the Chief Executive and the Auditor

ABRO and the Chief Executive are responsible for the measurement and reporting of the Trading Fund's performance against the Key Targets.

I examine and conclude on whether the Trading Fund has:

- Provided full details of performance against all ABRO's Key Targets;
- Ensured that all performance information is reliable and fairly presented.

Basis of conclusion

The validation includes an examination, on a test basis, of evidence relevant to the amounts and disclosures of the outturns and achievements included within the Statement. It also includes an assessment of the significant judgements and methodologies made by ABRO and the Chief Executive in the Statement's preparation.

Conclusion

The Statement of Performance above includes all ABRO's 2005-2006 Key Targets and it reliably and fairly presents the Agency's performance against the Key Targets. I have no observations to make on this Statement.



John Bourn
Comptroller and Auditor General
5th July 2006

National Audit Office
157-197 Buckingham Palace Road
London
W1W 9SP

ABRO | Board

Chairman

1. Michael Gates *MBA, FCA*

Responsible for leading the ABRO Board, to ensure it operates efficiently and effectively in its role of developing strategy, and overseeing and scrutinising ABRO's plans and performance.

Michael Gates was appointed in January 2005 and brings significant industrial experience from a number of blue-chip companies, most recently Shell International Petroleum where he was Finance Director for China and Hong Kong, Regional Finance Adviser for the Far East and Investor Relations Manager. He is also a non-executive director for the United Kingdom Hydrographic Office.

Chief Executive

2. Peter Moore

Peter Moore was appointed Chief Executive of ABRO in August 2005, responsible to the Owner for delivering the strategic aims and objectives of the business and providing corporate governance leadership.

Peter has extensive manufacturing, marketing, commercial and logistics experience in a variety of supply and engineering organisations both in the public and private sectors. In his last appointment he was Chief Executive Officer of Malta Shipyards Limited group of companies where he was responsible for the re-structuring and turn-around of the business and re-establishing the company as a major player in the ship repair, offshore and military sectors.

Deputy Chief Executive

3. Malcolm Westgate

Responsible for Business Development, HR, Secretariat, Audit, Health and Safety, Environment and Fire, Risk and Facilities Management.

Malcolm Westgate was appointed to ABRO in April 2002 following an extensive career in the Ministry of Defence, latterly as Director of HR/IT for the DLO's Warship Support Agency. He was also the Head of Profession for MoD Nuclear Suitably Qualified and Experienced Personnel in MoD.

In recent years he was Managing Director of the Royal Naval Armament Depot, Beith, Deputy Chief Executive of the Naval Bases and Supply Agency, Chief Inspector Explosives for the Navy Department and Chief Executive of the Disposal Sales Agency.

Finance Director

4. Stuart Ash *FCCA*

Responsible for finance, business systems and the delivery of high quality financial management information to the business.

Stuart Ash was appointed in October 2001 and has wide experience in finance, commercial and project management gained from 20 years at director level in the defence industry with Racal, Thorn, Ferranti and Brown & Root. This includes seven years at Atomic Weapons Establishment, Aldermaston as Finance Director.



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Operations Director

5. David Mather *MBA, BSc, CEng, MIEE*

Responsible for developing and delivering the operations strategy which underpins ABRO's strategic aims and objectives.

David Mather was appointed Operations Director in September 2002. He has gained experience in various engineering sectors including the machine tool industry, car industry and more recently defence. He has implemented a number of successful change management programmes and has extensive knowledge of modern manufacturing techniques.

Sales & Marketing Director

6. Ian Metcalf *MA, FIPT*

Responsible for delivering and managing a robust marketing and sales strategy.

Ian Metcalf was appointed in January 2006 and has a track record of success in major sales to US DoD, UK MoD and European defence ministries. In recent appointments he has been responsible for transforming business relationships with MoD from short-term transactional activity to long-term partnered contracts delivering value to both parties.

Commercial Director

7. Geoff Thompson *CIPS, MAPM*

Responsible for commercial arrangements with industry.

Geoff Thompson was appointed in March 2002 and has had an extensive and wide-ranging career within the MoD. Recent appointments have included providing commercial support to the tri-service helicopter fleet and prior to that being at the forefront of the MoD's partnering initiatives with industry.

Non-Executive Director

8. Tim Johnson

Tim Johnson was appointed to the ABRO Board in May 2005.

He is currently a Director both at the Ministry of Defence, where he advises Ministers on their shareholding interests in Trading Funds and at the Shareholder Executive, where he works across a range of Government shareholdings. Previously he had a varied career in Her Majesty's Treasury where roles included managing the Treasury's interests in Royal Mail and implementing the public private partnership for National Air Traffic Services.

Non-Executive Director

9. Michael Jones *FRAeS, MIMechE, MIEE*

Michael Jones was appointed to the ABRO board in January 2003.

He has business experience in both automotive and aerospace, obtained in the US, Europe, Middle East and Far East. He was Managing Director of a US automotive multi-national, and has run plants in both the USA and Europe.

Michael joined Smith Aerospace in 1997 and was appointed to his current position Aerospace Systems Vice President in 2004 after holding appointment as Managing Director UK Operations, Group Director and Managing Director, Civil Systems.

Non-Executive Director

10. Richard Holroyd *MBA, MA*

Richard Holroyd was appointed to the ABRO board in January 2003.

Currently also a Non-Executive Director of Cantrell & Cochrane Plc, of Otto Weibel AG in Switzerland and a Member of the United Kingdom Competition Commission. Previously he was Managing Director of Colmans of Norwich, European Director, Reckitt & Colman and Head of the Global Marketing Futures department of Shell International.

Non-Executive Director

11. Jane Cannon *MBE*

Jane served as a non-executive director from May 2005 to May 2006.

She is currently Group Director of Strategy and Planning for Qinetiq which she joined from BT where she undertook various roles, from leading a business unit of 800 people who operate the UK based international networks to driving the transformation and change agenda for BT Wholesale.

Jane was previously Technical Director of an engineering company that specialised in automating factory machinery and has also worked for a venture capital firm and for the Cabinet Office.

She was awarded the MBE in 2003 for services to business and engineering.

National Industrial Trade Union Representative

12. Laurence Faircloth

Laurence was appointed as industrial trade union representative in January 2006.

He is National Officer for Amicus with responsibilities for all members employed within MoD and its agencies, together with national responsibilities for government departments such as prisons.

National Secretary of Prospect – Trade Union Representative

13. Steve Jary *PhD, MSc*

Steve Jary was appointed as non-industrial trade union representative in March 2005.

He is National Secretary of Prospect and leads for the union in the defence policy arena. Accountable for the management of a negotiating team of the union based in Prospect's London headquarters, he is responsible for conducting collective bargaining across a range of employers and for personal representation of members.

Steve has worked in a variety of capacities for Prospect and its predecessors for over 17 years. In 1992 he was principal author of a joint union policy on defence diversification which led to the creation of the Defence Diversification Agency in 1997. He has been a member of the Employment Tribunals of England and Wales since 2002, sitting in the London Central region.



ABRO | Remuneration Report

1. Introduction

This report has been prepared in accordance with the Directors' Remuneration Regulations 2002. The Regulations require the auditors to report to the agency's members on the 'auditable part' of the Directors' Remuneration Report and to state whether in their opinion that part of the report has been properly prepared. The Report has therefore been divided into separate sections for audited and unaudited information.

UNAUDITED INFORMATION

2. The Remuneration Committee

The Remuneration Committee was appointed by ABRO Board and is made up of the 3 non-executive directors - Mr Michael Jones, Ms Jane Cannon (until May 2006) and Mr Tim Johnson - a director level representative of the MoD Directorate of Business Delivery. Mr Richard Holroyd is the non-executive chair. The Deputy Chief Executive ABRO acts as the Secretary of the Committee and other individuals including the Chairman and the Chief Executive are normally invited as appropriate. The committee met twice during the year ended March 2006.

The purpose of the committee is:

- To consider and approve the Fixed Term Contract Directors' bonus scheme, including the proposed criteria, assessment of performance, and recommended payouts.
- To endorse the objectives and amount of money that will be made available for distribution to employees under the Corporate Profit Share Scheme based on an assessment of the performance of ABRO against its key performance targets and the level of declared profit.
- To consider, if appropriate, whether the Senior Civil Servants at ABRO should either be included in the ABRO's Profit Share scheme or the wider MoD SCS bonus scheme, and subsequently: either to agree the bonus to be paid to ABRO Senior Civil Servants within the overall amount of money set for distribution under the Corporate Profit Share scheme; or to review and approve the Chief Executive's recommendations on the ABRO Senior Civil Servants' bonuses to the MoD Pay Committee.
- To consider and, if appropriate, endorse the overall quantum and policies applied for deciding on payments of special performance bonuses as recommended by the Chief Executive. To review a summary list prepared on a six monthly basis of all bonus payments (exceeding £100) made within the overall allocated budget for these payments.
- To review and approve any proposed revisions to the Corporate Profit Share scheme.
- To consider and advise on any other remuneration issues, as directed by the ABRO Board or requested by the ABRO Chairman and/or Chief Executive.



3. Remuneration Policy

Directors in ABRO are appointed either through the MoD Senior Civil Service (SCS) scheme or from outside industry as Fixed Term Appointments (FTAs). Those Directors who are part of the SCS come under the remit of the MoD's pay strategy as endorsed by the Main Pay Committee. It supplements the performance management arrangements for SCS which seek to encourage continuous improvement, contribute to delivery of MoD's key performance targets and deal with poor individual performance. It also underlies the work on the Civil Service Management Board agenda for Improving Leadership Capacity in the SCS.

The main components of ABRO Director remuneration comprise –

Basic Salary

Basic salary is reviewed annually in line with Cabinet Office provisions applying to senior appointments, not on standard performance related pay terms; the annual uprate is usually close to the indicators for inflation (in recent years 2.5-3%). ABRO Chairman's fee is set by the Permanent Under Secretary (PUS) and in 2005 was paid at the rate of £1000 per day. In 2005 each other non-executive director received £600 per day plus any travel and subsistence costs incurred. This excludes the representative from MoD's Directorate of Business Development whose services are not charged to ABRO. The Chairman of the Remuneration Committee also received an additional £600 per quarter. Non-Executive

Directors are not involved in any discussion about their own remuneration. Their fees are reviewed by PUS and from November 2006 the Chairman will receive a fixed salary of £40,000 per year paid monthly in arrears, set on the basis that the role should require circa 40 days per year. All payments made to non-executive directors are non-pensionable.

Annual Bonus Scheme

ABRO bonuses run in parallel to the MoD SCS arrangements. The Pay Committee monitors the inter-relationship between individual and team bonuses to ensure consistency, that performance measures are suitably aligned and that the total reward package is reasonable. The Pay Committee liaises with ABRO Remuneration Committee as required to ensure that totality of remuneration in ABRO does not become disproportionate to the rest of the SCS.

Directors who are SCS officers are covered by the MoD SCS bonus scheme. ABRO Fixed Term Appointees at Director level are able to earn up to a 10% annual performance related bonus against targets negotiated each year with the Chief Executive. The bonus is non-pensionable and non-consolidated and is paid subject to the assessment of performance as a one-off lump sum at the end of the annual bonus review period.

The table below shows bonuses/performance targets for directors for 2004/05 paid in 2005/06:

	% Objectives Achieved	Bonus as % Salary
Peter Moore¹	N/A	N/A
Stuart Ash	85	9
David Mather	85	7
Ian Metcalf²	N/A	N/A
Graeme Rumbol	<i>Consent for disclosure not received</i>	
Geoff Thompson	<i>Consent for disclosure not received</i>	
Malcolm Westgate³	N/A	N/A

¹ Appointed 1 August 2005

² Joined ABRO January 2006

³ Covered under the civil service bonus scheme

External Appointments

No Executive Director currently has membership of any other Departmental Boards.

ABRO | Remuneration Report (continued)

4. Service Contracts

Executive Directors	Date of Appointment	Unexpired Term	Employee Notice Period
Peter Moore	August 2005	28 months	6 months
Stuart Ash	October 2001	17 months	6 months
David Mather	September 2002	30 months	6 months
Ian Metcalf	January 2006	33 months	6 months
Graeme Rumbol ¹	<i>Consent for disclosure not received</i>		
Geoff Thompson	<i>Consent for disclosure not received</i>		
Malcolm Westgate ²	April 2002	N/A	N/A

¹ Left ABRO September 2005.

² SCS Directors and therefore covered by Civil Service Terms and Conditions.

Non-Executive Directors	Date of Appointment	Unexpired Term	Employee Notice Period
Michael Gates ¹	January 2005	< 6 Months ¹	1 Month
Michael Jones	January 2004	7 Months	1 Month
Richard Holroyd	January 2004	7 Months	1 Month
Jane Cannon	May 2005	Contract Expired	1 Month
Tim Johnson ²	May 2005	N/A ²	N/A

¹ Mr Gates holds a provisional contract which expires on the appointment of the successful candidate recruited through open competition. This recruitment process is currently underway.

² Mr Johnson is the representative of MoD's Directorate of Business Development. This is a permanent position on ABRO's Board and is a service resourced at the discretion of MoD.

AUDITED INFORMATION

5. Directors' Remuneration

The following table sets out an analysis of pre-tax remuneration during the year ended March 2006 and total remuneration for 2005.

Executive Directors	Total 05/06 (£k)	Total 04/05 (£k)
Peter Moore ¹	80 - 85	N/A
Stuart Ash	90 - 95	90 - 95
David Mather	105 - 110	105 - 110
Ian Metcalf ²	20 - 25	N/A
Graeme Rumbol	<i>Consent for disclosure not received</i>	
Geoff Thompson	<i>Consent for disclosure not received</i>	
Malcolm Westgate	85 - 90	80 - 85

¹ Appointed 1 August 2005 – therefore only 8 months remuneration shown.

² Joined ABRO January 2006 – therefore only 3 months remuneration shown.

Non-Executive Directors	Fees 2005/06 (£)	Fees 2004/05 (£)
Michael Gates	38,167	11,736
Michael Jones	7,200	5,662
Richard Holroyd	11,100	9,825
Jane Cannon	5,700	N/A
Tim Johnson ¹	N/A	N/A

¹ Salary and pension costs of full-time government officials are borne by their parent departments.

6. Directors' Pensions

	Real increase in pension £000	Real increase in related lump sum at age 60 £000	Total accrued pension at age 60 at 31/03/2006 £000	Total accrued lump sum at age 60 £000	CETV at 01/04/2005 £000	CETV at 31/03/2006 £000	Real increase in CETV funded by employer £000
Peter Moore¹ (Chief Executive)	0 - 2.5	N/A - Premium	0 - 5	N/A - Premium	0	15	18
Stuart Ash (Finance Director)	0 - 2.5	2.5 - 5.0	0 - 5	10 - 15	65	88	25
David Mather (Operations Director)	0 - 2.5	0	5 - 10	0	47	72	26
Ian Metcalf² (Sales & Marketing Director)	0 - 2.5	N/A - Premium	0 - 5	N/A - Premium	0	4	4
Graeme Rumbol (Sales & Marketing Director)	<i>Consent for disclosure not received</i>						
Geoff Thompson (Commercial Director)	<i>Consent for disclosure not received</i>						
Malcolm Westgate (Company Secretary)	0 - 2.5	2.5 - 5.0	35 - 40	115 - 120	670	721	24

¹ Appointed 1 August 2005 – therefore only 8 months remuneration shown.

² Joined ABRO January 2006 – therefore only 3 months remuneration shown.

Pension benefits are provided through CSP arrangements. Civil servants may be in one of three statutory based 'final salary' defined benefit schemes (classic, premium, and classic plus). The schemes are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under the three schemes are increased annually in line with changes in the Retail Price Index. New entrants after 1 October 2002 may choose between membership of premium or joining a good quality 'money purchase' stakeholder arrangement with a significant employer contribution (partnership pension account).

Employee contributions are set at the rate of 1.5% of pensionable earnings for classic and 3.5% for premium and classic plus. Benefits in classic accrue at the rate of 1/80th of pensionable salary for each year of service. In addition, a lump sum equivalent to three years' pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable

earnings for each year of service. Unlike classic, there is no automatic lump sum (but members may give up (commute) some of their pension to provide a lump sum). Classic plus is essentially a variation of premium, but with benefits in respect of service before 1 October 2002 calculated broadly as per classic. The partnership pension account is a stakeholder pension arrangement.

The employer makes a basic contribution of between 3% and 12.5% (depending on the age of the member) into a stakeholder pension product chosen by the employee. The employee does not have to contribute but where they do make contributions, the employer will match these up to a limit of 3% of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8% of pensionable salary to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement). Further details about the CSP arrangements can be found at the website www.civilservice-pensions.gov.uk

ABRO | Remuneration Report (continued)

6. Directors' Pensions (continued)

A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The reported increase in CETV reflects the increase in CETV effectively funded by the employer. It takes account of the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The CETV figures, and from 2003-04 the other pension details, include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the CSP arrangements and for which the CS Vote has received a transfer payment commensurate to the additional pension liabilities being assumed. They also include any additional pension benefit accrued to the member as a result of their purchasing additional years of pension service in the scheme at their own cost. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries. The Principal Civil Service Pension Scheme (PCSPS) is an un-funded multi-employer defined benefit scheme but ABRO is unable to identify its share of the underlying assets and liabilities. A full actuarial valuation was carried out as at 31 March 2003. Details can be found in the resource accounts of the Cabinet Office: Civil Superannuation (www.civilservice-pensions.gov.uk). For 2005/6, pursuant to the Superannuation Act 1972, employer's contributions of £8,211k were payable to the PCSPS (2004/5 £6,036k) at one of four rates in the range 16.2 per cent to 24.6 per cent of pensionable pay, based on salary bands. Rates will increase from 2006/7. The contribution rates reflect benefits as they are accrued, not when the costs are actually incurred, and reflect past experience of the scheme.

7. Approval

This Directors' Remuneration Report has been approved by ABRO Chief Executive.



Peter Moore
Chief Executive
3 July 2006



ABRO | Statement of ABRO's and Chief Executive's Responsibilities

Under section 4(6)(a) of the Government Trading Funds Act 1973 the Treasury has directed ABRO to prepare a statement of accounts for each financial year in the form and on the basis set out in the Accounts Direction. The accounts are prepared on an accruals basis and must give a true and fair view of the Agency's state of affairs at the year end and of its income and expenditure, total recognised gains and losses and cash flows for the year.

In preparing the accounts ABRO is required to:

- Observe the Accounts Direction issued by the Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- Make judgements and estimates on a reasonable basis;
- State whether applicable accounting standards have been followed, and disclose and explain any material departures in the financial statements;
- Prepare the financial statements on the going concern basis, unless it is inappropriate to presume that ABRO will continue in operation.

The Treasury has appointed the Chief Executive of ABRO as the Accounting Officer for ABRO. His relevant responsibilities in this role, including his responsibility for propriety and regularity of the public finances for which he is answerable and for keeping of proper records, are set out in the Accounting Officers' Memorandum, issued by the Treasury and published in "Government Accounting".



“The accounts are prepared on an accruals basis and must give a true and fair view of the Agency's state of affairs at the year end”

ABRO | Chief Executive's Statement on Internal Control

1. Scope of Responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of ABRO's policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Government Accounting.

I am accountable to the Minister (Armed Forces) through the Owner's Advisory Council who receive ABRO's Business plan and objectives. In addition it has sight of regular performance reports and ABRO's strategic risks and action plans.

To support me as Accounting Officer, ABRO has the following governance structures in place:

- The Trading Fund Board comprising of the executive directors, a non-executive chairman and 4 non-executive directors. Executive directors are personally responsible for the management of risks within their functional area.
- ABRO Audit Committee, chaired by a non-executive director, providing support to the company's corporate governance practices.

2. The Purpose of the System of Internal Control

The system of internal control is designed to manage risk to a reasonable level, rather than to eliminate all risk of failure to achieve policies, aims and objectives. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of ABRO policies, aims and objectives; to evaluate the likelihood of those risks being realised and the impact should they be realised; and to manage them efficiently, effectively and economically. The system of internal control has been in place in ABRO for the year ended 31 March 2006 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.



“The Board receives regular reports on business activity and sets and reviews targets to measure financial and other performance”

3. Capacity to Handle Risk

The ABRO Business Risk Management Strategy sets out roles and responsibilities at all levels for the risk management process. The ABRO Board has provided leadership to the risk management process through its appointment of corporate staff with specific responsibilities for developing the risk management process. In addition, each corporate level risk is “owned” by an individual Director who is responsible for managing it and ensuring that associated mitigating factors are implemented.

Training was provided in-year for risk coordinators at sites on risk management and business continuity. This included identification, assessment, recording, and managing risks. Practical control self assessment training was also attended by the corporate governance team with the view to a gradual implementation of the technique into business areas to enhance the risk management process.

Risk focal points have been established for each Head Office functional area and risk facilitation workshops were held across all functions in order to improve the understanding of risk and develop functional risk registers.

During the year there has been liaison with other MoD Trading Funds agencies to discuss risk management and assurance in order to identify good practice and lessons learned.

4. The Risk and Control Framework

Work has been carried out this year to increase the understanding of ABRO’s risk and control environment. Risk registers are in place at each site and for each Head Office functional area with risks aligned to Key Targets and corporate objectives. Risks are predominantly measured and escalated on an inherent basis using standard defined criteria. There is a focus on root cause analysis of each risk in order to focus the mitigation actions more effectively. Work in 06/07 will further develop ABRO’s understanding of its risk and control environment to enable risks to be meaningfully measured at a residual level.

Other practices in place for the identification and management of risk are:

- Business Continuity Plans are in place for all ABRO owned sites and a programme of desk top exercises is planned for June/July 06.
- The creation and maintenance of project risk registers forms part of ABRO’s bid management process.
- Appropriate insurance arrangements are in place.
- Anti fraud and theft strategy continues to be promoted. There have been no new instances of reported fraud or theft.

ABRO | Chief Executive's Statement on Internal Control (continued)

5. Review of Effectiveness

As Accounting Officer, I also have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within ABRO who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Board and the Audit Committee

and a plan to address weaknesses and ensure continuous improvement of the system is in place.

The key elements of the mechanisms in place to provide effective internal control are:

Audit Committee

The Audit Committee meets quarterly and consists of 3 non-executive directors with a non-executive chairman. The meetings are attended by representatives from the National Audit Office and Mazars, who work in partnership as ABRO's external auditors; Defence Internal Audit; ABRO Internal Audit; and relevant personnel from within the business guided by the agenda. The committee reviews the system of internal control and minutes are available to the Board.

During the year a non-executive director from MoD Directorate Business Development (DBD) became a member of the Audit Committee (March 06) and from May 06, ABRO is a non-executive below complement.

Internal Audit

The internal audit service reviews the effectiveness of business processes and is provided by an in-house team of auditors supplemented by the MoD's Defence Internal Audit (DIA). The annual audit programme is developed on a risk basis and agreed by the Audit Committee. Assignments are carried out in accordance with Government Internal Audit Standards and findings and reports are presented to the audit committee along with the sponsoring Director.

Other Assurance Providers

Assurances are received by the Board from regular reports on quality, health, safety, environmental protection, and fire risks. In addition ABRO is subject to review by other independent bodies including BSI, Environment Agency, Defence Fraud and Analysis Unit (DFAU) and Defence Security Standards Organisation (DSSO) which examines ABRO's approach to both security and business continuity.

Performance Monitoring

The Board receives regular reports on business activity and sets and reviews targets to measure financial and other performance.

Financial Management

The system of internal financial control provides reasonable, although not absolute, assurance that assets are safeguarded, transactions authorised and properly recorded, and that material errors or irregularities would either be prevented or would be detected within a timely period.

Control Environment

Control is exercised through an organisation structure with clearly defined levels of responsibility and authority, and appropriate operational procedures as well as financial reporting procedures and management review. Management Assurance Statements for the year ended 31st March 2005 have been signed by all Directors and General Managers to confirm that they have discharged their responsibilities in respect of the systems of internal control.



6. Significant Control Weaknesses

Update on control weaknesses identified in 04/05 Report & Accounts

Work has continued throughout 05/06 to improve the robustness of the demand, supply and material management systems. In addition actions have been taken to reduce surplus and obsolete stock holdings from 11.9m to £4.7m and reduce overall stock holdings from £33.7m to £18.9m. The 06/07 audit programme includes audits of stock and supply chain management which will provide independent assurance to the Board that the control environment in this area has been strengthened.

There was successful prosecution of the fraud case stated in ABRO's 04/05 Report & Accounts with the accused receiving a custodial sentence. Efforts are ongoing to resolve the issue of the significant amount of stock which was evidential to the case.

Significant control weaknesses identified in 05/06

A historic control weakness, from before ABRO became a Trading Fund in 2003, over the reconciliation of goods received and invoiced meant that a large provision was held on the balance sheet. Although this provision reduced over the subsequent years as IT systems and processes were improved, a Goods Received Not Invoiced (GRNI) balance of £9.3m remained in the accounts as at end of 05/06. An estimate of the true balance resulted in a proposal to release £3.7m of the provision. A review by Defence Internal Audit found no evidence that the revised GRNI balance is materially mis-stated. Further planned audit work by DIA during May/June 06 on the revised internal control system will provide an assurance that the risk of reoccurrence is mitigated.

7. Future Developments

Along with the continuing work to further embed risk management within the organisation, planned future developments include:

- Increased coherence of ABRO's audit and assurance functions to ensure adequate coverage of the identified risk areas. This will be achieved by bringing together Internal Audit, Security, Quality, Health, Safety and Environment roles under a Head of Corporate Governance.
- Formalisation of the process for following up audit recommendations to ensure delivery of agreed actions.
- Combined risk and performance reporting using the balance scorecard method reporting by business stream and location.
- Focus on improving business continuity planning including incorporating supplier issues, standardising the approach across ABRO and developing a suitable testing strategy.



Peter Moore
Chief Executive
3 July 2006

ABRO | Directors' Report

Statutory Background

These accounts have been prepared in accordance with a direction given by HM Treasury in line with section 4(6) of the Government Trading Funds Act 1973 and in accordance with the Government Financial Reporting Manual (FReM).

Principal Activities and Significant Changes During the Year

The principal activities were the repair, remanufacture and engineering support of a wide range of land-based weapon systems, support equipment and ancillaries for the United Kingdom Armed Forces, together with the provision of these services to an increasing number of commercial and local authority organisations.

The principal activities are described in more detail in the Management Commentary on pages 8-11.

ABRO became a Trading Fund on 1 April 2002, having previously been a vote funded agency of the Ministry of Defence.

Dividend

A Dividend of £12.0 million was paid to the Ministry of Defence during the year.

Fixed Assets

During the year the site operated by ABRO at Warminster was disposed of and a lease back arrangement entered into. All Fixed Assets owned by ABRO were subjected to a quinquennial professional revaluation during the year.

The financial effect of these and other changes to Fixed Assets are shown in note 7 to the accounts.

Market Value of Land

The land assets were professionally revalued by GVA Grimley at 31 March 2006. During the year a strategic review was conducted of ABRO's activities including site utilisation. Those sites which are expected to be fully utilised were valued on an existing use basis; sites which are expected to have their activities significantly reduced or curtailed were valued at open market value where this could be determined. Therefore there is no significant difference between the open market value and the book value of land.



Directors

The Executive Directors who served during the year were:

Mr Peter Moore	Chief Executive (Appointed 1 August 2005)
Mr Malcolm Westgate	Deputy Chief Executive (Acting Chief Executive until 31 July 2005)
Mr Stuart Ash	Finance Director
Mr Geoff Thompson	Commercial Director
Mr David Mather	Operations Director
Mr Graeme Rumbol	Sales and Marketing Director (Resigned 9 September 2005)
Mr Ian Metcalf	Sales and Marketing Director (Appointed 3 January 2006)

The non – executive Directors were:

Mr Michael Gates	Chairman
Mr Richard Holroyd	
Mr Michael Jones	
Ms Jane Cannon	
Mr Tim Johnson	



Directors' Interests

No Director held any company directorship or other significant interest which may conflict with their management responsibilities.

Pension Liabilities

Civilian staff are covered by the provisions of the Principal Civil Service Pensions Schemes (PCSPS). Details of how pensions liabilities are treated in the accounts are shown in note 1 G to the accounts on page 31.

Creditor Payment Policy

It is the ABRO's policy to comply with the Companies Act 1985, (Miscellaneous Accounting Amendments) Regulations 1996 (SI 1996/189), and the Confederation of British Industry's prompt payment code on creditors.

It is ABRO's policy to pay its suppliers within contracted payment terms or in the absence of specially agreed terms within 30 days of receipt of a valid invoice.


During the year ended 31 March 2006 in excess of 95% of ABRO's payments were made within this policy.

Auditors and Cost of Audit

ABRO's annual accounts are audited by the Comptroller and Auditor General. ABRO's auditor is the National Audit Office. The cost of the audit of the Annual Accounts was £67,500 and the audit of the Key Targets was £2,500. No payment was made to the auditor for any other service.

As Accounting Officer of ABRO, the Chief Executive is responsible for the disclosure of relevant audit information and can confirm that:

- there is no relevant audit information of which the auditors are unaware;
- he has taken all necessary steps to ensure that he is aware of the relevant audit information; and
- he has taken all necessary steps to establish that the auditors are aware of the information.


Peter Moore
Chief Executive
3 July 2006

ABRO | The Certificate and Report of the Comptroller and Auditor General to the Houses of Parliament

I certify that I have audited the financial statements of ABRO for the year ended 31 March 2006 under the Government Trading Funds Act 1973. These comprise the Income and Expenditure Account, the Balance Sheet, the Cashflow Statement and Statement of Total Recognised Gains and Losses and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective Responsibilities of ABRO, The Chief Executive and Auditor

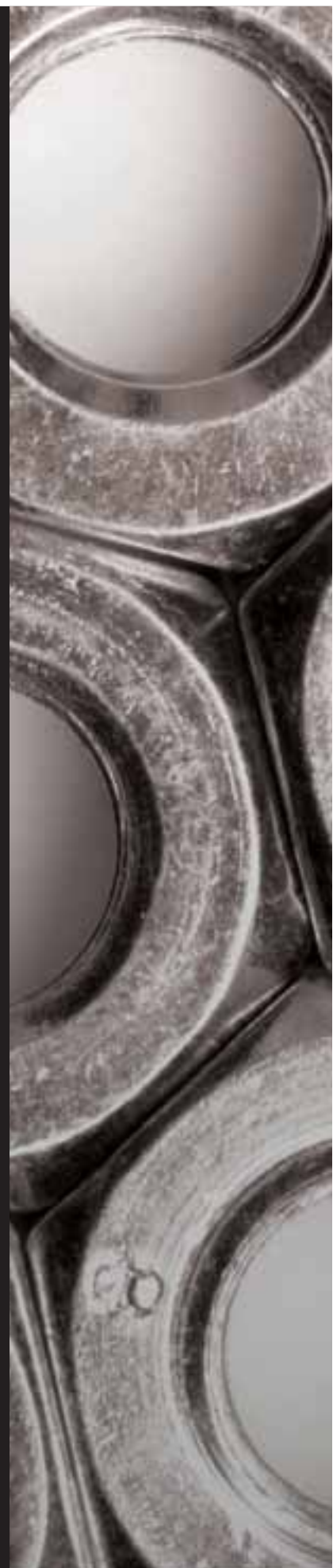
ABRO and the Chief Executive are responsible for preparing the Annual Report, the Remuneration Report and the financial statements in accordance with the Government Trading Funds Act 1973 and HM Treasury directions made thereunder and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of ABRO's and the Chief Executive's Responsibilities.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Government Trading Funds Act 1973 and HM Treasury directions made thereunder. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. I also report to you if, in my opinion, the Annual Report is not consistent with the financial statements, if ABRO has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by relevant authorities regarding remuneration and other transactions is not disclosed.

I review whether the statement on pages 20-23 reflects ABRO's compliance with HM Treasury's guidance on the Statement on Internal Control, and I report if it does not. I am not required to consider whether the Accounting Officer's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of ABRO's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises only the Chairman's and Chief Executive's Statements, the Directors' Report, the unaudited part of the Remuneration Report and the Management Commentary. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.



“The financial statements give a true and fair view, in accordance with the Government Trading Funds Act 1973”

Basis of Audit Opinion

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the Board and Chief Executive in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the ABRO's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error and that in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinions

In my opinion:

- **the financial statements give a true and fair view, in accordance with the Government Trading Funds Act 1973 and directions made thereunder by HM Treasury, of the state of ABRO's affairs as at 31 March 2006, total recognised gains and losses, cash flows and of its surplus for the year then ended;**
- **the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Government Trading Funds Act 1973 and HM Treasury directions made thereunder; and**
- **in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.**

I have no observations to make on these financial statements.



John Bourn
Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria, London SW1W 9SP
5 July 2006

ABRO | Accounts

Profit and Loss Account for the Year ended 31 March 2006

	Note	2005/06 £'000	2004/05 £'000
Turnover	2	136,943	150,909
Cost of sales	3	(113,427)	(136,666)
Gross profit		23,516	14,243
Operating expenses	3	(17,366)	(18,199)
Operating Profit		6,150	(3,956)
Loss on disposal of fixed assets		(1,161)	(269)
Profit on ordinary activities before interest		4,989	(4,225)
Interest receivable and similar income	5	905	503
Interest payable and similar charges	6	(1,424)	(1,545)
Profit/(Loss) for the financial year		4,470	(5,267)
Dividend		(12,000)	-
Transfer from General Reserve		(7,530)	(5,267)

There were no discontinued operations in 2005/06 or 2004/05.

The notes on pages 30 to 39 form part of these accounts.

Balance Sheet at 31 March 2006

	Note	31-Mar-06 £'000	31-Mar-05 £'000
Fixed Assets			
Tangible Assets	7	34,678	42,784
Current Assets			
Stock	8	20,022	25,430
Debtors	9	31,713	34,667
Cash at Bank and in Hand	10	11,678	12,279
		63,413	72,376
Current Liabilities			
Creditors:			
amounts falling due within one year	12	(28,951)	(37,968)
Net current assets		34,462	34,408
Total assets less current liabilities		69,140	77,192
Creditors due after more than one year		-	-
Provisions for liabilities and charges		-	-
Total capital employed		69,140	77,192
Financed by:			
Public dividend capital		19,405	19,405
Long term loans	13	21,542	23,696
Revaluation reserve	14	12,262	16,401
General reserve	15	15,931	17,690
Total government funding	20	69,140	77,192

The notes on pages 30 to 39 form part of these accounts.



P Moore, Chief Executive, 3 July 2006

Statement of Total Recognised Gains and Losses for the Year ended 31 March 2006

	2005/06 £'000	2004/05 £'000
Profit/(Loss) for the financial year	4,470	(5,267)
Unrealised revaluation surplus	1,632	1,507
Total recognised gains and losses relating to the year	6,102	(3,760)

The notes on pages 30 to 39 form part of these accounts.

Cash Flow Statement for the Year ended 31 March 2006

	2005/06 £'000	2004/05 £'000
Reconciliation of operating profit to cash inflow from operating activities		
Operating Profit	6,150	(3,956)
Depreciation (Note 7)	2,939	3,357
Permanent diminution in value and reclassifications of Fixed Assets (Note 7)	2,107	-
(Decrease) in provisions for liabilities and charges	-	(500)
Decrease in stocks	4,630	3,689
Decrease in debtors	2,954	7,666
Increase(Decrease) in creditors	(9,017)	(9,574)
Net Cash Inflow from operating activities	9,763	682
Cash Flow Statement		
Net Cash Inflow from operating activities	9,763	682
Returns on investments and servicing of finance (Note 19a)	(519)	(1,042)
Capital expenditure (Note 19a)	4,309	(2,659)
	13,553	(3,019)
Dividend paid	(12,000)	-
Net cash flow before use of liquid resources and financing	1,553	(3,019)
Financing (Note 19a)	(2,154)	(2,154)
(Decrease) in cash and bank balance	(601)	(5,173)
(Decrease) in cash	(601)	(5,173)
Cash inflow from movement in debt	2,154	2,154
Change in net funds (Note 19b)	1,553	(3,019)
Net funds at 1 April 2005	(13,573)	(10,554)
Net funds at 31 March 2006	(12,020)	(13,573)

The notes on pages 30 to 39 form part of these accounts.

ABRO | Accounts (continued)

Notes to the Accounts For the Year ended 31 March 2006

1. Accounting Policies

A. Basis of Accounting

The accounts have been prepared in accordance with the Accounts Direction issued by HM Treasury on 13 January 2006, pursuant to section 4(6) of the Government Trading Funds Act 1973 and in accordance with the Government Financial Reporting Manual (FRM). They follow the accruals concept of accounting and the historical cost convention, modified to include revaluation of Fixed Assets and Stocks as set out in notes D and E below. Subject only to compliance with the requirements set out in the Accounts Direction, the accounts also:

- a. comply with the accounting and disclosure requirements of Companies Act 1985, insofar as they are appropriate and the disclosure and accounting requirements contained in "The Government Financial Reporting Manual" and any other guidance which the Treasury may issue;
- b. comply with generally accepted accounting practice in the United Kingdom (UK GAAP);
- c. comply with the accounting standards issued by the Accounting Standards Board except to the extent that they are advised inapplicable by the Treasury.

B. Value Added Tax

Since the transition to Trading Fund status on 1 April 2002 the Trading Fund has been separately registered for VAT.

C. Turnover

Turnover represents the invoiced value of sales net of VAT.

D. Fixed Assets and Depreciation

- i. Land and Buildings
 - a. Department Estate is treated as an asset of the Trading Fund although legal ownership rests with the Secretary of State for Defence. The policy reflects the Trading Fund's position as the beneficial user of the property.
 - b. An Independent valuation of the Departmental Estate assets of the Trading Fund was carried out at 31 March 2006 by GVA Grimley. The valuations were carried out in accordance with the Statements of Asset Valuation Practice and Guidance Notes Issued by the Royal Institution of Chartered Surveyors. The valuation is on the basis of Existing Use Value except for one site where Depreciated Replacement Cost was adopted and those sites where there is expected to be a significant curtailment or reduction in activities where an Open Market Valuation was adopted.

- c. In order to meet HM Treasury requirements for Current Cost Accounting, assets have been re-valued annually to reflect their current cost, in the years between professional valuations, using indices provided by the Corporate Financial Controller of the Ministry of Defence.

- d. Leasehold property is treated in the manner set out by Statement of Standard Accounting Practice Number 21 (SSAP21). Major refurbishment expenditure is capitalised.

ii. Plant, machinery and vehicles, IT and Comms equipment

- a. Plant, machinery and vehicles, IT and Comms equipment are capitalised where the useful life exceeds one year and the cost of acquisition exceeds £5,000.
- b. A full valuation of all items of plant, machinery and vehicles and IT and Comms equipment held by ABRO was carried out at 31 March 2006 by Messrs GVA Grimley. This valuation was based on Depreciated Reinstatement Cost.
- c. The valuation of capitalised plant and equipment including computers has been reviewed annually using indexation rates provided by Corporate Financial Controller of the Ministry of Defence are applied.

iii. Depreciation

- a. Freehold land is not depreciated.
- b. Depreciation on buildings, plant and equipment and office equipment is calculated to write off the cost or valuation of assets by equal instalments over their estimated useful lives which are periodically reviewed for obsolescence. The lives assumed for the main categories of asset are as follows:

Asset Category	Estimated Useful Life
Buildings	50 yrs
Plant and Equipment	5-20 yrs
Computers	3-5 yrs
Vehicles	5-20 yrs

Where additional Capital Expenditure is made within an existing building the additional expenditure is written off over the remaining life of the existing building.

F. Stocks and Work in Progress

i) Valuation.

Stocks are valued at the lower of cost or net current replacement cost, if materially different, and net realisable value. For work in progress these costs include both direct costs and attributable overheads based on normal levels of activity. Net realisable value is the estimated price at which stocks can be sold in the normal course of business after allowing for all costs to bring them from their existing state to a finished condition.

ii) Provision for obsolete surplus and defective stocks – significant estimation technique.

Provision is made, where necessary, for obsolete, surplus and defective stocks.

The provision is based on 100% provision against the value of any stocks considered to be obsolete. Provision is also made against any surplus stocks. Surplus stocks are estimated on the basis of projected consumption using historical trends. Stock is analysed into four categories based on frequency of usage. Any stock balance remaining in the two lowest usage categories after five years projected usage is the subject of a 100% provision less a nominal amount for disposal proceeds.

G. Pensions

Civilian staff are covered by the provisions of the Principal Civil Service Pensions Schemes (PCSPS). The PCSPS is an unfunded multi-employer defined benefit scheme. However, since ABRO is unable to identify its share of the underlying assets and liabilities it is accounted for as a defined contribution scheme. Contributions are paid to the Paymaster General at rates determined from time to time by Government Actuary. Service personnel are deemed to be on loan to ABRO, which carries no liability for their pension other than insofar as these form a constituent element of the monthly loan service charge paid to the Ministry of Defence for their services.

Full provision for early retirements is normally made in the year of retirement.

H. Foreign Currencies

Assets and liabilities denominated in a foreign currency are translated at the rate(s) of exchange ruling at the balance sheet date. Transactions are recorded at the rate ruling at the time of the transaction. Exchange differences are taken to the Income and Expenditure account.

I. Treatment of Operating Leases

All expenditure incurred in respect of operating leases is charged to operating expenses in the year in which they arise. ABRO has no finance leases.

ABRO | Accounts (continued)

2. Turnover

The analysis of activity by business segment was as follows:

	2005/06 £'000	2004/05 £'000
Sales to MoD	119,695	135,479
Sales to Third Parties	17,248	15,430
Total Turnover	136,943	150,909

All turnover relates to the same class of business i.e. repair, maintenance and overhaul.
There were no discontinued operations in 2005/06 or 2004/05.

3. Cost of Sales and Operating Expenses

	2005/06 £'000	2004/05 £'000
Cost of sales	113,427	136,666
Operating expenses	17,366	18,199
	130,793	154,865

Cost of Sales has been defined as that expenditure which is directly related to services or products being supplied to customers. This will include direct materials and labour and fixed and variable overheads to the extent that they relate specifically to production.

Operating expenses include all costs relating to the general management of the business.

These costs are further analysed by expenditure type as follows:

	Note	2005/06 £'000	2004/05 £'000
Staff costs	4	65,809	66,606
Supplies and services consumed		46,690	72,524
Accommodation costs		7,766	6,916
Depreciation and impairment charges		4,960	3,357
Operating lease and similar hire purchase rentals:			
Plant and machinery		10	5
Other		238	132
Auditors' Fee		70	70
Other expenses		5,250	5,255
Total cost of sales and operating expenses		130,793	154,865

There were no net gains or losses from foreign currency transactions charged.

4. Staff Costs and Numbers

a. Disclosure of information related to Directors is dealt with in the Remuneration Report.

b. The average number of employees during the period was made up as follows:

	2005/06 £'000	2004/05 £'000
Industrial Staff	1789	1858
Non Industrial Staff	594	653
Service Personnel	1	2
Agency temporary and contract staff	107	102
	2491	2615

c. Total staff costs for the year were as follows:

	2005/06 £'000	2004/05 £'000
Salaries, wages and allowances	52,233	54,698
Social security costs	3,963	4,081
Pension costs	8,211	6,036
Agency staff costs	1,402	1,791
	65,809	66,606

One post within ABRO is occupied by a serving member of the Armed Forces. Salary cost for this employee is charged to ABRO by the MoD. Apart from the element included in this charge, ABRO carries no liability for the pension costs of these individuals.

5. Interest Receivable

Interest receivable of £905,000 (2004/05 £503,000) shown on the face of the Profit and Loss Account relates to amounts received from balances held in interest bearing accounts with commercial bankers and with the Paymaster General.

6. Interest Payable

	2005/06 £'000	2004/05 £'000
Interest Payable on loans wholly repayable within five years	-	-
Interest Payable on loans not wholly repayable within five years	1,424	1,545
	1,424	1,545

ABRO | Accounts (continued)

7. Tangible Fixed Assets

	Freehold Land and Buildings £'000	Plant, Machinery & Vehicles £'000	IT & Comms Equipment £'000	Assets in course of construction £'000	Total £'000
Cost or Valuation:					
At 1 April 2005	52,292	19,080	1,112	1,179	73,663
Additions	31	456	478	232	1,197
Disposals	(10,669)	(1,298)	(20)	-	(11,987)
Permanent diminutions in value	(629)	(1,220)	(171)	-	(2,020)
Revaluations	(12,788)	(12,217)	(633)	-	(25,638)
Reclassifications	202	300	588	(1,177)	(87)
At 31 March 2006	28,439	5,101	1,354	234	35,128
Depreciation:					
At 1 April 2005	18,006	12,270	603	-	30,879
Charged	1,446	1,134	359	-	2,939
Disposals	(4,348)	(950)	(20)	-	(5,318)
Revaluations	(15,104)	(12,101)	(845)	-	(28,050)
Reclassifications	-	-	-	-	-
At 31 March 2006	0	353	97	-	450
Net Book Value:					
At 31 March 2006	28,439	4,748	1,257	234	34,678
At 1 April 2005	34,286	6,810	509	1,179	42,784

Valuation

Qualified valuers revalue assets every five years. GVA Grimley carried out an independent valuation as at 31 March 2006. The valuations were carried out in accordance with the Statements of Asset Valuation Practice and Guidance Notes issued by the Royal Institution of Chartered Surveyors. For Land and Buildings the valuation was on the basis of Existing Use Value except for one case where Depreciated Replacement Cost was adopted and three sites where activity levels are expected to be curtailed or significantly reduced for which open market value was used.

For Plant, Machinery and Vehicles and IT and Comms equipment the valuation was based on Depreciated Reinstatement Cost.

In order to meet HM Treasury's requirements for Current Cost Accounting, assets are revalued annually to reflect their current cost using indices provided by the Corporate Financial Controller of the Ministry of Defence.

Whole of Government Accounts

No dwellings are included in Freehold Land and Buildings.

Plant, Machinery and Vehicles includes transport equipment with a net book value of £210,000.

8. Stock

	31-Mar-06	31-Mar-05
	£'000	£'000
Raw Materials and Consumables	18,881	33,698
Work in progress	5,824	5,973
Provision for obsolete and surplus stock	(4,683)	(14,241)
	20,022	25,430

9. Debtors

	31-Mar-06	31-Mar-05
	£'000	£'000
Trade debtors	23,487	31,987
Other debtors	7,828	1,163
Prepayments and accrued income	398	1,549
Provision for bad and doubtful debts	0	(32)
Total Debtors and Prepayments	31,713	34,667

10. Cash at Bank and in Hand

	31-Mar-06	31-Mar-05
	£'000	£'000
Cash in Commercial Bank Current Accounts	5,595	11,182
Current accounts with H.M. Paymaster General	6,081	1,095
Cash in Hand	2	2
	11,678	12,279

11. Derivatives

Interest Rate Risk

ABRO finances its operations through a mixture of retained profits and government borrowings. ABRO borrowings are all at fixed rates of interest, no financial instruments are used to manage ABRO's exposure to interest rate fluctuations.

Liquidity Risk

60% of ABRO's borrowings at the year-end mature in more than five years.

ABRO has access to short term borrowing facilities to ensure short term flexibility.

Foreign Currency Risk

All foreign currency balances at the year end were translated at the exchange rate in operation at the year end. Any exchange rate differences were taken to the Profit and Loss Account. ABRO has incurred expenditure in foreign currencies and these transactions have been translated into sterling at the exchange rate in operation at the date at which the transaction occurred.

There were no derivatives or financial instruments contracted and no hedging transactions during the year.

ABRO has taken advantage of the exclusion to disclose short term debtors and creditors as per FRS 13.

ABRO | Accounts (continued)

12. Creditors: Amounts Falling Due Within One Year

	31-Mar-06 £'000	31-Mar-05 £'000
Loans repayable within 12 months	2,154	2,154
Trade creditors	10,265	19,882
Other creditors	2,058	2,104
Value added tax	4,945	4,193
Other taxes and social security	1,768	1,468
Accruals and other deferred income	7,761	8,167
	28,951	37,968

13. Long Term Loans

Government loan, repayable by instalments, and bearing interest at 5.625% per annum.

	31-Mar-06 £'000	31-Mar-05 £'000
Analysis of repayments:		
Between 1 and 2 years	2,155	2,155
Between 2 and 5 years	6,463	6,463
After 5 years	12,924	15,078
	21,542	23,696

Amounts repayable within one year are included in Creditors.

14. Revaluation Reserves

	2005/06 £'000	2004/05 £'000
Balance as at 1 April	16,401	15,161
Revaluation of Fixed Assets	2,412	1,972
Backlog Depreciation	-	(751)
Revaluation of stocks	(780)	287
Realised element on disposal to General Reserve	(5,771)	(268)
Revaluation Reserve as at 31 March	12,262	16,401

15. General Reserve

	2005/06 £'000	2004/05 £'000
Balance as at 1 April	17,690	22,689
Retained (Loss) for the year	(7,530)	(5,267)
Realised element of the Revaluation Reserve	5,771	268
Balance as at 31 March	15,931	17,690

16. Capital Commitments

	31-Mar-06 £'000	31-Mar-05 £'000
Contracted for but not provided for in the accounts:		
Commitments for capital expenditure	21	126

17. Contingent Liabilities

ABRO has commissioned an environmental survey of the Warminster site as part of the contract for the sale of the site. In the event of the survey revealing environmental problems that require remediation it is possible that ABRO may have to undertake corrective work. The likelihood of ABRO needing to undertake remedial work is considered by ABRO to be low and the extent and cost of any possible works are unknown. However the issue remains a contingent liability at the balance sheet date (2005 Nil).

18. Operating Lease Commitments

	31-Mar-06 £'000	31-Mar-05 £'000
Operating commitments under operating leases (including land and buildings) expiring:		
Within 1 year	532	4
Between 2 to 5 years	405	140
Over 5 years	0	0
Total commitments	937	144

19. Notes to Cash Flow Statement

Note 19(a) Gross cash flows

	2005/06 £'000	2004/05 £'000
Returns on investment and servicing of finance		
Interest received	905	503
Interest paid	(1,424)	(1,545)
	(519)	(1,042)
Capital expenditure		
Payments to acquire tangible fixed assets	(1,197)	(2,672)
Receipts from sales of tangible fixed assets	5,506	13
	4,309	(2,659)
Financing		
Increase in short term borrowings	-	-
Repayment of short term borrowings	-	-
Repayment of long term borrowings	(2,154)	(2,154)
	(2,154)	(2,154)

ABRO | Accounts (continued)

Note 19(b) Gross cash flows

	At 1 April 2005 £'000	Cash Flow in Year £'000	Other Changes in year £'000	At 31 March 2006 £'000
Cash in hand and at bank	12,279	(601)	-	11,678
Bank overdraft	0	-	-	0
	12,279	(601)	-	11,678
Debt due within 1 year	(2,154)	-	-	(2,154)
Debt due after 1 year	(23,698)	2,154	-	(21,544)
Total debt	(25,852)	2,154	-	(23,698)
Net (Debt)	(13,573)	1,553	-	(12,020)

20. Reconciliation of Movements in Government Funds

	2005/06 £'000	2004/05 £'000
1 April - as previously reported	77,192	83,106
Profit for year before dividend	4,470	(5,267)
Revaluation reserve movement in year	(4,139)	1,240
Other movement in retained earnings	5,771	268
Movement in long term loan	(2,154)	(2,155)
Dividend paid	(12,000)	0
Government Funding per Balance Sheet	69,140	77,192

21. Related Party Transactions

The Ministry of Defence is regarded as a related party. During the year ABRO has had a significant number of material transactions with the Department, and with other entities for which the Department is regarded as the parent department.

None of ABRO's Board Members, key managerial staff or other related parties have undertaken any material transactions with ABRO during the year.

22. Post Balance Sheet Events

There have been no post Balance Sheet events.

23. Losses and Special Payments

There were no losses or special payments made during the year ended 31 March 2006.

24. Intra Government Balances

As at 31 March 2006 the analysis of Debtor and Creditor balances was as follows:

	Debtor Balances	Creditor Balances
	£'000	£'000
Central Government	20,342	18,414
Local Government	142	1
NHS Trusts	17	0
Bodies External to Government	11,212	10,536
Total	31,713	28,951

These accounts are included in debtors and creditors respectively.

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