SOPHOS

2019 Annual Report and Accounts

Innovative, simple and highly effective cybersecurity solutions, for organisations of any size

Sophos delivers award-winning endpoint protection harnessing the power of artificial intelligence ("AI"), enabling unmatched defence against malware, exploits, and ransomware. Our network security offers the world's best visibility, protection, and response, powered by deep learning and synchronized security. And we combine the power of AI and automation to simplify compliance, governance, and security monitoring in the public cloud.

At Sophos we know that the solution to complexity is not more complexity. We tackle security challenges with clarity and confidence, knowing that simple security is better security.

Find out more at
www.sophos.com

2019 Highlights

Revenue

+11%

Adjusted Operating Profit

+87%

Business Highlights

- Strong growth in subscription revenue, up 16% year-on-year
- Strong demand for our cloud solutions, with over 135,000 of our customers managing their security via the Sophos Central cloud platform
- Sophos is now established as a leader in the fast-growing market for next-gen cybersecurity solutions, founded on powerful artificial intelligence capabilities
- Renewal rates within the Group's subscription business remain at healthy levels at 124%
- The Group remains well-positioned competitively, with industry-leading technology and a differentiated strategy for synchronized security
- Step change in profitability, reflecting good revenue growth and operating leverage

CHAIRMAN'S INTRODUCTION

Our strategic progress has positioned Sophos as one of the world's leading next-generation cybersecurity vendors.

Despite the challenges we faced in FY19 selling against an exceptional prior-year comparative which resulted in a 1 per cent reduction in billings, our subscription-based business model together with continued demand delivered a 124 per cent renewal rate and 35,000 net new customers, and enabled us to achieve growth of 11.2 per cent in revenue, driven by a 15.9 per cent growth in subscription revenue. Additionally, as we've continued to grow the number of customers deploying both our endpoint and UTM/next-gen firewall to approximately 12.1 per cent, our now 335,000-strong customer base represents a compelling opportunity as we look to continue to increase adoption rates of multiple products across our portfolio.

We continue to prioritise investment in innovation, which has produced important advances this year. Sophos Intercept X Advanced with EDR automates much of the process of active threat hunting via some of the world's most advanced deep learning, neural network-based artificial intelligence. With the latest Sophos XG Firewall, customers are able to manage their Sophos security solutions fully within the Sophos Central cloud platform. These and other innovations, and looking forward, a robust development calendar for the near and medium term, contribute to our evolution – already well underway – to become one of the world's leading next-generation cybersecurity vendors. Already 47 per cent of our FY19 billings came from our next-generation products. As this evolution continues, we believe our differentiated strategy around synchronized security spanning endpoint, network, and public cloud will further drive demand.

We also continue our investments in our sales and marketing operations, emphasising continued partner support, customer service, and productivity. Our strategy of channel partnering along with our relentless culture to serve our customers and partners we believe has enhanced our visibility and market reach, our customer following, and our growth opportunities as we continue to strengthen our next-generation offerings.

Our market continues to show significant demand for cybersecurity solutions across an increasingly complex landscape of devices, networks, and applications in organisations of all sizes. We believe our rigorous and strategic focus on security solutions managed centrally through the cloud, our focus on channel partners serving these customers, our differentiated offerings in the market, our robust product roadmap, our substantial customer base, and the scale and momentum of our next-generation offerings represent powerful ingredients for our continued growth and market leadership.

On behalf of our Board, thank you very much to our Sophos team members and partners around the world for your hard work and dedication to deliver value to our customers and returns to our shareholders. To our partners, customers, and investors, thank you very much for your continued support and confidence. We maintain our relentless focus to keep earning it.

Peter Gyenes

Non-Executive Chairman

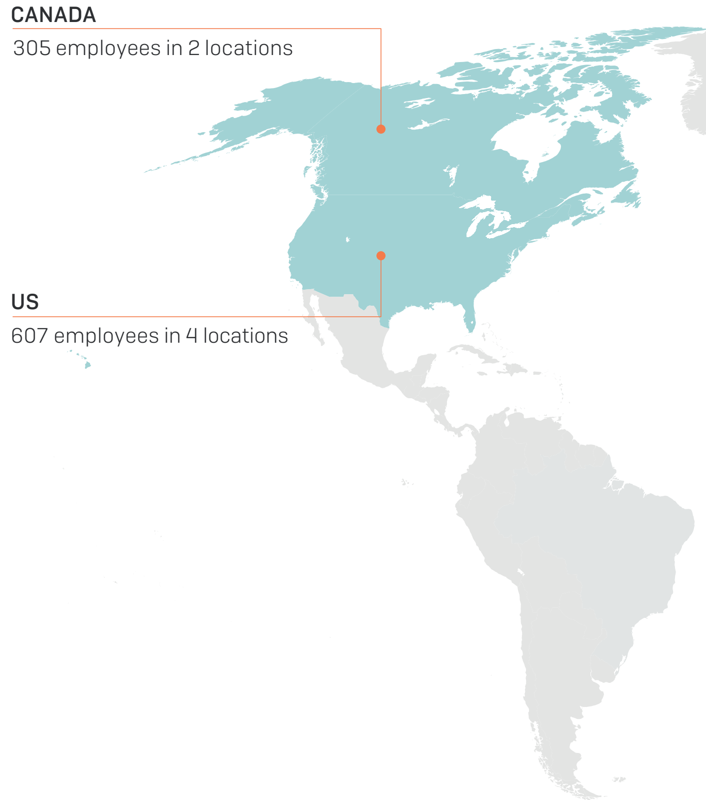
CONTENTS

Find out more at:
www.sophos.com

AT A GLANCE

Cybersecurity evolved, Sophos is a global leader in next-gen

Sophos is at the forefront at a pivotal moment of evolution in the cybersecurity industry. The Group is a global leader in next-gen, cloud-managed network and enduser cybersecurity, and consequently is helping to drive change that is reshaping the market, as it harnesses the power of world-leading artificial intelligence, through deep learning neural networks, to adapt ever more quickly to the emerging threat landscape. At the heart of the strategy lies the concept of synchronized security, where all of the Group's products actively work together in order to provide faster, more accurate detection, and greater levels of automation than ever before.



Geographic footprint

Sophos is a truly global company with more than 50 offices around the world, with major offices in the UK, USA, Canada, India and Germany.

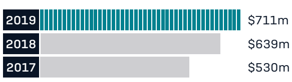
PARTNERS	END USER CUSTOMERS	OFFICES	EMPLOYEES
47,000	382,000	51	3,400

GAAP financial highlights

Revenue

$711m

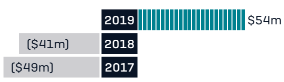
(FY18: $639m)



Profit/(Loss) Before Tax

$54m

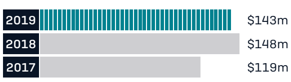
(FY18: ($41m))

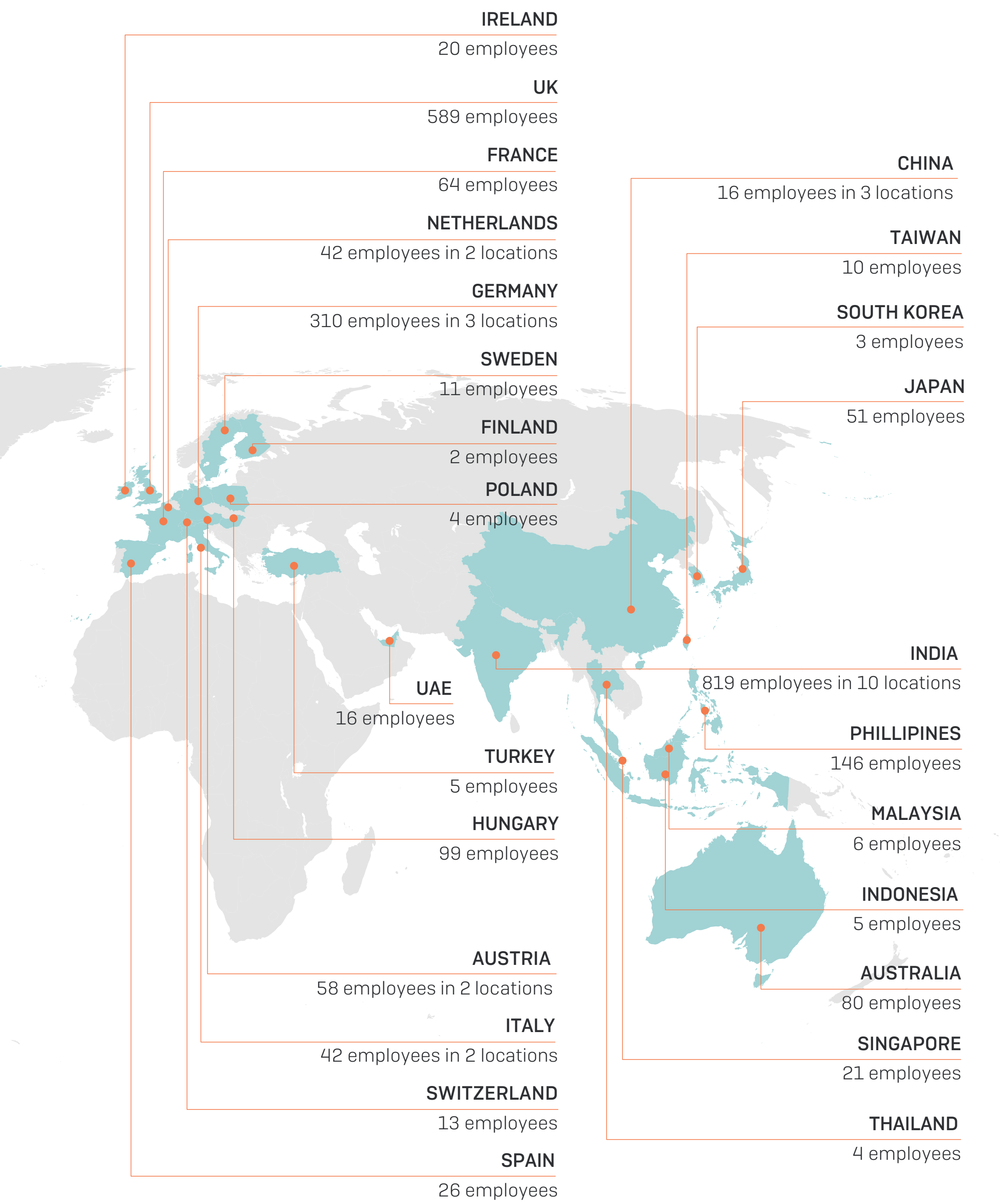


Net Cash Flow From Operating Activities

$143m

(FY18: $148m)





Our 2019 Awards

CIO Choice
Network Security
CIO Choice 2018

CRN
ARC – Annual Report Card awards
Overall Winner – Network Security and Overall Winner – Endpoint Security + Scored 100 for Ease of Doing Business

CRN Germany
Sophos
IT Security Vendor of the Year

CRN UK
Sophos
Security Vendor of the Year

CRN US
Intercept X with Deep Learning
CRN Tech Innovator Award
Intercept X and XG Firewall
CRN Products of the Year

Information Age
Sophos
Employer of the Year

Funkschau
XG Firewall
Product of the Year in category "Cybersecurity"

Computing Security Excellence Awards
Intercept X
Innovation of the Year

Channelnomics
Security Innovation
Security Innovation of the Year

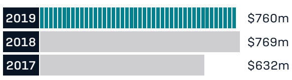
Computer Bild
Sophos
Trusted Solutions Award 2019 in the category "IT Security"

Non-GAAP financial highlights

Billings[1]

$760m

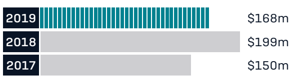
(FY18: $769m)



Cash EBITDA[1]

$168m

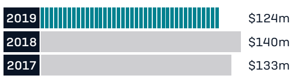
(FY18: $199m)



Unlevered Free Cash Flow[1]

$124m

(FY18: $140m)



1 Definitions and reconciliations of non-GAAP measures are included in note 5 of the Financial Statements and in the glossary

OUR INVESTMENT PROPOSITION

Continued growth in revenue and significant long-term profitability

1. COMPELLING INDUSTRY FUNDAMENTALS

A large, dynamic, growing market opportunity

- Security is consistently the top priority for corporate IT spend
- The total market is estimated to be worth around $43 billion, growing at around 8 per cent per annum, within which the Group's products address markets growing even faster
- The cybersecurity threat environment is constantly evolving in scale and sophistication, presenting new challenges at a rapid pace to organisations of all sizes
- Sophos is well-positioned to take advantage of opportunities as a leader in high growth areas, for example next-generation endpoint, cloud, network, and synchronized security

Total cybersecurity market

$43B

See Our Markets for further information on page 14

2. DIFFERENTIATED STRATEGY

A clear and compelling strategy

- Sophos is solely focused on cybersecurity and we strive to deliver industry-leading technology that is simple to deploy, use and manage
- Sophos offers enterprise-grade technology, independently rated as amongst the best in the industry, appropriate to enterprises of any size, including SMEs with fewer resources
- The Group's sales strategy is 100 per cent "channel first" and as a result of considerable investment the Group now has more than 46,000 global partners

Proportion of customers with <5,000 employees

86%

See Strategic Framework for further information on page 18

3. SaaS SUBSCRIPTION FINANCIAL MODEL

High recurring revenues and renewal rates

- Sophos principally sells Software as a Service ("SaaS") via both recurring, upfront subscription billings and increasingly through monthly MSP billings, which provide significant visibility and stability of future revenues and are increasing the focus of the Directors on Revenue and Adjusted Operating Profit measures
- The Group has a proven ability to deliver consistent new customer growth and maintain strong renewal rates
- The business generates significant cash flows which are reinvested to drive future growth, via innovation, building brand awareness, and sensible acquisitions
- The total renewal base now exceeds $1.2 billion

Proportion of revenue from subscriptions

84%

See Financial Review for further information on page 28

4. THE SOPHOS BRAND

Innovative, simple and highly effective security

- Sophos is very proud of our brand and the ethos of simplicity that it represents – which spans all that Sophos does
- The Group employs a highly creative digital marketing approach, utilising educational in-person events and social media outreach
- With one of the world's leading threat intelligence operations, SophosLabs, and a reputation for excellence built over many years, Sophos is a trusted voice in the world of cybersecurity

Annual sales and marketing investment

$260m

5. OPPORTUNITIES FOR GROWTH

An expectation to continue to outperform the IT security market

- Differentiation is a key driver of market share gains
- Innovation will remain a key growth driver, with internal investment supplemented by sensible, disciplined technology acquisitions
- Despite a broad international reach, the Group sees opportunities for further regional expansion
- Synchronized security lies at the heart of an integrated product portfolio, delivered via the cloud in Sophos Central, and provides significant cross-sell and upsell opportunities
- Sophos is focused on continuing to build its partner network and increasing sales productivity

Net renewal rate

124%

See Our Markets
for further information on page 14

6. EXPERIENCED MANAGEMENT TEAM

Consistently delivering against strategic goals

- Strongly motivated team with the background and skills to deliver profitable growth over the long term
- Extensive experience in running large technology businesses, typically with more than 20 years of experience in their respective fields
- Completely aligned in driving forward the Sophos vision and strategy of innovative, simple, and highly effective security

Threat landscape

The seven uncomfortable truths of endpoint security

Four out of five organisations are struggling with threat detection and response due to lack of security expertise.

The results of a recent independent report (Seven Uncomfortable Truths of Endpoint Security[1], March 2019), commissioned by Sophos to better understand the realities of endpoint security today, showed that one of the key challenges in stopping today's advanced attacks is the lack of the specialist cybersecurity skills to address them.

While organisations recognise they need better help, addressing this skills shortage is no easy task, with 79 per cent of respondents citing cybersecurity recruitment as a challenge. Putting the necessary teams in place is an uphill battle, and organisations are increasingly looking to technology, such as artificial intelligence, to fill in the gaps.

Endpoint Detection and Response ("EDR") has swiftly become must-have technology and nine in ten plan to add it to their defences, with 61 per cent planning to do so within the next six months. Sophos believes this makes sense, as EDR helps to reduce the time spent investigating security incidents and increases visibility into the threat chain. Interestingly, EDR has become a tool for all, and we see almost equal demand from both smaller and larger organisations.

Find out more at:
[1]www.sophos.com/truths

For more information see page 08

Strategic Report

KEY PRODUCT AND TECHNOLOGY DEVELOPMENTS

IT security experts have first-responder forensics at their fingertips with endpoint detection and response

Endpoint Detection and Response ("EDR")

Intercept X Advanced with EDR powered by deep learning technology delivers faster, more extensive threat discovery.

START WITH THE STRONGEST PROTECTION

To stop breaches before they start, prevention is crucial. Intercept X consolidates unmatched protection and endpoint detection and response into a single solution. This means that most threats are stopped before they can ever cause damage and Intercept X Advanced with EDR provides additional cybersecurity assurance with the ability to detect, investigate, and respond to potential security threats.

ADD EXPERTISE NOT HEADCOUNT

Intercept X Advanced with EDR replicates the tasks normally performed by skilled analysts, so organisations can add expertise without having to add staff. Unlike other EDR solutions which rely on highly skilled human analysts to ask questions and interpret data, Intercept X Advanced with EDR is powered by machine learning and enhanced with curated SophosLabs threat intelligence.

GUIDED INCIDENT RESPONSE

Intercept X Advanced with EDR allows administrators to answer the tough questions about security incidents by providing visibility into the scope of an attack, how it started, what was impacted, and how to respond. Security teams of all skill levels can quickly understand their security posture thanks to guided investigations which offer suggested next steps, clear visual attack representations, and built-in expertise.

Sophos' deep learning neural network is trained on hundreds of millions of samples to look for suspicious attributes of malicious code to detect never-before-seen threats. It provides broad, expert analysis of potential attacks by comparing the DNA of suspicious files against the malware samples already categorised in SophosLabs.

Until now, effective investigation and incident response has only been achievable in organisations with a dedicated security operations center ("SOC") or specialised IT security team trained to hunt and analyse cyber-attacks. With Sophos Intercept X Advanced with EDR, businesses of all sizes, and those with limited resources, can add threat tracking and SOC-like capabilities to their security defences, reducing the time criminal hackers can hide in their network.

With a single click, IT managers have on-demand access to curated intelligence from SophosLabs, guided investigations into suspicious events, and recommended next steps. To maintain full visibility into the threat landscape, SophosLabs tracks, deconstructs, and analyses 400,000 new and previously unseen suspicious files and attack components each day. By providing access to SophosLabs data, IT managers of all skill levels have first-responder forensics at their fingertips to best determine if and what types of attacks are happening.

Product timeline

2012	2013	2015	2016
Mobile Control launched	Sophos Central launched	Synchronized Security launched First XG Firewall launched	Mobile Control became Sophos Mobile Sandboxing integrated into XG Firewall Intercept X launched Sophos Email launched Sophos Central Device Encryption Sophos Wireless launched

Sophos XG Firewall

In November 2018, Sophos released the latest version of its XG Firewall introducing another industry first: Lateral Movement Protection, to prevent cyber-attacks or exploits from spreading and infiltrating further into a compromised network. XG Firewall integration into Sophos Central further strengthens the value and benefits of the Sophos ecosystem as it simplifies management for Sophos customers while bolstering protection by easily enabling synchronized security.

Sophos for AWS, Azure, and Google Cloud

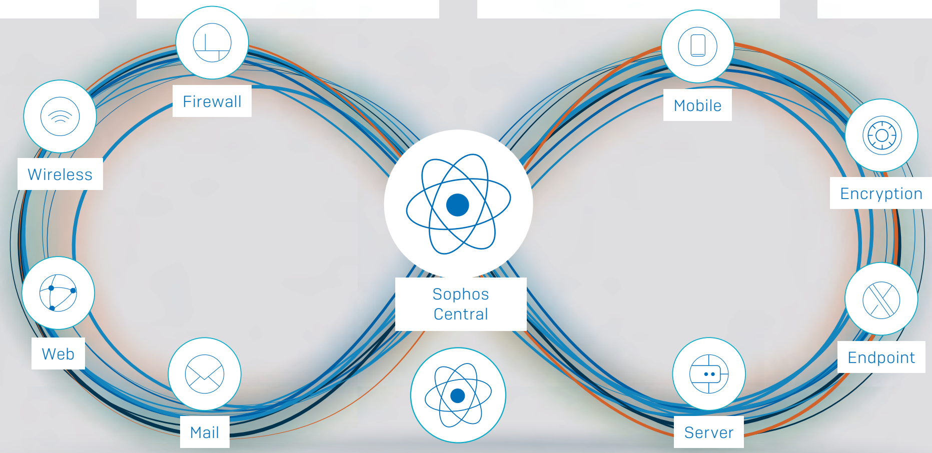
Sophos provides server and network security for hosted environments in Amazon Web Services, Microsoft Azure, and Google Cloud Platform. To enhance the protection across public cloud environments, Sophos Cloud Optix offers an artificial intelligence-based cloud security analytics, compliance, and DevSecOps platform to provide effective end-to-end protection in public cloud services such as AWS, Azure, and Google.

Sophos Wireless

New versions of the APX series of wireless access points were released, along with synchronized security support when used in combination with Sophos Intercept X and Sophos Mobile managed in Sophos Central. Since February 2019, customers now also have the flexibility to choose between managing their APX Series access points in either Sophos Central or XG Firewall, broadening the addressable market in this space considerably.

Sophos Email

Sophos Email is email security delivered simply through Sophos Central's easy-to-use single management console, protecting users from unwanted and malicious email threats today, and tomorrow, with the latest artificial intelligence to defend against ransomware and zero-day malware.



Sophos Central

Sophos provides the ability for remote management and deployment of all Sophos products through a single integrated cloud-based management console, Sophos Central. This is an industry first as Sophos is the only vendor to offer both a leading Firewall and Endpoint solution managed from the same cloud console.

Sophos Intercept X

In October 2018, Sophos added EDR to its award-winning Intercept X Advanced product. With Sophos Intercept X Advanced with EDR, businesses of all sizes and those with limited resources can add threat tracking and SOC-like capabilities to their security defences, reducing the time criminal hackers can hide in their network.

Sophos Intercept X for Server

In July 2018, Sophos released Intercept X for Server, next-generation server protection with predictive deep learning technology that provides constantly evolving security against cyber threats. Combined with synchronized security intelligence sharing and easy management from Sophos Central, Intercept X for Server is a powerful addition that helps defend businesses from becoming the next victim.

Sophos Mobile

Sophos Mobile is built natively in Sophos Central, making it the only Unified Endpoint Management ("UEM") and Mobile Threat Defense ("MTD") solution in the world that is an integral part of a leading next-gen cybersecurity platform. Includes best-in-class protection for mobile devices using the same deep learning technologies found in Sophos Intercept X.

Sophos Phish Threat

Sophos Phish Threat security awareness and computer-based training provides a unique window onto the organisation, and its employees susceptibility to attack, through regular phishing simulation and engaging training. Phish Threat stands out in the market by integrating with Sophos email through Sophos synchronized security to allow IT security teams to identify at-risk users within the organisation and train them to identify, and not click on phishing attacks.

View more information on our website
www.sophos.com

2017

Phish Threat launched
XG Firewall introduced Synchronized App Control
Intercept X added deep learning

2018

Phish Threat integrated into Sophos Central
Intercept X for Server released
New WiFi Access Points launched – APX Series
Wireless added Synchronized Security
XG Firewall added Cloud App Visibility
Intercept X added EDR

2019

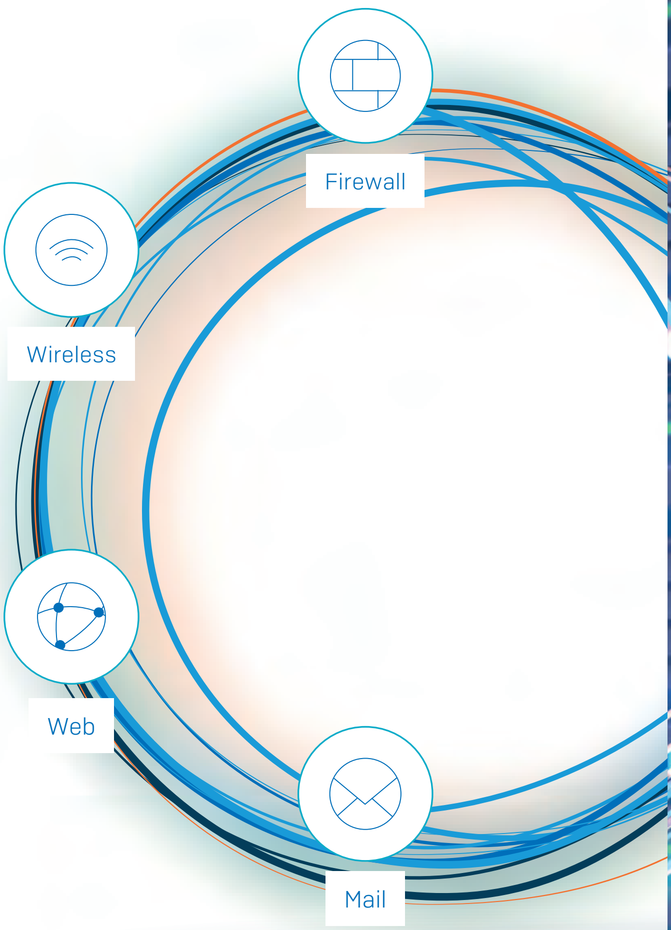
XG Firewall integrated into Sophos Central
XG Firewall introduced Lateral Movement

Spotlight on

Network security

Sophos XG Firewall provides unprecedented visibility into a company's network, its users, and its applications directly from the control centre.

With cybercriminals constantly finding new ways to infiltrate a system, it's crucial that businesses protect their networks with a security system that exposes blind spots. Having visibility into what's on the network is critical to detecting and preventing breaches. Sophos has innovated key technology advancements to provide customers with unmatched visibility and protection. Hackers can be stopped as they attempt to move laterally within networks and provide IT managers with visibility into the different, potentially risky, applications employees are knowingly or unknowingly downloading onto their systems. Sophos also knows how important it is for security layers to talk and share intelligence. With synchronized security, Sophos network and endpoint security talk to each other, isolating infected devices automatically and stopping cybercriminals in their tracks. With the recent announcement of Sophos Central management of XG Firewall, partners and organisations now have the added benefit of synchronized security on the cloud-based management platform. This allows them to manage their next-gen network and endpoint protection from a single pane of glass, accelerating threat detection and response.



"Get rich on-box reporting and the option to add Sophos iView for centralised reporting across multiple firewalls"

GARTNER MAGIC QUANDRANT	NSS LABS
Leader	Recommended

MQ Leader
Gartner, "Magic Quadrant for Unified Threat Management (SMB Multifunction Firewalls)," Rajpreet Kaur, Claudio Nevia, 20 September 2018

NSS Recommended
NSS Labs, "Next Generation Firewall Test Report – Sophos XG Firewall 750 SFOS v17.0.7 MR7," Devon James, Michael Shirley, Tim Otto, 13 September 2018

Spotlight on

Enduser security

Intercept X delivers unmatched protection against unknown malware, exploits, and ransomware by combining cutting-edge technologies, such as deep learning and endpoint detection and response.

"Intercept X uses a deep learning neural network that works like the human brain"

GARTNER MAGIC QUADRANT	SE LABS ENTERPRISE ENDPOINT PROTECTION	SE LABS SMALL BUSINESS ENDPOINT PROTECTION	MRG EFFITAS EXPLOIT PROTECTION	MRG EFFITAS MALWARE PROTECTION
Leader	AAA rated	AAA rated	#1	#1
MQ Leader Gartner, "Magic Quadrant for Endpoint Protection Platforms," Ian McShane, Avivah Litan, Eric Ouellet, Prateek Bhajanka, 24 January 2018	**SC Labs AAA rated** SC Labs, "Enterprise Endpoint Protection Apr – Jun 2018"	**SC Labs AAA rated** SC Labs, "Small Business Endpoint Protection Apr – Jun 2018"	**MRG #1 exploit** MRG Effitas, "Exploit and Post-exploit Protection Functionality Test," 24 May 2018	**MRG #1 malware** MRG Effitas, "Comparative Malware Protection Assessment," 28 February 2018

The endpoint, be it laptop, server, or mobile device, is the ultimate target for cyber attackers. Once they get a foot hold, cybercriminals use multiple methods to escalate privileges, steal data, or move laterally to move valuable systems. This is why prevention is key. Sophos uses deep learning and endpoint detection and response ("EDR") to predict, prevent, and protect against threats. Like Sophos' network security, its endpoint security solutions, including Intercept X, synchronise to provide added intelligence and immediate action. By working together, these security components can provide businesses with more control and improve their defences from persistent and determined attackers. Specifically, with Sophos Intercept X with EDR, Sophos' latest endpoint offering, businesses of all sizes can add threat tracking and SOC-like capabilities to their security defences. Intercept X with EDR compares the DNA of suspicious files against malware samples already categorised in SophosLabs, accelerating detection. IT managers also have on-demand access to curated threat intelligence, which allows them to better understand and decipher whether a potential attack is underway and where it's happening. When time is of the essence to interrupt an attack or prevent an adversary from moving deeper into the network, Sophos endpoint security is essential.

OUR MARKETS

The threat landscape is evolving along with security technologies; advanced protection supported by machine learning is highly effective at stopping attacks from the less skilled cybercriminals and forcing those who are both motivated and able to significantly increase their attack vectors and methods

IT SECURITY MARKET[1]

TAM

$43B

CAGR

8.4%

Cybersecurity strategies within all organisations must evolve to address these smarter and stronger adversaries.

In 2018 there was a significant advancement in hand-delivered, targeted ransomware attacks that reaped multi-million-dollar gains. Targeted ransomware is more damaging than a 'spray and pray' campaign as human attackers can stake out victims, think laterally, trouble shoot obstructions, and wipe out back-ups so the ransom must be paid. This interactive and intelligent attack style where adversaries manually manoeuvre through a network step-by-step is increasing in popularity. Sophos experts believe the financial success of SamSam, BitPaymer, and Dharma will inspire more targeted attacks and expects reports of more in 2019.

Cybercriminals are using readily available Windows systems administration tools. This is a shift in threat execution, as more attackers employ advanced persistent threat ("APT") techniques to exploit the capabilities of essential and built-in IT admin tools including PowerShell files and Windows Scripting executables as their route to advance through a system.

By creating a sequence of different script types, hackers can instigate a chain reaction before IT managers even detect that a threat is on the network. Once started it's difficult to stop the payload from executing.

In 2018 there was a continued increase in malware for Android phones, tablets, and Linux-based IoT devices. As homes and businesses deploy more internet-connected devices, criminals are exploiting them to use as nodes in huge botnet attacks. VPNFilter demonstrated how malware can affect embedded systems and devices that have no obvious user interface. Other automated attacks hijacked devices to use for DDoS attacks, to mine cryptocurrency, and infiltrate networks.

The scale of the cybercriminal industry has reached a point where organisations have to assume that they have been attacked on some level and focus on achieving the greatest levels of network visibility with advanced detection and response technologies.

CORPORATE ENDPOINT SECURITY[2]

TAM

$7.6B

CAGR

8.6%

ADDITIONAL CROSS-SELL

Encryption[3]

$0.7B

Email Security[1]

$2.5B

Web Security[1]

$3.5B

Enterprise Mobility Management[4]

$3.2B

UTM AND NEXT-GEN FW[5]

TAM

$12.5B

CAGR

10.0%

1 Worldwide IT Security Products Forecast, 2018–2022: Do You Make Friends or Acquire Technology to Round Out a Portfolio? (August 2018, IDC #US44182918) and represents expected market size in 2019

2 Worldwide Corporate Endpoint Security Forecast, 2018–2022 (July 2018, IDC #US43992718) and represents expected market size in 2019

3 Worldwide Endpoint Encryption Forecast, 2018–2022 (May 2018, IDC #US43488218) and represents expected market size in 2019 expressed in $B

4 Worldwide Enterprise Mobility Management Software Forecast, 2018–2022 (September 2018, IDC #US43984018) and represents expected market size in 2019

5 Worldwide Network Security Forecast, 2018–2022: Hybrid and Multicloud Driving Investment in Core Technologies (July 2018, IDC #US44154217) and represents expected market size in 2019

OUR BUSINESS MODEL

Competitively well-positioned, with industry-leading technology, and a differentiated strategy

Resources and relationships

TALENTED AND MOTIVATED EMPLOYEES

Sophos is privileged to count some of the most talented individuals in the cybersecurity industry among its employees

CULTURE OF INNOVATION

We continually innovate and evolve in order to provide effective protection for our customers against a rapidly evolving threat landscape

STRONG PARTNER RELATIONSHIPS

Our network of over 45,000 partners is a key asset of our business, and we are independently recognised for the high-quality program offerings we deliver to our channel

MARKET LEADING REPUTATION

Sophos has capitalised on its long heritage and is now firmly established as a clear leader in the market for next-gen cybersecurity solutions, independently recognised for our technology strengths

STRATEGY

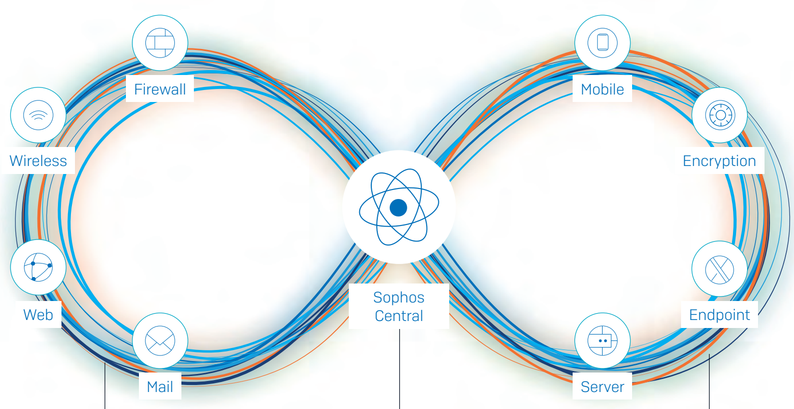
Grow through channel partners. Maintain technology leadership. Operate responsibly

GOVERNANCE AND RISK MANAGEMENT

Sophos is committed to good corporate governance, in order to build a successful business that is sustainable over the long term

How we create value

Products and platform



NETWORK SECURITY

- Comprehensive next-gen firewall protection that blocks unknown threats, automatically responds to incidents, and exposes hidden risks on your network
- Enterprise grade secure Web, Wireless Network and cloud Email protection, which is simple and easy to use

See our focus spread for further information on page 10

ENDUSER SECURITY

- Advanced endpoint protection, combined with signatureless anti-exploit, anti-ransomware, and root cause analysis to protect endpoints from advanced threats
- Comprehensive Enterprise Mobility Management, Server Security, and data protection

See our focus spread for further information on page 13

Sophos Central

Sophos Central is a unified cloud administration console for managing all Sophos products. Customers benefit from improved security effectiveness, the ability to manage their security via a single integrated cloud console, and powerful synchronized security features

Design products for organisations of any size
Our enterprise-grade cybersecurity solutions are designed for use by organisations of any size, being simple and easy to deploy for smaller enterprises with fewer resources

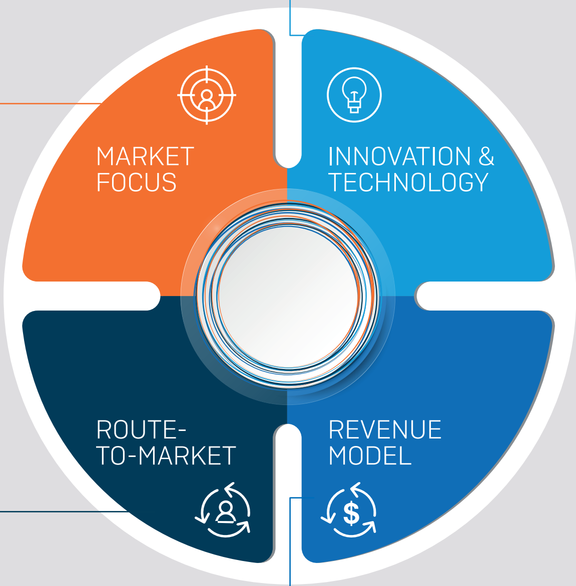
Pioneering synchronised cybersecurity
Sophos combines an intuitive security platform with award-winning products that actively work together as a security system, providing enhanced security

See our technology spread for further information on page 08

Product and platform development
Sophos is investing to deepen and broaden a synchronized security vision, where its products are able to share information in real-time, with unmatched levels of speed, detection and automation

Zero trust
Sophos is investing to ensure its solutions enable highly secure computing in a world where the perimeter has vanished and there is no longer the concept of a safe, internal network

See our technology spread for further information on page 08



Channel 'First'
Sophos only sells through its channel of more than 45,000 partners around the world

Channel 'Best'
In a recent independent survey, Sophos was recognised as being in a unique position to provide synchronized security, and ranked highest in all sub-categories*

See our technology spread for further information on page 08

Revenue types:
Subscription
The majority of the business comes from annual recurring subscription revenues

Hardware and other
Other revenue streams include the hardware related to firewall appliances and a small amount of services revenue

See our technology spread for further information on page 08

* CRN's 2018 Annual Report Card (ARC) Awards)

Stakeholder outcomes

CUSTOMERS
Customers benefit from comprehensive, integrated, enterprise-grade security and our commitment to continual innovation

124%
Net renewal rate

EMPLOYEES
We are committed to enabling our employees to do the best work of their careers at Sophos, through active employee engagement

83%
Employee engagement survey participation

PARTNERS
We continue to make a significant investment in our partner network, providing the tools, training, and support to enable them to succeed

c.8,000
'Blue chip' partners

SHAREHOLDERS
Strong growth in subscriptions, including upsell and cross-sell, allows for ongoing investment in growing our business and strong operating cash flow

42%
Three year total shareholder return

STRATEGIC FRAMEWORK

Innovative, simple, highly-effective, cloud-managed cybersecurity for enterprises of any size

1. MAINTAIN TECHNOLOGY LEADERSHIP

Focused on cybersecurity, and with a commitment to the cloud, Sophos prioritises investment to deliver new capabilities and products at a rapid pace to maintain its independently-ranked leadership position.

Priorities

Efficient investment in research and development to ensure a strong product roadmap, enabling Sophos to evolve with the changing threat landscape.

Promote a culture of innovation throughout the business, to create and capture intellectual capital, and attract leading talent.

Disciplined approach to technology acquisitions to expand the product offering, gain technical expertise, and bolster internal development efforts.

Channel education to support and enable channel partners, improving their expertise across the Sophos product platform, and helping them to transition customers to our next-gen cloud technologies.

2. CHANNEL 'FIRST', CHANNEL 'BEST'

Sophos is committed to its channel only sales strategy, with a global partner ecosystem that has grown to more than 45,000 channel partners, with close to 8,000 'blue-chip' partners demonstrating higher levels of productivity.

Priorities

Strengthen existing partner relationships and increase partner productivity through investment in tools, training, support and education.

Optimise incentives for product and cloud transition to drive further uptake of Sophos Central, improve retention rates, product penetration and average customer spend, and help partners grow their managed service ("MSP") businesses.

Further regional expansion of partner network to drive additional growth, enabling Sophos to efficiently scale and capture the global opportunity in our chosen markets.

Maintain best-in-class renewal rates by improving retention rates and successfully cross-selling additional products at the point of customer renewals.

3. OPERATE RESPONSIBLY

Efficiently grow and scale the business through responsible investment and engagement with all stakeholders, including our people, customers, partners and investors.

Priorities

Financial discipline:

- Focus on cost control, operating margin leverage, and working capital management.
- Bolster returns through value-enhancing investment in innovation and technology acquisitions.

Corporate responsibility framework:

- Securing customers.
- Engaging employees.
- Enhancing communities.
- Protecting the environment.

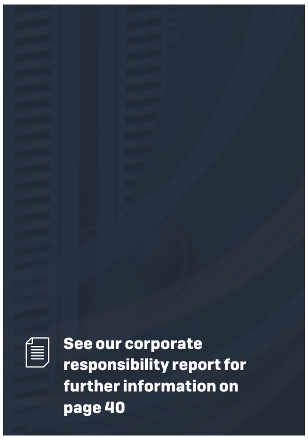
$144M R&D expenditure all charged to Income Statement	188K Customers using next-gen products	140K Customers on Sophos Central cloud platform

See our technology spread for further information on page 08

45K Total number of channel partners	c.8K 'Blue chip', most productive partners	47K MSP customers
35% Subscriptions in Sophos Central cloud	124% Net renewal rate, including upsell and cross-sell	25% Customers with more than one product

See www.sophos.com/partners for further information

$711M Revenue	$109M Adjusted operating profit	$143M Net cash flow from operating activities
3,400 Number of employees	86% Overall employee satisfaction	87% Employee retention rate



See our corporate responsibility report for further information on page 40

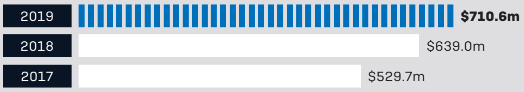
KEY PERFORMANCE INDICATORS

The Group makes use of a number of key performance indicators ("KPIs") to measure its performance against the Group's strategy, as well as providing key inputs into modelling of future performance. Definitions of KPIs are included in the glossary and further explanation and reconciliation of non-GAAP measures are included in Note 5 of the Financial Statements. As the mix of the Group's business transitions over time toward "cybersecurity as a service", the Directors continue to evaluate which indicators best reflect underlying activity. In this respect, the Directors are now increasingly focussing on both Revenue and Adjusted Operating Profit on a more regular basis and may consider promoting these to full KPIs in future reporting periods. In FY19, Annual Recurring Revenue was $631.3 million and Adjusted Operating Profit was $109.0 million.

Revenue

$710.6M

(FY18: $639.0m)



Revenue reflects the element of billings recognised in the period. The majority of billings are for subscription contracts that are recognised rateably over the contract term.

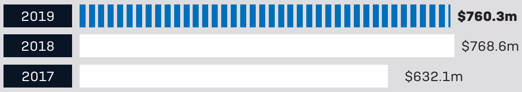
Performance

Strong growth as prior-period subscription billings are now converting to revenue.

Billings

$760.3M

(FY18: $768.6m)



Billings represents the value of goods and services invoiced to customers and is a key leading indicator of future revenue performance.

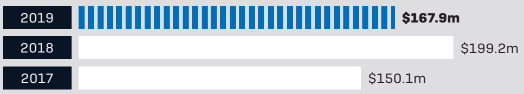
Performance

Billings remain at prior-year levels which reflects a challenging comparative, where Enduser product demand had been significantly boosted by the high-profile ransomware attacks in 2017.

Cash EBITDA

$167.9M

(FY18: $199.2m)



Cash EBITDA provides visibility of earnings from the period, even if the associated revenue for that period's billings have not yet been recognised.

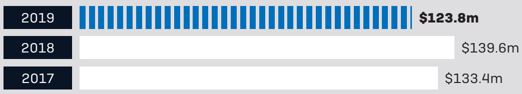
Performance

Cash EBITDA margins decrease as overheads, particularly sales and marketing expenditure, increased year-on-year as the Group continues to invest in future growth.

Unlevered Free Cash Flow

$123.8M

(FY18: $139.6m)



Unlevered free cash flow represents the amount of cash generated by operations after allowing for capital expenditure, taxation and working capital movements.

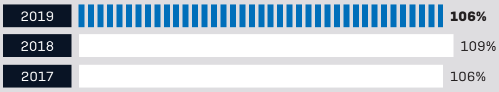
Performance

Reduction due to reduced cashflow from exceptional items and operating activities.

Retention Rate

106%

(FY18: 109%)



Retention rate, after upsell and cross-sell, is a measure of long-term value of customer agreements and the Group's ability to retain end users.

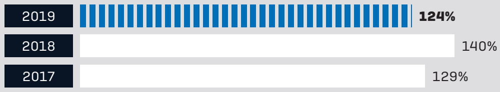
Performance

Steady retention rate reflecting sustained billings and an increase in cross-sell.

Renewal Rate

124%

(FY18: 140%)



Renewal rate, including upsell and cross-sell, measures the ability of the Group to retain end users in period and expand the nature or volume of products used by them.

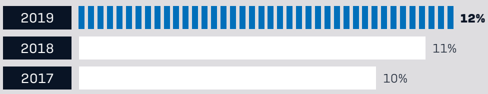
Performance

Reduction on prior-year, which was boosted by the impact of ransomware attacks, though rate continues to be strong reflecting the effectiveness of the cloud strategy and cross-sell opportunities.

Endpoint/UTM Cross-sell

12%

(FY18: 11%)



The continued growth of the business partly depends on successfully selling additional products and services to existing customers.

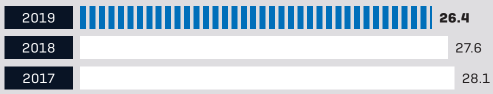
Performance

Continued improvement in cross-sell rate as the Group has demonstrated the benefit of synergies in management, support, and functionality, primarily through Sophos Central.

Weighted Average Contract Length

26.4

(FY18: 27.6)



The weighted average contract length, measured in months, gives the Group an indication of the period over which future revenue will be recognised.

Performance

Reduced weighted average contract length, due to fewer larger deals and the growth in monthly billings to new customers from the MSP business.

“FY19 was a challenging year, primarily due to a difficult compare. However, we are pleased with the strategic progress we made during the year as we drive Sophos’ transition to be a market leader in next-generation cybersecurity”

Kris Hagerman
Chief Executive Officer

CHIEF EXECUTIVE’S STATEMENT

Next-gen Billings Growth	Total Subscription Base
30%	$1.2B
(FY18: 114%)	(FY18: $1.1B)

For the fiscal year 2019 (“FY19”), Sophos delivered an 11.2 per cent increase in total revenue (12.0 per cent at constant currency), driven by a 15.9 per cent (16.7 per cent at constant currency) increase in subscription revenue. Profitability improved significantly, with 87 per cent growth in adjusted operating profit. The Group also reported a profit before taxation of $54 million and operating cash conversion remained strong.

We continued to see healthy growth in our customer base, and closed the year with over 335,000 term customers, having added more than 35,000 net new term customers in FY19. Growth in MSP was particularly strong, with 119 per cent growth and ARR now at $27 million. When including our MSP program, our customer base now exceeds 382,000. Importantly, we saw continued strong demand for our next-gen security solutions, consisting of our most advanced products, managed in our Sophos Central integrated cloud management platform, including Intercept X for endpoint security, and XG Firewall for network security. Our next-gen business grew 30 per cent at constant currency to $340 million and represented 47 per cent of FY19 billings.

Evolution to security as a system

1985

Peter Lammer c1985

Jan Hruska c1985

Founded in Abingdon (Oxford), UK

1988

FIRST checksum-based antivirus software

1989

FIRST signature-based antivirus software

1996

Voted **BEST** small/medium sized company in UK

US PRESENCE established in Boston

Billings were broadly unchanged year-over-year, principally reflecting a return to more traditional levels of cross-sell activity in our Enduser security business that had seen unusually elevated levels of demand and growth in the comparative period, due to a new product release and high-profile global ransomware outbreaks. This is reflected in the headwind we saw to the renewal rate, which declined to 124 per cent in FY19, compared to 140 per cent in the prior-year. We saw lower hardware sales in the year in our Network business, as customers extended refresh cycles; however, Network customer subscription renewal rates remained healthy. During the year we experienced a shift in the billings mix, with somewhat fewer large multi-year deals combined with stronger growth in smaller customers particularly driven by our MSP business, which typically generates monthly billings, as opposed to traditional term contracts with an average duration of 26 months.

The world of cybersecurity is changing rapidly, driven by more attackers, using more sophisticated approaches, in an overall technology landscape that itself is undergoing radical change: public cloud infrastructure, SaaS, AI, zero-trust networks, 5G, IoT, security delivered as a service, etc. If cybersecurity solutions are to be effective today and looking forward, they must continue to evolve – and rapidly. Sophos has fully embraced this challenge, and we are proactively driving an exciting transition to next-gen security across our product line, and across our customer and partner base.

Transition to next-gen cybersecurity

We started our next-gen business roughly five years ago literally from zero. At the close of FY19, our next-gen business generated over $340M in billings from over 175,000 customers, 47,000 of which were through MSPs. Today Sophos is one of the clear industry leaders in next-gen cybersecurity, and in Q4, FY19 we added more than 11,000 net new customers to our next-gen security portfolio. And it didn't happen overnight. During the past five plus years, we have steadily made next-gen cybersecurity a strategic and operational priority:

- We shifted our entire company to fully embrace the cloud
- We took all our most advanced, flagship products and enabled them to be managed in a single, integrated cloud-based management console called Sophos Central
- We pioneered a concept called "synchronized security", where different cybersecurity products, especially across endpoint and network, actively communicate with each other to deliver both better security and better manageability
- We committed to be a world leader in applying AI, and especially deep learning neural networks, to the discipline of cybersecurity

2007 Acquired ENDFORCE

2008 Acquired Utimaco Safeware AG

2011 Acquired astaro

2012 Acquired DIALOGS

CHIEF EXECUTIVE'S STATEMENT CONTINUED

Subscription Revenue Growth

16%

(FY18: 25%)

Recurring Subscriptions Net Renewal Rate

124%

(FY18: 140%)

We are now seeing the impact of those investments in the scale, growth, and robust product roadmap associated with our next-gen offerings. Our next-gen portfolio is the future of Sophos, and as our business fully transitions to next-gen over time, we believe there will be multiple and significant benefits to Sophos, our customers, and our partners:

- Advanced capabilities. Our next-gen products leverage cutting-edge capabilities, including artificial intelligence and synchronized security, to deliver enhanced security that is at the same time easier to manage.
- Robust platform for innovation. Our next-gen products feature modern architectures that are more modular, scalable, and open – which means we can innovate faster. And as we focus more of our product development resources on our next-gen portfolio, we can advance them faster vs. competitors.
- Improved metrics. Our business metrics for our next-gen products managed in Sophos Central are consistently stronger than their traditional counterparts: higher customer satisfaction, higher retention rates, higher levels of upsell and cross-sell, lower operating costs for our partners, etc.
- Opportunity for margin leverage. Our next-gen portfolio is rapidly increasing its share of our total Sophos business. As it does so, over time we can streamline our product development, go-to-market, support, and back office investments to focus on fewer products.

Strategic innovation priorities

We are excited about the opportunity to continue to drive Sophos' evolution into a fully next-gen cybersecurity company – which is already well underway – and to lead the industry in applying next-gen technologies and business models to deliver better protection for customers that stays ahead of the ever-changing threat landscape, and at the same time is easier to manage and administer. We are making strategic investments in a variety of areas:

1. Synchronized security. Several years ago, we introduced the concept of synchronized security – in which multiple Sophos products, including endpoint, firewall, server, mobile, email, and others – could share information in real-time, with unmatched levels of speed, detection, and automation. We now plan to take the concept of synchronized security to a whole new level, through our Darwin project – which will allow multiple security sensors, whether from Sophos or other vendors, to operate as a system to deliver unparalleled protection, with greater visibility, automation, and manageability.
2. Artificial Intelligence (AI). The scale and sophistication of the threat landscape is outpacing the ability of humans alone to respond. Sophos is already a leader in applying artificial intelligence and deep learning to improve cybersecurity. Going forward, we will continue to advance our AI capabilities, and broaden and deepen our use of AI across our entire next-gen portfolio.

Evolution to security as a system continued

2013

DIVESTED non-core Cyber business

2014

Acquired Cyberoam

Acquired mojave networks

2015

Acquired SurfRight A SOPHOS Company

Acquired Reflexion

IPO LONDON STOCK EXCHANGE

LAUNCHED Synchronized Security

"At the heart of our product strategy lies the concept of synchronized security, and we are investing heavily to deepen and broaden this vision, enabling all of our products to share information in real-time, with unmatched levels of speed, detection and automation"

3. Openness. Sophos Central is a powerful integrated management platform for Sophos' next-gen products. This year we will be opening up Sophos Central through a rich set of APIs available to customers, our reseller partners, and other security vendors. We believe opening up Sophos Central will make it more attractive, flexible, and useful to customers and partners, and extend the vision and value proposition of synchronized security. Just as Sophos has committed to be a leader in cybersecurity innovation, we are committing to also be a leader in openness.
4. Public cloud. Public cloud represents a sea change in computing. Our endpoint, network, and server products – in both physical and virtual form – already help protect public cloud environments. With the recent launch of our Cloud Optix product, based on technology from our acquisition of Avid Secure, we are meaningfully enhancing and extending our security value proposition in cloud environments.
5. Zero-trust networks. We are architecting our solutions to enable more effective security in a "zero-trust" world where over time the traditional network perimeter and the concept of a "safe" internal network will be less common. Instead, "zero trust" will become the norm, with ubiquitous high-bandwidth connectivity driven by new platforms like 5G encouraging many organisations to operate in a mode of "never trust, always verify", based on user identity, data, location, and context.
6. Everything as a service. "As a service" is taking over virtually all areas of technology and technology-driven businesses, and cybersecurity is no different. Over time, we expect to make all our solutions available as a service: endpoint as a service, firewall as a service, public cloud security as a service, and more. In addition, the shift to "as a service" is driving a dramatic transformation in the channel, where cybersecurity value-added resellers of all sizes are rapidly transitioning their businesses to become service providers for their customers, which enables them to move up the value chain to become more strategic and also enhances the predictability of their business model and customer "stickiness". Just over two years ago we introduced a new MSP program explicitly designed to enable and support our partners as they embrace this multi-billion dollar new opportunity, and we believe our product portfolio, integrated cloud management console, and channel focus are an ideal fit for MSP partners. In the relatively short time since launch, we have seen rapid growth in MSP and we closed FY19 with annual recurring revenue of $27 million from more than 47,000 customers, growing over 100 per cent year-over-year.

FY19 product innovation

During the year we made significant advances in our product portfolio, particularly in our next-gen products:

- We enhanced the Sophos Central platform, especially in its management and administration capabilities for larger environments and features designed for MSPs to adopt Sophos Central and deploy and manage multiple Sophos products for their customers.
- Intercept X Advanced with Endpoint Detection and Response ("EDR") represented a key advance in our endpoint offering, designed to protect against active hacking and advanced threats that may already exist on customer networks. Backed by on-demand access to intelligence curated by SophosLabs and built on the foundation of our industry-leading deep-learning neural network technology, we have achieved best-in-class detection rates, combined with leading (low) false-positive rates, and unmatched levels of automation.

2016

Acquired PhishThreat

Acquired Barricade

2017

Acquired invincea

2019

Acquired AVID Secure

Acquired DarkBytes

CHIEF EXECUTIVE'S STATEMENT CONTINUED

Through this innovative use of advanced AI, we are now enabling enterprises of any size, even the most resource-constrained, to identify and prevent cyber-attacks in real time with threat-tracking and first-responder forensics at their fingertips.

- XG Firewall v17.5 was an important new release in our flagship next-gen firewall product that enables customers for the first time to seamlessly manage their firewall within the Sophos Central integrated cloud platform. In addition, v17.5 offers powerful new synchronized security features, including lateral movement detection, to prevent threats from spreading on the same network segment, and synchronised user ID. The ability to manage the firewall within Sophos Central is an important strategic step and one that we believe will aid future cross-selling activities between the firewall and the rest of our product set.
- We delivered Intercept X for Server, enhancing our existing server protection through the addition of deep learning and anti-exploit capabilities. Intercept X for Server protects the high-value information that is typically stored on servers and often targeted by cybercriminals.
- We supplemented our own organic product enhancement efforts via targeted acquisitions of two companies: Avid Secure and DarkBytes:
  - Avid Secure has accelerated our roadmap for cloud security and lies at the heart of our new Sophos Cloud Optix product. Cloud Optix provides unmatched visibility into cloud environments, and leverages AI and automation to simplify compliance, governance, and security monitoring in the cloud. Public cloud providers like AWS and Azure offer customers extraordinary flexibility and power in how they build and operate their cloud infrastructure environments, but they don't provide for full security. Instead they run a Shared Responsibility model – they ensure security of the cloud, while customers are responsible for anything they place in the cloud. This is where our new Cloud Optix product comes in, which starts with the premise that you can't secure what you can't see. Cloud Optix represents an important new strategic opportunity for Sophos and allows us to extend our protection to span across endpoint, network, and public cloud environments.
  - DarkBytes brings to Sophos a highly talented team with significant experience in managed detection and response ("MDR") and Security Orchestration Automation Response ("SOAR"). We are using the DarkBytes technology to enhance our internal efforts to develop a new MDR service offering, which we expect to release in FY20, and we believe represents a natural complement to our EDR product and an exciting cross-sell opportunity for our Intercept X installed base.

'Channel First' and 'Channel Best'

Our extensive global partner channel is a key strategic asset for Sophos and remains a key differentiator, compared to other IT security vendors that often operate conflicting routes to market. Our total partner network expanded to approximately 47,000 during the year and, encouragingly, the number of our most active and productive 'blue-chip' partners rose to 8,000, up from 7,000 a year ago.

We were pleased to be recognised once more as the "overall winner" for both Network Security and Endpoint Security in CRN's 2018 Annual Report Card (ARC) Awards, in recognition of the high quality and innovative product and program offerings we deliver to our partner channel. Sophos ranked highest in all sub-categories and topped the new sub-category for managed and cloud services.

Outlook

The demand environment for cybersecurity solutions continues to be robust, and we are confident that we are well positioned competitively, especially as more organisations move to adopt next-gen cybersecurity offerings. Increasingly, organisations of all sizes are looking for cloud-native solutions, centralised administration, integrated products, AI-powered protection, openness, and a service-oriented approach to security. Our next-gen solution set and strategy align well with these demands and have helped Sophos deliver strong growth in subscription revenue and customer count. We have become a leader in the next-gen cybersecurity market, and we are excited about the road ahead.

We believe the drivers are in place for continued future revenue growth, principally driven by growth in our subscription business, especially in our next-generation products. We intend to continue to invest to support this growth, with a return to operating profit margin leverage after FY20.

Finally, I want to thank our entire Sophos team, and our extensive network of channel partners around the world, whose talent and passionate commitment enable us to protect and support over 382,000 organisations (and growing!), every single day. We sincerely appreciate all you do to make the world a safer place.

Kris Hagerman
Chief Executive Officer
15 May 2019

CASE STUDY

Sophos Cloud Optix – solving the toughest challenges in cloud security

Sophos Cloud Optix helps enable our vision to evolve synchronized security within the cloud – providing the best protection and visibility, wherever your data resides.

Public cloud providers such as AWS, Azure and Google offer businesses enormous flexibility as to how they build their cloud environments, allowing them to innovate in ways that wouldn't be possible on premise.

When it comes to securing the cloud and the data that sits within it, public cloud providers operate a Shared Responsibility model: whilst they ensure security of the cloud infrastructure, their customers are responsible for any data they place in the cloud.

Consequently, visibility is the toughest challenge businesses face as they seek to optimise their cloud security posture.

Sophos Cloud Optix is designed to address the three major cloud security challenges customers are facing.

The first is the lack of visibility across multiple cloud environments, whereby many businesses are challenged to confidently state how many assets they have running in the cloud.

A second challenge lies in the effective implementation and maintenance of security and compliance. This can be very challenging due to the dynamic nature of the cloud where things are constantly changing.

Finally, businesses need to address security issues proactively, as they arise. Attacks are becoming more sophisticated and targeted, at the same time that the attack surface is expanding. It is no longer possible for teams to manually respond to all security alerts, with an urgent need for automation when it comes to incident response.

Sophos Cloud Optix solves these challenges, by making cloud workload visible, and simplifying compliance and threat response. Cloud Optix automates the discovery of an organisation's assets in the public cloud, allowing continuous compliance reporting, and instant automated remediation and incident response.

Find out more at www.sophos.com/cloud-optix

"Revenue growth was strong in the year-ended 31 March 2019 as prior-period subscription billings converted into revenue and as the recently established MSP channel increased in scale"

Nick Bray
Chief Financial Officer

FINANCIAL REVIEW

Strong revenue and adjusted operating profit performance

For 31 March 2019 ("FY19"), in constant currency Sophos delivered a 12.0 per cent increase in total revenue, driven by a 16.7 per cent increase in subscription revenue.

With the impact of the change to IFRS 15, Revenue from Contracts with Customers reflected in both periods, this growth reflects a true underlying rate. Reported subscription revenue grew 15.9 per cent, whilst total reported revenue grew 11.2 per cent. Deferred revenue at the end of the period increased to $742.1 million from $728.6 million a year ago representing a reported growth of 1.9 per cent; lower than revenue growth due to $36.2 million of foreign exchange revaluation principally arising from the weakening of euro and sterling against the US dollar. The deferred revenue balance gives the Group good visibility of future revenue, with $428.6 million of the deferred revenue due for recognition in less than one year, an increase of 5.1 per cent over the prior-year, or 10.7 per cent at constant currency.

Billings at reported exchange rates decreased by one per cent to $760.3 million, within which subscription billings were flat year-on-year at $644.6 million. This performance reflects a challenging prior-year comparison, where Enduser product demand had been significantly boosted by the high-profile ransomware attacks in 2017 and the launch of the Group's next-gen endpoint product. In addition to this, albeit of lesser extent, the Group experienced a headwind to Network billings as a result of a legacy product transition, principally in the first half, a slow-down in hardware sales as customers extend refresh cycles; and, the increasing significance of the MSP channel with monthly billings.

Revenue

$711M

(FY18: $639M)

Profit/(Loss) After Taxation

$29M

(FY18: ($61M))

Net Cash Flow From Operating Activities

$143M

(FY18: $148M)

The Group made an operating profit of $60.9 million in the year and adjusted operating profit increased by $50.7 million to $109.0 million, primarily as a result of strong revenue growth. This year's result benefited from a foreign exchange gain of $1.5 million, compared to a foreign exchange loss of $6.9 million in the prior-year.

The Group's profit before taxation increased by $94.6 million to $53.6 million, from a loss of $41.0 million in the prior-year, primarily as a consequence of the $80.6 million improvement in operating profit supported by a $13.4 million reduction in finance expenses. Finance expenses benefited from foreign exchange gains in the current year resulting from the strengthening of both sterling and the euro against the US dollar, compared to foreign exchange losses in the prior-year.

The Group's profit for the year increased by $87.8 million to $26.9 million in the year-ended 31 March 2019, which given only a small increase in the year-on-year income tax charge was primarily attributable to the improvement in the profit before taxation.

Cash flow from operating activities remained strong at $142.9 million, reduced by $4.8 million from $147.7 million in the prior-year. The small overall decrease was due to an increase in overheads, partially offset by a reduction in the cashflow outflow on exceptional items and an improved use of working capital. Unlevered free cashflow decreased by $15.8 million to $123.8 million representing the reduction in net cash flow from operating activities adjusted for the cashflow impact of exceptional items.

The table below presents the Group's financial highlights on a reported basis:

	FY19 $M	FY18[1] $M	Change %
Statutory measures			
Revenue	710.6	639.0	11.2
Profit / (Loss) before taxation	53.6	(41.0)	nm
Net cash flow from operating activities	142.9	147.7	(3.2)
Alternative performance measures[2]			
Billings	760.3	768.6	(1.1)
Cash EBITDA	167.9	199.2	(15.7)
Adjusted operating profit	109.0	58.3	87.0
Unlevered free cash flow	123.8	139.6	(11.3)

1 Restated for the adoption of IFRS 15 and change in accounting policy in respect of research and development expenditure tax credit scheme and provision for interest on uncertain tax positions, as explained in note 2 of the Financial Statements

2 Definitions and reconciliations of non-GAAP measures are included in note 5 of the Financial Statements

FINANCIAL REVIEW CONTINUED

Revenue and deferred revenue

The Group adopted IFRS 15 Revenue from Contracts with Customers in the current year and has therefore restated the results for the prior-year on a consistent basis, see note 2 of the Financial Statements for further details.

The Group's revenue increased by $71.6 million, or 11.2 per cent, to $710.6 million in the year-ended 31 March 2019. Subscription revenue was notably strong in the period, with reported growth of 15.9 per cent, or 16.7 per cent on a constant currency basis, because of strong prior-period billings and incremental growth of the MSP channel in the current period.

	FY19 $m (Reported)	FY18[1] $m (Reported)	Growth % (Reported)	Growth % (CC)
Revenue by Region:				
– Americas	253.3	223.6	13.3	13.4
– EMEA	363.6	324.5	12.0	12.7
– APJ	93.7	90.9	3.1	6.2
	710.6	639.0	11.2	12.0
Revenue by Product:				
– Network	328.5	316.5	3.8	4.7
– Enduser	348.4	291.8	19.4	20.2
– Other	33.7	30.7	9.8	10.0
	710.6	639.0	11.2	12.0
Revenue by Type:				
– Subscription	593.9	512.4	15.9	16.7
– Hardware	106.8	115.1	(7.2)	(6.3)
– Other	9.9	11.5	(13.9)	(12.8)
	710.6	639.0	11.2	12.0

1 Restated for the adoption of IFRS 15 as explained in note 2 of the Financial Statements

Revenue in the period of $710.6 million comprised $394.1 million from the recognition of prior-period deferred revenues and $316.5 million from in-period billings. The majority of the Group's billings, which are recognised over the life of the contract, relate to subscription products (FY19: 84.8 per cent; FY18: 83.8 per cent), with the benefit from increased billings being spread over a number of years on the subsequent recognition of deferred revenue. The deferred revenue balance at the end of the period of $742.1 million increased $13.5 million year-on-year, an increase of 1.9 per cent. This was mainly due to a net deferral of billings amounting to $49.7 million partially offset by a net currency revaluation of $36.2 million, a consequence of the weakening of the euro and sterling against the US dollar during the year. Deferred revenue due within one year at the balance sheet date of $428.6M increased by 5.1 per cent at actual rates or by 10.7 per cent in constant currency.

Revenue in the Americas increased by $29.7 million or 13.3 per cent to $253.3 million in the year-ended 31 March 2019, supported by the recognition of prior-period Enduser billings from the Sophos Central platform and the growth of the MSP channel in the current period.

EMEA revenue increased by $39.1 million or 12.0 per cent to $363.6 million in the year-ended 31 March 2019, with growth in Enduser in particular, but also aided by Network sales.

APJ revenue increased by $2.8 million, or 3.1 per cent to $93.7 million in the year-ended 31 March 2019, with good growth in Enduser products partially offset by a decline in Network sales following the legacy product transition.

Billings

Group reported billings decreased by $8.3 million or 1.1 per cent to $760.3 million in the year-ended 31 March 2019. This represented a 0.1 per cent decrease on a constant currency ("CC") basis.

	FY19 $m (Reported)	FY18 $m (Reported)	Growth % (Reported)	Growth % (CC)
Billings by Region:				
– Americas	267.8	270.0	(0.8)	(0.7)
– EMEA	395.3	395.1	0.1	0.9
– APJ	97.2	103.5	(6.1)	(2.8)
	760.3	768.6	(1.1)	(0.1)
Billings by Product:				
– Network	345.9	353.4	(2.1)	(1.1)
– Enduser	377.1	383.2	(1.6)	(0.7)
– Other	37.3	32.0	16.6	17.1
	760.3	768.6	(1.1)	(0.1)
Billings by Type:				
– Subscription	644.6	644.2	0.1	1.0
– Hardware	105.7	113.7	(7.0)	(6.1)
– Other	10.0	10.7	(6.5)	(4.6)
	760.3	768.6	(1.1)	(0.1)

Billings by region

Americas

Billings attributable to the Americas decreased by $2.2 million to $267.8 million in the period, representing a 0.8 per cent reduction on a reported basis and 0.7 per cent on a constant currency basis; this decrease largely driven by a decline in Enduser products due to the stronger performance in the prior-year compare as a consequence of the impact of the WannaCry ransomware outbreak and the launch of Intercept X, the Group's next-gen endpoint product, partially offset by an improved performance in UTM sales.

EMEA

Billings attributable to EMEA increased by $0.2 million to $395.3 million in the period, representing 0.1 per cent growth on a reported basis and 0.9 per cent growth on a constant currency basis. An increase in sales of Server products being partially offset by a reduction in endpoint and email products.

APJ

Billings attributable to APJ decreased by $6.3 million to $97.2 million in the period, representing 6.1 per cent on a reported basis and 2.8 per cent on a constant currency basis. As in the Americas, growth was negatively impacted by the stronger performance in the prior-year compare compounded by a legacy Network product transition in the first-half of the year partially offset by an improvement in sales of Server products.

FINANCIAL REVIEW CONTINUED

Billings by product

Network products

The Group's billings attributable to Network products decreased by $7.5 million to $345.9 million in the period, representing 2.1 per cent reduction on a reported basis and 1.1 per cent on a constant currency basis. This was mainly a consequence of the previously reported legacy product transition and lower hardware sales to existing customers, who extended their refresh cycles.

Enduser products

The Group's billings attributable to Enduser products decreased by $6.1 million to $377.1 million in the period representing 1.6 per cent reduction on a reported basis and 0.7 per cent on a constant currency basis. The comparative period benefitted from increased demand driven by high-profile ransomware attacks and the launch of Intercept X, the Group's next-gen endpoint product, whilst the current period saw an increasing significance of the MSP channel which delivers monthly billings.

Billings by type

Subscription billings

The Group's billings attributable to subscriptions increased by $0.4 million to $644.6 million in the period, representing 0.1 per cent growth on a reported basis and 1.0 per cent growth on a constant currency basis. The lower year-on-year growth rate was due to the stronger performance in the prior-year compare as a consequence of the impact of the WannaCry ransomware outbreak and the launch of Intercept X, the Group's next-gen endpoint product, which also resulted in the prior-year in abnormal cross-sell and renewal rates. Within subscription billings, amounts invoiced to managed service providers ("MSPs") increased year-on-year which, combined with a reduction in the number of larger deals in FY18, lowered the overall average deal size.

Hardware billings

The Group's billings for hardware decreased by $8.0 million to $105.7 million, representing 7.0 per cent fall on a reported basis and 6.1 per cent fall on a constant currency basis. This was mainly a consequence of the previously reported legacy product transition and lower hardware sales to existing customers, who extended their refresh cycles. However, hardware sales to existing customers is being partially offset by improved hardware sales to new customers.

Key billings metrics

Billings from new customers

Billings from new customers, including all MSP billings and excluding OEM and consumer, remained consistent at 24.7 per cent of total billings compared to 24.2 per cent in the year-ended 31 March 2018.

Retention and renewal rates

The Group's net retention and renewal rates include the impact of cross-selling and upselling, which helps the Group evaluate the success of its strategy to broaden the sales of its product portfolio to existing customers. The Group's net retention rate decreased from 109.2 per cent at 31 March 2018 to 105.6 per cent at 31 March 2019. The Group's renewal rate decreased to 124.2 per cent from 139.7 per cent. Both measures were impacted by the significant increase in cross-sell and upsell during the prior period arising from the impact of the WannaCry ransomware outbreak and the launch of Intercept X, the Group's next-gen endpoint product.

Billings by size

Sophos' products are suitable for organisations of any size but are specifically tailored for the Group's target market of mid-market enterprises, typically with fewer than 5,000 employees. The proportion of billings to this target market remained stable at 86 per cent in the period compared to 85 per cent in the year-ended 31 March 2018.

Billings by length of contract

Subscription agreements sold by the Group are of differing durations and are generally between one and three years in duration. The last twelve months' weighted average contract duration, which provides an indication of the period over which future revenue will be recognised, was 26.4 months for the year-ended 31 March 2019, a small decrease on the 27.6 months for the year-ended 31 March 2018, due primarily to fewer larger deals in the current year which tend to be longer in length and the growth in monthly billings to new customers from the Group's MSP business which increased from 1.1 per cent of total billings in the prior-year to 2.5 per cent in the current year.

The billings analysis of contracts by subscription length for each year was as follows:

Constant currency	FY19 %	FY18 %
Under one year	37.7	34.5
One to two years	6.9	7.0
Two to three years	46.1	48.0
Greater than three years	9.3	10.5

Cross-sell and upsell opportunities

As the threat landscape evolves and Sophos continues to innovate, there is an opportunity to cross-sell additional products and services, or to upsell enhanced versions of products or additional licences to existing customers.

The percentage of customers who own both a Sophos Endpoint and UTM product has continued to improve. At 31 March 2019, approximately 12.1 per cent of customers had both a UTM product and an Endpoint product compared to 11.2 per cent of customers at 31 March 2018.

Across the entire installed base, customers currently have on average 1.4 products, leaving significant room for future cross-selling activity. Sophos Central is a fundamental driver of the cross-sell strategy. As customers move onto the cloud platform and take additional products, the Group's cross-sell metrics have improved, in particular, the average customer spend and the average number of products per Sophos Central customer, the latter higher than the Group average at 1.7.

Cost of sales

Cost of sales increased by $2.4 million to $146.4 million in the period. This was due to increased hosting costs as more of the Group's customers move to cloud managed products, costs associated with supporting the Group's products and services that naturally increase as the Group grows, partially offset by a reduction in the volume of appliances sold.

Sales and marketing

Sales and marketing expenses increased by $20.0 million or 8.3 per cent, to $259.9 million in the period. Sales and marketing expenses increased at a rate that exceeded billings growth to facilitate continued support of the business with the reduction in sales productivity largely being a consequence of an increase in the volume of transactions at a slightly reduced average deal size year-on-year. Going forward, sales and marketing expenses are targeted to grow at slightly less than the rate of billings growth in order to provide margin leverage.

Research and development

Research and development expenses increased by $3.6 million, or 2.6 per cent, to $143.9 million in the period. The Group has a strong focus on new and enhanced products to address the significant market opportunity that it believes exists and allocates resources accordingly. Research and development expenditure, which in both current and prior period was expensed to the consolidated statement of profit or loss in full, is broadly targeted to grow at the rate of billings.

General finance and administration

General finance and administration expenses, excluding exceptional items, foreign exchange and the amortisation of intangible assets, decreased by $1.3 million, or 1.5 per cent, to $87.9 million in the period. The decrease was due to a lower share-based payment expense partially offset by an increase in underlying general finance and administration expenses. The share-based payment expense decreased by $5.4 million to $36.9 million, due to a revision of the expected vesting for performance awards granted and as a consequence of a lower share price applied to cash-settled schemes. Underlying general finance and administration expenses increased by 8.7 per cent to $51.0 million, reflecting the annualised increase resulting from prior-period investments in people as well as an increase of certain ongoing compliance costs.

Exceptional items, included within general finance and administration expenses, were a net credit of $3.8 million in the period, compared to a net expense of $13.2 million in the prior-year. The current period credit arose on fair value changes in acquisition contingent consideration, partially offset by some restructuring and legal costs.

Amortisation of intangible assets

Amortisation of intangible assets decreased by $8.3 million, or 32.9 per cent, to $16.9 million in the period. The decrease was due to the Group's reducing balance amortisation policy being greater than the increase arising from acquisitions in the current period.

Currency movements and impact

The Group recorded a foreign exchange gain of $1.5 million in the period resulting from a weakening of the euro and sterling against the US dollar; compared with a loss of $6.9 million in the comparative period.

Cash EBITDA

Cash EBITDA decreased by $31.3 million or 15.7 per cent to $167.9 million in the period. Cash EBITDA margins decreased to 22.1 per cent from 25.9 per cent in the prior-period, as overheads, particularly sales and marketing expenditure, increased year-on-year whilst billings decreased slightly. The reconciliation of Cash EBITDA to operating loss is included in note 5 of the Financial Statements.

FINANCIAL REVIEW CONTINUED

Adjusted operating profit

Adjusted operating profit increased by $50.7 million to $109.0 million in the period, resulting from strong revenue growth and benefiting from a small foreign exchange gain partially offset by increased sales and marketing expenditure. The reconciliation of adjusted operating profit to operating loss is included in note 5 of the Financial Statements.

Operating profit

Operating profit was $60.9 million in the period, compared to a loss of $19.7 million in the comparative period which represents an improvement of $80.6 million. This was principally driven by strong growth in revenue, a foreign exchange gain in the period, compared to a loss in the comparative period, a decrease in the amortisation charge, and an exceptional credit compared to an exceptional loss in the comparative period. These gains were partially offset by an increase in overheads including Sales and Marketing costs.

Net finance costs

Net finance costs decreased by $14.0 million to $7.3 million in the period, due mainly to foreign exchange gains on euro denominated debt following the strengthening of the US dollar in the period, resulting in a $6.4 million gain compared to a $9.6 million loss in the prior-year. Interest on uncertain tax positions increased by $2.6 million to $3.5 million due to the switch in the period of the overall tax balance from deferred tax to current tax, interest only being accrued on the latter balance.

Income tax

The Group's tax charge for the year was $26.7 million (FY18: $19.9 million) with an effective tax rate of 49.8 per cent (FY18: 48.5 per cent). The tax charge is higher than the prior-period primarily due to the Group generating a profit, compared with a loss in the comparative period.

Profit before tax and profit for the period

The profit before tax increased by $94.6 million to $53.6 million from a loss of $41.0 million in the prior-year, whilst the Group's profit for the year-ended 31 March 2019 increased by $87.8 million to $26.9 million from a loss of $60.9 million in the prior-year . This is as a result of strong revenue growth supported by increased Sales and Marketing spend and the benefit of a foreign exchange gain of $1.5 million, compared to a foreign exchange loss of $6.9 million in the prior-year combined with a slightly higher tax charge as explained above.

Cash flow

Net cash flow from operating activities decreased by $4.8 million to $142.9 million from $147.7 million in the prior period. The small overall decrease was due to a $9.9 million reduction in the cashflow outflow on exceptional items, a $7.0 million improved use of working capital within the business, both being offset by an increase in overheads, primarily in relation to Sales and Marketing expenses.

Unlevered free cashflow decreased by $15.8 million to $123.8 million from $139.6 million in the prior-period representing the reduction in net cash flow from operating activities adjusted for the cashflow impact of exceptional items.

	FY19 $M	FY18[1] $M
Cash EBITDA[2]	**167.9**	**199.2**
Net deferral of revenue	(49.7)	(129.6)
Net deferral of expenses	0.9	8.4
Foreign exchange	1.5	(8.1)
Depreciation	(11.6)	(11.6)
Adjusted operating profit	**109.0**	**58.3**
Net deferral of revenue	49.7	129.6
Net deferral of expenses	(0.9)	(8.4)
Exceptional items [3]	(3.1)	(13.0)
Depreciation	11.6	11.6
Foreign exchange	(1.5)	8.1
Change in working capital [2]	(5.2)	(12.2)
Corporation tax paid [2]	(16.7)	(26.3)
Net cash flow from operating activities	**142.9**	**147.7**
Exceptional items [3]	3.1	13.0
Net capital expenditure [2]	(22.2)	(21.1)
Unlevered free cash flow	**123.8**	**139.6**

1 Restated for the adoption of IFRS 15 and change in accounting policy in respect of research and development expenditure tax credit scheme ("RDEC") and provision for interest on uncertain tax positions, as explained in note 2 of the Financial Statements

2 Unlevered free cash flow is also represented by the sum of the marked rows and has been presented to enhance understanding of the Group's cash generation capability

3 Excludes non-cash movements on exceptional items

Changes in working capital

Working capital is closely monitored by the Group. The change in working capital continues to reflect growth in the business albeit with a slightly lower outflow in the current year in part due to continued close control of receivables and payables with debtors' days outstanding of 42 days (FY18: 41 days).

Capital expenditure

Capital expenditure primarily comprises the acquisition of intangible assets as well as property, plant and equipment. Net capital expenditure was largely flat year-on-year, with a small increase in tangible assets being offset by a decrease in intangible assets.

Cash tax

Cash tax remains payable because of profits arising in local subsidiaries. Corporation tax paid of $16.7 million is lower than in the prior-year (FY18: $26.3 million) due to lower taxable profits in subsidiaries outside of the UK. The US paid less tax due to a cut in the rate of federal income tax and a tax overpayment in the prior year. Royalties paid to higher tax jurisdictions also declined as acquisitions were integrated.

Financing

There were no changes in the financing of the Group in the year with net debt decreasing to $127.7 million from $186.2 million in the comparative period. As a result of continued strong net cash flows, cash retained within the business increased to $172.1 million from $120.1 million and is the key driver for the reduction in net debt. Further analysis of movements on a cash basis is provided in note 33 of the Financial Statements.

Dividends

The Directors propose that the Company will pay a final dividend in respect of the year-ended 31 March 2019 amounting to 3.7 US cents per share (FY18: 3.5 US cents). Combined with the interim dividend of 1.5 US cents per share gives a total dividend for the financial year of 5.2 US cents (FY18: 4.9 US cents). Subject to shareholder approval the final dividend will be paid on 11 October 2019 to all shareholders on the register on 20 September 2019.

Nick Bray

Chief Financial Officer

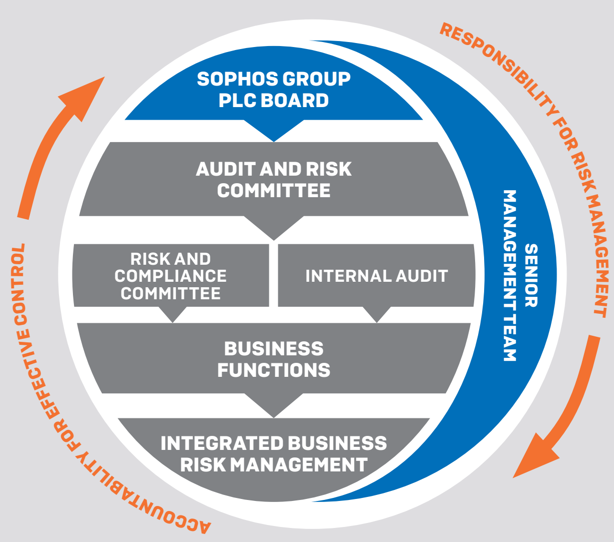
15 May 2019

Principal risks are identified through a business wide risk assessment process, along with an evaluation of the strategy and operating environment of the Group

The risk review process encompasses the identification, management and monitoring of risks in each area of the business. This process includes an assessment of the risks to determine the likelihood of occurrence, potential impact and the adequacy of the mitigation or controls already in place. A review is then undertaken by the Risk and Compliance Committee, which evaluates the principal risks of the Group with reference to its strategy and the operating environment.

The Audit and Risk Committee monitors and challenges these processes, reviewing the Group's Consolidated Risk Register and reporting material risks to the Board. There may be other risks or uncertainties that could emerge in the future, however the Group's ongoing commitment to risk management will seek to address and mitigate the future risks, as and when they become apparent.

Structure of risk management



The Directors consider the following matters to be the principal risks and uncertainties (in no specific order) affecting the Group:

RECRUITMENT AND RETENTION OF KEY PERSONNEL

Risk movement

↑

How it impacts us

The ongoing success of Sophos is dependent on attracting and retaining global high-quality employees at all levels in the business who can effectively implement the Group's strategy.

Failure to attract, retain or develop high quality employees across the business could limit the Group's ability to deliver its business plan.

What we are doing

Making Sophos a great place to work is central to the Group's strategy.

Sophos is increasing its commitment to diversity and inclusion by introducing new programmes to attract and develop diversity of all types.

Additionally, Sophos has a commitment to all levels of training and development throughout the organisation.

Reward schemes are continuously evaluated to drive and reward performance and ensure retention of key talent.

Annual employee engagement surveys enable progress of the Group's people actions to be monitored, areas of improvement identified, and necessary actions performed.

The cybersecurity industry continues to be a competitive marketplace for talent. As such, Sophos is increasing our commitment to strong recruitment processes supported by robust remuneration programmes, which are benchmarked appropriately.

DEFECTS OR VULNERABILITIES IN PRODUCTS OR SERVICES

Risk movement

↔

How it impacts us

The Group's products and services are complex, and as such they have contained and may in the future contain, design or manufacturing defects or errors that are not detected until after their commercial release and deployment by end customers. These defects could cause the Group's products or services to be vulnerable to security attacks, cause them to fail to help security networks, temporarily interrupt end customers' networking traffic, and fail to prevent or detect viruses or similar threats. Further, due to the evolving nature of threats and the continual emergence of new threats, the Group may fail to identify and update its threat intelligence or other virus databases in time to protect its end customers' networks and devices.

As a result, actual or perceived defects or vulnerabilities in the Group's products or services, the failure of the Group's products or services to prevent a security threat could harm the Group's reputation and divert the Group's resources.

What we are doing

Sophos is committed to extensive test cycles and quality procedures which are subject to continuous improvement.

Sophos employs combinations of internal and external quality reviews and testing of products, including source code reviews, public and private third party efficacy testing, automated code tests and various forms of penetration testing. The Group encourages a healthy collaboration with the security research community, as described in the Responsible Disclosure Policy: https://www.sophos.com/security.

Sophos continues to run a Bug Bounty program to leverage the skills of thousands of individuals to help make our products and web properties more secure. The Group sees good activity from the research community, allowing us to resolve software defects before they can be exploited by attackers. This and other measures have allowed us to slightly reduce this risk.

Further, Sophos protects the privacy and security of its customers worldwide through our pledge to never engineer backdoors into our products as described here: https://www.sophos.com/nobackdoors.

FALSE DETECTION OF THREATS

Risk movement

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How it impacts us

The Group's products may falsely detect threats or malware that do not actually exist in applications or content based on the Group's classification of application type, virus, malware, vulnerability exploits, data or URL categories (known as 'false positives'). These false positives, while inherent in the Group's industry, may impair the perceived reliability of the Group's products and may therefore adversely impact market acceptance of the Group's products.

If the Group's products restrict important files or applications based on falsely identifying them as malware or some other item that could be restricted, this could adversely affect end customers' systems and cause material system failures. Any such false identification of important files or applications could result in negative publicity, damage to the Group's reputation, loss of end customer and sale, increased costs to remedy any problem and risk of litigation, any of which could materially adversely affect the Group's financial condition and operating results.

What we are doing

Sophos strives for continuous improvement in our world class Sophos Labs threat research operation. The Group invests in ongoing staff training and process optimisation, as well as enhancements to testing and quality systems and procedures.

In 2017, Sophos developed and launched a new reputation-based false positive suppression system to complement the introduction of "Deep Learning" artificial intelligence predictive modules in its products. Additionally, there is proactive focus on improvement of processes to enable early detection of a false positive event, as well as applying a 'lessons learnt' approach through root cause analysis.

Product enhancements were introduced to the Intercept X product in late 2017 to allow our partners and customers to manage occurrences of false positives on their own, enabling us and them to deal with those rare or even unique files that might evade our reputation and prevalence suppression techniques.

Sophos acknowledges the inherent risk associated with a false positive incident within the industry and is committed to ensuring there are mitigating processes in place to manage any incident, large or small, in order to minimise the impact on the Group's customers.

PRINCIPAL RISKS AND UNCERTAINTIES CONTINUED

PRODUCT PORTFOLIO MANAGEMENT

Risk movement

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How it impacts us

Sophos has an extensive number of products, enhanced further by acquired technologies. The extent of investment in each product needs to be managed and prioritised taking into account the expected future prospects. Additionally, consideration must be given to the ability to be able to adequately support the entire product range.

Failure to manage the product portfolio adequately could result in inappropriate investment focus in relation to research and product innovation. This could result in products that do not meet the requirements of customers or partners and the risk they will look to alternative solutions, resulting in the potential loss of both new and existing revenue streams.

Failure to protect the Group's intellectual property could adversely affect the ability of the Group to operate in its markets.

Additionally, insufficient focus on key research and innovation projects may damage the long-term growth prospects of the Group.

What we are doing

Sophos continues to focus on and improve the interaction between Product Management, Product Development, Sales and Marketing and all Support functions in an integrated product development approach.

Internal processes are run to identify opportunities for standardisation and consistency across products lines. This helps eliminate redundancies, reduce development and support costs, and improve partner and customer experiences through a more predictable and coherent product portfolio.

Sophos is working to bring all products under a single cloud management platform to deliver a common management experience for the portfolio and a comprehensive solution that will encourage existing customers using on premise products to migrate to cloud management. The Group is also working on enabling instances of portability of the cloud infrastructure where required in order to address any privacy or data sovereignty issues that our customers/partners might face.

The Group takes all appropriate opportunities to protect its intellectual property and brands.

Sophos customer and partner communities continue to be invaluable resources in guiding portfolio management decisions. They provide immediate and constant feedback on how well Sophos is meeting its requirements, improvements that Sophos can make to its current offerings and opportunities for portfolio consolidation or expansion.

Whilst Sophos continues to make significant investments in the technology and infrastructure of the Group, the risk has increased due to the growing demand and reliance on cloud delivery for the Group's products.

In addition, the migration to Next Gen products has some risk during the transition and end of life cycle.

DISRUPTION TO DAY-TO-DAY GROUP OPERATIONS

Risk movement

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How it impacts us

Sophos is at risk of disruption to its day-to-day operations from a disaster incident which may seriously impact IT systems or access to office space. A failure in the operation of the Group's key systems or infrastructure on which the Group relies could cause a failure of service to its customers and negatively impact the Sophos brand.

What we are doing

Incident management procedures and escalation processes are in place as well as maintaining security, business continuity and disaster recovery plans. Sophos continues to invest in cloud technology that provides resilient infrastructure for the Company.

IT SECURITY AND CYBER RISK

Risk movement

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How it impacts us

As a provider of IT security products, the Group is a higher profile cyber-attack target. The Group's infrastructure, services and products may have vulnerabilities that have from time to time been, and may in the future be, targeted by attacks specifically designed to disrupt the Group's business and harm the Group's reputation.

If an actual or perceived breach of security occurs in the Group's internal systems, it could adversely affect the market perception of the Group's products. In addition, a security breach could affect the Group's ability to operate its business, including the Group's ability to provide support services to end customers.

What we are doing

Sophos has a dedicated cybersecurity team focused on identifying risks related to cyber-attacks and planning appropriate protection, detection, response and recovery mechanisms. The Group is focused on day-to-day active monitoring and hunting for threats, improving response processes and implementing continual improvements to governance, technology and education and awareness programmes.

Sophos continues to increase its investment in cybersecurity and improve its cybersecurity capabilities on a quarterly basis.

PROCESSES, CONTROLS AND COMPLIANCE

Risk movement

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How it impacts us

The Sophos Group operates across many geographies with differing legal and market requirements. There is a risk that without adequate controls, policies and procedures, Sophos might be unable to meet its strategic objectives.

What we are doing

Sophos continues to review its internal processes and control environment to assess and improve. Sophos has also centralised many financial functions, for example, accounts receivable/payable and purchasing, enabling consistent controls and a Group-wide process. The Group regularly reviews and updates its policies such as anti-bribery and corruption, modern slavery and data protection. The risk management process is overseen by the Risk and Compliance Committee, the Audit and Risk Committee and ultimately the Board.

In concluding on the risks and uncertainties that are considered to be significant for the Group the Directors assess a wide range of issues, which included the following that are not considered to be principal risks:

Brexit

Following the decision by the UK electorate to exit, in due course, from the European Union ("Brexit"), the Directors continue to keep under consideration the expected impact of Brexit on the Group. A cross-functional Brexit working Committee has been put in place during the financial year, and that Committee continues to assess, respond to, and monitor developments, which may impact the Group's business.

As the Group operates internationally with a diverse geographic spread which results in only 12 per cent of the Group's revenue, any fluctuations in the sterling exchange rate, are, to a degree, balanced with sterling denominated costs which mitigates the impact on the US dollar functional currency of the Group.

The exact nature of the trading arrangements between the UK and the EU subsequent to the UK's exit from the EU remains uncertain and as a consequence the Directors have considered a number of scenarios and the Group's potential responses to them. This scenario planning has included anticipating changes to the operations of the Group and its supply chain, which are not considered to be significant or posing a heightened risk to the Group. The impact of Brexit on the current and future employees has also been considered and while there may be some disruption or changes in the UK, these are not currently anticipated to materially affect one of the Group's principal risks, the 'Recruitment and retention of key personnel'.

Due to the uncertainty of the method by which Brexit will be achieved, the Group have put into place processes to handle a hard Brexit, should that be the route that the UK takes.

Patent infringement

In addition, the Directors consider the risk of claims of patent infringement against the Group's products, which is considered to be a software industry-wide risk. The risk is not considered to be a standalone principal risk and is instead factored into the Directors' consideration of 'Product portfolio management', which is a principal risk.

CORPORATE RESPONSIBILITY REPORT

Sophos is committed to defending its customers against criminal activity and acting as a responsible business

Our approach

With over 335,000 customers around the world, Sophos recognises the responsibility it holds in providing the right tools to protect its clients and educate them on the importance of digital security. The Group's business model is built on securing its customers from the risks of cybercrime by offering innovative, simple and highly effective cybersecurity solutions.

Beyond the impact of Sophos' own products and services, the Group recognises the duty it has in conducting its business activities in a responsible way. With over 3,400 employees across more than 40 offices, it is vital that the Group maintains the highest standards of conduct. To achieve this, Sophos focuses on operating openly and transparently, treating its people fairly, creating a diverse culture and reducing its environmental impacts.

In the year, the Group further enhanced its commitment to corporate responsibility ("CR") and work will continue on further establishing the Group's CR strategy and improving measurement across key areas of focus.

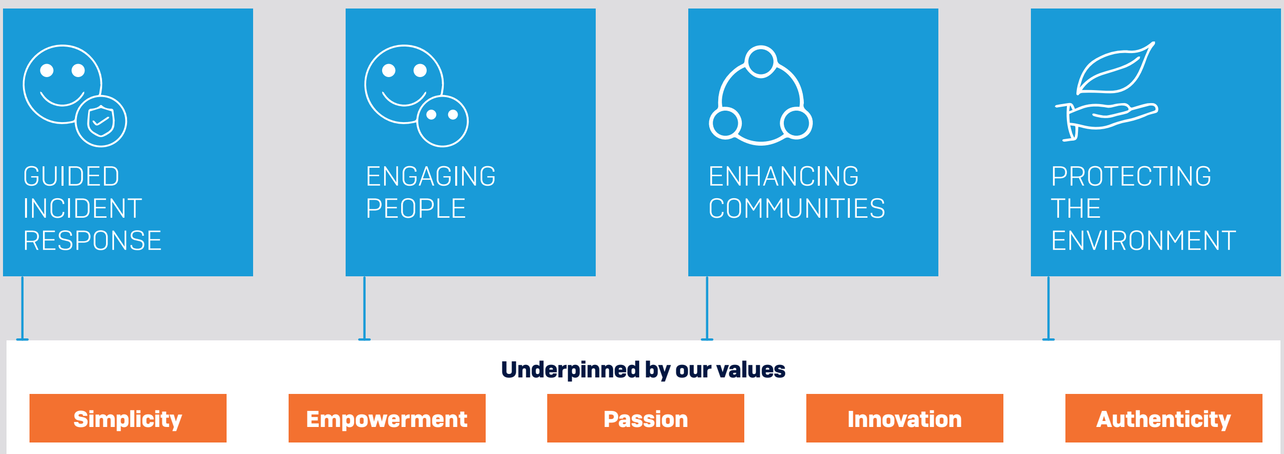
Managing corporate responsibility

Ultimate responsibility for Sophos CR activities lies with the Senior Management Team ("SMT") who set the Group's strategic approach, develop key policies and coordinate activities. The SMT is comprised of the Chief Executive Officer, Chief Financial Officer and other individuals who head key Group functions.

The Group's functional heads take leading roles in key strategic CR areas such as gender, HR and environmental management. The SMT are also responsible for ensuring global compliance with key internal and external policies including:

- Anti-human trafficking and slavery policy
- Diversity policy
- Anti-corruption and bribery policy
- Whistleblowing policy
- UK Modern Slavery Act

Sophos CR framework



The SMT support the Audit and Risk Committee ("ARC") and the Risk and Compliance Committee ("RCC") in ensuring compliance with the Code of Conduct, as well as financial compliance and global risk management (see page 36). Moving forward the Group aims to implement a CR Steering Committee to reinforce commitment to corporate responsibility and promote strategic action across the organisation.

Non-financial information statement

This section of the strategic report constitutes the Group's non-financial information statement, produced to comply with sections 414CA and 414CB of the Companies Act. The information listed is incorporated by cross-reference:

Reporting requirement	**Policies and standards which govern our approach**	**Information necessary to understand our business and its impact, policy due diligence and outcomes**
Environmental matters (including the impact of the Company's business on the environment)	Environmental Statement	Protecting the environment, page 50
Employees	Ethics and Responsible Business Policy Colleague Policy[1] Equal Opportunities[1] Diversity Policy	page 40 https://www.sophos.com
Social matters	Company Events[1]	Enhancing communities, page 49
Respect for human rights	Data Privacy Policy[1] Anti-Slavery and Trafficking Statement Information and Cyber Security Policy[1]	https://www.sophos.com
Anti-corruption and anti-bribery	Anti-corruption Policy Anti-bribery Policy	https://www.sophos.com
Description of business model		Our business model, page 16
Description of the non-financial key performance indicators		Key performance indicators, page 20 Our strategic priorities, page 18

1 Certain Group Policies and internal standards and guidelines are not published externally

The policies mentioned above form part of the Group's Policy Framework which is founded on key risk management principles. The policies which underpin the principles define mandatory requirements for risk management. Robust processes and controls to identify and report policy outcomes are in place and were followed in FY19.

CORPORATE RESPONSIBILITY REPORT CONTINUED

Engaging with key stakeholders

Communicating with key stakeholders is vital in helping to better understand their needs and requirements. The Group conducted several engagement activities throughout FY19, to encourage two-way dialogue with key stakeholder groups. Local offices also play a significant role in forming lasting relationships with local stakeholders, including community members.

Key stakeholders	Engagement channels	Key activities in the year
Channel partners	• Channel 'best' commitment to have channel-excellence and industry 'best' at the Group's core • Industry-leading partner programme • Partner conferences and global events • Dedicated partner portal • Partner advisory councils • Webinars and live online events including product and threat landscape training	• Partner conferences in the Americas, EMEA and APJ with CEO and members of the SMT participating as speakers • Regional partner programmes • Partner advisory meetings in key markets
End customers	• Community and support forums • Social media engagement • Dedicated and targeted product communications • VIP Newsletter and Sophos News updates • Daily industry news service – NakedSecurity • Free tools for home use (Sophos Home, XG Firewall, Sophos Mobile) • Enduser events in key markets • Webinars and live online events	• Customer events across Americas, EMEA and APJ markets • Significant upgrade to Sophos Home Premium offering, including industry-leading next-gen artificial intelligence capabilities
Employees	• Intranet site "Sophos Hub" for collaboration, communication and information • Annual employee survey • Access to online training tools and instructor-led training	• Annual kick-off led by CEO • Quarterly business updates • Local kick-off events • Social events run locally
Investors and analysts	• Investor roadshows • Results presentations and webcasts • Conference calls • Annual general meeting • Investor and analyst 1:1 meetings	• Major refresh to investor website launched, with new tools and resources to aid analysis and understanding • Publication of Company-compiled consensus • Comprehensive consultation with respect to revised remuneration policy and matters of corporate governance • Analyst and investor visits to UK headquarters • Participation in leading investor conferences in US and Europe
Community	• Employee driven charity and community actions in local offices, supported by senior management team and local management	• Continued sponsorship of the UK National Computing Museum • Charitable and community activities undertaken around the world supporting a wide range of causes

Securing our customers

Sophos' mission is to be the best in the world at delivering innovative, simple and highly effective cybersecurity solutions. With more than 100 million users across 150 countries and 335,000 businesses relying on Sophos to protect them against complex threats and data loss, the Group has a significant duty to protect and secure its customers 24/7.

Organisations are struggling to identify the entry point of most attacks and do not know how long an attacker might have been on their network. A recent survey by Sophos revealed that 20 per cent of IT managers admitted not knowing how their most significant attack got in and 17 per cent couldn't determine how long an attack was resident on a network. On average, organisations that investigate one or more potential security incidents each month spend 48 days a year (four days a month) investigating them. It is not surprising that 80 per cent of respondents wished they had a stronger IT team in place*.

In November 2018, Sophos introduced two significant developments to help address the top concerns of organisations worldwide. The most recent version of the XG Firewall includes lateral movement protection to prevent targeted, manual cyber-attacks or exploits from infiltrating further into a compromised network. By sharing intelligence between the firewall and endpoints and automatically isolating infected systems, organisations can reduce the blind spots on their network switches or LAN segments that can become launch pads for attacks. The new features in Sophos XG Firewall prevents threats from spreading, even where the firewall doesn't have direct control over traffic.

In October 2018, Sophos launched Intercept X Advanced with EDR. Effective investigation and incident response had previously only been achievable in organisations with a dedicated Security Operations Center ("SOC") or specialised IT security team trained to hunt and analyse cyber-attacks. With Sophos Intercept X Advanced with EDR, businesses of all sizes and those with limited resources can add threat tracking and SOC-like capabilities to their security defences, reducing the time criminal hackers can hide in their network.

CASE STUDY

Synchronized security

Spicerhaart, a UK-based real estate agency has deployed Sophos Intercept X and XG Firewall network protection and is benefitting from synchronized security. Prior to deploying Sophos, Spicerhaart experienced several CryptoLocker-style ransomware attacks. Due to robust backups, no ransom was paid and the data was restored. However, Andrew Chaplin, IT Infrastructure Manager at Spicerhaart, knew that they could become the target of subsequent cyber-attacks and needed to put Sophos security in place. In addition, the pressure to achieve and maintain compliance with GDPR, which came into effect in May 2018, also influenced a greater priority on data security.

"Staying ahead of today's cyber threats is paramount. With synchronized security, we have coordinated our defences and maximised all of our resources. Regardless of the attack complexity or surface, we are now more prepared than ever before"

* www.sophos.com/truths

Collaboration is key

The cybersecurity market today is complex, crowded and competitive. Organisations are overwhelmed with the daily response to threats and the numerous security solutions that are on the market. At Sophos, our mission is to be the best in the world at delivering innovative, simple and highly effective cybersecurity solutions, and to do that we collaborate with all industry participants.

SophosLabs contributed significantly to the industry's understanding of the cybersecurity ecosystem with dedicated research into recent threats, cybercriminal behaviour, and recommendations for building algorithms for machine learning. This research provides in depth analysis and steps for best security practices for fellow researchers and customers alike. This research is available on Sophos.com. Highlights include:

- SamSam: The (Almost) Six Million dollar Ransomware.
- Chalubo Botnet Wants to DDoS From Your Server or IoT Device.
- "Known Unknowns": Overcoming Catastrophic Failure Modes in Artificial Intelligence.
- Machine Learning With Feature Selection Using Principal Component Analysis for Malware Detection: A Case Study.
- Grandcrab 101: All About the Most Widely Distributed Ransomware at the Moment.
- SophosLabs 2019 Threat Report.

In addition to in-depth research, SophosLabs has been issuing data directly from researchers as it is analysed. In SophosLabs Uncut on Sophos News, researchers from all over the world are now sharing with the industry pertinent reports about threats they've deconstructed or uncovered.

Sophos Executives have also actively contributed to the advancement of the industry, including the sharing of contextual threat data with industry partners in the Cyber Threat Alliance ("CTA"). CTA brings executives and experts from cybersecurity vendors together to collaborate in a non-competitive environment for the advancement of the industry. In February this year, Sophos CTO, Joe Levy joined CTA's Board of Directors.

"Being transparent when discussing future technology strategies between competing vendors has always been challenging, but by creating a trusted forum where the industry's brightest minds can come together, we're able to join forces and strengthen the fight against adversaries." – Joe Levy, CTO, Sophos.

In June 2018, the non-profit Anti-Malware Testing Standards Organisation ("AMTSO") officially approved and adopted the AMTSO Testing Protocol Standard. As a founding member, Sophos was proud to vote in favour of the standard.

While imperfect and challenging, independent testing of cybersecurity technology is important to Sophos. In the Principles of Third Party Testing, Sophos outlines why testing is good for vendors, customers and the industry as whole.

> "There should be a partnership between the testing labs, end users and vendors. Testing labs should under-promise and over-deliver, and work with vendors to configure environments correctly. End users should continuously be clear on the specific items they want to see reviewed, and vendors should make it easy for their products to be scrutinised"

Joe Levy, CTO, Sophos

Number of Employees

3,400

(FY18: 3,300)

Overall Employee Satisfaction

86%

(FY18: 87%)

Engaging people

Guided by the Group's core values of simplicity, empowerment, passion, innovation and authenticity, the Group seeks to promote a culture where its people can thrive. For Sophos, this means promoting strong business ethics and putting in place policies and programmes to build trust with employees.

Creating an ethical culture

As a first priority, Sophos seeks to uphold individual human rights in its operations and expects the same from all partners. The Group's policies outline the behaviours expected from employees and suppliers at all times and set out the Group's zero tolerance approach towards any form of modern slavery, discrimination, or unethical behaviour relating to bribery, corruption or business conduct.

To support its people, the Group makes development opportunities available to all employees through access to one of the largest online libraries of e-learning courses in the world for technical, personal and leadership skills development, as well as role-specific training and access to Instructor-Led Training. This training is aligned to personal development initiatives such as quarterly manager 'check-ins' and real-time coaching.

Promoting diversity

The Sophos diversity policy outlines the Group's commitment to building an inclusive culture, where people feel able to be their best at work, irrespective of age, race, sexual orientation, religion, national origin or gender. Sophos is passionate about creating a workplace that promotes equal opportunities and prides itself on recognising and rewarding team members based on merit above anything else.

At the end of the financial year, the gender breakdown of employees and Directors was is shown in the table below:

	31 Mar 2019		31 Mar 2018	
	Female	**Male**	**Female**	**Male**
Executive & Non-Executive Directors	2	6	2	7
Senior Managers*	20	65	18	75
Employees	767	2,521	760	2,500

* The Group has defined senior managers as members of the SMT and their direct reports (excluding executive Directors separately reported) as is set out in the Groups' diversity policy.

In 2017, the UK government introduced new legislation requiring companies with 250 or more employees to publish their gender pay gap. The Group's median gender pay gap in the 12 months to April 2017 was 23.4 per cent. In the 12 months to April 2018, Sophos reduced this gap to 17.2 per cent, and achieved greater female representation in the upper pay quartiles.

The Group believes its current pay gap is due to lower female representation at the higher levels of the organisation and a high percentage of men in specialist positions carrying a higher market premium. It is however encouraging to see progress, as the Group continues to enhance gender diversity and ensure equitable pay for all genders throughout their careers.

In line with this commitment, Sophos continued to promote gender diversity in FY19 through its actions and activities, which included:

- Continuing our work as one of the founding organisations of the PWC "Tech She Can" initiative.
- In FY19, Sophos women attended and sponsored various women in technology and cybersecurity events in our major office locations.
- Introducing new Maternity Leave Policies.
- Celebrating International Women's Day with various global office events, speakers, support of local women charities and special recognition of a spotlight of women across Sophos.
- Introducing a new apprenticeship scheme to provide alternative routes for women to pursue technical careers at Sophos.
- Providing unconscious bias training to managers and employees.

Sophos women in technology

The Sophos Women in Technology forum was launched in late 2017 to promote gender diversity in the technology industry. There are now dedicated groups running in the UK, Canada, U.S. and India with galvanising launch events, subsequent actions, and projects.

The purpose of the initiative is to make Sophos a great place to work for women in the technology industry – spanning technical and non-technical roles. The focus of the group is to help women develop the skills they need, and create a supportive environment where they can progress in the business and enhance their career development at Sophos.

Sophos staff walk against breast cancer

A 60+ strong group of Sophos colleagues, known as the “Sophos Interceptors”, hit the Thames Path to walk a marathon along the course of the river from our office in Abingdon to Pangbourne, near Reading, as part of the Breast Walk Ever campaign.

The group ran a number of fund-raising activities in advance of the walk, from car washes to dunk tanks, culminating in a fantastic £22,500 being raised for the charity.

CORPORATE RESPONSIBILITY REPORT CONTINUED

Enhancing communities

Sophos is committed to helping others and using its resources, expertise and insights to make a positive difference to the communities where it operates. The Group encourages local offices around the world to support community projects and initiatives relevant to them and participated in many local initiatives to enhance communities during the year.

UK

The Group became a corporate foundation sponsor at the National Museum of Computing in Bletchley in 2017, where the history of computing and security can be seen in action with the world's largest collection of functioning historical computers. Sophos has committed to sponsor the museum until 2020 and in FY19 our funding helped them completely refurbish a classroom, which is now used multiple times each week to host school children. There is a particular focus on bringing girls into coding and helping children with autism, and Sophos supported this by sending a presenter and resources to a girls STEM day which hosted 80 young female students.

Canada

Every December for the past several years, Sophos Canada employees have raised funds for YWCA's "Presents of Peace".

This local initiative focuses on assisting families in need so that they may have a special Christmas. In 2018, employees were matched with two families for whom funds were raised through activities such as bake sales, raffles, auctions and sporting competitions.

Employees volunteered in building a Habitat for Humanity home to help families in need of affordable housing.

Over 60 employees volunteered to help support, clean and maintain park trails and their surrounding environment.

US

In December, a "Giving Tree" decorated with Christmas wishes of children in foster care is erected in the office. Employees purchase and wrap all the gifts. A group of employees volunteer at a local food pantry on a monthly basis.

India

Sophos India focuses its community engagement efforts on improving the infrastructure of a local village near to its offices. Ropda was selected by employees after extensive community engagement and recognition of a local need. With the aim of enhancing the quality of life for people living in the village, the team identified four key focus areas to target:

- **Education:** Despite there only being one school in the village, the attendance rate was just 25 per cent when Sophos employees arrived in Ropda. To address this, a campaign was launched to encourage parents to enrol their children into school to improve literacy rates. As a result, the attendance rate increased from 25 per cent to 85 per cent by the end of the year, including 100 per cent attendance for exams. A water purification plant was also built at the school, as well as a meal shed to encourage better health and hygiene. Sophos is now in the process of building another school.
- **Sanitation:** As is common in many Indian rural villages, there was no central sanitation facility or drainage system in the village. Toilets were built in over 20 houses, and a drainage system was installed throughout the village to ensure effective waste management and cleanliness.
- **Infrastructure**: 60 solar street lights were installed to reduce the financial burden of villagers and promote renewable energy. Beyond this, a new road was constructed to better connect the village to the surrounding community.
- **Health and fitness:** Half-yearly health check-ups were introduced and villagers were put in contact with local hospitals where they are now able to seek treatment at a subsidised cost.

tCO_2e per $m billings

10.5

(FY18: 12.9)

Protecting the environment

As an office-based organisation, Sophos is an environmentally low-impact business. The Group has therefore not adopted a formal environmental policy. Despite this, the Group recognises the responsibility it has in managing its environmental performance and conducting local initiatives to reduce its overall carbon footprint, waste profile and water impact.

Greenhouse gas emissions

In line with the Companies Act 2006, Sophos is required to measure and report on its Greenhouse Gas ("GHG") emissions disclosures. These have been calculated for the year-ending 31 March 2019, in line with the Group's financial year. The calculation of the disclosures has been performed in accordance with Greenhouse Gas Protocol Corporate Standard and using the UK government's conversion factor guidance for the year reported.

The Group's operations that primarily release GHG includes usage of electricity and gas of owned and leased offices, business travel and usage of vehicles. The Group keeps its data capture process under review, seeking to extend the availability of direct information wherever possible. Where direct information for certain sites is not available, estimates have been developed that enable reporting for them. These estimates are revised if new or improved data is obtained.

The Group will continue to build its GHG reporting capabilities. The Group's chosen intensity ratio is 'tonnes of CO_2 equivalent per million US dollars of billings' as it aligns with Sophos' strategic growth ambitions.

Creating an environmentally friendly HQ

The Group commissioned a greening study of its global headquarters in Abingdon, Oxfordshire. The purpose of the study was to benchmark the current environmental, health and wellbeing performance of the building against current best practice and against direct and indirect competitors.

The findings of the study showed that the building performance was consistent with intermediate good practice and the building management was consistent with standard good practice. The study highlighted areas of future improvement. The findings and recommendations of this report will be a key driver for developing best practice in environmental sustainability to match the growth aspirations and objectives of the Company.

The Group is endeavouring to achieve the standards in environmental performance, health and wellbeing that is expected of a global technology organisation at the Group's headquarters.

		Year-ended 31 March 2019 tCO_2e	Year-ended 31 March 2018 tCO_2e	Year-ended 31 March 2017 tCO_2e
Scope 1	Combustion of natural gas and operation of owned vehicles	220.9	320.0	251.8
Scope 2	Electricity consumption in offices	4,487.2	4,457.3	4,681.9
Scope 3	Business travel (air and car)	3,260.9	5,117.4	4,510.9
Total		7,969.0	9,894.7	9,444.6
Intensity ratio				
tCO_2e per $M of billings		10.5	12.9	14.9

Strategic report approval

The strategic report on pages 8 to 50 was approved by the Board on 15 May 2019 and signed on its behalf by:

Kris Hagerman

Chief Executive Officer

15 May 2019

Zero to landfill

The Group moved to a ‘zero to landfill’ waste supplier in 2018 at the Abingdon HQ. As such all site waste is sent for recycling and where not possible the waste goes through energy recovery resulting in zero to landfill. Over the course of the last financial year, the Abingdon office saved the equivalent of 17.27 tons of CO_2 and generated over 24MWh of energy from its waste. From the paper and card that was recycled the equivalent of 259 trees were saved. In January of 2019 a new strategy for recycling was adopted with the removal of all personal desk bins on site and the implementation of new recycling stations. As part of the new recycling strategy, the introduction of food waste recycling was put in place which will be used in biomass boilers to produce energy through the waste supplier.

Managed Service Providers

Sophos MSP Connect

Sophos Central provides the platform for the Sophos MSP Connect program, with a comprehensive product set enabling our channel partners to fully meet their customers' security requirements. From endpoint and server protection to email, web, mobile, wireless, public cloud, phishing simulation, and encryption.

The intuitive partner dashboard within Sophos Central allows channel partners to manage all of their customers' Sophos products through a single, intuitive cloud interface. There are clear benefits as this reduces administration time and provides our partners with an additional service revenue opportunity. Furthermore, Sophos Central delivers synchronized security, with all the products sharing information via a patented Security Heartbeat™ and automatically responding to threats, thus delivering faster, better protection, and giving Sophos Managed Service Partners a unique differentiator.

Allowing a trusted partner to manage their security estates remotely via Sophos Central is a particularly attractive model for many smaller enterprises. Typically, these businesses lack the resources to establish, monitor and maintain an effective cybersecurity operation, hence a service-based monthly subscription model, leveraging the partner's expertise, is an effective option. The Group's MSP business is growing rapidly and now has over 47,000 customers, and thousands of channel partners on the program.

Find out more at:
www.sophos.com/msp

Governance

BOARD OF DIRECTORS

PETER GYENES
Non-Executive Chairman

COMMITTEE MEMBERSHIP
Chairman of Nomination
Member of Remuneration

EXPERIENCE
Peter joined the Sophos Board in June 2006, bringing experience with corporate growth and value creation to the Group's vision for integrated threat management leadership. Peter has four decades of experience in technical, sales, marketing and general management positions within the computer systems and software industry globally and was most recently the Chairman and CEO of Ascential Software Corporation. He has also served on the boards of Carbonite Inc., Applix Inc., BladeLogic Software, Epicor Software Corporation, Lawson Software, EnerNOC Inc., Cimpress NV, Intralinks Holdings, Inc. and webMethods.

QUALIFICATIONS
BA in Mathematics and an MBA, Columbia University, New York

KEY EXTERNAL APPOINTMENTS
Director of Information Builders, Inc., Pegasystems Inc., RealPage, Inc. and is trustee emeritus of the Massachusetts Technology Leadership Council

KRIS HAGERMAN
Chief Executive Officer

COMMITTEE MEMBERSHIP
Member of Disclosure

EXPERIENCE
Kris joined Sophos in 2012 as CEO. Kris was most recently CEO of Corel Corporation, and prior to that, group president, data centre management at Symantec, where he led a business of more than $1.5 billion that represented nearly 30 per cent of Symantec's global revenue. Prior to Symantec, Kris was EVP and GM, storage and server management, at Veritas Software where, during his tenure, the company's revenue more than doubled, before its acquisition by Symantec. Earlier in his career, Kris was founder and CEO of BigBook and prior to that, Affinia. Kris also held positions at Silicon Graphics and McKinsey & Company.

QUALIFICATIONS
BA in Russian and Economics, Dartmouth College, an M.Phil. in International Relations, Cambridge University, and an MBA, Stanford Graduate School of Business

KEY EXTERNAL APPOINTMENTS
None

NICK BRAY
Chief Financial Officer

COMMITTEE MEMBERSHIP
Member of Disclosure

EXPERIENCE
Nick joined Sophos in 2010 as CFO, bringing more than 20 years' experience in the technology sector, extensive international operational skills and significant public company experience on both the London Stock Exchange and Nasdaq. Nick was most recently CFO at Micro Focus International plc, where he was instrumental in the company tripling revenue and increasing market capitalisation from circa £200 million to in excess of £1 billion. He has also held Group CFO roles at Fibernet Group plc and Gentia Software plc, as well as senior financial positions at Comshare Inc. and Lotus Software.

QUALIFICATIONS
First class BA in Civil Engineering, Aston University, and a qualified Chartered Accountant

KEY EXTERNAL APPOINTMENTS
Non-Executive Director of De La Rue plc

SANDRA BERGERON
Independent Non-Executive Director

COMMITTEE MEMBERSHIP
Member of Audit and Risk, Remuneration and Nomination

EXPERIENCE
Sandra joined the Sophos Board in June 2010. Sandra has more than 20 years' security, operations and board advisory expertise having previously served on the boards of TraceSecurity Inc., Tipping Point, Netegrity, Nuance Communications, TriCipher Inc., and ArcSight Inc. Earlier in her career Sandra spent 10 years at McAfee, Inc. holding a number of key executive positions.

QUALIFICATIONS
MBA from Xavier University, Cincinnati, Ohio and a BBA in Business Administration (Cum Laude), Georgia State University

KEY EXTERNAL APPOINTMENTS
Director of F5 Networks, Inc. and Qualys Inc

ELEANOR LACEY
Executive Vice President, Chief Legal Officer and Group Company Secretary.

COMMITTEE MEMBERSHIP
Member of Disclosure

EXPERIENCE
Eleanor joined Sophos in 2016 as SVP General Counsel and Company Secretary. Most recently, Eleanor had been SVP, General Counsel and Corporate Secretary at SurveyMonkey Inc. Prior to SurveyMonkey she has held the roles of General Counsel and VP of Business Development at Corel Corporation, VP of Corporate Development at SupportSoft, Inc. and VP and General Counsel at Niku Corporation, prior to its acquisition by Computer Associates.

ROY MACKENZIE

Non-Executive Director

COMMITTEE MEMBERSHIP

Member of Nomination

EXPERIENCE

Roy joined the Sophos Board in June 2010. Roy is a partner of Apax Partners' technology and telecoms team. He joined Apax Partners in 2003 and has been involved in a variety of technology focussed investments including Epicor Software Corporation, NXP Semiconductors, and King Digital Entertainment plc. Previously, Roy worked at McKinsey & Company, Inc., focusing on consulting clients in the high technology sector and also held product management positions at Psion Computers.

QUALIFICATIONS

MBA, Stanford Graduate School of Business and an MA in Engineering, Imperial College, London

KEY EXTERNAL APPOINTMENTS

Director of Duck Creek Software, Inc. and Exact Holdings NV

RICK MEDLOCK

Independent Non-Executive Director

COMMITTEE MEMBERSHIP

Chairman of Audit and Risk
Member of Remuneration and Nomination

EXPERIENCE

Rick joined the Sophos Board in April 2017. Rick has 30 years of experience in the financial management of large international technology companies. Rick is currently CFO of Synamedia, the leading provider of video content solutions. Previously, Rick was CFO at Worldpay until the completion of its merger with Vantiv in February 2018 prior to which, Rick was CFO of Misys until December 2013. Before joining Misys, Rick had spent nine years as CFO of Inmarsat plc and seven years as CFO and Company Secretary of NDS Group plc. He was also a Non-Executive Director and Chairman of the Audit Committee of Edwards Vacuum (Edwards Group Ltd). He spent the early part of his career in a variety of roles as CFO of a number of private equity backed technology companies in the UK and the US.

QUALIFICATIONS

MA in Economics, University of Cambridge and a qualified Chartered Accountant

KEY EXTERNAL APPOINTMENTS

CFO of Synamedia Holdings Limited

VIN MURRIA OBE

Independent Non-Executive Director

COMMITTEE MEMBERSHIP

Member of Audit and Risk, Remuneration and Nomination

EXPERIENCE

Vin joined the Sophos Board in January 2017. Vin was founder and CEO at Advanced Computer Software and CEO of Computer Software Group. Previously, Vin was also an Independent Non-Executive Director of Zoopla Property Group plc, a Non-Executive Director of Chime Communications, Greenko Group and Concateno. Vin was named Cisco's Woman of the Year and Tech Entrepreneur of the Year in 2012 and in addition, Advanced Computer Software was named Tech Company of the Year in 2014. Vin received an OBE for services to the Digital Economy and the Empowerment of Women in Software and Technology in the 2018 New Year's Honours list.

QUALIFICATIONS

BSc (Hons), an MBA, and a Doctorate business administration (Honorary), Edinburgh Napier University

KEY EXTERNAL APPOINTMENTS

Independent Non-Executive Director at Softcat plc and DWF Group plc and a Non-Executive Director at finnCap Group plc, Senior Advisor – Rothschild Global Advisory team, and a partner at Elderstreet Investments

PAUL WALKER

Senior Independent Director

COMMITTEE MEMBERSHIP

Chairman of Remuneration
Member of Audit and Risk and Nomination

EXPERIENCE

Paul joined the Sophos Board in June 2015. Paul brings more than 30 years of technology and senior leadership experience to the Board of Sophos, having served for 16 years as CEO of Sage Group plc., a leader in business solutions for small and medium businesses. With extensive board experience, Paul is currently Non-Executive Chairman of Halma plc and Ashtead Group plc. Paul is also a Non-Executive Director of Experian plc, but will retire in July 2019 following the completion of his third three-year term. Paul has previously served on the boards of WANdisco plc, Diageo plc, and My Travel Group plc and Perform Group Ltd.

QUALIFICATIONS

BA in Economics, York University, and a qualified Chartered Accountant having trained at Ernst & Young

KEY EXTERNAL APPOINTMENTS

Non-Executive Chairman of Halma plc and Ashtead Group plc, and a Non-Executive Director of Experian plc

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QUALIFICATIONS

J.D., Yale Law School and BA in History and English, University of Massachusetts at Amherst

KEY EXTERNAL APPOINTMENTS

None

CORPORATE GOVERNANCE STATEMENT

CHAIRMAN'S INTRODUCTION

Ensuring that we create a framework and culture that supports good governance is at the heart of what we do as a Board and is one of my principal responsibilities as Chairman.

In doing so, long-term value for shareholders is created and the interests of our key stakeholders is promoted.

Dear Shareholder,

With the full support of the Board, I am committed to maintaining a robust governance framework to ensure that we discharge our duties responsibly in setting our strategy and long-term objectives, monitoring and providing oversight to the performance of management and progress of our business, managing our risks, and carrying out our business with integrity. Good corporate governance is critical in helping to build a successful business that is sustainable over the longer term, in the dynamic, fast-paced markets in which we operate. The revised UK Corporate Governance Code ("the Code"), which we will report more formally next year, specifically puts relationships between companies, shareholders and stakeholders at the heart of long-term success and places emphasis on businesses building trust by creating strong relationships with key stakeholders. This report sets out our approach to governance and the work of the Board and its Committees during the year.

In carrying out these responsibilities, the Board holds meetings regularly with management to review operating performance and strategic progress.

Corporate Governance Code compliance

The Board spends considerable time focusing not only on operational matters, risks and financial reporting, but also focuses on how the strategy is being implemented and progress maintained. We also focus on the longer-term future and the implications that a changing market place might have. We do this in several ways, including actively seeking out internal and external perspectives on how the market place might develop and what risks and opportunities might emerge and how these should be addressed.

Board meetings in FY19

April	May	July
100% attendance	100% attendance	90% attendance

UK Corporate Governance Code compliance

This report, which is available on the Company's website, explains the key features of the Company's governance structure to provide a greater understanding of how the main principles of the Code have been applied and to highlight areas of focus during the year. The Code can be found on the FRC's website at **www.frc.org.uk**.

During the year, the Company complied with all the principles and provisions of the 2016 Code.

Board evaluation

FY17	FY18	FY19	FY20
External evaluation	Internal evaluation	Internal evaluation	External evaluation

I am pleased to report that Sophos has this year complied in full with the Principles, and applied the provisions of the Code and expects to continue to do so during this year.

Board composition

Steve Munford stepped down as a Non-Executive Director on 8 February 2019. Steve had been a member of the Board for almost four years, having previously served as the Company's Chief Operating Officer and Chief Executive Officer. On behalf of the Board, I would like to thank Steve for his invaluable contribution to Sophos during the past 15 years. Full details of the Board's composition are set out on page 54 and 55.

Board evaluation

In accordance with current best practice and the Code, the Board undertakes an annual formal evaluation of its performance and effectiveness and that of each Director and its Committees. As Chairman, I see this as an opportunity for the Board to re-focus how it operates and to assess whether any adjustments are required to improve further its effectiveness. We welcome the UK Government's continued focus on wishing to improve the quality and effectiveness of Board evaluations, in particular, those conducted using external parties.

In March 2019, with the support of the Company Secretary, I led the FY19 evaluation of the Board and its Committees, with the internally generated questionnaires focusing on the priority areas identified in the previous year's evaluation and how effectively these have been progressed. The outcomes and decisions we are taking are summarised on pages 60 and 61.

Shareholder engagement

The Board encourages and maintains an active dialogue with shareholders, listens to the views of representatives of investors and financial institutions, and regularly monitors and considers shareholder sentiment and feedback. We believe that the design and operation of a robust yet evolving governance framework, appropriate for a group of the scale and ambition of Sophos, remains critical in ensuring we properly understand the views of our shareholders. Further details of our engagement with shareholders during the year are noted earlier in this report, on page 42, and in the Annual Statement of the Remuneration Committee Chairman, on pages 78 to 81.

Conclusion

Each of us on our Board are committed to a governance framework, across the organisation. We believe that this provides the appropriate environment to ensure rigorous focus on creating long-term value, together with focus on all of our stakeholders.

Peter Gyenes

Non-Executive Chairman

15 May 2019

August	November	February
100% attendance	90% attendance	100% attendance

Our governance structure

The Company's governance is structured through the Board and a number of Committees that support the effective discharge of its duties, as illustrated below.

Board of Directors

The Board is collectively responsible for the long-term success of the business. It provides leadership and direction, including setting and overseeing the implementation of the strategy, monitoring management activity and performance, building relationships and trust with our major stakeholders, ensuring that the Group operates within an appropriate risk and control framework and establishing the culture and values of the organisation.

More details on the roles and responsibilities of the Board are set out on pages 62 to 66

Audit and Risk Committee

The Audit and Risk Committee is responsible for oversight of the Group's financial reporting processes and significant financial judgements, the integrity and clarity of the Financial Statements, review of the risk management and internal controls framework, and agreeing the scope and effectiveness of the external audit process. The Audit and Risk Committee also directly oversees the process for the selection of the external auditor and makes recommendations for their appointment.

For further information, see pages 71 to 76

Nomination Committee

The Nomination Committee reviews the structure, size and composition of the Board and its Committees, and makes recommendations to the Board accordingly. It has responsibility for succession planning at Board level to ensure that the Board retains an appropriate and diverse balance of skills and experience to effectively lead the Company.

For further information, see pages 68 to 70

Remuneration Committee

The Remuneration Committee reviews and recommends to the Board the Remuneration Policy and determines the remuneration packages of the Executive Directors whilst overseeing the appropriateness of the remuneration structure for executive management and the wider employee population.

For further information, see pages 78 to 101

Disclosure Committee

The Disclosure Committee is responsible for overseeing the disclosure of information by the Company to meet its obligations under the Market Abuse Regulations and the Financial Conduct Authority's List Rules and Disclosure Guidance and Transparency Rules.

For further information, see page 77

Risk and Compliance Committee

The Risk and Compliance Committee is a management Committee that has a direct reporting line to the Audit and Risk Committee, providing an additional level of assurance.

Senior Management Team (SMT)

The SMT is led by the CEO and comprises senior management from across the business. Its role is to provide the highest executive level governance and discussion forum, responsible for optimising performance and delivery of strategic objectives. It also assists in the implementation of operating plans, budgets, policies and procedures, and manages the operational and financial performance of the business.

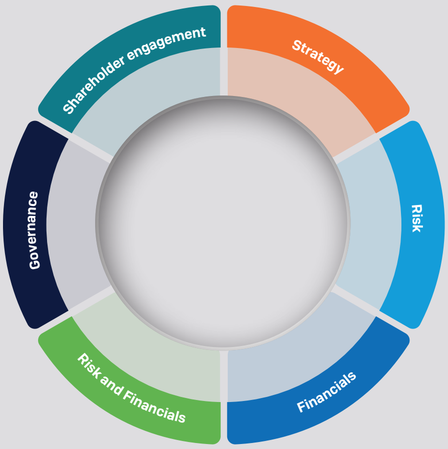
Attendance at scheduled meetings of the Board and Committees held during the year

Where Directors were not able to attend meetings, this was entirely due to prior business commitments. In each case, they reviewed the papers circulated for that meeting and provided comments directly to the Chairman or Committee Chairman, as appropriate.

	Board	Audit and Risk Committee	Nomination Committee	Remuneration Committee	Disclosure Committee
Peter Gyenes[1]	100%		100%	100%	
Kris Hagerman	100%				100%
Nick Bray	100%				100%
Sandra Bergeron	67%	100%	100%	100%	
Roy Mackenzie	100%		67%		
Rick Medlock[2]	83%	100%	100%	100%	
Steve Munford[4]	100%				
Paul Walker[3]	100%	83%	100%	100%	
Vin Murria	100%	100%	100%	100%	

1 Peter Gyenes is Chairman of the Board and of the Nomination Committee
2 Rick Medlock is Chairman of the Audit and Risk Committee
3 Paul Walker is Chairman of the Remuneration Committee
4 Steve Munford resigned as of 8 February 2019

Board focus during FY19



Strategy

- Provided strong oversight of the Group's strategy and growth plans, and considered the key risks; and,
- Discussed potential future acquisition opportunities in support of the Company's strategy.

Risk

- Retained focus on the performance of the Company's existing portfolio of products, key risks to delivery for the portfolio, together with the ongoing portfolio management strategy and different portfolio scenarios; and,
- Retained focus on risk, and in particular cybersecurity.

Financials

- Reviewed the Company's operating results and Financial Statements with management and the Company's external auditor. The Board also reviewed and approved the operating plan for the fiscal year.

Risk and financials

- Reviewed the Annual Report including detailed consideration of the identified principal risks and their continued effective management to achieve the Group's strategic objectives, the ongoing appropriateness of the adoption of the going concern basis of accounting, the appropriateness of the Viability Statement disclosure; and, ensured that the Annual Report was fair, balanced, and understandable and it provided the information necessary to assess the Group's position and performance, business model and strategy.

Governance

- Reviewed the changing corporate governance landscape and kept under review the Group's own corporate governance arrangements including GDPR preparedness, internal policies relating to share dealing, inside information and disclosure, whistle blowing, and the Modern Slavery Act Transparency Statement;
- Retained focus on those areas recommended for improvement during the FY18 Board evaluation process and implemented changes accordingly; and,
- Undertook an internal evaluation of its performance and effectiveness, and that of each Director and Committees.

Shareholder engagement

- Undertook a shareholder engagement programme with key shareholders concerning the proposed new Remuneration Policy. Advisors also provided the Board with an update on investor sentiment. Further details can be found in the Annual Statement of the Remuneration Committee Chairman on pages 78 to 81.

CORPORATE GOVERNANCE STATEMENT CONTINUED

Board evaluation

In accordance with current best practice and the Code, the Board undertakes an annual formal evaluation of its performance and effectiveness and that of each Director and its Committees. It is the Board's policy to invite external evaluation every three years. The last external evaluation took place in FY17, and the Board will conduct its next external evaluation during FY20. As part of the FY19 Board Evaluation Paul Walker and the NEDs considered, without the Chairman present, the Chairman's performance.

Evaluation process during FY19

1. The Chairman with the support of the Company Secretary discussed and agreed the scope of the evaluation. A questionnaire was developed for the Board and for each of its Committees.
2. The relevant questionnaires were issued to each of the Directors for consideration and comment, and appropriate time provided for completion.
3. The Company Secretary compiled the individual Director responses and, following analysis of the comments, provided a report to the Chairman for consideration. A paper setting out the findings, along with proposed actions, was discussed by the Board.
4. Following discussion, the Board agreed objectives for its own performance and that of its Committees for the next 12 months. The Chairman and Company Secretary agreed to monitor and facilitate the implementation of any actions as required and provided progress updates to the Directors.

The Board questionnaire focused on the four principal matters raised during the previous evaluation, as well as considering various aspects of risk.

Group strategy (utilising the 2019 Strategy Day as the measure)

- The appropriateness of the agenda, the quality of the pre-meeting papers and how these might be improved.
- The allocation of time.
- How well were the long-term strategic issues drawn out.
- How well was the competitor landscape covered and understood by the Board.
- The clarity and articulation of the conclusions reached.

Succession

- The appropriateness of the current Board composition.
- The key changes that might be made to the profile of the Board over the next three years to match the Company's strategic goals.

Directors' development

- The approach to Board development/training, with a mix of the use of external resources and its internal focus on targeted topics at Board and Committee meetings.

Stakeholder engagement

- The Board's understanding of the views and requirements of various stakeholders (shareholders, customers and channel partners).
- The Board's understanding of the view and requirements of employees across the organisation.
- The culture and behaviours across the Group.

Actions taken in FY19 following the FY18 evaluation

Overall the evaluation of the Board and its Committees was very positive with progress noted in each of the development areas identified during last year's Board evaluation, namely Annual Strategy Day; Succession (Board and Management); Development (Directors) and Stakeholder Engagement. Some recurring themes had emerged across the Board and its Committees which have been summarised below and which will form the basis of the matters to be addressed during FY20 to further improve the effectiveness of the Board and its Committees and how they operate. For the Committees specifically, the effective use of time and the quality of the information provided were both factors positively scored.

Recommendations for FY20 following the FY19 evaluation are set out below:

Board agenda: Built into each year's calendar from November 2018 onwards is a dedicated Annual Strategy Day when Directors take part in a structured programme with the wider management team and invite speakers on the long-term strategy of the organisation and the context within which it operates. Topics at the November 2018 Strategy Day included the wider industry landscape, product and go-to-market strategies. The structure of the day and the pre-circulated papers were well received, although recommendations were made on how these might be improved.

The next Strategy Day will be taking place in December 2019. Account will be taken of the feedback received from the Directors and incorporated into the planning for December. Amongst several identified opportunities to enhance the programme in FY20, consideration would be given to providing more visibility on the financial model and the options which management believe they face, the investments required and how these options might manifest in terms of financial outcomes over the long-term plan. In future, and on a quarterly basis, strategy checkpoints would be incorporated into the Board's agenda.

Board succession: This remains a key area of consideration for the Nomination Committee. From feedback received, and owing to the retirement of Steve Munford in December 2018, a skills matrix is being prepared highlighting any gaps the Directors believe currently exist or are likely to exist going forwards due to normal Board rotation and the new UK Corporate Governance Code. A structured and managed succession plan is being prepared and will be addressed by the Committee over the coming year.

Developing stakeholder engagement: There was a general view that the Board's understanding of various constituencies could be strengthened, particularly in respect to the management layers below the senior management team, the wider workforce. With the new UK Corporate Governance Code and the requirement for Boards to engage more effectively with the wider workforce, the Board will put in place mechanisms through which its designated Non-Executive Director can interact more effectively with the wider workforce. Whilst developing these new mechanisms, it will also make use of those existing opportunities for engagement, including feedback from employee surveys. This will also help the Board more effectively monitor culture and behaviours throughout the organisation.

Board development: The Board's development programme, established in FY19, comprises a mix of internal and external development opportunities and topics for Board and Committee meetings through the remainder of FY20. From feedback received during the evaluation, the new programme covers the appropriate topics on shareholder sentiment, regulations and governance as well as the technical and competitive landscape relevant to the Group. Going forward into FY20, this new programme will be monitored, feedback will be sought and, where thought necessary, amended ahead of FY21. Risk management was specifically identified during the evaluation as a topic requiring more focused training.

CORPORATE GOVERNANCE STATEMENT CONTINUED

Our approach to governance

The Company is committed to maintaining a high standard of corporate governance. This report, which is available on the Company's website, including the Audit and Risk Committee report, Directors' Remuneration report, the Nomination Committee report and the Disclosure Committee report, explains how the Company has applied the main principles and provisions of the Code: leadership; effectiveness; accountability; remuneration; and, relations with shareholders.

The Company's business model is explained in the strategic report. It is the Board's view that it has been fully compliant with the principles, and applied the provisions of the Code throughout the financial year.

Details of Directors' independence are set out on pages 63 and 64.

A: Leadership

A.1 The role of the Board

The Board is collectively responsible to Sophos shareholders for promoting the long-term success of the Company and the operation of effective governance arrangements. The steps the Board takes to facilitate this are set out on page 67. The Board provides leadership and sets the Company's strategic long-term objectives.

The Board held six scheduled Board meetings during the year and holds additional meetings, as required. In addition, a meeting is held each year at which strategic issues are considered in depth, with members of the SMT invited to attend. All Directors are expected to attend all Board and relevant Committee meetings in addition to general meetings of the Company, including the Annual General Meeting ("AGM"). Details of Board and Committee attendance for the year are set out on page 59.

The Board has a number of Committees that support the effective discharge of its duties. The various committee reports can be found on pages 68 to 101 of this report.

A.2 Division of responsibilities

The division of responsibilities between the Chairman and CEO, and the role of the Senior Independent Director ("SID"), are clearly defined and are available on the Company's website at: investors.sophos.com.

The Board supports the separation of these roles and the partnership between Peter Gyenes and Kris Hagerman is constructive and based on mutual trust.

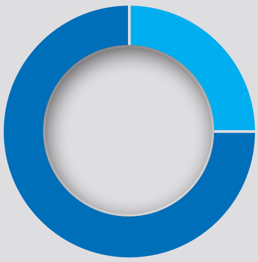
Board matters

A formal schedule of matters reserved for the Board is published on the Company's website. Each year, the Board also undertakes a review of its schedule of matters reserved. This review took place in May 2019, with only minor updates.

The Board

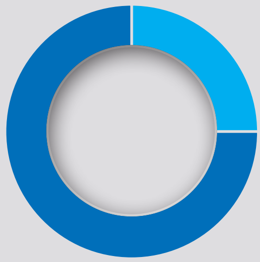
- Overall management of the Group, its strategy and long-term objectives
  - Approval of the Group's annual and half-year results, dividend policy and shareholder distributions
  - Corporate governance arrangements and Board evaluation
- Determining the Remuneration Policy for the Directors and the SMT
  - Succession to the Board and SMT
  - Approval of all material corporate transactions
- Ensuring that necessary resources and the appropriate risk management controls, processes and culture are in place to deliver its strategy and long-term objectives
  - Approval of all material policies including Diversity, Anti-Bribery and Corruption, Modern Slavery, Share Dealing and Whistle Blowing

Board independence



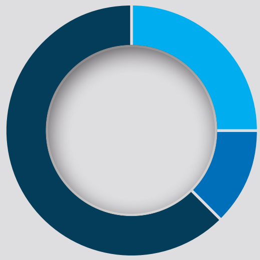
Non-Executive	75%
Executive	25%

Gender breakdown



Male	75%
Female	25%

Length of service



0-3 years	25%
3-6 years	12.5%
6+ years	62.5%

The separation of authority enhances independent oversight of the executive management by the Board and helps to ensure that no one individual has unfettered authority.

A.3 The Chairman

The Chairman leads the Board and is responsible for its effective operation, for overseeing strategy and for ensuring each Director contributes to effective decision-making.

The Company Secretary, with the Chairman, sets the Board's agenda for the year and ensures sufficient time is available for the discussion of all items.

A.4 Non-Executive Directors

Paul Walker was SID for the duration of the year. The responsibilities of the SID include meeting with shareholders as an alternative contact to the Chairman, CEO or CFO and working closely with the Chairman, acting as a sounding board and providing support. The SID is expected to commit six days per year to the role and will commit significantly more in exceptional years. This is in addition to the expected time commitment of a Non-Executive Director ("NED").

The NEDs are encouraged to challenge constructively and to help develop proposals on strategy, scrutinise the performance of management in meeting agreed goals and objectives, and monitor reporting. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. The Chairman meets with the NEDs without the Executive Directors ("EDs") present after each physical Board meeting, and individually with each NED at least once a year.

During the year, the Directors had no unresolved concerns about the operations of the Company, its governance or any proposed action. It is Company policy that any such unresolved concern must be recorded in the Board minutes.

B: Effectiveness

B.1 Board composition

At the date of publication, there are six NEDs, including the Non-Executive Chairman, on the Board and two EDs. The Board composition is compliant with B.1.2 of the Code, as at least half of the Board, excluding the Chairman comprises independent NEDs.

Independence

During the year, the Board kept under review the overall balance of skills, experience, independence and knowledge of Board and Committee members and their diversity, including gender, and weighed carefully its overall size and ability to meet the requirements of the business. It is the Board's view that its current members have a wide range of skills and experience. The Board believes that crucial to its ability to lead the Company successfully it requires a membership that combines detailed knowledge of the Group's operations and history, the technology industry in which the Group operates, leadership of a global business, and being listed on the London Stock Exchange.

The Board is confident that the balance of independence weighed against the strong judgement and considerable knowledge that each NED brings, is right and appropriate for Sophos.

Further details are outlined on pages 68 and 69 of the Nomination Committee report.

CORPORATE GOVERNANCE STATEMENT CONTINUED

In accordance with the Code, the Board undertakes an annual review of the independence of its NEDs taking into account each individual's professional characteristics, behaviour and their contribution to unbiased and independent debate. The Board considers that the NEDs, led by the SID, Paul Walker, have the skills, experience, and knowledge of the Group, and the markets in which we operate, to enable them to discharge their respective duties and responsibilities effectively. Each NED is prepared to question and to challenge management.

The Board considers four of its NEDs to be independent for the purposes of the Code; Roy Mackenzie is not considered independent.

The Board recognised that Sandra Bergeron's overall length of service was more than eight years after the 2018 AGM which may lead some investors to question her independence. The Board has re-considered this issue and agrees that Sandra continues to maintain and contribute an independent view in all Board deliberations and brings invaluable security, operations and board advisory expertise spanning more than 20 years.

Comments have been made regarding Paul Walker's past participation in a restricted share arrangement, as noted in the Annual Report on Remuneration, which may have led some investors to question his independence. The Board are agreed that since his appointment as SID, Paul, whose technology and senior leadership experience spans more than 30 years, has been independent in character and judgement and he remains an active and committed Board member and Chairman of the Remuneration Committee.

The Board consider that Peter Gyenes was independent upon appointment and continues to maintain and contribute an independent view. Peter brings valued leadership to the Board and unwavering commitment to supporting the Company to achieve its long term strategic objectives.

Conflicts of interest

The Company has established procedures whereby actual and potential conflicts of interest arising from current and proposed roles to be undertaken by Directors of the Board with other organisations are regularly reviewed in respect of both the nature of those roles, their time commitment, and for proper authorisation to be sought prior to the appointment of any new Director. The Board consider these procedures to be working effectively. Directors are required to notify the Company when they become aware of any actual or potential conflict of interest.

The Board deals with each notified conflict of interest, or potential conflict of interest, on its individual merit and takes into consideration all the circumstances. The following conflicts of interest have been authorised by the Board for the relevant period.

- Roy Mackenzie is a partner at Apax Partners, LP. Apax Partners, LP is a wholly owned subsidiary of Apax Partners, LLP. Both Apax Partners, LP and Apax Partners, LLP are advisors of the Apax Funds, which wholly own Pentagon Lock Sarl, Pentagon Lock 6-A Sarl, Pentagon Lock 7-A Sarl and Pentagon Lock US Sarl, and shares a common owner with Apax Global Alpha Limited (collectively "Apax"). It is noted, that:
  - following the admission of the Company's shares to the London Stock Exchange in 2015, Apax controlled 35.2 per cent of the voting rights in the Company and at 31 March 2019, controlled 10.77 per cent of the voting rights in the Company; and,
  - Apax is a shareholder of Global Logic, with whom the Company maintains an ongoing supplier relationship.
- Sandra Bergeron sits on the boards of F5 Networks and Qualys, Inc., suppliers of application delivery networking and cloud security and compliance management solutions, respectively.
- Vin Murria is a Non-Executive Director of Softcat plc, with whom the Company maintains an ongoing customer relationship.

B.2 Appointments to the Board

There were no appointments to the Board during the year. The succession and appointment process is led by the Nomination Committee with strong oversight from the Board. Further details concerning the succession and appointment process, and the Company's policy on diversity are set out in the Nomination Committee report on page 70.

All NEDs serve on the basis of letters of appointment which are available for inspection upon request, as well as being available to view at the Company's Registered Office and at the AGM. The letters of appointment set out the expected time commitment of NEDs who, on appointment, undertake that they will have sufficient time to meet what is expected of them. NEDs are appointed for an initial three-year term and the continuation of their appointment is conditional on satisfactory performance and subject to annual re-election at the Company's annual general meetings. EDs serve on the basis of service agreements which are also available for inspection upon request.

Further details on the EDs' service agreements are included in the Directors' Remuneration Policy, on page 88.

Board skills and experience

NAME	ANALOGOUS SECTOR/CONTENT	PLC/NED	US	SITTING EXECUTIVE	FINANCE/CAPITAL MARKETS	OPERATIONAL EXPERIENCE	CUSTOMER/ MARKETING
Peter Gyenes	■	■	■		■	■	■
Kris Hagerman	■	■	■	■	■	■	■
Nick Bray	■	■		■	■	■	
Sandra Bergeron	■	■	■		■	■	■
Roy Mackenzie	■	■	■		■		■
Rick Medlock	■	■		■	■	■	
Vin Murria	■	■		■	■	■	■
Paul Walker	■	■			■	■	■

B.3 Commitment

During the year, the Board considered the external commitments of its Chairman, SID and other NEDs and is satisfied that these do not conflict with their duties and time commitments as Directors of the Company. EDs may accept external appointments with the prior approval of the Chairman, provided that such appointments do not prejudice the executive's ability to fulfil their duties for the Group.

B.4 Development

The Chairman, with the support of the Company Secretary, is responsible for the induction of new Directors, and the ongoing development of all Directors. An induction programme is provided to all Directors on joining the Board, designed to provide an understanding of the Group's business, governance and key stakeholders. The induction process continues to evolve and currently includes the provision of an induction pack and past Board materials, meetings with key individuals and the Company's advisors, and briefings on the Company's products, as well as key business, legal and regulatory issues facing the Group.

As the business environment changes, it is important to ensure the Directors' skills and knowledge are refreshed and updated regularly. Accordingly, the Company Secretary ensures that updates on topical corporate governance, regulatory and technical matters are published to Directors at Board meetings and by means of communications between meetings.

B.5 Information and support

The Board's approach to training and development opportunities continues to develop and the Company Secretary (in consultation with the Chairman) works closely with Directors to ascertain their training and development needs. Through this process, the Board's approach continues to be tailored to address the identified areas for focus. Each year the Directors are invited to attend the annual Partner Conferences to support their familiarity with the Group's products and operations.

The Directors have full access to the Company Secretary, who advises the Board and the Board Committees on relevant matters, including compliance with the Company's policies and Board procedures, relevant legislation and regulation, including the Listing Rules and the Code and other governance standards. The Company Secretary provides guidance and advice to the Board and individual Directors regarding their duties, responsibilities and powers and ensures the proper administration of the proceedings and matters relating to the Board. The CEO and the Company Secretary work together to ensure that Board papers are clear, accurate, delivered in a timely and secure manner to Directors, and are of sufficient quality to enable the Board to discharge its duties effectively. Directors may obtain independent professional advice at the Company's expense in the furtherance of their duties, where considered necessary or advisable.

All Directors have access to an online portal to which Board materials are published, including information about the Company and helpful guidance documents for their reference as Directors of a UK listed company.

CORPORATE GOVERNANCE STATEMENT CONTINUED

B.6 Evaluation

Full details of the evaluation process, together with recommendations for FY20, can be found on pages 60 and 61.

B.7 Election and re-election

In accordance with the Company's Articles of Association ("Articles") and the Code, each Director is subject to election at the first AGM following their appointment, and re-election at each subsequent AGM. The Directors unanimously recommend the re-election of all other members of the Board. Full biographical details for all Directors can be found on pages 54 and 55 and also summarised in the Notice of AGM.

C: Accountability

C.1 Financial and business reporting

A Statement of the Directors' Responsibilities regarding the Financial Statements, including the status of the Group as a going concern, is set out on pages 106 and 107, with an explanation of the Group's strategy and business model, together with relevant risks and performance metrics, which are set out in the strategic report on pages 16 to 40.

A further statement is set out on page 107, confirming that the Board considers that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position, performance, business model and strategy.

C.2 Risk management and internal controls

The Board has carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity. Further details concerning how they are being managed or mitigated can be found on pages 36 to 39.

The Audit and Risk Committee report explains the process carried out for the ongoing assessment of the effectiveness of the Company's risk management and internal control systems on pages 71 to 76.

The Board's assessment of the prospects of the Company, its expectation that the Company will be able to continue in operation and meet its liabilities as they fall due, and the viability statement, is set out on page 106.

C.3 Audit Committee and Auditor

The Audit and Risk Committee Report on pages 71 to 76 sets out the details of the composition of the Committee, including the expertise of its members, and outlines how the Committee has discharged its responsibilities in FY19.

The Board has delegated a number of responsibilities to the Audit and Risk Committee, including: oversight of the Group's financial reporting processes; management of the external auditor; and, management of the internal risk management processes. KPMG LLP have expressed their willingness to continue as the Company's auditor. Resolutions proposing their reappointment and to authorise the Committee to determine their remuneration will be proposed at the 2019 AGM.

D: Remuneration

D.1 Level and components of remuneration

The Annual Report on Remuneration on pages 91 to 101 outlines the activities of the Committee during FY19. The Directors' Remuneration Policy, including relevant remuneration components and how they support the achievement of the strategic long-term objectives of the Company are set out on pages 82 to 90. The Annual Report on Remuneration sets out the implementation of remuneration during FY19, including salary, bonus and share awards, and any payments for loss of office paid to Directors.

This year a new Remuneration Policy will be submitted for consideration by shareholders at the 2019 AGM. Details of the new Remuneration Policy and the process followed in consulting with major shareholders is outlined in the Annual Statement of the Remuneration Committee Chairman on page 78 and Directors' Remuneration Policy on pages 82 to 90.

D.2 Procedure

The Board has delegated a number of responsibilities to the Remuneration Committee, including the setting of the Group's overall Remuneration Policy and strategy, as well as the remuneration arrangements for the EDs and SMT and their direct reports. During FY19, no individual was present when their own remuneration was being discussed.

E: Relations with Shareholders

E.1 Dialogue with Shareholders

The Board recognises that meaningful engagement with its shareholders is integral to the continued success of the Group. Throughout FY19, members of the Board have sought to actively engage with shareholders on a number of occasions, through meetings, presentations and roadshows.

NEDs are kept informed of the views of the shareholders through periodic reports from the CEO and the CFO, including inputs from the corporate brokers with whom they are in regular contact.

As required by reporting Regulations the Directors have been consulting with major shareholders with regards to the renewal of the Group's Remuneration Policy. Details of this process as well as the details of the new Remuneration Policy can be found in the Annual Statement of the Remuneration Committee Chairman on page 78 and Directors' Remuneration Policy on pages 82 to 90.

There are also additional requirements in the new Code, which apply to accounting periods beginning on or after 1 January 2019, and these are as follows:

- When 20 per cent or more of votes cast against a board recommended resolution at an AGM, a company should provide background and any resulting actions when announcing results – at the 2018 AGM Sophos had a 20 per cent vote against the remuneration policy and Sophos noted this in the subsequent results announcement, along with an explanation on how the Board intended to remedy this for the coming year.
- Stakeholder and workforce engagement – additional information on the methods the Company use to engage with its workforce will be reported in 2020.

Annual General Meeting

The AGM will be held on 25 September 2019 at the Company's registered office. All shareholders have the opportunity to attend and vote, in person or by proxy. The Notice of AGM is sent to all shareholders who have requested to receive hard copy documentation and can also be found on our website at: investors.sophos.com.

The Notice of AGM sets out the business of the meeting and explanatory notes on all proposed resolutions. Separate resolutions are proposed in respect of each substantive issue. The AGM is one of a number of key forums through which the Company communicates with shareholders.

By order of the Board

Eleanor Lacey

Company Secretary

15 May 2019

NOMINATION COMMITTEE REPORT

CHAIRMAN

Peter Gyenes

MEETINGS HELD

3

COMMITTEE MEMBERS

Sandra Bergeron
Roy Mackenzie
Rick Medlock
Vin Murria
Paul Walker

All appointments as at 31 March 2019

Attendance of members at the meetings of the Committee are noted on page 59

Dear Shareholder,

The Committee met three times during the year and ensures that Board and Committee composition is appropriate for a company of Sophos' scale and ambition. The key aspects of the Committee's role, together with the main areas of consideration and the activities undertaken during the year are set out in this report.

Committee composition and meeting attendance

The composition of the Committee complies with the UK Corporate Governance Code ("the Code"), which provides that a majority of its members should be independent Non-Executive Directors ("NED").

The Committee is chaired by the Chairman of the Board. The Company Secretary is secretary to the Committee and attends all meetings. Other attendees at Committee meetings may differ from time to time and, upon invitation from the Committee, include the Chief Executive Officer ("CEO"), Chief Legal Officer ("CLO"), and other members of the Senior Management Team ("SMT").

The Chairman of the Committee provides updates to the Board on the proceedings of each meeting. The Board also receives copies of the minutes of each meeting.

Role and responsibilities

The Committee is responsible for regularly evaluating the balance of skills, knowledge, experience and diversity of the Board and its Committees, as well as the size, structure and composition of each. It is also responsible for periodically reviewing the Board, Committees and senior management structure, succession plans, and identifying, with management, the priorities for succession planning in respect of each position. On an annual basis, the Committee considers the re-election of Directors prior to their recommended approval by shareholders. The full terms of reference of the Committee can be found on the Company's website at www.sophos.com.

Board composition and independence

Excluding the Chairman, the Board is comprised of 57 per cent independent NEDs (FY18: 50 per cent).

The Board believes that crucial to its ability to lead the Company successfully it requires experience relevant to operations of the scale and ambitions of Sophos. In addition, it requires detailed knowledge of the technology industry in which the Group operates, and the corporate governance and regulatory environment associated with publicly listed companies, particularly in the UK.

The consideration of independence is an ongoing process and in the spirit of the current Code, and cognisant of the provisions of the new Code relating to directors' independence, the Committee is committed to ensuring the Board and its Committees remain appropriately constituted. The Committee will continue to take this into consideration when selecting new candidates, as well as technical and personal capabilities that would bring value to the Board and its Committees.

Board appointments

The Committee leads the Board appointment process and makes recommendations to the Board, as appropriate. There were no appointments during the year.

The Company's current process in relation to Board appointments is set out below:

Non-Executive Director

- The Committee Chairman and search consultants submit a short-list of candidates to the Committee and CEO for review and inclusion of additional candidates.
- The Committee Chairman, Senior Independent Director ("SID"), CEO and Chief Financial Officer ("CFO") each meet selected candidates. Successful candidates go on to meet each Board member.
- After all Board members have met the candidates, the Committee makes its recommendation to the Board.

Executive Director

- The Committee Chairman and the CEO or, if engaged, search consultants, submit a short-list of candidates to the Committee.
- The Committee Chairman, SID, CEO and CFO each meet the selected candidates. Successful candidates go on to meet some or all of the Committee members.
- The Committee's assessment is reviewed with the Chairman of the Board and the CEO, and the Committee makes its recommendation to the Board.

Succession

During the year, the Committee conducted a review of succession to SMT roles and those individuals who had been identified internally who would be suited to take on each role, as appropriate. Internal successors were categorised by their relative readiness to assume any such role, and where it was not possible to identify a suitable internal successor, an external successor would be identified, as and when appropriate. Management would look at the implementation of development plans to address any internal successor's relative readiness to assume any such role. The Committee has kept a watching brief on succession to Board roles during the year and would continue to do so during FY20.

Main activities

The Committee has an annual forward agenda developed from its terms of reference with standing items that the Committee considers at each meeting.

FY19 focus areas

- Review the composition of the Board and its Committees
- Consider the implications for Board composition of the results of the FY19 Board evaluation
- Consider succession plans for Board, Committee and SMT appointments
- Identify a number of technical and personal capabilities which the Board would value in any new NED
- Review the Company's Diversity Policy and consider the Company's objectives to deliver against its commitments
- Monitor external commitments of the Board, as they relate to their time commitments to the Company and potential conflicts of interest
- Review and recommend the election and re-election of Directors at the Company's 2019 AGM
- Monitor actions pursuant to recommendations through Board and Committee self-assessment

NOMINATION COMMITTEE REPORT CONTINUED

Diversity

At 31 March 2019, the proportion of women on the Board was 25 per cent (FY18: 22 per cent). Sophos will make its fourth data submission to the Hampton-Alexander Review in July 2019. The Company's Diversity Policy is published on its website at: investors.sophos.com and will be reviewed in 2019 to determine whether any adjustments are required. It has been noted that some FTSE listed companies have developed their diversity policies beyond gender alone and now address diversity in a broader context, which is more in keeping with the Company's own philosophy.

The Company recognises the benefits of diversity in its broadest sense, including gender and ethnicity, and will continue to ensure that all forms of diversity are actively considered when contemplating future appointments to the Board, and recruitment and promotion to the SMT, and their direct reports. As set out in the Company's Diversity Policy, the Board is mindful of the recommendations of the Hampton-Alexander Review and also the reviews conducted by Parker on ethnic diversity of UK boards and by McGregor Smith on race in the workplace.

Details of a number of diversity initiatives put in place across the Group are set out in the Corporate Responsibility report on page 46, together with details of diversity within our workforce, including at Board and senior management level.

Board diversity objectives

The Board's objectives for achieving diversity on the Board are set out below:

- All Board appointments will be made on merit, in the context of the skills, knowledge and experience that are needed for the Board to be effective.
- Ensure lists of potential NEDs include diverse candidates of appropriate merit.
- Encourage the emergence of female candidates and candidates of diverse backgrounds among the senior management talent pool.
- Only engage executive search firms who have signed up to the voluntary Code of Conduct on gender diversity and best practice.

In addition to taking into account gender, ethnicity and other forms of diversity, the Committee seeks to achieve the optimal balance of skills, experience, independence and knowledge of Sophos and the industry as a whole amongst the Board and SMT, and their direct reports in order to support the Company's long-term strategic objectives.

The Committee will continue to keep these measurable objectives under review and will make recommendations to the Board for their revision, as appropriate. The Committee is pleased with the Group's performance against these objectives to date but acknowledges that this is a process which continues.

Performance evaluation

The Committee's performance was assessed as part of the Board's annual effectiveness review. It was concluded that the Committee operated effectively in FY19. In response to findings of the review, Committee members will continue to focus on succession planning, particularly in light of the new Code and Sandra Bergeron and Roy Mackenzie are coming to the end of their third three-year term in 2019.

Through a combination of internal and external education, involving periodic interaction with third party advisors, NEDs have access to a significant culture of training and development.

The Committee also undertakes a review of its terms of reference and composition each year. This review took place in May 2019, with only minor updates.

Peter Gyenes

Chairman of the Nominations Committee

15 May 2019

AUDIT AND RISK COMMITTEE REPORT

CHAIRMAN

Rick Medlock

MEETINGS HELD

5

COMMITTEE MEMBERS

Sandra Bergeron
Vin Murria
Paul Walker

All appointments as at 31 March 2019

Attendance of members at the meetings of the Committee are noted on page 59

Dear Shareholder,

The Committee met five times during the year. Set out in this report are details of the key aspects of the Committee's role, together with the main activities it has undertaken and the significant issues it has considered during the year.

The composition of the Committee is compliant with the Principles of the UK Corporate Governance Code (Code), which provides that all members should be independent Non-Executive Directors ("NED"). In line with the requirements of the Code and the FRC's Guidance on Audit Committees, Rick Medlock, the Committee Chairman, has recent and relevant financial experience through his previous employment in senior financial positions at large and UK listed companies, and is a qualified Chartered Accountant.

The Board is also satisfied that all members of the Committee have extensive experience of the technology industry in which we operate, sufficient to enable the Committee to exercise its duties effectively. Full biographical details are set out on pages 54 and 55.

The Company Secretary is secretary to the Committee and attends all meetings. Other attendees at Committee meetings may differ from time to time and, upon invitation from the Committee, include the Chairman, the Chief Executive Officer ("CEO"), the Chief Financial Officer ("CFO"), Chief Legal Officer ("CLO"), Vice President of Finance, Vice President Internal Audit and Risk and other members of the Senior Management Team ("SMT"). Representatives from the external auditor (KPMG LLP) attend all Committee meetings, with the internal auditor (Ernst & Young LLP) attending as required.

The Chairman of the Committee provides updates to the Board on the key matters covered at each meeting. The Board also receives copies of the minutes of each meeting.

Role and responsibilities

The Committee has a fundamental role to play in reviewing, monitoring and challenging the integrity and effectiveness of the Company's financial reporting and internal control processes. The Committee also oversees the relationship between the Group and its external auditor and makes recommendations to the Board on their appointment. In addition, the Committee monitors and reviews the external auditor's independence, objectivity and the effectiveness of the audit process, taking into account relevant legal, professional and regulatory requirements. The full terms of reference of the Committee can be found on the Company's website at: investors.sophos.com.

AUDIT AND RISK COMMITTEE REPORT CONTINUED

Main activities

The Committee has an annual forward agenda, developed from its terms of reference, with standing items that the Committee considers at each meeting, in addition to any specific matters arising, and topical business or financial items on which the Committee has chosen to focus. The Chairman and the Company Secretary have worked together to review and, where appropriate, refresh the annual forward agenda to bring in to greater focus areas of importance for the Committee, and the Company.

FY19 focus areas

Accounting, tax and financial reporting

The Committee has:

- reviewed and approved the quarterly trading updates, half-year and annual Financial Statements, significant financial reporting judgements and disclosures, and investor presentations;
- reviewed and approved the going concern and viability assessments, and the annual external statement thereon;
- reviewed updates on accounting matters, including consideration of relevant accounting standards and underlying assumptions, and the impact of changing accounting standards; and,
- reviewed and approved the interim and full-year dividend proposals and declared them to be in line with the Company's dividend policy.

Risk management and internal controls

The Committee has:

- reviewed and approved the internal audit plan for the year as well as longer-term objectives and reports and updates of the work performed by the in-house internal audit team and Ernst & Young LLP ("EY"), as the outsourced internal audit providers appointed by the Committee in 2015;
- reviewed and approved the risk assessment process and, in particular the identification and assessment of the Company's principal risks and the attendant disclosures;
- received and noted regular updates from the Risk and Compliance Committee ("RCC"), a management Committee that has a direct reporting line to the Committee, to provide an additional level of assurance to the Committee; and,
- received and noted regular updates from the CLO concerning pending or ongoing litigation, and statutory or regulatory risks, including General Data Protection Regulation and consideration of any new regulations relevant to the Group.

External Auditor

The Committee has:

- supported the lead audit partner in carrying out his duties at the Company;
- met with the external auditor, KPMG, to review the annual audit plan and receive their findings and reports on the annual audit and interim review; and,
- reviewed and approved the external auditor evaluation paper prepared by management covering the external auditor's independence and objectivity, and evaluation of the effectiveness of the audit process, together with the attendant recommendation for reappointment.

Performance evaluation

The Audit and Risk Committee's performance was assessed as part of the Board's annual effectiveness review. It was concluded that the Committee operated effectively in FY19, noted that its time was used effectively, and information provided was of a good quality. The Committee members will continue to work closely with management to consider the Group's risk profile and review and challenge the Company's systems for risk management and internal control as the Company grows and evolves.

The Committee also undertakes a review of its terms of reference and composition each year. This review took place in May 2019, with only minor updates.

Significant issues

The issues considered by the Committee that are deemed to be significant to the Group are set out below:

Revenue recognition

The Group generates revenue from sales of products through subscriptions, hardware and the rendering of enhanced support or professional services. There is a risk that revenue is inappropriately recognised if revenue is incorrectly apportioned to a product or service or if the recognition criteria of the product is not correct.

The Group has a revenue recognition policy in place that details the application of relevant standards to the products and services sold by the Group. The policy includes rules for applying fair value to components of multiple element arrangements and timing of recognition dependent upon the individual nature of the goods or services sold. At half-year and year-end, management provide to the Committee an accounting paper on revenue recognition, any changes arising from updated standards and a commentary on the revenue recognised. In the current year, additional consideration has been given to the first time application of IFRS 15 for the Group.

The Group's external auditor have reported to the Committee that they have reviewed the revenue recognition policy and processes, as well as performing detailed testing of revenue recognition across the year and found revenue to be appropriately accounted for.

Having provided appropriate challenge to management and the external auditor, the Committee has concluded that revenue recognition for the Group is appropriate.

Reporting requirements and presentation

The Group makes use of certain non-GAAP measures and discloses certain items separately within the consolidated statement of profit or loss as exceptional items which, in the opinion of the Directors, enables an enhanced understanding of the performance of the Group. The use of these measures and disclosures is judgemental in nature.

The use of non-GAAP measures and the classification of certain income statement items as exceptional by the Group have been reviewed by the Committee during the year with reference to authoritative guidance and regulations as well as through discussions with management and external advisors. The Committee is satisfied that the use of such measures is appropriate and enhances the understanding of the Group's financial performance and its prospects.

The Committee has also reviewed the disclosures made in this Annual Report and has discussed them with the external auditor, so as to ensure that it is comfortable with the content and presentation made in the Annual Report.

Internal controls and risk management

During the year, the Committee has received and reviewed reports regarding risk management and the principal risks identified across the Group. The Committee was satisfied with the risk management process and with the relevance of the risks identified. It was also satisfied with the level of assurance provided by the Group's Internal Audit and Risk Management function, which is supported by EY. The Committee has concluded that sound risk management and internal control systems have been maintained throughout the year.

Whilst the Board is ultimately responsible for the Group's systems of risk management and internal control, each of the individual functional leaders are recognised as key drivers of the process through which risks and uncertainties are identified. The Board recognises that rigorous internal control systems are critical to managing risks and fundamental to the achievement of its strategic objectives. The Board further acknowledges that these systems are designed to manage rather than eliminate risk in the Group.

The formal process for identifying, evaluating and managing significant risks faced by the Group performed within the Internal Audit and Risk Management function is reviewed by the RCC. The risk framework has been designed to capture operational and strategic risks and evaluate control mitigations. This provides additional assurance to the Committee who have ultimate responsibility for the oversight and review of the adequacy and effectiveness of the Group's systems of internal controls. The external auditor provide a supplementary, independent and autonomous perspective on those areas of the internal control system which they assess in the course of their work. Their findings are regularly reported to both the Committee and the Board.

AUDIT AND RISK COMMITTEE REPORT CONTINUED

Key elements of the internal controls environment are:

- annual budgets and strategic plans performed for all business units and the Group as a whole;
- monitoring of performance against budget and subsequent forecast with reporting to the Board on a regular basis;
- monthly review of detailed key performance indicators;
- all contracts are reviewed at a level of detail appropriate to the size and complexity of the contract;
- timely reconciliations are performed for all significant balance sheet accounts;
- clearly defined organisational structure and authorisation lines;
- the RCC that oversees the risk management process; and
- the Committee, which approves audit plans and assesses the overall appropriateness of the Group's internal control environment.

The preparation and issue of financial reports is managed by the Group's finance department, as delegated by the Board. The Group's financial reporting process is controlled using the Group accounting policies and reporting systems. The Group finance department supports all reporting entities with guidance on the preparation of financial information.

Each legal entity has a Finance Director or Controller who has responsibility and accountability for providing information which is in accordance with agreed policies. The financial information for each entity is subject to a review at reporting entity and Group level by the CFO alongside the Vice President of Finance. The Annual Report is reviewed by the Committee in advance of presentation to the Board for approval. Additionally, the Finance Director or Controller of the reporting entity completes a self-certified quarterly questionnaire which is used to identify control strengths and weaknesses across all financial areas with any weaknesses being subsequently addressed.

The Group also maintains a consolidated Risk Register which sets out the nature and extent of the significant risks facing the Group. Each of the risks are prioritised according to likelihood of occurrence and potential impact to the Group and the register ensures that all risks are identified, measured, mitigated, and managed by the appropriate owner in line with the risk appetite of the Group.

The Directors, through the use of appropriate procedures, systems and the employment of competent personnel, have ensured that measures are in place to maintain compliance with the Company's obligation to keep adequate accounting records. The accounting records are kept at the registered office of each legal entity.

How we manage risk

The Sophos Board is ultimately responsible for ensuring effective identification, assessment and management of risk across the Group. Central to the risk management process is the Group's culture of openness, transparency and accountability.

The Internal Audit and Risk Management function manage and drive the risk management framework and operate on an independent basis providing further assurance to the Committee and the Board. The risk management framework enables a robust assessment process to identify risks in line with the overall achievement of the business strategy. This function also ensures that all relevant and significant risks identified across the business are mapped to the Internal Audit plan for the year. In addition, the Group's annual planning and quarterly forecasting cycles include discussions around business risks identified to ensure appropriate investment by the Group.

On a quarterly basis, the RCC reviews the status of risk exposures and risk management throughout the business as managed by the Internal Audit and Risk Management function. The RCC is a Committee of senior leaders authorised by the Board to provide an additional level of assurance to the Committee in overseeing risk management and internal control activities. On behalf of the Board, the Committee reviews and challenges the effectiveness of the risk management process.

The Group takes a two-pronged approach to identifying risks:

1) A top-down approach at the senior leadership team level; these are the principal risks which could have a serious impact on the strategic business plan of the Group and may encompass several of the risks identified in the bottom-up approach.

2) A bottom-up approach at the business function level; these risks are managed at the operational level with an appropriately defined escalation process in place for those risks rated as high.

A series of risk identification approaches are used, such as risk identification and horizon scanning workshops, interviews, and inclusion of risk discussions in team meetings. Risk registers are fully owned at the business function level and registers are maintained and reviewed on a quarterly basis.

All identified risks are assessed against a pre-defined scoring matrix and prioritised accordingly. Any risks identified in the bottom-up approach deemed to be rated as higher risk are escalated in line with pre-defined escalation procedures for further evaluation.

Following the identification of risks, a risk management plan is developed and implemented; this is managed by the assigned risk owner with regular feedback to the RCC.

Regular reporting of risk management ensures each risk is re-evaluated on a timely basis to ensure that all relevant risks are identified and managed appropriately and that the Board is focused on the principal risks identified.

Whistleblowing

A whistleblowing policy is in place in the Group enabling employees to confidentially report matters of concern. The Committee receives details of any matters raised.

Internal Audit

EY continue to support the Sophos Internal Audit and Risk Management function. The Group's CFO provides oversight and co-ordination of Internal Audit with support from the RCC. In order to ensure independence, the Internal Audit function has a direct reporting line to the Committee and its Chairman.

The nature and scope of the Internal Audit plan, using a risk-based approach, was approved by the Committee, with any subsequent changes to the plan requiring further approval.

The results of the audits were assessed alongside responses from management. Any outcomes graded as requiring improvement were considered in detail by the Committee along with the appropriateness of mitigation plans to resolve the issues identified.

At each meeting, the Committee received audit reports and updates from the Internal Auditor, in order to ascertain progress in completing the internal audit plan and to review results of the audits. The Internal Audit plan continues to be developed through a review of formal risk assessments, together with consideration of the Group's key business processes and functions that could be subject to audit. The Committee monitored and reviewed the scope and results of the internal auditor's activities as well as the effectiveness of Internal Audit during the financial year.

Review of effectiveness

The Board, through the Committee, has reviewed and considered the effectiveness of the risk management and system of internal controls in operation across the Group.

Any system of control can only ever provide reasonable and not absolute assurance that control weaknesses or irregularities do not exist, or that there is no risk of material errors, losses, fraud, or breaches of laws or regulations.

Accordingly, the Group is continually seeking to improve the effectiveness of its systems of internal control.

The main objectives of the Group's internal control systems are:

- to ensure its aims and objectives are met;
- to ensure adherence to management policies;
- to ensure compliance with statutory requirements;
- to safeguard assets; and
- to ensure the relevance, reliability and integrity of information, so ensuring as far as possible the completeness and accuracy of records.

AUDIT AND RISK COMMITTEE REPORT CONTINUED

The Committee has concluded that the Group's risk management and system of internal controls is deemed effective. This is informed by a number of sources:

- The audit work undertaken by the Internal Audit function.
- Risk management procedures managed and reviewed by the RCC.
- Reports issued by the Group's external auditor.

A detailed review of the Group's management of each principle risk or uncertainty is explained on pages 36 to 39.

External Auditor

The Committee reviews and makes recommendations with regard to the appointment and reappointment of the external auditor. In making these recommendations, consideration is given to auditor effectiveness and independence, partner rotation and any other factors that may impact the reappointment of the external auditor.

There are no contractual restrictions on the choice of external auditor and the Committee considers on an annual basis the need for a formal tender process in accordance with the provisions of the Code.

The Group's auditor, KPMG LLP, were appointed for the year-ended 31 March 2001 with the audit engagement partner rotation last occurring for the year-end 31 March 2018. In view of this, it is now the intention of the Directors to tender the audit contract, currently held by KPMG, during the year-ending 31 March 2020.

The external auditor may perform certain non-audit services for the Group, though above a certain level of materiality, any such non-audit services require pre-approval by the Audit and Risk Committee and are only permitted to the extent allowed by relevant laws and regulations.

Non-audit fees for the year-ended 31 March 2019 were $0.1m (FY18: $0.1m). Full details of auditor remuneration is shown in note 10 to the Financial Statements.

Review of effectiveness of External Auditor

An important role of the Committee is to assess the effectiveness of the external audit process. In performing this assessment, the Committee:

- reviewed the annual audit plan and considered the auditor's performance against that plan along with any variations to it;
- met with the audit engagement partner to review the audit findings and responses received to questions raised by the Committee;
- held regular meetings with the audit engagement partner, including in the absence of executive management;
- considered their length of tenure;
- reviewed the nature and magnitude of non-audit services provided; and,
- reviewed the external auditor's own independence confirmation presented to the Committee.

Based on the assessment performed, the Committee has recommended to the Board that a resolution to reappoint KPMG LLP be proposed at the 2019 AGM.

Rick Medlock

Chairman of the Audit and Risk Committee

15 May 2019

DISCLOSURE COMMITTEE REPORT

CHAIRMAN

Kris Hagerman

MEETINGS HELD

5

COMMITTEE MEMBERS

Nick Bray
Eleanor Lacey

All appointments as at 31 March 2019

Attendance of members at the meetings of the Committee are noted on page 59

The Committee comprises the Chief Executive Officer ("CEO"), Chief Financial Officer ("CFO") and Chief Legal Officer ("CLO"), and is chaired by Kris Hagerman, the CEO. A quorum of two members, including at least one Executive Director is required for the transaction of business.

The Company Secretary is secretary to the Committee.

The Board also receives copies of the minutes of each meeting.

Role and responsibilities

The Committee is responsible for the implementation and monitoring of systems and controls in respect of the identification, management and disclosure of inside information and for ensuring that regulatory announcements, shareholder circulars, prospectuses and other documents issued by the Company comply with applicable legal or regulatory requirements. The primary responsibilities of the Committee include:

- Review of the preliminary results announcement, the half-year results and any other trading statements, and investor presentations.
- Review of information provided to the Committee, consideration of its potential categorisation as inside information and determination of the date and time at which that inside information first existed within the Company.
- Determination of whether any identified inside information gives rise to an immediate disclosure obligation, or whether it is permissible to delay disclosure.
- Review and approval of announcements in respect of disclosable projects.

At each Board and Senior Management Team meeting, transactions or events are considered against the disclosure obligations of the Company and whether any matter is considered to be price sensitive.

The Committee also undertakes a review of its terms of reference and composition each year. This review took place in May 2019, with only minor updates.

Main activities

Key issues reviewed by the Disclosure Committee during the year, included:

FY19 focus areas

- The preliminary results announcement
- The trading update for the three-months ended 30 June 2018
- The proposed final dividend
- The announcement in respect of the interim results for the six-months ended 30 September 2018
- The interim dividend
- The trading update for the three-months ended 31 December 2018

ANNUAL STATEMENT OF THE REMUNERATION COMMITTEE CHAIRMAN

CHAIRMAN

Paul Walker

MEETINGS HELD

3

COMMITTEE MEMBERS

Sandra Bergeron
Peter Gyenes
Rick Medlock
Vin Murria

All appointments as at 31 March 2019

Attendance of members at the meetings of the Committee are noted on page 59

Dear Shareholder,

As Chairman of Sophos' Remuneration Committee, I am pleased to present the FY19 Directors' Remuneration report, which has been prepared by the Committee and approved by the Board. In line with the UK reporting regulations, this report is divided into three sections:

- the Annual Statement of the Remuneration Committee Chairman, including a 'Remuneration at a Glance' section on pages 80 and 81;
- the proposed future Directors' Remuneration Policy, which will be submitted to a binding shareholder vote at the Annual General Meeting ("AGM") on 25 September 2019. Further details on the proposed changes to the Policy (and the rationale for these) are set out on pages 82 to 90; and,
- the Annual Report on Remuneration, which focuses on our remuneration arrangements and incentive outcomes for the year under review and how the Committee intends to implement the proposed Remuneration Policy in FY20, set out on pages 91 to 101.

The Annual Report on Remuneration will be put to an advisory vote at the AGM in September 2019.

The context for Executive remuneration at Sophos

The IT security market is global, as is the market in which Sophos competes for high calibre executive talent. In order for Sophos to be able to attract and retain executives in the relevant geographies with the right skills and experience to drive the long-term success of the Group, the Committee believes that remuneration packages need to be appropriately calibrated to be competitive globally, including in the UK, where Nick Bray our Chief Financial Officer ("CFO") is located, and on the US West Coast, where Kris Hagerman our Chief Executive Officer ("CEO") and many of the Group's executives are located.

At the 2016 AGM, the Committee implemented a remuneration policy that was designed to balance this need, to be competitive globally with accepted UK market and best practice, and to measure and reward the performance of the Group's executives against the best measures of the Group's performance given its current size and stage of growth. In line with the Large and Medium-Sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013, we are required to submit the remuneration policy to a new binding shareholder vote at the 2019 AGM. The UK remuneration governance landscape continues to evolve at pace, and the Committee has considered the implications of these developments for our Policy. In addition to the external context for executive director remuneration at Sophos, the

Committee has also reviewed the remuneration arrangements that are operated for other levels of the organisation and evaluated what changes may be appropriate as Sophos matures as a business. This holistic assessment ensures that the Committee's decisions regarding executive remuneration are consistent with the Group's philosophy of pay, effectively underpin our corporate culture and reinforce delivery of our strategy. We have conducted a two-way consultation with our major shareholders on the remuneration policy we are proposing which we believe will ensure Sophos is able to continue to compete in a global market for senior executive talent with the right skills and experience to drive the long-term success of the Group, while reflecting investor feedback (and the latest developments in remuneration governance best practice) as well as aligning more closely with market norms for UK-listed companies.

As the 'Remuneration at a Glance' section overleaf demonstrates, strong billings and cash EBITDA performance over the last three years has contributed to the Group's significant growth in share price 33.7 per cent since Listing and Total Shareholder Return ("TSR") outperformance of the FTSE250 index. The Committee is comfortable that pay outcomes are appropriately aligned with Group performance against its strategic objectives and longer-term shareholder value creation.

Remuneration decisions in FY19

Following the strong results achieved in the year-ended 31 March 2018, Sophos experienced lower than expected results in the year-ended 31 March 2019, with billings of $760.3 million and cash EBITDA of $167.9 million at actual rates, against stretching targets. As a result, Kris Hagerman and Nick Bray will not receive bonuses.

In alignment with the Directors Remuneration Policy approved at the 2016 AGM, in recognition of FY18 company performance, during the year, Kris Hagerman and Nick Bray were granted awards of 500 and 390 per cent of salary respectively, under the Sophos Group Long-Term Incentive Plan 2015 (LTIP) in recognition of the strong results for the year ending 31 March 2018. Performance share units (comprising 75 per cent of the awards) vest after three years subject to achievement of annual billings and cash EBITDA targets, and restricted share units (25 per cent of the awards) vest over four years subject to continued employment only. Details of performance share units that have vested during the year to 31 March 2019 are set out on page 94.

Remuneration for FY20

Following a review of Group performance and their personal contribution, the salaries of the Executive Directors ("ED") will remain unchanged for FY20. This compares to the average increase expected for the wider employee population of c.3 per cent. For FY20, the annual bonus opportunity will be in line with our proposed Policy, and will be based on Revenue, Adjusted Operating Profit, and personal performance objectives. Targets have been set by the Committee to continue to require significant stretch performance for full payout to be achieved. The bonus will continue to be paid in cash. In FY20, the Committee also intends to grant long-term incentive awards to EDs in line with the proposed Remuneration Policy. Performance Share Units ("PSU") awards (which will represent 75 per cent of the total award opportunity) will vest subject to three-year Revenue Growth (subject to an Adjusted Operating Profit underpin) and three-year Relative TSR vs the FTSE250 index (excluding investment trusts). Further details of our approach to implementing our new Policy are set out in the Annual Report on Remuneration, on page 91.

On behalf of the Committee, I appreciate the feedback and broad support received from the shareholders and proxy advisors we consulted on the proposed Policy. The Committee remains committed to an open and transparent dialogue with all shareholders and welcomes feedback at any time of year. I will also be available at the forthcoming AGM to answer your questions, where I also hope to receive your support for our proposed Policy and the 2019 Annual Report on Remuneration.

On behalf of the Remuneration Committee:

Paul Walker

Chairman of the Remuneration Committee

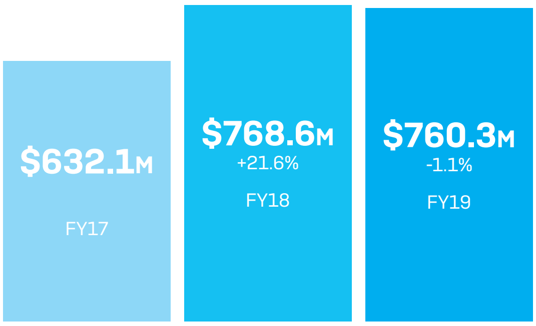
15 May 2019

This report, prepared by the Remuneration Committee ('the Committee') on behalf of the Board, takes account of the UK Corporate Governance Code and the latest Investment Association, ISS and PLSA guidelines, and has been prepared in accordance with the provisions of the Act, the Listing Rules of the Financial Conduct Authority and the Large and Medium-Sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. The Act requires the Auditor to report to the Company's Shareholders on the audited information within this report and to state whether in their opinion those parts of the report have been prepared in accordance with the Act. The Auditor's opinion is set out on pages 110 to 117 and those aspects of the report that have been subject to audit are clearly marked.

REMUNERATION AT A GLANCE

KPI – Performance snapshot

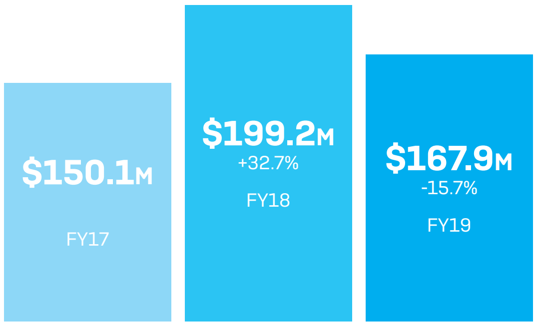
Billings



Used as a measure in the annual bonus and PSU

Billings is an important measure that represents the value of products and services invoiced to customers. Cash is received at the start of a subscription period and consequently billings are a key forward indicator of future performance.

Cash EBITDA



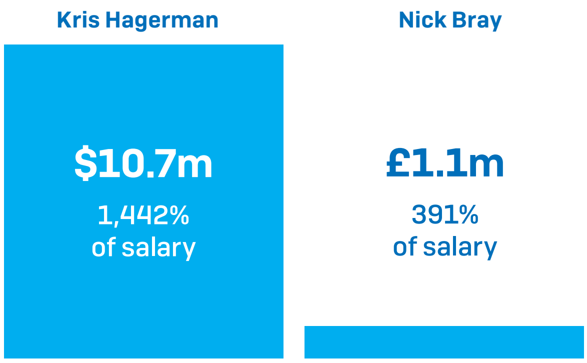
Used as a measure in the annual bonus and PSU

EBITDA (as defined in the scheme rules) provides visibility of cash earnings during the period, even if the associated revenue for that period's billings has not yet been recognised.

Executive Director remuneration in FY19

	Kris Hagerman $000	Nick Bray £000
Salary	735	298
Taxable benefits	2	17
Pension	9	15
Single-year variable	–	–
Restricted stock units	933	296
Performance stock units	3,000	1,038
All employee schemes	4	–
Total	4,683	1,664

Executive Director shareholdings



Implementation of Policy in FY20

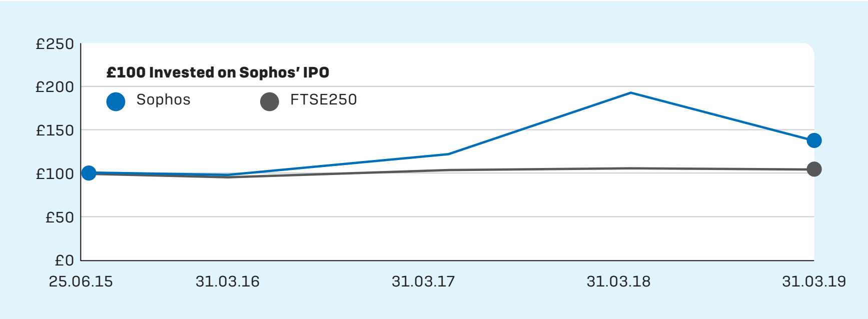
Salary

No increase to salaries, which will remain at $740,000 for Kris Hagerman and £300,000 for Nick Bray.

Annual bonus

Opportunities are reduced from FY19 at 150% and 120% of salary for Kris Hagerman and Nick Bray, respectively. Payout will be based 80 per cent on Revenue and Adjusted Operating Profit, and 20 per cent on personal performance. Payable 100 per cent in cash.

Total Shareholder Return ("TSR") since IPO

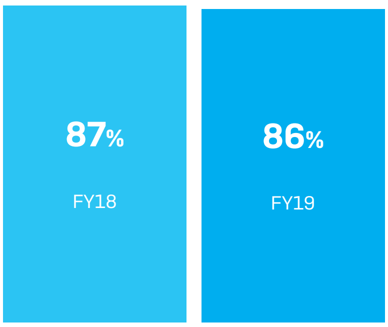


Close alignment through significant stock ownership

TSR is a key measure of shareholder value creation and beginning with FY20 awards, it will be incorporated as a standalone measure of performance in the LTIP. The interests of the Group's EDs are aligned closely with those of shareholders through their share ownership, as well as through the denomination of LTIP awards in stock units.

Number of employees

Overall employee satisfaction



LTIP

FY20 awards to be made over performance share units (at least 75% of the total award) and restricted shares, within normal policy limits. PSU awards will vest based on Revenue growth and TSR over the three-year period ending on March 31, 2022. RSU awards vest three years from grant.

Benefits

Unchanged from FY19.

DIRECTORS' REMUNERATION POLICY

The overarching principles of the remuneration policy are to provide a competitive package of fixed and variable pay that will enable the Group to ensure it has executives with the right skills and experience to drive the success of the Company, and that their remuneration is linked to shareholder interests and the Company's long-term success.

The remuneration philosophy is:

- to promote the long-term success of the Company, with stretching performance targets which are rigorously applied;
- to provide appropriate alignment between the Company's strategic goals, shareholder returns and executive reward; and,
- to have a competitive mix of base salary and short and long-term incentives, with an appropriate proportion of the package determined by stretching targets linked to the Company's performance.

EDs' fixed and variable remuneration arrangements have been determined taking into account:

- the role, experience in the role, and performance of the ED;
- the location in which the ED is working;
- remuneration arrangements at UK listed companies of a similar size and complexity;
- remuneration arrangements at US high-technology companies of a similar size and complexity, including companies with which the Company competes for talent; and,
- best practice guidelines for UK listed companies set by institutional investor bodies.

In advance of the expiry of our Policy (approved by shareholders at the 2016 AGM), the Remuneration Committee undertook a thorough review of our existing Policy in late 2018 to ensure that it would continue to enable Sophos to compete in the global market for senior executive talent, while reflecting investor feedback and developments in UK remuneration governance, as well as aligning more closely with UK market norms for established listed companies. This section describes the Group's proposed remuneration policy for Directors which will be submitted to a binding shareholder vote at the Annual General Meeting on 25 September 2019. Set out below is a summary of the major changes proposed to the version approved by shareholders in 2016.

Key changes proposed to our Remuneration Policy

1. Incentive award opportunities

- The maximum annual bonus opportunity will be 150 per cent of salary (previously 200 per cent of salary). The target annual bonus opportunity will be set at 67 per cent of maximum (to maintain the on-target total cash opportunity at current levels), with threshold performance paying 17 per cent of maximum.

- The maximum total long-term incentive opportunity in normal circumstances will be 300 per cent of salary (previously 500 per cent of salary), to more closely reflect UK market norms. Annual awards will continue to comprise a combination of Performance Stock Units ("PSU") and Restricted Stock Units ("RSU"), with PSUs comprising at least 75 per cent of the award opportunity. The continuation of this policy reflects competitive practices in our major markets for talent, including other high-technology US West Coast companies. The maximum total long-term incentive opportunity in exceptional circumstances will be 500 per cent of salary (previously 750 per cent of salary). Exceptional circumstances include, but are not limited to, the recruitment of a new executive director.

2. Extension of long-term incentive time horizons

- To support the principle of alignment of executive and long-term shareholder interests, RSU awards in the future will vest 100 per cent after three years (previous awards vest 25 per cent on the first anniversary of grant, with the remainder vesting on a quarterly basis over the following three years).

- In addition, any net vested shares (i.e. excluding those sold to cover the tax liability arising when an award vests) from PSU or RSU awards made in the future will be required to be held for a further holding period of two years before being released to the individual. The holding period will also apply to awards held by leavers until its normal expiry date.

3. Performance linkage

- Our proposed Policy continues to provide an appropriate degree of flexibility to determine the performance measures that will apply to the annual bonus and long-term incentive awards at the start of each cycle. However, it is proposed that the following measures be used for future incentive cycles:
  - Annual bonus to be based: 40 per cent on Revenue, 40 per cent on Adjusted Operating Profit, and 20 per cent on Personal Objectives. The two financial measures will operate independently, but accelerators do not take effect until both metrics hit target; and,
  - PSU awards to be based: 50 per cent on three-year Revenue growth (with an Adjusted Operating Profit underpin), and 50 per cent on three-year relative TSR vs the FTSE250 index (excluding investment trusts).

4. Increase to shareholding guidelines

- It is proposed that the in-post shareholding guideline be calibrated as 1x the annual long-term incentive award opportunity, i.e. 300 per cent of salary for the Group CEO and 250 per cent of salary for the Group CFO (previously: 200 per cent of salary for both Directors).

- With regards to the post-employment shareholding requirement, our proposal for the two-year holding period to continue to apply to awards held by leavers (see above) supports the principle of share retention post-employment. In addition, good leavers will retain an interest in unvested long-term incentive awards (albeit pro-rated for time and, in the case of PSUs, remaining subject to performance over the performance period). **The pre-tax value of outstanding awards (whether vested-but-held or unvested) for a good leaver at cessation of employment could be up to 1,200 per cent of base salary (CFO: 1,000 per cent). Where an executive is a bad leaver, vested-but-held awards could have a pre-tax value of up to 600 per cent of base salary (CFO: 500 per cent).** The Committee believes that this sustained share ownership and alignment of interests with shareholders beyond cessation of employment is in line with the UK Corporate Governance Code.

Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Fixed pay: Base salary			
To attract and retain talent of the right calibre and with the ability to contribute to strategy, by ensuring base salaries are competitive in the relevant talent market.	Base salaries are reviewed annually, with reference to individual performance, Group performance, competitiveness against relevant markets for talent, salary increases across the Group and the position holder's experience, competence and criticality to the business. Any increases are generally effective from 1 July.	Executive Directors' salary increases will normally be in-line with those for the wider employee population. However, higher salary increases may be made where there is a change in role or responsibilities or a significant market misalignment.	Individual and Group performance is taken into account when determining appropriate salary levels.
Fixed pay: Pension			
Provide post-retirement benefits for participants in a cost-efficient manner and in alignment with that of the wider workforce.	Pension contributions are provided, with a choice of funding vehicles: US 401(k) savings plan for all US employees or group personal pension scheme.	The CEO currently receives a matching contribution of up to 3 per cent of salary under his US 401(k) savings plan, subject to the applicable maximum contribution (US$24,500 for FY18). The CFO receives up to 5 per cent of salary as a contribution to a group personal pension scheme. These pension arrangements have been, and remain, consistent with the pension arrangements offered throughout the organisation more widely. Any new Executive Director appointed from the effective date of this Policy will be eligible for the same pension contribution as the rest of the Sophos workforce in the relevant market.	None.

DIRECTORS' REMUNERATION POLICY CONTINUED

Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Fixed pay: Benefits			
To provide competitive benefits for each role.	Benefits currently include the provision of medical and dental insurance, life and disability insurance, travel insurance, personal tax return preparation, and car allowance. Reasonable relocation, travel and subsistence allowances (and, in certain circumstances, cash allowances in respect of the associated tax charge) and other benefits may be provided based on individual circumstances.	There is no overall maximum value set out for benefits. They are set at a level that is comparable to market practice and appropriate for individual and Company circumstances. The Committee retains the discretion to amend benefits in exceptional circumstances or in circumstances where factors outside of the Group's control have materially changed (e.g. increases in insurance premiums).	None.
Variable pay: Annual bonus			
Aims to focus executives on achieving stretching financial targets relevant to the business priorities for the financial period.	Performance measures and targets are set prior to or shortly after the start of the relevant financial period. At the end of the financial period, the Remuneration Committee will determine the extent to which the targets have been achieved. Awards are typically delivered in cash; however, the Committee has discretion to defer awards in cash or in shares. The Committee has discretion to reduce the bonus in the event of serious financial misstatement or misconduct. In extreme cases of misstatement or misconduct, the Committee may claw back annual bonus payments previously made.	The maximum bonus opportunity for EDs will be up to 150 per cent of salary. Up to 67 per cent of maximum will vest for target performance. The Committee may award up to 17 per cent of maximum for threshold performance.	The annual bonus will be based on achievement of stretching financial targets and personal performance. Personal performance will be weighted at 20% of the annual bonus opportunity for FY20 and for future years for which this policy applies, personal performance will have a weighting of no more than a third of the bonus opportunity. Details of the measures used during the period under review are set out on pages 92 and 93. The Committee has discretion to adjust the formulaic bonus outcome downwards (or upwards with shareholder consultation) within the limits of the plan, to ensure alignment of pay with the underlying performance of the business.

Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Variable pay: Long-term incentive plan ("LTIP")			
Aligns the interests of executives with shareholders in growing the value of the business over the long-term.	The plan provides for annual awards of restricted shares and performance shares to eligible participants. Awards made in the future will normally vest on the third anniversary of grant. Other than for restricted shares, vesting is based on three-year performance. Any net vested shares from PSU or RSU awards made in the future will be required to be held for a further holding period of two years before being released to the individual. Shares subject to the two-year holding period are not forfeitable if a participant leaves employment, except in cases where the Committee, at its absolute discretion, determines that clawback/malus is appropriate. The Committee has discretion to reduce any unvested long-term incentive awards, or to vary the opportunities for future awards, in the case of serious financial misstatement or misconduct. In extreme cases of misconduct or misstatement, the Committee may claw back vested long-term incentive awards. Participants are eligible to receive cash or shares equal to the value of dividends that would have been paid over the vesting period on shares that vest.	Awards may be made up to a maximum of 300 per cent of salary in normal circumstances and up to 500 per cent in exceptional circumstances (including, but not limited to, recruiting an individual). The award size is reviewed in advance of grant. No performance-based awards will vest below threshold. Up to 25 per cent of each element will vest for achievement of threshold performance under each metric, then increase on a straight-line basis to full vesting for achieving stretch performance. It is anticipated that no more than 25 per cent of aggregate awards in any one year will be over restricted shares or options.	Performance-based awards: Vesting is subject to continued employment and performance against two measures, which are intended to be as follows for awards made over the life of the Policy: – Revenue growth (subject to an adjusted operating profit underpin) ;and, – Relative Total Shareholder Return as compared to the FTSE250 index (excluding investment trusts). It is the intention that the weighting of the measures will be equal (i.e. 50 per cent each) but the Committee will consider, and adjust if deemed appropriate, the weighting at the start of each cycle. In addition, other measures may be considered for future cycles to help capture the strategic goals of the business and may be used in conjunction with these metrics. Time-based awards: restricted shares will vest 100 per cent after three years. The Committee has discretion to adjust the formulaic LTIP award downwards (or upwards with shareholder consultation), within the limits of the plan, to ensure alignment of pay with the underlying performance of the business.
Other arrangements: Shareholding guidelines			
To align Directors' interests with the long-term interests of shareholders.	EDs are required to retain a minimum shareholding in the Company and are required to retain 50 per cent of shares vesting (after tax) under the LTIP for a minimum of two years until the shareholding guideline has been met. Further details of the level of shareholding guideline currently in operation is set out on page 99.	n/a	None.

DIRECTORS' REMUNERATION POLICY CONTINUED

Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Other arrangements: All-employee schemes			
To encourage share ownership across the workforce.	Save as You Earn ("SAYE") and Employee Stock Purchase Plan ("ESPP") schemes are operated by the Company for eligible employees, in which EDs may participate on the same terms.	Participation is capped at the prevailing approved limit at the time eligible employees are invited to participate, or such lower limit as determined by the Remuneration Committee.	None.
Other arrangements: Non-Executive Directors' fees			
To reflect the time commitment in preparing for and attending meetings, the duties and responsibilities of the role and the contribution expected from the Non-Executive Directors.	Annual base fee for Chairman. Annual base fee for Non-Executive Directors. Additional fees paid to the chairmen of Board Committees. Additional fees may be paid if there is a material increase in time commitment required. Non-Executive Directors do not participate in any incentive schemes, nor do they receive any pension or benefits (other than nominal travel expenses and, in certain circumstances, cash allowances in respect of the associated tax charge).	Any increases to Non-Executive Director fees will be considered as a result of the outcome of a review process and taking into account wider market factors, e.g. inflation. There is no prescribed individual maximum fee. Further details are set out on page 96.	None.

Notes to the policy table

Performance measure selection and approach to target setting

As the Group's strategy has evolved and business priorities have changed, Revenue and Adjusted Operating Profit are considered to be the best measures of the Group's annual performance.

Annual bonus targets will be set prior to, or shortly after, the start of the financial year. Targets will be based around the annual budget approved by the Board and take into account the Group's performance over the prior year, as well as an appropriate degree of challenge to provide an incentive to outperform the annual budget. Threshold and stretch performance levels for performance-based awards under the LTIP will be set at the start of the three-year performance period. The Committee aims to set stretching but achievable financial targets, taking account of a range of reference points, including market consensus and the Group's strategic plan. The level of TSR outperformance required for full vesting is set by reference to the level of outperformance that would have been equivalent to broadly upper quartile performance over rolling three-year periods historically.

Differences in Remuneration Policy operated for other employees

The remuneration for other employees comprises the same components as set out in the policy, being base salary, annual bonus, long-term incentive participation, pension, life assurance, and benefit provision. Annual bonus and long-term incentive arrangements share a similar structure and pay-out arrangement, although the mix between performance-based and time-based awards, and the maximum award, varies by seniority and role.

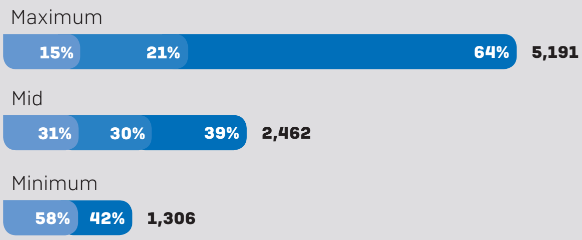
Other

Any commitment made prior to, but due to be fulfilled after, the approval and implementation of the policy detailed in this report will be honoured, including awards made to Directors (both Executive and Non-Executive) prior to the initial public offering of the Company's shares in 2015 ("IPO"). The Committee also retains discretion to make minor, non-significant changes to the Policy without reverting to shareholders.

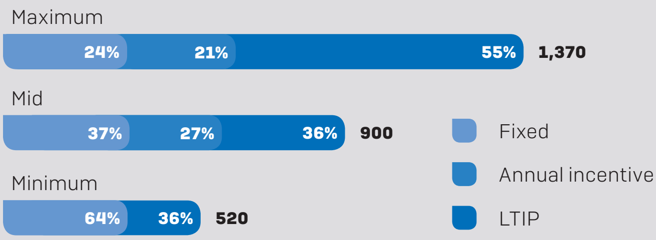
Performance scenarios

The graphs below provide estimates of the potential future reward opportunities for EDs, and the potential split between the different elements of remuneration under three different performance scenarios; 'Minimum', 'Mid' and 'Maximum'.

Chief Executive Officer $000



Chief Financial Officer £000



The potential reward opportunities illustrated are based on the policy to be presented for approval at the AGM on 25 September 2019, applied to the base salaries in force at 1 April 2019. The assumptions made in illustrating potential reward opportunities are shown in the table below:

Performance scenario	Fixed pay	Annual bonus	LTIP (performance-based awards)	LTIP (time-based awards)
Minimum	Salary as at most recent review date Benefits and pension value as for the most recent financial period	No annual bonus payable	Threshold not achieved	Full vesting
Mid		On target annual bonus payable	Performance warrants threshold vesting	
Maximum		Maximum annual bonus payable	Performance warrants full vesting	
Maximum (with LTIP awards valued assuming 50 per cent share price appreciation)			Performance warrants full vesting, plus 50 per cent share price appreciation	Full vesting, plus 50 per cent share price appreciation

Approach to remuneration for new Executive Director appointments

In the cases of hiring or appointing a new ED, the Remuneration Committee may make use of all the existing components of remuneration, as follows:

Component	Approach	Maximum opportunity
Base salary	The base salaries of new appointees will be determined based on the experience and skills of the individual, relevant market data and their current basic salary.	n/a
Pension	Membership of pension scheme or salary supplement on a similar basis to other executives, as described in the policy table. Other than in exceptional cases (such as to replace existing arrangements for new recruits) the Committee does not anticipate pension benefits as being at a cost to the Company that would exceed 20 per cent of base salary.	In line with policy table
Benefits	New appointees will be eligible to receive benefits in line with the policy which may include (but are not limited to) car allowance, medical insurance and life insurance.	n/a
Annual bonus	The structure described in the policy table will apply to new appointees with the relevant maximum being pro-rated to reflect the proportion of employment over the year.	150 per cent of base salary
LTIP	New appointees will be granted awards under the LTIP on similar terms as other executives, as described in the policy table.	Up to 500 per cent of base salary
All-employee schemes	New appointees may be eligible to participate in all-employee schemes on the same basis as other employees.	In line with policy table

DIRECTORS' REMUNERATION POLICY CONTINUED

In determining appropriate remuneration for a new ED, the Committee will take into consideration all relevant factors to ensure that arrangements are in the best interests of the Group and its shareholders. In addition to the remuneration arrangements set out above, the Committee may make an award in respect of a new appointment to 'buy-out' incentive arrangements forfeited on leaving a previous employer, using Listing Rule 9.4.2 R if necessary. In doing so, the Committee will take account of relevant factors including any performance conditions attached to these awards, the likelihood of those conditions being met, and the proportion of the vesting period remaining. The fair value of any 'buy-out' will not exceed that of the award being foregone.

In cases of appointing a new ED by way of internal promotion, the approach will be consistent with the policy for external appointees detailed above. Where an individual has contractual commitments made prior to their promotion to Board level, the Group will continue to honour these arrangements. Incentive opportunities for below Board employees are no higher than for EDs, but measures may vary.

In recruiting a new Non-Executive Director, the Committee will use the policy as set out in the table on page 86.

Service contracts and exit payment policy

Non-Executive Directors ("NED")

The appointments of each of the Chairman and the NEDs are for a fixed-term of three years and subject to annual re-election by the Company at the AGM. Their letters of appointment set out the terms of their appointment and are available for inspection upon request. They are not eligible to participate in the annual bonus, nor do they receive any additional pension or benefits (other than nominal travel expenses) on top of the fees disclosed on page 96. NED appointments may be terminated at any time upon written notice or in accordance with the Articles and receive no compensation on termination.

NED	Role	Appointment date	Term of appointment
Peter Gyenes	Chairman	4 June 2018	Three years
Paul Walker	Senior Independent Director	4 June 2018	Three years
Sandra Bergeron	Independent NED	4 June 2018	Three years
Roy Mackenzie	NED	4 June 2018	Three years
Vin Murria	Independent NED	3 January 2017	Three years
Rick Medlock	Independent NED	3 April 2017	Three years

Executive Directors

On 11 June 2015, each of the EDs entered into a service agreement with the Company, which are available for inspection upon request.

ED	Role	Appointment date	Term of appointment
Kris Hagerman	CEO	11 June 2015	12 months
Nick Bray	CFO	11 June 2015	12 months

The employer is entitled to terminate an ED's employment by payment of a cash sum in lieu of notice, equal to (i) the basic salary that would have been payable, and (ii) the cost that would have been incurred in providing the ED with medical insurance benefits for any unexpired portion of the notice period (the ''Payment in Lieu''). The Company can alternatively choose to continue providing the medical insurance benefits under item (ii) instead of paying a cash sum representing their cost. The Payment in Lieu will be paid in monthly instalments over the notice period.

In specified circumstances (not involving a change of control, in which case the severance payment applicable is as described below), each ED is entitled to terminate his employment without notice and receive a severance payment. The severance payment will be equal to the Payment in Lieu and paid in a single lump sum. The specified circumstances are where either: (a) the employer terminates or gives notice to terminate the ED's employment without cause; or (b) the ED terminates his employment in response to: a material diminution of his authority, duties, responsibilities or status in a manner inconsistent with his service agreement; a breach of a fundamental term of his service agreement; a material reduction in his annual basic salary or target bonus opportunity; or being required to relocate his place of work beyond a specified distance (each a ''Good Leaver Reason'').

Each ED is entitled to a severance payment, paid in a single lump sum, in the event of a termination of his employment by his employer without cause or by the ED for a Good Leaver Reason at any time during a period ending 18 months after any change of control of the Company (whether by way of a general offer or a scheme of arrangement or compromise) and beginning three months prior to the announcement of such general offer or scheme of arrangement or compromise. The severance payment will be equal to the sum of: (i) 150% of the ED's annual basic salary; (ii) 150% of the ED's target bonus for the Company's financial year in which the termination occurs; and (iii) the total cost of providing the ED with the benefits (including pension contributions) to which he is entitled under his service agreement for a period of 12 months.

The Group's change of control provisions are standard practice in the US (where many of the Senior Management Team, including the CEO, are located) and to renegotiate contracts would likely represent an increased cost for the Company (where this provision may never be triggered). For future hires, the Committee will consider the appropriateness of the contractual provisions at that time, taking into account prevailing market practice in the geography that the executive is located.

The Company's policy on termination payments is to consider the circumstances on a case-by-case basis, taking into account the executive's contractual terms, the circumstances of termination and any duty to mitigate. The table below summarises how incentives are typically treated in different circumstances:

Reason for leaving	Treatment
Bonus	
Summary dismissal, resignation	Awards lapse.
Good leaver	Eligible for an award to the extent that performance conditions have been satisfied, pro-rated for the proportion of the financial year served, with Committee discretion to treat otherwise.
Change of control	Eligible for an award to the extent that performance conditions have been satisfied up to the change of control, pro-rated for the proportion of the financial year served, with Committee discretion to treat otherwise. Executives may be eligible for an enhanced bonus payment in the case of termination of employment within 18 months of a change of control, as described above.
Long-term incentives	
Summary dismissal, resignation	Awards lapse.
Good leaver	Outstanding awards will normally be pro-rated to the date of leaving, with Committee discretion to treat otherwise and with discretion to either test at the end of relevant performance periods, or immediately assess, whether or not relevant performance criteria have been met.
Change of control	Outstanding awards will normally vest and be tested for performance over the period to change of control, and be pro-rated for time based on the proportion of the period served, with Committee discretion to treat otherwise. Executives may be eligible for additional vesting in the case of termination of employment within 18 months of a change of control.
All-employees schemes	
Treated in line with applicable scheme rules.	

DIRECTORS' REMUNERATION POLICY CONTINUED

External appointments of Executive Directors

EDs may only accept external appointments with the prior approval of the Chairman, provided that such appointments do not prejudice the executive's ability to fulfil their duties for the Group. Any fees for outside appointments would normally be retained by the Director.

Consideration of employment conditions elsewhere in Group

The Committee takes into account the general basic salary increase being offered to employees elsewhere in the Group when annually reviewing the salary increases and remuneration for the EDs. The Committee is also informed of management decisions regarding incentive structures and remuneration arrangements for all other staff and considers these when making decisions in relation to ED remuneration. This approach ensures remuneration arrangements are appropriately cascaded across the Group to support our culture and delivery of our strategy, while differentiation by organisational level and/or geography ensures Sophos is able to compete effectively in all talent markets. Employees have not been consulted in respect of the design of the Group's senior executive remuneration policy.

Consideration of shareholder views

The Committee takes shareholder feedback into careful consideration when reviewing remuneration and regularly reviews the Remuneration policy in the context of key institutional shareholder guidelines and best practice. It is the Committee's policy to consult with major shareholders prior to making any major changes to its executive remuneration structure.

ANNUAL REPORT ON REMUNERATION

The following section provides details of remuneration outcomes for the financial year ended 31 March 2019 for Directors who served on the Board during the year, and how the Remuneration policy will be implemented in FY20.

The Remuneration Committee

The Committee met three times during the year.

Committee composition and meeting attendance

The composition of the Committee is compliant with the Provisions of the Code, which provides that its members should comprise at least three independent Non-Executive Directors and that the Chairman of the Group may be a member, but not chair, of the Committee due to his independence at the time of his appointment. The Committee is chaired by Paul Walker, the Senior Independent Director ("SID"). The Company Secretary is secretary to the Committee and attends all meetings. Other attendees at Committee meetings may differ from time to time and, upon invitation from the Committee, include the Chief Executive Officer ("CEO"), Chief Human Resources Officer ("CHRO") and other senior executives, but they are not present when their own remuneration is set.

Role and responsibilities

The Committee is responsible for overseeing the Group's Remuneration policy and practices having regard for relevant legal and regulatory requirements, the provisions and recommendations of the Code and associated guidance.

The key responsibilities of the Committee include, to:

- determine and monitor the remuneration policy for the Chairman, Executive Directors and the senior management team it is designated to consider;
- ensure that the remuneration policy and reward decisions support the Sophos business strategy and sustainable long-term performance;
- set specific remuneration packages which include salary, annual bonus, share incentives, pension and benefits;
- review the Executive Directors' service contracts;
- review remuneration trends across the Group and in the market in which Sophos operates; and,
- approve employee share-based incentive plans and associated performance conditions and targets.

Main activities

The Committee has an annual forward agenda, developed from its terms of reference, with standing items that the Committee considers at each meeting, in addition to any specific matters arising, and topical business or governance items on which the Committee has chosen to focus. The work of the Committee undertaken during the year is summarised throughout this report.

External advisers

Mercer Kepler, independent remuneration consultants appointed by the Committee in FY16 after consultation with the Board, continued to act as the remuneration adviser to the Committee during the year. Mercer Kepler reports directly to the Committee Chairman and is a signatory to and abides by the Code of Conduct for Remuneration Consultants (which can be found at www.remunerationconsultantsgroup.com).

The fees paid to Mercer Kepler in respect of work carried out for the Remuneration Committee in FY19 totalled £136,622 (FY18: £52,681). In addition, a separate and distinct department of Mercer (also part of the MMC Group of companies), provided independent verification and consultation services to Sophos during FY19 in relation to the Company's UK Gender Pay Gap and Pay Programme analysis, and reported directly to the CHRO. The Committee Chairman undertook due diligence to ensure that Mercer Kepler remains independent of the Company and that the advice provided is impartial and objective. The Committee is satisfied that the advice provided by Mercer Kepler is independent, and will continue to undertake such due diligence periodically.

ANNUAL REPORT ON REMUNERATION CONTINUED

Performance evaluation

The Remuneration Committee's performance was assessed as part of the Board's annual effectiveness review. It was concluded that the Committee operated effectively in FY19. In response to findings of the review, Committee members will continue to give significant weight to shareholder sentiment whilst balancing this with the recruitment and retention needs of the business and in particular, in their consideration of the Company's remuneration policy as it is reviewed for renewed shareholder vote at the 2019 AGM.

The Committee also undertakes a review of its terms of reference and composition each year. A review was carried out in May 2019, with only minor updates. The full terms of reference of the Committee can be found on the Company's website at: investors.sophos.com.

Single total figure of remuneration for Executive Directors (Audited)

The table below sets out the total single figure of remuneration received by each Executive Director who served during the year-ended 31 March 2019 and the prior-year:

	Kris Hagerman ($000)		Nick Bray (£000)	
	FY19	FY18	FY19	FY18
Salary[1]	735	716	298	291
Taxable benefits[2]	2	3	17	16
Pension[3]	9	8	15	15
Single-year variable[4]	0	638	0	207
Restricted stock units[5]	933	877	296	283
Performance stock units[6]	3,000	6,458	1,038	2,186
All employee schemes	4	4	–	–
Total	4,683	8,704	1,664	2,998

1 Amount earned in respect of the year

2 Taxable benefits include: Kris Hagerman: medical and dental, life and disability insurance and reimbursement of up to $10,000 per annum for the preparation of his tax returns; Nick Bray: Car allowance (FY19: £15K FY18: £14K), life, private medical and critical illness insurances, travel and personal accident insurances, and employee assistance programme arrangements

3 The Company's pension contributions during the year of up to three per cent and five per cent of salary for Kris Hagerman and Nick Bray, respectively

4 Bonus payment for performance during the year

5 RSUs: The face value at grant, using market price on day of issue, of time-based RSUs

6 PSUs: The estimated value at vesting of PSUs for which the performance period ends at the end of the relevant financial year. For FY19, reflects the number of FY17 PSUs vesting in FY20 subject to performance over the three-year period ended 31 March 2019, valued using the average middle market quotation of the shares on the main market of the London Stock Exchange ("MMQ") over the three-months to 31 March 2019 (converted at daily US dollar rates for Kris Hagerman), and including the estimated value of dividends accruing over the vesting period on this award

Base salary

In April 2019, the Remuneration Committee reviewed the salaries of Kris Hagerman and Nick Bray, with neither receiving an increase. Pay as of 1 July 2019 remains unchanged:

Executive Director	July 2019	July 2018	Increase %
Kris Hagerman	$740,000	$740,000	0.0%
Nick Bray	£300,000	£300,000	0.0%

Pension and benefits

Kris Hagerman receives medical and dental insurance, travel insurance, life and disability insurance, a reimbursement of up to $10,000 per annum for the preparation of his tax returns and, under his employer's standard US 401(k) savings plan for all US employees, is entitled to receive a matching contribution of up to 3 per cent of his salary, subject to any annual maximum contribution applicable to US 401(k) savings plans from time to time. For the calendar year 2019, this annual employee contribution maximum is $25,000.

Nick Bray is entitled to receive up to five per cent of his base salary as a contribution to a group personal pension scheme. In FY19 he also received an annual car allowance of £15,000 (paid monthly), life insurance, private medical and critical illness insurance, travel insurance, personal accident insurance and employee assistance programme arrangements.

Incentive outcomes for FY19

Annual bonus

The Group operates an annual performance-related bonus scheme for a number of senior executives including Executive Directors. Bonus opportunities for FY19 were 200 per cent of salary for Kris Hagerman and 160 per cent of salary for Nick Bray. Target bonus was 50 per cent of the maximum opportunity.

The level of annual bonus earned in any one year is based on Group performance against pre-determined financial targets for the year and personal performance. In FY19, the bonus was based 80 per cent on billings and EBITDA, as defined by the scheme rules, with 12.5 per cent of maximum vesting for threshold performance and 50 per cent for target performance. The remaining 20 per cent of the bonus opportunity is based on personal performance. No bonus is awarded for performance below the threshold. The financial element payout is based on the lower of the implied payouts for billings and EBITDA, so to achieve any vesting of this element, executives were required to perform on both billings and EBITDA.

Financial performance

The financial targets for the FY19 annual bonus are no longer considered commercially sensitive, and are disclosed in full, alongside performance against these targets, below:

Performance measure	Threshold (12.5% payout)	Target (50% payout)	Stretch (100% payout)	Achievement	Vesting (% of element)
Billings	$866M	$899M	$1,079M	87%	0%
EBITDA	$229M	$238M	$285M	71%	0%

Performance was measured using constant currency exchange rates. For levels of performance between the points set out in the table above, bonus payout was determined on a straight-line, pro-rata basis. The overall bonus payout was based on the lower of the implied payouts for billings and EBITDA, and was therefore zero per cent of maximum for the financial element.

Personal performance

Following the end of FY19, the Committee assessed each Executive Director's performance against personal objectives set at the start of the year and in-line with Company objectives. Performance of the Executive Directors in respect of overall FY19 Company performance was assessed to warrant a payout of zero per cent for the personal element.

ANNUAL REPORT ON REMUNERATION CONTINUED

Long-Term Incentive Plan

FY17 PSU awards vesting (audited)

PSU awards were granted to Kris Hagerman and Nick Bray in FY17 (calendar year 2016). These awards are subject to performance against annual billings and cash EBITDA targets set for each of the financial years FY17, FY18 and FY19. Performance against each of these measures over the completed performance period is summarised in the table below:

Performance period	Weighting (of max.)	Performance measure	Initial Vesting: Threshold (25% vesting)	Initial Vesting: Stretch (100% vesting)	Accelerator Vesting: Super Stretch (1 x multiplier)	Accelerator Vesting: Maximum (1.25 x multiplier)	Financial year outcome	Vesting outcome (out of 125%)
FY17	One-third	Billings	$554M	$615M	$655M	$706M	$632M	100%
		Cash EBITDA	$127M	$142M	$157M	$169M	$150M	100%
FY18	One-third	Billings	$637M	$707M	$766M	$826M	$769M	101%
		Cash EBITDA	$150M	$166M	$189M	$204M	$194M	107%
FY19	One-third	Billings	$732M	$814M	$896M	$967M	$760M	51%
		Cash EBITDA	$176M	$195M	$230M	$284M	$162M	Nil
			Average of the lowest vesting outcomes in FY17, FY18 and FY19				67.0%	

Overall vesting (based on the aggregate of the lowest vesting outcome for each performance period)

For each performance year, the vesting outcome is based on the lower of that warranted by billings performance and cash EBITDA performance. Based on the performance outcomes set out above, 67.0 per cent of the FY17 PSU awards will vest, representing 53.60 per cent of the maximum opportunity. Details of the awards vesting to Executive Directors are set out in the table below:

Executive Director	Interests held	% vesting	Interests vesting	Date of vesting	Share price at vesting[1]	Value (£000)
Kris Hagerman	993,603	67.00%	665,714	14 Jun 2019	336.9p	2,243
Nick Bray	447,744	67.00%	299,988	14 Jun 2019	336.9p	1,011

1 The estimated value of vested awards is calculated using the MMQ over the three months to 31 March 2019. The estimated value of dividends accruing over the vesting period on these awards for Kris Hagerman and Nick Bray are $81K (£62K) and £28K respectively, and will be paid in cash

The RSU awards are not subject to future performance conditions, and will vest over four years, subject to continued employment, with 25 per cent of the awards vesting on 1 June 2019 and the remainder vesting on a quarterly basis thereafter until 1 June 2022.

The PSU awards vest subject to the vesting outcome implied by performance against annual targets over the three years to the financial year-ending 31 March 2021, with the award vesting (to the extent that targets are met) on the third anniversary of grant. Targets for the three years are set at the start of the performance period. Vesting is based on the lower of the implied payouts for billings and cash EBITDA, with 25 per cent vesting for threshold performance, 100 per cent for stretch performance, and 125 per cent vesting for maximum performance. The table on page 95 sets out the face value of awards granted in FY19 which can vest, subject to performance set out above, and in the table below.

No awards will vest for performance below the threshold.

Performance targets for outstanding PSU awards

The Committee believes that disclosing the individual annual financial performance targets for FY20 and FY21 in this report would put the Company at a competitive disadvantage to its international and privately held competitors, that are not subject to similar disclosure requirements. However, the Committee remains committed to disclosing (on a retrospective basis) the annual financial targets attaching to outstanding PSU awards, and performance against these.

FY18 PSU awards

			Initial Vesting		Accelerator Vesting			
Performance period	**Weighting (of max.)**	**Performance measure**	**Threshold (25% vesting)**	**Stretch (100% vesting)**	**Super Stretch (1 x multiplier)**	**Maximum (1.25 x multiplier)**	**Two-year performance to 31 March 2018**	**Vesting outcome (out of 125%)**
FY18	One-third	Billings	$663M		$736M	$825M	$769M	109%
		Cash EBITDA	$164M		$182M	$204M	$194M	113%
FY19	One-third	Billings	$772M		$858M	$989M	$760M	0%
		Cash EBITDA	$204.6M		$227M	$252M	$162M	0%
FY20	One-third	Billings	To be disclosed in the FY20 Annual Report on Remuneration					
		Cash EBITDA						

Note: actual vesting is dependent on the performance against targets for each of the financial years FY18 to FY20 and is based on the lower of the implied payouts for billings and cash EBITDA (i.e. the measures are equally weighted); sliding scale vesting applies between threshold and stretch, and super stretch and maximum. The final total vesting percentage will not be known until the end of the three-year performance period).

FY19 PSU awards

			Initial Vesting				
Performance period	**Weighting (of max.)**	**Performance measure**	**Threshold (25% vesting)**	**Stretch (100% vesting)**	**Maximum (1.25 x multiplier)**	**One-year performance to 31 March 2018**	**Vesting outcome (out of 125%)**
FY19	One-third	Billings	$801M	$890M	$989M	$760M	0%
		Cash EBITDA	$203M	$226M	$259M	$162M	0%
FY20	One-third	Billings	To be disclosed in the FY20 Annual Report on Remuneration				
		Cash EBITDA					
FY21	One-third	Billings	To be disclosed in the FY21 Annual Report on Remuneration				
		Cash EBITDA					

Note: following the publication of the Company's external billings targets during the year, the structure for the LTIP PSU awards' performance conditions has been simplified. The gap between the previous Stretch and Super Stretch targets has been removed for all PSU awards made from FY18 onwards. Actual vesting is dependent on the performance against targets for each of the financial years FY18 to FY20 and is based on the lower of the implied payouts for billings and cash EBITDA (i.e. the measures are equally weighted). Vesting on a sliding scale between 25 and 100 per cent applies between threshold and stretch, and a 1.25 multiplier applies up to the maximum 125 per cent vesting for performance above stretch. The final total vesting percentage will not be known until the end of the three-year performance period.

Dilution limits

Sophos will continue to manage dilution within the context of maintaining award levels within a 10 per cent limit over five years, the limit that has applied since the equity incentive plans were approved at IPO. The Committee is aware that this is higher than the limit adopted by many UK companies and preferred by many institutional investors of 5 per cent over 10 years in respect of discretionary awards and 10 per cent over 10 years in respect of all schemes. The Committee believes the higher limit we operate is necessary in part because of the broad based nature of our equity incentive plans, under which shares are provided to a large proportion of our employees (including SAYE and ESPP schemes open to most employees). The equity incentive plans are a key part of the Group's employee compensation package, and reflects the need to be able to compete with other US and international companies for the high-calibre employees and executives required to secure Sophos' future success.

At 31 March 2019, dilution under all our incentive schemes was c.6.7 per cent, and continues to reflect the front-loaded approach to equity incentive grants following the IPO.

ANNUAL REPORT ON REMUNERATION CONTINUED

Single Total Figure of Remuneration for Non-Executive Directors (Audited)

The table below sets out the total single figure of remuneration received by each Non-Executive Director who served during the year-ended 31 March 2019 and the prior-year:

	Base fee ($000)		Additional fees ($000)		Other ($000)		Total ($000)	
	2019	2018	2019	2018	2019	2018	2019	2018
Peter Gyenes	250	250	5	5	–	–	255	255
Sandra Bergeron	150	150	–	–	–	–	150	150
Edwin Gillis	–	66	–	7	–	–	–	73
Rick Medlock	150	150	15	8	–	–	165	158
Steve Munford[1]	128	150	–	–	-	–	128	150
Vin Murria	150	150	–	–	–	–	150	150
Paul Walker	150	150	25	25	–	–	175	175

1 Steve Munford stepped down 7 Feb 2019

Exit payments made in year (Audited)

No exit payments were made to Directors in FY19.

Payments to past Directors (Audited)

No payments were made to past Directors in FY19.

External directorships

In FY19 Nick Bray received £58K as a Non-Executive Director of De La Rue plc (FY18: £58K).

Remuneration for FY19

Base salary

Salaries for Kris Hagerman and Nick Bray, effective from 1 July 2019, will be $740,000 and £300,000, respectively. This is lower than increases awarded to the broader employee population of c.3 per cent, representing a 0 per cent increase on previous year base.

Pension and benefits

In line with the Remuneration Policy, the Executive Directors will continue to receive pension contributions of 3 to 5 per cent of salary. They will also continue to receive benefits in line with the Policy.

Annual bonus

For the year-ending 31 March 2020, the Committee will operate the annual bonus using an updated framework with new measures. Revenue and Adjusted Operating Profit targets have been set by the Committee and will require Executive Directors to deliver significant stretch performance to achieve full payout. Given the close link between these targets and Sophos' competitive strategy, these financial targets are considered commercially sensitive and will not be disclosed in advance but will be disclosed on a retrospective basis in next year's Annual Report on Remuneration.

All of the bonus will be paid in cash. Bonus payments are subject to malus and clawback provisions.

Long-Term Incentive Plan

In FY20, the Committee intends to grant long-term incentive awards to Executive Directors in line with the amended remuneration policy following the 2019 AGM, see page 85. Full details of the awards will be set out in the Annual Report for the year-ending 31 March 2020. LTIP awards are subject to malus and clawback provisions.

Non-Executive Director fees (including the Chairman)

With effect from the IPO, the fees payable to the Chairman of the Board and other Non-Executive Directors ("NED") are as follows:

		Fee p.a.
Chairman of the Board		$250,000
NED base fee		$150,000
Additional fees:	Audit and Risk Committee Chairman	$15,000
	Remuneration Committee Chairman	$10,000
	Nominations Committee Chairman	$5,000
	Senior Independent Director	$15,000

There will be no change to the NED fee policy set out above for FY20.

Percentage change in CEO remuneration

The table below shows the percentage change in the CEO's remuneration from the prior-year compared to the average percentage change in remuneration for all other employees. To provide a meaningful comparison, the analysis is based on a consistent set of employees, i.e. the same individuals appear in the FY18 and FY19 populations.

	% change FY18 to FY19	
	CEO	Other employees
Base salary	0%	9%
Taxable benefits	–	–
Single-year variable	-100%	-100%

Relative importance of spend on pay

The following table shows, for FY19 and FY18, the actual expenditure and percentage change in total employee costs and percentage change in distributions to shareholders.

	FY19 $M	FY18 $M	Change %
Shareholder distributions – dividends[1]	23.9	21.8	10%
Total employee expenditure[2]	370.1	361.9	2%

1 Represents dividends paid in each financial year

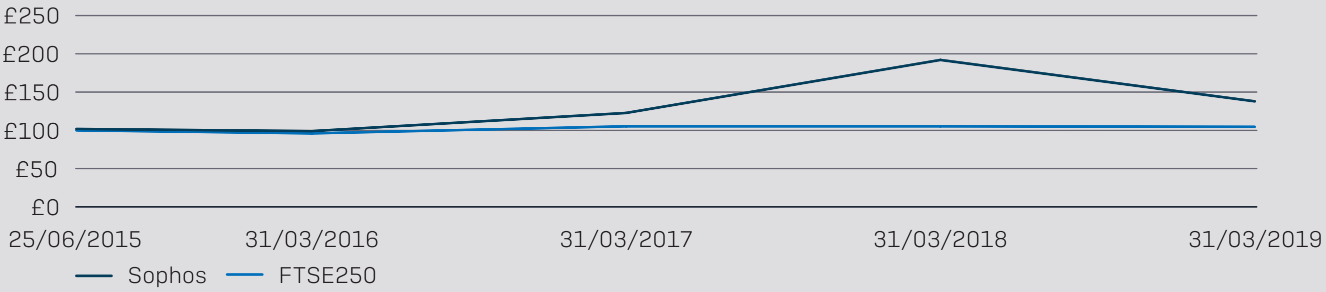
2 Total employee expenditure includes wages and salaries, social security costs, pension and other costs and share-based payments, see note 10 of the Financial Statements

ANNUAL REPORT ON REMUNERATION CONTINUED

Pay for performance

In line with the reporting regulations, Sophos is required to provide a graph showing the Company's TSR performance (share price plus dividends paid) compared with the performance of a relevant comparator group since IPO, assuming a nominal £100 investment in both the Company and the comparator group at the start of the timeframe. Companies are also required to show the CEO's single figure of remuneration and actual variable pay outcomes over the same period.

Sophos has chosen to compare its performance against the FTSE250 Index, as the Company became a constituent of the index on IPO. The table below details the CEO's single figure of remuneration and actual variable pay outcomes over the same period. As Sophos completed its IPO in July 2015, TSR data and pay disclosure is available from this date to 31 March 2019 only.



	FY17	FY18	FY19
Incumbent	Kris Hagerman	Kris Hagerman	Kris Hagerman
CEO single figure of remuneration ($000)	$2,322	$8,704	$4,683
Annual bonus outcomes (% of maximum)	55%	44%	0%
PSU vesting outcome (% of maximum)	n/a	93%	54%

Statement of shareholder voting

The following table shows the result of the advisory vote on the 2018 Annual Report on Remuneration at the 2018 AGM and the binding vote on the Remuneration Policy at the 2016 AGM.

	For		Against		Withheld
	Number	%	Number	%	Number
Remuneration Policy (2016 AGM)	279,603,831	72.15%	107,903,661	27.85%	4,904,177
2018 Annual Report on Remuneration	267,403,495	67.62%	128,070,534	32.38%	5,171

Following the 2018 AGM, the Company published an interim statement in response to the result of the advisory vote on the Annual Report on Remuneration, which received a 32.38 per cent vote against the resolution. This disappointing result reflected continued divergence in shareholder views over several of the features of the Company's executive remuneration arrangements that depart from generally-accepted UK practice, but reflect competitive practices in relevant talent markets for the Group.

Since the 2018 AGM, the Remuneration Committee has conducted a comprehensive review of the Policy and is proposing a number of revisions intended to align the Company's Executive Director remuneration policy more closely with UK market norms and appropriately respond to recent developments in remuneration governance. Details of the proposed Policy are set out in the Policy Report on pages 82 to 90 of this report.

The Company has been consulting with its largest shareholders and proxy advisors on the proposed Policy in recent months. While some divergence from UK market norms remains necessary to enable the Company to attract and retain executives in the relevant geographies, with the right skills and experience to ultimately drive the long-term success of the Company, those shareholders that responded during the consultation period indicated broad support for the proposed changes. The proposed future Policy will be put to a binding vote at the AGM on 25 September 2019 and the Committee hopes that it can count on the support of shareholders.

Directors' share ownership (Audited)

The table below shows the shareholding of each Director against their respective shareholding requirement as at 31 March 2019. There have been no changes to shareholdings between 1 April 2019 and 15 May 2019.

		Share and option awards					
	Beneficially owned	Subject to performance	Subject to continued employment only	Vested but not yet exercised	Shareholding required (% of salary)	Current shareholding (% of salary)	Requirement met
Kris Hagerman	2,722,605	1,822,166	932,350	3,908,352	200	1,442	Yes
Nick Bray	381,138	791,080	410,617	–	200	391	Yes
Peter Gyenes	286,631	–	–	–			
Sandra Bergeron	214,974	–	–	–			
Roy Mackenzie	–	–	–	–			
Rick Medlock	–	–	–	–			
Vin Murria	50,000	–	–	–			
Paul Walker	190,695	–	–	–			

None of the Directors had an interest in the shares of any subsidiary undertaking of the Company or in any significant contracts of the Group, with the exception of Vin Murria who is also a Non-Executive Director of Softcat plc, with whom the Company maintains an ongoing customer relationship.

ANNUAL REPORT ON REMUNERATION CONTINUED

Summary of outstanding share awards

The interests of the Directors in the Company's share schemes as at 31 March 2019 are summarised in the table below.

Director	Date of award	Awards held at 1 Apr 18	Granted during the year	Exercised during the year	Forfeited during the year	Awards held at 31 Mar 19	Exercise price[1]	Market price at grant	Performance period	Vesting period/ date	Expiry date
Kris Hagerman											
Pre-IPO options	10 Oct 12	2,150,232	–	(250,000)	–	1,900,232	$ 0.598	$ 0.598	n/a	1 Aug 13 – 1 Aug 17	10 Oct 22
Pre-IPO options	10 Oct 12	2,258,120	–	(250,000)	–	2,008,120	$ 0.598	$ 0.598	exit event	1 Jul 15	10 Oct 22
LTIP – PSU	7 Aug 15	716,292	115,394	(831,686)	–	–	–	265p	1 Apr 15 – 31 Mar 18	7 Aug 18	6 Aug 25
LTIP – PSU	14 Jun 16	993,603	–	–	–	993,603	–	179p	1 Apr 16 – 31 Mar 19	14 Jun 19	13 Jun 26
LTIP – PSU	16 Jun 17	478,272	–	–	–	478,272	–	436p	1 Apr 17 – 31 Mar 20	16 Jun 20	15 Jun 27
LTIP – PSU	14 Jun 18	–	350,291	–	–	350,291	–	596p	1 Apr 18 – 31 Mar 21	14 Jun 21	13 Jun 28
LTIP – RSU	7 Aug 15	104,460	–	(74,614)	–	29,846	–	265p	n/a	7 Aug 16 – 7 Aug 19	6 Aug 25
LTIP – RSU	7 Aug 15	1,081,461	–	(491,573)	–	589,888	–	265p	n/a	7 Aug 16 – 7 Aug 20	6 Aug 25
LTIP – RSU	14 Jun 16	207,001	–	(103,500)	–	103,501	–	179p	n/a	14 Jun 17 – 14 Jun 20	13 Jun 26
LTIP – RSU	16 Jun 17	159,424	–	(69,748)	–	89,676	–	436p	n/a	16 Jun 18 – 16 Jun 21	15 Jun 27
LTIP – RSU	14 Jun 18	–	116,763	–	–	116,763	–	596p	n/a	14 Jun 19 – 14 Jun 22	13 Jun 28
ESPP	1 Jan 18	1,629	–	(1,629)	–	–	482p	567p	n/a	30 Jun 18	30 Jun 18
ESPP	2 Jul 18	–	1,498	(1,498)	–	–	311p	631p	n/a	31 Dec 18	31 Dec 18
ESPP	1 Jan 19	–	2,676	–	–	2,676	TBD	366p	n/a	30 Jun 19	30 Jun 19

1 Under Group scheme rules exercise price is to be not less than 85 per cent of the lesser of market value on date of grant and market value on date of exercise

Director	Date of award	Awards held at 1 Apr 18	Granted during the year	Exercised during the year	Forfeited during the year	Awards held at 31 Mar 19	Exercise price	Market price at grant	Performance period	Vesting period/ date	Expiry date
Nick Bray											
LTIP – PSU	7 Aug 15	337,079	54,303	(391,382)	–	–	–	265p	1 Apr 15 – 31 Mar 18	7 Aug 18	6 Aug 25
LTIP – PSU	14 Jun 16	447,744	–	–	–	447,744	–	179p	1 Apr 16 – 31 Mar 19	14 Jun 19	13 Jun 26
LTIP – PSU	16 Jun 17	194,985	–	–	–	194,985	–	436p	1 Apr 17 – 31 Mar 20	16 Jun 20	15 Jun 27
LTIP – PSU	14 Jun 18	–	148,351	–	–	148,351	–	596p	1 Apr 18 – 31 Mar 21	14 Jun 21	13 Jun 28
LTIP – RSU	7 Aug 15	463,484	–	(210,674)	–	252,810	–	265p	n/a	7 Aug 16 – 7 Aug 20	6 Aug 25
LTIP – RSU	7 Aug 15	49,158	–	(35,113)	–	14,045	–	265p	n/a	7 Aug 16 – 7 Aug 19	6 Aug 25
LTIP – RSU	14 Jun 16	93,280	–	(46,640)	–	46,640	–	179p	n/a	14 Jun 17 – 14 Jun 20	13 Jun 26
LTIP – RSU	16 Jun 17	64,995	–	(28,435)	–	36,560	–	436p	n/a	16 Jun 18 – 16 Jun 21	15 Jun 27
LTIP – RSU	14 Jun 18	–	49,451	–	–	49,451	–	596p	n/a	14 Jun 19 – 14 Jun 22	13 Jun 28
SAYE	24 Jun 16	11,111	–	–	–	11,111	162p	202p	n/a	8 Aug 19	8 Feb 20

As outlined in the IPO prospectus, Kris Hagerman continues to hold share options granted under the Pentagon Holdings Management Equity Plan ("MEP") that were issued prior to the IPO. Nick Bray's (until exercised under the JOE agreement in FY16) MEP options (a "Linked Option") were linked to a parallel award under a JOE Agreement. Awards under a JOE agreement entitle the participant to call for the transfer to him by the Trustee of the JOE agreement of that part of the beneficial interest in any jointly owned shares which vest, upon payment by the participant of a price specified in the JOE Agreement. Rights under a JOE Agreement may only be exercised to the extent that a Linked Option has not been exercised and vice versa.

The rules of the MEP provide that 50 per cent of a MEP option is subject to time vesting and 50 per cent is subject to performance vesting. On Admission, 66.2 per cent of the awards subject to performance vested. Depending on the length of service of a MEP participant, the Company may require that a portion of an option which is vested as to performance may only be exercised at a later date.

On behalf of the Board

Paul Walker

Chairman of the Remuneration Committee
15 May 2019

DIRECTORS' REPORT

The Directors of Sophos Group plc ("the Company") present their Annual Report on the affairs of the Group, together with the Consolidated Financial Statements and Auditor Report on the Group for the year-ended 31 March 2019.

There are a number of legal and regulatory requirements with which the Company must comply, such as the Companies Act 2006 ("the Act"), the Listing Rules and the Disclosure Guidance and Transparency Rules ("DTRs"), which are addressed in this section (together with the Corporate Governance Statement set out on pages 56 to 57, and committee reports on pages 68 to 101, that have been incorporated into this Directors' report by cross-reference).

Strategic report

The Strategic report, which also forms part of this report and is presented on pages 8 to 39 of this Annual Report, includes a fair review of the business, a description of the principal risks and uncertainties facing the Group and an indication of likely future developments.

A summary of general disclosures (incorporated in this Directors' Report)

The following information required to be disclosed in this Directors' report is set out on the pages listed below:

	Page Number
Likely future developments[1]	22 to 27
Policy on disability[1]	41
Employee engagement[1]	46
Greenhouse gas emissions[1]	50 and 51
Names of Directors who served during the year	54 and 55
Results	118 and 119
Details of employee share plans	85 and 86
Subsidiary and associated undertaking and branches	167 and 168
Financial risk management	36 to 39

1 Information required by the Large and Medium-sized Companies (Accounts and Reports) Regulations 2008 are included in the Strategic report

The majority of the disclosures required under LR 9.8.4 R are not applicable to the Group. The table below sets out the location of the disclosures for those requirements that are applicable:

Applicable sub-paragraph	Page number
Publication of unaudited financial information	28 to 35
Details of long-term incentive schemes	91 to 101
Allotment of equity securities	163 to 166
Contracts of significance	103
Agreements with controlling shareholders	103

Articles of Association and Constitution

Sophos Group plc is domiciled in England and incorporated in England and Wales under Company Number 09608658.

The Articles of Association of the Company ("the Articles") may only be amended by a special resolution at a meeting of the shareholders. The current Articles can be found on the Group's website at: investors.sophos.com.

Directors' interests

A summary of the Directors' remuneration, employment contracts and interests in the shares of the Company are set out in the Annual Report on Remuneration on pages 91 to 101.

None of the Directors had an interest in any significant contracts of the Group or its subsidiaries, except for Vin Murria who is also a Non-Executive Director of Softcat plc, with whom the Company maintains an ongoing customer relationship.

Directors' indemnity and insurance

Throughout the year, the Company has purchased and maintained Directors' and Officers' liability insurance in respect of itself and its Directors, and the Directors of Group subsidiary companies. The Directors also have the benefit of the indemnity provision contained in the Articles.

The Company has entered into qualifying third-party indemnity arrangements for the benefit of all its Directors in a form and scope which comply with the requirements of the Companies Act 2006 and which were in force throughout the year and remain in force.

Relationship Agreement

Pentagon Lock Sarl, Pentagon Lock 6-A Sarl, Pentagon Lock 7-A Sarl and Pentagon Lock US Sarl (collectively "Apax") previously held more than 30 per cent of the issued ordinary share capital of the Company and still hold more than 10 per cent of the issued ordinary share capital as at 31 March 2019. On 26 June 2015, the Company and Apax entered into a Relationship Agreement which regulates the ongoing relationship between the Company and Apax (as the "controlling shareholder") in accordance with the Listing Rules.

The Board can confirm that throughout the period:

- the Company has complied with the agreement's independence provisions;
- as far as the Company is aware, the controlling shareholder and its associates have complied with the agreement's independence provisions; and,
- as far as the Company is aware, the controlling shareholder has procured the compliance of non-signing controlling shareholders with the agreement's independence provisions.

Significant agreements

The following significant agreements are in place as at 31 March 2019, which include provisions that would enable the counterparties to alter or terminate the agreements upon a change of control of the Company following a takeover bid:

- a syndicated secured term loan ("Facility A") of $235.0 million entered into on 1 July 2015;
- a syndicated secured term loan ("Facility B") of €60.0 million entered into on 1 July 2015;
- a revolving credit facility agreement ("RCF 1") of $30.0 million entered into on 1 July 2015; and,
- a revolving credit facility agreement ("RCF 2") of $40.0 million entered into on 6 February 2017.

Further details of financing agreements in place are included in note 24 of the Financial Statements.

Share capital and substantial shareholders

The share capital of the Company is set out in note 27 of the Financial Statements; ordinary shares of three pence each are the only class of share in issue. As at 31 March 2019 and 15 May 2019 the Company was notified under DTR 5 of the following significant holdings of voting rights in its shares set out in the table below. No change in voting interests in the ordinary share capital of the Company, disclosable under the DTRs, has been notified to the Company between 31 March 2019 and 15 May 2019.

	As at 31 March 2019	
Name	**Ordinary shares held**	**Percentage of total ordinary shares**
Apax	51,936,344	10.77
Jan Hruska	42,543,360	8.82
Peter Lammer	42,543,360	8.82
Franklin Templeton Institutional, LLC	23,376,977	4.85
Standard Life Investments (Holdings) Limited	22,724,690	4.71
Old Mutual plc	19,821,783	4.11
ODDO Meriten Asset Management	12,954,464	2.68

DIRECTORS' REPORT CONTINUED

Analysis of shares held as at 31 March 2019

Number of shares held	Number of shareholders	% of shareholders	Holding	% of total capital
100	33	3.2738	2,073	0.0004
200	35	3.4722	5,711	0.0012
500	72	7.1429	27,712	0.0058
1,000	113	11.2103	91,971	0.0191
2,000	93	9.2262	139,736	0.0290
5,000	147	14.5833	489,421	0.1016
10,000	79	7.8373	559,048	0.1160
50,000	156	15.4762	3,769,323	0.7822
100,000	72	7.1429	5,130,687	1.0647
500,000	105	10.4167	24,830,528	5.1530
1,000,000	34	3.3730	25,790,422	5.3522
5,000,000	49	4.8611	115,139,589	23.8943
10,000,000	9	0.8929	56,243,352	11.6719
50,000,000	10	0.9921	162,964,556	33.8192
99,999,999,999	1	0.0992	86,685,577	17.9895
Total	1,008		481,869,706	

Voting rights

All of the issued and outstanding ordinary shares of the Company have equal voting rights, with one vote per share. There are no special control rights attaching to them.

Transfer of shares

The transfer of shares is governed by the Articles which allows any member to transfer certificated shares in any usual form or in any other form for which the Board may approve. The Board may, in its absolute discretion, refuse to register a transfer of a certificated share that is not fully paid, provided that the refusal does not prevent dealings in the Company from taking place on an open and proper basis. The Board may also refuse to register the transfer of a certificated share unless the instrument of transfer is (i) lodged, duly stamped (if stampable), at the office or at another place appointed by the Board, accompanied by the certificate for the shares to which it relates and such other evidence as the Board may reasonably require to show the right of the transferor to make the transfer; (ii) in respect of only one class of shares; and (iii) in favour of not more than four transferees.

Appointment and retirement of Directors

Unless otherwise determined by ordinary resolution, the number of Directors shall be no less than three but is not subject to any maximum number. The Board may appoint a person who is willing to act to be a Director, either to fill a vacancy or as an additional Director and in either case whether or not for a fixed term.

At every Annual General Meeting ("AGM") all the Directors at the date of the notice convening the AGM shall retire from office. If the Company does not fill the vacancy at the meeting the retiring Director shall, if willing to act, be deemed to have been re-appointed unless at the meeting it is resolved not to fill the vacancy or unless a resolution for the reappointment of the Director is put to the meeting and lost.

A person ceases to be a Director as soon as:

(i) notification is received by the Company from the Director that they are resigning or retiring from office;

(ii) that person has been absent for more than six consecutive months without permission of the Board and the Board resolves that their office be vacated;

(iii) the person has become physically or mentally incapable of acting as a Director and may remain so for more than three months;

(iv) a bankruptcy order is made against that person;

(v) a composition is made with that person's creditors generally in satisfaction of that person's debts;

(vi) that person ceases to be a Director by virtue of any provision of the Act or is prohibited from being a Director by law; or,

(vii) that person is removed from office pursuant to the Articles.

Powers of the Directors

Subject to provisions of the Companies Act 2006, the Articles, and to any directions given by special resolution, the business of the Company shall be managed by the Directors who may exercise all the powers of the Company.

Dividends

The Directors have declared dividends as noted below and continue to adopt a progressive dividend policy targeting approximately mid-single digit per cent growth per annum, reflecting the cash-generative nature of the Group.

Ordinary shares

Interim Dividend of 1.5 US cents per share paid 14 December 2018 (2018: 1.4 US cents per share).

Proposed Final Dividend of 3.7 US cents per share to be paid on 11 October 2019 (2018: 3.5 US cents per share).

Total dividend of 5.2 US cents per share for 2019 (2018: 4.9 US cents per share).

Sophos Group plc is the parent Company of the Group and is a non-trading investment company for the Group, holding investments in subsidiaries financed by Group companies. Sophos Group plc has retained earnings of $919.4 million, which approximates the distributable reserves. At the end of the prior-year Sophos Group plc had retained earnings of $946.1 million, after paying dividends in that year totalling $21.8 million, the distributable reserves thereby having significant cover for the dividends being proposed. The Group is strongly cash generative with trading activities continuing to support the dividends made and proposed, details of cash on hand is included in note 33 of the Financial Statements.

The dividend policy and availability of distributable reserves or cash to make future dividend payments is influenced by the principal risks, and their mitigations, discussed on pages 36 to 39 which are factored into the Group's viability review and statement disclosed on page 101. Prior to the proposal of a dividend the Directors review both the distributable reserves and cash available on hand as well as the impact of the proposed dividend on each of them in light of other cash commitments and investment intentions. On the basis of the latest review the Directors consider the current dividend policy to be appropriate and sustainable.

Annual General Meeting

The notice of the AGM which sets out the resolutions to be proposed at the 2019 AGM accompanies this Annual Report and Accounts. The 2019 AGM will be held at 3.00pm on 25 September 2019 at: The Pentagon, Abingdon Science Park, Abingdon, OX14 3YP.

Research and development

The Group continues to undertake research and development activity relating to its principal activities.

In the year-ended 31 March 2019, the Group spent 18.9 per cent of its billings on research and development (FY18: 18.3 per cent). Development expenditure is capitalised if the requirements of IAS 38 have been met, further details are included in note 4.10 of the Financial Statements.

Political donations

The Group's policy is not to make any political donations. Accordingly, no political donations were made in the year-ended 31 March 2019 (FY18: no political donations were made).

Authority to issue shares and authority to purchase own shares

The Company was authorised by shareholders at the 2018 AGM to allot shares and also to make market purchases of up to 10 per cent of the Company's issued share capital, as permitted under the Company's Articles. The Company did not repurchase shares during the year or make any shares the subject of a charge. The Company will seek to renew these authorities at the 2019 AGM, within the limits set out in the AGM Notice.

Shares held in the Employee Benefit Trust

The Trustees of the Employee Benefit Trust will abstain from voting or exercising any other rights in respect of any shares held by them and in which no beneficial interest is held by any beneficiary unless otherwise directed by the Company.

Statement of compliance with the Competition and Markets Authority ("CMA") order

With the exception of the audit tender process referred to on page 76, the Company confirms that it has complied with The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Processes and Audit Committee Responsibilities) Order 2014 (Article 7.1), published by the CMA on 26 September 2014.

DIRECTORS' REPORT CONTINUED

Going concern

Having made appropriate enquiries and considered the Group's forecasts, the Directors consider that the Group has sufficient resources to continue for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Financial Statements.

Further details regarding the adoption of the going concern basis can be found in the viability statement below.

Viability statement

The Directors have assessed the viability of the Group over a three-year period, taking into account the Group's current position and the potential impacts of the principal risks documented on pages 36 to 39 of the Annual Report. Based on this assessment, the Directors confirm that they have a reasonable expectation that the Company will be able to continue to operate and to meet its liabilities as they fall due over the three years to 31 March 2022.

The Group prepares annually, and on a rolling basis, a strategic plan, which is predicated on a detailed year one budget and higher-level forecasts thereafter. The output of this plan is used to perform debt and associated covenant headroom profile analysis, which includes sensitivity to business as usual risks such as billings and EBITDA impacts. A bottom-up operating plan is prepared on an annual basis for presentation to the Board.

Following assessment of the planning process, the Directors have determined that a three-year period is an appropriate period over which to assess the Group's viability. Whilst the Directors have no reason to believe that the Group will not be viable over a longer period; the period of three years has been chosen as this matches the term of the majority of the Group's sales (typically one to three years in duration, with a weighted average contract life of around 26 months) which therefore aids the accuracy of forecasting with a single renewal cycle, thereby providing a greater degree of certainty and, in the view of the Directors, still provides an appropriate long-term outlook.

In making this viability statement, the Board 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. Where individual principal risks did not impact the future viability of the Group, consideration was given to potential principal risk combinations. The process of identifying, assessing and managing principal risks is set out in the Audit and Risk Committee report on pages 71 to 76.

Post balance sheet events

There have been no material events from 31 March 2019 to the date of this report.

Auditor

KPMG LLP has expressed their willingness to continue in office as auditor of the Company and accordingly a resolution for the re-appointment of KPMG LLP as auditor of the Company is to be proposed to the shareholders at the 2019 AGM.

Disclosure of information to Auditor

The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware and each Director has taken all the steps that he or she ought to have taken as a Director to make them aware of any relevant audit information.

Statement of Directors' responsibilities in respect of the Annual Report and the Financial Statements

The Directors are responsible for preparing the Annual Report and the Group and parent Company Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent Company Financial Statements for each financial year. Under that law they are required to prepare the Group Financial Statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and applicable law. As explained in note 4 to the Group Financial Statements, the Group, in addition to complying with its legal obligation to apply IFRSs as adopted by the EU, has also applied IFRSs as issued by the International Accounting Standards Board ("IASB"). Under company law the Directors have elected to prepare the parent Company Financial Statements in accordance with UK accounting standards, including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

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 of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and parent Company Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant, reliable and prudent;
- for the Group Financial Statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent Company Financial Statements, state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the parent Company Financial Statements;
- assess the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and,
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its Financial Statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of Financial Statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic report, Directors' report, Directors' Remuneration report and Corporate Governance Statement that complies with that law and those regulations.

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

Responsibility statement of the Directors in respect of the Annual Financial Report

We confirm that to the best of our 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 Strategic report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

We consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

By order of the Board

Eleanor Lacey

Company Secretary

15 May 2019

Sophos Mobile – secure unified endpoint management

"Imagine an attack that starts with a phishing email that you are just as likely to open on your mobile device, and tap the link with your finger, as you are to click it with a mouse on your laptop. Yet, it is estimated that more than half of businesses have no mobile security in place[1]"

As we move towards 'zero trust' networking, enhanced conditional access is crucial. With remote working on the increase and the knock-on effect that has on corporate data access across a variety of mobile devices, there is a growing requirement to enable user productivity without compromising data security.

Sophos Mobile is a secure Unified Endpoint Management ("UEM") solution that helps businesses spend less time and effort to manage and secure traditional and mobile endpoints. The only UEM solution that integrates natively with a leading next-gen endpoint security platform, Sophos Mobile supports management of Windows 10, macOS, iOS, and Android devices. This is all managed via the Group's single, integrated cloud management console – Sophos Central.

With a rich set of device management capabilities, containers, and market-leading encryption, Sophos helps customers keep sensitive business email and documents protected on mobile devices, even for users working with personal devices. The Group's leading antivirus and ransomware protection safeguards users and devices from malicious content and apps. Sophos Mobile includes phishing URL scanning as standard in addition to all the other great protections like deep learning based malware detection.

1 Verizon Mobile Security Index 2019

Find out more at:
www.sophos.com/mobile

Financial Statements

Independent Auditor's Report

to the members of Sophos Group plc only

1. Our opinion is unmodified

We have audited the Financial Statements of Sophos Group plc ("the Company") for the year ended 31 March 2019 which comprise the Consolidated Statements of Profit and Loss, Comprehensive Income, Financial Position, Changes in Equity, and Cash Flows, and the Company Only Statements of Financial Position and Changes in Equity and the related notes, including the accounting policies in note 4.

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 March 2019 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 as adopted by the European Union (IFRSs as adopted by the EU);
- the parent Company Financial Statements have been properly prepared in accordance with UK accounting standards, 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.

Additional opinion in relation to IFRSs as issued by the IASB

As explained in note 4 to the Consolidated Financial Statements, the Group, in addition to complying with its legal obligation to apply IFRSs as adopted by the EU, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion, the Consolidated Financial Statements have been properly prepared in accordance with IFRSs as issued by the IASB.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the Audit Committee.

We were first appointed as auditor by the Directors on 25 January 2001. We were then subsequently appointed as auditors of the listed Group for EU PIE purposes. The period of total uninterrupted engagement is for the 19 financial years ended 31 March 2019. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

Overview	
Materiality: group financial statements as a whole	$6.8m (2018: $6.3m) 1% (2018: 1%) of Group revenue
Coverage	98% (2018: 99%) of Group revenue

Key audit matters		**vs 2018**
Recurring	Revenue recognition	◀▶
	Recoverability of parent Company's investment in subsidiaries	◀▶
New	Going Concern	▲

2. Key audit matters: including our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the Financial Statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the Financial Statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
Revenue recognition ($710.6 million; 2018 (restated: $639.0 million) Refer to page 73 (Audit Committee Report), page 129 (accounting policy) and page 143 (financial disclosures).	**Accounting treatment:** As the Group expands and product portfolios evolve, there is considerable risk associated with recognising revenue on contracts containing multiple promised goods or services. Judgement is required in determining each performance obligation of the arrangement and estimating their respective stand-alone selling prices. The Group makes reference to the list prices of separate performance obligations and discounts given on the total contract. This judgement around allocation of discounts to separate performance obligations could materially affect the timing and quantum of revenue recognised in each period. Consequently, this is considered to be an area that had the greatest effect on the Group audit.	**Our procedures included:** ▪ **Controls design:** We evaluated the design and implementation of the control ensuring review and approval of non standard contract terms which may impact revenue recognition; ▪ **Control operation:** We evaluated the operating effectiveness of IT controls over the establishment of list prices in the sales order system which directly impact determination of stand-alone selling prices; ▪ **Tests of details:** We selected a sample of Group billings from throughout the year and with reference to list prices and discounts given, we recalculated the stand-alone selling prices to assess whether the determination of stand-alone selling price of each separate performance obligation was in line with Group Policy. We also inspected a sample of contracts in the year, assessing the impact of contract terms on revenue recognition; ▪ **Accounting analysis:** We assessed the Group's policy in respect of transaction price allocation to separate performance obligations and revenue recognition against the relevant accounting standards; and ▪ **Assessing transparency:** We assessed the adequacy of the Group's disclosure regarding the identification of separate performance obligations and determination of stand-alone selling prices. **Our results** ▪ We found the amount of revenue recognised in the year as at 31 March 2019 to be acceptable (2018: acceptable).

INDEPENDENT AUDITOR'S REPORT CONTINUED

to the members of Sophos Group plc only

2. Key audit matters: including our assessment of risks of material misstatement continued

	The risk	Our response
Going Concern Refer to page 106 (Directors' Report), page 126 (accounting policy) and page 158 (financial disclosures).	**Disclosure quality** The Financial Statements explain how the Board has formed a judgement that it is appropriate to adopt the going concern basis of preparation for the group and parent Company. That judgement is based on an evaluation of the inherent risks to the Group's and Company's business model and how those risks might affect the Group's and Company's financial resources or ability to continue operations over a period of at least a year from the date of approval of the Financial Statements. The risk identified as most likely to adversely affect the Group's and Company's available financial resources over this period was the ongoing refinancing negotiations. The risk for our audit was whether or not those risks were such that they amounted to a material uncertainty that may have cast significant doubt about the ability to continue as a going concern. Had they been such, then that fact would have been required to have been disclosed.	**Our procedures included:** **Funding assessment:** ▪ For existing lenders that are due to provide refinancing under a new facility, we requested confirmations as to their attitude to participate. ▪ We assessed the current facility covenant requirements and the adherence to these as at the balance sheet date. **Historical comparisons:** ▪ We assessed the historical accuracy of the Group's forecasts, as well as challenging the forecasting process in place. **Sensitivity analysis:** ▪ We considered sensitivities over the level of available financial resources indicated by the Group's financial forecasts taking account of reasonably possible (but not unrealistic) adverse effects that could arise from these risks individually and collectively; **Benchmarking assumptions:** ▪ We compared the Group's assumptions to externally derived data in relation to key inputs such as growth rates; **Assessing transparency:** ▪ We assessed the adequacy of the Group's disclosure regarding the determination of the going concern assessment with reference to the dependence of the cash flow forecast on refinancing activities. **Our results:** We found the disclosure of going concern without any material uncertainty to be acceptable (2018 result: acceptable).

	The risk	Our response
Recoverability of parent company's investment in subsidiaries ($1,130.6 million; 2018: $1,099.1 million) Refer to page 73 (Audit Committee Report), page 176 (accounting policy) and page 177 (financial disclosures).	**Forecast based valuation:** The carrying amount of the parent Company's investments in subsidiaries is significantly in excess of the net assets of the Group as a whole, and is assessed for recoverability using a discounted cash flow model to calculate value in use ("VIU"). Due to the inherent uncertainty involved in forecasting and discounting future cash flows for a VIU model, this is one of the key judgemental areas that our audit concentrates on.	**Our procedures included:** **Our sector experience:** we challenged the assumptions used in the cash flows included in the discounted cash flow model by using our sector experience through evaluating the current level of trading, including identifying any indications of a downturn in activity, by examining the post year end management accounts and considering our knowledge of the Group and the market; **Benchmarking assumptions:** we assessed the reasonableness of key external inputs, such as projected long term economic growth and discount rates, by benchmarking these against those used by comparable listed companies; **Historical comparison:** we assessed the reasonableness of the budgets by considering the historical accuracy of the previous forecasts; and **Comparing valuations:** we compared the sum of the discounted cash flows to the Group's market capitalisation to assess the reasonableness of those cash flows. **Our results** We found the carrying amount of the parent Company's investment in subsidiaries to be acceptable (2018: acceptable).

We continue to perform procedures over the appropriateness of the presentation of exceptional expenses and alternative performance measures. Following updates to the presentation of exceptional expenses, alternative performance measures and related disclosures, we have not assessed this as one of the most significant risks in our current year audit and, therefore, it is not separately identified in our report this year.

INDEPENDENT AUDITOR'S REPORT CONTINUED

to the members of Sophos Group plc only

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

Materiality for the Group Financial Statements as a whole was set at \$6.8m (2018: \$6.3m), determined with reference to a benchmark of Group revenue of which it represents 1% (2018: 1%). We consider Group revenue to be the most appropriate benchmark as it provides a more stable measure year on year than Group profit before tax.

Materiality for the parent Company Financial Statements as a whole was set at \$6.6m (2018: \$5.9m), determined with reference to a benchmark of total assets, of which it represents 0.6% (2018: 0.6%).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding \$340k, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Of the Group's 27 (2018: 27) reporting components, we subjected 4 (2018: 7) to full scope audits for Group purposes and 2 (2018: 2) to specified risk-focused audit procedures. The latter were not individually financially significant enough to require a full scope audit for group purposes, but did present specific individual risks that needed to be addressed.

The components within the scope of our work accounted for the percentages illustrated opposite.

The remaining 2% of total Group revenue, 10% of Group profit before tax and 17% of total Group assets is represented by 21 reporting components, none of which individually represented more than 2% of any of total Group revenue, Group profit before tax or total Group assets. For these residual components, we performed analysis at an aggregated Group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The Group team instructed component auditors as to the significant areas to be covered, including the relevant risks detailed above and the information to be reported back. The Group team approved the component materialities, which ranged from \$2m to \$5.1m, having regard to the mix of size and risk profile of the Group across the components. The work on one of the four components (2018: five of the seven components) was performed by component auditors and the rest, including the audit of the parent Company, was performed by the Group team.

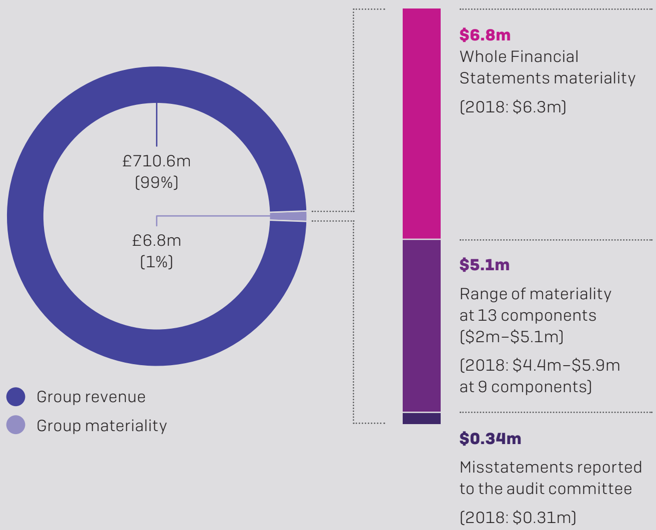
The Group team visited 1 (2018: 2) component location in Germany (2018: Germany and India) to assess the audit risk and strategy. Video and telephone conference meetings were also held with these component auditors and the majority of the others that were not physically visited. At these visits and meetings, the findings reported to the Group team were discussed in more detail, and any further work required by the Group team was then performed by the component auditor.

Group Revenue

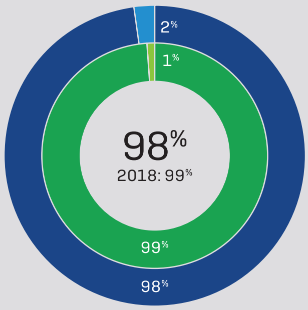
\$710.6m (2018: \$639.0m)

Group Materiality

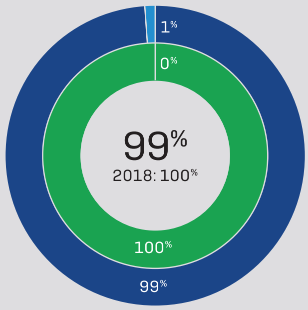
\$6.8m (2018: \$6.3m)



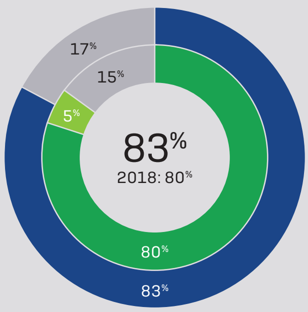
Group Revenue



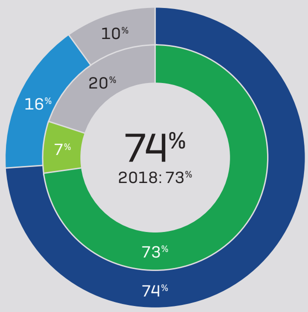
Group Billings



Group Total Assets



Group Profit Before Tax



- Full scope for Group audit purposes 2019
- Specified risk-focused audit procedures 2019
- Full scope for Group audit purposes 2018
- Specified risk-focused audit procedures 2018
- Residual components

4. We have nothing to report on going concern

The Directors have prepared the Financial Statements on the going concern basis as they do not intend to liquidate the Company or the Group or to cease their operations, and as they have concluded that the Company's and the Group's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over their ability to continue as a going concern for at least a year from the date of approval of the Financial Statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the Group and the Company will continue in operation.

We identified going concern as a key audit matter (see section 2 of this report). Based on the work described in our response to that key audit matter, we are required to report to you if:

- we have anything material to add or draw attention to in relation to the directors' statement in Note 4.2 to the Financial Statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the Group and Company's use of that basis for a period of at least twelve months from the date of approval of the Financial Statements; or
- the related statement under the Listing Rules set out on page 106 is materially inconsistent with our audit knowledge.

We have nothing to report in these respects.

5. We have nothing to report on the other information in the Annual Report

The Directors are responsible for the other information presented in the Annual Report together with the Financial Statements. Our opinion on the Financial Statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our Financial Statements audit work, the information therein is materially misstated or inconsistent with the Financial Statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

Strategic report and Directors' Report

Based solely on our work on the other information:

- we have not identified material misstatements in the strategic report and the Directors' Report;
- in our opinion the information given in those reports for the financial year is consistent with the Financial Statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Directors' Remuneration Report

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

Disclosures of principal risks and longer-term viability

Based on the knowledge we acquired during our Financial Statements audit, we have nothing material to add or draw attention to in relation to:

- the Directors' confirmation within the Directors' Viability Statement (page 106) 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 and liquidity;
- the Principal Risks disclosures describing these risks and explaining how they are being managed and mitigated; and
- the Directors' explanation in the Directors' Viability Statement of how they have assessed the prospects of the Group, over what period they have done so and why they considered 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.

INDEPENDENT AUDITOR'S REPORT CONTINUED

to the members of Sophos Group plc only

5. We have nothing to report on the other information in the Annual Report continued

Under the Listing Rules we are required to review the Directors' Viability Statement. We have nothing to report in this respect.

Our work is limited to assessing these matters in the context of only the knowledge acquired during our Financial Statements audit. As we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of anything to report on these statements is not a guarantee as to the Group's and Company's longer-term viability.

Corporate governance disclosures

We are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our Financial Statements audit and the Directors' statement that they consider that the Annual Report and Accounts taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; or
- the section of the Annual Report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We are required to report to you if the Corporate Governance Statement does not properly disclose a departure from the eleven provisions of the UK Corporate Governance Code specified by the Listing Rules for our review.

We have nothing to report in these respects.

6. We have nothing to report on the other 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.

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 107, the Directors are responsible for: the preparation of the Financial Statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of Financial Statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the Financial Statements as a whole are free from material misstatement, whether due to fraud or other irregularities (see below), or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud, other irregularities or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the Financial Statements from our sector experience, through discussion with the Directors (as required by auditing standards), from inspection of the Group's regulatory and legal correspondence and discussed with the Directors the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. This included communication from the Group to component audit teams of relevant laws and regulations identified at Group level.

The potential effect of these laws and regulations on the Financial Statements varies considerably.

7. Respective responsibilities continued

Firstly, the Group is subject to laws and regulations that directly affect the Financial Statements including financial reporting legislation (including related companies legislation), distributable profits legislation and taxation legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Group is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the Financial Statements, for instance through the imposition of fines, litigation or the loss of the Group's licence to operate. We identified the following areas as those most likely to have such an effect: intellectual property, health and safety, anti-bribery, employment law, and certain aspects of company legislation recognising the nature of the Group's activities. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the Directors and other management and inspection of regulatory and legal correspondence, if any. Through these procedures, we became aware of actual non-compliance and considered the effect as part of our procedures on the related financial statement items. The identified actual or suspected non-compliance was not sufficiently significant to our audit to result in our response being identified as a key audit matter.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the Financial Statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the Financial Statements, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8. The purpose of our audit work and to whom we owe our responsibilities

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.

Robert Seale (Senior Statutory Auditor)

for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

15 May 2019

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

For the year-ended 31 March 2019

	Note	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Revenue	7	710.6	639.0
Cost of sales		(146.4)	(144.0)
Gross profit		564.2	495.0
Sales and marketing		(259.9)	(239.9)
Research and development		(143.9)	(140.3)
General finance and administration:		(99.5)	(134.5)
– Underlying		(51.0)	(46.9)
– Share-based payments		(36.9)	(42.3)
– Exceptional items	8	3.8	(13.2)
– Amortisation of intangible assets		(16.9)	(25.2)
– Foreign exchange gain / (loss)		1.5	(6.9)
Operating profit / (loss)		60.9	(19.7)
Finance income	13	0.9	0.3
Finance expense	13	(8.2)	(21.6)
Profit / (loss) before taxation		53.6	(41.0)
Income tax charge	14	(26.7)	(19.9)
Profit / (loss) for the year		26.9	(60.9)
Earnings per share ($ cents)			
Basic and diluted EPS	15	5.6	(13.2)
Diluted EPS	15	5.4	n/a
Adjusted operating EPS	15	14.4	3.6
Diluted adjusted operating EPS	15	13.9	3.4

All of the loss for the year is attributable to equity holders of the parent Company.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year-ended 31 March 2019

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Profit / (loss) for the year	26.9	(60.9)
Other comprehensive losses :		
Items that will not be reclassified subsequently to profit or loss:	–	–
Items that may be reclassified subsequently to profit or loss:		
– Exchange differences arising on translation of foreign operations[1]	(33.7)	(2.6)
Total other comprehensive losses	(33.7)	(2.6)
Comprehensive loss for the year	(6.8)	(63.5)

1 Exchange difference arising on translation of foreign operations for the year-ended 31 March 2019 of $33.7M include a loss of $39.5M in respect of a re-denomination of goodwill as set out in note 16

All of the comprehensive loss for the year is attributable to equity holders of the parent Company.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 March 2019

Company registered number: 09608658	Note	31 March 2019 $M	31 March 2018 Restated See note 2 $M	31 March 2017 Restated See note 2 $M
Non-current assets				
Intangible assets	16	837.0	869.9	856.0
Property, plant and equipment	18	23.9	25.4	23.4
Deferred tax asset	14	115.0	120.7	100.1
Other receivables	20	16.4	17.5	28.8
		992.3	1,033.5	1,008.3
Current assets				
Tax assets		5.6	3.7	3.9
Inventories	19	10.6	16.0	16.2
Trade and other receivables	20	195.3	210.8	157.8
Cash and cash equivalents	21	172.1	120.0	68.1
		383.6	350.5	246.0
Total assets		1,375.9	1,384.0	1,254.3
Current liabilities				
Trade and other payables	22	102.2	134.1	107.3
Deferred revenue	23	428.6	407.9	315.0
Tax liabilities		36.3	21.1	20.0
Financial liabilities	24	4.5	17.4	71.1
Provisions	25	0.1	–	0.4
		571.7	580.5	513.8
Non-current liabilities				
Trade and other payables	22	10.1	8.2	3.9
Deferred revenue	23	313.5	320.7	238.8
Financial liabilities	24	302.8	306.8	296.3
Provisions	25	7.5	3.3	2.1
Deferred tax liabilities	14	14.6	14.5	21.3
		648.5	653.5	562.4
Total liabilities		1,220.2	1,234.0	1,076.2
Net assets		155.7	150.0	178.1
Represented by:				
Share capital	27	22.5	22.0	21.6
Share premium		126.6	122.3	118.4
Merger reserve		(200.9)	(200.9)	(200.9)
Retained earnings		119.8	116.8	199.5
Share-based payment reserve		153.4	121.8	68.9
Translation reserve		(65.7)	(32.0)	(29.4)
Total equity		155.7	150.0	178.1

These Consolidated Financial Statements were approved by the Board of Directors on 15 May 2019 and were signed on its behalf by:

Nick Bray

Chief Financial Officer

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year-ended 31 March 2019

	Share Capital $M	Share Premium $M	Merger Reserve $M	Retained Earnings $M	Share-Based Payment Reserve $M	Translation Reserve $M	Total $M
As previously reported	21.6	118.4	(200.9)	148.1	68.9	(29.4)	126.7
Adjustments (see note 2)				51.4			
At 31 March 2017 restated	21.6	118.4	(200.9)	199.5	68.9	(29.4)	178.1
Loss for the period:	–	–	–	(60.9)	–	–	(60.9)
Other comprehensive loss	–	–	–	–	–	(2.6)	(2.6)
Total comprehensive loss	–	–	–	(60.9)	–	(2.6)	(63.5)
Share options exercised	0.4	3.9	–	–	–	–	4.3
Share-based payments expense	–	–	–	–	39.6	–	39.6
Share-based payments deferred tax	–	–	–	–	13.3	–	13.3
Cash dividends (see note 28)	–	–	–	(21.8)	–	–	(21.8)
At 31 March 2018	22.0	122.3	(200.9)	116.8	121.8	(32.0)	150.0
Profit for the period:	–	–	–	26.9	–	–	26.9
Other comprehensive loss	–	–	–	–	–	(33.7)	(33.7)
Total comprehensive loss	–	–	–	26.9	–	(33.7)	(6.8)
Share options exercised	0.5	4.3	–	–	–	–	4.8
Share-based payments expense	–	–	–	–	35.0	–	35.0
Share-based payments taxation	–	–	–	–	(3.4)	–	(3.4)
Cash dividends (see note 28)	–	–	–	(23.9)	–	–	(23.9)
At 31 March 2019	22.5	126.6	(200.9)	119.8	153.4	(65.7)	155.7

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year-ended 31 March 2019

	Note	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Profit / (loss) for the year		26.9	(60.9)
Adjusted for:			
Depreciation		11.8	11.6
Amortisation of intangible assets		16.9	25.2
Amortisation of fair value adjustment on deferred income		(0.1)	1.0
Fair value adjustment on contingent consideration		(6.9)	0.2
Foreign exchange expense		(1.5)	8.1
Share-based payments expense	29	35.0	39.6
Finance income	13	(0.9)	(0.3)
Finance expense	13	8.2	21.6
Profit on disposal of assets		(0.2)	–
Income tax charge		26.7	19.9
		115.9	66.0
Decrease in inventories		4.7	1.7
Decrease / (increase) in trade and other receivables		8.3	(32.6)
(Decrease) / increase in trade and other payables		(20.1)	10.4
Increase in deferred revenue	23	49.9	128.7
Increase / (decrease) in provisions		0.9	(0.2)
Cash generated from continuing operations		159.6	174.0
Income taxes paid		(16.7)	(26.3)
Net cash flow from operating activities		142.9	147.7
Investing activities			
Purchase of property, plant and equipment	18	(12.8)	(10.0)
Acquisition of subsidiaries net of cash acquired	33	(30.9)	(4.9)
Purchase of intangible assets - software	16	(9.7)	(11.1)
Proceeds on sale of assets		0.3	–
Finance income	13	0.9	0.3
Net cash flow from investing activities		(52.2)	(25.7)
Financing activities			
Proceeds from issue of shares		4.8	4.2
Dividends paid		(23.9)	(21.8)
Repayment of borrowings	33	–	(50.0)
Transaction costs related to borrowings	33	–	(0.1)
Finance lease payments		–	(0.1)
Finance costs		(10.9)	(9.1)
Net cash flow from financing activities		(30.0)	(76.9)
Increase in cash and cash equivalents		60.7	45.1
Net foreign exchange differences		(8.6)	6.8
Cash and cash equivalents at the start of the period		120.0	68.1
Cash and cash equivalents at the end of the period	21	172.1	120.0

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year-ended 31 March 2019

1 General information

Reporting entity

Sophos Group plc ("the Company") is a company domiciled in the United Kingdom. The Company's registered office is Sophos Group plc, The Pentagon, Abingdon Science Park, Abingdon, Oxfordshire, OX14 3YP, United Kingdom. The Consolidated Financial Statements of the Company as at and for the year-ended 31 March 2019 comprise the Company and its subsidiaries (together referred to as "the Group"). The Group is a leading provider of cloud-enabled enduser and network security solutions.

2 Changes in accounting policies

Adoption of IFRS 15

The Group has adopted IFRS 15 Revenue from Contracts with Customers ("IFRS 15") in the year-ended 31 March 2019 and in doing so has applied the retrospective transition approach without applying any of the practical expedients included in the standard. Consequently, the year-ended 31 March 2018 comparative information has been restated on the same basis.

The adoption of IFRS 15 principally impacted the Group in three ways:

- the earlier recognition of revenue on certain termed licence software products; where they are adjudged to have a distinct performance obligation element that transfers the benefit of ownership at the point of sale rather than over the life of the licence;
- the recognition of rebates in line with the recognition of revenue over the term of the licences sold, which were previously recognised at the point of sale; and,
- the deferral of commissions and other incremental costs incurred to obtain a contract with a customer in line with the recognition of revenue, which were also previously recognised at the point of sale, and expensed as incurred.

Re-allocation of Certain Components of the Income Tax Charge

The research and development expenditure tax credit scheme ("RDEC") is one which enables UK companies to reclaim a certain percentage of its research and development expenditure via the tax authorities.

Separately, where the Group has an uncertain tax position ("UTP") it may make a provision for any interest payable on final resolution of the open tax computation.

In accordance with best practice, the Group has reconsidered its accounting in respect of these two separate items and no longer recognises them as an integral part of the income tax charge. Consequently, the year-ended 31 March 2018 comparative information has been restated to present it on a consistent basis.

The change in accounting principally impacted the Group as follows:

- Expenditure on research and development now includes the RDEC credit;
- The finance expense now reflects the provision for interest on uncertain tax positions; and,
- The income tax charge no longer includes either of the above items.

The following tables summarises the impact of these changes for each line item of the Group's consolidated statement of profit or loss and the consolidated statement of financial position for the year-ended 31 March 2018 comparative information. There was no material impact on the Group's consolidated statement of cash flows.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

2 Changes in Accounting Policies continued

Consolidated statement of profit or loss for the year-ended 31 March 2018

	As previously reported $M	IFRS 15 Adjustment $M	RDEC / Interest on UTP $M	Restated $M
Revenue	640.7	(1.7)	–	639.0
Cost of sales	(143.3)	(0.7)	–	(144.0)
Gross profit	497.4	(2.4)	–	495.0
Sales and marketing	(249.0)	9.1	–	(239.9)
Research and development	(145.8)	–	5.5	(140.3)
General finance and administration:	(134.5)	–	–	(134.5)
Operating loss	(31.9)	6.7	5.5	(19.7)
Finance income	0.3	–	–	0.3
Finance expense	(20.7)	–	(0.9)	(21.6)
Loss before taxation	(52.3)	6.7	4.6	(41.0)
Income tax charge	(14.0)	(1.3)	(4.6)	(19.9)
Loss for the period	(66.3)	5.4	–	(60.9)
Earnings per share (US cents)				
Basic and diluted EPS	(14.4)	1.2	–	(13.2)
Adjusted operating EPS	10.0	1.5	1.2	12.7
Diluted Adjusted operating EPS	9.5	1.3	1.1	11.9

Consolidated statement of financial position as at 31 March 2018

	As previously reported $M	IFRS 15 Adjustment $M	RDEC / Interest on UTP $M	Restated $M
Non-current assets				
Deferred tax asset	125.8	(5.1)	–	120.7
Other non-current assets	896.6	16.2	–	912.8
	1,022.4	11.1	–	1,033.5
Current assets				
Tax assets	8.2	–	(4.5)	3.7
Trade and other receivables	177.8	28.5	4.5	210.8
Other current assets	136.0	–	–	136.0
	322.0	28.5	–	350.5
Current liabilities				
Deferred revenue	423.9	(16.0)	–	407.9
Income tax payable	23.0	–	(1.9)	21.1
Other current liabilities	151.5	–	–	151.5
	598.4	(16.0)	(1.9)	580.5
Non-current liabilities				
Deferred revenue	331.8	(11.1)	–	320.7
Provisions	1.4	–	1.9	3.3
Deferred tax liabilities	6.0	8.5	–	14.5
Other non-current liabilities	315.0	–	–	315.0
	654.2	(2.6)	1.9	653.5
Net assets	91.8	58.2	–	150.0

Consolidated statement of financial position as at 31 March 2017

	As previously reported $M	IFRS 15 Adjustment $M	RDEC / Interest on UTP $M	Restated $M
Non-current assets				
Deferred tax asset	105.3	(5.2)	–	100.1
Other non-current assets	880.7	27.5	–	908.2
	986.0	22.3	–	1,008.3
Current assets				
Tax assets	7.7	–	(3.8)	3.9
Trade and other receivables	145.2	8.8	3.8	157.8
Other current assets	84.3	–	–	84.3
	237.2	8.8	–	246.0
Current liabilities				
Deferred revenue	330.6	(15.6)	–	315.0
Income tax payable	21.0	–	(1.0)	20.0
Other current liabilities	178.8	–	–	178.8
	530.4	(15.6)	(1.0)	513.8
Non-current liabilities				
Deferred revenue	250.4	(11.6)	–	238.8
Provisions	1.1	–	1.0	2.1
Deferred tax liabilities	14.4	6.9	–	21.3
Other non-current liabilities	300.2	–	–	300.2
	566.1	(4.7)	1.0	562.4
Net assets	126.7	51.4	–	178.1

3 Application of New and Revised International Financial Reporting Standards ("IFRSs")

IFRS 9 – Financial Instruments

IFRS 9 – Financial Instruments which was issued in July 2014, became effective for the Group from 1 April 2018. The introduction of the new standard had no material impact on the Group.

IFRS 16 – Leases

IFRS 16 – Leases, which was issued in January 2016, will become effective for the Group from 1 April 2019.

IFRS 16 replaces existing guidance on leases, including IAS 17 Leases, IFRIC 4 – Determining whether an Arrangement contains a Lease, ISC-15 Operating Leases – Incentives and SIC27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 introduces a single, on-balance sheet lease accounting model whereby the lessee recognises a right-of-use ("ROU") asset and a corresponding financial liability to the lessor, representing the obligation to make lease payments. The standard includes two recognition exemptions for lessees; "low value assets" (e.g. personal computers) and short-term leases with a term of less than 12 months.

The Group will apply IFRS 16 initially on 1 April 2019 using the modified retrospective approach whereby the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings on 1 April 2019, with no restatement of comparative information.

In the Consolidated Statement of Profit or Loss, the operating lease expenditure will be replaced by depreciation of the ROU asset together with a finance expense. Alternative performance measures which exclude depreciation, will benefit from the adoption of IFRS 16 through the removal of the operating lease charge. In the Consolidated Statement of Cash Flows, "Net cash flow from operating activities" will see an improvement because of the depreciation adjustment, with a corresponding increased outflow in "Net cash flow from financing activities".

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

3 Application of New and Revised International Financial Reporting Standards ("IFRSs") continued

The adoption of IFRS 16 is not expected to have an impact on the Group's ability to comply with loan covenants under the Senior Facilities Agreement dated 6 February 2017; as that agreement is drafted on a "frozen GAAP" basis.

The Directors have completed an initial assessment of the estimated impact on the Consolidated Financial Statements. Based on the information currently available, the Group expects to recognise additional lease liabilities of $68.9M together with ROU assets comprising offices and plant and equipment of $61.3M. However, the actual impacts of adopting the standard on 1 April 2019 may change because:

- interpretation of new accounting policies are subject to change until the Group presents its first Financial Statements that include the date of initial application; and,
- the impact will depend on future economic conditions including the Group's borrowing rate and the extent to which the Directors choose to use the available practical expedients and recognition exemptions.

The Group has not applied the following new and revised IFRSs that have been issued but are not yet effective. The Directors do not anticipate that these IFRSs will have a significant effect on the Group's consolidated financial information:

Effective for annual periods beginning on or after January 2019:

IFRIC 23 – Uncertainty over Income Tax Treatments

Amendments to IFRS 9 – Prepayment features with negative compensation

Amendments to IAS 28 – Long-term interests in Associates and Joint Ventures

Amendments to IAS 19 – Plan amendment, curtailment or settlement

Various – Annual improvements to IFRS standards 2015 – 2017

Effective for annual periods beginning on or after January 2020:

Amendments to references to conceptional framework in IFRS standards

Effective for annual periods beginning on or after January 2021:

IFRS 17 – Insurance Contracts

4 Significant Accounting Policies

4.1 Statement Of Compliance

The Consolidated Financial Statements have been prepared using International Financial Reporting Standards as adopted by the European Union ("EU") as they apply to the Group. In addition to complying with its legal obligation to apply IFRSs as adopted by the EU, the Group has also applied IFRSs as issued by the International Accounting Standards Board; collectively "IFRS".

4.2 Going Concern

The Group has considerable financial resources together with contracts with a large number of customers and across different geographic areas and industries. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully.

The Group has reported a net profit of $26.9M for the year-ended 31 March 2019 (2018: Loss of $60.9M), a net cash flow from operating activities of $142.9M (2018: $147.7M) and at 31 March 2019 has net current liabilities of $188.1M (2018: $230.0M). After excluding short-term deferred revenue from current liabilities, the Group has net current assets of $240.5M including significant cash and cash equivalent balances of $172.1M and, given the cash-generative nature of the Group's operations and the visibility of future renewals, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future.

The Group meets its current funding requirements through a five-year facility which at 31 March 2019 amounted to $302.4M that is repayable in July 2020. The nature of the Group's subscription business is such that there is good visibility in the timing of cash inflows. Based, in part, on the phasing of the renewal base, the Directors have prepared projected cash flow information for the three-year period from the date of their approval of these Financial Statements. On the basis of this cash flow information and discussions with the Group's bankers, the Directors expect that the current loan facilities will be renewed on the majority of the Group's borrowings (which, based on the cash flow projections, will be sufficient to cover cash flow requirements) on or before expiry and accordingly, this has been reflected in the cash flow forecast.

Based on the above indications, the Directors believe that it remains appropriate to prepare the annual Consolidated Financial Statements on a going concern basis. The Financial Statements do not include any adjustments that would result from the basis of preparation being inappropriate.

Further information regarding the Group's business activities, together with the factors likely to affect its future development, performance and position is set out in the strategic report on pages 8 to 51. Further information regarding the financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the strategic report and the notes to the Consolidated Financial Statements. In addition, note 26 to the Consolidated Financial Statements includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, and its exposures to credit risk and liquidity risk.

4.3 Basis of Consolidation

The consolidated historical financial information has been prepared under the historical cost convention and is presented in US dollars. All values are rounded to the nearest 0.1 million ($M) unless otherwise indicated. The functional currency of Sophos Group plc is US dollars. The Group uses US dollars as its presentation currency to aid comparability of its financial information with that of its peers and the industry; whose information is generally presented in US dollars.

The accounting policies used in preparing the consolidated historical financial information for the year-ended 31 March 2019 have been consistently applied to all years presented and are set out below.

The historical financial information consolidates the financial information of Sophos Group plc and the entities it controls (its subsidiaries) at 31 March 2019. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The financial information of the subsidiaries is prepared for the same reporting period as the parent Company, using consistent accounting policies.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions that are recognised in the statement of financial position of the individual reporting entities, are eliminated in full on consolidation.

4.4 Foreign Currency Translation

The individual historical financial information of each Group company is prepared in the currency of the primary economic environment in which it operates (its functional currency). Each entity in the Group determines its own functional currency and items included in the historical financial information of each entity are measured using that functional currency.

In preparing the financial information of the individual companies, transactions in foreign currencies are recorded at the rate of exchange prevailing at the date of the transaction. Monetary assets and liabilities in foreign currencies are translated at the exchange rate prevailing at the reporting date. All exchange differences are taken to the Consolidated Statement of Profit or Loss, except for differences on monetary assets and liabilities that form part of the Group's net investment in a foreign operation. These are taken directly to equity until the disposal of the net investment, at which time they are recognised in the Consolidated Statement of Profit or Loss. Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operation and translated at the closing rate.

On consolidation, assets and liabilities of foreign subsidiaries are translated into the presentation currency (US dollars) at the exchange rate prevailing at the reporting date. Income and expense items are translated into US dollars at the prior-month closing rate to that in which the transaction took place because they approximate the rate of exchange at the transaction dates. Exchange differences arising on the translation of opening net assets of entities whose functional currency is not US dollars, together with differences arising from the translation of the net results at average or actual rates to the exchange rate prevailing at the reporting date, are taken to equity.

On disposal of a foreign entity, the deferred accumulated amount recognised in equity relating to that particular foreign operation is recognised in the Consolidated Statement of Profit or Loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

4 Significant Accounting Policies continued

4.5 Critical Accounting Judgements and Key Sources of Estimation Uncertainty

The preparation of Consolidated Financial Statements requires Directors to make estimates and assumptions that affect the amounts reported for assets and liabilities as at the reporting date and the amounts reported for revenues and expenses during the period.

Judgements

In the process of applying the Group's accounting policies described in this note, the Directors have made the following judgements that have a significant effect on the amounts recognised in the historical financial information.

Revenue

The Group sells software products under fixed term contracts and perpetual licences. Where there is a multi-element arrangement, the consideration receivable is allocated to each performance obligation of the arrangement and this is done on the basis of an estimate of their respective transaction price. In determining the standalone selling price of each performance obligation, Directors make reference to current prices of individual elements and adjust this by its relative share of discounts applied to the entire sale, regardless of any separate prices stated within the contract. See note 7.

Classification of exceptional items and presentation of non-GAAP measures

The Directors exercise their judgement in the classification of certain items as exceptional and outside of the Group's underlying results. The determination of whether an item should be separately disclosed as an exceptional item or other adjustments requires judgement on its materiality, nature and incidence, as well as whether it provides clarity on the Group's underlying trading performance. In exercising this judgement, the Directors take appropriate regard of IAS 1 "Presentation of Financial Statements'' as well as guidance issued by the Financial Reporting Council and the European Securities and Market Authority on the reporting of exceptional items and alternative performance measures. The overall goal of the Directors is to present the Group's underlying performance without distortion from one-off or non-trading events regardless of whether they be favourable or unfavourable to the underlying result. Further details of the individual exceptional items, and the reasons for their disclosure treatment, are set out in note 8.

Research and development costs

Development costs will be capitalised in accordance with the accounting policy set out in this note. Determining the amounts to be capitalised requires the Directors to make assumptions regarding the capitalisation criteria requirements of IAS 38 – Intangible assets. See note 16.

Legal proceedings

The Directors' at the reporting date form a judgement in relation to the probable outcome of ongoing litigation against the Group. These judgements take account of available information, historical experience and the likelihood of different possible outcomes. See note 34.

Estimates

The key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below. The nature of estimation means that actual outcomes could differ from those estimates.

Business combinations

Where a business combination includes a contingent consideration, the Directors are required to make an assessment at the time of the acquisition of the most likely amount required to be settled. This will include estimates of the outcome of future performance measures as agreed between the parties. Note 24 sets out the financial liability at the end of the period and details the method of calculation as estimated at the balance sheet date.

Income tax

The liability for income taxes at the balance sheet date includes the Directors estimates of the amount of tax payable on open tax computations where the liabilities remain to be agreed with the tax authorities. These estimates may differ from the actual outcome and are further discussed in 4.16 and note 14 below.

4.6 Revenue Recognition

The Group operates exclusively through a channel distribution model using a two-tier channel distribution structure around the world, with the exception of the UK where it operates a one-tier structure. Under the two-tier arrangement, the Group will contract with and invoice distributors, who will in turn transact with partners, who will ultimately transact with the end user. Under the one-tier arrangement the Group will transact with the partner who will transact with the ultimate end user. Consequently, in the judgement of the Directors, the Group's customers are both distributors and partners under the respective models and sales contracts are therefore not with the end user. In both scenarios, the accounting treatment of sales contracts is the same, and in all cases the Group regards itself as a principal and not an agent.

In cases where support has been purchased, the responsibility for providing that support, and for all products providing maintenance and definition updates, remains with the Group rather than with channel partners and distributors. The Directors do not consider this changes the nature of the relationship with the customer.

Software licences sold by the Group provide security protection amongst other things against ransomware, malware and malicious viruses.

The vast majority of the Group's software licences include rights to support and frequent product updates, the access to which is granted at the point a licence is provided to the customer and continues through the term of the licence to which the customer has subscribed, resulting in the software licence service being performed over a period of time. As a result, for these right-of-access licences, Billings occur on day one whilst Revenue is recognised over time, because of the ongoing obligations to provide updates over the term of the licence.

Standard sales contracts do not include return rights; and in accordance with industry practice, customers only have a right of refund for undelivered product on the hardware or software licences that they have purchased. In a minority of cases, agreements do allow for some limited returns. These very limited return rights are taken into account when considering the appropriate recognition of Revenue.

The Group does not recognise Billings nor Revenue until the criteria requiring delivery, and consequently transfer of control, of hardware or software licences to be completed have been met.

Revenue is therefore recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the transaction price of the consideration received, after discounts and rebates but excluding VAT and other sales taxes or duty.

The following specific recognition criteria must also be met before revenue is recognised: where there is a multi-element arrangement, the consideration receivable is allocated to each performance obligation of the arrangement and this is done on the basis of an estimate of their respective transaction price. In determining the standalone selling price of each performance obligation, the Directors make reference to current prices of individual elements and adjust this by its relative share of discounts applied to the entire sale, regardless of any separate prices stated within the contract.

The impact of the adoption of IFRS 15 Revenue from contracts with customers in the prior year is set out in note 2.

Revenue from software licences and service contracts

The Group sells software products under fixed-term contracts and under perpetual licences. Revenue on software licences and service contracts is recognised when the Group has met its obligation in relation to the product or services, which is on delivery of all relevant components for perpetual licences and over the life of the agreed licence for termed products. The Group considers perpetual licences as a right-of-use licences which are recognised at the time of Billing.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

4 Significant Accounting Policies continued

4.6 Revenue Recognition continued

Fixed-term contracts - subscriptions

End users who receive software products at the start of the contract under a fixed-term licence are entitled to receive regular updates and upgrades for the duration of the licence term which usually run for periods ranging up to five years.

Revenue for these fixed-term contracts is recognised rateably over the period that the contractual obligation exists.

Accrued and deferred revenue arising on long-term contracts is included in receivables as accrued income and payables as deferred revenue, as appropriate.

Where the Group contracts with an original equipment manufacturer ("OEM") or a service provider, rather than an end user, it mirrors the above policy and recognises the revenue in line with the contractual terms granted to the end user.

Perpetual licences

Revenue is recognised immediately where customers purchase software products under a perpetual licence. Revenue in respect of support and maintenance contracts associated with perpetual licences is recognised rateably over the life of the support / maintenance contract. Revenue from perpetual licences is recognised as part of Other Revenue, see note 7.

Sale of goods - hardware appliances

Where software licences and hardware are sold together, if the software is not essential to the functionality of the tangible product, then the revenue from the sale of goods is recognised immediately. However, where the software is essential to the functionality of the tangible product and the hardware cannot function without the software, revenue from the sale of goods is recognised rateably over the period of the associated software licence contract.

Interest income

Interest income is recognised as interest accrues.

4.7 Property, Plant and Equipment

Property, plant and equipment is stated at cost less accumulated depreciation and accumulated impairment losses. Cost comprises the aggregate amount paid and the fair value of any other consideration given to acquire the asset and includes costs directly attributable to making the asset capable of operating as intended.

Except for freehold land, depreciation is provided to write off the cost less the estimated residual values of all property, plant and equipment on a straight-line basis over their estimated useful life as follows:

Freehold buildings	25 years
Leasehold improvements	Over the lease period
Computer equipment	3 – 5 years
Other plant and equipment	5 years
Motor vehicles	4 years
Fixtures and fittings	6 – 10 years

The carrying values of property, plant and equipment are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable and are written down immediately to their recoverable amount.

An item of property, plant and equipment is de-recognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on de-recognition of the asset is included in the Consolidated Statement of Profit or Loss in the period of de-recognition.

The residual values, useful lives and methods of depreciation of the assets are reviewed, and adjusted if appropriate, at each financial year-end.

4.8 Business Combinations and Goodwill

Business combinations are accounted for using the acquisition accounting method. This involves recognising identifiable assets (including previously unrecognised intangible assets) and liabilities (including contingent liabilities and excluding future restructuring) of the acquired business at fair value.

Business combinations on or after 1 April 2004 are accounted for under IFRS 3. Any excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities is recognised in the Consolidated Statement of Financial Position as goodwill and is not amortised. To the extent that the net fair value of the acquired entity's identifiable assets, liabilities and contingent liabilities is greater than the cost of the investment, a gain is recognised immediately in the Consolidated Statement of Profit or Loss. Goodwill recognised as an asset as at 31 March 2004 is recorded at its previous carrying amount under UK GAAP and is not amortised.

After initial recognition, goodwill is stated at cost less any accumulated impairment losses, with the carrying value being reviewed for impairment, at least annually and whenever events or changes in circumstances indicate that the carrying value may be impaired. Goodwill assets considered significant in comparison to the Company's total carrying amount of such assets have been allocated to cash-generating units or groups of cash-generating units. Where the recoverable amount of the cash-generating unit is less than its carrying amount including goodwill, an impairment loss is recognised in the Consolidated Statement of Profit or Loss.

The carrying amount of goodwill allocated to a cash-generating unit is taken into account when determining the gain or loss on disposal of the unit, or of an operation within it.

4.9 Intangible Assets

Intangible assets are carried at cost less accumulated amortisation and accumulated impairment losses.

Intangible assets acquired separately from a business are carried initially at cost. An intangible asset acquired as part of a business combination is recognised outside of goodwill if the asset is separable or arises from contractual or other legal rights and its fair value can be measured reliably. Expenditure on internally developed intangible assets is taken to the Consolidated Statement of Profit or Loss in the period in which it is incurred to the extent that the expenditure does not qualify for capitalisation under research and development costs.

Where computer software is not an integral part of a related item of computer hardware, the software is classified as an intangible asset. The capitalised costs of software for internal use include external direct costs of materials and services consumed in developing or obtaining the software, and incremental payroll and payroll-related costs arising from the assignment of employees to implementation projects. Capitalisation of these costs ceases no later than the point at which the software is substantially complete and ready for its intended internal use.

Intangible assets with a finite life have no residual value and are amortised over their expected useful lives as follows:

Intangible assets arising on acquisition of subsidiaries

Intellectual property	–	5 – 15 years reducing balance basis
Brand names	–	15 – 20 years reducing balance basis
Customer base	–	6 – 14 years reducing balance basis

Other purchased intangible assets

Software	–	3 years straight-line basis

The amortisation expense on intangible assets with finite lives is recognised in the Consolidated Statement of Profit or Loss as a general finance and administration cost, as most of the intangible assets are used by functions not reflected in Cost of Sales. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least annually.

The carrying value of intangible assets is reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortised. The term of their useful life is reviewed annually to determine whether indefinite life assessment continues to be appropriate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

4 Significant Accounting Policies continued

4.10 Research and Development Costs

Expenditure on research activities is expensed as incurred.

Development expenditure is recognised as an intangible asset when its future recoverability can reasonably be regarded as assured and technical feasibility and commercial viability can be demonstrated.

During the period of development, the asset is tested for impairment annually. Following the initial recognition of the development expenditure, the cost model is applied requiring the asset to be carried at cost less any accumulated amortisation and accumulated impairment losses. Amortisation of the asset begins when development is complete and the asset is available for use. It is amortised over the period of expected future sales.

Development expenditure incurred on minor or major upgrades, product fixes and updates or other changes in software functionalities does not satisfy the criteria, as the product is not substantially new in its design or functional characteristics. Such expenditure is therefore recognised as an expense in the Consolidated Statement of Profit or Loss as incurred.

4.11 Impairment of Assets

At least annually, or when otherwise required, Directors review the carrying amounts of the Group's tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount or value in use of the asset is estimated in order to determine the extent of any impairment loss.

Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money as well as risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately in the Consolidated Statement of Profit or Loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but not beyond the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised immediately as income in the Consolidated Statement of Profit or Loss, although impairment losses relating to goodwill may not be reversed.

4.12 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost includes all costs incurred in bringing each product to its present location and condition. The cost of raw materials, consumables and goods for resale is based on the purchase cost and is determined on a first-in, first-out basis.

Net realisable value is based on estimated selling price less any further costs expected to be incurred to completion and disposal.

4.13 Financial Instruments

Financial assets and liabilities are recognised in the Group's statement of financial position when the Group becomes party to the contractual provisions of the instrument. When financial instruments are recognised initially they are measured at fair value, being the transaction price plus, in the case of financial assets and financial liabilities not at fair value through profit or loss, directly attributable transaction costs.

Trade receivables

Trade receivables, which generally have 30-90 day payment terms mainly depending on the jurisdiction, are carried at original invoice amount, including value added tax and other sales taxes, less an estimate made for doubtful receivables based on an expected credit loss model through a review of any outstanding amounts at the period-end. Provision for bad debts is made in the period in which they are identified.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and bank deposits repayable in 90 days or less. For the purpose of the Consolidated Statement of Cash Flows, cash and cash equivalents consist of cash in hand and bank deposits net of outstanding bank overdrafts.

Trade payables

Trade payables are recognised at cost, which is deemed to be materially the same as the fair value.

Classification of equity instruments as debt or equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

When equity instruments are issued, any component that creates a financial liability of the Group is presented as a liability in the Consolidated Statement of Financial Position; measured initially at fair value net of transaction costs and thereafter at amortised cost until extinguished on conversion or redemption. The corresponding dividends relating to the liability component are charged as interest expense in the Consolidated Statement of Profit or Loss.

Equity instruments issued by the Company are recorded as the proceeds received, net of direct issue costs. Equity instruments are classified according to the substance of the contractual arrangements entered into.

Interest bearing loans and borrowings

Obligations for loans and borrowings are recognised when the Group becomes party to the related contracts and are measured initially at fair value less directly attributable transactions costs.

After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Gains and losses arising on the re-purchase, settlement or other cancellation of liabilities are recognised respectively in finance income and finance expense.

Gains and losses arising on the revaluation of loans and borrowings denominated in currencies other than the entity's functional currency are recognised in finance expense.

Derivative financial instruments

The Group sometimes uses derivative financial instruments, principally forward foreign currency contracts to reduce its exposure to exchange rate movements and interest rate caps to reduce its exposure to fluctuating interest rates. The Group does not hold or issue derivatives for speculative or trading purposes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

4 Significant Accounting Policies continued

4.13 Financial Instruments continued

Derivative financial instruments are recognised as assets and liabilities measured at their fair values at the reporting date. Changes in the fair values are recognised in the Consolidated Statement of Profit or Loss and this is likely to cause volatility in situations where the carrying value of the hedged item is either not adjusted to reflect fair value changes arising from the hedged risk or is so adjusted but that adjustment is not recognised in the Consolidated Statement of Profit or Loss. Provided the conditions specified by IFRS 9 — Financial Instruments are met, hedge accounting may be used to mitigate this volatility.

4.14 Leases

Prior to the adoption of IFRS 16 Leases, which applies form 1 April 2019, leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

4.15 Provisions

A provision is recognised when the Group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the effect is material, expected future cash flows are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability.

Where the Group expects some or all of a provision to be reimbursed, for example under an insurance policy, the reimbursement is recognised as a separate asset but only when recovery is virtually certain.

The expense relating to any provision is presented in the Consolidated Statement of Profit or Loss net of any reimbursement.

Where discounting is used, the increase in the provision due to unwinding the discount is recognised as a finance expense.

4.16 Taxation

The income tax charge represents the sum of current and deferred taxes. Current tax payable or recoverable is based on the taxable profit for the period. Taxable profit differs from profit reported in the Consolidated Statement of Profit or Loss because some items of income or expense are taxable in different periods or may never be taxable or deductible. The Group's liability for current tax is calculated using UK and foreign rates and laws that have been enacted or substantively enacted by the reporting period date.

A current tax provision is recognised when the Group has a present obligation as a result of a past event and it is probable that the Group will be required to settle that obligation. Tax liabilities are recognised when it is considered probable that there will be a future outflow of funds to a taxing authority. They are measured using one of the following methods, depending on which of the methods the Directors expect will better reflect the amount the Group will pay to the tax authority.

The single best estimate method is used where there is a single outcome that is more likely than not to occur. This will happen, for example, where the tax outcome is binary or the range of possible outcomes is limited. The most likely outcome may be that no tax is expected to be payable, in which case the provision is nil.

Alternatively, a probability weighted expected value is used where, on the balance of probabilities, something will be paid to the tax authority but the possible outcomes are widely dispersed with low individual probabilities (i.e. there is no single outcome more likely than not to occur). In this case, the provision is the sum of the probability-weighted amounts in the range. In assessing provisions against uncertain tax positions, management uses in-house tax experts, professional firms and previous experience of the taxing authority to evaluate the risk. However, it remains possible that uncertainties will ultimately be resolved at amounts greater or smaller than the liabilities provided.

The Group's current tax provision relates to the Directors' estimate of the amount of tax payable on open tax computations where the liabilities remain to be agreed with authorities. The uncertain tax items for which provision is made (see note 13), relate to the interpretation of tax legislation impacting arrangements entered into in the ordinary course of business. Due to the uncertainty associated with such items, it is possible that at a future date, on conclusion of open tax matters, the final outcome may vary. The Group reports cross-border transactions undertaken between Group subsidiaries on an arm's-length basis in tax returns in accordance with OECD guidelines. However, transfer pricing relies on the making of estimates and it is frequently possible for there to be a range of legitimate and reasonable views. This means that it is impossible to be certain that the tax returns basis will be sustained on examination. Discussions with tax authorities relating to cross-border transactions and other matters are ongoing in several of the Group's major trading jurisdictions. Although the timing and amount of final resolution of these uncertain tax positions cannot be reliably predicted, no significant impact on the profitability of the Group is expected to result.

Deferred tax is the tax expected to be payable or recoverable in the future arising from temporary differences between the carrying amounts of assets and liabilities in the Consolidated Financial Statements and the corresponding tax bases used in the computation of taxable profit. It is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. The rate is based on tax rates that have been enacted or substantively enacted by the reporting period date. Deferred tax is charged or credited in the Consolidated Statement of Profit or Loss, except when it relates to items charged or credited to other comprehensive income or directly to equity, in which case the deferred tax is dealt with in other comprehensive income or in equity. Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the income taxes levied in the same taxation authority on either the same entity or on different taxable entities which intend to settle the current tax assets and liabilities on a net basis.

Disclosures relating to tax are set out in note 14.

4.17 Pensions and Other Post-Retirement Benefits

The Group operates defined contribution pension schemes for its employees. The assets of the schemes are held separately from those of the Group in independently administered funds. Contributions to defined contribution schemes are recognised in the Consolidated Statement of Profit or Loss in the period in which they become payable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

4 Significant Accounting Policies continued

4.18 Share-Based Payments

Employees (including senior executives and Directors) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions"). The Group also grants cash-settled awards in certain jurisdictions in order to ensure compliance with tax, regulatory or legal country specific requirements.

Equity-settled transactions

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date on which they are granted. The fair value is determined by using an appropriate pricing model, further details of which are given in note 29.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, ending on the date on which the relevant employees become fully entitled to the award.

At each reporting date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and the Directors best estimate of the achievement or otherwise of non-market conditions and of the number of equity instruments that will ultimately vest or, in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous reporting date is recognised in the Consolidated Statement of Profit or Loss, with a corresponding entry in equity.

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period. In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification. No reduction is recognised if this difference is negative.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any cost not yet recognised in the Consolidated Statement of Profit or Loss for the award is expensed immediately. Any compensation paid up to the fair value of the award at the cancellation or settlement date is deducted from equity, with any excess over fair value being treated as an expense in the Consolidated Statement of Profit or Loss.

Cash-settled transactions

A liability is recognised for the fair value of cash-settled transactions. The fair value is measured at grant and each subsequent reporting date up to and including the settlement date. The change in fair value is recognised in the Consolidated Statement of Profit or Loss with a corresponding entry in liabilities for cash-settled transactions.

4.19 Exceptional Items

Exceptional items are those that in the judgement of the Directors need to be disclosed by virtue of their size, nature or incidence, in order to draw the attention of the reader and to report the underlying business performance of the Group. Such items are included within the income statement caption to which they relate, and are separately disclosed either in the notes to the Consolidated Financial Statements or on the face of the Consolidated Statement of Profit or Loss.

4.20 Events After the Reporting Date

Events between the reporting date and the date on which the Consolidated Financial Statements are approved, favourable and unfavourable, providing evidence of conditions that existed at the reporting date, adjust the amounts recognised in the Consolidate Financial Statements. Those that indicate conditions arising after the reporting date are disclosed but are not recognised within the Consolidated Financial Statements.

5 Alternative Performance Measures ("APM's")

The Group uses certain financial measures that are not defined or recognised under IFRS. The Directors believe that these non-GAAP measures supplement GAAP measures to help in providing a further understanding of the results of the Group and are used as key performance indicators within the business to aid in evaluating its current business performance. The measures can also aid in comparability with other companies, particularly in the cybersecurity industry, who use similar metrics. However as the measures are not defined by IFRS, other companies may calculate them differently or may use such measures for different purposes to the Group.

Constant currency measures have limitations, particularly as the currency effects that are eliminated may constitute a significant element of the Group's revenue and expenses and could materially impact the Group's performance. The Directors do not evaluate the Group's results and performance on a constant currency basis without also evaluating the Group's financial information prepared at actual foreign exchange rates in accordance with IFRS.

Other than for the calculation of adjusted operating EPS (see note 15), the definition of non-GAAP measures in the year-ended 31 March 2019 is consistent with those presented for the year-ended 31 March 2018. The reconciliation of non-GAAP measures to GAAP measures is set out below.

Billings

Billings represent the value of products and services invoiced to customers after receiving a purchase order from the customer and delivering products and services to them, or for which there is no right to a refund. Billings do not equate to statutory revenue.

	Year-ended 31 March 2019 $M	**Year-ended 31 March 2018 Restated See note 2 $M**
Revenue	710.6	639.0
Net deferral of revenue (see note 23)	49.7	129.6
Billings	760.3	768.6
Currency revaluation	25.9	18.7
Constant currency billings	786.2	787.3

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

5 Alternative Performance Measures ("APM's") continued

Adjusted Operating Profit and Cash EBITDA

Adjusted Operating Profit ("AOP") provides a supplemental measure of earnings that facilitates review of operating performance on a period-to-period basis by excluding non-recurring and other items that are not indicative of the Group's underlying operating performance.

Adjusted Operating Profit is a key profit measure used by the Board to assess the underlying financial performance of the Group. Adjusted Operating Profit is stated before the following items for the following reasons:

- Exceptional items, as set out in note 8, are one of the items that in the judgement of the Directors should be disclosed separately by virtue of their size, nature or incidence, in order to show the underlying business performance of the Group.
- Charges for the amortisation of acquired intangibles are excluded from the calculation of adjusted Operating Profit. This is because these charges are based on judgements about their value and economic life, are the result of the application of acquisition accounting rather than core operations, and whilst revenue recognised in the income statement does benefit from the underlying technology that has been acquired, the amortisation costs bear no relation to the Group's underlying ongoing operational performance. In addition, amortisation of acquired intangibles is not included in the analysis of segment performance used by the chief operating decision maker.
- Share-based payment charges are similarly excluded from the calculation of adjusted Operating Profit because these represent a non-cash accounting charge for transactions that could otherwise have been settled in cash or not be limited to employee compensation. These charges also represent long-term incentives designed for long-term employee retention, rather than reflecting the short-term underlying operations of the Group's business. The Directors acknowledge that there is an ongoing professional debate on the add-back of share-based payment charges but believe that as they are not included in the analysis of segment performance used by the chief operating decision maker and their add-back is consistent with metrics used by a number of other companies in the global cybersecurity industry, that this treatment remains appropriate.

Cash earnings before interest, taxation, depreciation and amortisation ("Cash EBITDA") is defined as the Group's Operating Profit / (loss) adjusted for depreciation and amortisation charges, any gain or loss on the sale of tangible and intangible assets, share option charges, unrealised foreign exchange differences (on the basis that they are non-cash income and expenses) and exceptional items, with billings replacing recognised revenue. The unrealised foreign exchange differences are included within the foreign exchange gain of $1.5M (2018: loss of $6.9M) disclosed on the face of the Consolidated Statement of Profit or Loss. The Directors consider this metric a useful supplemental measure of earnings that provides visibility on actual cash earned in the year. The replacement of revenue with billings adjusts for the net deferral of revenue, whereas the weighted average contract term is around 28 months, a more material adjustment is generated than for the short-term working capital variations derived from the application of the accruals concept. Therefore, whilst Cash EBITDA is not a pure cash flow metric, it represents a closer approximation to cash earned in the period from the trading that has taken place. Depreciation and unrealised foreign exchange differences are adjusted as they do not represent cash costs of the business.

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Operating profit / (loss)	60.9	(19.7)
Amortisation of intangible purchased assets	16.9	25.2
Share-based payments expense	35.0	39.6
Exceptional items	(3.8)	13.2
Adjusted Operating Profit	109.0	58.3
Depreciation	11.6	11.6
Unrealised foreign exchange loss	(1.5)	8.1
Net deferral of revenue	49.7	129.6
Net deferral of related selling expenses (see note 20)	(0.9)	(8.4)
Cash EBITDA	167.9	199.2
Billings	760.3	768.6
Revenue	(710.6)	(639.0)
Net deferral of revenue	49.7	129.6

As set out in note 2, the Company made changes in the period to its significant accounting policies in respect of IFRS 15 – Revenue and certain components of the income tax charge. The following table summarises the impact of these changes for each line item of the Group's adjusted Operating Profit and Cash EBITDA for the year-ended 31 March 2018 comparative information.

	As previously reported $M	IFRS 15 Adjustment $M	RDEC / Interest on UTP $M	Restated $M
Operating loss	(31.9)	6.7	5.5	(19.7)
Amortisation of intangible purchased assets	25.2	–	–	25.2
Share-based payments expense	39.6	–	–	39.6
Exceptional items	13.2	–	–	13.2
Adjusted Operating Profit	46.1	6.7	5.5	58.3
Depreciation	11.6	–	–	11.6
Unrealised foreign exchange loss	8.1	–	–	8.1
Net deferral of revenue	127.9	1.7	–	129.6
Net deferral of related selling expenses	–	(8.4)	–	(8.4)
Cash EBITDA	193.7	–	5.5	199.2
Billings	768.6	–	–	768.6
Revenue	(640.7)	1.7	–	(639.0)
Net deferral of revenue	127.9	1.7	–	129.6

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5 Alternative Performance Measures ("APM's") continued

Unlevered Free Cash Flow

Unlevered free cash flow represents net cash flow from operating activities adjusted for exceptional items and net capital expenditure. Unlevered free cash flow provides an understanding of the Group's cash generation and is a supplemental measure of liquidity in respect of the Group's operations without the distortions of exceptional and other non-operating items.

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Net cash flow from operating activities	142.9	147.7
Exceptional items	3.1	13.0
Net capital expenditure	(22.2)	(21.1)
Unlevered free cash flow	123.8	139.6

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Cash EBITDA	167.9	199.2
Net capital expenditure	(22.2)	(21.1)
Change in working capital	(5.2)	(12.2)
Corporation tax paid	(16.7)	(26.3)
Unlevered free cash flow	123.8	139.6

6 Segment Information

For internal management reporting purposes, the operating segments are determined to be geographic segments as the Group's risks and rates of return are affected predominantly by the different economic environments. This is consistent with the information provided to the Chief Operating Decision Maker. The Group has only one operating segment based on product on the basis that the products and services offered to external customers are very similar and therefore do not result in different risks and rates of return for the Group.

The Group's geographical segments are based on the location of the Group's operations consisting of Europe, Middle East and Africa ("EMEA"), The Americas and Asia Pacific and Japan ("APJ").

Billings are the value of products and services invoiced to customers after receiving a purchase order from the customer and delivering products and services to them, or for which there is no right to a refund. Billings does not equate to statutory revenue.

Billings are classified by the geographic location of direct customers, OEMs and the distributors which purchase our products. The geographic location of OEMs or distributors may be different from that of end customers. A disclosure of billings and revenue by region is included in the Financial Review on page 28.

The accounting policies of the reportable segments are the same as the Group's accounting policies described in note 4. Segment profits represent the profit earned by each segment without allocation of central administration costs including Directors' salaries, finance expenses and income tax expense. This is the measure reported to the Chief Operating Decision Maker, the Chief Executive Officer, and Senior Management Team for the purposes of resource allocation and assessment of segment performance.

Transfer prices between geographical segments are set on an arm's length basis in a manner similar to transactions with third parties.

Geographical segments

The following tables present billings, expenditure and certain asset information regarding the Group's geographical segments for the year-ended 31 March 2019 and 31 March 2018.

Year-ended 31 March 2019	Americas $M	EMEA $M	APJ $M	Total $M
Billings (see note 5)	267.9	395.2	97.2	760.3
Regional cost of sales	(12.8)	(36.2)	(12.9)	(61.9)
Regional gross margin	255.1	359.0	84.3	698.4
Regional sales and marketing expense	(77.8)	(85.9)	(31.4)	(195.1)
Regional Operating Profit	177.3	273.1	52.9	503.3
Revenue deferral				(49.7)
Central costs				(364.0)
Amortisation				(16.9)
Depreciation				(11.8)
Net finance expense				(7.3)
Profit before taxation				53.6

Year-ended 31 March 2018 Restated (see note 2)	Americas $M	EMEA $M	APJ $M	Total $M
Billings (see note 5)	270.0	395.1	103.5	768.6
Regional cost of sales	(14.7)	(38.1)	(16.2)	(69.0)
Regional gross margin	255.3	357.0	87.3	699.6
Regional sales and marketing expense	(76.7)	(79.0)	(32.0)	(187.7)
Regional Operating Profit	178.6	278.0	55.3	511.9
Revenue deferral				(129.6)
Central costs				(365.2)
Amortisation				(25.2)
Depreciation				(11.6)
Net finance expense				(21.3)
Loss before taxation				(41.0)

Other segment information

Segment assets	31 March 2019 $M	31 March 2018 Restated See note 2 $M
Americas	373.3	393.5
EMEA	737.3	713.1
APJ	150.3	156.7
Total segment assets	1,260.9	1,263.3
Unallocated assets	115.0	120.7
Consolidated total assets	1,375.9	1,384.0

Unallocated assets relate to deferred tax, as the segment assets reviewed by the Chief Operating Decision Maker does not include deferred tax.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

6 Segment Information continued

Depreciation and amortisation	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Americas	6.6	7.5
EMEA	18.1	24.9
APJ	4.0	4.4
Total depreciation and amortisation	28.7	36.8

Non-current assets by country	31 March 2019 $M	31 March 2018 Restated See note 2 $M
UK	42.5	43.4
USA	22.0	18.5
Germany	5.1	5.9
Other countries	22.4	19.0
Total non-current assets by country	92.0	86.8

Non-current assets by country excludes deferred tax assets and goodwill. Goodwill has been excluded as a split by country is not available and the Directors consider that the cost to develop such analysis would be excessive.

Revenue from external customers by country	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
UK	83.2	73.5
USA	222.2	199.0
Germany	143.5	128.4
Other countries	261.7	238.1
Total revenue from external customers by country	710.6	639.0

The Group's revenue is diversified across its entire end customer base and no single end user accounted for greater than 10 per cent of the Group's revenue in either 2018 or 2019. In 2019 two distributors accounted for 15 per cent each, and one distributor for 11 per cent of Group billings which were attributable to all segments of the Group (2018: three distributors accounted for 15 per cent, 14 per cent and 12 per cent each).

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7 Revenue

Revenue recognised in the Consolidated Statement of Profit or Loss is analysed as follows:

Revenue by Product:	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Network	328.5	316.5
Enduser	348.4	291.8
Other	33.7	30.7
Total	710.6	639.0

Revenue by Type:	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Subscription	593.9	512.4
Hardware	106.8	115.1
Other	9.9	11.5
Total	710.6	639.0

8 Exceptional Items

Exceptional items are those that in the judgement of the Directors need to be disclosed by virtue of their size, nature or incidence, in order to draw the attention of the reader and to show the underlying business performance of the Group. Such items are included within the income statement caption to which they relate and are separately disclosed on the face of the Consolidated Statement of Profit or Loss.

During the year-ended 31 March 2019, the Group incurred restructuring and integration costs of $0.8M in the finalisation of a FY18 project (2018: $10.2M), litigation costs incurred in relation to the defence of certain intellectual property claims arising in previous years of $0.6M (2018: $3.0M), and legal fees of $1.7M (2018: Nil) in connection with a one-off strategic review of the Group's sales policies and procedures pertaining to the use of some of the Group's products in certain overseas territories. In addition, following the final settlement of contingent consideration in respect of the acquisition of Invincea, Inc., an excess financial liability of $6.9M has been released as an exceptional item. This resulted in a total exceptional income of $3.8M (2018: Cost of $13.2M). Tax relief on these exceptional items amounted to $0.5M (2018: $2.6M).

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For the year-ended 31 March 2019

9 Profit / (loss) on Ordinary Activities

The profit (2018: loss) on ordinary activities before taxation is stated after charging:

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Depreciation of property, plant and equipment	11.8	11.6
Amortisation of intangible assets	16.9	25.2
Research and development expenditure	(143.9)	(140.3)
Operating lease rentals:		
Property	14.0	12.5
Other	1.6	1.6
Pension scheme contributions	8.9	8.4
Impairment of trade receivables	0.6	0.6
Net foreign currency differences	(1.5)	6.9

10 Auditor's Remuneration

The Group paid the following amounts to its auditor in respect of the audit of the historical financial information and for other non-audit services provided to the Group.

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Audit of the Financial Statements	0.4	0.4
Subsidiary local statutory audits	0.2	0.3
Total audit fees	0.6	0.7
Other assurance services	0.1	0.1
Total non-audit fees	0.1	0.1

11 Employee Costs

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Wages and salaries	286.0	271.8
Social security costs	25.6	27.3
Pension costs	8.9	8.4
Other costs	12.7	12.1
	333.2	319.6
Share-based payments (see note 29)	36.9	42.3
Total employee costs	370.1	361.9

Included in wages and salaries above are $4.2M (2018: $4.0M) relating to retention payments arising on business combinations.

The average number of employees during the period, analysed by category, was as follows:

	Year-ended 31 March 2019	Year-ended 31 March 2018
Technical	1,934	1,868
Sales and marketing	1,211	1,124
Administration	358	327
Total average number of employees	3,503	3,319

12 Directors' Remuneration

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Directors' emoluments	2.3	3.3
Gains on exercise of share options	3.6	3.5
Gains on vesting of LTIP awards	14.5	4.2
Total Directors' remuneration	20.4	11.0

Directors' emoluments represent all earnings and aggregate contributions to pension schemes made during the year as a Director of Sophos Group plc and its subsidiaries. Further details can be found in the Group's Remuneration Report on pages 91 to 101.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

13 Finance Income and Expense

Finance income	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Interest on bank deposits	0.9	0.3

Finance expense	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Interest expense on loans and borrowings	9.3	8.7
Other interest and bank charges	0.5	0.3
	9.8	9.0
Accretion on contingent consideration	0.1	0.9
Interest on uncertain tax positions (see note 25)	3.5	0.9
Foreign exchange (gain) / loss on borrowings	(6.4)	9.6
Amortisation of facility fees	1.2	1.2
Total finance expense	8.2	21.6

14 Taxation

UK corporation tax for the year-ended 31 March 2019 is calculated at 19% (2018: 19%) of the estimated assessable loss for the period.

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Current income tax:		
UK corporation tax	1.3	1.2
Adjustments in respect of previous years UK tax	0.3	0.3
Overseas tax before exceptional items	22.2	23.0
Adjustment in respect of previous years	13.1	10.2
Total current tax charge	36.9	34.7
Deferred tax:		
Origination and reversal of temporary differences	2.5	(16.7)
Impact of changes in US tax rate	-	5.4
Adjustment in respect of previous years	(12.7)	(3.5)
Total deferred tax credit	(10.2)	(14.8)
Total income tax charge	26.7	19.9

The following table reconciles the theoretical corporation tax expense to the reported tax expense using the UK corporation tax rate. The reconciling items represent the impact of rate differentials in tax jurisdictions and the impact of non-taxable benefits and non-deductible expenses arising from differences between the local tax base and the reported Financial Statements.

	Year-ended 31 March 2019 $M	**Year-ended 31 March 2018 Restated See note 2 $M**
Profit / (loss) for the year before taxation	53.6	(41.0)
Loss for the year before taxation multiplied by the standard rate of corporation tax in the UK of 19% (2018: 19%)	10.2	(7.7)
Effects of:		
Adjustments in respect of previous years	0.8	7.1
Change in tax rate during the year	1.4	3.6
Expenses not deductible for tax purposes	11.8	9.4
Losses not recognised	(0.9)	–
Higher tax rates on overseas earnings	7.7	3.8
Research and development and other tax credits	(1.9)	(0.6)
Impact of US tax reform on deferred tax	–	5.4
Other movements	(2.4)	(1.1)
Charge for taxation on profit / (loss) for the year	26.7	19.9

The Group's taxation strategy is published at www.sophos.com/en-us/medialibrary/PDFs/legal/sophos-group-tax-policy-fy19.pdf and is aligned to its business strategy and operational needs. Oversight of taxation is within the remit of the Audit and Risk Committee. The Chief Financial Officer is responsible for tax strategy supported by a global team of tax professionals. Sophos strives for an open and transparent relationship with all revenue authorities and is vigilant in ensuring that the Group complies with current tax legislation. The Group proactively seeks to agree arm's length pricing with tax authorities to mitigate tax risks of significant cross-border operations. The Group actively engages with policy makers, tax administrators, industry bodies and international institutions to provide informed input on proposed tax measures, so that it and they can understand how those proposals would affect the Group. However, a tax authority may seek adjustment to the filing position adopted by a Group company and it is accepted that interpretation of complex regulations may lead to additional tax being assessed. Uncertain tax positions are monitored regularly and a provision made in the accounts where appropriate.

Key Influences

The Group's tax rate is sensitive to the geographic mix of profits and reflects a combination of higher rates in certain jurisdictions, such as Germany and India, a lower rate in the UK and US and other rates that lie in between in other territories.

The Group receives incentives in certain jurisdictions. In the UK, the Research & Development Expenditure Credit is claimed and is accounted for as a credit to the appropriate research and development expense. In FY19 there was a change in the accounting policy to more closely align to the accounting treatment in comparable organisations resulting in the tax charge increasing by $5.7M (2018: $4.5M through restatement, see note 2). There is no guarantee that these incentives will continue to be applicable in future years.

Tax liabilities are recognised when it is considered probable that there will be a future outflow of funds to a taxing authority. The methodology used to estimate liabilities is set out in note 4.16. Within current liabilities is $35M (2018: $20.0M) in respect of liabilities for uncertain tax positions, the majority of which relates to the risk of challenge from tax authorities to the geographic allocation of profits across the Group and are likely to be resolved as part of a mutual agreement procedure with the relevant tax authorities. Following bilateral tax authority relief procedures it is anticipated that $11.3M (2018 $Nil) of this current liability will be available to utilise against a tax liability in the UK so a deferred tax asset has been recognised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

14 Taxation continued

Consequently, the net tax balance sheet position for uncertain tax positions is $23.7M (2018 $20M). The Group anticipates that a number of tax audits are likely to conclude in the next 12 to 24 months. Due to the uncertainty associated with such tax items, it is possible at a future date, on the conclusion of open tax matters, the final outcome may vary significantly.

The change in tax rate during the year occurs in respect of the re-measurement of a deferred tax asset due to the future reduction of the UK tax rate.

Expected Future Rate

Over the medium-term the tax rate is likely to stabilise as the integration of acquisitions in higher rate jurisdictions are completed. However, the tax rate may fluctuate if business changes are implemented in response to legislation arising from the OECD's Base Erosion & Profit Shifting Project. Legislative change in key territories is being monitored and acted upon.

The Group does not anticipate any significant impact on the future tax charge, liabilities or assets, as a result of the triggering of Article 50(2) of the Treaty on European Union, but cannot rule out the possibility that, for example, a failure to reach satisfactory arrangements for the UK's future relationship with the European Union, could have an impact on such matters.

The European Commission has concluded its investigation into the UK's controlled foreign company ("CFC") rules. The CFC rules levy a charge on foreign entities controlled by the UK that are subject to a lower rate of tax, however there is currently an exemption available for 75% of this charge if the activities being undertaken by the CFC relate to financing. The EC concluded that this exemption is in breach of EU State Aid rules. However, whilst we are awaiting further detail from HMRC, the position has not changed from a tax accounting perspective. The risk is possible, but not probable. UK ministers have yet to decide on whether to pursue an appeal. No provision for this potential liability of $3.6M has been provided in these Consolidated Financial Statements as it is not clear what, if any, the ultimate financial result will be.

Deferred tax assets and liabilities are attributable to the following:

	31 March 2019 $M	31 March 2018 Restated See note 2 $M
Deferred income tax assets in relation to:		
Deferred revenue	40.9	40.0
Tax value of carry forward losses of UK subsidiaries	37.0	24.2
Tax value of carry forward losses of overseas subsidiaries	6.2	6.4
Advanced capital allowances	7.5	7.7
Share-based payments	11.6	27.7
Other temporary differences	11.8	14.7
Total	115.0	120.7
Deferred income tax liabilities in relation to:		
Intangible assets	6.1	5.9
Deferred selling cost	8.5	8.5
Other temporary differences	-	0.1
Total	14.6	14.5

As at 31 March 2019 the aggregate amount of temporary differences associated with undistributed earnings of subsidiaries for which deferred tax liabilities have been recognised was $Nil (2018: $Nil). No liability has been recognised because the Group is in a position to control the reversal of temporary differences and it is probable that such differences will not reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realised or the liability settled, based on tax rates that have been enacted or substantively enacted at the reporting date.

Other temporary timing differences

The deferred tax asset relating to other temporary differences of $11.8M (2018: $14.7m) has decreased during the current period primarily due to the decrease in short-term timing differences balances. It includes temporary differences arising on short-term timing differences and the UK Research & Development Expenditure Credit that isn't paid due to UK tax loss position.

Losses

A deferred tax asset has been recognised in respect of losses where current forecasts indicate profits will arise in the forecast period against which the losses recognised will be offset. At the balance sheet date the Group has unused tax losses of $540.1M (2018: $500.4M) available for offset against future profits. A deferred tax asset has been recognised in respect of $241.4M (2018: $166.4M) of such losses. No deferred tax asset has been recognised in respect of the remaining $298.7M (2018: $334.0M) as it is not considered probable that there will be the required type of future trading or non-trading profits available in the correct entities necessary to permit offset and recognition.

Share-Based Payments

A remuneration expense for share-based payments is recorded in the Consolidated Statement of Profit or Loss over the period from the award date to the vesting date of the relevant options. Where there is a temporary difference between the accounting and tax bases, a deferred tax asset may be recorded. Any deferred tax asset arising on share option awards is calculated as the estimated amount of tax deduction to be obtained in the future. This is based on the Group's share price at the reporting date so will be impacted by share price movement and is pro-rated to the extent that the services of the employee have been rendered over the vesting period. If this amount exceeds the cumulative amount of the remuneration expense at the statutory rate, the excess is recorded directly in equity, against retained earnings. Similarly, current tax relief in excess of the cumulative amount of the remuneration expense at the statutory rate is also recorded in retained earnings. Deferred tax assets have only been recognised in jurisdictions in which future tax deductions are expected.

15 Earnings Per Share

Basic earnings per share ("EPS") is calculated by dividing the profit for the period attributable to equity holders of the parent by the weighted average number of ordinary shares outstanding during the period.

Diluted EPS is calculated by dividing the profit for the period attributable to equity holders of the parent by the weighted average number of ordinary shares outstanding during the period plus the weighted average number of shares that would be issued if all dilutive potential ordinary shares were converted into ordinary shares. In accordance with IAS 33, the dilutive earnings per share are without reference to adjustments in respect of outstanding shares when the impact would be anti-dilutive.

Adjusted operating EPS is calculated by dividing the adjusted Operating Profit for the period after adjusting for taxation attributable to equity holders of the parent by the weighted average number of ordinary shares outstanding during the period.

In each case, the weighted average number of shares takes into account the weighted average number of own shares held during the period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

15 Earnings Per Share continued

The following reflects the income and share data used in calculating EPS:

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 Restated See note 2 $M
Profit / (loss) for the period attributable to the equity holders of the Company	26.9	(60.9)
Adjusted Operating Profit for the period attributable to the equity holders of the Company (see note 5)	109.0	58.3
Total tax charge	(26.7)	(19.9)
Reverse tax impact of:		
Net finance expense	(2.5)	(5.9)
Amortisation	(3.1)	(4.8)
Share-based payments	(7.4)	(8.5)
Exceptional items	(0.5)	(2.6)
Adjusted Operating Profit after tax	68.8	16.6

	Year-ended 31 March 2019	Year-ended 31 March 2018
Weighted average number of shares (000's):	476,320	459,969
Effects of dilution from:		
Share options	7,039	11,475
Restricted Share Units	10,397	17,125
Diluted	493,756	488,569

	$ Cents	$ Cents
Basic and diluted EPS	5.6	(13.2)
Diluted EPS	5.4	n/a
Adjusted operating EPS	14.4	3.6
Diluted adjusted operating EPS	13.9	3.4

16 Intangible Assets

	Goodwill $M	Intellectual Property $M	Software $M	Other $M	Total $M
Cost					
At 31 March 2017	809.5	388.3	37.1	265.3	1,500.2
Additions	–	14.8	6.1	–	20.9
Effect of movements in exchange rates	16.7	5.1	4.4	7.6	33.8
At 31 March 2018	826.2	408.2	47.6	272.9	1,554.9
Additions	–	–	4.7	–	4.7
Acquired through business combinations	12.2	20.8	–	–	33.0
Effect of movements in exchange rates	(52.9)	(3.7)	(3.2)	(6.0)	(65.8)
At 31 March 2019	785.5	425.3	49.1	266.9	1,526.8
Amortisation/Impairment loss					
At 31 March 2017	0.2	361.6	25.3	257.1	644.2
Charge for the year	–	13.4	8.1	3.7	25.2
Effect of movements in exchange rates	–	5.0	3.1	7.5	15.6
At 31 March 2018	0.2	380.0	36.5	268.3	685.0
Charge for the period	–	9.6	5.3	2.0	16.9
Effect of movements in exchange rates	–	(3.7)	(2.5)	(5.9)	(12.1)
At 31 March 2019	0.2	385.9	39.3	264.4	689.8
Net book value					
At 31 March 2018	826.0	28.2	11.1	4.6	869.9
At 31 March 2019	785.3	39.4	9.8	2.5	837.0

There has been no impairment to intangible assets held by the Group during the year.

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For the year-ended 31 March 2019

16 Intangible Assets continued

Goodwill

Following a review of the allocation of goodwill to foreign operations, the Directors have determined that goodwill of $543.1M which arose on the acquisition of the Group by APAX on 15 June 2010 should have been allocated differently. This element of the goodwill was previously denominated in US dollars and has now been allocated into functional currencies of the underlying foreign operations.

The re-denomination has given rise to a total reduction in the carrying value of goodwill of $39.3M, that has been recognised in the year-ended 31 March 2019. Had this allocation taken place from acquisition, a $36.0M increase in the carrying value would have been recognised in the year-ended 31 March 2018 and a cumulative decrease of $50.0M in the carrying value would have been recognised as at 31 March 2017. As this change has no impact on either the statement of profit or loss nor the statement of cash flows and as the net prior-period impact of $14.0M is not material in the context of the overall value of goodwill or net assets, it is, in the judgement of the Directors, appropriate to affect the change in allocation in the current period.

This change in the carrying value of $39.3M is a part of the $52.9M reflected in the line “effect of movements in exchange rates” in the table above. An equal and opposite entry is a part of the $33.7M recognised as “exchange differences arising on translation of foreign operations” in other comprehensive income, and subsequently the translation reserve in equity.

This adjustment has had no impact on the conclusion of the Group’s annual impairment review.

Other intangible assets

Intellectual property is amortised on a reducing balance basis over its estimated useful life of up to 15 years.

Software is amortised on a straight-line basis over three years.

Other intangibles comprise customer relationships, with a gross value of $247.4M and a net book value of $1.0M, and brand names with a gross value of $22.5M and a net book value of $1.5M.

Customer relationships are amortised on a reducing balance basis over a period of up to 14 years and brand names on a reducing balance basis over a period of up to 20 years.

The Group does not have any intangible assets with indefinite useful lives.

The Group has not capitalised development costs in the year-ended 31 March 2019 (2018: $Nil) as the Directors believe the criteria set out in IAS 38 have not been met. See note 4.

17 Impairment of Goodwill and Intangibles

Before recognition of impairment losses, the carrying amount of goodwill had been allocated as follows:

	31 March 2019 $M	31 March 2018 $M
Americas	273.6	288.2
EMEA	413.0	434.2
APJ	98.7	103.6
	785.3	826.0

Impairment of goodwill and intangible assets is tested annually, or more frequently where there is indication of impairment.

Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately in the Consolidated Statement of Profit or Loss.

Goodwill is considered impaired if the carrying value of the cash-generating unit to which it relates is greater than the higher of fair value less costs of disposal and the value in use.

For the year-ended 31 March 2019, the Directors have reviewed the value of goodwill based on internal value in use calculations. The key assumptions for these calculations are discount rates, growth rates and expected changes to billings and direct costs during the period.

The Group prepares cash flow forecasts derived from the Directors' most recent financial forecasts for the following five years. The growth rates for the five-year period are based on Directors' expectations of the medium-term operating performance of the cash-generating unit, planned growth in market share, industry forecasts, growth in the market and specific regional considerations and are in line with past experience. Discount rates have been estimated based on rates that reflect current market assessments of the Group's weighted average cost of capital.

The key assumptions used in the assessments in the year-ended 31 March 2019 are as follows:

	Americas	EMEA	APJ
Long-term regional growth rate beyond five years	2.5%	1.5%	2.0%
Discount rate	9.0%	9.0%	10.0%

The key assumptions used in the assessments in the year-ended 31 March 2018 were as follows:

	Americas	EMEA	APJ
Long-term regional growth rate beyond five years	2.5%	1.5%	2.0%
Discount rate	9.5%	9.5%	10.5%

As at 31 March 2019, there were no indicators of impairment that suggested the carrying amounts of the Group's long-lived assets are not recoverable. In order to assess the sensitivity in the assumptions made, the Directors have flexed the discount rate upward by thirty per cent of the above rates, and noted that this still did not give any indication of impairment.

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18 Property, Plant and Equipment

	Land and Buildings $M	Plant and Machinery $M	Fixtures and Fittings $M	Total $M
Cost				
As at 31 March 2017	15.0	36.9	4.9	56.8
Additions	0.9	7.8	1.3	10.0
Disposals	–	(0.4)	–	(0.4)
Effect of movements in exchange rates	5.4	4.0	0.6	10.0
As at 31 March 2018	21.3	48.3	6.8	76.4
Additions	2.6	8.6	1.6	12.8
Disposals	(0.1)	(0.3)	(0.1)	(0.5)
Effect of movements in exchange rates	(3.7)	(3.2)	(0.6)	(7.5)
As at 31 March 2019	20.1	53.4	7.7	81.2
Depreciation				
As at 31 March 2017	8.2	23.0	2.2	33.4
Charge for the year	2.6	8.1	0.9	11.6
Disposals	–	(0.3)	–	(0.3)
Effect of movements in exchange rates	3.1	2.8	0.4	6.3
As at 31 March 2018	13.9	33.6	3.5	51.0
Charge for the year	2.7	8.2	0.9	11.8
Disposals	–	(0.3)	–	(0.3)
Effect of movements in exchange rates	(2.2)	(2.6)	(0.4)	(5.2)
As at 31 March 2019	14.4	38.9	4.0	57.3
Net book value				
As at 31 March 2018	7.4	14.7	3.3	25.4
As at 31 March 2019	5.7	14.5	3.7	23.9

There has been no impairment to the property, plant and equipment held by the Group during the year.

19 Inventories

	31 March 2019 $M	31 March 2018 $M
Finished goods and goods for resale	10.6	16.0

The amount of write-down of inventories included as an expense within the Consolidated Statement of Profit or Loss was $2.0M (2018: $1.4M).

20 Trade and Other Receivables

Trade receivables are non interest-bearing and are generally on 30–90 day payment terms depending on the geographical territory in which sales are generated. The carrying value of trade and other receivables also represents their fair value. During the year-ended 31 March 2019 a provision for impairment of $0.6M (2018: $0.6M) was recognised in operating expenses against receivables.

	31 March 2019 $M	31 March 2018 Restated See note 2 $M
Current		
Trade receivables	128.7	151.8
Prepayments	26.9	23.1
Deferral of contract acquisition costs	31.5	29.5
Other receivables	8.2	6.4
Total current trade and other receivables	195.3	210.8
Non-current		
Deferral of contract acquisition costs	15.1	16.2
Other receivables	1.3	1.3
Total non-current trade and other receivables	16.4	17.5

The net contract acquisition expense deferred within the Consolidated Statement of Profit or Loss was $0.9M of the total $259.9M of Sales and Marketing costs (2018: $8.4M / $239.9M).

At 31 March 2019, trade receivables at a nominal value of $1.2M (2018: $0.9M) were impaired and fully provided for. Movements in the provision for impairment of receivables were as follows:

	31 March 2019 $M	31 March 2018 $M
At 1 April	0.9	0.4
Charge for the year	0.6	0.6
Amounts written off	(0.2)	(0.1)
Effects of movements in exchange rates	(0.1)	–
At 31 March	1.2	0.9

The analysis of trade receivables that were past due, but not impaired is as follows:

Up to three months	0.6	1.5
Three to six months	0.3	0.2
Greater than six months	–	1.0
Total	0.9	2.7

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21 Cash and Cash Equivalents

	31 March 2019 $M	31 March 2018 $M
Cash at bank and in hand	134.3	67.2
Short-term deposits	37.8	52.8
Total cash and cash equivalent	172.1	120.0

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates.

22 Trade and Other Payables

	31 March 2019 $M	31 March 2018 $M
Current		
Trade payables	35.8	39.6
Accruals	46.6	68.4
Social security and other taxes	12.7	14.9
Other payables	7.1	11.2
Total current trade and other payables	102.2	134.1
Non-current		
Other payables	10.1	8.2
Total non-current trade and other payables	10.1	8.2

Trade payables are non interest-bearing and are normally settled on 30-day terms or as otherwise agreed with suppliers.

23 Deferred Revenue

	31 March 2019 $M	31 March 2018 Restated See note 2 $M
Current	407.9	315.0
Non-current	320.7	238.8
At 1 April	728.6	553.8
Billings deferred during the year	760.3	768.6
Revenue released to the Consolidated Statement of Profit or Loss	(710.6)	(639.0)
Net deferral	49.7	129.6
Acquired through business combinations	0.2	–
Translation and other adjustments	(36.4)	45.2
Current	428.6	407.9
Non-current	313.5	320.7
At 31 March	742.1	728.6

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24 Financial Liabilities

The fair values of financial assets and liabilities are included at the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the end of the reporting period. The following methods and assumptions are used to estimate the fair values:

- Cash and cash equivalents – approximates to the carrying amount
- Finance leases – approximates to the carrying amount
- Bank loans – approximates to the carrying amount
- Receivables and payables – approximates to the carrying amount

Where financial assets and liabilities are measured at fair values their measurement should be classified into the following hierarchy:

- Level 1 – quoted prices (unadjusted) in active markets from identical assets or liabilities
- Level 2 – inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)
- Level 3 – inputs for the asset or liability that are not based on observable market data

The Group had a Level 3 financial liability of $7.5M of contingent consideration measured at fair value through profit and loss at 31 March 2019 (2018: $17.9M). The fair value of contingent consideration is determined using a probability-weighted average of outcomes discounted back to the acquisition date.

The primary unobservable inputs comprise the forecast billings ($Nil to $10.0M) and cumulative aggregate billings growth rate (47%) and the risk adjusted discount rate (4.0%). The estimated fair value would increase / (decrease) if the revenue growth rate was higher / (lower) or the risk adjusted discount rate was lower / (higher).

Total financial liabilities at the end of the reporting period were as follows:

	31 March 2019 $M	31 March 2018 $M
Contingent consideration	4.5	17.4
Total current financial liabilities	4.5	17.4
Non-current instalments due on bank loans	302.4	308.8
Unamortised facility fees	(2.6)	(2.5)
Contingent consideration	3.0	0.5
Total non-current financial liabilities	302.8	306.8
Total financial liabilities	307.3	324.2

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

24 Financial Liabilities continued

Loans and Borrowings

Included in borrowings are bank loans of $302.4M (2018: $308.8M) as analysed below. This note provides information about the contractual terms of the Group's interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Group's exposure to interest rate, foreign currency and liquidity risk, see note 26.

	31 March 2019 $M	31 March 2018 $M
Current instalments due on bank loans	–	–
Non-current instalments due on bank loans	302.4	308.8
Total bank loans	302.4	308.8

The bank loans are repayable as follows:

	31 March 2019 $M	31 March 2018 $M
Due within one year	–	–
Due between two and five years	302.4	308.8
Total bank loans	302.4	308.8

The Group entered into an amended Senior Facilities agreement on 6 February 2017, whereby an additional Revolving Credit Facility was added to the existing agreement. Following the amendment, the following terms apply to the bank loans outstanding at 31 March 2019:

Facility	Interest	Margin	Principal M	Principal $M
Facility – A	Libor	1.25%	$235.0	235.0
Facility – B	Euribor	1.25%	€60.0	67.4
Revolving Credit Facility 1	Libor	1.25%	–	–
Revolving Credit Facility 2	Libor	2.25%	–	–
				302.4

Repayment and Maturity

Facility A ($235.0M), Facility B (€60.0M), Revolving Credit Facility 1 (multicurrency up to $30.0M) are repayable in full on the termination date at the end of the 60-month term on 1 July 2020. Revolving Credit Facility 2 (multicurrency up to $40.0M) is repayable in full on the termination date on 2 July 2020.

Any utilisation of a Revolving Credit Facility is repayable on the last day of its interest period, any amount repaid may be re-borrowed. The margin payable on the facilities is dependent upon the ratio of the Group's net debt to Cash EBITDA as defined in the facility agreement.

The bank loans are secured by fixed and floating charges over the assets of certain Group companies including businesses, undertakings, securities, properties, revenues or rights of every description.

Contingent Consideration

Movements in contingent consideration during the year-ended 31 March 2019 were as follows:

Contingent Consideration	Avid Secure Inc. $M	Invincea, Inc. $M	Silent Break Security LLC $M	Reflexion Networks Inc. $M	Total $M
At 31 March 2017	–	19.4	1.2	1.1	21.7
Fair value contingent consideration	–	–	0.2	–	0.2
Accretion	–	0.6	0.2	0.1	0.9
Cash paid	–	(3.7)	–	(1.2)	(4.9)
At 31 March 2018	–	16.3	1.6	–	17.9
Fair value contingent consideration	–	(6.9)	–	–	(6.9)
Assumed on business combination	6.4	–	–	–	6.4
Accretion	–	–	0.1	–	0.1
Cash paid	–	(9.4)	(0.6)	–	(10.0)
At 31 March 2019	6.4	–	1.1	–	7.5

The undiscounted contingent consideration is due as follows:

	31 March 2019 $M	31 March 2018 $M
Due within one year	4.0	17.4
Due between two and five years	3.9	0.6
Total undiscounted contingent consideration	7.9	18.0

Avid Secure Inc.

As part of the purchase agreement with the previous owners of Avid Secure Inc., a contingent consideration has been agreed. The consideration is dependent on the billings of products including the intellectual property acquired with Avid Secure Inc. for the 24-month period to 5 January 2021, with a maximum payout of $6.7M. The fair value of the contingent consideration at the acquisition date was estimated at $6.4M. The contingent consideration is due for measurement to the former shareholders quarterly on 31 March, 30 June, 30 September and 31 December. The final measurement period is from 1 October 2020 to 5 January 2021.

Invincea, Inc.

As part of the purchase agreement with the previous owners of Invincea, Inc., a contingent consideration has been agreed. The consideration is dependent on the billings of products including the intellectual property acquired with Invincea, Inc. for the 12-month period to 21 March 2018 with a maximum payout of $20.0M. The fair value of the contingent consideration at the acquisition date was estimated at $19.3M. The contingent consideration is due for measurement to the former shareholders on 30 June 2017, 30 September 2017, 31 December 2017 and 21 March 2018 respectively. The final instalment was paid in the year-ended 31 March 2019.

Silent Break LLC

As part of the purchase agreement with the previous owners of the “PhishThreat” technology, a contingent consideration has been agreed. The consideration is dependent on the billings of the “PhishThreat” product range for three annual periods commencing 1 March 2017 and ending on 28 February 2020 with a maximum payout of $2.0M. The fair value of the contingent consideration at the acquisition date was estimated at $1.2M. The contingent consideration is due for measurement to the sellers on 28 February 2018, 2019 and 2020 respectively.

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25 Provisions

	Total $M
At 31 March 2017 – restated (see note 2)	2.5
Arising during the year	1.1
Released during the year	(0.4)
Exchange differences	0.1
At 31 March 2018	3.3
Arising during the year	4.4
Exchange differences	(0.1)
At 31 March 2019	7.6
31 March 2019	
Current	0.1
Non-current	7.5
Total provisions	7.6
31 March 2018	
Current	–
Non-current	3.3
Total provisions	3.3

Included in the carried forward provisions are $5.4M relating to provisions for interest on uncertain tax positions and $2.2M of other provisions.

Provision for Interest on Uncertain Tax Positions

A change in accounting policy adopted in FY19 resulted in interest on uncertain tax positions being accounted for within the interest charge instead of within the tax charge. An amount of $3.5M was charged in the current-year, compared to $0.9M in the prior-year, the increase consequent upon tax being provided on various open audits. Interest has been accrued from the point when the current tax charge arose.

Other Provisions

The opening provisions of $1.4M related to the Group's obligations to make good the dilapidations of various leasehold premises at the end of the lease periods and an unfunded, compulsory retirement indemnity plan in France, payable only if the employees are working for the Group when they retire. The provision arising in the year-ended 31 March 2019 related to further dilapidation charges of $0.9M (2018: $Nil) and in the year-ended March 2018 related to the retirement indemnity plan of $0.2M (2019: $Nil).

26 Financial Risk Management

Financial risk management is conducted at a Group level, applying treasury policies which have been approved by the Board. The major financial risks to which the Group is exposed relate to interest rate risk, credit risk and movements in foreign currency exchange rates. Where appropriate, cost effective and practicable, the Group uses various financial instruments to manage these risks. The main purpose of these financial instruments is to reduce the impact on the Group operations of changes in market rates. No speculative use of derivatives, currency or other instruments is permitted.

The Directors review and agree policies for managing each of these risks as summarised below:

Liquidity Risk

The Group prepares budgets annually in advance. This enables the Group's operating cash flow requirements to be anticipated and to ensure sufficient liquidity is available to meet foreseeable needs, financial obligations and to invest any surplus cash assets safely and profitably. Quarterly covenant tests are performed and monitored by the Directors at quarterly Board meetings.

The Group's objective is to maintain a balance between continuity of funding, minimising finance costs and maintaining flexibility through the use of short-term deposits and intra-group loan arrangements.

Capital Management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximise shareholder value.

The capital structure of the Group consists of cash and cash equivalents as disclosed in note 21, borrowings as disclosed in note 24 and equity attributable to equity holders of the parent, comprising issued capital, reserves and retained earnings, as disclosed in the Consolidated Statement of Changes in Equity.

The Group manages its capital structure, and makes adjustments to it, in light of changes in economic conditions. The Group reviews the capital structure on a regular basis and considers the cost of capital and the risks associated with each class of capital.

Credit Risk

The Group's principal financial assets are cash and bank deposits and trade and other receivables.

The Group's credit risk is primarily attributable to its trade receivables. In order to manage credit risk, the Directors set limits for customers based on a combination of payment history and third party credit references. Credit limits are reviewed by the credit controller on a regular basis in conjunction with debt ageing and collection history.

The amounts presented in the Consolidated Statement of Financial Position are net of allowance for doubtful debts. An allowance for impairment is made where there is an identified loss event which, based on previous experience, is evidence of a reduction in the recoverability of cash flows. The expense recognised in the Consolidated Statement of Profit or Loss in respect of doubtful debts during the period is disclosed in note 9.

The Group has no significant concentration of credit risk in trade receivables; exposure is spread over a large number of counterparties and customers.

With respect to cash and deposits, the Group's exposure to credit risk arises from the risk of default by the counterparty with a maximum exposure equal to the carrying amount of these assets. To mitigate this risk, cash and deposits are only held with reputable banking institutions. The Group reduces the concentrations of credit risk in cash and deposits by holding balances with a number of separate institutions, wherever possible with banks that are also lenders to the Group.

Interest Rate Risk

The Group is exposed to interest rate risk primarily due to the long-term debt obligations with floating rates of interest.

Interest Rate Sensitivity

A change of 100 basis points in market interest rates would have increased/(decreased) equity and profit and loss by the amounts shown below.

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Increase in interest rates	(3.1)	(3.3)
Decrease in interest rates	3.1	3.3

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26 Financial Risk Management continued

Foreign Currency Risk

The Group is exposed to translation and transaction foreign exchange risk. Several other currencies in addition to the reporting currency of US dollar are used, including sterling and the euro. The Group experiences currency exchange differences arising upon retranslation of monetary items (primarily short-term inter-Company balances and long-term borrowings), which are recognised as an expense in the period the difference occurs. The Group endeavours to match cash inflows and outflows in the various currencies; the Group typically invoices its customers in their local currency and pays its local expenses in local currency, as a means to mitigate this risk.

The Group is also exposed to exchange differences arising from the translation of its subsidiaries' Financial Statements into the Group's reporting currency of US dollar, with the corresponding exchange differences taken directly to equity.

The following table illustrates the movement that ten per cent in the value of sterling or the euro against the US dollar would have had on the Group's profit or loss for the period and on the Group's equity as at the end of the period.

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
10% movement in sterling to US dollar value		
Profit or loss	1.7	5.1
Equity	33.8	37.4
10% movement in euro to US dollar value		
Profit or loss	1.5	7.5
Equity	(9.8)	(10.8)

Any foreign exchange variance would be recognised as unrealised foreign exchange in the Consolidated Statement of Profit or Loss and have no impact on cash flows.

27 Share Capital

	Year-ended 31 March 2019		Year-ended 31 March 2018	
Shares issued and fully paid	**000's**	**$M**	**000's**	**$M**
At 1 April of £0.03 each	468,488	22.0	459,642	21.6
Issued for cash on exercise of options	3,631	0.5	3,445	0.4
Issued under the Sophos Group Long Term Incentive Plan 2015	9,751	–	5,401	–
At 31 March, Ordinary shares of £0.03	481,870	22.5	468,488	22.0

28 Distributions Made and Proposed

Cash dividends on ordinary shares declared and paid	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Final dividend for the year-ended 31 March 2017 at $0.033 per share	–	15.3
Interim dividend for the year-ended 31 March 2018 at $0.014 per share	–	6.5
Final dividend for the year-ended 31 March 2018 at $0.035 per share	16.7	–
Interim dividend for the year-ended 31 March 2019 at $0.015 per share	7.2	–
Total cash dividends paid	23.9	21.8

The Directors have proposed that the Company will pay a full-year dividend for the year-ended 31 March 2019 amounting to 3.7 US cents per share (2018: 3.5 US cents per share).

Proposed final dividends on ordinary shares are subject to approval at the Annual General Meeting, to be held on 25 August 2019, and are consequently not recognised as a liability at 31 March 2019.

29 Share-Based Payments

On 25 June 2015, and in connection with the reorganisation of the Group immediately prior to admission of the Company's shares for trading on the London Stock Exchange, participants with existing options outstanding under the Pentagon Holdings SARL approved share plans were offered to exchange their options for new options over shares in Sophos Group plc.

On 11 June 2015, and in connection with the admission of the Company's shares for trading on the London Stock Exchange, the Company's Board of Directors approved the following share-based payment plans:

The Sophos Group Long Term Incentive Plan 2015, ("2015 LTIP")

The 2015 LTIP plan aims to motivate and retain employees and align their interest with shareholders. Under the plan the Remuneration Committee of the Board can award the following types of awards: Performance Share Units, Restricted Share Units, Share Options, Conditional Share Awards, Cash-Based Awards or Forfeitable Shares.

Sophos Group SAYE Option Scheme 2015 ("SAYE")

The SAYE plan aims to encourage wider share ownership amongst UK employees of the Group by offering an HMRC approved share save scheme, whereby employees are offered options to buy shares at a discount following a pre-set savings period.

Sophos Group 2015 Employee Stock Purchase Plan ("ESPP")

The ESPP plan aims to encourage wider share ownership amongst US employees of the Group by offering options compliant with Section 423 of the Internal Revenue Code. Employees are offered options to buy shares at a discount following a pre-set savings period.

Sophos Group International SAYE Option Scheme 2015 "(International SAYE")

The International SAYE plan aims to encourage wider share ownership amongst the Group's employees outside of the UK and US by offering options to buy shares at a discount following a pre-set savings period.

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29 Share-Based Payments continued

Share-Based Payment Expense

The expense recognised for employee services received during the year is as follows:

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Cash-settled transactions	1.9	2.7
Equity-settled transactions	35.0	39.6
Total share-based payment expense	36.9	42.3

The cash-settled expense comprises cash-based awards together with certain social security taxes. The carrying value of the liability as at 31 March 2019 was $1.6M (2018: $3.1M).

Share Options

The fair value of equity-settled share options granted is measured as at the date of grant using a Black-Scholes model, taking into account the terms and conditions upon which the options were granted.

The following table illustrates the weighted average inputs into the Black-Scholes model in the year:

	Year-ended 31 March 2019	Year-ended 31 March 2018
Weighted average share price ($ cents)	676.10	628.23
Weighted average exercise price ($ cents)	558.54	516.70
Expected volatility	54.91%	38.20%
Expected life of options (years)	1.69	2.08
Risk free rate	1.56%	1.49%
Dividend yield	0.81%	0.70%

The weighted average fair value of options granted during the year was $ cents 220.53 (2018: $ cents 185.33).

The expected volatility reflects the assumption that the historical share price volatility is indicative of future trends, which may not necessarily be the actual outcome. An increase in the expected volatility will increase the estimated fair value.

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected life used in the model has been adjusted, based on the Director's best estimate, taking into account the effects of exercise restrictions, non-transferability and behavioural considerations. An increase in the expected life will increase the estimated fair value.

The number and weighted average exercise prices ("WAEP") of, and movements in, share options during the year are set out below:

	Year-ended 31 March 2019		Year-ended 31 March 2018	
	Number 000's	**WAEP £ pence**	**Number 000's**	**WAEP £ pence**
Outstanding at the start of the year	14,224	94.0	16,973	79.9
Awarded	1,258	377.8	1,667	317.2
Forfeited	(436)	283.3	(648)	138.6
Exercised	(3,840)	98.3	(3,768)	92.7
Outstanding at the end of the year	11,206	120.8	14,224	94.0
Exercisable at the end of the year	7,718	65.2	10,030	58.3

The weighted average share price for options exercised during the year was £ pence 506 (2018: £ pence 512).

Options outstanding at the end of the year had the following range of exercise prices and weighted average remaining contractual terms ("WARCT"):

	Exercise price $ cents / £ pence	31 March 2019		31 March 2018	
		Number 000's	**WARCT Years**	**Number 000's**	**WARCT Years**
	$ 47.5891	204	1.2	259	2.2
	$ 59.7813	5,566	3.7	8,134	4.7
	$ 70.7937	87	5.2	300	6.2
	$ 91.2452	17	5.2	23	6.2
	$ 155.7461	2,109	5.5	2,742	6.5
	$ 210.8078	355	5.9	371	6.9
	£ 162.0000	1,452	0.9	1,537	1.9
	£ 311.0000	440	0.3	–	–
	£ 371.0000	523	1.9	620	2.9
	£ 367.8800	–	–	238	0.3
	£ 462.0000	453	2.9	–	–
Outstanding at the end of the year		11,206		14,224	4.6

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

29 Share-Based Payments continued

Restricted Shares

The following table illustrates the number and weighted average share price ("WASP") on date of award of, and movements in, non-vested restricted shares in the year:

	Year-ended 31 March 2019		Year-ended 31 March 2018	
Restricted shares	**Number 000's**	**WASP $ cents**	**Number 000's**	**WASP $ cents**
Outstanding at the start of the year	64	155.75	127	155.75
Awarded	–	–	–	–
Forfeited	–	–	–	–
Vested	(64)	155.75	(63)	155.75
Outstanding at the end of the year	–	–	64	155.75

Restricted Share Units

The following table illustrates the number and WASP on date of award, and movements in, restricted share units ("RSUs") and cash-based awards granted under the 2015 LTIP:

	Year-ended 31 March 2019		Year-ended 31 March 2018	
Restricted share units	**Number 000's**	**WASP £ pence**	**Number 000's**	**WASP £ pence**
Outstanding at the start of the year	14,840	316.09	15,350	215.92
Awarded	8,749	478.44	6,337	453.14
Forfeited	(1,421)	426.11	(1,421)	284.15
Released	(6,822)	309.77	(5,426)	218.49
Outstanding at the end of the year	15,346	401.27	14,840	316.09

RSUs and cash-based awards have a vesting period between two to five years, with no award vesting within the first 12 months of the grant.

Performance Share Units

The following table illustrates the number and WASP on date of award, and movements in, performance share units ("PSUs") granted under the 2015 LTIP:

	Year-ended 31 March 2019		Year-ended 31 March 2018	
Performance share units	**Number 000's**	**WASP £ pence**	**Number 000's**	**WASP £ pence**
Outstanding at the start of the year	7,546	269.65	6,024	219.41
Awarded	1,721	506.74	1,719	440.50
Forfeited	(2,234)	414.51	(197)	223.96
Released	(2,949)	262.64	–	–
Outstanding at the end of the year	4,084	295.41	7,546	269.65

PSUs vest on one vesting date following a three year vesting period which will comprise three financial years. The awards are divided into three equal parts which will each be subject to a separate annual performance condition linked to the financial performance of the Group.

30 Pension Schemes

The Group contributes to defined contribution pension schemes in the UK and to similar or state pension schemes overseas for the benefit of the employees and Directors. The assets of the schemes are administered by trusts or other bodies in funds independent from the Group.

The pension cost charge for the period represents contributions payable by the Group to the funds and amounted to $8.9M (2018: $8.4M).

Contributions of $0.9M (2018: $1.3M) to the defined contribution pension scheme were outstanding, but not overdue, at 31 March 2019.

31 Related Party Transactions

The consolidated financial information includes the financial information of Sophos Group plc and the subsidiaries listed in the following table:

Country of incorporation	Subsidiary undertaking	Principal activity / registered address	Class of shares held	Percentage of shares held
Australia	Sophos Pty Ltd [3]	Selling IT security solutions *Level 11, 1 Elizabeth Plaza, North Sydney, NSW 2060, Australia*	Ordinary	100%
Canada	Sophos Inc [3]	Selling IT security solutions *3400, 350-7th Ave SW, Calgary AB T2P 3N9, Canada*	Common	100%
France	Sophos Sarl [3]	Selling IT security solutions *River Ouest, 80 Quai Voltaire, 95870 Bezons, France*	Ordinary	100%
Germany	Sophos Holdings GmbH [3]	Holding Company *Gustav-Stresemann-Ring 1, 65189 Wiesbaden, Germany*	Ordinary	100%
	Sophos Technology GmbH [4]	Research and Development *Amalienbadstr. 41/ Bau 52 76227 Karlsruhe, Germany*	Ordinary	100%
Hong Kong	Sophos Hong Kong Co Ltd [3]	Selling IT security solutions *18th Floor, Edinburgh Tower, The Landmark, 15 Queen's Road Central, Hong Kong*	Ordinary	100%
Hungary	Sophos Hungary Kft [3]	Research and Development *Aliz Utca, 1 Office Garden, Irodahaz A Epulet, 1117 Budapest, Hungary*	Ordinary	100%
India	Sophos Technologies Private Ltd [9]	Selling IT security solutions *Sophos House, Saigulshan Complex, Beside White House, Panchwati Cross Road, Ahmedabad 380006, Gujarat, India*	Ordinary	100%
	Avidsecure India Private Limited [11]	Services Company *H. No.140/7, Sector 7 Gurugram, Gurgaon, HR 122001, India*	Ordinary	100%
Ireland	Sophos Security Technology Ltd [3]	Research and Development *6th Floor, 2 Grand Canal Square, Dublin 2, Ireland*	Ordinary	100%
Italy	Sophos Italia Srl [3]	Selling IT security solutions *Corso Europa 2, 20122, Milano, Italy*	Ordinary	100%
Japan	Sophos KK [3]	Selling IT security solutions *Izumi Garden Tower 10F, 1-6-1 Roppongi, Minato-ku Tokyo 106-6010 Japan*	Ordinary	100%
Luxembourg	Aspen Finance Co Sarl [2]	Financing Company *1–3, Boulevard de la Foire, L-1528, Luxembourg*	Ordinary	100%

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

31 Related Party Transactions continued

Country of incorporation	Subsidiary undertaking	Principal activity / registered address	Class of shares held	Percentage of shares held
Netherlands	Sophos BV [3]	Selling IT security solutions	Ordinary	100%
		Hoevestein 11B, 4903 SE Oosterhout NB, Netherlands		
	SurfRight BV [8]	Selling IT security solutions	Ordinary	100%
		Lansinkesweg 4, 7553 AE Hengelo, Netherlands		
Singapore	Sophos Computer Security Pte Ltd [3]	Selling IT security solutions	Ordinary	100%
		60 Paya Lebar Road, #08-13 Paya Lebar Square, Singapore 409051		
Spain	Sophos Iberia Srl [3]	Selling IT security solutions	Ordinary	100%
		Ava Del General Peron, 38 – 8a Planta, Madrid 28020, Spain		
Sweden	Sophos AB [3]	Selling IT security solutions	Ordinary	100%
		Färögatan 33, 164 51 Kista, Stockholms län, Sweden		
Switzerland	Sophos Schweiz AG [3]	Selling IT security solutions	Ordinary	100%
		Bernstrasse 390, 8953 Dietikon, Switzerland		
	Astaro Trading AG [5]	Historical purchasing entity	Ordinary	100%
		c/o RA lic. jur. Hans Rudi Alder, Pestalozzistrasse 2 8200 Schaffhausen, Switzerland		
Taiwan	Sophos Taiwan Ltd [3]	Services Company	Ordinary	100%
		5F-4, No. 57, Sec. 1 Chongqing S. Road, Zhongzheng Dist., Taipei City 100 Taiwan (R.O.C.)		
Turkey	Sophos Turkey Technoji Ltd Sirketi [3]	Services Company	Ordinary	100%
		Barbaros Mah. Halk Cad., Palladium Residence (A Blok) Apt. No: 8 A / 4, Atasehir/Istanbul, Turkey		
UK	Sophos Holdings Ltd [1]	Holding Company	Ordinary	100%
	Sophos Treasury Ltd [2]	Financing Company	Ordinary	100%
	Sophos Limited [2]	Selling IT security solutions	Ordinary	100%
	Sophos Nominees Limited [3]	Share nominee company	Ordinary	100%
		The Pentagon, Abingdon Science Park, Abingdon, OX14 3YP, UK		
USA	Sophos Inc [3]	Selling IT security solutions	Ordinary	100%
		3 Van de Graaff Drive, 2nd Floor, Burlington, MA 01803, USA		
	Cyberoam Inc [6]	Services Company	Ordinary	100%
		Corporation Service Company, Princeton South Corporate Ctr, Suite 100, Charles Ewing Blvd, Ewing, 08628, USA		
	Reflexion Networks Inc [7]	Selling IT security solutions	Ordinary	100%
		1209 Orange St, Wilmington, County of New Castle DE 19801, USA		
	Invincea, Inc [7]	Selling IT security solutions	Ordinary	100%
	Sandboxie Holdings, LLC [10]	Services Company	Ordinary	100%
	Avid Secure Inc. [7]	Services Company	Ordinary	100%
		Corporation Service Company, 251 Little Falls Drive, Wilmington, DE 19808, USA		
	Darkbytes, Inc. [7]	Services Company	Ordinary	100%
		22390 Ortega Dr, Salinas CA 93908, USA		

1 Shares held by Sophos Group Plc
2 Shares held by Sophos Holdings Ltd
3 Shares held by Sophos Limited
4 Shares held by Sophos Holdings GmbH
5 Shares held by Sophos Technology GmbH
6 Shares held by Sophos Technologies Private Ltd
7 Shares held by Sophos Inc
8 Shares held by Sophos BV
9 Shares held by Sophos Limited and Sophos Nominees Limited
10 Shares held by Invincea, Inc
11 Shares held by Avidsecure Inc.

Other Related Parties

During the year the Group entered into transactions, in the ordinary course of business with other related parties.

During the year-ended 31 March 2019, no provisions were made for doubtful debts under IFRS 9 relating to amounts owed by related parties (2018: $Nil). As at 31 March 2019 no amounts were owed to or from related parties other than subsidiary companies (2018: $Nil).

Sales and purchases between related parties are made at normal market prices. Outstanding balances with entities other than subsidiaries are unsecured, interest free and cash settlement is expected within 60 days of invoice. Terms and conditions for transactions with subsidiaries are the same, with the exception that balances are placed on inter-company accounts with no specified credit period.

The Group has not provided or benefitted from any guarantees for any related party receivables or payables.

The Company and certain subsidiaries have provided unsecured guarantees to certain third parties within the normal course of business, the majority of which were in favour of certain lenders in respect of some of the Group's borrowing facilities. As at 31 March 2019, these guarantees totalled $302.4M (2018: $308.8M) relating to the Group's financing facilities.

Compensation of Key Management Personnel (Including Directors)

	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Short-term employee benefits	6.6	9.1
Post-employment benefits	0.1	0.1
Share-based payments - equity-settled	10.4	17.7
Total	17.1	26.9

Short-term employee benefits comprise fees, salaries, benefits and bonuses earned during the year as well as non-monetary benefits.

Post-employment benefits comprise the cost of providing defined contribution pensions to senior management in respect of the current period.

Share-based payments comprise the cost of senior management's participation in share-based payment plans for the period as measured by the fair value of awards in accordance with IFRS2.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

32 Business Combinations

On 5 January 2019, Sophos Inc. acquired for cash 100 per cent of the share capital of Avid Secure Inc., a company incorporated in Delaware, United States. The acquisition is significantly strengthening the Group's portfolio of cloud protection technology including cloud governance, risk and compliance.

Acquisition-related expenses of $0.3M have been excluded from the consideration transferred and have been recognised as an expense within General finance and administration.

Assets acquired and liabilities assumed on the day of acquisition were as follows:

	Book value $M	Adjustment $M	Fair value $M
Non-current assets:			
Intangible assets			
Intellectual property	–	14.6	14.6
Current assets:			
Trade and other receivables	0.2	–	0.2
Cash and cash equivalents	0.4	–	0.4
Non-current liabilities:			
Deferred tax liability	–	2.7	2.7
Current liabilities:			
Deferred revenues	0.2	–	0.2
Trade and other payables	0.1	–	0.1
Net assets recognised at the date of acquisition	0.3	11.9	12.2
Cash paid			13.9
Contingent consideration			6.4
Goodwill arising on acquisition – Avid Secure Inc.			8.1

Prior to the acquisition, Avid Secure Inc. operated in a complimentary market sector to the Group and, accordingly, the operations of Avid Secure Inc. are incremental to those of the Group. The impact of the acquisition of Avid Secure Inc. on the Operating Profit of the Group for the period-ended 31 March 2019 was insignificant. Had Avid Secure Inc. been owned since 1 April 2018, revenue for the year-ended 31 March 2019 would have increased over the reported revenue by approximately $0.3M. The impact on the Operating Profit of the Group would have been approximately $0.1M.

On 28 January 2019, Sophos Inc. acquired for cash 100% of the share capital of Darkbytes, Inc., a company incorporated in California, United States. The acquisition is significantly strengthening the Group's foundational technology for a Managed Detection and Response ("MDR") solution.

Acquisition-related expenses of $0.2M have been excluded from the consideration transferred and have been recognised as an expense within General finance and administration.

Assets acquired and liabilities assumed on the day of acquisition were as follows:

	Book value $M	Adjustment $M	Fair value $M
Non-current assets:			
Intangible assets			
Intellectual property	–	6.2	6.2
Current assets:			
Cash and cash equivalents	0.1	–	0.1
Non-current liabilities:			
Deferred tax liability	–	1.1	1.1
Current liabilities:			
Trade and other payables	0.1	–	0.1
Net assets recognised at the date of acquisition	–	5.1	5.1
Cash paid			7.5
Deferred consideration			1.7
Goodwill arising on acquisition – Darkbytes, Inc.			4.1

Prior to the acquisition, Darkbytes, Inc. operated as a technology start-up and, accordingly, the operations of Darkbytes, Inc. are incremental to those of the Group. The impact of the acquisition of Darkbytes, Inc. on the Operating Profit of the Group for the period-ended 31 March 2019 was insignificant. Had Darkbytes, Inc. been owned since 1 April 2018, the impact on both revenue and Operating Profit for the year-ended 31 March 2019 would have been immaterial.

Goodwill arose in all the above business combinations because the cost of the combination included amounts in relation to the benefit of expected synergies, future market development and the assembled workforce. These benefits are not recognised separately from goodwill because they do not meet the recognition criteria for identifiable intangible assets. None of the goodwill recognised is expected to be deductible for income tax purposes.

The Group did not enter into any business combinations during the year-ended 31 March 2018.

33 Notes to the Consolidated Statement of Cash Flows

Acquisition of subsidiaries net of cash acquired	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Consideration paid, satisfied in cash:		
– Darkbytes, Inc.	7.5	–
– Avid Secure Inc.	13.9	–
– Invincea, Inc.	9.4	3.7
– Intellectual Property – Silent Break Security	0.6	–
– Reflexion Networks Inc.	–	1.2
Net cash purchased	(0.5)	–
Acquisition of subsidiaries net of cash	30.9	4.9

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

For the year-ended 31 March 2019

33 Notes to the Consolidated Statement of Cash Flows continued

Movement in net debt	31 March 2018 $M	Cash flow $M	Non-cash movements $M	Effect of movements in exchange rates $M	31 March 2019 $M
Cash and cash equivalents	(120.1)	(60.7)	–	8.7	(172.1)
Obligations under finance leases	–	–	–	–	–
Bank loans	306.3	–	(0.1)	(6.4)	299.8
Gross debt	306.3	–	(0.1)	(6.4)	299.8
Net debt	186.2	(60.7)	(0.1)	2.3	127.7

Movement in net debt	31 March 2017 $M	Cash flow $M	Non-cash movements $M	Effect of movements in exchange rates $M	31 March 2018 $M
Cash and cash equivalents	(68.1)	(45.2)	–	(6.8)	(120.1)
Obligations under finance leases	0.1	(0.1)	–	–	–
Bank loans	345.6	(50.1)	1.1	9.7	306.3
Gross debt	345.7	(50.2)	1.1	9.7	306.3
Net debt	277.6	(95.4)	1.1	2.9	186.2

34 Commitments and Contingent Liabilities

Operating lease arrangements	Year-ended 31 March 2019 $M	Year-ended 31 March 2018 $M
Amount recognised for the year:		
Property	14.0	12.5
Other	1.6	1.6
Total	15.6	14.1

At the reporting date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	31 March 2019 $M	31 March 2018 $M
Within one year	15.3	14.0
In the second to fifth years inclusive	41.3	34.8
After five years	21.1	19.7
Total	77.7	68.5

Commitments for the Acquisition of Property, Plant and Equipment

At 31 March 2019 the Group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to $0.5M (2018: $Nil).

Guarantees

At 31 March 2019 the Group had outstanding guarantees provided to third parties of $1.6M (2018: $1.3M).

Legal Proceedings

The Group is involved in a number of legal and compliance proceedings that are incidental to our business. Although it is possible that adverse decisions (or settlements) may occur in one or more of the cases, it is not currently possible to estimate the potential loss or losses. The final outcome of these proceedings, individually or in the aggregate, is not expected to have a material impact on the business.

In line with previous periods, litigation is currently in process against various entities within the Group. Allegations related to patents have been made with claims for unspecified damages. In addition, The Group is also investigating apparent non-compliance with certain regulatory matters pertaining to the use of some of the Group's products in certain overseas territories.

In accordance with IAS 37.92, the Group does not provide further information on the grounds that this could seriously prejudice the outcome of the litigation. The Directors are of the opinion that the current claims against the Group can be successfully resisted; and is fully co-operating with the relevant regulatory bodies in relation to any matters of apparent regulatory non-compliance.

35 Principal Exchange Rates

Principal exchange rates	Year-ended 31 March 2019	Year-ended 31 March 2018
Translation of sterling into US dollar ($:£1.00)		
Average	1.3183	1.3264
Closing	1.3031	1.4028
Translation of euro into US dollar ($:€1.00)		
Average	1.1636	1.1664
Closing	1.1229	1.2299

When calculating performance measures on a constant currency basis, the Group uses the closing balance sheet rate of the previous year.

36 Events After the Reporting Period

There are no material events after the reporting period which require disclosure in accordance with IAS10.

COMPANY ONLY STATEMENT OF FINANCIAL POSITION

At 31 March 2019

Company registered number: 09608658	Note	31 March 2019 $M	31 March 2018 $M
Non-current assets			
Deferred tax asset		7.5	8.8
Investments in subsidiary undertakings	3	1,130.6	1,099.1
Loan due from subsidiary	4	93.5	93.5
		1,231.6	1,201.4
Current assets			
Amounts due from subsidiaries		30.0	27.8
Total current assets		30.0	27.8
Total assets		1,261.6	1,229.2
Current liabilities			
Amounts due to subsidiaries		67.4	46.7
Total current liabilities		67.4	46.7
Net assets		1,194.2	1,182.5
Represented by:			
Share capital	5	22.5	22.0
Share premium		126.6	122.3
Retained earnings		919.4	946.1
Share-based payment reserve		125.7	92.1
Total equity		1,194.2	1,182.5

These Financial Statements were approved by the Board of Directors on 15 May 2019 and were signed on its behalf by:

Nick Bray

Chief Financial Officer

COMPANY ONLY STATEMENT OF CHANGES IN EQUITY

At 31 March 2019

	Share Capital $M	Share Premium $M	Retained Earnings $M	Share-Based Payment Reserve $M	Total $M
At 31 March 2017	21.6	118.4	977.1	55.6	1,172.7
Loss for the period:	–	–	(9.2)	–	(9.2)
Other comprehensive profit or loss:	–	–	–	–	–
Total comprehensive loss	–	–	(9.2)	–	(9.2)
Share options exercised	0.4	3.9	–	–	4.3
Share-based payments - expense	–	–	–	39.6	39.6
Share-based payments - tax	–	–	–	(3.1)	(3.1)
Cash dividend	–	–	(21.8)	–	(21.8)
At 31 March 2018	22.0	122.3	946.1	92.1	1,182.5
Loss for the period:	–	–	(2.8)	–	(2.8)
Other comprehensive profit or loss:	–	–	–	–	–
Total comprehensive loss	–	–	(2.8)	–	(2.8)
Share options exercised	0.5	4.3	–	–	4.8
Share-based payments - expense	–	–	–	35.0	35.0
Share-based payments - tax	–	–	–	(1.4)	(1.4)
Cash dividend	–	–	(23.9)	–	(23.9)
At 31 March 2019	22.5	126.6	919.4	125.7	1,194.2

The Directors believe that the retained earnings of the Company are all distributable.

NOTES TO THE COMPANY ONLY STATEMENTS

For the year-ended 31 March 2019

1 Principal Accounting Policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's Financial Statements.

Basis of Preparation

The Company and its trading subsidiaries have considerable financial resources and a large number of customer contracts across different geographic areas and industries. As a consequence, the Directors believe the Company is well placed to manage its business risks successfully.

The Company operates as an investment company for the Sophos Group, holding investments in subsidiaries financed by Group companies. As the Company is an intrinsic part of the Group's structure, the Directors have a reasonable expectation that Group companies will continue to support the Company through trading and cash generated from trading for the foreseeable future. Thus the Group continues to adopt the going concern basis in preparing the Financial Statements.

The Financial Statements have been prepared in accordance with Financial Reporting Standard 102 ("FRS 102") and under the historical cost accounting rules.

Under section 408 of the Companies Act 2006, the Company is exempt from the requirement to present its own profit and loss account.

The Company is considered to be a qualifying entity for the purposes of FRS 102 and has applied the exemptions available under FRS 102 in respect of the cash flow statement and key management personnel compensation.

As the Consolidated Financial Statements of the Company include the equivalent disclosures, the Company has also taken the exemptions available under FRS 102 in respect of disclosures in respect of share-based payments, financial instruments and the requirements of Section 33 Related Party Disclosures paragraph 33.7.

Investments

Investments in subsidiary undertakings are stated at cost less any provision for impairment.

Foreign Currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account. Non-monetary assets and liabilities denominated in foreign currencies are stated at historical foreign exchange rates.

Interest-Bearing Loans and Borrowings

Obligations for loans and borrowings are recognised when the Company becomes party to the related contracts and are measured initially at fair value less directly attributable transactions costs. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses arising on the repurchase, settlement or otherwise cancellation of liabilities are recognised respectively in finance income and finance expense.

Going Concern Basis

The Company operates as an investment company for the Sophos Group, holding investments in subsidiaries financed by Group companies. As the Company is an intrinsic part of the Group's structure, the Directors have a reasonable expectation that Group companies will continue to support the Company through distribution or debt/financing supported by trading and cash generated. Thus the Group continues to adopt the going concern basis in preparing the Financial Statements.

2 Profit and Loss Account

The loss after tax dealt with in the books of the Company was $2.8M (2018: $9.2M). Under section 408 of the Companies Act 2006 the Company is exempt from the requirement to present its own profit and loss account.

3 Investments

	31 March 2019 $M	31 March 2018 $M
Investment in Sophos Holdings Limited	1,035.8	1,035.8
Investment in Sophos Limited	94.8	63.3
At 31 March	1,130.6	1,099.1

The investment in Sophos Holdings Limited, a holding company for the Sophos Group, comprises 100% of the ordinary share capital.

The investment in Sophos Limited comprises share-based payment expenses for equity awards granted to participants employed by Sophos Limited and its subsidiaries.

4 Loan Due From Subsidiary

As part of the re-financing of the Group on 1 July 2015, the Company lent $93.5M to Sophos Holdings Limited, a wholly owned subsidiary.

The loan carries a variable interest rate based on the Group's Senior Facility A loan plus a margin of 0.1% and is repayable in full at the end of a 60-month term on 1 July 2020.

5 Share Capital

	Year-ended 31 March 2019		Year-ended 31 March 2018	
Shares issued and fully paid	**000's**	**$M**	**000's**	**$M**
At 1 April of £0.03 each	468,488	22.0	459,642	21.6
Issued for cash on exercise of options	3,631	0.5	3,445	0.4
Issued under the Sophos Group Long Term Incentive Plan 2015	9,751	–	5,401	–
At 31 March, Ordinary shares of £0.03	481,870	22.5	468,488	22.0

6 Functional Currency

Sophos Group plc is registered in England and Wales and has a functional currency of US dollars.

GLOSSARY

Adjusted Operating Profit	Adjusted Operating Profit represents the Group's Operating Profit/(loss) adjusted for amortisation charges, share option charges and exceptional items
AES	Advanced Encryption Standard
Americas	North and South America
APJ	Asia-Pacific and Japan
ARR	Annual Recurring Revenue, being the annualised equivalent of term licenses, subscription agreements and maintenance contracts including OEM and MSP but excluding perpetual licenses
Billings	Billings represents the value of products and services invoiced to customers after receiving a purchase order from the customer and delivering products and services to them, or for which there is no right to a refund
Blue chip	Channel partners who transact five or more deals in a trailing six-month period
Board	The Board of Directors of Sophos Group plc
BYOD	Bring Your Own Device
CAGR	Compound annual growth rate
Cash EBITDA	Cash EBITDA is defined as the Group's Operating Profit adjusted for depreciation and amortisation charges, any gains or losses on the sale of tangible and intangible assets, share option charges, unrealised foreign exchange differences and exceptional items with billings replacing revenue
Cash EBITDA margin	Cash EBITDA margin is calculated as Cash EBITDA as a percentage of Billings
Channel first	The distribution model used by the Group, where products are sold to end customers through a network of channel partners and distributors
Company	Sophos Group plc
Constant currency	The group uses US dollar-based constant currency models to measure performance. These are calculated by applying a single exchange rate to local currency transactions for both the current and prior-year. This gives US dollar denominated measures that exclude variances attributable to foreign exchange rate movements
Deep Learning	An advanced form of machine learning inspired by the way the human brain works. It is the same type of machine learning often used for facial recognition, natural language processing, self-driving cars, and other advanced fields of computer science and research
Directors	The Executive and Non-Executive Directors of the Company
DPI	Deep Packet Inspection
EBITDA	Earnings before interest, taxation, depreciation and amortisation
EMEA	Europe, Middle East and Africa
Enduser / end user	Enduser being a sub-set of the Group's products; end user being the ultimate user and customer of the Group's products
GHG	Greenhouse gas
Group	The group of companies owned by Sophos Group plc
HTML5	The fifth revision of the HyperText Markup Language of the internet used for structuring and presenting content for the world wide web
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
KPI	Key Performance Indicator
MSP	Managed Service Provider
Next-gen	The Group's most advanced products, managed in Sophos Central, notably including Sophos Intercept X for endpoint protection and the Sophos XG Firewall
OEM	Original Equipment Manufacturer
RED	Remote Ethernet Device
Renewal rate	Renewal rates are calculated by comparing the US dollar amount of contracts renewed in a period (including instances of cross-sell and upsell) to the US dollar amount of contracts available for renewal in the period
Retention rate	Retention rates are calculated by comparing the US dollar amount of contracts renewed in a period (including instances of cross-sell and upsell) to the US dollar amount of total contracts at the start of the period
Secure SSL	Secure Sockets Layer, a standard security technology for establishing an encrypted link between a server and a client
Unlevered free cash flow	Unlevered free cash flow represents cash EBITDA less purchases of property, plant and equipment and intangibles, plus cash flows in relation to changes in working capital and taxation
UTM/NGFW	Unified Threat Management/Next-Generation Firewall
VAR	Value-Added Reseller
VPN	Virtual Private Network
Weighted average contract length	Weighted average contract length is calculated on a last 12-month basis, at constant currency and provides an indication of the period over which future revenue will be recognised

COMPANY INFORMATION

Directors

Peter Gyenes
Kris Hagerman
Nick Bray
Sandra Bergeron
Roy Mackenzie
Rick Medlock
Vin Murria
Paul Walker

Registered office and corporate headquarters

Sophos Group plc
The Pentagon,
Abingdon Science Park,
Abingdon, OX14 3YP,
United Kingdom.

Tel: +44 1235 559933
www.sophos.com
Registered number: 09608658
Registered in England and Wales

Registrar Services

Link Asset Services
34 Beckenham Road,
Beckenham,
BR3 4TU.

Investor Relations

investors.sophos.com
investor.relations@sophos.com

Public Relations

Tulchan Communications
85 Fleet Street,
London,
EC4Y 1AE.

Auditor

KPMG LLP
15 Canada Square,
London,
E14 5GL.

SHAREHOLDER INFORMATION

Share listings

The Ordinary shares are listed on the London Stock Exchange under the symbol SOPH: www.londonstockexchange.com

Shareholder services

Shareholder Portal

To access online information about your shareholdings visit www.signalshares.com. The website also provides information useful to the management of investments together with an extensive schedule of frequently asked questions. In order to view your shareholdings the shareholder reference number is required which can be found at the top of the share certificate or on the last dividend tax voucher.

Alternatively, you can contact Link's Customer Support Centre which is available to answer any queries you have in relation to your shareholding:

- By email
  enquiries@linkgroup.co.uk
- By post
  Link Asset Services, The Registry, 34 Beckenham Road, Beckenham, Kent, BR3 4TU.
- By phone
  UK – 0871 664 0300, from overseas call +44 (0) 371 664 0300 calls cost 12p per minute plus your phone company's access charge. Calls outside the United Kingdom will be charged at the applicable international rate. Link are open between 09:00–17:30, Monday to Friday excluding public holidays in England and Wales.

Share price information

The latest information on Sophos Group plc share price can be found on the Company's website: investors.sophos.com.

Electronic communications

Receiving the Company's communications electronically allows the Company to communicate with its shareholders in a more environmentally friendly way which supports our commitments to sustainability.

Be scam smart

Investment scams are designed to look like genuine investments.

Spot the warning signs

Have you been:

- contacted out of the blue?
- promised tempting returns and told the investment is safe?
- called repeatedly?
- told the offer is only available for a limited time? If so, you might have been contacted by fraudsters.

Avoid investment fraud

Reject cold calls:
If you have received unsolicited contact about an investment opportunity, the chances are it is a high-risk investment or a scam. You should treat the call with extreme caution. The safest thing to do is to hang up.

Check the FCA Warning List:
The FCA Warning List is a list of firms and individuals they know are operating without their authorisation.

Get impartial advice:
Think about getting impartial financial advice before you hand over any money. Seek advice from someone unconnected to the firm that has approached you.

Report a scam

If you suspect that you have been approached by fraudsters please tell the FCA using the reporting form at www.fca.org.uk/ consumers/report-scam-unauthorised-firm. You can also call the FCA Consumer Helpline on 0800 111 6768.

If you have lost money to investment fraud, you should report it to Action Fraud on 0300 123 2040 or online at www.actionfraud.police.uk

Find out more at www.fca.org.uk/scamsmart

Financial calendar

Announcement of results

The results of the Group are normally published at the following times:

- Half-year results for the six months to 30 September in mid-November.
- Preliminary announcement for the year to 31 March in late May.
- Annual Report and Accounts for the year to 31 March in mid-June.

Dividend payments

Our current policy is to make dividend payments at the following times:

- Interim dividend in December.
- Final dividend as reasonably practicable following the AGM, which in 2019 is on 25 September.

2019 final dividend timetable:

- Record date: 20 September.
- Dividend paid: 11 October.

Cautionary statement

This Annual Report and Accounts has been prepared for, and only for, the members of Sophos Group plc ("the Company"), as a body, and no other persons. The Company, its Directors, employees, agents or advisers do not accept or assume responsibility to any other person to whom this document is shown or into whose hands it may come and any such responsibility or liability is expressly disclaimed. By their nature, the statements concerning the risks and uncertainties facing the Group in this Annual Report and Accounts involve uncertainty since future events and circumstances can cause results and developments to differ materially from those anticipated. The forward-looking statements reflect knowledge and information available at the date of preparation of this Annual Report and Accounts and the Company undertakes no obligation to update these forward-looking statements. Nothing in this Annual Report and Accounts should be construed as a profit forecast.

Designed and produced by emperor
Visit us at emperor.works

SOPHOS

Cybersecurity evolved

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