COSTAIN GROUP PLC ANNUAL REPORT 2014

MEETING NATIONAL NEEDS

150 years of pioneering solutions

For 150 years, Costain has been engineering solutions for major infrastructure projects. We understand what it takes to innovate and deliver pioneering solutions which meet national needs.

1935

In 1935 Costain was a true pioneer in international construction and built 11 miles of the Trans-Iranian Railway – seven tunnels and two viaducts in isolated mountainous terrain.

1944

Costain played a major part in wartime innovation by helping to create the Mulberry Harbour which was used to land troops on the Normandy beaches in 1944.

1982

Thames Barrier, lead Contractor on

one of the largest

movable flood barriers in the world.

1993

Channel Tunnel Joint Venture, founder member of the longest undersea tunnel in the world.

2011

Next Generation Carbon Capture.

Fulfilling a lead role

in developing technology capable of reducing CO_2 emissions by 95%.

2011

High Speed 2 rail link,

acting consultant

providing buildability advice.

2012

E.ON Holford, underground gas storage. Playing a

highly significant

role in UK gas delivery.

2013

The Big Infrastructure Conversation, in collaboration with BITC,

brought industry leaders together

to tackle youth unemployment.

2016

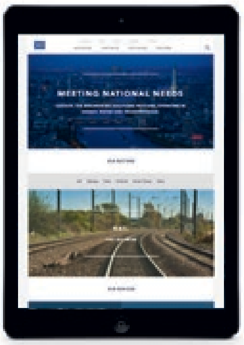
Evaporator D Project, Sellafield (completing 2016)

Largest nuclear decommissioning project in the UK.

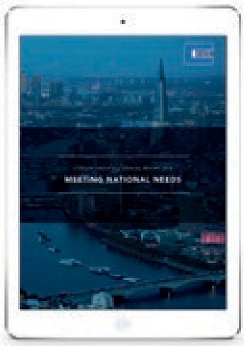
Costain 2014

By focusing on meeting essential national needs, we will realise our vision of being one of the UK's top engineering solutions providers which in turn will create sustainable value for all our stakeholders.

Other sources of information



Costain.com



Annual Report online

Key to icons in this report

- More information available online
- Related information in this report
- Key performance indicators
- Advisory and concept development
- Specialist design
- Programme management
- Complex project delivery
- Technology integration
- Asset optimisation and support

Contents

Who we are and what we do

Costain is an engineering solutions provider delivering integrated consulting, project delivery and operations and maintenance services, with a portfolio of achievements spanning 150 years of innovation and technical excellence. We meet essential national needs by providing world-class engineering and technology-led solutions to our blue-chip customers in the UK's energy, water and transportation markets.

Go to costain.com for more

Our business is split into two core operating and reporting divisions, Infrastructure and Natural Resources.

I

Infrastructure

The infrastructure division delivers engineering solutions in:

Rail
Delivering end-to-end asset life-cycle solutions across the entire railway, from major station projects to multi-disciplinary rail projects.

Highways
Providing end-to-end highways services and delivering technology-led solutions for our customers.

Power
Playing a significant role in safely delivering the energy infrastructure that will satisfy the UK's future needs.

NR

Natural Resources

The Natural Resources division delivers engineering solutions in:

Water
Providing engineering solutions to UK water utility companies across the asset life-cycle.

Nuclear
Creating the facilities to manage nuclear waste safely using the latest technology-led solutions.

Oil & Gas
Providing full life-cycle engineering services in the development, design, delivery and maintenance of Oil & Gas infrastructure.

Go to page 31 for Divisional review

Integrated solutions across six service lines

To reflect our value proposition, and as we continue to broaden our services and enhance our product range, we have evolved our business architecture to meet the changing need of our major blue-chip customers.

Advisory and concept development

The development of solutions and options for our customers' most pressing problems.

Specialist design

Complex and niche engineering solutions.

Programme management

The operational and commercial management of programmes of complex interrelated projects.

Complex project delivery

The engineering and management of the delivery of large complex infrastructure projects.

Technology integration

Providing a service through technology to manage, connect and transform infrastructure assets.

Asset optimisation and support

Long-term contracts to operate and maintain physical infrastructure assets.

ENERGY
WATER
TRANSPORTATION

Focusing on essential national needs

Find out more about our business model on page 18

TRANSPORT

INTEGRATED TECHNOLOGY IS SMARTER FOR EVERYONE

Services: Technology integration

Customer: Highways Agency

Electronic Service Delivery for Abnormal Loads (ESDAL2)

The Highways Agency appointed Costain to deliver a technology solution that would improve the service for road users moving Abnormal Indivisible Loads (AIL) around Britain's highways. As part of the technology solution, Costain provides a hosted software application with access provided via web portals to the Highways Agency, hauliers, police, and bridge and highways authority users. The solution includes the provision of a help desk to support system users and to manage and maintain the solution. The collaboration provided by the web portals boosts efficiency and eliminates wasted time and effort on the part of hauliers and the authorities. It also enables the Highways Agency's Abnormal Loads Team to collaborate with stakeholders to plan routes and authorise Special Orders for the largest movements.

"We now provide one integrated system which is faster and far more friendly for all users. It's having a very real and positive effect on our roads."

James Bulleid, Highways Technology Director, Costain, NEF Innovation of the Year (above)

Find out more about our business model on page 18

Customer: Thames Water UK

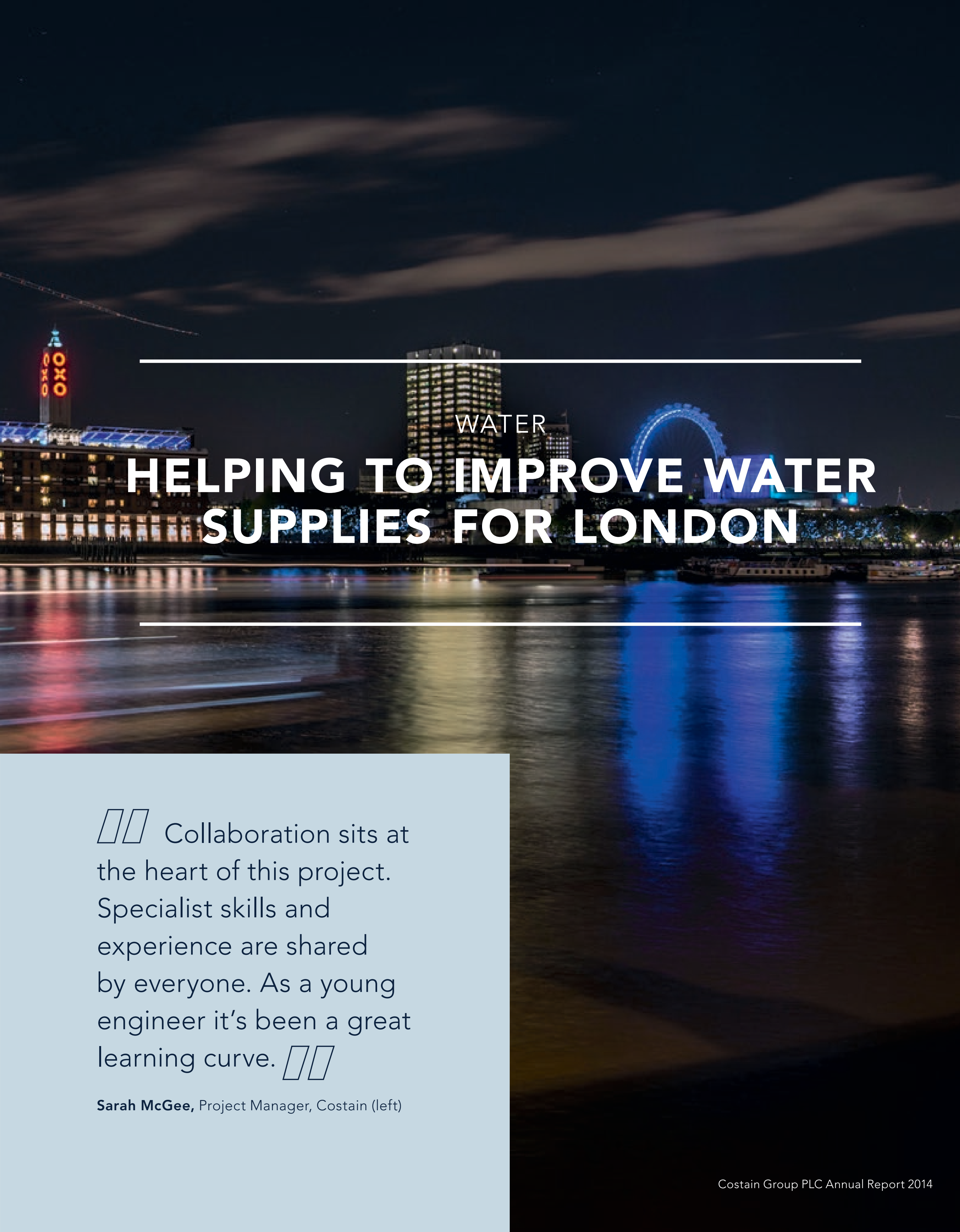
AMP6 Capital Programme

Costain, part of Thames Water's industry-leading eight$_2$O alliance, will help deliver billions of pounds of essential improvements to Thames Water's ageing network over the AMP6 period. To date, Costain has provided key members of the eight$_2$O management team and has played a significant role in the development of programme strategy and approach to standardisation and offsite manufacture. As the programme moves into delivery, Costain together with its partner Atkins, will be responsible for delivering half of the overall capital programme. Thames Water is using the alliance model to achieve greater efficiency in the delivery of its business plan, with a greater emphasis on collaborative team-working, innovation, sustainability and an integrated supply community, in a bid to lock in long-term value to the company and its customers.

Services: | **Advisory and concept development** | **Specialist design** | **Complex project delivery**

WATER

HELPING TO IMPROVE WATER SUPPLIES FOR LONDON



"Collaboration sits at the heart of this project. Specialist skills and experience are shared by everyone. As a young engineer it's been a great learning curve."

Sarah McGee, Project Manager, Costain (left)

Find out more about our business model on page 18

Customer: Magnox

Bradwell FED Treatment Project

Costain delivered the engineering, procurement, construction and commissioning of the Bradwell Fuel Element Debris (FED) Treatment Project, which is part of the decommissioning programme taking Magnox's Bradwell site into a long-term state of care and maintenance.

FED is the most significant solid Intermediate Level Waste (ILW) hazard, by volume, stored on Magnox sites. Costain's application of innovative thinking and extensive industry experience has resulted in the development of an innovative dissolution process which dissolves FED waste in nitric acid, greatly accelerating the accepted process using carbonic acid. This process has been shown to reduce the volume of FED waste by over 90%. This form of hazard reduction will make a significant contribution to the nuclear waste legacy clean up in the UK.

> This process reduces the amount of waste, the associated long-term storage costs and has lower environmental impacts. I am proud to be a part of it.

Fernando Campos, Process Engineer, Costain (left)

Services:

- Advisory and concept development
- Specialist design
- Programme management
- Complex project delivery
- Technology integration

ENERGY

REDUCING THE IMPACT OF NUCLEAR WASTE IN THE UK

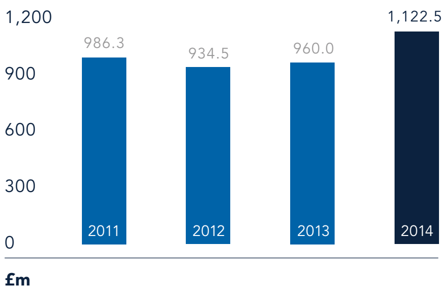
Highlights
Strategy delivering results

Go to page 41 for more

Financial highlights

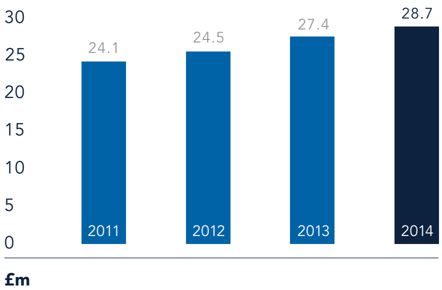
Revenue[1]

£1,122.5m



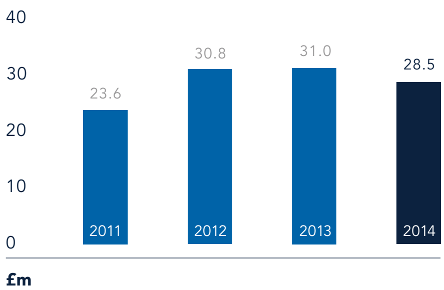
Underlying operating profit[2]

£28.7m



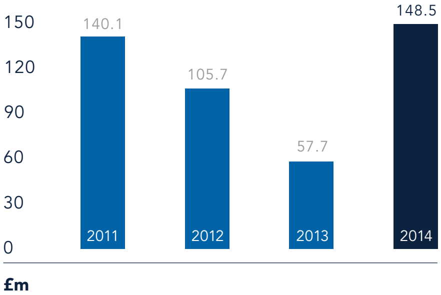
Adjusted profit before tax[3]

£28.5m



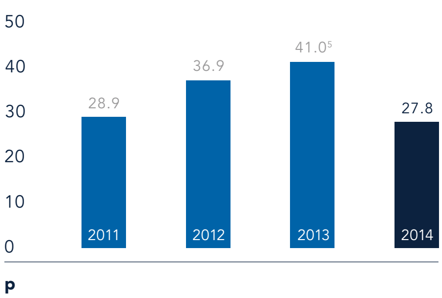
Net cash balance

£148.5m



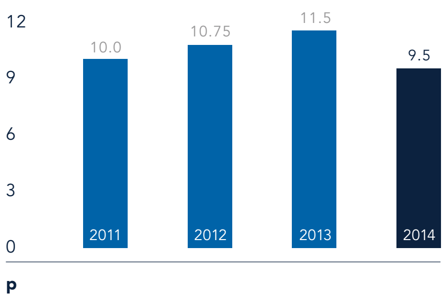
Adjusted basic earnings per share[3]

27.8p



Dividend per share

9.5p



	2014	2013
Revenue[1]	**£1,122.5m**	£960.0m
Operating Profit		
– Underlying[2]	**£28.7m**	£27.4m
Profit before tax		
– Adjusted[3]	**£28.5m**	£31.0m
– Reported	**£22.6m**	£12.9m
Basic earnings per share		
– Adjusted[3]	**27.8p[4]**	41.0p[5]
– Reported	**22.2p[4]**	17.6p[5]
Net Cash balance	**£148.5m**	£57.7m
Dividend per share	**9.5p[4]**	11.5p

[1] Including share of joint ventures and associates.

[2] Underlying operating profit before Other items; amortisation of acquired intangible assets and employment related and other deferred consideration and in 2013, £3.7m one-off costs associated with the offer for May Gurney Integrated Services plc.

[3] Results stated before Other items (as stated in 2 above) and in 2013 a non-cash impairment of £9.8m on the carrying value of assets in non-core Land Development activity in Spain.

[4] On the enlarged capital base following the capital raise completed in March 2014.

[5] Restated for the bonus element of the capital raise completed in March 2014.

These are the definitions used throughout the Strategic report.

Operational highlights

Her Majesty the Queen opened Reading Station after the critical redevelopment project was handed over ahead of schedule.

Examples of Contract Awards

1. Appointed by Network Rail as one of four suppliers to the £2 billion National Electrification Programme
2. Appointed to three transmission frameworks with National Grid to provide a broad range of services, including front end engineering design, programme management, construction and asset optimisation
3. Secured a place on the Highways Agency's five-year Collaborative Delivery Framework for the improvement of England's motorways and major A roads
4. Contract, awarded by Perenco, to deliver Engineering, Procurement and Construction services for the environmental upgrade of the Dimlington gas terminal on Humberside
5. Appointed by Southern Water to help deliver its 2015 – 2020 (AMP6) investment programme
6. Awarded a contract by Scottish Water to construct the Shieldhall Tunnel in Glasgow
7. Appointed by BAE Systems as one of its framework contractors on the eight-year, £300m-plus programme to redevelop its submarine site, in Barrow-in-Furness, Cumbria

Environmental and social highlights

Employee engagement

75%

of employees think Costain is a great place to work

Go to page 34 for more

RoSPA Awards

29

29 Awards: one Order of Distinction, seven Gold Medals, 17 Gold Awards, 4 Silver Awards

CO_2 emissions

24,692T CO_2e

94% waste diverted from landfill

Go to page 34 for more

Chairman's statement


David Allvey, Chairman

I am delighted to report that Costain had another year of strong performance and made further progress in its corporate development.

Delivering growth

The rigorous implementation of our *'Engineering Tomorrow'* strategy has delivered increases in revenue, underlying operating profit and a record forward order book which now stands at £3.5 billion.

Across the business we have continued to create and deliver innovative solutions to help address critical national needs in energy, water and transportation.

We successfully completed a capital raise of £70.3 million (net of expenses) to enable the business to take greater advantage of opportunities in its chosen markets and thereby accelerate the Group's medium and long-term growth prospects.

Dividend

At the time of the capital raise, the Group confirmed that it intended to continue with a progressive dividend policy, targeting an ongoing dividend cover of around two times underlying earnings.

Our performance and confidence in the long-term prospects for the Group has resulted in the Board recommending a final dividend of 6.25 pence per share on the capital base enlarged by the capital raise completed in March (2013: 7.75 pence per share). On a pro forma basis, allowing for the issue of new shares in connection with the capital raise, this represents an increase of approximately 25% in the total amount of dividend paid to shareholders compared with the total dividend for 2013.

Governance

As Chairman, my priority is to ensure the effectiveness of the Board and, once again, we made good progress in delivering against our objectives. During the year, an externally facilitated evaluation of Board performance was conducted and actions were agreed to further improve the effectiveness of the Board.

Go to page 45 for more

In 2014, we welcomed two new independent Directors to the Board. Alison Wood joined Costain as a Non-Executive Director in February, succeeding Mike Alexander as Chair of the Remuneration Committee when he retired from the Board in March. We were also pleased to announce the appointment of David McManus as a Non-Executive Director in May.

Corporate citizenship

We have an outstanding team at Costain, one that takes its role in society and its corporate responsibility very seriously.

In 2015, Costain is celebrating its 150th anniversary and, to help mark this special occasion, we are undertaking the Costain 150 Challenge, which will change many people's lives by raising £1 million for the Costain Charitable Foundation's four chosen charities: British Heart Foundation, Macmillan Cancer Support, The Prince's Trust and Samaritans. A number of fundraising events are taking place across the business.

Outlook

We have delivered another strong performance, with increases in revenue and underlying operating profit and an enhanced net cash position.

Costain has an established reputation for innovative multi-disciplined services that enables the Group to win large, long-term contracts addressing the UK's national needs in energy, water and transportation.

This strong market position and the additional capital secured during the year is enabling the Group to accelerate its growth, as demonstrated by a record order book of £3.5 billion.

David Allvey
Chairman
02 March 2015

Chief Executive's review

Andrew Wyllie, CBE, Chief Executive

This has been another good year for Costain, the engineering solutions provider.

Through our unique and focused *'Engineering Tomorrow'* strategy we have successfully positioned the business to provide the range of innovative integrated services demanded by our customers to meet critical national needs in energy, water and transportation.

During the year, we added to our skills and breadth of capability, developed our market proposition through the introduction of new technologies and ensured that we consistently delivered on the commitments given to our customers.

Our capability was further enhanced in March when we successfully completed a capital raise of £70.3 million (net of expenses).

The proceeds are being utilised for a number of purposes including: ensuring the requisite financial capacity to support anticipated further increases in contract size and duration; investing in innovation and technology; financing bid costs; and, providing flexibility to make selected in-fill acquisitions to complement Costain's existing capabilities as opportunities arise.

Market trends and developments

There is growing consensus across the political spectrum of the explicit link between investment in a 21st century infrastructure and the creation of sustainable economic growth and global competitiveness.

The UK Government's 2014 National Infrastructure Plan has set out an overall investment of over £320 billion to 2020-21 in an identified pipeline of projects in the UK, including a further £15 billion announced in December 2014 on road infrastructure.

Go to page 26 for more

The UK market is further defined by significant and long-term planned expenditure programmes underpinned by committed regulated spend and essential capital investment. With the majority of this total investment expected to continue to come from the private sector, the opportunities in our markets are substantial.

At the same time, and as we anticipated, the changing nature and increasing complexity of the requirements of the major customers in these markets continues to change fundamentally the way in which they procure services and work with their supplier partners.

These trends have created a rapidly changing and dynamic market environment in which further consolidation has taken place and is expected to continue.

Unique *'Engineering Tomorrow'* strategy

We have been successfully implementing our unique and evolving *'Engineering Tomorrow'* strategy for a number of years. Our target customers are large organisations that need solutions to their complex business requirements.

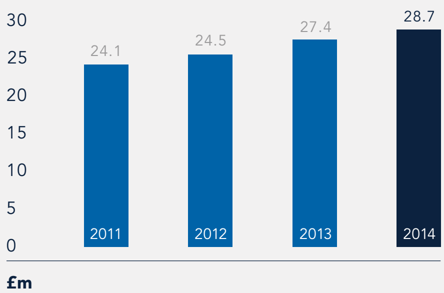
We are a trusted delivery partner that collaborates strategically at all levels with our customers. We use our detailed customer understanding to create and deliver innovative engineering and technology-led solutions.

We win by developing insightful and trusted relationships with our customers, enabling a better understanding of their needs and allowing us to identify, create and deliver the best solution. Our strategy is profitable because our customers value our long-term commitment to the relationships and trust us to address their challenges in a collaborative and innovative way.

Chief Executive's review
continued

Underlying operating profit

£**28.7**m



We sustain our competitive advantage by delivering on our promises and staying ahead using our customer insight to constantly improve our proposition.

Our major customers, who are spending and will continue to spend billions of pounds in meeting national infrastructure needs, are consolidating their supply chains as they seek to derive business benefits by working in a more strategic and collaborative manner with a reduced number of preferred Tier One providers through larger longer-term contracts. To be successful in the future we must continue to grow the business, both organically and by targeted acquisition, to ensure that we have the scale and capability to satisfy the full range of their service needs for increasingly complex and large-scale projects.

Innovation driving value

Engineering, technology and innovation are in the DNA at Costain.

We recognise that no customer will buy the same product, with the same attributes at the same price point year after year. It is therefore essential that we continuously improve the products and services that we provide and enhance value for our customers.

Our ability to develop and offer innovative solutions – often ones which our customers have not previously considered – is a fundamental differentiator. It drives our ability to secure very high levels of repeat business with major customers who regard Costain as a long-term partner in the development, delivery and optimal operation of their assets.

Our contracts now involve a significant amount of collaboration amongst the supply chain, our partners and external stakeholders, such as researchers and universities, utilising the latest information-sharing software and technology.

We have research and development relationships established with eight leading universities and have continued to progress a number of patent applications. We also moved 400 people into our new engineering centre in Manchester.

£3.5bn

record forward order book

Innovations, in collaboration with partners, which have added value to our customers' businesses this year, include:

- Use of the Costain 'WeCARE' system for predictable pre-planned and cost-effective Technology Asset Maintenance using data analytics;
- Creation of 3-D models utilising 3-D printing technologies to articulate complex engineering solutions;
- Application of manufacturing assembly best practice to achieve significantly accelerated project delivery and cost savings.

Good operating results and strong cash position

Revenue, including the Group's share of joint ventures and associates, for the year increased to £1,122.5 million (2013: £960.0 million), circa 30% of which was derived from support service related activities.

Group underlying operating profit increased to £28.7 million (2013: £27.4 million).

Adjusted profit before tax was £28.5 million (2013: £31.0 million); the reduction is due to the significant profit generated in 2013 on the sale of the Group's minority shareholdings in three joint ventures. Adjusted basic earnings per share was 27.8 pence (2013: 41.0 pence), the lower level also reflecting the enlarged capital base following the capital raise completed in March 2014.

The Infrastructure division had an excellent year with increases in revenue, operating profit and order book. The Natural Resources division delivered an operating profit excluding the impact of a provision associated with the legacy Greater Manchester Waste PFI contract awarded in 2007, as detailed in the Divisional review.

The Group's net cash position at 31 December 2014 was £148.5 million (2013: £57.7 million). The increase in the net cash position reflects the successful £70.3 million (net of expenses) capital raise in March, and benefitted from the timing of positive contract cash flows at the period end. As previously highlighted, the Group's net cash position has changed as we continue to increase our workload with major customers who utilise lower-risk target-cost, cost-reimbursable contracts. The average month-end net cash was £95.6 million (2013: £50.7 million) and we anticipate small increases from this level going forward.

Record order book

The ability to provide and integrate a wide range of multidisciplined skills and services, along with our strong market position and reputation for innovation, has enabled us to secure over £1.5 billion worth of large and complex projects and contract extensions during the course of the year which include:

- the delivery of Network Rail's National Electrification Programme;
- appointment to the Highways Agency's Collaborative Delivery Framework;
- a position on three transmission frameworks for National Grid;
- a framework contract with BAE Systems for their submarine site redevelopment programme;
- appointment by Southern Water for their AMP6 investment programme;
- the delivery of EPC services for the upgrade of the Dimlington gas terminal for Perenco.

Consequently, the Group's order book has further increased, finishing the year at a new record level of £3.5 billion (31 December 2013: £3.0 billion).

As well as including over £1.0 billion of revenues secured for 2015 (as at 31 December 2013: over £750 million secured for 2014), the order book also provides good long-term visibility with £2.5 billion of revenues secured for 2016 and beyond.

Chief Executive's review
continued

The increasingly strategic nature of Costain's long-term customer relationships has ensured that over 90% of the order book comprises repeat business and, given the complexity of the customer's requirements, over 90% is in a target cost, cost reimbursable, collaborative forms of contract providing good long-term earnings visibility. The Group also has a strong preferred bidder position increased to over £500 million.

Such a level of secured work gives us good reason to look to the future with confidence, especially as the level of active tendering across all our target markets remains high.

The Group's tender success rate is now better than one in three of all opportunities pursued, a win-rate that has improved significantly as a consequence of the implementation of our strategy to focus on the needs of major customers. These customers are increasingly procuring contracts on a larger and longer-term basis, reflected in the fact that over 70% of the Group's order book is for contracts or frameworks with a remaining value in excess of £100 million. The average life of a contract in the Group has increased considerably in the last few years and is now over four years in duration.

'Costain Cares'

Our customers continue to place great emphasis on the 'good citizen' credentials of their supply chain partners. Given the profile of their businesses and the nature of the activities we undertake, how we deliver our services is as important to them as what we do. Increasingly, customers insist that their Tier One providers share their corporate and social responsibility values and failure to embrace this means non-qualification for tender lists.

The management of Health and Safety is a core value at Costain. We place a priority on the management of Safety, Health and Environment, and the Group's Accident Frequency Rate (AFR) improved to 0.10 (2013: 0.12), which compares favourably with our peer group. We also received 17 Gold Awards from RoSPA, seven Gold Medals and a prestigious Order of Distinction. Notwithstanding the improved performance, and in view of the prosecution and fine for Health and Safety breaches following the death in 2011 of a subcontract worker at a site in Newbury, we recognise that there is still more we must do to achieve our objective of zero accidents.

Our 'Costain Cares' programme places responsible, effective and collaborative stakeholder relationships at the core of everything we do. It is a central part of our value proposition to customers and has a direct impact on the size and quality of our order book.

In the year, we retained our Platinum status in the Business in the Community index, recognising our proactive commitment to the environmental and social aspects of our operations.

Costain further improved its position in the annual assessment by Management Today magazine of Britain's Most Admired Companies, ranking 52nd overall, up from 55th the previous year.

Teamwork

We adopt a 'One Costain' philosophy across the Group, and that is evident in the way in which our team of over 3,500 people work together to deliver an outstanding service to customers and deliver strong business performance.

We have continued to develop and enhance skills across the business and there are currently 179 graduates and 80 apprentices on our structured development programmes.

During the year, David Taylor was appointed to the Executive Board as Group Commercial Director, replacing Patrick Bruce who is retiring from the Group in March 2015 after over 40 years of service.

Outlook

We have delivered a strong performance, and successfully completed a capital raising to enable the Group to accelerate its growth. We are excited by the many opportunities that lie ahead and, with an outstanding team and record order book, we look forward to reporting on further progress in 2015.

Andrew Wyllie CBE
Chief Executive
02 March 2015

Group Executive Board
Driving our strategy

The Executive Board has primary authority for the day-to-day management of the Group's operations, following policies laid down by the Group Board. It consists of the Executive Directors and other senior managers and is chaired by Andrew Wyllie, Chief Executive. The members of the Executive Board are:

Andrew Wyllie CBE
Chief Executive

Anthony Bickerstaff
Finance Director

Tim Bowen
Corporate Development Director

Martin Hunter
Group Financial Controller

Darren James
Managing Director – Infrastructure

David Taylor
Group Commercial Director

Alex Vaughan
Managing Director – Natural Resources

Tracey Wood
Legal Director and Company Secretary

Our business model

We have a unique *'Engineering Tomorrow'* strategy of partnering with major blue-chip customers with very complex requirements. Together we are meeting essential national needs that in turn will create long-term sustainable value for our investors and all our other stakeholders.

The resources we call on to run our business

Human – the skills, experience, productivity, diversity and excellence of our people enable us to operate safely, reliably and efficiently and to deliver our projects on time and within budget.

Social and relationship – maintaining quality relationships with all our stakeholders is fundamental to creating and sustaining our business.

Intellectual – our knowledge-based assets give us a key competitive advantage that underpins our growth ambitions.

Financial – the financial resources (through shareholder capital, retained profits, debt and cash generation) we need to run our business and fund our activities.

Primary activities

1. Unique customer focus

We target customers and markets where there is committed regulated spend and essential capital investment, addressing essential national needs and that have a total investment spend of more than £87 billion.

- Water: £12.0bn
- Power: £12.6bn
- Nuclear: £5.8bn
- Highways: £7.7bn
- Rail: £26.0bn
- Oil & Gas: £23.0bn

2. Range of innovative services

By maintaining and developing the capabilities and services our customers demand through the whole life, end-to-end life-cycle of their assets, we ensure we meet their complex business challenges.

- Advisory and concept development
- Specialist design
- Programme management
- Complex project delivery
- Technology integration
- Asset optimisation and support

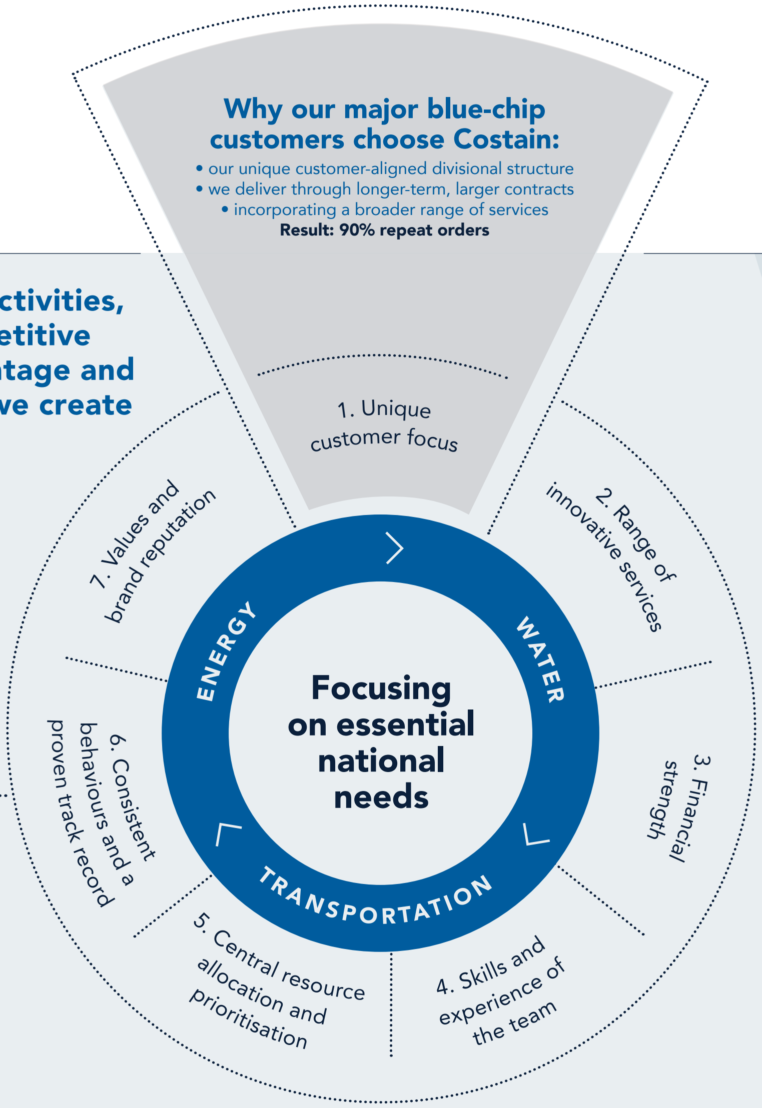
3. Financial strength

We target blue-chip customers with longer-term, larger contracts and extensions. We have an order book worth £3.5 billion and a repeat order rate of over 90%. More than 90% of our business is made up of low-risk, target-cost, cost-reimbursable contracts. This combination gives us long-term stability and sustainability of revenue and earnings.

4. Skills and experience of the team

Our experts deliver innovative, efficient and value-driven solutions for customers. It is vital that we attract, develop and retain individuals with world-class expertise. We invest significantly in developing and broadening the skills and capabilities of our team.

Our activities, competitive advantage and how we create value



Our outputs and goals

Vital national infrastructure solutions

See the case studies on pages 04 – 09.

Financial goals – create long-term growth and returns for shareholders.

For more go to page 41.

Non-financial goals – build a sustainable business that creates economic, environmental and social value.

For more go to page 34.

Our competitive advantage

5. Central resource allocation and prioritisation

In managing our central resource allocation to prioritise and optimise asset deployment we ensure:

- Effective and efficient resource allocation
- Targeted business development activities
- Performance management

6. Consistent behaviours and a proven track record

We have a proven track record of reliable, safe service delivery. We consistently demonstrate all the vital attributes our customers and stakeholders expect to see in their partners.

- Operating our business safely, sustainably and responsibly through our Costain Cares programme
- Continuing to develop a range of innovative solutions
- Building skilled and experienced teams
- Maintaining financial strength and stability

7. Values and brand reputation

We have a respected brand and reputation amongst our peers and customer base. We are recognised as one of the UK's best known and most admired companies sitting at 52nd place in the league table organised by Management Today magazine.

Performing responsibly is integral to our success and to the sustainability of our business. Our set of values drives our behaviour and provides the basis for all our decisions. Everyone at Costain is committed to being:

- Customer focused
- Open and honest
- Safe and environmentally aware
- Team players
- Accountable
- Innovative – improving continuously and therefore the…
- Natural choice

Quick links

Go to costain.com for more

Engineering tomorrow: **Our strategic priorities**

Our strategic focus is to enhance our growth and market position by providing innovative and sustainable solutions to increasingly complex and large-scale national needs. Our *'Engineering Tomorrow'* strategy will ensure we remain competitive and continue to deliver shareholder value.

Priority	Measure	Target
1. Operating safely, efficiently and responsibly The Health and Safety of our people and everyone who is involved with Costain remains our highest priority. We demand that safety must be adhered to at all times to ensure that we operate in an environment which is free from harm. We concentrate on solutions that deliver best value for customers. This requires an unrelenting focus on our customers' costs and our own operating procedures. We believe that responsible business is integral to delivering greater value to our customers and all our stakeholders. Our commitment to delivering services responsibly and sustainably is vitally important to the Group. We are focused on building a long-term sustainable business that creates economic, environmental and social value.	KPI Accident Frequency Rate ('AFR')	To continually improve safety performance with a zero tolerance approach
	KPI CO_2 equivalent emissions	To reduce our measured emissions
	KPI Underlying operating profit	In line with business plan
	KPI Net cash balance	Maintain a net cash balance at an appropriate level to suit the business requirements
2. Continue to enhance customer insight The ability to understand the challenges facing our customers is crucial if we are to strengthen and evolve our relationships with them. Continuing to enhance our customer insight is one of our top priorities and it is by building strategic, long-term, collaborative partnerships that we are best positioned to deliver innovative solutions to these customers. Additional value is delivered to both customers and end users by operating efficiently with a strong focus on speed and agility and an uncompromising attitude to safety. We recognise that talented, integrated and accountable project teams are fundamental to maximising the opportunities presented by unique customer insights.	KPI Repeat business	In line with business plan
	Customer satisfaction	Enhance customer engagement to gain a greater insight into our performance

In accordance with the requirements of the Companies Act 2006 (Strategic and Directors' Report) Regulations 2013, the Group has adjusted its carbon reporting boundaries.

Emissions under this regulation cover scope 1 and 2 emissions for all Costain Group activities, including overseas interests and joint ventures, in which the Company has a 50% or greater financial stake. In 2015, we will continue to expand our scope of reporting to ensure that we incorporate all scope 1 and 2 emissions where Costain has a financial interest.

Performance

AFR, 2014

0.10

2013 total 14,365 tCO_2e
Scope 1 10,474 tCO_2e
Scope 2 3,891 tCO_2e
Emissions intensity 14.85

2014 total 24,692 tCO_2e
Scope 1 20,600 tCO_2e
Scope 2 4,092 tCO_2e
Emissions intensity 21.99

Underlying operating profit, 2014

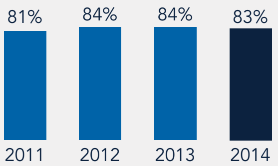
£28.7m

Net cash balance, 2014

£148.5m

Repeat business, 2014

+90%



Customer satisfaction, 2014

83%

Our focus in 2015

- Continuous improvement in the group AFR towards our goal of zero harm
- Increase the proportion of Costain staff who have had a medical within the last two years

- Reduce measured carbon emissions intensity by 55% by 2020 (against 2009 baseline)

- Continue to increase the Group's underlying operating profit in line with the business plan

- Maintain a focus on cash management

Continue to build strategic relationships with our customers, gaining deeper insights into their business challenges

Use the latest technology to increase the frequency and depth of our customer engagement and feedback

Principal risks and uncertainties

- Health, Safety and Environmental
- Operational delivery
- Financial strength
- Pension liabilities
- Failure of IT systems

Go to page 28 for more

- Political, economic and market conditions
- Winning new work
- Operational delivery

Go to page 28 for more

Engineering tomorrow: **Our strategic priorities**

continued

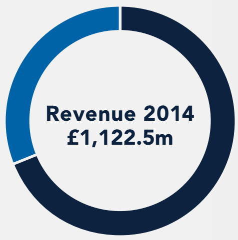
Priority	Measure	Target
3. Grow by broadening and integrating our services We continue to deliver engineering services across the full asset life-cycle, from advisory and design to operations and maintenance, to broaden and enhance our service offering. We have developed our value proposition across six core service lines in an increasingly integrated offering to customers: advisory and concept development, specialist design, programme management, complex project delivery, technology integration, asset optimisation and support.	KPI Order book	To build a strong order book in line with the business plan
	KPI Revenue	In line with business plan
4. Develop best-in-class team Attracting, retaining and developing the best people for Costain is key to our success. We continue to grow and enhance our capability in line with our customers' needs for the relevant skills for today and tomorrow. By investing in a diverse, knowledgeable and highly capable workforce, with transferable skills, we can be sure that we have a pipeline of talent throughout the business.	Staff turnover	To provide initiatives and working conditions in order to retain key staff
	KPI Diversity and inclusion	To value diversity and inclusion in the workforce
	Investment in training and development	To grow skills and capabilities in line with the business plan

Performance

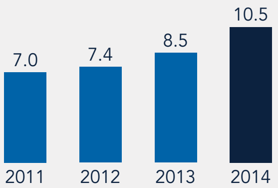
Order book value, 2014

£3.5bn

70% Programme delivery
30% Support services related activities



69% Programme delivery
31% Support services related activities



Staff turnover, 2014

10.5%

Outer pie chart	Middle pie chart	Inner pie chart
UK employees	**Board members**	**Senior Management**
Female 645	Female 1	Female 12
Male 2,743	Male 6	Male 120
Total 3,388	Total 7	Total 132

Outer pie chart	Middle pie chart	Inner pie chart
UK employees	**Board members**	**Senior Management**
Female 681	Female 2	Female 14
Male 2,857	Male 6	Male 155
Total 3,538	Total 8	Total 169

10,000+ training days, 2013

£3.0m invested

14,318 training days, 2014

£3.4m invested

Our focus in 2015

Increase revenue and order book across our six core service lines

Continue to grow organically and through acquisition

Deliver key actions resulting from the 2014 employee engagement survey

Deliver unconscious bias training across the business (rolled over from 2014)

Continue to broaden the skills and capabilities of our workforce

Principal risks and uncertainties

- Political, economic and market conditions
- Financial strength
- Winning new work
- Operational delivery
- Mergers and acquisitions

Go to page 28 for more

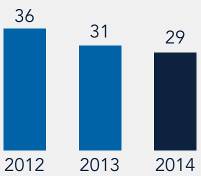
- People and skills
- Financial strength

Go to page 28 for more

Engineering tomorrow: **Our strategic priorities**
continued

Priority	Measure	Target
5. Create and deliver innovative sustainable solutions We are focused on creating intelligent, sustainable solutions that improve the performance of our customers' businesses. We invest in research, innovation and emerging technology to provide customers with new services that reduce impact on the communities we serve. By aligning our pipeline of innovation to our customer challenge, we are able to work closely with them through every stage of development.	Number of patents used to deliver new high value service to our customers	Increase the number of patents in line with the business plan
	Number of innovations	Continue to extract innovative solutions through an open innovation programme
6. Working in collaboration Partnering and collaboration form a central part of our approach. Both are essential in delivering complex engineering and services. In a market where collaboration continues to deliver value, Costain focuses on developing strategic partnerships to support the development of broader services and technology.	KPI Supply chain performance	Average key supplier performance score greater than 50%
	Collaborative contracts	Increase the % of work in lower risk, cost-reimbursable contracts

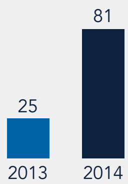
Performance	Our focus in 2015	Principal risks and uncertainties



Total no. of patents, 2014

29

Continue to identify, develop and exploit patent technology to enhance our competitive advantage in the marketplace



Total no. of innovations, 2014

81

Costain will seek to attract 100 new innovations through the supply chain innovation portal in 2015

- People and skills
- Financial strength

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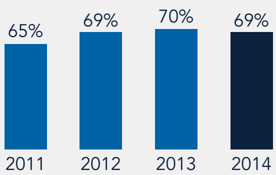
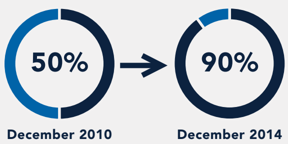


Supplier performance, 2014

69%

To continue to work in close collaboration with our supply chain, involving them at the earliest opportunity to ensure optimum solutions are developed for our customers



Collaborative contracts, 2014

+90%

To continue to increase our revenue from alliance/ framework contracts

- People and skills
- Political, economic and market conditions
- Operational delivery
- Supply chain/joint venture risk

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Our markets
Our focus and the opportunities we see

The sectors in which the Costain Group is active have, in total, a targeted investment spend of more than £87 billion per annum for the immediate future. Below is a summary of activity in those sectors.

Water

Total:

£12bn

Potential: £6.4 billion
Addressable: £2.9 billion

Ofwat's final determination for the sixth asset management cycle will see the investment of £44 billion in improving services, improving resilience and protecting the environment. This will be delivered through 522 performance commitments to deliver a high-quality service to customers with incentives to promote success. This demonstrates a continued commitment to spend in the sector. The regulators' focus on total expenditure (Totex) provides an opportunity to grow into higher value services and drive efficiency across the industry.

Highways

Total:

£7.7bn

Potential: £3.2 billion
Addressable: £2.8 billion

Our road network requires significant investment. Road congestion is forecast to keep increasing, costing the economy billions each year and causing frustration to road users. The road network is also an ageing asset.

The Government's response in December 2014 was to announce its 'Roads Investment Strategy'– the biggest-ever upgrade of the UK's existing roads. The Government has committed £15 billion to improve the national road network.

- £6 billion to resurface 80% of the national network
- £9 billion to add 1,300 extra lane miles
- Over 60 junction improvements to the national road network

Through the National Infrastructure Plan the Government will also be providing local authorities in England with £5.8 billion over 2014-2020 for the maintenance of local highways.

Power

Total:

£12.6bn

Potential: £6.4 billion
Addressable: £1.5 billion

Between 2014 and 2020, an estimated £34 billion of further investment may be needed in electricity and £7.6 billion in gas networks[1].

Resilient energy networks are critical for energy security and vital components of a successful economy. Historically, our existing networks have served us well but they are ageing and out of date. Not only do we need to rebuild our networks to ensure resilience, we need to expand them so we can take advantage of the new types of low carbon energy generation. We also need to modernise them so we can take advantage of the new ways of controlling power flows – ultimately developing smart grids that are much more responsive and can deliver better efficiency and higher energy savings.

Our national networks also need to be more integrated with neighbouring markets. Increased interconnection will support the UK's energy security, affordability and decarbonisation objectives, and support the development of a single European electricity market.

In addition to network infrastructure, the requirement for clean energy for the future is attracting investment in carbon capture and storage projects and technology, as well as new nuclear power stations. There is over £46 billion of planned investment in this area[1].

[1] Source: HMG, DECC – Delivering UK Energy Investment: Networks. Published: January 2015

Nuclear

Total:

£5.8bn

Potential: £3.2 billion
Addressable: £1.0 billion

Significant opportunities exist in the UK nuclear market, both in decommissioning and new power plant construction. The Nuclear Decommissioning Authority continues to accelerate its strategy to manage the clean up of the legacy sites offering long-term clean up and decommissioning contracts. In conjunction with the Government's objective to deliver 16GW of new nuclear capacity by 2030 and growth in the MOD market, this presents further opportunity for Costain's position to grow further in the Nuclear sector.

Oil & Gas

Total:

£23bn

Potential: £5.1 billion
Addressable: £2.6 billion

The challenges faced with the reducing oil price will drive operators to reduce costs, work more efficiently and re-evaluate project execution. This will provide opportunities for Costain to build upon its reputation as a value-added solution provider of full life-cycle engineering services. With its particular expertise in all sectors, Costain is ideally positioned for involvement in necessary brownfield upgrade and expansion projects; the growing demand for oil and gas storage; and the enhancement and maintenance of transmission systems. Further opportunities lie ahead in regards to the increasing momentum for UK development of unconventional gas and carbon capture projects.

Rail

Total:

£26bn

Potential: £11.6 billion
Addressable: £6.5 billion

The Government underpins its commitment to rail with industry-wide strategic engagement and ongoing investment. UK plc is benefiting from this, with passenger journeys set to grow a further 30% over the next decade on a safer, more reliable and cost-effective railway. Technology driven 'digital solutions' will help achieve these national needs. The £38 billion investment on the national rail networks over the next five years is underway, covering electrification, station enhancements and route upgrades, with further significant commitments to London Rail, Crossrail and London Underground. HS2 continues to gather pace

as a key emerging market. We have developed our specialist railway skills to provide a full spectrum portfolio for customers.

Principal risks and uncertainties

This section highlights the principal risks and uncertainties facing the Group together with the key mitigating activities in place to manage those risks.

The Board formally reviews the material risks and ensures that these are appropriately managed by the management team. The Board retains the ultimate responsibility for the Group's risk management framework, including reviewing its effectiveness. It has, however, delegated responsibility for annually reviewing the overall effectiveness of the risk management programme to the Audit Committee. The internal audit function provides assurances to the Audit Committee of the effectiveness of the internal control procedures through completion of the annual audit plan, which takes into account current business risks.

The table below lists the principal risks and uncertainties facing the Group at the date of this Report. This list is not intended to be exhaustive. Some risks have not been included in this section on the basis that they are not considered to be material or are not presently known to the Board.

Risk and Impact	Mitigation
Health, Safety and Environment • Failure to prevent a major safety incident/accident or environmental event which could adversely affect the Group's reputation and its operational and financial performance	The health and safety of our people and everyone who is impacted by Costain remains our highest priority. Accordingly, Costain has detailed Health and Safety policies in place to minimise such risks. Regular Health and Safety visits by experienced professionals and on-site training take place to reduce the risk of human error. Any breaches in procedures are reported quickly and acted upon as appropriate. A Health and Safety committee also meets monthly to develop a consistent approach and consider best practice. Performance metrics in the Group's Annual Incentive Plan also include a key non-financial indicator for Health and Safety.
Political, economic and market conditions • Change in Government and policy on spending • Residual effects of the global economic downturn resulting in contracts being cancelled or postponed	The strategy of the Group is to focus on major customers in the UK energy, water and transportation markets. These markets are defined by significant and long-term planned expenditure programmes underpinned by committed regulated spend and essential capital investment. The future opportunities in these markets are substantial. The UK Government's National Infrastructure Plan has identified investment of over £320 billion to 2020-21 in an identified pipeline of projects in the UK, including a further £15 billion announced in December 2014 on road infrastructure. The plan has identified that the funding for investment will be 65.6% from the private sector, 13.8% representing a mix of public and private sources and 20.6% from the public sector.
Financial strength • Unable to demonstrate to customers the required level of financial resource resulting in failure to win long-term contracts • Inability to maintain competitive scale in a consolidating market • Failure to maintain adequate working capital to operate the business	The Group has a strong balance sheet with a positive net cash position and no significant debt. In March 2014, the Group successfully completed a capital raise of £70.3 million (net of expenses) to enable the business to take greater advantage of the opportunities in its chosen markets and therefore accelerate the Group's medium and long-term growth prospects. The capital raise significantly increased the net asset base of the Company. The Group has in place extensive unutilised banking and bonding facilities.

Risk and Impact	Mitigation
Winning new work • Competition and failure to win work	The Group's unique *'Engineering Tomorrow'* strategy focuses on blue-chip customers whose major spending plans are underpinned by strategic national needs, regulation commitments or essential maintenance requirements. The Group has successfully developed strong relationships with these customers across a range of markets in energy, water and transportation that need solutions to their complex business requirements. The Group regularly monitors the pipeline of opportunities available. The Group's ongoing drive, both organically and by acquisition, to broaden its skills and breadth of capability, develop its market proposition through the introduction of new technologies and its strong brand and excellent reputation for delivery, will also provide it with a competitive edge.
Operational delivery • Failure to deliver the services to the time, cost or quality required in the contract • Failure to accurately assess risks, costs, time or contractual terms • Design faults • Procurement delay or failure • Failure to obtain/renew insurance or refusal of claim by insurers	Costain has in place policies, processes and procedures for the tendering, preparation, planning and delivery of contracts. These are brought together in the 'Costain Way' setting out the requirements for all employees. Costain has defined delegated authority levels for approving all tenders. All significant contracts are subject to review by the Investment Committee. To mitigate the cost risk, experienced and qualified staff are used to prepare bids, which are subject to internal review and approval before submission. During the life of the contract, regular contract leaders' meetings take place to discuss safety, progress, quality, cost, financial performance, end forecast, risk, etc. Work on site is audited by in-house specialists and reports are prepared so that corrective action, where required, can be taken. A senior executive is responsible for overall quality issues, the updating of best practice and ensuring compliance. The senior executive is also responsible for reviewing and updating the Group's procedures in line with the changing business.
Supply chain/joint venture risks • Failure of subcontractors, suppliers or joint venture partners resulting in failure to deliver contracts on time and to budget	The Group seeks to ensure that it is not over-reliant on any one subcontractor, supplier or joint venture partner. In addition, the Group maintains a list of preferred subcontractors and suppliers which is reviewed regularly. The Group also undertakes financial monitoring of subcontractors and suppliers and endeavours to maintain a dialogue with them in order to identify any issue or cause for concern. The Group has in use an external audit system to ensure compliance by its preferred and strategic suppliers.

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Principal risks and uncertainties
continued

Risk and Impact	Mitigation
People and skills • Failure to attract, retain and develop a best-in-class team in an increasingly competitive market may limit the Group's ability to grow the business as anticipated	To support its goal to develop a best-in-class team, the Group's remuneration policy is designed to attract and retain high-calibre individuals in an increasingly competitive market and to remunerate fairly, whilst not encouraging inappropriate business risk to be taken. Pay and conditions of employment are also regularly reviewed against the prevailing market and bench marked against competitors to ensure that the Group remains competitive at all levels. The Group has in place a well-developed succession planning process which is regularly monitored. This process includes carrying out talent reviews and encouraging ongoing development at all levels. The Group also seeks to actively engage with employees through engagement surveys.
Pension liabilities • Failure to manage the Group's pension scheme so that the liabilities are within a range appropriate to its capital base which could have an adverse impact on the Group's operational results	The Group manages a legacy defined benefit scheme and continually reviews the actions it can take to mitigate long-term risk and consults professional advisers, as necessary. The scheme was closed to new members from 1 June 2005 and to future accrual on 30 September 2009. A number of other actions have been taken to manage the obligations in the scheme, including the transfer of assets into the scheme and the implementation of Enhanced Transfer Value and Pension Increase Exchange exercises. A full actuarial valuation of the scheme as at 31 March 2013 was concluded during 2014 and the Group agreed a deficit recovery plan with the Trustee.
Acquisitions • Failure to integrate successfully an acquired business or recognise and mitigate new and related risks could have a damaging impact on the Group's future revenue and profits	Full due diligence is carried out before any acquisition is made. Integration plans are put in place and managed by a dedicated team and progress monitored against pre-agreed performance indicators.
Failure of IT systems • Failure of IT systems, inability to manage and/or to integrate IT systems, as well as the failure to store key documentation securely, could cause financial loss to the Group and expose the Group to breaches of legislation and fines.	A senior executive is responsible for the IT systems and has a suitably qualified team for support. Critical areas are subject to testing and include rapid recovery as well as sound data backup procedures. Online security training is provided for safe usage and storage of documentation. The Group is accredited to ISO/IEC 27001:2005 Information Security Management System.

Divisional review

£785m

Infrastructure revenue

£2.3bn

Infrastructure order book

We have two core operating and reporting divisions within our business: Infrastructure and Natural Resources.

Our customer-aligned divisional structure has enabled us to continue to focus our resources on identifying and securing the most attractive new business opportunities across the sectors in which we operate.

Infrastructure

The Infrastructure division, which operates in the Highways, Rail and Power sectors, experienced another year of strong growth as major customers continued to invest in upgrading and renewing the UK's infrastructure assets, encouraged by Government initiatives such as the National Infrastructure Plan.

Revenue (including share of joint ventures and associations) increased to £785.2 million (2013: £560.6 million) whilst adjusted profit from operations rose to £38.3 million (2013: £31.4 million) as the division performed well on existing projects and secured significant new contracts across all its target sectors. Profit margins in the year were at the upper end of our expectations and included the benefit of the award of gain-share and bonuses on a number of projects.

The order book for the division has grown to £2.3 billion (2013: £1.9 billion) as we have secured significant new orders and contract extensions from customers. We have also delivered several major Early Contractor Involvement ('ECI') schemes through the planning and statutory process, prior to commencing delivery phase. The level of tendering activity remains high with a significant opportunity pipeline.

In Highways, Costain continued to build on its status as a leading supplier to the Highways Agency. The Group secured a place on their five-year, £5 billion Collaborative Delivery Framework and was awarded three Smart Motorway schemes as part of the Managed Motorway Programme on which Costain is a long-term partner. The Group also continued to deliver significant maintenance works within the Asset Support Framework and three Managing Agent Contracts. Our broad, multidisciplinary capability is also enabling close involvement at earlier stages of major projects through ECI schemes, which then lead to contract extensions for the delivery phase, for example on the A556 Knutsford project.

Costain has also continued to be a major supplier to the Welsh Government, with the All Wales Technology contract progressing well and the A465 ECI contract now moving to the construction phase following the Group's successful delivery of the front-end engineering and design stage of the project. The Group's work on strengthening the strategically important Hammersmith flyover for Transport for London is also progressing on time and on budget.

In Rail, a Costain joint venture was awarded the largest share of Network Rail's £2 billion National Electrification Programme and the Edinburgh to Glasgow Improvement Project. The Group's position as one of the most significant service providers for Crossrail, Europe's largest infrastructure project, was reinforced with the award of the North East Spur contract, whilst Costain's other works for Crossrail at Paddington Station, Bond Street Station and Paddington New Yard continue to progress well.

Her Majesty the Queen opened Reading Station after the critical redevelopment project was handed over ahead of schedule. At London Bridge, one of the busiest transport hubs in the UK, Costain has continued to deliver on key milestones, including bringing into use, six new platforms.

In Power, the Group is making significant progress delivering National Grid's London Power Tunnels project, which involves the construction of the longest tunnel under London in history. In addition, the Group has also secured repeat work with National Grid following appointment to their high voltage underground and overhead transmission line frameworks.

Divisional review
continued

£335m
Natural Resources revenue

£1.2bn
Natural Resources order book

The Costain team has delivered several key overhead line projects for UK Power Networks and also continues to perform operations and maintenance activities for SSE, E.ON and Scottish Power. The Group is also engaged at the ECI stage with EDF in the development of the Hinkley C new nuclear power plant, designing and developing the cooling system marine tunnel.

Natural Resources

The Natural Resources division encompasses Costain's activities in the Oil & Gas, Nuclear and Water sectors.

Revenue (including share of joint ventures and associations) for the year was £335.0 million (2013: £397.6 million), with adjusted profit from operations, including £4.0 million profit on transfer of interest in associates to The Costain Pension Scheme, of £0.5 million (2013: £12.8 million, including £9.1 million profit on sale of interest in joint ventures). The reduction in revenue reflects our policy of prioritising and allocating tendering resources towards the most attractive opportunities for growth across the Group at any point in time.

The adjusted operating result for the year includes additional costs for the completion of the legacy waste PFI contract awarded in 2007 for the Greater Manchester Waste Disposal Authority as described on page 33. Excluding these costs, the division generated an operating profit and is trading in line with expectations including an increasing level of tendering costs for new work. The division has increased its forward order book to £1.2 billion (2013: £1.1 billion) and is expected to benefit from customer spend in its target markets which are underpinned by regulatory and legislative requirements.

In Water, the Group continued to deliver successfully AMP5 frameworks for United Utilities, Southern Water, Severn Trent Water, Welsh Water and Northumbrian Water. Looking to the future, Costain has been awarded places on the five-year AMP6 programmes, which commence in April 2015, for Thames Water, Severn Trent Water and Southern Water. The Group is continuing to deliver the large waste water treatment plants at Liverpool and Woolston, and has completed the award-winning Brighton & Hove scheme. In addition, work commenced on the Shieldhall contract with Scottish Water.

Costain continued to broaden its specialist capabilities in the Oil & Gas market where it believes it will continue to secure new work although there will be some impact from the recent falls in the oil price. In 2014, the Group secured a contract with Centrica Energy for EPC services as part of the Barrow Gas Terminals Project and with Perenco for its Freon replacement project at Dimlington.

We continue to deliver support services for the Oil and Pipelines Agency, including operations, maintenance and upgrade services across its network of jet fuel pipelines and storage facilities, with a further one-year extension being awarded in the year. Costain Upstream, which delivers asset development and asset improvement consulting services from its base in Aberdeen, has performed well and continued to secure new work including an extension to the Premier Oil framework.

Land Development

In Nuclear, the Group is now a major contract partner with BAE having been appointed to its £300 million, eight year programme to re-develop the submarine site in Barrow-in-Furness. The delivery of Evaporator-D construction at the Sellafield Nuclear Reprocessing Facility in West Cumbria continues as expected. The Fuel Element Debris dissolution facility at Bradwell was successfully handed over for active commissioning.

During December, handover was achieved on the final waste facility on the legacy Greater Manchester Waste Disposal Authority PFI contract awarded in 2007. All 46 facilities on the contract are now either fully completed or in the warranty period under the terms of the contract during which further work and plant modifications will be completed. In achieving handover of the final facility, we received in December contractual retention and milestone payments of £14 million. As previously reported, Costain is in discussions with relevant contract counterparties and the Group's insurers regarding the issues that have arisen on this contract. The Board expects a successful outcome to these discussions. In 2014, a provision has been taken for additional costs to complete the project. It has been the Group's policy since 2009 not to pursue fixed-price contracts of this nature.

We completed the Parkway development in Newbury, a mixed retail and residential project, and reached agreement on the final account for the work with our client. Following legal proceedings, a fine of £0.5 million for health and safety breaches relating to the death of a contract worker at the site in 2011 was incurred.

The Group's non-core Land Development activity in Spain, undertaken in a 50:50 joint venture with Santander Bank, continued to be subject to challenging market conditions. The joint venture has a portfolio of in excess of 500 hectares of land in Southern Spain with varying levels of planning approval for residential and hotel development. It also holds two leisure businesses, a golf club and 624-berth yacht marina, adjacent to Gibraltar. Both leisure activities have reported improving revenue streams, particularly in the marina where the boat repair yard is in demand and is assisting in raising marina occupancy.

Whilst the Spanish economy continues to show signs of improvement, there remains considerable uncertainty as to when significant recovery will be achieved. Revenue was £2.3 million (2013: £1.8 million) and the loss after tax was £1.3 million (2013: £2.1 million). As anticipated, no significant land sales were completed in the year

Corporate Responsibility review

We are committed to delivering projects and services responsibly and sustainably, ensuring that we meet our customers' and society's needs while managing the social, environmental and economic issues that impact our business either directly or through our supply chain.

"Costain Cares is a continued commitment to you, our stakeholder, to focus on the issues you care about."

Andrew Wyllie CBE, Chief Executive

Through stakeholder engagement and by assessing our impacts and level of influence, we have identified key priorities that are material to our business and are of importance to our key stakeholders.

Costain Cares, our Corporate Responsibility (CR) strategy and vision to build a longer-term sustainable business that creates economic, environmental and social value, addresses these key priorities.

Our approach

Costain Cares is based on three fundamental pillars: Relationships, Our Environment and The Future.

1. Relationships

We encourage open, honest and respectful communication and believe in strong, long-lasting relationships that are mutually beneficial.

We will:

- provide a safe working environment free from harm;
- provide a healthy working environment for all our people;
- support the local communities in which we operate, ensuring we leave a lasting legacy;
- provide sustainable solutions and the highest standards of service for our customers;
- attract, retain and develop the best people for the Costain Group; and
- operate a collaborative, responsible supply chain where our partners support us in delivering efficient, innovative and sustainable solutions.

2. Our Environment

We operate in the built environment, where we meet national needs for strategic investment in infrastructure. Next, we compete in the economic environment, where we must deliver value for customers and shareholders. Finally, we have to deliver responsibly to the natural environment for the benefit of everyone.

Where possible, we will work with our customers and supply chain to:

- reduce our impact on climate change;
- conserve natural resources through effective waste management, minimising water consumption and sustainable sourcing of materials; and
- protect and enhance the environment.

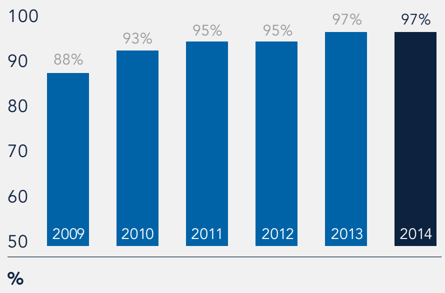
3. The Future

We play an important role in the provision of infrastructure vital to the UK economy. The benefits of investment in infrastructure today will be felt for many years to come.

We will:

- be one of the UK's top engineering solutions providers
- provide a sustainable return on investment for our shareholders;
- invest in innovation to provide solutions to tomorrow's challenges;
- work with our customers and supply chain to develop skills to respond to future needs within our sector; and
- contribute to economic growth by supporting our supply chain, including small and medium-sized enterprises.

BITC CR Index performance



Our CR performance

The next page summarises our progress against our key CR priorities that are not already reported on either in our review of strategic priorities on page 20 or financial performance on page 41.

More details about our Costain's CR work are available online at costain.com/our-culture

The Board is responsible and the Executive Board is accountable for all aspects of CR including setting policy and strategy and providing leadership to drive our CR programme. Every employee is expected to work in a responsible and sustainable way.

In addition to measuring performance against our strategy, we also measure and benchmark ourselves against our peers and other companies in the wider marketplace by participating in Business in the Community (BITC) CR Index. The CR Index illustrates how companies integrate responsible business at strategic and operational levels. In 2014, we were proud to retain Platinum status.

Corporate Responsibility review
continued

1. Relationships

Goal: To provide a working environment where the health of our people is protected, their wellbeing is enhanced and everyone returns home safely at the end of the working day

A safe working environment free from harm

Key highlights

- The launch of the Costain Safe Start Toolkit aimed at ensuring that every worker at Costain starts work safely. The toolkit includes a training package which focuses on developing the communication skills of the managers and supervisors who put people to work.
- Two successful safety, health and environmental (SHE) Leadership Impact days were held across the Group in April and October. Led by the two Managing Directors, approximately 50 senior business leaders visited over 50 sites and the two principal offices in order to engage with site personnel and demonstrate commitment from the highest level. The two key themes for both days were the importance of putting people to work safely using the Safe Start toolkit and the management of health and wellbeing.

Metrics

Accident Frequency Rate

A 9% reduction in the last four years

Group All Accident Frequency Rate

A 9.5% reduction in the last four years

Focus for 2015

- Achieve a Group AFR of 0.08.
- Hold two SHE Leadership Impact Days.
- Undertake comprehensive SHE readiness reviews prior to start up of all new contracts.
- Actively participate in European Health & Safety Week in October.

A healthy working environment for all our people

Key highlights

- Strengthened our policy with regard to 'wellbeing' medicals for non-safety critical staff by making voluntary medicals available to everyone working with us.
- The delivery of two company-wide health campaigns to raise awareness of:
  – the health risks associated with construction dust
  – cancer.
- The second campaign was delivered by Macmillan Cancer Support who visited over 20 sites and the two principal offices, reaching a total audience of over 1,500 people.
- Signed up to the Institute of Occupational Safety and Health (IOSH) 'No Time to Lose' campaign, aimed at improving understanding of the causes of occupational cancer and helping businesses to take action.

Metrics

3.3 days

lost (on average per employee) in 2014 through absence
Note: this is the first year this data has been reported on

Focus for 2015

- Continue the promotion of wellbeing medicals for our non-safety critical staff. Our aim is for 75% of Costain staff to have undergone a medical within the last two years by the end of 2015.
- Develop and trial a Health Maturity Matrix which will comprise a list of incremental standards which will allocate Gold, Silver or Bronze status to our contracts in respect of their management of health and wellbeing. We aim to adopt the Matrix company-wide in 2016.
- Continue to promote health and wellbeing in the workplace through the delivery of three company-wide campaigns. The campaigns in 2015 will focus on Vibration, Personal Wellbeing and Mental Health.

Goal: To Support the local communities in which we operate, ensuring we leave a lasting legacy

Work in partnership with local communities

Key highlights

- In 2014, a number of our projects were recognised by the Considerate Constructors Scheme. We received five Gold Awards, three Silver Awards, seven Bronze Awards and two of our projects were runners-up in the Most Considerate Site Award. The awards recognise sites' excellent standards of consideration towards their neighbours, their workforce and the environment. Award winners are selected from the top performing 10% of sites registered under the scheme.

Metrics

Group average Considerate Constructors Scheme

40.6

out of 50, consistently high scores

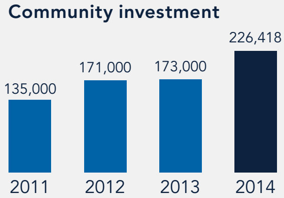
Community investment

Key highlights

- Founded the Costain Charitable Foundation, a registered charity.
- Launched the Costain 150 Challenge in celebration of Costain's 150th anniversary.

Metrics

Community investment



68%

increase in charitable donations in the last four years

Focus for 2015

- Raise £1 million for the Costain Charitable Foundation's four chosen charities: the British Heart Foundation, Macmillan Cancer Support, The Prince's Trust and Samaritans.

Heysham to M6 Link Scheme

This long-awaited dual carriageway and park-and-ride scheme will improve access and ease congestion for local businesses and residents, while a park-and-ride scheme will help boost the Lancaster economy.

The Heysham to M6 Link scheme will provide the long-awaited connection from the M6 at Junction 34 to the Morecambe and Heysham peninsula. Since construction began in early 2014, the scheme is set to realise a number of key environmental and community benefits including improved air quality, biodiversity, increased passenger access and employment opportunities.

Reducing our carbon footprint

We have been working closely with our supply chain partner, Lafarge Tarmac, to minimise the carbon footprint during the construction phase, a target that also delivered safety and cost benefits.

Early engagement on the design and materials led to a total carbon reduction of 21% from the original design. Our team were able to identify considerable savings in the quantity of materials required and the embodied carbon footprint of the entire project. The new design reduced the aggregate tonnage by nearly 25% alone, while the largest carbon savings have been realised through the reduction in asphalts. There is opportunity to identify even further carbon and cost reductions.

Safety remains a high priority during delivery. Our team is proud of the safety record (current AFR 0.11) and work they have done with local road users to raise awareness and prevent road risk.

Supporting the local community

The local community has also benefited from the scheme with Costain insisting on using local labour where possible. This has resulted in 85% of agency personnel living locally, 80 of whom were previously unemployed. We have also recruited five apprentices to assist in the successful delivery of the scheme.

For further details on this and other case studies, please visit our website: http://costain.com/our-culture/costain-cares-stories

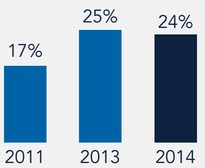
Corporate Responsibility review
continued

1. Relationships continued
Goal: To attract, retain and develop the best people for the Costain Group

Provide initiatives and working conditions in order to retain key staff

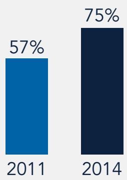
Key highlights
- Enhanced the population of our Annual Incentive Plan in order to engage and retain top talent.
- Conducted Group-wide employee engagement survey.
- Further successful grant made under the Company's Save As You Earn (SAYE) scheme which encourages and supports share ownership by employees.

Metrics
SAYE take-up by eligible employees



SAYE take-up remains at a strong level

Employee engagement



75% of employees think Costain is a great place to work

Focus for 2015
- Deliver the key actions identified in the 2014 engagement survey focusing on communications and visibility of career opportunities.
- Conduct a full survey, with a smaller pulse survey in-between to track key drivers every two years.

London Bridge Legacy
At London Bridge station, we are striving to maintain a fit and healthy workforce, to reduce our use of natural resources, eliminate waste, maximize our talent and skills, integrate business into the community and help tackle low employment in the London Borough of Southwark.

Key benefits, as at December 2014:
- c.£1.8 million spent with local and small and medium-sized businesses (SMEs) by December 2014
- 99% of waste diverted from landfill
- 26 apprenticeships offered

We are working with our client, Network Rail, to ensure long-term employee and project value by implementing sustainable solutions both in design and construction. We have introduced a number of best practices and initiatives that will help us provide a sustainable legacy.

Integrating business into the community
Engagement with local companies and recruiting local SMEs is important to promote local economic sustainability. By holding local supplier events and encouraging companies to develop their offering, we have contributed towards the economy of the London Borough of Southwark.

By identifying skills gaps within the local community and gaining our Skills Academy status in 2013, we have helped young people obtain employment, providing them with the basic training needed in the construction industry.

Environmental responsibility
We proactively work to minimise all impacts through changes in methods or mitigation in advance of major works. Automated monitoring systems have been installed around the worksite to assess noise and air quality impacts and allow us to pinpoint any problems.

One of our focuses has been the responsible procurement of materials and services using tools such as our material use plan. This allows us to make informed decisions about the materials that we use on projects.

The project has required the removal of over 200,000 tonnes of waste, and despite the contaminated nature of the sites we have diverted over 99% of the waste from landfills.

For further details on this and other case studies please visit our website: http://costain.com/our-culture/costain-cares-stories

2. Our environment

Goal: To conserve natural resources

Goal: To protect and enhance the environment

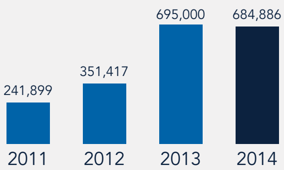
Conserve natural resources

Key highlights

- We continued to raise awareness of efficient material and waste management and identify, in early phases of contracts, ways to minimise materials and eliminate waste.
- Where feasible, we used the CL:AIRE Code of Practice to manage materials and, therefore, reduce waste.
- We continued to work closely with our supply chain to minimise or eliminate wastage and ensure we reduced or limited and recovered as much waste as possible.

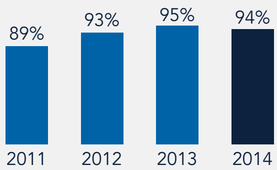
Metrics

Tonnes of waste removed



We have under taken a number of high volume excavation projects in the last four years…

Waste diverted from landfills



…but the percentage of waste we divert from landfills remains consistently high.

Focus for 2015

- Continue to drive resource efficiency and improve our systems with the aim of maximising the efficient use of resources.
- Work closely with our supply chain to continue to reduce waste production and increase diversion from landfills.

Protect and enhance the environment

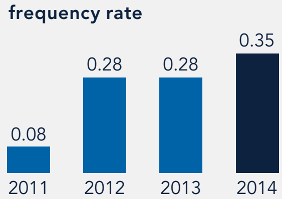
Key highlights

- Significantly raised awareness over the last three years of environmental incidents and the importance of reporting, undertaken via numerous mechanisms including increased levels of training and communication initiatives.

Metrics

Environmental incidents

Environmental incident frequency rate



Better staff training has led to an increase in awareness and the reporting of incidents.

Prosecutions, cautions, notices

0 **No environmental prosecutions, cautions or notices in the last eight years**

Focus for 2015

- We are committed to minimising our impact on the environment and reducing our overall environmental incidents year-on-year.
- Reduce our Environmental Incident Frequency Rate to 0.31.

Corporate Responsibility review
continued

3. The Future

Goal: To work with our customers and supply chain to develop skills to respond to future needs within our sector

Goal: To contribute to economic growth by supporting our supply chain, including small and medium-sized enterprises

Raising awareness of engineering opportunities among young people

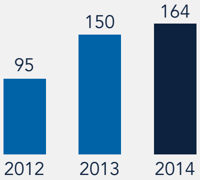
Key highlights

- 74 young people took part in Costain's 'Get Into Construction' course, a two-week work experience/training programme with The Prince's Trust. Over 50% of the young people who took part have gone into employment.
- Launched Costain's Science, Technology, Engineering and Maths (STEM) app, 'Engineering your Tomorrow' with over 1,000 downloads to date.

Metrics

50 Engagement with over 50 schools in the last 12 months

Number of work experience placements



Over 400 placements in the last three years

Focus for 2015

- 100% of contracts to develop and implement community engagement plans.

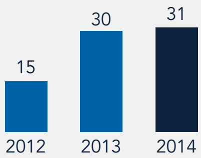
Working in collaboration with our supply chain and partners

Key highlights

- Launched the Costain supply chain innovation portal to make collaborating on innovation a reality for hundreds of businesses focused on accelerating new solutions.
- Held Costain supply chain conference, attended by senior representatives of our supply chain partners and Costain's senior management team.
- Founded the factory thinking forum to develop new innovative solutions and enhance best practice in off-site manufacturing.

Metrics

Number of SMEs engaged in our supply chain academy



To date, 76 supply chain partners have been through the academy, a total of 2,280 participants

Focus for 2015

- Achieve level three of the Sustainable Procurement Task Force Flexible Framework.
- Two further intakes of the supply chain academy.
- Roll out sustainable procurement guidance and training to our procurement teams and strategic partners.

Finance Director's review

Anthony Bickerstaff, Finance Director

This review brings together the key financial metrics of the Group and sets out the matters of financial significance.

Overview

Group revenue, including share of joint ventures and associates, was £1,122.5 million for the year to 31 December 2014 (2013: £960.0 million). The Group generated a 5% increase in underlying operating profit to £28.7 million (2013: £27.4 million). The increased profit reflects the Group's continued focus on long-term repeat orders with blue chip customers.

Profit before tax, before other items, for the year was £28.5 million (2013: £31.0 million). Basic earnings per share, before other items, amounted to 27.8 pence (2013: 41.0 pence). Reported basic earnings per share were 22.2 pence (2013: 17.6 pence).

Profit before tax, before other items, includes profits on the transfer or disposal of the Group's PFI equity portfolio and in 2014, the Group transferred its remaining two PFI investments into The Costain Pension Scheme (CPS) at a value agreed with the Trustee of the scheme of £7.4 million, which resulted in a profit on the transfer of £4.0 million. In 2013, the Group sold its minority shareholdings in three joint venture companies as part of the disposal of this portfolio, for an aggregate consideration of £12.0 million. The Group realised a profit of £9.1 million as a result of this sale.

The Group secured a number of new contracts and extensions and the Group's order book increased to £3.5 billion (31 December 2013: £3.0 billion).

The results of the Group's operating divisions are considered in the Divisional review section and are shown in the segmental analysis in the financial statements.

Capital raising

On 18 March 2014, the Group successfully completed the raising of £70.3 million (net of expenses) of new capital. The proceeds are being, and will be, utilised:

- to demonstrate to customers the Group's financial capacity to support the anticipated further increases in contract size and duration;
- to invest in innovation and technology necessary to enhance the service offering to customers;
- to finance bid costs associated with a greater number of large scale projects for which the Group is in a position to tender;
- to fund likely increased working capital requirements arising from the move in the market towards target-cost, cost-reimbursable contracts;
- to provide flexibility to make selected in-fill acquisitions to complement Costain's existing capabilities as opportunities arise; and
- for general corporate purposes.

Finance Director's review
continued

Interest

Net finance expense amounted to £3.6 million (2013: £4.0 million). The interest payable on bank overdrafts, loans and other similar charges was £2.2 million (2013: £2.6 million) and the interest income from bank deposits and other loans and receivables amounted to £0.7 million (2013: £0.7 million). In addition, the net finance expense includes the interest cost on the net liabilities of the pension scheme of £1.4 million (2013: £2.1 million) and £0.7 million (2013: £Nil) unwind of discount on deferred consideration.

Tax

The Group's effective rate of tax was 7.1% of the profit before tax (2013: 3.1%). The lower than normal rate of tax arose owing to tax relief on the sale of shareholdings in PFI assets, Research and Development tax relief claims, timing differences not previously recognised as deferred tax assets, and the effect on the brought-forward deferred tax balances of the reduction in the rate of corporation tax to 20%.

Dividend

The Board has recommended a final dividend for the year of 6.25 pence per share (2013: 7.75 pence per share) to bring the total for the year to 9.5 pence per share (2013: 11.5 pence per share). The reduction in dividend per share is due to the increase in the number of shares as a result of the new capital raised during the year.

In accordance with the pension deficit recovery plan agreed with the Trustee of the CPS, the Group will make an additional cash contribution to the pension scheme to match the total deficit contribution to the total amount of dividends paid to shareholders.

Shareholders' equity

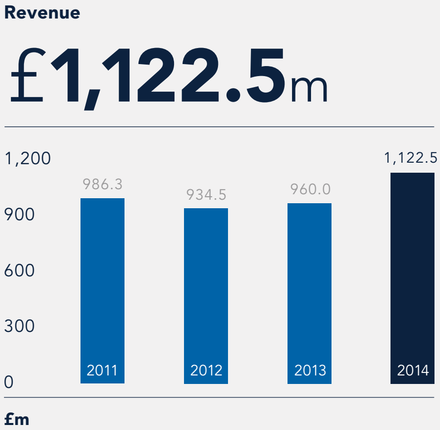
Shareholders' equity increased in the year to £110.8 million (2013: £43.3 million). The profit for the year amounted to £21.0 million and other comprehensive expenses to £16.1 million. The movements are detailed in the consolidated statements of comprehensive income and expense and changes in equity in the financial statements. The most significant change to shareholders' equity resulted from the capital raise completed during the year.

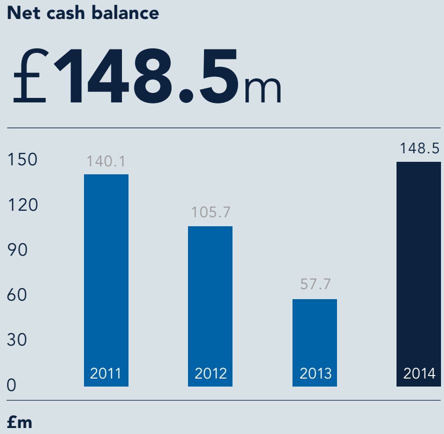
Pensions

As at 31 December 2014, the Group's pension scheme deficit in accordance with IAS 19, net of deferred tax, was £33.4 million (2013: £29.4 million). The scheme deficit position has increased primarily as a result of a reduction in the discount rate used to calculate the liabilities offset by a decrease in the assumed inflation rate, the return on assets and company contributions.

As part of the ongoing actions to manage the Group's pension obligations, in 2014, the Group transferred its interest in two PFI investments into the CPS at a value agreed with the Trustee of the scheme of £7.4 million.

In the year, agreement was reached with the Trustee of the CPS regarding the triennial actuarial review as at 31 March 2013 and the associated deficit recovery plan. As anticipated, the annual cash contribution to the scheme deficit has been agreed at £7.0 million per annum (increasing annually with inflation) plus an additional contribution to bring the total contributions to match the total dividend amount paid by the Company over the next three years.





Cash flow and borrowings

The Group has a positive cash balance, which was £148.5 million as at 31 December 2014 (2013: £84.3 million) and no borrowings (2013: £26.6 million), this included cash held by joint operations of £24.1 million (2013: £25.6 million).

As set out in the consolidated cash flow statement, the Group had a positive operating cash flow, together with outflows for payment of dividends and pension deficit contributions. The cash balance was enhanced by the £70.3 million capital raising completed during the year. The average month-end net cash balance during 2014 was £95.6 million (2013: £50.7 million).

Contract bonding and banking facilities

The Group's long-term contracting business is dependent on it being able to supply performance and other bonds as necessary. This means maintaining adequate facilities from banks and surety bond providers to meet the current and projected usage requirements. The Group has contract bonding and banking facilities of £495 million with a maturity date of 30 June 2017 with its relationship banks and surety companies.

Treasury

The Group's treasury and funding activities are undertaken by a centralised treasury function. Its primary activities are to manage the Group's liquidity, funding and financial risk, principally arising from movements in interest rates and foreign currency exchange rates.

The Group's policy is to ensure that adequate liquidity and financial resources are available to support the Group's growth development, while managing these risks. The Group's policy is not to engage in speculative transactions. Group Treasury operates as a service centre within clearly defined objectives and controls and is subject to periodic review by internal audit.

Liquidity risk

The Group finances its operations primarily by a mixture of working capital, funds from shareholders, retained profits and borrowings. The Directors regularly monitor cash usage and forecast usage to ensure that projected financing needs are supported by adequate cash reserves or bank facilities.

Finance Director's review
continued

Foreign currency exposure

Translation exposure: the results of the Group's overseas activities, mainly non-core Land Development in Spain, are translated into sterling at rates approximating to the foreign exchange rates ruling at the dates of the transactions. The balance sheets of overseas subsidiaries and investments are translated at foreign exchange rates ruling at the balance sheet date.

Transaction exposure: the Group has small transactional currency exposures arising from subsidiaries' commercial activities overseas and from overseas supply purchases for business in the UK. Where appropriate, the Group requires its subsidiaries to use forward currency contracts to minimise any currency exposure unless a natural hedge exists elsewhere within the Group.

Interest rate risks and exposure

The Group enters into financial instruments, where necessary, to finance its operations. Various financial instruments (for example, trade receivables and trade payables) arise directly from the Group's operations.

The main exposure to interest rate fluctuations within the Group's operations arises from surplus cash, which is generally deposited with the Group's relationship banks, and bank borrowings.

Anthony Bickerstaff
Finance Director
02 March 2015

Corporate Governance report

"Our role is to create a robust governance framework that encourages transparency and accountability."

David Allvey, Chairman

Chairman's summary statement

Dear Shareholder

As Chairman, I am accountable for corporate governance at Costain.

Our Board is ultimately responsible for the success of the business and we are committed to the highest standards of corporate governance to enable us to continue to achieve our vision of being one of the UK's leading engineering solutions providers. Our role is to create a robust governance framework that encourages transparency and accountability, combined with a meticulous and efficient approach to internal control and risk management.

I lead a team that is diverse across a range of measures, including skills, experience, gender and nationality. In May 2014, we further strengthened our Board with the appointment of David McManus, whilst in April 2014 Alison Wood, who had been appointed to the Board in February 2014, became Chair of the Remuneration Committee following the retirement of Mike Alexander. My focus continues to be on maintaining a strong team.

In keeping with the requirements of the UK Corporate Governance Code ('the Code'), we carried out an externally facilitated evaluation of the Board's performance in 2014. This was conducted by way of personal interviews and detailed questionnaires. Further details can be found on page 50 of the Corporate Governance report.

In addition, the Board undertook wide-ranging discussions on key strategic issues and this included a number of Board workshops attended by members of the Executive Board and third-party advisers. These conversations continued to be focused on implementing our unique and evolving *'Engineering Tomorrow'* strategy, including the ongoing consideration of potential in-fill acquisitions to complement Costain's existing capabilities as opportunities arise. A business plan was approved in December 2014.

The following pages discuss in more detail the Board's various activities during the year, explaining how the various committees govern our approval and operating procedures.

David Allvey
Chairman
02 March 2015

Board of Directors
Experienced leadership

Committee membership
1 Member of the Remuneration Committee.
2 Member of the Audit Committee.
3 Member of the Nomination Committee.

Go to page 17 to read about the Executive board

Go to pages 54 to 74 to read more about Committee activity

David P Allvey (69)[3]
FCA, ATII
Non-Executive Chairman

Appointment
November 2001

Skills and experience
David Allvey was appointed Chairman in January 2008 prior to which he was Chairman of the Audit Committee. With a career that started in civil engineering and subsequently as a Chartered Accountant, his previous roles include Group Finance Director for BAT Industries plc, Barclays Bank plc and Chief Operating Officer for Zurich Financial Services, member of the UK Accounting Standards Board, member of the International Accounting Standards Insurance Group, Non-Executive Director of Thomas Cook plc (2007 to 2012), Senior Non-Executive Director of Intertek Group plc (2002 to 2011), Senior Non-Executive Director of William Hill plc (2002 to 2011), Senior Independent Director of Friends Life FPG Limited (formerly Friends Provident Group plc) (2009 to 2011) and Chairman of Arena Coventry Ltd (2006 to 2012).

External appointments
Senior Independent Director of Friends Life Group plc, Non-Executive Director of Clydesdale Bank plc and National Australia Group Europe Limited.

Anthony O Bickerstaff (50)
FCCA
Finance Director

Appointment
June 2006

Skills and experience
Tony Bickerstaff was appointed Finance Director in June 2006. Tony has extensive knowledge of the construction and support services sectors both in the UK and overseas. He is responsible for all aspects of the financial management of the Group as well as playing a major role in the Group's strategic and operational development. Previously, Tony was with the Taylor Woodrow Group, which he joined in 1982. He held a number of senior management and financial positions in Taylor Woodrow including Finance Director of Taylor Woodrow Construction Limited. Prior to becoming Finance Director, he was Divisional Operations Director in charge of Taylor Woodrow Group's PFI projects.

External appointments
Non-Executive Director and Chair of the Audit Committee of Low Carbon Contracts Company Limited & Electricity Settlements Company Limited.

Andrew Wyllie (52)
CBE, FREng, MBA, BSc, CEng, FICE, CCMI
Chief Executive

Appointment
September 2005

Skills and experience
Andrew Wyllie was appointed Chief Executive in September 2005. He was previously Managing Director of Taylor Woodrow Construction Ltd (2001 to 2005) and a member of the Taylor Woodrow plc Executive Committee. Andrew joined Taylor Woodrow in 1984 and worked on major contracts in Africa, the Middle East, the Far East and the UK. He was awarded the CBE for services to Construction and Engineering.

External appointments
Non-Executive Director of Scottish Water.

James Morley (66)[1,2,3]
BSc, FCA
Senior Independent Director

Appointment
January 2008

Skills and experience
James Morley was appointed as the Senior Independent Director in January 2013 prior to which he served as Chairman of the Audit Committee from January 2008 until the end of October 2012. He is a Chartered Accountant with some 27 years' experience as a board member of both listed and private companies. Previous roles include Chief Operating Officer of Primary Group Ltd (2006 to 2007), Group Finance Director of Cox Insurance Holdings plc (2002 to 2005), Group Finance Director of Arjo Wiggins Appleton plc (1999 to 2001), Group Executive Director Finance of Guardian Royal Exchange plc (1990 to 1999), Deputy Chief Executive and Finance Director of Avis Europe plc (1976-1989), Non-Executive Director of the Bankers' Investment Trust plc (1994 to 2008), Non-Executive Director of W S Atkins plc (2001-2009), Non-Executive Director of Trade Indemnity Group plc (1991-1996) and Non-Executive Chairman of Acumus Ltd. (2011-2012).

External appointments
Non-Executive Director of The Innovation Group plc, Clarkson plc, Speedy Hire plc, BMS Group Ltd. and Minova Insurance Holdings Ltd.

Committee membership
1 Member of the Remuneration Committee.
2 Member of the Audit Committee.
3 Member of the Nomination Committee.

Go to page 17 to read about the Executive board

Go to pages 54 to 74 to read more about Committee activity

Jane A Lodge (59)[1,2,3]
FCA, BSc
Independent Non-Executive Director

Appointment
August 2012

Skills and experience
Jane Lodge was appointed as a Non-Executive Director in August 2012 and was appointed Chair of the Audit Committee with effect from the end of October 2012. Prior to this Jane spent 35 years at Deloitte LLP (UK), 25 as an audit partner advising global companies, particularly in the manufacturing, house-building and property and construction sectors. She was senior partner of the Birmingham office and the Deloitte UK Manufacturing Industry Sector.

External appointments
Non-Executive Director and Chair of the Audit Committee, Devro PLC, Non-Executive Director, Black Country Living Museum Trust Ltd, Non-Executive Director and Chair of the Audit Committee, DCC PLC, Non-Executive Director, Bromsgrove School Foundation and Non-Executive Director and Chair of the Audit Committee, Stemcor Holdings Ltd.

Ahmed Aly Samy (59)[3]
BCom/Accounting
Non-Executive Director

Appointment
November 2013

Skills and experience
Ahmed Samy was appointed as a Non-Executive Director in November 2013. He is Deputy Director General Investment Affairs of Mohammed Abdulmohsin Al-Kharafi & Sons Co. W.L.L., and his responsibilities include managing the company's offshore investments on international markets, evaluation and implementation of project/ investment opportunities and undertaking various corporate actions including mergers and acquisitions. Previous to his 25 years in the investment field, Ahmed Samy gained 11 years' banking experience, culminating in his appointment as Staff Credit Officer at Commercial International Bank (formerly Chase National Bank), Egypt.

External appointments
Board Member of Credit Bank of Albania

David McManus (61)[1,2,3]
BSc
Independent Non-Executive Director

Appointment
May 2014

Skills and experience
David McManus was appointed as a Non-Executive Director with effect from 12 May 2014. David began his career with the Fluor Corporation (1975-1980) after graduating in civil engineering and went on to hold a number of executive positions in Shell UK (1980-1989), LASMO plc (1989-1994), Atlantic Richfield Company (ARCO) (1994-2000), BG Group (2000-2004) and as Executive Vice President, International Operations of Pioneer Natural Resources (2004-2012). David was formerly a Non-Executive Director of Cape plc (2004-2012), serving as Chairman from 2006 to 2008.

External appointments
Non-Executive Director at the Hess Corporation, FlexLNG, Rockhopper Exploration plc and Caza Oil & Gas Inc.

Alison J Wood (51)[1,2,3]
MBA, BA
Independent Non-Executive Director

Appointment
February 2014

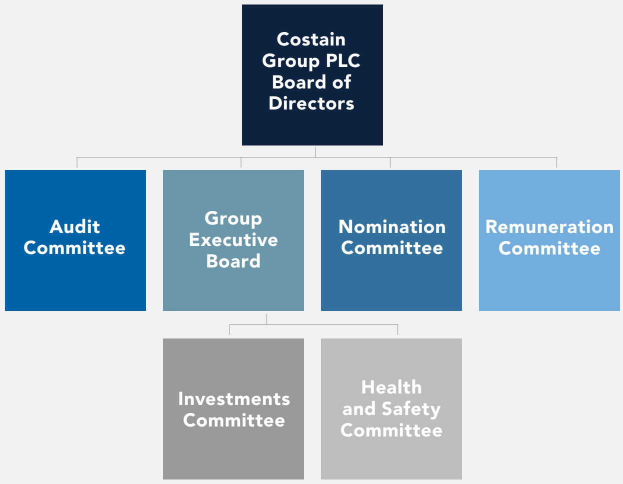
Skills and experience
Alison Wood was appointed as a Non-Executive Director with effect from 1 February 2014 and was appointed as Chair of the Remuneration Committee from the beginning of April 2014. Alison is the former Global Director of Strategy and Corporate Development at National Grid plc (2008-2013). Before that, Alison spent nearly 20 years in a number of strategy and leadership roles at BAE Systems plc including Group Strategic Development Director. Alison has also held Non-Executive Director positions with BTG plc (2004-2008) and Thus Group plc (2007-2008).

External appointments
Non-Executive Director at Cobham plc and Senior Independent Director at e2v technologies plc.

Former Director
Mr Mike Alexander retired as a Non-Executive Director with effect from 31 March 2014.

Corporate Governance report continued

Board structure



Principles statement

The Board of Directors of Costain Group PLC is committed to achieving the highest standards of corporate governance.

These principles are considered to be central to the effective management of the business and to maintaining the confidence of investors.

Statement of compliance

The version of the Code[1] applicable to the current reporting period is the September 2012 UK Corporate Governance Code. Throughout the year, the Company complied with the provisions of the Code, except for provision B.2.3, which requires Non-Executive Directors to be appointed for a specific term because the Company's two major shareholders are entitled to appoint a Non-Executive Director for so long as they each hold 7% of the then issued ordinary share capital of the Company, as detailed on page 50 of this Corporate Governance report.

The Audit Committee report on pages 54 to 57, the Nomination report on page 58 and the Directors' remuneration report on pages 59 to 74 are also incorporated into this report by reference.

Role of the Board

The Company is controlled through its Board. The Board's main role is to create long-term value for shareholders by providing entrepreneurial and prudent leadership of the Company, setting the Company's strategic aims, ensuring that the necessary financial and other resources are available and that the appropriate controls are in place to deliver these objectives.

The Board has adopted a schedule of matters specifically reserved for its approval. The schedule details key aspects of the affairs of the Company which the Board does not delegate, including key strategic, operational and financial issues. A copy of the schedule of matters can be found on the Company's website at **www.costain.com**

The Group's organisational structure is established and overseen by the Board and designed to allow effective decision-making and to meet corporate governance standards. A diagram illustrating the structure is shown above.

The Board has established Committees which are responsible for audit, remuneration and succession. Each Committee plays a vital role in helping the Board to ensure that high standards of corporate governance are maintained throughout the Group. The Committees are governed by terms of reference which are reviewed annually and can be viewed in the corporate governance section of the Company's website. The members of each Committee and details of their attendance are shown on page 49.

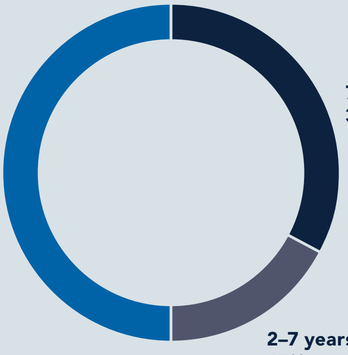
The Group Executive Board is accountable for running the business and delivering the Group strategy. It consists of the Executive Directors and other senior managers, is chaired by Andrew Wyllie (Chief Executive) and works with the support of a number of operational committees and functions. Further details can be found on page 17.

Board composition

As at the date of this report, the Board comprised the Chairman, two Executive Directors and four independent Non-Executive Directors and one nominee Non-Executive Director. The nominee Non-Executive Director is nominated by one of the Company's major shareholders, Mohammed Abdulmohsin Al-Kharafi & Sons Company for General Trading, General Contracting and Industrial Structures WLL. The membership of the Board and biographical details of all the Directors can be found on pages 46 to 47.

[1] A copy of the Code is publicly available at www.frc.org.uk

Length of Service
Non-Executive Directors as at 31 December 2014



The biographies illustrate that the Non-Executive Directors have a range of business and financial experience that is important and relevant to the management of the Company. The Board believes that there is an appropriate balance between Executives and Non-Executives and that this balance is enhanced by the varying lengths of service of the Non-Executive Directors depicted in the pie-chart above.

The Board recognises the importance of greater diversity (not just gender specific) in the boardroom and throughout the business, further details of which are given in the Nomination Committee report on page 58.

The Directors' attendance record at the scheduled Board meetings and Board Committee meetings for the year ended 31 December 2014 is shown in the table below. For the Board and Committee meetings, attendance is expressed as the number of meetings that each Director attended out of the number that they were eligible to attend. In addition, ad-hoc meetings were arranged to deal with matters between the scheduled meetings as appropriate.

Board independence

The Board considers each of its independent Non-Executive Directors to be independent in character and judgment and there are no relationships or circumstances which are likely to affect (or could appear to affect) the judgment of such Non-Executive Directors.

The Nomination Committee continues to review succession on a regular basis.

At the time of his original appointment in January 2008, the Chairman of the Company was considered independent by the Board. However, in accordance with the Code, the ongoing test of independence is not applicable in relation to the Chairman.

The Company complies with the requirement under provision B.1.2 of the Code that at least half of the Board, excluding the Chairman, should comprise Non-Executive Directors determined by the Board to be independent, notwithstanding that this requirement is waived in respect of smaller companies, such as the Company, which are members of the FTSE SmallCap Index.

Appointments to the Board and retirement of Directors

Alison Wood was appointed to the Board as a Non-Executive Director on 1 February 2014 and succeeded Mike Alexander as Chair of the Remuneration Committee upon his retirement from the Board on 31 March 2014. David McManus was appointed to the Board as a Non-Executive Director on 12 May 2014.

The appointment and replacement of Directors is governed by the Company's Articles of Association, the Code, the Companies Act 2006 and related legislation. The Articles of Association may be amended by a special resolution of the Company's shareholders. The Company's Articles of Association require that all Directors, including nominee Non-Executive Directors, should be subject to election by shareholders at the first opportunity after their appointment and to re-election thereafter at intervals of no more than three years. The Company's Articles of Association also provide that Non-Executive Directors who have served for longer than nine years should be subject to annual re-election. Accordingly, the aforementioned provisions of the Company's Articles of Association comply with provision B.7.1 of the Code, as applicable to smaller companies below the FTSE 350.

	Board Maximum 8	Audit Committee Maximum 5	Remuneration Committee Maximum 5	Nomination Committee Maximum 1
Executive Directors				
Andrew Wyllie	8/8	5[(d)]	3[(d)]	1[(d)]
Tony Bickerstaff	8/8	5[(d)]	2[(d)]	1[(d)]
Non-executive Directors				
David Allvey	8/8	5[(d)]	4[(d)]	1/1
James Morley	7/8	3/5	5/5	1/1
Mike Alexander[(a)]	2/2	2/2	1/1	n/a
Jane Lodge	8/8	5/5	5/5	1/1
Alison Wood[(b)]	8/8	5/5	5/5	1/1
David McManus[(c)]	5/5	3/3	2/2	1/1
Ahmed Samy	7/8	n/a	n/a	1/1

(a) Retired from the Board with effect from 31 March 2014.
(b) Appointed to the Board with effect from 1 February 2014 and appointed as Chair of the Remuneration Committee with effect from 1 April 2014.
(c) Appointed to the Board with effect from 12 May 2014.
(d) Not a member of the Committee – attendance at meeting by invitation.

Corporate Governance report continued

Board effectiveness

The Board has established a formal process for the evaluation of the performance of the Board and its principal Committees.

An externally facilitated Board review was conducted between November 2014 and January 2015 by SCT Consultants Ltd (who, having no other connection with the Company, were considered to be independent). The process involved the completion of detailed online questionnaires by all Board members and the Company Secretary, observation of a Board meeting, document review and interviews with Board members and the Company Secretary.

The results of the evaluation were discussed at the February 2015 Nomination Committee meeting attended by all Board members and the Board has already started to formulate the necessary actions in order to focus on the perceived areas of improvement and will continue to review its procedures, effectiveness and development in the financial year ahead.

The Board considers that the performance review shows that each Director continues to contribute effectively and the Board as a whole demonstrates good practice on the key indicators of Board effectiveness.

The next independently facilitated review is expected to take place in 2016/17 in accordance with provision B.6.2 of the Code, notwithstanding that this requirement is waived in respect of smaller companies, such as the Company, which are members of the FTSE SmallCap Index.

Re-election

In accordance with the Company's Articles of Association and provision B.7.1 of the Code, David Allvey, Andrew Wyllie and David McManus will offer themselves for re-election at the next Annual General Meeting. Having due regard to the results of the externally facilitated review of the Board's performance conducted by SCT Consultants Ltd, and to periodic internal evaluations, the Board confirms that it is of the opinion that each of the Directors standing for re-election continues to make an effective and valuable contribution to the Board and should therefore be re-elected at the forthcoming Annual General Meeting.

The Chairman and Non-Executive Directors all have terms and conditions of appointment which are available for inspection during normal business hours at the Company's registered office.

An independent Non-Executive Director's appointment is for an initial period of three years, at the expiry of which time the appointment is reviewed to determine whether the appointment should continue. Mohammed Abdulmohsin Al-Kharafi & Sons Company for General Trading, General Contracting and Industrial Services WLL and the other major shareholder UEM Builders Berhad are each entitled to appoint a Non-Executive Director for so long as these shareholders each hold 7% of the aggregate nominal value of the then issued ordinary share capital of the Company. UEM Builders Berhad has not taken advantage of this option since 4 December 2009. In consequence, the Company did not comply with provision B.2.3 of the Code, which requires that all Non-Executive Directors should be appointed for a specific term.

Board induction and training

On appointment, the Directors take part in an induction programme, pursuant to which they receive information about the Group, the role of the Board and the matters reserved for its decision, the terms of reference and membership of the principal Board Committees and the powers delegated to the Committees, the Group's corporate governance practices and procedures, and the latest financial information about the Group.

As regards the continuing professional development of the Executive and Non-Executive Directors, Board members, independent of any formal training arranged by the Company, are encouraged to attend seminars and conferences on issues relevant to their appointment as Directors of a public company, particularly matters concerned with corporate governance, audit and remuneration issues. In addition, Board site visits are considered essential to ensure that Directors have a thorough understanding of the business operations and issues that affect the Group. The Board also takes part in the Company's Health and Safety training programmes.

Operation of the Board

In order to discharge their duties, the Directors are provided with full and timely access to papers prior to Board meetings via a fully encrypted electronic portal system. Directors are also free to seek any further information they consider necessary. In addition, between Board meetings, the Chairman and Non-Executive Directors have access to the Chief Executive, Finance Director and Company Secretary in order to progress the Company's business. The Chairman and Non-Executive Directors also receive a weekly report from the Chief Executive, monthly management accounts, internal audit reports and regular management reports and information, which enable them to scrutinise the Group and its management's performance against agreed objectives.

All Board members have access to all information relating to the Group and have access to the advice and services of the Company Secretary (who is responsible for ensuring that Board procedures are followed) and who is also the Company's Legal Director. The appointment and removal of the Company Secretary is a matter reserved for Board approval. The Board also obtains advice from professional advisers as and when required at the expense of the Company.

Directors' conflicts of interest

The Company has procedures in place for managing conflicts of interest. The Board has satisfied itself that there is no compromise to the independence of the Directors who have appointments on the boards of, or relationships with, other companies. The Board requires Directors to declare all appointments which could result in a possible conflict of interest and has adopted appropriate processes to manage and, if appropriate, approve any such conflict.

Corporate Responsibility (CR)

The Board receives reports from the Company's CR Director and monitors progress on a regular basis.

Shareholder communication and engagement

The Company remains committed to maintaining good relationships with both institutional and private shareholders. There continues to be regular dialogue with institutional investors and brokers.

Towards the end of 2014, the Group's CR Director was also appointed as the Investor Relations Director, reflecting the Company's continued commitment to investor relations.

At the time of the announcement of the full-year and half-year results, presentations are made to brokers' analysts, the press and institutional investors. These presentations are available on the Company's website at **www.costain.com**. In addition, there are meetings with analysts, financial journalists and institutional investors throughout the year including a 'Capital Markets Day' held on 5 November 2014.

The Chairman is available to discuss strategy and governance issues with shareholders, and James Morley, as the Senior Independent Director, is available to shareholders if they have concerns that have not been, or cannot be, addressed through the Chairman.

The Company obtains feedback from its brokers, Investec and Liberum Capital, on the views of institutional investors on a non-attributed basis. As a matter of routine, the Board reviews reports from its brokers on issues relating to recent share price performance, trading activity and institutional sentiment. The Board also receives copies of relevant analysts' reports on an ad-hoc basis.

The Board regards the Annual General Meeting as an important opportunity to communicate directly with shareholders. Board members, including the Chairs of the Remuneration, Nomination and Audit Committees, attended the 2014 meeting and propose attending the 2015 meeting where they will be available to answer questions.

Shareholders may raise issues or concerns by contacting the Group's Investor Relations Director via the email address stated on the Company's website or by writing to the Company Secretary.

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Corporate Governance report continued

Risk management and internal control

Risk management

The Board is responsible for making a robust assessment of the principal risks facing the Company and for ensuring that appropriate mitigating actions are in place to manage them.

The principal risk and uncertainties facing the Company at the date of this report can be found on pages 28 to 30 of the Strategic report.

Risk management processes are incorporated within the Company's normal management and governance processes at all levels and form an integral part of the day-to-day activity of the Company. For example, at the pre-bid stage, a risk appetite document is used to determine whether to pursue an opportunity or not. Risks are also identified as part of the work winning process , including a pre-qualification and pre-tender review process for obtaining approval to bid a project from the Investments Committee. Following contract award, there is a continuous review of risks and opportunities by both the contract leader and commercial manager. These are updated on a monthly basis and the top five risks and opportunities are reviewed by Group senior management.

The Company also has a corporate risk and opportunity register, which is monitored and updated regularly by the Group Executive Board, as well as sector business risk registers. The Board and Audit Committee receive reports on the Company's main corporate risks and opportunities.

The risk management strategy is regularly reviewed and the Group's risks and opportunities compared against those of other blue-chip companies. The Group reviews any changes in moving into new markets, such as its recent move into technology contracts, and attempts to identify any emerging risks and possible effects on the business.

Internal Audit provides independent assurance that risks inherent to the Company's business processes are reasonably controlled and assists management in assessing those risks and how effectively they are managed by internal controls. Internal Audit also promotes best practice in risk management processes to ensure delivery of corporate objectives.

In 2014, Internal Audit conducted project and departmental reviews to appraise and report on the effectiveness of the risk management processes. All reviews carried out were subject to appropriate follow-up action to provide assurance that accepted recommendations have been implemented effectively. The overall assessment is that there is a strong risk management culture within the Group which is continuing to develop.

The Board also assesses the effectiveness of the Group's reporting controls to ensure that the Group's risk profile reflects its strategic objectives.

Internal controls system

The Board is responsible for the Group's system of internal controls and for reviewing its effectiveness. Such a system, however, can only manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss.

The Board maintains full control over strategic, financial, operational and compliance issues. Management of the Group is delegated to the Chief Executive, who is assisted by members of the Executive Board. The Chief Executive has full authority to act subject to the matters reserved to the Board and to the requirements of Group policies.

Following the introduction in 2013 of 'the Costain Way', a common platform which contains all governance, controls, policies and procedures, the Company has further fine-tuned the control environment and delivered training to its users.

The effectiveness of the Company's risk management and internal control systems are regularly reviewed by the Board, in compliance with the Code and such a review was undertaken during the year. The review covered all controls, including financial, operational and compliance controls and risk management.

Operational controls

Controls and procedures are detailed in Group policy statements, procedure manuals and other written instructions, which are reviewed and updated regularly.

The Company uses an operational management system ('the Costain Way'). The objective of the Costain Way is to provide assurance that:

- Company activities across the business are compliant with appropriate legislation and codes of practice;
- Company systems, procedures and processes are effective at mitigating identified risks;
- customer expectations are understood, communicated and effectively delivered;
- management controls are consistently applied across the Group; and
- performance is reviewed, validated and continually improved.

The Costain Way has been externally certified by BSi as compliant to ISO 9001, ISO 14001, OHSAS 18001, ISO 22301, ISO 27001 and BS 11000.

Each contract leader completes monthly reports, that include information on safety, health and environmental statistics, cash flow, value, cost and profit, claims and variations, risk management, progress and staffing levels. All projects operate within a controlled framework of best practice, safety, health and environmental guidelines and the project management team monitors, and the safety, health and environmental advisers audit, compliance with, and execution of, those guidelines.

The Board and Group Executive Board receive regular reports on safety, health and environmental performance and significant operational matters. The Group Executive Board is responsible for ensuring compliance with Company procedures. The Chief Executive is the Board member responsible for Health and Safety.

Financial controls

There is a comprehensive annual budgeting system, linked to the annual strategy review, for each business within the Group. The budget for the following year is reviewed and finalised by the Executive Board, alongside the three-year business plan, before final approval by the Board in December.

The Company also has in place internal controls and risk management systems in relation to the Company's financial reporting process and the Group's process for preparation of consolidated accounts. These internal controls are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes. The Company produces a monthly rolling forecast update for the current year which is compared with the annual budget. Each division's performance is reviewed monthly by management and reported against budget to the Board and Executive Board. The reports cover profit and loss and cash flow with an accompanying narrative on significant issues underlying the financial reports. Furthermore, a review of the consolidated financial statements is completed by management to ensure that the financial position and results of the Group are appropriately reflected therein. The Group Treasurer and Group Taxation Manager also report to the Audit Committee, via the Finance Director, on any issues of significance to the Group.

Compliance

The Group's policies contain a statement on business conduct, emphasising the legal, ethical and moral standards that must be employed in all the Company's business dealings. This statement is regularly reviewed and updated as appropriate to ensure compliance with any change in legislation. The Company expects the highest standards from all employees, suppliers and joint venture partners.

In the event of a critical legal issue, a legal report is submitted to the Board. An annual review of all litigation valued above £50,000 is submitted to, and reviewed by, the Board. Significant legal and regulatory changes are notified to the appropriate staff and training given where necessary.

Audit Committee report

"The robust assessment of principal risks facing the Company will continue to be an area of focus."

Jane Lodge, Chair of the Audit Committee

Chairman's summary statement

Dear Shareholder

I am pleased to take this opportunity, on behalf of the Board, to present our report on the work of the Audit Committee ('the Committee') in respect of the year ended 31 December 2014.

In this report, we have set out the Committee's ongoing responsibilities and key tasks undertaken over the last year including reviewing the appropriateness of the Company's financial reporting, the effectiveness of the Company's risk management and internal controls systems, together with the robustness of the internal and external audit process.

Looking ahead, the Committee welcomes the changes to the revised UK Corporate Governance Code ('the Code') and the Financial Reporting Council's ('the FRC') Guidance on Risk Management, Internal Control and Related Financial and Business Reporting issued in September 2014. These changes apply to accounting periods beginning on or after 1 October 2014 and the Company has started to monitor the Company's risk management and internal control systems on an ongoing basis and a robust assessment of principal risks facing the Company will continue to be an area of focus.

Jane Lodge
Chairman of the Audit Committee
02 March 2015

Operation of the Committee

The Committee is comprised exclusively of independent Non-Executive Directors. The members of the Committee and details of their attendance at meetings are given on page 49. Biographies are shown on pages 46 to 47.

The Company considers that it has in Jane Lodge, as Chair of the Audit Committee, an appropriate person possessing what the FRC's Guidance on Audit Committees describes as recent and relevant financial experience. Prior to joining the Costain Board, Jane, a chartered accountant, spent 35 years at Deloitte LLP (UK), with 25 years as an audit partner advising global companies, particularly in the manufacturing, house-building and property and construction sectors. She was also senior partner of the Birmingham office and the Deloitte UK Manufacturing Industry Sector.

The meetings of the Committee are normally also attended by the Chairman, the Chief Executive, the Finance Director, the External Auditor, the Head of Internal Audit and the Group Financial Controller. Other senior executives will attend as required to provide information on matters being discussed which fall into their area of responsibility. The Committee regularly meets privately with the External Auditor and Head of Internal Audit. The Company Secretary is the Secretary to the Committee.

Terms of reference

The Committee's terms of reference are available from the Company Secretary and are published on the Company's website at **www.costain.com.** These are reviewed annually and some minor changes were made in 2014.

Role of the Audit Committee

In accordance with its terms of reference and in compliance with the Code, the Committee is responsible for:

- monitoring the integrity of the Group's financial statements and any formal announcement relating to the Group's performance, and reviewing significant financial judgments contained in them;
- monitoring the effectiveness of the external audit process and making recommendations to the Board in relation to the appointment, reappointment and remuneration of the External Auditor;
- ensuring that an appropriate relationship between the Group and the External Auditor is maintained, including reviewing non-audit services and fees;
- reviewing the Group's system of internal controls and the processes for management of the risks facing the Group;
- reviewing the effectiveness of the internal audit function and approving, in consultation with the Chief Executive, the appointment and termination of employment of the head of that function; and
- reviewing its terms of reference and its effectiveness from time to time and recommending to the Board any changes required as a result of the review.

Principal activities during the year

In 2014, the principal activities of the Committee and the manner in which it discharged its responsibilities were as follows:

Financial statements

The Committee reviewed the Group's draft financial statements, preliminary and interim results and reports from the External Auditor, on the outcome of its reviews and audits in 2014.

Significant accounting matters

The Committee considered key accounting issues, matters and judgments in relation to the Group's financial statements and disclosures relating to:

(1) Key contract judgments

As more fully explained in Note 2, on pages 92 to 98, the majority of the Group's activities are undertaken via long-term contracts and these contracts are accounted for in accordance with IAS 11, which requires estimates to be made for contract costs and revenues. These costs and revenues may be affected by a number of uncertainties that depend on the outcome of future events and may need to be revised as events unfold and uncertainties are resolved.

Management bases its judgments of costs and revenues and its assessment of the expected outcome of each long-term contractual obligation using detailed contract valuations and forecast of the costs to complete. Given the Company's extensive portfolio of contracts, a large proportion of time was spent by the Committee during the year reviewing the positions and judgments taken by management on a number of material contracts across the Group, through discussions with management and the External Auditor.

This review included inter alia consideration of the Manchester Waste Disposal Authority PFI contract awarded in 2007. The Committee noted that during December 2014, handover was achieved on the final waste facility. All 46 facilities on the contract are now either fully completed or in the warranty period under the terms of the contract, during which some further work and plant modifications will be completed. In achieving handover of the final facility, the Group received in December 2014 contractual retention and milestone payments of £14 million. It was also noted that the Group is in discussions with relevant contract counterparties and the Group's insurers regarding the issues that have arisen on the contract. The Board expects a successful outcome to these discussions. During the year, a provision has been taken for additional costs to complete the project. It has been the Group's policy since 2009 not to pursue fixed-price contracts of this nature.

On the basis of these reviews, the Committee concluded that it was content with the judgments that had been made.

Audit Committee report continued

(2) Pension

The Group's defined benefit scheme requires significant judgments in relation to the assumptions for inflation, future pension increases, investment returns and member longevity that underpin the valuation. Each year, in selecting the appropriate assumptions, the Committee takes written advice from an independent qualified actuary. The assumptions and sensitivities are set out in Note 20 on pages 120 to 123.

(3) The carrying value of goodwill and intangible assets

As set out in Note 11 on page 107, the goodwill and acquired intangible balances within the Group relate to the acquisition of companies. During the year ended 31 December 2014, the Committee critically reviewed the analysis performed by management on goodwill and intangibles and agreed with the amortisation charge in respect of intangibles and that no impairment to goodwill was necessary.

(4) Alcaidesa Holding SA

The Committee has reviewed the net realisable value of each of the land holdings in Spain held by the Group's 50:50 joint venture. The Committee addressed this issue by considering the report from management on the review carried out of the net realisable value of each of the land holdings in Spain and of the carrying value of the marina assets, and the golf courses including the use of external valuations. The Committee agreed that no further impairment should be taken against the assets of the joint venture.

(5) Cash flow and working capital

The Group's processes for the management of cash flow and working capital is also an area which the Committee has reviewed in detail, particularly in view of the capital raising which took place in March 2014. The Committee concluded that it was satisfied with these processes.

(6) Future IFRS and UK GAAP developments

During the year, the Committee received a management report from the External Auditor regarding future accounting developments likely to affect the presentation of the Group's financial statements including capitalisation of operating leases and revenue recognition on long-term contracts.

Independence of the External Auditor

The Company's External Auditor is KPMG LLP ("KPMG").

In order to ensure the independence and objectivity of the External Auditor, the Committee monitors the non-audit services being provided to the Group by its External Auditor, and has adopted a policy on the provision of non-audit services by the External Auditor with the objective of ensuring that such services do not impair the independence or objectivity of the External Auditor.

The policy also sets out a number of key principles that underpin the provision of non-audit services by the External Auditor: the External Auditor should not audit its own firm's work; make management decisions for the Group; have a mutuality of financial interest with the Group; or be put in the role of advocate for the Group.

Approval of the Committee is required for any services provided by the External Auditor where the fee is likely to be in excess of £25,000. The Committee reviews all services being provided by the External Auditor annually to assess the independence and objectivity of the External Auditor, taking into consideration relevant performance and regulatory requirements, so that those are not impaired by the provision of permissible non-audit services.

In 2014, the External Auditor performed non-audit services in reporting on working capital in connection with the capital raising. The External Auditor was selected as the most cost-effective and efficient supplier to undertake these services based on their thorough understanding of the Group and their particular expertise. In the financial year, the Company spent £0.4 million (2013: £1.7 million) with the External Auditor in respect of non-audit fees.

In accordance with best practice and professional standards, the Company also requires its External Auditor to adhere to a rotation policy whereby the audit engagement partner is rotated after five years. The External Auditor is also required to periodically assess whether, in its professional opinion, it is independent and those views are shared with the Audit Committee.

The Senior Statutory Auditor (who has signed the Audit report on behalf of KPMG on page 82) is Mr Andrew Marshall who was appointed as the lead audit partner at the beginning of 2013.

The Audit Committee is satisfied that the independence of the External Auditor is not impaired given the audit engagement partner has recently changed and that the amount of non-audit fees are of a level that does not impact upon KPMG's objectivity and independence.

Audit quality and approach to audit tender

As part of a formal review process, external audit effectiveness questionnaires are completed by members of the Committee, the Executive Directors, other members of the Executive Board Committee and certain members of the finance team. Based on the responses to the questionnaires, the Company Secretary produces a report for detailed consideration by the Committee.

Based on its consideration of the report, together with its own ongoing assessment, for example, through the quality of the External Auditor's reports and the audit partner's interaction with the Committee, the Committee remains satisfied with the efficiency and effectiveness of the external audit.

The Committee has not therefore considered it necessary to require the audit to be put out to tender. The Committee continues to be satisfied with the work of the External Auditor, considers that it remains objective and independent and has unanimously recommended to the Board that a resolution for the reappointment of KPMG as the Company's External Auditor be proposed to shareholders at the 2015 AGM.

The Committee recognises the requirements in the 2012 Code that the External Audit contract be put out to tender at least every ten years, notwithstanding that this requirement is waived in respect of smaller companies, such as the Company, which are members of the FTSE SmallCap Index. In addition, the Committee has also discussed the new EU regulation in relation to rotation including the proposed transition rules and has considered the potential optimum timing for a tender of the External Audit. The lead audit partner was not present during such discussions.

Risk management and internal controls

Details of the Group's internal controls and risk management are more fully set out on pages 52 to 53 of the Corporate Governance report.

The Committee has evaluated the effectiveness of the system of internal controls and risk management operated within the Group pursuant to the FRC's guidance on internal control. The evaluation covered all controls, including financial, operational and compliance controls and risk management.

The Committee has also considered the confidential reporting and whistle blowing procedures the Company has in place and is satisfied with the process.

Internal audit

The Group has an internally resourced internal audit function reporting directly to the Committee. The Committee is responsible for monitoring and reviewing the operation and effectiveness of this function. During the year, the Committee undertook an internal assessment of the effectiveness and independence of the internal audit function.

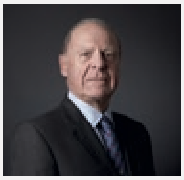
The Committee has received regular reports on the programme and findings of reviews at each of its meetings during the course of the year and action plans to resolve any highlighted areas.

The Company has decided to create a new role of Group Risk Manager who will be responsible for the management of risk across the Group and will be accountable directly to the Committee.

Accountability

The Board is required to present a fair, balanced and understandable assessment of the Company's financial position and prospects. The responsibilities of the Directors and External Auditor are set out on pages 79 to 82. As set out in the Director's report, the Directors consider the Company's business is a going concern.

Nomination Committee report



"The Board aims to have a broad range of skills, backgrounds and experience whilst following a policy of ensuring that the best people are appointed".

David Allvey, Chairman

Dear Shareholder

The Nomination Committee ('the Committee') is comprised exclusively of independent Non-Executive Directors. The members of the Committee and details of their attendance at Committee meetings are given on page 49. Biographies are shown on pages 46 to 47.

Role of the Committee

The principal role of the Committee is to review the structure and composition of the Board and to identify and propose to the Board suitable candidates to fill Board vacancies.

The Committee directs the periodic Board effectiveness reviews, both internal and external, which forms part of the regular evaluation and development work conducted by the Board to ensure it continues to improve its overall effectiveness. The Committee also reviews management training and succession planning arrangements in respect of the Company's senior executives. The Company Secretary is the Secretary of the Committee.

The Board aims to have a broad range of skills, backgrounds and experience whilst following a policy of ensuring that the best people are appointed. Within this context, and as part of the ongoing process of refreshing the Board, the Company will continue to encourage and welcome interest from candidates drawn from a diverse background, who will add to the Board's diversity.

As reported last year, with effect from 1 February 2014, Alison Wood was appointed as a Non-Executive Director and became Chair of the Remuneration Committee with effect from 1 April 2014 upon the retirement from the Board of Mike Alexander.

With effect from 12 May 2014, David McManus was appointed to the Board as a Non-Executive Director. The Committee instructed Odgers Berndtson (who do not have any other connection with the Company) to identify appropriate external candidates, and after meetings with shortlisted candidates, the Committee identified David McManus as a suitable appointee and recommended his appointment to the Board. David brings considerable experience to his role and enhances the skill set of the Board as a whole.

Main activities during the year

In 2014, the Committee discharged its responsibilities by performing the following activities:

- Reviewing the overall structure and composition of the Board;
- Commissioning an independent external review of Board effectiveness, facilitated by SCT Consultants Ltd ('SCT'), which concluded in December 2014. Following the completion of a questionnaire, each member of the Board was interviewed individually on a confidential basis by SCT and the results of the external review were then discussed by the Nomination Committee. Further details of this review can be found on page 50 of the Corporate Governance report;
- Reviewing potential candidates for the position of Non-Executive Director and making recommendations to the Board as to their appointment;
- Receiving notifications from Directors of situations, such as proposed external appointments, in which a potential conflict of interest may arise;
- Reviewing/recommending to the Board the reappointment of those Directors who are due to offer themselves for re-election at the Annual General Meeting in accordance with the Articles of Association, following due consideration of the Board's policy on independence and the results of periodic Board performance reviews;
- Reviewing succession planning in respect of the Executive Directors; and
- Reviewing succession planning and development of talent in respect of the Company's senior executives.

David Allvey
Chairman
02 March 2015

Directors' remuneration report

"We continue to take a disciplined approach to ensure that our remuneration framework supports the strategic direction of the Company".

Alison Wood, Chair of the Remuneration Committee

Chairman's summary statement

Dear Shareholder

I became Chairman of the Remuneration Committee ('the Committee') with effect from 1 April 2014, having been a member since joining the Company's Board in February 2014.

I am pleased to present, on behalf of the Board, our Directors' remuneration report in respect of the year ended 31 December 2014.

Remuneration Policy

Last year, we made a number of changes to our Executive Director remuneration framework in order to simplify the structure and shift the balance of Executives' incentives towards the long-term without increasing the overall level of incentive pay. These changes were set out in our Policy report which was subject to a binding vote at our 2014 AGM. We were pleased that the Policy report was approved by shareholders with a 97% vote in favour (including discretionary votes).

During 2014, we have not made any significant changes to our remuneration arrangements and we continue to take a disciplined approach to ensure that our remuneration framework supports the strategic direction of the Company and the implementation of our *'Engineering Tomorrow'* strategy.

The following is an overview of how our remuneration policy supports the strategic priorities of the business as set out on pages 20 to 25 of the Strategic report:

- The Health and Safety of our people and everyone who is involved with Costain remains our highest priority. Accordingly, the performance metrics for our Annual Incentive Plan ('AIP') includes a key non-financial indicator around Health and Safety targets;
- To encourage behaviours which facilitate the delivery of sustainable growth and the future development of the business, allowing us to meet our business goal of delivering value to all our stakeholders:
  - the performance metrics for our AIP aim to balance earnings growth and other key financial objectives (including cash and order book targets) with non-financial indicators, particularly Health and Safety targets and specific individual objectives;
  - a third of any AIP award earned is deferred into shares to ensure that executives consider the longer term impacts of their decisions and the effect on the sustainability of the business;
  - our Long-Term Incentive plan ('LTIP') captures long-term growth in earnings. An additional two years' deferral on half the LTIP was introduced last year to support longer-term alignment between Executive Directors and shareholders; and
  - the performance targets are set to reward sustainable business performance, whilst not encouraging inappropriate business risks to be taken;
- To support our goal to develop a best-in-class team, our remuneration policy is designed to attract and retain high-calibre individuals in an increasingly competitive market and to remunerate executives fairly and responsibly.

Directors' remuneration report continued

Performance and variable pay outcomes for the year ended 31 December 2014

As described in the Strategic report, the Company continues to perform strongly delivering profitable earnings growth and strong progress against the Company's key strategic priorities. The key highlights are as follows:

- Revenue increased to £1.1 billion (2013: £960.0 million)
- Underlying operating profit up to £28.7 million (2013: £27.4 million)
- Net cash balance of £148.5 million (2013: £57.7 million)
- Record forward order book up 17% to £3.5 billion (2013: £3.0 billion)
- Over £1.0 billion of revenue secured for 2015, (as at 31 December 2013: over £750 million secured for 2014)

The performance targets set for both the AIP and LTIP represent a significant stretch. Taking into account the performance achieved during the year, AIP payments to Executive Directors were 71.6% and 75.3% of the maximum AIP opportunity for the Chief Executive and Finance Director respectively. Further rationale for these payments can be found on pages 66 to 67.

The LTIP award granted on 9 May 2012 was based on performance to the year ended 31 December 2014 and is due to vest in May 2015 (subject to the Committee's determination that the performance conditions have been met) at 50% of maximum, in light of aggregate adjusted EPS of 107.7 pence delivered over the performance period.

Reward changes for 2015

No changes are being made to our reward framework in 2015.

We approved salary increases for the Executive Directors of 2.5% after carefully considering their performance, the range of salary increases awarded to other employees and market reference points.

Conclusion

The following pages describe in further detail how we have implemented our remuneration policy in respect of 2014, together with our approach for 2015.

The Policy report approved last year will remain in force. We have therefore published the Policy table but not the full Policy section, recognising that it was approved by shareholders at our 2014 AGM. The Policy report in its entirety is available on our website in the 2013 Annual Report.

Overall, given the Company's performance over the one- and three-year periods to the end of the 2014 financial year, we believe that the remuneration of the Executive Directors in respect of 2014 reflects our success in the delivery of our *'Engineering Tomorrow'* strategy and the drive for long-term growth for our shareholders.

Alison Wood
Chair of the Remuneration Committee
02 March 2015

Remuneration disclosure

This report, approved by the Board, has been prepared in accordance with the provisions of the Companies Act 2006 and Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. It also meets the requirements of the UK Listing Authority's Listing Rules and the Disclosure and Transparency Rules.

It is unaudited unless otherwise stated. In this report we describe how the principles of good governance relating to Directors' remuneration, as set out in the UK Corporate Governance Code ('the Code'), are applied in practice. The Remuneration Committee ('the Committee') confirms that throughout the financial year the Company has complied with these governance rules and best practice provisions.

The report is in two sections:

- Extract from the Policy report. This section contains the policy table summarising the remuneration policy approved at the 2014 AGM and is for information only.
- The Annual Report on Remuneration. This section sets out details of how our remuneration policy was implemented for the year ended 31 December 2014 and how we intend for the policy to apply for the year ended 31 December 2015 and is the subject of an advisory shareholder vote.

Extract from the Policy report

This report sets out the Company's Policy on the remuneration of its Directors. This Policy was approved by shareholders under a binding vote at the AGM in 2014 and will apply until replaced by a new or amended policy.

Remuneration Policy for Executive Directors is set out below.

Element	Purpose and link to strategy	Operation	Maximum opportunity
Salary	• To attract and retain high-calibre individuals. • Reflects skills, experience over time. • Provides an appropriate level of basic fixed income whilst avoiding excessive risk arising from over reliance on variable income.	• Generally reviewed annually (with any change effective 1 April) but exceptionally at other times of the year. • Set with reference to individual performance, experience and responsibilities. • Reflects the market rate for the individual and their role, determined with reference to remuneration levels in companies of similar size and complexity, taking into account pay levels within the Company in general. • Higher increases may be appropriate where an individual is promoted, changes role or where an individual is appointed on a below-market salary with the expectation that his salary will increase with experience and performance.	• Salaries to apply for the year from 1 April 2015 are: – Chief Executive: £448,159 – Finance Director: £296,906 • There is no maximum salary value.
Annual Incentive Plan ('AIP')	• To incentivise the achievement of key financial and strategic targets for the forthcoming year without encouraging excessive risk taking. • Promotes greater alignment with shareholders. • To facilitate share ownership.	• The Committee considers and approves the measures and targets at the start of each year and ensures they are aligned with business strategy and are sufficiently stretching. • Financial metrics comprise at least three quarters of AIP opportunity, of which at least half will be a measure of Group profit. • In addition to these financial metrics, the AIP includes Health and Safety targets and personal objectives. • In setting financial parameters, the Committee takes into account the Company's internal budgets and, where applicable, investors' expectations. The targets applying to financial measures are based on a sliding scale. • Two-thirds paid in cash. • Not pensionable. • Deferral into shares of one third of earned AIP; this vests on the second anniversary of grant (subject to continued employment and not being under notice of termination, either given or received, on the date of vesting). • Shares provided under the AIP are typically purchased by a trust on behalf of the Group so as to not lead to any dilution of shareholder interest. • Awards may be subject to clawback if the Committee becomes aware of a material misstatement to the audited accounts, an error in calculation of targets resulting in an overpayment, gross misconduct or criminal behaviour on the part of a participant.	• Maximum: 150% of salary. • There is no minimum opportunity.

Element	Purpose and link to strategy	Operation	Maximum opportunity
Long-Term Incentive Plan ('LTIP')	• Aligned to main strategic objectives of delivering sustainable profit growth which in turn should deliver enhanced returns.	• Annual grant of performance shares, half of which vest after three years subject to continued service and performance targets, and half of which vest after five years (the final two years being subject only to continued service). • LTIP performance is measured over three years. • The performance condition consists of a measure of EPS over a three-year period, starting with the year of grant. • Awards may be subject to clawback if the Committee becomes aware of a material misstatement to the audited accounts, an error in calculation of targets resulting in an overpayment, gross misconduct or criminal behaviour on the part of a participant.	• LTIP awards with a face value of not more than 100% of salary. • Amount that is paid for achievement of threshold performance: 15% of the maximum.
SAYE Scheme	• Offered to all eligible UK employees, to facilitate share ownership and provide further alignment with shareholders.	• Periodic grants which normally vest after three or five years subject to continued service.	• Executive Directors are eligible to participate in the SAYE Scheme on the same terms as other employees.
Pension	• To aid retention and remain competitive in the market place.	• Annual pension allowance. • Paid as a cash contribution to the Defined Contribution pension scheme and/or a cash supplement.	• Allowance up to 22% of base salary.
Other benefits	• To aid retention and be competitive in the marketplace. • Healthcare benefits in order to minimise business disruption.	• Company car and fuel (or car allowance). • Medical insurance. • Life assurance.	• N/A.
Share ownership guidelines	• Further alignment of interests between Costain Board and shareholders.	• Executive Directors are required to build and maintain a shareholding worth not less than 100% of base salary through the retention of vested share awards or through open-market purchases.	• N/A.

Notes

The choice of the performance metrics applicable to the AIP reflect the Committee's aim that our annual incentives should balance the delivery of earnings growth and other key financial objectives with non-financial indicators, particularly Health and Safety targets, and specific individual objectives. The LTIP captures long-term growth in earnings, which we believe is most closely aligned with the financial performance expected by our shareholders.

The quantum of salary, benefits and incentive packages of Executives (and senior management) are set with reference to market comparatives and the impact of an individual's role. Employees below Executive level receive packages that are reflective of their role and typically have less emphasis on variable, performance-related pay than for Executive Directors. Long-term incentives are provided only for the most senior executives who, it is anticipated, have the greatest potential to influence the overall performance of the Company.

Remuneration Policy for Chairman and Non-Executive Directors

Element	Purpose and link to strategy	Operation	Maximum opportunity
Fees	• Attract and retain high-performing individuals.	• Remuneration for Non-Executive Directors, other than the Chairman, is determined by the Board, following consultation between the Chairman and the Chief Executive. The Chairman's fee is determined by the Board following consultation between the Committee and the Chief Executive. Fees are reviewed annually and any increase is effective from 1 April. • Remuneration for Non-Executive Directors, other than the Chairman, comprises a basic annual fee for acting as Non-Executive Director of the Company and additional fees for the Senior Independent Director, and chairmanship of the Audit and Remuneration Committees.	• N/A.
Share ownership guidelines	• Alignment of interests between Costain Board and shareholders.	• Non-Executive Directors are required to build and maintain a shareholding worth not less than 100% of their annual fee.	• N/A.

Annual Report on Remuneration

Operation of Committee

The Remuneration Committee is comprised exclusively of independent Non-Executive Directors. The members of the Committee and details of their attendance at the Remuneration Committee meetings are given on page 49. Biographies are shown on pages 46 to 47.

Alison Wood was appointed as a Non-Executive Director on 1 February 2014 and became chair of the Committee at the beginning of April 2014 upon the retirement from the Board of Michael Alexander.

Terms of reference

The Committee's terms of reference are available on the Company's website at **www.costain.com** or from the Company Secretary. Copies of the letters appointing the Committee's advisers can be obtained from the Company Secretary.

Remuneration Committee activity

The following table sets out the key remuneration issues which the Committee covered at each of the meetings over the course of the year.

Date	Key agenda items
5 February 2014	Approved the methodology to be used to determine the extent that EPS performance conditions have been met with regard to the LTIP granted in 2011
	Approved the methodology to be used to determine the extent to which the EBITA performance condition has been met for the proposed 2014 DSBP grant relating to the 2013 base year
	Approved the 2013 annual cash bonuses subject to final audit of the 2013 accounts
	Approved the Chairman's and Non-Executives' fees for 2014
	Reviewed the Directors' remuneration report
	Reviewed the draft resolutions seeking approval to the new 2014 LTIP and new 2014 SDP at the 2014 AGM
31 March 2014	Approved the methodology to be used to adjust the Company's various share plans following the capital raising approved by shareholders on 17 March 2014
	Approved the vesting of the 2011 LTIP
	Granted awards under the DSBP for the 2013 base year
	Noted the vesting of the 2012 DSBP
7 May 2014	Noted the approval by shareholders at the 2014 AGM of the new LTIP and SDP
	Noted that first awards under the SDP would be made in 2015 subject to eligible participants receiving a bonus in respect of the 2014 year end
	Approved an adjustment to the proposed performance targets for the 2014 LTIP grant to reflect the capital raising in March 2014
	Granted awards under the new 2014 LTIP
18 August 2014 (Annual Concept Meeting)	Reviewed market trends and shareholder sentiments
	Reviewed Executive Directors' remuneration, confirming overall packages are fit for purpose with an appropriate balance of incentives which align with strategy and which do not encourage excessive risk
	Reviewed the overall structure of the AIP, approving the harmonisation of deferral levels so that all eligible participants receive 33% of award achieved deferred in shares
9 December 2014	Approved amendments to the HMRC approved plans to reflect changes under the Finance Act 2014
	Approved the proposed 2015 LTIP performance targets
	Approved the proposed 2015 AIP performance measures and list of participants
	Approved the 2015 annual salary increases for the Executive Directors, Executive Committee and the wider workforce

Definitions:

LTIP: Long-Term Incentive Plan

DSBP: Deferred Share Bonus Plan

SDP: Share Deferral Plan

AIP: Annual Incentive Plan

Advice provided to the Committee

Advice was sought where appropriate from other sources. During the course of the year, the Chief Executive, the Finance Director, the Group's Chairman, the Group HR Director, and the Legal Director and Company Secretary were invited to attend various meetings of the Committee, although none was present when their own remuneration was being discussed.

To assist the Committee in ensuring that the Company's remuneration practices take due account of market and best practice, the Committee has access to experienced specialist independent consultants. During the year, the Committee took advice, as appropriate, from Deloitte LLP (a member firm of Deloitte Touche Tohmatsu Limited) and from New Bridge Street (a trading name of Aon Hewitt Limited).

It is the policy of the Committee to put the remuneration consultant function out to tender on a periodic basis to ensure that the Company continues to receive independent support and advice of a high standard. Following a tender process in 2014 by the Committee, Deloitte LLP were appointed in place of New Bridge Street to act as the Company's remuneration consultants. Deloitte LLP received fees of £50,208 and New Bridge Street received fees of £93,712 for the year ended 31 December 2014.

Both Deloitte LLP and New Bridge Street are founder signatories to the Remuneration Consulting Group's Code of Conduct. Neither Deloitte nor New Bridge Street (nor any other part of the Deloitte or Aon Hewitt group of companies) provided other services to the Company during the year and, having no other connection with the Company, Deloitte LLP and New Bridge Street are considered to be independent.

Voting on the remuneration report at the AGM in 2014

Last year's remuneration report was approved by shareholders with a 99.64% (2013 AGM: 96.90%) vote in favour (including discretionary votes).

Implementation of Policy in the year to 31 December 2014

Single Total Figure of remuneration for each Director

This table and the associated footnotes have been audited by KPMG LLP.

	2014						2013					
	Salary & Fees £	Taxable Benefits £	Pension* £	Annual Incentive £	LTIP** £	Total £	Salary & Fees £	Taxable Benefits £	Pension £	Annual Incentive*** £	LTIP**** £	Total £
Executive Directors												
A Wyllie	434,562	13,275	95,603	469,583	315,984	1,329,007	423,963	13,283	93,272	482,017	241,086	1,253,621
A O Bickerstaff	287,898	11,775	63,337	327,175	209,339	899,524	280,876	11,783	61,793	333,467	159,718	847,637
Chairman												
D P Allvey	135,226	–	–	–	–	135,226	131,928	–	–	–	–	131,928
Non-Executive Directors												
J A Lodge	52,722	–	–	–	–	52,722	51,437	–	–	–	–	51,437
D McManus[1]	28,165	–	–	–	–	28,165	–	–	–	–	–	–
J Morley	50,060	–	–	–	–	50,060	48,839	–	–	–	–	48,839
A Samy[2]	43,669	–	–	–	–	43,669	3,572	–	–	–	–	3,572
A J Wood[3]	44,919	–	–	–	–	44,919	–	–	–	–	–	–
S G Younis[4] (former Director)	–	–	–	–	–	–	39,032	–	–	–	–	39,032
M R Alexander[5] (former Director)	12,285	–	–	–	–	12,285	48,839	–	–	–	–	48,839

* Pension contributions of £40,000 were paid to Andrew Wyllie's chosen pension arrangement and the balance was paid to him directly as a taxable benefit. Pension contributions of £10,000 were paid to Anthony Bickerstaff's chosen pension arrangement and the balance was paid to him directly as a taxable benefit.

** The value of the 2012 LTIP which is due to vest in 2015 is subject to the Committee's determination (see Note (c) below).

*** The Annual Incentive for 2013 includes payments under the legacy annual bonus scheme and legacy DSBP.

**** Figures adjusted following capital raising in March 2014 and using the share price as at the date of exercise being £2.65.

[1] Appointed as a Non-Executive Director w.e.f. 12 May 2014.

[2] Appointed as a Non-Executive Director w.e.f. 30 November 2013.

[3] Appointed as a Non-Executive Director w.e.f. 1 February 2014 and as Chair of the Remuneration Committee w.e.f. 1 April 2014.

[4] Retired as a Non-Executive Director w.e.f. 30 November 2013.

[5] Retired as a Non-Executive Director w.e.f. 31 March 2014.

Additional Notes to the single total figure of remuneration

(a) Taxable benefits provided to Executive Directors

The main benefits available to the Executive Directors during 2014 (and their approximate values) were a car allowance of £12,000 (2013: £12,000) for Andrew Wyllie and £10,500 (2013: £10,500) for Anthony Bickerstaff together with private medical insurance for both Executive Directors of £1,275 (2013: £1,283). This package of benefits was unchanged from 2013.

(b) Determination of the 2014 Annual Incentive

As reported in last year's Directors' remuneration report, during 2013 the Committee decided to simplify the structure of the annual bonus plan by combining the annual cash bonus and the legacy Deferred Share Bonus Plan (DSBP) into one Annual Incentive Plan (AIP). The operation of the deferred element of the new AIP was approved by the Company's shareholders at the 2014 AGM.

The combined maximum AIP opportunity for the Chief Executive and the Finance Director for the year ended 31 December 2014 remained unchanged from 2013 at 150% of base salary, with one-third of the earned AIP award to be deferred into shares for a further two years (i.e. maintaining the same level of deferral as under the operation of the legacy DSBP) and two-thirds of the earned AIP award paid in cash. Grants will be made under the Company's Share Deferral Plan (SDP) in March 2015.

The performance measures established by the Committee for the 2014 AIP continued to align reward with the Company's *'Engineering Tomorrow'* strategy whilst not encouraging inappropriate business risks to be taken. These included inter alia a maximum target measure of £31.6 million for Group EBITA[1]. In addition, all measures were subject to an underpin for cash in order to encourage the timely collection of cash. This underpin is defined as "cash received by the Group from project and contract operations equal to 90% of budgeted gross margin". If this underpin was not achieved, the 2014 AIP would be subject to a reduction of 10%.

The achievement of the performance measures has been reviewed, with appropriate input from the Audit Committee, following the end of the year. The maximum 2014 AIP opportunity against each of the performance measures is shown below, together with the AIP award actually achieved. The cash underpin has also been achieved.

In determining the bonus outcome for the Executive Directors, the Committee took into account that performance against the principal financial measure (EBITA), calculated in accordance with the scheme rules, would include the profit recognised on the transfer of assets into the pension scheme. The Committee took the view that this profit should not count fully towards the EBITA measure for the 2014 bonus and therefore reviewed the bonus outcome, both including and excluding the effect of this transfer, determining that the bonus payable should be at the mid-point of these two results. The result in the right-hand column shows this adjusted amount which will form the basis for payment.

The Committee is satisfied that these measures remain aligned with the execution and delivery of the Company's strategy.

Performance measures	AIP opportunity – maximum percentage of bonus		Actual performance	AIP award – as a percentage of bonus		Adjusted AIP award – as a percentage of bonus	
	Andrew Wyllie	Anthony Bickerstaff		Andrew Wyllie	Anthony Bickerstaff	Andrew Wyllie	Anthony Bickerstaff
Group EBITA[1]	66.7%	66.7%	£31.4m	65.4%	65.4%	52%	52%
Group Cost Control	6.7%	6.7%	+	0%	0%	0%	0%
Group Health and Safety	6.7%	6.7%	AFR 0.10 scored inspections achieved	3.4%	3.4%	3.4%	3.4%
Order Book Contract Profit	3.3%	3.3%	+	3.3%	3.3%	3.3%	3.3%
Total Order Book	3.3%	n/a	£3.5bn	2.9%	n/a	2.9%	n/a
Cash Balance	3.3%	3.3%	£148.5m	3.3%	3.3%	3.3%	3.3%
Cash Conversion	3.3%	n/a	+	0%	n/a	0%	n/a
Pension Risk Management	n/a	3.3%	+	n/a	3.3%	n/a	3.3%
Personal Performance[2]	6.7%	10.0%	n/a	6.7%	10.0%	6.7%	10.0%
Total	100%	100%	n/a	85.0%	88.7%	71.6%	75.3%

[1] Calculated on an adjusted basis as approved by the Committee.

[2] Includes building, maintaining and developing the executive team and personal development.

[+] The Committee has determined that these particular performance measures remain commercially sensitive and, as such, has chosen not to disclose them as they provide our competitors with insight into our business plans.

(c) Vesting of the 9 May 2012 LTIP award

The LTIP award granted on 9 May 2012 was based on performance to the year ended 31 December 2014 and is due to vest in May 2015, subject to the Committee's determination that the performance conditions have been met.

This award has two performance conditions:

Aggregate EPS[1] for the financial years ended 31 December 2012, 2013 and 2014	Vesting level (for 50% of the award)
Below 81.66 pence	0%
81.66 pence	15%
Between 81.66 pence and 90.73 pence	15% – 100% pro rata
90.73 pence or more	100%

Operating profit for the financial year ended 31 December 2014	Vesting level (for 50% of the award)
Below £29.6 million	0%
Between £29.6 million and £37 million	0% – 50% pro rata
£37 million	50%
Between £37 million and £44.4 million	50% – 100% pro rata
£44.4 million	100%

[1] As adjusted following the capital raising in March 2014.

In addition, the Committee agreed that no element of the award relating to the Operating Profit shall vest unless an EPS underpin has been met which requires that the aggregate EPS performance condition as shown above is met in full and that the EPS for the financial year ending 31 December 2014 is at least 32.21 pence (as adjusted following the capital raising in March 2014).

EPS for the financial year ended 31 December 2014 calculated on an adjusted basis approved by the Committee was 24.8 pence and aggregate EPS for the financial years ended 31 December 2012, 2013 and 2014 (calculated on the same basis) was 107.7 pence. As a result, 100% of the element relating to aggregate EPS is due to vest (50% of the maximum award), and 0% of the element relating to Operating Profit is due to vest (50% of the maximum award). Therefore, 50% of the awards granted on 9 May 2012 are due to vest in May 2015 and are shown in the table below:

	Number of shares granted[1]	Number of shares due to vest[2]	Number of shares due to lapse	Dividends on shares due to vest	Total shares due to vest[2]	Estimated value[3]
Andrew Wyllie	222,524	111,262	111,262	–	111,262	£315,984
Anthony Bickerstaff	147,422	73,711	73,711	–	73,711	£209,339

[1] As adjusted following the capital raising in March 2014.

[2] Subject to the Committee's official determination that the performance conditions have been met and to any other adjustment.

[3] Valued based on the average share price over the final three months of the financial year ended 31 December 2014, being £2.84.

(d) Pensions and life assurance

Under their terms of engagement, the Executive Directors are entitled to an annual pension allowance of 22% of base salary. Life assurance cover of four times base salary is provided through the Costain Life Assurance Scheme. The annual premiums payable in respect of life assurance for Andrew Wyllie and Anthony Bickerstaff were £2,016 (2013: £1,950) and £1,335 (2013: £1,292) respectively.

The Group offers a Group Flexible Retirement Plan which was set up in 2009 with Standard Life for employees and senior management. Neither Executive Director participated in the scheme.

(e) Chairman

Remuneration for the Chairman comprises a basic annual fee which was set at £136,056 with effect from 1 April 2014 (1 April 2013: £132,737).

(f) Non-Executive Directors

Remuneration for Non-Executive Directors, other than the Chairman, comprises a basic annual fee for acting as a Non-Executive Director of the Company and additional fees for the Senior Independent Director and chairmanship of the Audit and Remuneration Committee. The annual fees set with effect from 1 April 2014 were as follows:

2014 Fees	Basic Fee	Senior Independent Director	Audit Committee Chairman	Remuneration Committee Chairman
Fees	£43,937	£6,430	£9,109	£6,430

Other grants made during the year

2014 LTIP Grant

Grants were made under the LTIP on 7 May 2014. The grant level for the Executive Directors remains at 100% of salary. Half of the award vests after three years, subject to continued service and performance conditions (as set out below), and the other half vests after five years (the final two years being subject only to continued service), thereby ensuring long-term alignment of the Executive Directors' and shareholders' interests.

Performance measures for the 2014 LTIP are as follows:

Aggregate EPS[1] over the financial years ended 31 December 2014, 2015 and 2016	Vesting level (for 100%) of the award
Below 83.9 pence	0%
83.9 pence	15%
92.9 pence or more	100%
Between 83.9 pence and 92.9 pence	Between 15% and 100% pro-rata on a straight-line basis

[1] As adjusted following the capital raising in March 2014.

The share awards granted under the 2014 LTIP are as follows:

	Number of shares	Face value[1]	End of performance period	Threshold vesting	Weighting (% of award)
Andrew Wyllie	164,467	£435,838	31 December 2016	15% EPS	100%
Anthony Bickerstaff	108,959	£288,741	31 December 2016	15% EPS	100%

[1] Valued using the share price on the day prior to the date of grant (7 May 2014), being £2.65 pence per share.

All-employee share plans

The Company granted options under the Costain Group PLC Sharesave Plan to the Executive Directors during 2014, details of which are shown on page 74.

Implementation of Policy in the year to 31 December 2015

Salary

For 2015, the Committee approved a 2.5% increase for the Executive Directors, effective 1 April 2015. A 2.5% salary increase budget will also be applied across the Company in 2015. The results of the salary review are set out in the table below:

	Salary 2015	Salary 2014	% change
Andrew Wyllie	**£448,159**	£437,228	2.5%
Anthony Bickerstaff	**£296,906**	£289,664	2.5%

Non-Executive Director fees

Non-Executive Directors' fees, and Chairman's fees, were not increased with effect from 1 April 2015.

2015 Annual Incentive

Executive Directors and other senior management are eligible for annual bonuses under the AIP to encourage improved performance, with targets established by the Committee to align rewards with the Company strategy. The targets were set at the end of December 2014/beginning of 2015 and are clearly aligned with the delivery of our *'Engineering Tomorrow'* strategy. Their achievement will be reviewed, with appropriate input from the Audit Committee, at the end of the year.

The combined maximum bonus opportunity for the Chief Executive and the Finance Director for the year ended 31 December 2015 will remain unchanged from 2014 at 150% of base salary, with one-third of earned bonus deferred into shares for a further two years and two-thirds of earned AIP opportunity paid in cash.

The performance measures for the 2015 AIP are as follows:

Performance Measures	2015 AIP Opportunity – Maximum Percentage of Bonus	
	Andrew Wyllie	Anthony Bickerstaff
Group EBITA	60%	60%
Group Cost Control	6%	6%
Group Health and Safety	10%	10%
Order Book Contract Profit	6%	4%
Total Order Book	6%	n/a
Cash Balance	6%	4%
Personal Performance	6%	16%
Total	100%	100%

The Committee has chosen not to disclose in advance the target performance for maximum achievement for the year ended 31 December 2015, as these include items which the Committee considers commercially sensitive. The Committee will continue to provide retrospective disclosure of certain target performance for maximum achievement in next year's Annual Report on Remuneration to the extent the Committee determines these measures are not commercially sensitive.

2015 LTIP Grant

The grant level for the Executive Directors remains at 100% of salary. Subject to the achievement of performance conditions as set out below, half of the award will vest after three years and the other half will vest after five years (the final two years being subject only to continued service), thereby ensuring long-term alignment of the Executive Directors' and shareholders' interests.

It is proposed that the targets for the 2015 LTIP awards will be as follows:

EPS performance condition

Sum of the EPS for the financial years ending 31 December 2015, 2016 and 2017	Vesting level for awards
Below 83.9 pence	0%
83.9 pence	15%
96.9 pence or more	100%
Between 83.9 pence and 96.9 pence	Between 15% and 100% pro-rata on a straight-line basis

The Committee has the discretionary power to vary these EPS targets. It is anticipated that the 2015 LTIP awards will take place in March 2015.

The Committee believes that EPS remains the most appropriate metric to use under the LTIP, as growth in EPS is one of the key drivers of the Company's share price. As with previous LTIP awards, EPS for the awards that are due to be made in 2015 shall be calculated on an adjusted basis.

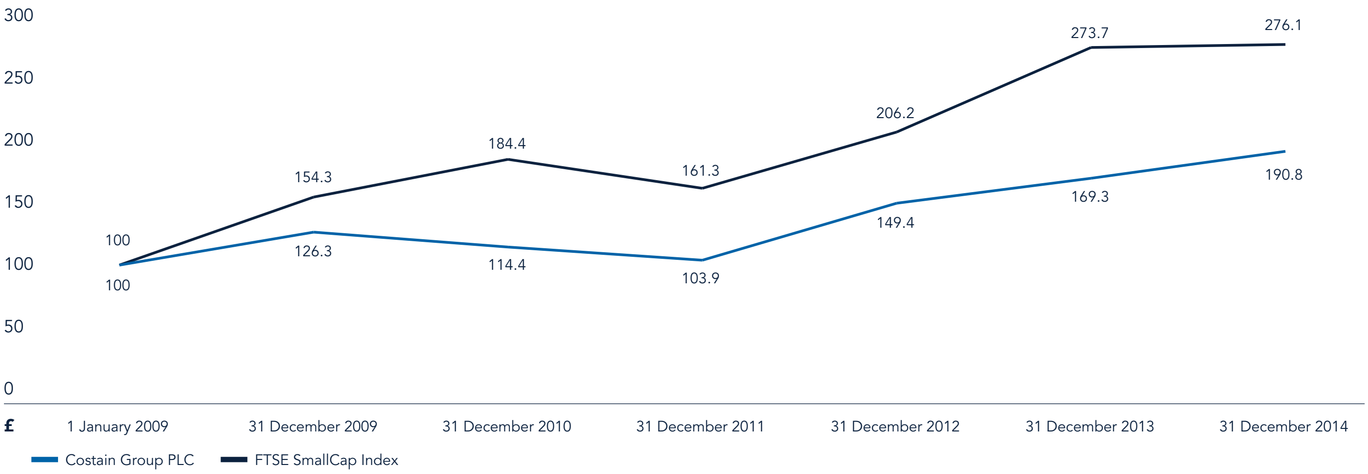
A clawback and malus provision is incorporated in the AIP and the LTIP (and the legacy DSBP) with regard to any material misstatement to audited accounts, an error in calculation of targets resulting in an overpayment, gross misconduct or criminal behaviour on the part of a participant.

Other information

Performance graph

The graph below shows the value, by 31 December 2014, for £100 invested in Costain Group PLC on 1 January 2009 compared with the value of £100 invested in the FTSE SmallCap Index. The Committee believes that the SmallCap Index is an appropriate Index to use as it is the index in which the Company is a constituent and comprises companies of a more similar size to Costain than the FTSE All-Share.

Total shareholder return (from 1 January 2009)



Source: Thomson Reuters Datastream

Change in Chief Executive's remuneration

	Year ending 31 December				
	2014	2013	2012	2011	2010
Total remuneration	£1,329,007	£1,251,239	£1,089,337	£1,228,332	£1,603,014
AIP (%)	71.6%	75%	55%	86%	94%
LTIP vesting (%)	50%	50%	100%	100%	96%

Statement of change in pay of Chief Executive compared to other employees

The table below shows the movement in the remuneration for the Chief Executive between the current and previous financial year compared to the average (per head) for all employees.

	2014	2013	% change
Chief Executive			
– salary	£434,562	£423,963	2.50%
– benefits	£13,275	£13,283	–0.06%
– bonus[1] (annual incentive)	£482,017	£345,412	39.60%
Average per employee			
– salary[2]	£41,705	£39,616	5.27%
– benefits[3]	£4,579	£4,679	–2.41%
– bonus[4] (annual incentive)	£3,331	£3,239	2.84%

[1] Bonus figures for the Chief Executive are calculated on the basis of the combined cash bonus actually paid and the value of the share options that were granted under the DSBP during 2013 and 2014 (for the financial years ended 31 December 2012 and 2013 respectively).

[2] Average salary for employees is calculated on the basis of the annual monthly UK salary bill divided by the average number of monthly paid UK employees.

[3] Employee benefits are calculated based on the total cost to the Company of private medical insurances, life assurance, company cars and car allowances, averaged per head for monthly paid employees.

[4] Bonus figures earned for 2014 for the whole Company are not available, hence for employees, the comparator figure is the total bonus payments made to monthly paid employees during 2013 and 2014 averaged per head.

Relative importance of spend on pay

The table below illustrates the change in expenditure by the Company on remuneration paid to all the employees of the Group and distributions to shareholders from the financial year ending 31 December 2013 to the financial year ending 31 December 2014.

	2014 £million	2013 £million	% change
Overall expenditure on pay	162.1	151.4	2.1%
Dividend	8.4*	7.2	16.7%*

* In March 2014, the Group raised net proceeds of £70.3 million by way of a Firm Placing and Placing and Open Offer of 33,382,068 new ordinary shares and amended its dividend policy resulting in an increase in the total dividend payment

These matters were selected to be shown as they represent key distributions by the Group to its stakeholders.

Directors' appointment

The dates of each of the Director's original appointment and expiry of current term are as follows:

Director	Date of original appointment	Expiry of current term[1]
Andrew Wyllie	25 April 2005	Terminable on 12 months' notice
Anthony Bickerstaff	03 March 2006	Terminable on 12 months' notice
David Allvey	01 November 2001	Close of 2015 AGM
James Morley	09 January 2008	Close of 2017 AGM
Jane Lodge	01 August 2012	01 August 2015
Alison Wood	01 February 2014	01 February 2017
David McManus	09 May 2014	09 May 2017
Ahmed Samy	30 November 2013	Close of 2017 AGM

[1] Expiry of Current Term is subject to:
(a) the appointment of an independent Non-Executive Director can be terminated by reasonable notice on either side (of not less than one month);
(b) re-election is required at the AGM following their appointment, subsequent re-election at intervals of no more than three years and re-election at each AGM if having served on the Board for more than nine years, in accordance with the UK Corporate Governance Code and the Company's Articles of Association. The Directors standing for re-election at the 2015 AGM will be David Allvey, Andrew Wyllie and David McManus.

External directorships

Andrew Wyllie was appointed as a Non-Executive Director of Scottish Water on 7 April 2009 and, in respect of the appointment for the year ended 31 December 2014, he was paid £20,016 (2013: £19,872). Anthony Bickerstaff was appointed as a Non-Executive Director and Chair of the Audit Committee of Low Carbon Contracts Company Limited and Electricity Settlements Company Limited on 11 November 2014 and in respect of the appointment for the year ended 31 December 2014, he was paid £4,253 (2013: n/a). The Executive Directors have retained these fees in accordance with the policy set out in the Policy report.

Share awards under the legacy DSBP

Under the legacy DSBP, deferred bonus awards were granted in the following two forms:

i. an option with a nil exercise price over a fixed value of shares ('the Combined Deferred Award'), which is granted in combination with an HMRC approved market value option over a fixed number of shares ('the Option') – this applies to an individual maximum of £30,000; and

ii. an option with a nil exercise price over a fixed number of shares ('Deferred Award').

Details of the Executive Directors' participation in the DSBP are as follows:

Executive	Date granted	Balance at 1 January 2014	Granted during year	Share price at date of grant	Vested during year	Market price at date of vesting	Market price at date of exercise	Amount realised on exercise (excluding deduction of tax)	Balance at 31 December 2014	Actual/ expected vesting date
Andrew Wyllie	04.04.12	84,109*[1]	–	215p*	84,109[2]	265p	265p	£237,027	–	April 2014
	03.04.13	39,122*[1]	–	259p*	–	–	–	–	39,122	April 2015-2023
		11,576* (£29,981)*[3]	–	–	–	–	–	–	11,576 (£29,981)	
		11,576*[4]	–	–	–	–	–	–	11,576	
	07.05.14	–	61,778[1]	290p	–	–	–	–	61,778	May 2016-2024
Anthony Bickerstaff	04.04.12	55,722*[1]	–	215p*	55,722[2]	265p	265p	£157,030	–	April 2014
	03.04.13	21,918*[1]	–	259p*	–	–	–	–	21,918	April 2015-2023
		11,576* (£29,981)*[3]	–	–	–	–	–	–	11,576 (£29,981)	
		11,576*[4]	–	–	–	–	–	–	11,576	
	07.05.14	–	40,928[1]	290p	–	–	–	–	40,928	May 2016-2024

* As adjusted following capital raising in March 2014.

[1] Number of shares under the Deferred Award.

[2] In addition, Andrew Wyllie and Anthony Bickerstaff received 5,150 and 3,412 dividend shares respectively upon vesting.

[3] Maximum number and value of shares under the Combined Deferred Award.

[4] Number of shares under the Option.

The value of the shares under the Combined Deferred Award and the Option are equal. The Combined Deferred Award and the Option must normally be exercised at the same time. When calculating the maximum value of the shares under a Deferred Award that may be granted under the terms of the Plan, the value of the shares under the Option is not counted.

All of the awards become exercisable on the second anniversary of the date of grant subject to the continued employment of the participant. The value of the shares delivered under the Combined Deferred Award on exercise is the same as the value of the shares under that award at the time of grant. The number of shares under the Deferred Award and Option at grant will be delivered to the participants on exercise. To the extent that all or any part of an award becomes exercisable, it remains, subject to the DSBP Rules, exercisable until the tenth anniversary of the date of grant.

Share awards under the LTIP

Executive	Date granted	Balance at 1 January 2014	Granted during year	Share price at date of grant	Vested during year	Market price at date of vesting	Market price at date of exercise	Lapsed during year	Amount realised on exercise (excluding deduction of tax)	Balance at 31 December 2014	Actual/ expected vesting date
Andrew Wyllie											
	12.04.11[1]	181,952*	–	224p*	90,976	265p	265p	90,976	£241,086	–	April 2014
	09.05.12[2]	222,524*	–	187p*	–	–	–	–	–	222,524	May 2015
	07.05.13[3]	175,502*	–	241p*	–	–	–	–	–	175,502	May 2016
	07.05.14[4]	–	164,467	265p	–	–	–	–	–	164,467	May 2017
Anthony Bickerstaff											
	12.04.11[1]	120,542*	–	224p*	60,271	265p	265p	60,271	£159,718	–	April 2014
	09.05.12[2]	147,422*	–	187p*	–	–	–	–	–	147,422	May 2015
	07.05.13[3]	116,817*	–	241p*	–	–	–	–	–	116,817	May 2016
	07.05.14[4]	–	108,959	265p	–	–	–	–	–	108,959	May 2017

[1] 50% of the award was subject to an aggregate EPS for the financial years ended 31 December 2011, 2012 and 2013 of 102.3 pence (15% vests) to EPS of 112.6 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The remaining 50% of the award was based on an EPS for the financial year ended 31 December 2013 of 47 pence (0% vests) to EPS of 56 pence (100% vests) on a sliding scale between 0% and 100% pro-rata to the actual EPS achieved (EPS targets rounded as appropriate). 50% of the target was met.

[2] 50% of the award (Tier 1) was subject to an aggregate EPS target for the financial years ended 31 December 2012, 2013 and 2014 of 81.66* pence (15% vests) to EPS of 90.73* pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The remaining 50% of the award (Tier 2) was based on operating profit for the financial year ending 31 December 2014 of £37 million (50% vests) to £44.4 million (100% vests) on a sliding scale between £29.6 million and £44.4 million pro-rata to the operating profit actually achieved. In addition, no element of the Tier 2 award would vest unless the EPS (before pension interest) for the financial year ended 31 December 2014 was at least 32.21* pence and Tier 1 has vested in full. Subject to the Committees' confirmation, 50% of the target has been met.

[3] 50% of the award (Tier 1) is subject to an aggregate EPS target for the financial years ended 31 December 2013, 2014 and 2015 of 80.48* pence (15% vests) to EPS of 90.73 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The remaining 50% of the award (Tier 2) is based on operating profit for the financial year ending 31 December 2014 of £42 million (50% vests) to £50 million (100% vests) on a sliding scale between £35 million and £50 million pro-rata to the operating profit actually achieved. In addition, no element of the Tier 2 award will vest unless the EPS (before pension interest) for the financial year ended 31 December 2015 is at least 33.84* pence and Tier 1 has vested in full.

[4] 100% of the award is subject to an aggregate EPS target for the financial years ended 31 December 2014, 2015 and 2016 of 83.9 pence (15% vests) to EPS of 92.9 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. 50% of the award will normally vest three years after grant, subject to the satisfaction of the performance conditions over the three-year financial period ending 31 December 2016, whilst the remaining 50% of the award will normally vest on the fifth anniversary of the date of grant (with no further performance conditions applying) provided the individual remains an employee or officer of the Company.

* As adjusted following capital raising in March 2014.

The LTIP awards, which are expressed as options, are subject to an exercise price of £1. At 31 December 2014, the derived mid-market price of the ordinary shares in the Company, as advised by the Company's brokers, was 280 pence. The range of the share price of the ordinary shares during 2014 was 250 pence to 300 pence.

Share Options under the Save As You Earn (SAYE) scheme

Details of the Executive Directors' SAYE options are as follows:

Executive	Date granted	Balance at 1 January 2014	Granted during year	Exercise price	Exercised during year	Market price at date of exercise	Lapsed during year	Amount realised on vesting	Balance at 31 December 2014	Exercised/ Exercisable from/to
Andrew Wyllie	11.10.11	1,755*	–	190.73p*	1,755	291p	–	£5,107	–	Nov 2014
	30.09.13	1,689*	–	206.55p*	–	–	–	–	1,689	Nov 2016–May 2017
	29.09.14	–	2,253	234.80p	–	–	–	–	2,253	Nov 2017–May 2018
Anthony Bickerstaff	11.10.11	1,755*	–	190.73p*	1,755	294p	–	£5,160	–	Nov 2014
	30.09.13	1,689*	–	206.55p*	–	–	–	–	1,689	Nov 2016–May 2017
	29.09.14	–	2,253	234.80p	–	–	–	–	2,253	Nov 2017–May 2018

* As adjusted following capital raising in March 2014.

Directors' shareholdings

Details of the Directors' share interests in the Company as at 31 December 2014 and at the date of this report are as follows:

Director	Beneficially owned	Outstanding DSBP awards	Outstanding LTIP awards	Outstanding SAYE awards	Shareholding guidelines (% of salary/fee)	Actual Shareholding (% of salary/fee)
Andrew Wyllie	340,000	112,476	562,493	3,942	100%	175.51%
Anthony Bickerstaff	186,691	74,422	373,198	3,942	100%	139.08%
David Allvey[1]	15,888	–	–	–	100%	24.93%
James Morley	47,111	–	–	–	100%	202.29%
Jane Lodge[1]	25,809	–	–	–	100%	111.32%
Alison Wood[2]	6,666	–	–	–	100%	2.97%
David McManus[3]	0	–	–	–	100%	0%
Ahmed Samy	0	–	–	–	100%	0%

[1] Part held by a connected person.

[2] Appointed as a Non-Executive Director w.e.f. 1 February 2014 and as Chair of the Remuneration Committee w.e.f. 1 April 2014.

[3] Appointed as a Non-Executive Director w.e.f. 12 May 2014.

The Directors are encouraged to build and maintain a shareholding worth not less than 100% of base salary/fee through the retention of vested share awards (for the Executive Directors) or through open market purchases.

Directors' report

The Directors submit to the members their report and accounts of the Company for the year ended 31 December 2014.

The Corporate Governance report on pages 45 to 74 and the the Strategic report on pages 21 and 38 (with regard to information about employee involvement and greenhouse gas emissions) are also incorporated into this report by reference.

The Company has chosen to include the disclosure of likely future developments of the Company's business in the Strategic report.

Incorporation and constitution

Costain Group PLC is domiciled in England and incorporated in England and Wales under Company Number 1393773.

Profit and dividends

The profit after tax for the financial year ending 31 December 2014 amounted to £21.0 million (2013: £12.5 million). An interim dividend of 3.25 pence per share (2013: 3.75 pence) amounting to £3.2 million (2013: £2.5 million) was paid on 24 October 2014. A final dividend at the rate of 6.25 pence per share (2013: 7.75 pence) amounting to £6.3 million (2013: £5.2 million) will also be recommended to shareholders at the Annual General Meeting to be held on 6 May 2015. If approved, the dividend will be paid on 22 May 2015 to shareholders registered at close of business on 17 April 2015.

Dividends and other distributions

The Company may, by ordinary resolution, from time to time declare dividends not exceeding the amount recommended by the Board. Subject to the Companies Act 2006, the Board may pay interim dividends, and also any fixed rate dividend, whenever the financial position of the Company, in the opinion of the Board, justifies its payment. If the Directors act in good faith, they are not liable for any loss that shareholders may suffer because a lawful dividend has been paid on other shares which rank equally with or behind their shares.

The Board may withhold payment of all or any part of any dividends or other monies payable in respect of the Company's shares from a person with a 0.25% interest in a class of the Company's shares if such a person has been served with a restriction notice after failure to provide the Company with information concerning interests in those shares required to be provided under the Companies Act 2006.

Going concern

The Directors believe, after due and careful enquiry that the Group has adequate resources to continue operations for the foreseeable future. For this reason, the Directors continue to adopt the going concern basis in preparing the 2014 financial statements.

Share capital

The Company's share capital consists of ordinary shares with a nominal value of 50 pence each.

The issued share capital of the Company as at 31 December 2014 was £50,601,346.50, consisting of 101,202,693 ordinary shares of 50 pence each.

33,382,068 new ordinary shares of 50 pence each were issued by the Company on 18 March 2014 following approval by shareholders to a capital raising in the sum of approximately £70.3 million (net of expenses).

Further details of the share capital of the Company can be found in Note 21 on page 123.

The awards granted in April 2011 under the 2002 Long-Term Incentive Plan (LTIP) matured as at 31 December 2013 resulting in the vesting of awards in April 2014 over 603,275 ordinary shares of 50 pence each with an exercise price of £1 per exercise. Further details with regard to the vesting of the 2011 LTIP awards can be found in the Directors' remuneration report on page 73.

At the 2013 Annual General Meeting, shareholders approved the renewal of the scrip dividend scheme which authorises the Directors to offer and allot ordinary shares in lieu of cash dividends to those shareholders who elect to participate in the scrip dividend. In April 2014, 191,503 ordinary shares of 50 pence each were allotted to shareholders in respect of the final dividend for 2013, and 73,270 ordinary shares of 50 pence each were allotted to shareholders in October 2014 in respect of the interim dividend for 2014. Further information on the scrip dividend scheme is set out on page 129. Details about joining the scrip dividend scheme can also be found on the Company's website at **www.costain.com**.

Restrictions on transfer of securities

There are no restrictions on the transfer of securities in the Company, except:

- that certain restrictions may from time to time be imposed by laws and regulations (for example, insider trading laws); and
- pursuant to the Disclosure and Transparency Rules of the Financial Conduct Authority (DTR3) whereby certain employees of the Company require the approval of the Company to deal in the Company's ordinary shares.

The Company is not aware of any agreements between holders of securities that may result in restrictions on the transfer of securities.

Major shareholders

As at 20 February 2015, the Company had been notified, including under the Disclosure and Transparency Rules issued by the Financial Conduct Authority (DTR5), of the following voting interests in its ordinary share capital:

Shareholder	Number of shares/ Voting rights	% of voting rights
UEM Builders Berhad[(i)]	13,810,850	13.65
Mohammed Abdulmohsin Al-Kharafi & Sons Company for General Trading, General Contracting and Industrial Structures WLL[(i)]	10,429,490	10.31
Miton Group plc	5,101,741	5.04
JO Hambro Capital Management Group Limited	5,085,708	5.03

(i) Shares are held by nominees on behalf of these beneficial owners.

Rights and obligations attaching to shares

In accordance with the Articles of Association, the Company can issue shares with any rights or restrictions attached to them provided such rights or restrictions do not restrict any rights or restrictions attached to existing shares. These rights or restrictions can be decided either by ordinary resolutions passed by the shareholders or by the Directors as long as there is no conflict with any resolution passed by the shareholders. Subject to the Articles of Association, the Companies Act 2006 and other shareholders' rights, the issue of shares is at the disposal of the Board.

Powers in relation to the Company issuing or buying back its own shares

The Directors may only issue and buy back shares if authorised to do so by the Articles of Association or the shareholders in general meeting. At the Company's Annual General Meeting held on 7 May 2014, shareholders granted an authority to the Directors to allot ordinary shares up to an aggregate nominal amount of £16.7 million. As this authority is due to expire on 6 May 2015, shareholders' approval will be sought to renew the Directors' authority to allot ordinary shares at the 2015 Annual General Meeting, up to an aggregate nominal amount of £16,867,991. As at 31 December 2014, the only shares that had been allotted were in order to satisfy awards under employee share schemes and the scrip dividends. The Directors did not request authority to buy back any of the Company's shares at the last Annual General Meeting in 2014 and they do not propose to do so at this at this year's Annual General Meeting.

Securities carrying special rights

No person holds securities in the Company carrying special rights with regard to control of the Company.

Restrictions on voting

No member shall be entitled to vote at any general meeting or class meeting in respect of any share held by him/her if any call or other sum then payable by him/her in respect of that share remains unpaid or if a member has been served with a restriction notice (as defined in the Articles of Association) after failure to provide the Company with information concerning interests in those shares required to be provided under the Companies Act 2006.

The Company is not aware of any agreement between holders of securities that may result in restrictions of voting rights.

Rights under the employee share schemes

ACS HR Solutions Share Plan Services (Guernsey) Limited, as Trustee of the Costain Group Employee Trust, held 0.36% of the issued share capital of the Company as at 31 December 2014 on trust for the benefit of those employees who exercise their share awards/options under the Company's Long-Term Incentive Plan, Deferred Share Bonus Plan, Share Deferral Plan and Save As You Earn Scheme (in respect of 'good leavers' who leave the employment of the Company before their contract matures). The Trustee does not exercise any right to vote or to receive a dividend in respect of this shareholding.

Powers of the Directors

Subject to the Company's Articles of Association, the Companies Act 2006 and any directions given to the Company by special resolution, the business of the Company will be managed by the Board who may exercise all the powers of the Company. In particular, the Board may exercise all the powers of the Company to borrow money, to guarantee, to indemnify, to mortgage or charge any of its undertaking, property, assets (present and future) and uncalled capital and to issue debentures and other securities and to give security for any debt, liability or obligation of the Company or of any third party.

Amendment of Articles of Association

Unless expressly specified to the contrary in the Articles of Association of the Company, the Company's Articles of Association may be amended by a special resolution of the Company's shareholders. A copy of the Articles of Association is available on the Company's website at **www.costain.com**.

Political donations

No political donations were made during the year ended 31 December 2014 (2013: nil). The Company has a policy of not making donations to political organisations.

Directors and Directors' interests

Brief biographies of the present members of the Board are given on pages 46 to 47.

In accordance with Article 78 of the Company's Articles of Association and provision B.7.1 of the Code, David Allvey, Andrew Wyllie and David McManus will offer themselves for re-election at the 2015 Annual General Meeting. David Allvey, having been in office for a continuous period in excess of nine years, is required to stand for re-election on an annual basis. Andrew Wyllie, having served on the Board at the time of the two preceding Annual General Meetings without retiring, and David McManus, having been appointed as a Director of the Company since the last Annual General Meeting, are both required to stand for re-election at the 2015 Annual General Meeting. David Allvey and David McManus have letters of appointment and Andrew Wyllie has a contract of employment with the Company, details of which are set out in the Directors' remuneration report.

With regard to the re-election of David Allvey, Andrew Wyllie and David McManus, following a formal performance evaluation, the Board is of the opinion that they each continue to perform effectively, that they demonstrate commitment to their particular roles and they ensure that proper time is devoted to Board and committee meetings.

No Director had any material interest in any contract of significance with the Group during the period under review. Details of Directors' emoluments and interests in shares in the Company, including any changes in interests during 2014, are contained in the Directors' remuneration report, which appears on pages 59 to 74.

Independent auditors

It is proposed that KPMG LLP are re-appointed as auditors of the Company and they will hold office from the conclusion of the AGM in May 2015 until the conclusion of the next general meeting at which the accounts are laid before the Company. See page 57 of the Audit Committee report and the Notice of Annual General Meeting, available on the Company's website at **www.costain.com**, for further details.

Significant agreements – change of control

The Directors are not aware of any significant agreements to which the Company and/or any of its subsidiaries or associates are a party that take effect, alter or terminate upon a change of control of the Company following a takeover bid, save in respect of the Facility Agreements relating to the Company's banking and surety bonding facilities, which would terminate upon a change of control. There are no agreements between the Company and its Directors or employees providing for compensation for loss of office or employment that occurs because of a takeover bid except that provisions of the Company's share schemes and plans may cause options and awards to be granted to employees under such schemes and plans to vest on a takeover.

Research and development

The Group is involved in research and development in all the sectors in which it operates. The Group's engineers and technical staff in these named sectors seek to develop and deliver technical advances. In undertaking certain elements of this research and development work, the Group is supported by arrangements with certain British universities and various technology specialists.

Greenhouse gas emissions

The Strategic report on page 21 details the greenhouse gas emissions disclosures required by the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013. This information is incorporated by reference into (and shall be deemed to form part of) this report.

Directors' indemnity

Costain Group PLC maintains liability insurance for its Directors and officers. There are no subsisting indemnities in favour of its Directors.

Appointment and replacement of Directors

The Directors shall be not less than two and not more than 18 in number. The Company may by ordinary resolution vary the minimum and/or maximum number of Directors.

A Director shall not be required to hold any shares in Costain Group PLC but is encouraged to do so under the Company's share ownership guidelines. Directors may be appointed by the Company by ordinary resolution or by the Board. A Director appointed by the Board holds office only until the next Annual General Meeting of the Company and is then eligible for reappointment. The Board, or any Committee authorised by the Board, may from time to time appoint one or more Directors to hold any employment or executive office for such period and on such terms as they may determine and may also revoke or terminate any such appointment. At every Annual General Meeting of the Company, any Director who has been appointed by the Board since the last Annual General Meeting, or who held office at the time of the two preceding Annual General Meetings and who did not retire at either of them, or who has held office with the Company, other than employment or executive office, for a continuous period of nine years or more at the date of the meeting, shall retire from office and may offer himself/herself for reappointment by the members.

The Company may by special resolution remove any Director before the expiration of his/her period of office. The office of a Director shall be vacated if: (i) he/she resigns or offers to resign and the Board resolves to accept such offer; (ii) his/her resignation is requested by all of the other Directors and all of the other Directors are not less than three in number; (iii) he/she is or has been suffering from mental or physical ill health and the Board resolves that his/her office be vacated; (iv) he/she is absent without the permission of the Board from meetings of the Board (whether or not an alternate Director appointed by him/her attends) for six consecutive months and the Board resolves that his/her office is vacated; (v) he/she becomes bankrupt or compounds with his creditors generally; (vi) he/she is prohibited by a law from being a Director; (vii) he/she ceases to be a Director by virtue of the Companies Act 2006; or (viii) he/she is removed from office pursuant to the Company's Articles of Association.

Employee information

The average number of employees within the Company and Group is shown in Note 5 to the financial statements on page 103.

Apart from ensuring that an individual has the ability to carry out a particular role, the Company does not discriminate in any way. The Company endeavours to retain employees if they become disabled, making reasonable adjustments to their role and, if necessary, looking for redeployment opportunities within the Group. The Company also ensures that training, career development and promotion opportunities are available to all employees irrespective of gender, race, age or disability.

The Company maintains a strong communication network and employees are encouraged to discuss with management matters of interest and issues affecting the day-to-day operations of the Group. Employees are kept informed of the financial and economic factors affecting the Company's performance, and other matters of concern to them as employees, through various means including regular updates from the Chief Executive and other senior managers and a Costain online news service. Employees also have the opportunity to provide feedback and ask questions at the annual staff road shows which take place around the country. Further details of the actions taken to introduce, maintain or develop arrangements aimed at employees are described in the Corporate Responsibility report on pages 38.

Essential contracts or other arrangements

Given the scope and diversity of the Company's activities, the Company does not consider that it has contractual or other arrangements which are essential to the business of the Group and which are required to be disclosed.

Disclosure of information to auditors

The Directors confirm that, so far as they are aware, there is no relevant audit information (as defined in section 418 of the Companies Act 2006) of which the Company's External Auditor is unaware and that each Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's external auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

By Order of the Board

T. Wood

Tracey Wood
Company Secretary
02 March 2015

Directors' responsibility statement

The Directors are responsible for preparing the Annual Report, the Director's remuneration report and accounts in accordance with applicable law and regulations.

Company law requires the Directors to prepare accounts for each financial year. Under that law, the Directors are required to prepare the Group and Company accounts in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the European Union ('EU').

Under Company law, the Directors must not approve the financial statements unless they are satisfied that these give a true and fair view of the state of affairs of the Group and the Company and of their profit or loss for that period.

In preparing each of the Group and the Company accounts, the Directors are required to:

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

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

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' report, Directors' remuneration report and Corporate Governance statement that comply with that law and those regulations.

The Directors are also 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.

The Directors are responsible for preparing the Annual Report in accordance with applicable law and regulations. The Directors consider the Annual Report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary to assess the Company's and the Group's performance, business model and strategy.

Each of the Directors of the Company confirms that, to the best of his or her knowledge:

- the Group accounts, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profits/losses of the Company (and of the Group 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 Company (and of the Group taken as a whole), together with a description of the principal risks and uncertainties that they face.

On behalf of the Board

David Allvey
Chairman
02 March 2015

Andrew Wyllie
Chief Executive
02 March 2015

Independent Auditor's report
to the members of Costain Group PLC only

Opinions and conclusions arising from our audit

1 Our opinion on the financial statements is unmodified

We have audited the financial statements of Costain Group PLC for the year ended 31 December 2014 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income and Expense, the Consolidated and Company Statement of Financial Position, the Consolidated and Company Statement of Changes in Equity, the Consolidated and Company Cash Flow Statement and related notes. In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 December 2014 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 IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; 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.

2 Our assessment of risks of material misstatement

In arriving at our audit opinion on the financial statements the risks of material misstatement that had the greatest effect on our audit were as follows:

Contract accounting estimates

Refer to page 55 (Audit Committee report) and pages 92 – 98 (accounting policies).

- *The Risk:* The Group recognises revenue and profit in accordance with IAS 11 based on the stage of completion of contracts which is assessed with reference to the proportion of contract costs incurred for the work performed to the balance sheet date, relative to the estimated total costs of the contract at completion. The recognition of revenue and profit therefore relies on estimates in relation to the final out-turn of costs on each contract. Changes to these estimates could give rise to material variances in the amount of revenue and profit/loss recognised. Cost contingencies may also be included in these estimates to take account of specific uncertain risks, or disputed claims against the Group, arising within each contract. These contingencies are reviewed by the Group on a regular basis throughout the contract life and adjusted where appropriate. Variations and claims, together with, in limited circumstances, insurance recoveries, are recognised on a contract-by-contract basis when the Group believes it is probable that the amount will be recovered from the customer or insurer and the amount can be measured reliably. Therefore, there is a high degree of risk and associated management judgement in: estimating the amount of revenue to be recognised by the Group with respect to the final out-turn on contracts; assessing the level of the contingencies; and recognising receipt of variations, claims and insurance recoveries.
- *Our response:* Using a variety of quantitative and qualitative criteria we selected a sample of contracts to assess and challenge the most significant and complex contract estimates. We obtained the detailed project management review papers from the Group to support the estimates made and challenged the judgements underlying those papers with senior operational, commercial and financial management. In this area our audit procedures included:
  - evaluating the financial performance of contracts against budget and historical trends;
  - completing site visits to certain higher risk or larger value contracts, physically inspecting the stage of completion of individual projects and identifying areas of complexity through observation and discussion with site personnel;
  - challenging the Group's judgement in respect of forecast contract out-turn, contingencies, settlements and the recoverability of contract balances via agreement to third-party certifications and confirmations and with reference to our own assessments, historical outcomes and industry norms;
  - analysing correspondence with customers around variations and claims and considering whether this information is consistent with the estimates made by the Group;

– analysing correspondence and meeting minutes with insurers around recognised insurance claims, analysing assessments of these claims undertaken by the insurer's legal or technical experts, if applicable, and considering whether this information supports the position taken on the contract;

– inspecting selected contracts for key clauses, identifying relevant contractual mechanisms such as pain/gain shares, design bonuses, liquidated damages and success fees and assessing whether these key clauses have been appropriately reflected in the amounts recognised in the financial statements;

– assessing whether the amounts recognised in the financial statements resulting from the estimates and assumptions made represent a balanced view of the risks and opportunities pertinent to each contract position;

– considering whether provisions against contracts sufficiently reflect the level of risk, and challenging the Group's judgement in this area with reference to our own assessments; and

– considering the adequacy of the Group's disclosures in respect of contract accounting and the key risks relating to these amounts.

Land and property assets held by equity accounted joint venture – valuation

Refer to page 56 (Audit Committee report), pages 92 – 98 (accounting policies) and pages 109 to 110 (financial disclosures).

- *The Risk:* Alcaidesa Holding SA (equity accounted joint venture of £25.2 million in the accounts) operates in the Spanish real estate market and holds as its principal non-current assets, a marina and two golf courses and, as its principal current asset, land held for development. The Group performs a yearly review for impairment of the non-current assets and of the net realisable value of the development land to determine if these assets are being recorded at an appropriate amount. Due to the continued depressed state of the Spanish economy and the property market in particular, the valuation of these assets represents a significant risk in the Group balance sheet.

- *Our response:* The non-current asset of the marina was valued internally by the Group using a discounted cash flow projection model which was subsequently reviewed and reported on by a third party valuer. In respect of this asset, our procedures included testing the design and operation of the model. We then examined the output of the external valuer which reported on the key inputs and assumptions driving the outputs of the model; we utilised a member of our team with specialist valuation skills to compare that with our historical experience, our knowledge of the relevant market and market forecasts for growth and inflation.

  The non-current assets of the golf courses were externally valued by a third party valuer using discounted cash flow projections. We have then examined the methodology of the projections and both the inputs and outputs of the external valuation exercise utilising a member of our team with specialist valuation skills to compare that with our historical experience, our knowledge of the relevant market and market forecasts for growth and inflation.

  Our audit procedures in respect of the land held for development in the Alcaidesa portfolio included inspecting copies of the external valuations for that land and evaluating whether the valuation firms that produced the reports were suitably qualified. We utilised a member of our team with specialist valuation skills to test the underlying assumptions by comparing them to market evidence and our knowledge of the sites.

We also reviewed the level of provision held at the Group level in relation to the Alcaidesa investment as a whole.

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

The materiality for the Group's financial statements as a whole was set at £1.4 million determined with reference to a benchmark of Group profit before taxation and finance charges of £26.2 million of which it represents 5.3%.

We report to the audit committee any corrected or uncorrected misstatements exceeding £70,000, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Independent Auditor's report continued

Audits for Group reporting purposes were performed by component auditors at the key reporting components in Spain, Aberdeen and by the Group audit team at the Group's head offices. These procedures covered 99% of total Group revenue; 99% of Group profit before tax and 99% of total Group assets. The segment disclosures in Note 3 set out the individual significance of specific countries.

The Group audit 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 audit team approved the component materialities. The audits undertaken for Group reporting purposes in Spain and Aberdeen were performed to materiality levels set by the Group audit team of £525,000 and £725,000 respectively, having regard to the size and risk profile of those components.

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

In our opinion:

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

5 We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the Annual Report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

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

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the Annual Report and financial statements taken as a whole is fair, balanced and understandable and provide the information necessary for shareholders to assess the Group's performance, business model and strategy; or
- the Audit Committee report does not appropriately address matters communicated by us to the Audit Committee.

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

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

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 75, in relation to going concern; and
- the part of the Corporate Governance report on page 48 relating to the Company's compliance with the ten provisions of the 2012 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope of report and responsibilities

As explained more fully in the Directors' responsibilities statement set out on page 79, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at **www.frc.org.uk/auditscopeukprivate**. This report is made solely to the Company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at **www.kpmg.com/uk/auditscopeukco2014a**, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

Andrew Marshall (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London E14 5GL
02 March 2015

Financial statements

Financial statements and other information

Consolidated income statement
Year ended 31 December

		2014			2013		
	Notes	Before other items £m	Other items £m	Total £m	Before other items £m	Other items £m	Total £m
Continuing operations							
Revenue	3	1,122.5	–	1,122.5	960.0	–	960.0
Less: Share of revenue of joint ventures and associates	13	(50.7)	–	(50.7)	(74.8)	–	(74.8)
Group revenue		1,071.8	–	1,071.8	885.2	–	885.2
Cost of sales		(1,011.6)	–	(1,011.6)	(826.7)	–	(826.7)
Gross profit		60.2	–	60.2	58.5	–	58.5
Administrative expenses		(31.5)	–	(31.5)	(31.1)	–	(31.1)
Exceptional transaction costs	4	–	–	–	–	(3.7)	(3.7)
Amortisation of acquired intangible assets		–	(3.0)	(3.0)	–	(1.8)	(1.8)
Employment related and other deferred consideration		–	(2.2)	(2.2)	–	(2.8)	(2.8)
Group operating profit		28.7	(5.2)	23.5	27.4	(8.3)	19.1
Profit on sales of interests in joint ventures and associates	4	4.0	–	4.0	9.1	–	9.1
Share of results of joint ventures and associates	13	(1.3)	–	(1.3)	(1.5)	(9.8)	(11.3)
Profit from operations	3	31.4	(5.2)	26.2	35.0	(18.1)	16.9
Finance income	7	0.7	–	0.7	0.7	–	0.7
Finance expense	7	(3.6)	(0.7)	(4.3)	(4.7)	–	(4.7)
Net finance expense		(2.9)	(0.7)	(3.6)	(4.0)	–	(4.0)
Profit before tax	3/4	28.5	(5.9)	22.6	31.0	(18.1)	12.9
Income tax	8	(2.2)	0.6	(1.6)	(1.8)	1.4	(0.4)
Profit for the year attributable to equity holders of the parent		26.3	(5.3)	21.0	29.2	(16.7)	12.5
Earnings per share							
Basic*	9	27.8p	(5.6)p	22.2p	41.0p	(23.4)p	17.6p
Diluted*	9	27.2p	(5.5)p	21.7p	39.4p	(22.5)p	16.9p

The impact of business disposals in either year was not material and, therefore, all results are classified as arising from continuing operations.

* 2013 has been restated for the bonus element in the 2014 capital raise.

Consolidated statement of comprehensive income and expense

Year ended 31 December

	2014 £m	2013 £m
Profit for the year	21.0	12.5
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of foreign operations	(2.0)	(0.2)
Cash flow hedges		
Group:		
Effective portion of changes in fair value during year	–	(0.1)
Net changes in fair value transferred to the income statement	0.1	0.2
Joint ventures and associates:		
Effective portion of changes in fair value (net of tax) during year	–	(0.2)
Net changes in fair value (net of tax) transferred to the income statement	–	1.2
Total items that may be reclassified subsequently to profit or loss	(1.9)	0.9
Items that will not be reclassified to profit or loss:		
Remeasurement of defined benefit obligations	(15.7)	8.6
Tax recognised on remeasurement of defined benefit obligations	1.5	(5.3)
Total items that will not be reclassified to profit or loss	(14.2)	3.3
Other comprehensive (expense)/income for the year	(16.1)	4.2
Total comprehensive income for the year attributable to equity holders of the parent	4.9	16.7

Consolidated statement of financial position

As at 31 December

	Notes	2014 £m	2013 £m
Assets			
Non-current assets			
Intangible assets	11	31.0	33.0
Property, plant and equipment	12	10.0	7.9
Investments in equity accounted joint ventures	13	25.5	27.1
Investments in equity accounted associates	13	0.3	0.2
Loans to equity accounted associates	13	1.7	4.8
Other	14	31.8	22.0
Deferred tax	8	9.2	9.8
Total non-current assets		109.5	104.8
Current assets			
Inventories		1.3	1.6
Trade and other receivables	14	197.1	190.6
Cash and cash equivalents	15	148.5	84.3
Total current assets		346.9	276.5
Total assets		456.4	381.3
Equity			
Share capital	21	50.6	33.4
Share premium		5.5	4.7
Foreign currency translation reserve		2.8	4.8
Hedging reserve		–	(0.1)
Retained earnings		51.9	0.5
Total equity attributable to equity holders of the parent		110.8	43.3
Liabilities			
Non-current liabilities			
Retirement benefit obligations	20	41.7	37.2
Other payables	18	4.5	4.3
Provisions for other liabilities and charges	19	0.1	0.4
Total non-current liabilities		46.3	41.9
Current liabilities			
Trade and other payables	18	296.3	266.1
Income tax liabilities	8	1.5	1.6
Bank overdrafts	15	–	1.6
Interest bearing loans and borrowings	16	–	25.0
Provisions for other liabilities and charges	19	1.5	1.8
Total current liabilities		299.3	296.1
Total liabilities		345.6	338.0
Total equity and liabilities		456.4	381.3

The financial statements were approved by the Board of Directors on 2 March 2015 and were signed on its behalf by:

A Wyllie
Director

A O Bickerstaff
Director

Registered number: 1393773

Company statement of financial position

As at 31 December

	Notes	2014 £m	2013 £m
Assets			
Non-current assets			
Investments in subsidiaries	13	100.1	97.9
Total non-current assets		100.1	97.9
Current assets			
Trade and other receivables	14	58.2	51.3
Cash and cash equivalents	15	10.2	–
Total current assets		68.4	51.3
Total assets		168.5	149.2
Equity			
Share capital	21	50.6	33.4
Share premium		5.5	4.7
Other reserves		14.2	12.0
Retained earnings		67.5	21.9
Total equity attributable to equity holders of the parent		137.8	72.0
Liabilities			
Non-current liabilities			
Provisions for other liabilities and charges	19	1.3	1.3
Total non-current liabilities		1.3	1.3
Current liabilities			
Trade and other payables	18	27.9	49.3
Income tax liabilities	8	1.5	1.5
Interest bearing loans and borrowings	16	–	25.0
Provisions for other liabilities and charges	19	–	0.1
Total current liabilities		29.4	75.9
Total liabilities		30.7	77.2
Total equity and liabilities		168.5	149.2

The financial statements were approved by the Board of Directors on 2 March 2015 and were signed on its behalf by:

A Wyllie
Director

A O Bickerstaff
Director

Registered number: 1393773

Consolidated statement of changes in equity

	Share capital £m	Share premium £m	Translation reserve £m	Hedging reserve £m	Merger reserve £m	Retained earnings £m	Total equity £m
At 1 January 2013	32.8	3.7	5.0	(1.2)	–	(8.5)	31.8
Profit for the year	–	–	–	–	–	12.5	12.5
Other comprehensive (expense)/income	–	–	(0.2)	1.1	–	3.3	4.2
Issue of ordinary shares under employee share option plans	0.5	0.6	–	–	–	(0.3)	0.8
Shares purchased to satisfy employee share schemes	–	–	–	–	–	(1.5)	(1.5)
Equity-settled share-based payments	–	–	–	–	–	2.2	2.2
Dividends paid	0.1	0.4	–	–	–	(7.2)	(6.7)
At 31 December 2013	33.4	4.7	4.8	(0.1)	–	0.5	43.3
At 1 January 2014	**33.4**	**4.7**	**4.8**	**(0.1)**	**–**	**0.5**	**43.3**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**21.0**	**21.0**
Other comprehensive (expense)/income	**–**	**–**	**(2.0)**	**0.1**	**–**	**(14.2)**	**(16.1)**
Issue of ordinary shares under employee share option plans	**0.4**	**0.2**	**–**	**–**	**–**	**(0.3)**	**0.3**
Issue of ordinary shares under capital raise (Note 21)	**16.7**	**–**	**–**	**–**	**53.6**	**–**	**70.3**
Transfer	**–**	**–**	**–**	**–**	**(53.6)**	**53.6**	**–**
Shares purchased to satisfy employee share schemes	**–**	**–**	**–**	**–**	**–**	**(2.0)**	**(2.0)**
Equity-settled share-based payments	**–**	**–**	**–**	**–**	**–**	**1.7**	**1.7**
Dividends paid	**0.1**	**0.6**	**–**	**–**	**–**	**(8.4)**	**(7.7)**
At 31 December 2014	**50.6**	**5.5**	**2.8**	**–**	**–**	**51.9**	**110.8**

There are no significant restrictions on the ability to remit overseas reserves.

Details of the nature of the above reserves are set out below.

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations that are not integral to the operations of the Company, as well as from the translation of liabilities that hedge the Group's net investment in a foreign subsidiary.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

Merger reserve

The capital raise was effected through a structure, which resulted in a merger reserve arising under Section 612 of the Companies Act 2006. Following the receipt of the cash proceeds through the structure, the excess of the net proceeds over the nominal value of the share capital issued has been transferred to retained earnings.

Company statement of changes in equity

	Share capital £m	Share premium £m	Other reserve £m	Merger reserve £m	Retained earnings £m	Total equity £m
At 1 January 2013	32.8	3.7	9.3	–	32.1	77.9
Comprehensive expense	–	–	–	–	(2.7)	(2.7)
Issue of ordinary shares under employee share option plans	0.5	0.6	–	–	(0.3)	0.8
Equity-settled share-based payments granted to employees of subsidiaries	–	–	2.7	–	–	2.7
Dividends paid	0.1	0.4	–	–	(7.2)	(6.7)
At 31 December 2013	33.4	4.7	12.0	–	21.9	72.0
At 1 January 2014	33.4	4.7	12.0	–	21.9	72.0
Comprehensive income	–	–	–	–	0.7	0.7
Issue of ordinary shares under employee share option plans	0.4	0.2	–	–	(0.3)	0.3
Issue of ordinary shares under capital raise (Note 21)	16.7	–	–	53.6	–	70.3
Transfer	–	–	–	(53.6)	53.6	–
Equity-settled share-based payments granted to employees of subsidiaries	–	–	2.2	–	–	2.2
Dividends paid	0.1	0.6	–	–	(8.4)	(7.7)
At 31 December 2014	50.6	5.5	14.2	–	67.5	137.8

Details of the nature of the above reserves are set out below.

Other reserve

The Company grants certain of its subsidiaries rights to its equity instruments as part of its share-based payment plan incentive schemes. The impact is recognised within this non-distributable reserve.

Merger reserve

The capital raise was effected through a structure, which resulted in a merger reserve arising under Section 612 of the Companies Act 2006. Following the receipt of the cash proceeds through the structure, the excess of the net proceeds over the nominal value of the share capital issued has been transferred to retained earnings.

Consolidated cash flow statement

Year ended 31 December

	Notes	2014 £m	2013 £m
Cash flows from operating activities			
Profit for the year		21.0	12.5
Adjustments for:			
Share of results of joint ventures and associates	13	1.3	11.3
Finance income	7	(0.7)	(0.7)
Finance expense	7	4.3	4.7
Income tax	8	1.6	0.4
Profit on sales of interests in joint ventures and associates	4	(4.0)	(9.1)
Depreciation of property, plant and equipment	4	2.0	2.4
Amortisation of intangible assets	4	3.4	2.3
Employment related and other deferred consideration		2.2	2.8
Shares purchased to satisfy employee share schemes		(2.0)	(1.5)
Share-based payments expense	5	2.2	2.7
Cash from operations before changes in working capital and provisions		31.3	27.8
Decrease in inventories		0.3	0.1
Increase in receivables		(16.3)	(12.2)
Increase/(decrease) in payables		33.1	(40.7)
Movement in provisions and employee benefits		(4.8)	(7.9)
Cash from/(used by) operations		43.6	(32.9)
Interest received		0.7	0.6
Interest paid		(3.6)	(2.9)
Income tax paid		(0.1)	(0.3)
Net cash from/(used by) operating activities		40.6	(35.5)
Cash flows from/(used by) investing activities			
Dividends received from joint ventures and associates	13	0.1	1.3
Additions to property, plant and equipment	12	(5.3)	(1.3)
Additions to intangible assets	11	(0.8)	(1.2)
Proceeds of disposal of property, plant and equipment		0.6	0.2
Additions to loans to joint ventures and associates	13	–	(2.2)
Additions to cost of investments	13	(1.7)	(2.7)
Repayment of loans to joint ventures and associates	13	0.1	-
Proceeds of sales of interests in associates	4	–	11.7
Acquisition related deferred consideration	17	(3.3)	(3.0)
Acquisition of interest in joint operation	11	(2.4)	–
Acquisition of subsidiary (net of acquired cash and cash equivalents and overdrafts)	25	–	(9.4)
Net cash used by investing activities		(12.7)	(6.6)
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		70.6	0.8
Ordinary dividends paid		(7.7)	(6.7)
(Repayment)/drawdown of revolving credit facility	16	(25.0)	25.0
Net cash from financing activities		37.9	19.1
Net increase/(decrease) in cash, cash equivalents and overdrafts		65.8	(23.0)
Cash, cash equivalents and overdrafts at beginning of the year	15	82.7	105.7
Cash, cash equivalents and overdrafts at end of the year	15	148.5	82.7

Company cash flow statement

Year ended 31 December

	Notes	2014 £m	2013 £m
Cash flows from operating activities			
Profit/(loss) for the year		0.7	(2.7)
Adjustments for:			
Finance income		(0.7)	(0.7)
Finance expense		0.1	0.3
Income tax		(0.4)	(1.1)
Cash used by operations before changes in working capital and provisions		(0.3)	(4.2)
Increase in receivables		(6.5)	(9.9)
Decrease in payables		(21.4)	(32.2)
Movement in provisions		(0.1)	(0.1)
Cash used by operations		(28.3)	(46.4)
Interest received		0.7	–
Interest paid		(0.1)	(2.8)
Income tax received		–	0.1
Net cash used by operating activities		(27.7)	(49.1)
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		70.6	0.8
Ordinary dividends paid		(7.7)	(6.7)
(Repayment)/drawdown of revolving credit facility	16	(25.0)	25.0
Net cash from financing activities		37.9	19.1
Net increase/(decrease) in cash and cash equivalents		10.2	(30.0)
Cash and cash equivalents at beginning of the year	15	–	30.0
Cash and cash equivalents at end of the year	15	10.2	–

Notes to the financial statements

1 General information

Costain Group PLC ('the Company') is a public limited company incorporated in the United Kingdom. The address of its registered office and principal place of business is disclosed on the last page of this Annual Report. The principal activities of the Company and its subsidiary undertakings (collectively referred to as 'the Group') are described in the Strategic report.

The consolidated financial statements of the Company for the year ended 31 December 2014 comprise the Group and the Group's interests in associates, joint ventures and joint operations. The parent company financial statements present information about the Company as a separate entity and not about its Group.

The financial statements were authorised for issue by the Directors on 2 March 2015.

2 Summary of significant accounting policies

Both the Company financial statements and the Group consolidated financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ('Adopted IFRS') and their related interpretations. On publishing the parent Company financial statements here together with the Group financial statements, the Company is taking advantage of the exemption in Section 408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements.

Basis of preparation

These financial statements are presented in pounds sterling, rounded to the nearest hundred thousand. The financial statements are prepared on the historical cost basis, except that financial assets and derivative financial instruments are stated at their fair value.

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. Judgments made by management in the application of IFRS that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed later in this Note.

Going concern

The Group's business activities and the factors likely to affect its future development, performance and position are set out in the Strategic report. The financial position of the Group, its cash flows, liquidity position, borrowing and bonding facilities, use of financial instruments and hedging activities, exposure to credit risk and its objectives, policies and processes for managing its capital and financial risk are described in the Financial review section of these financial statements and in Note 17.

The Group's principal business activity involves long-term contracts with a number of customers, virtually all in the United Kingdom. To meet its day-to-day working capital requirements, it uses cash balances provided from shareholders' capital and retained earnings and its borrowing facilities. As part of its contracting operations, the Group may be required to provide performance and other bonds. It satisfies these requirements by utilising its committed bonding facilities from banks and surety companies. These facilities have financial covenants that are tested quarterly.

The Directors have acknowledged the guidance "Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009" published by the Financial Reporting Council in October 2009. The Directors have considered these requirements, the Group's current order book and future opportunities and its available bonding facilities. Having reviewed the latest projections, including the application of reasonable downside sensitivities, the Directors believe that the Group is well-placed to manage its business risks successfully despite the current uncertain economic outlook. Accordingly, they continue to adopt the going concern basis in preparing these financial statements.

Accounting policies

The accounting policies set out below have, unless otherwise stated, been applied consistently by the Group and the Company to each period presented in these financial statements.

The following standards and interpretations are effective for the year ended 31 December 2014:

- IAS 27 (Revised) 'Separate Financial Statements'
- IAS 28 (Revised) 'Investments in Associates and Joint Arrangements'
- Amendment to IAS 32 'Financial Instruments: Presentation' – Offsetting Financial Assets and Financial Liabilities'
- IFRS 10 'Consolidated Financial Statements'
- IFRS 11 'Joint Arrangements'
- IFRS 12 'Disclosure of Interests in Other Entities'
- Transition guidance: Amendments to IFRS 10, IFRS 11 and IFRS 12 – amendments to simplify the transition to these standards.

The impact of these standards is limited to minor disclosure changes and alignment of accounting policies has not necessitated any prior year restatements.

2 Summary of significant accounting policies continued

Basis of consolidation

(a) The Group's financial statements include the financial statements of the Company and its subsidiaries. Subsidiaries are entities controlled by the Group and control exists when the Group is exposed to, or has the rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(b) Associates are operations over which power exists to exercise significant influence but not control. Associates are accounted for using the equity method.

(c) Joint ventures are those joint arrangements where control is shared with another entity, and where the Group has rights to the net assets of the arrangement. Joint ventures are accounted for using the equity method from the date that the joint venture commences until the date that joint control of the entity ceases.

(d) The presentation of investments in associates and joint ventures in the statement of financial position restricts the minimum carrying value to £Nil. Where the cost of investment would be negative, due to losses incurred, then an amount up to the value of the negative position is applied to any outstanding loan balance with the investment or, where future funding commitments exist, a provision is made up to the value of the commitment. Any such transfers of excess losses from the carrying value of investments are shown within reclassifications in Note 13.

(e) Joint operations are those joint arrangements over which joint control exists, established by contractual agreement and where the parties have rights to the assets and obligations for the liabilities relating to the arrangement. Where a joint operation exists, then the Group entity involved records the assets it controls, the liabilities and expenses it incurs and its share of income. Such joint operations are reported in the consolidated financial statements on the same basis. Transactions between Group companies and joint operations eliminate on consolidation.

(f) Intra-group balances and transactions together with any unrealised gains arising from intra-group transactions are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with associates, joint ventures and joint operations are eliminated to the extent of the interest in the entity or operation. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Currency translation

Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated to pounds sterling at the exchange rate ruling at the statement of financial position date. Foreign exchange differences arising on translation are recognised in the income statement.

The assets and liabilities of foreign operations are translated to pounds sterling at exchange rates ruling at the statement of financial position date. The revenues and expenses of foreign operations are translated to pounds sterling at rates approximating to the exchange rates ruling at the dates of these transactions.

Exchange differences arising from the translation of the net investment in foreign operations and of related hedges are recognised directly in equity and those that have arisen since 1 January 2004, the date of transition to IFRS, are presented as a separate component of equity. Cumulative exchange differences are released into the income statement upon disposal. Translation differences that arose before the date of transition to IFRS in respect of all foreign operations are not presented as a separate component.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable, net of value added tax and includes the share of revenue of joint operations. 97% of the Group's revenue arises from long-term contracts.

(a) Long-term contracts
Revenue arises from increase in the value of work performed on construction contracts and on the value of services provided during the year. Where the outcome of a long-term contract can be estimated reliably and it is probable that the contract will be profitable, revenue and costs are recognised by reference to the stage of completion of the contract activity at the statement of financial position date. Stage of completion is assessed by reference to the proportion of contract costs incurred for the work performed to date relative to the estimated total costs.

Variations and claims are included in revenue where it is probable that the amount, which can be measured reliably, will be recovered from the customer. When the outcome of a long-term contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred where it is probable those costs will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Notes to the financial statements
continued

2 Summary of significant accounting policies continued

Revenue recognition continued

Construction work in progress is stated at cost plus profit recognised to date less a provision for foreseeable losses and less amounts billed and is included in amounts due from customers for contract work. Cost includes all expenditure related directly to specific projects and an appropriate allocation of fixed and variable overheads based on normal operating capacity. Amounts valued and billed to customers are included in trade receivables. Where cash received from customers exceeds the value of work performed, the amount is included in credit balances on long-term contracts.

(b) Other revenue
Revenue from other services contracts is recognised when the service is provided.

Revenue from the sale of land is recognised when the significant risks and rewards of ownership have been transferred to the buyer, the amount of revenue can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Group.

Rental income is recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives are recognised as an integral part of the total rental income on a straight-line basis over the term of the lease.

Income statement presentation – Other items

In order to aid understanding of the underlying and overall performance of the Group, certain amounts are shown in the consolidated income statement in a separate column headed 'Other items'. Items are included under this heading where the Board considers them to be of a one-off and unusual nature or related to the accounting treatment of acquisitions.

Pre-contract costs

Costs associated with bidding for contracts are written off as incurred. When it is probable that a contract will be awarded, usually when preferred bidder status is secured, costs incurred from that date to the date of financial close are carried forward in the statement of financial position and included in amounts due from customers for contract work.

When financial close is achieved on PFI contracts, costs are recovered from the special purpose vehicle and pre-contract costs within this recovery that were not previously capitalised are credited to the income statement. When an interest in a special purpose vehicle is retained and that interest is accounted for as an associate or joint venture, the credit is recognised over the life of the construction contract to which the costs relate.

Research and development

Research and development activities are usually directly attributable to a project and accounted within project costs.

Goodwill and other intangible assets

Goodwill arising on acquisitions represents the excess of the fair value of the consideration over the identifiable assets, liabilities and contingent liabilities of the acquired entity and goodwill arising on the acquisition of subsidiaries is included in non-current assets. The attributable costs of acquisitions are expensed to the income statement.

Goodwill is reviewed annually for impairment and is carried at cost less accumulated impairment losses. Goodwill is included when determining the profit or loss on subsequent disposal of the business to which it relates.

Other intangible assets comprise acquired intangible assets: customer relationships, order book and brand and computer software. Customer relationships and other intangibles acquired are measured at the present value of cash flows attributable to the relationship less an appropriate contributory asset charge. Computer software is carried at cost; subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates, otherwise expenditure is expensed as incurred.

Amortisation begins when an asset is acquired or, in the case of computer software, available for use and is amortised over the following periods:

Brands	– on a straight-line basis up to three years.
Order book	– in line with expected profit generation up to three years.
Customer relationships	– on a straight-line basis up to seven years.
Computer software and development	– on a straight-line basis up to five years.

Property, plant and equipment

Property, plant and equipment is carried at cost less accumulated depreciation and impairment losses. Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items.
Cost comprises purchase price and directly attributable costs. Freehold land is not depreciated. For all other property, plant and equipment, depreciation is calculated on a straight-line basis to allocate cost less residual values of the assets over their estimated useful lives as follows:

Freehold buildings	– 50 years
Leasehold buildings	– shorter of 50 years or lease term
Plant and equipment	– remaining useful life (generally 3 to 10 years)

The assets' residual values and useful lives are reviewed and adjusted, if appropriate, at each statement of financial position date.

Investments – Company

Company investments in subsidiaries are carried at cost less provisions for impairment.

2 Summary of significant accounting policies continued

PFI investments

The Group has interests in PFI investments held through joint ventures and associates. These arrangements, whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public services, are accounted in accordance with IFRIC 12. Under this interpretation, the infrastructure assets within the Group's investments are recognised as financial assets because the operator has an unconditional right to receive a specified amount of cash or other financial asset over the life of the agreement. The operator recognises investment income in respect of the financial asset on an effective interest basis.

Impairment of non-financial assets

For the purposes of impairment testing, goodwill is allocated to each of the cash generating units expected to benefit from the synergies of the combination. Cash generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

The carrying amounts of other assets, except inventories and deferred tax assets, are reviewed at each statement of financial position date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated.

An impairment loss is recognised whenever the carrying amount of an asset, or its cash-generating unit, is less than the recoverable amount. Impairment losses are recognised in the income statement.

An impairment loss is reversed if there has been a change in the estimates resulting in the recoverable amount rising above the impaired carrying value of the asset. An impairment loss is reversed only to the extent that the carrying amount of the assets does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Provisions

A provision is recognised in the statement of financial position when there is 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. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

A provision for onerous contracts is recognised when the expected benefits to be derived from a contract are lower than the unavoidable cost of meeting the obligations under the contract.

Taxation

The tax expense represents the sum of United Kingdom corporation tax and overseas tax currently payable and deferred tax.

The tax currently payable is based on the taxable profit for the year. Taxable profit differs from profit before tax as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The liability for current tax is calculated using tax rates and laws that have been enacted or substantively enacted by the statement of financial position date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit and is accounted for using the statement of financial position liability method. Deferred tax liabilities are generally recognised for all temporary differences except for those specific exemptions set out below and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. The carrying amount of deferred tax assets is reviewed at each statement of financial position date. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill or other assets and liabilities, other than in a business combination, in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for temporary differences arising on investments in subsidiaries and interests in joint arrangements, 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. Deferred tax is calculated at the tax rates based on those enacted or substantially enacted at the statement of financial position date. Deferred tax is charged or credited in the income statement except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Additional taxes arising from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

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continued

2 Summary of significant accounting policies continued

Leases

Leases principally comprise operating leases. Payments made under operating leases are recognised as an expense in the income statement on a straight-line basis over the lease term. Any incentives to enter into operating leases are recognised as a reduction of rental expense over the lease term on a straight-line basis.

Financial guarantee contracts

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within the Group, the Company considers these to be insurance arrangements and accounts for them as such. In this respect, the guarantee contract is treated as a contingent liability until such time as it becomes probable that a payment under the guarantee will be required.

Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Dividends

Dividends are recognised as distributions in the period in which they are declared. Dividends proposed but not declared are not recognised but are disclosed in the Note 10 to the financial statements.

Share-based payments

These comprise equity-settled and cash-settled share-based compensation plans.

Equity-settled share-based payments are measured at fair value at the date of grant and the fair value is expensed over the vesting period, based on the estimate of awards that will eventually vest. For cash-settled share-based payments, a liability equal to the portion of the services received is recognised at its current fair value determined at each statement of financial position date. Fair value is measured by the use of a Black-Scholes option pricing model.

Where options are granted over shares in the Company to employees of subsidiaries, the Company recognises in its financial statements an increase in the cost of investment in its subsidiaries equivalent to the equity-settled share-based payment charge recognised in its subsidiaries' financial statements, with the corresponding credit being recognised directly in equity.

Retirement benefit obligations

A defined benefit pension scheme is operated in the United Kingdom, which provides benefits based on pensionable salary. The details are included in Note 20. The assets of the scheme are held separately from those of the Group.

Pension scheme assets are measured using market values. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high-quality corporate bond of equivalent term and currency to the liability. The liability recognised in the statement of financial position in respect of the defined benefit pension scheme is the present value of the defined benefit obligations less the fair value of scheme assets at the statement of financial position date.

Administration costs of the scheme are recognised in the income statement. The interest cost on the scheme's net liabilities is included in finance expense. Remeasurements of the net liability are recognised in the consolidated statement of comprehensive income.

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

Financial assets and liabilities

Financial assets and financial liabilities are recognised in the Group's statement of financial position when the Group becomes a party to the contractual provisions of the instrument.

(a) Financial assets

Financial assets are classified as loans and receivables. The classification depends on the nature and purpose of the financial asset and is determined at the time of initial recognition.

A financial asset is derecognised only when the contractual rights to the cash flows from that asset expire, or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

Loans and receivables
Loans and other receivables with fixed or determinable payments that are not quoted in an active market are classified as loans and receivables and measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Trade and other receivables
Trade and other receivables do not carry interest and are stated at their initial value less impairment losses.

Impairment of financial assets
Estimated recoverable amounts are based on the ageing of the outstanding receivable and provisions against individual receivables are recognised when management deems the amounts are not collectible.

2 Summary of significant accounting policies continued

Cash and cash equivalents
Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(b) Financial liabilities

Financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis. Where borrowings are the hedged item in an effective fair value hedge relationship, the carrying value is adjusted to reflect the fair value movements associated with the hedged risk. Financial liabilities are derecognised only when the obligations are discharged, cancelled or expire.

Trade payables
Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

(c) Derivative financial instruments

Derivative financial instruments are used to manage risks arising from changes in foreign exchange rates, interest rates and inflation and are measured at their fair value. The fair value of forward exchange contracts is their quoted market value at the statement of financial position date. Valuations for forward exchange contracts are determined using valuation techniques supported by reference to market values for similar transactions.

Certain derivative financial instruments are designated as hedges in line with established risk management policies and classified as follows:

- Fair value hedges that hedge the exposure to changes in the fair value of a recognised asset or liability; or
- Cash flow hedges that hedge exposure to variability in cash flows that is attributable to either a particular risk associated with a recognised asset or liability or a forecast transaction.

For fair value hedges, any gain or loss from re-measuring the hedging instrument at fair value is recognised in the income statement and adjusted against the carrying amount of the hedged item.

For cash flow hedges, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in equity, with any ineffective portion in the income statement. When hedged cash flows result in the recognition of a non-financial asset or liability, the associated gains or losses previously recognised in equity are included in the initial measurement of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in equity are transferred to the income statement in the same period in which the hedged cash flow affects the income statement.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss previously recognised in equity is retained in equity until the hedged transaction occurs. If the hedged transaction is no longer expected to occur, the net cumulative gain or loss is transferred to the income statement.

Any gains or losses arising from changes in fair value of derivative financial instruments not designated as hedges are recognised in the income statement.

Fair value measurement

When measuring the fair value of a financial or non-financial asset or liability, the group uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets and 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 (unobservable inputs).

If the inputs used to measure the fair value of an asset or liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the hierarchy as the lowest level input that is significant to the entire measurement.

In accordance with the transitional provisions of IFRS 13, the Group has applied the new fair value measurement guidance prospectively and has not provided any comparative information for new disclosures.

Significant areas of judgment and estimation

The estimates and underlying assumptions used in the preparation of these financial statements are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The most critical accounting policies and significant areas of judgment and estimation arise from the accounting for long-term contracts under IAS 11 Construction contracts, assessments of the carrying value of land and the carrying value of goodwill and acquired intangible assets and the assumptions used in the accounting for defined benefit pension schemes under IAS 19 Employee benefits.

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continued

2 Summary of significant accounting policies continued

Significant areas of judgment and estimation continued

The majority of the Group's activities are undertaken via long-term contracts and these contracts are accounted for in accordance with IAS 11, which requires estimates to be made for contract costs and revenues. In many cases, these contractual obligations span more than one financial period. Also, the costs and revenues may be affected by a number of uncertainties that depend on the outcome of future events and may need to be revised as events unfold and uncertainties are resolved.

Management bases its judgments of costs and revenues and its assessment of the expected outcome of each long-term contractual obligation on the latest available information, this includes detailed contract valuations and forecasts of the costs to complete. The estimates of the contract position and the profit or loss earned to date are updated regularly and significant changes are highlighted through established internal review procedures. The impact of any change in the accounting estimates is then reflected in the financial statements.

Alcaidesa Holding SA, one of the Group's joint arrangements, operates in the Spanish real estate market and holds land and property within its current and non-current assets. The company has also developed and operates a marina under a long-term concession agreement and has developed and operates two golf courses. At 31 December 2014, a review of the net realisable value of its land holdings has been undertaken using external professional valuers. A review of the carrying value of the marina and golf course assets has been undertaken using a discounted cash flow model. As a consequence of those reviews, no write downs in the value of Alcaidesa's assets were required in these financial statements.

Reviewing the carrying value of goodwill and intangible assets recognised on acquisition requires judgments, principally, in respect of growth rates and future cash flows of cash generating units, the useful lives of intangible assets and the selection of discount rates used to calculate present values are set out in Note 11.

Defined benefit pension schemes require significant judgments in relation to the assumptions for inflation, future pension increases, investment returns and member longevity that underpin the valuation. Each year in selecting the appropriate assumptions, the Directors take advice from an independent qualified actuary. The assumptions and resultant sensitivities are set out in Note 20.

IFRSs not applied

The following IFRSs having been endorsed, will be applicable in the future:

- IFRS 9 'Financial Instruments' – Published in July 2014 and replacing the existing guidance in IAS 39 'Financial Instruments: Recognition and Measurement.' IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

  The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 9.
- IFRS 15 'Revenue from Contracts with Customers' establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 'Revenue', IAS 11 'Construction Contacts' and IFRIC 13 'Customer Loyalty programmes.' IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2017, with early adoption permitted.

  The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 15.
- 'Accounting for Acquisitions of Interests in Joint Operations' (Amendments to IFRS 11).
- 'Clarification of Acceptable methods of Depreciation and Amortisation' (Amendments to IAS 16 and IAS 38).
- 'Defined Benefit Plans: Employee Contributions' (Amendments to IAS 19).
- Annual Improvements to IFRSs 2010-2012 Cycle.
- Annual Improvements to IFRSs 2011-2013 Cycle.

3 Operating segments

The Group has two core business segments: Natural Resources and Infrastructure plus the Land Development operations in Spain. The core segments are strategic business units with separate management and have different core customers or offer different services. This information is provided to the Chief Executive who is the chief operating decision maker. The segments are discussed in the Strategic report section of these financial statements.

The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies. The Group evaluates segment performance on the basis of profit or loss from operations before interest and income tax expense before and after other items. The segment results that are reported to the Chief Executive include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

Intersegment sales and transfers are not material.

2014	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Segment revenue					
External revenue	301.5	770.3	–	–	1,071.8
Share of revenue of joint ventures and associates	33.5	14.9	2.3	–	50.7
Total segment revenue	335.0	785.2	2.3	–	1,122.5
Segment profit/(loss)					
Operating profit/(loss)	(3.5)	38.3	–	(6.1)	28.7
Profit on sales of interests in joint ventures and associates	4.0	–	–	–	4.0
Share of results of joint ventures and associates	–	–	(1.3)	–	(1.3)
Profit/(loss) from operations before other items	0.5	38.3	(1.3)	(6.1)	31.4
Other items:					
Amortisation of acquired intangible assets	(1.5)	(1.5)	–	–	(3.0)
Employment related and other deferred consideration	(2.2)	–	–	–	(2.2)
Profit/(loss) from operations	(3.2)	36.8	(1.3)	(6.1)	26.2
Net finance expense					(3.6)
Profit before tax					22.6
Segment profit/(loss) is stated after charging the following:					
Depreciation	1.0	1.0	–	–	2.0
Amortisation (including acquired intangible assets)	1.7	1.7	–	–	3.4
Segment assets					
Reportable segment assets	133.5	139.7	25.2	0.3	298.7
Unallocated assets:					
Deferred tax					9.2
Cash and cash equivalents					148.5
Total assets					456.4

Notes to the financial statements
continued

3 Operating segments continued

2014	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Expenditure on non-current assets					
Property, plant and equipment	5.1	0.2	–	–	5.3
Intangible assets	0.8	–	–	–	0.8
Segment liabilities					
Reportable segment liabilities	104.0	190.5	–	7.9	302.4
Unallocated liabilities:					
Retirement benefit obligations					41.7
Income tax					1.5
Total liabilities					345.6

2013	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Segment revenue					
External revenue	324.6	560.6	–	–	885.2
Share of revenue of joint ventures and associates	73.0	–	1.8	–	74.8
Total segment revenue	397.6	560.6	1.8	–	960.0
Segment profit/(loss)					
Operating profit/(loss)	3.1	31.4	–	(7.1)	27.4
Profit on sales of interests in joint ventures and associates	9.1	–	–	–	9.1
Share of results of joint ventures and associates	0.6	–	(2.1)	–	(1.5)
Profit/(loss) from operations before other items	12.8	31.4	(2.1)	(7.1)	35.0
Other items:					
Exceptional transaction costs	–	–	–	(3.7)	(3.7)
Amortisation of acquired intangible assets	(1.2)	(0.6)	–	–	(1.8)
Employment related and other deferred consideration	(2.1)	(0.7)	–	–	(2.8)
Impairment of assets of joint venture	–	–	(9.8)	–	(9.8)
Profit/(loss) from operations	9.5	30.1	(11.9)	(10.8)	16.9
Net finance expense					(4.0)
Profit before tax					12.9
Segment profit/(loss) is stated after charging the following:					
Depreciation	1.0	1.4	–	–	2.4
Amortisation (including acquired intangible assets)	1.4	0.9	–	–	2.3
Segment assets					
Reportable segment assets	133.3	126.6	26.6	0.7	287.2
Unallocated assets:					
Deferred tax					9.8
Cash and cash equivalents					84.3
Total assets					381.3
Expenditure on non-current assets					
Property, plant and equipment	1.2	0.1	–	–	1.3
Intangible assets	0.7	2.9	–	–	3.6

3 Operating segments continued

2013	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Loans to joint ventures and associates	2.2	–	–	–	2.2

Segment liabilities					
Reportable segment liabilities	109.7	155.4	–	7.5	272.6
Unallocated liabilities:					
Retirement benefit obligations					37.2
Overdrafts					1.6
Borrowings					25.0
Income tax					1.6
Total liabilities					338.0

Geographical information

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets are based on the geographical location of the assets and exclude deferred tax assets.

2014	External revenue £m	Share of revenue of JVs and assoc's £m	Total segment revenue £m	Non-current assets £m
United Kingdom	1,070.7	48.3	1,119.0	75.1
Spain	–	2.4	2.4	25.2
Rest of the World	1.1	–	1.1	–
	1,071.8	50.7	1,122.5	100.3

2013	External revenue £m	Share of revenue of JVs and assoc's £m	Total segment revenue £m	Non-current assets £m
United Kingdom	875.7	73.0	948.7	68.4
Spain	–	1.8	1.8	26.6
Rest of the World	9.5	–	9.5	–
	885.2	74.8	960.0	95.0

Customers accounting for more than 10% of revenue

Two customers (2013: two) in the Infrastructure segment accounted for revenue of £443.5 million (2013: £289.6 million).

Notes to the financial statements

continued

4 Other operating expenses and income

	2014 £m	2013 £m
Profit before tax is stated after charging:		
Amortisation of intangible assets (Note 11)	3.4	2.3
Depreciation of property, plant and equipment (Note 12)	2.0	2.4
Exceptional transaction costs	–	3.7
Hire of plant and machinery	45.1	27.6
Rent of land and buildings	5.3	5.2
and after crediting:		
Profit on sales of interests in joint ventures and associates	4.0	9.1
Income from sub-leases of land and buildings	0.5	0.7

In December 2014, the Group transferred two PFI investments, Lewisham Schools for the Future Holdings 3 Limited and Lewisham Schools for the Future Holdings 4 Limited, to The Costain Pension Scheme for £7.4 million. The transfer amount was included as a contribution received by the Scheme (Note 20).

In 2013, costs of £3.7 million associated with the lapsed all share merger with May Gurney Integrated Services plc were shown as exceptional transaction costs within Other items.

In December 2013, the Group sold three minority shareholdings in three joint venture companies to Severn Trent Plc for an aggregate cash consideration of £12.0 million. The three companies were Severn Trent Costain Holdings Limited, Severn Trent Costain Services Limited and Severn Trent Costain Limited. As a result of the sale, the Group realised a profit of £9.1 million. £1.2 million of fair value adjustments on the PFI financial assets relating to cash flow hedges were recycled through the income statement as part of this profit.

Auditor's remuneration

	2014 £m	2013 £m
Fees payable to the Group's auditor for the audit of the annual financial statements	0.1	0.1
Fees payable to the Group's auditor and its associates in respect of:		
– Audit of financial statements of subsidiaries of the Company	0.3	0.3
– Other tax advisory services	–	0.1
– Transaction related services not covered above	0.4	1.6
	0.8	2.1

Amounts paid to the Company's auditor and its associates in respect of services to the Company, other than the audit of the Company's financial statements, have not been disclosed as the information is required instead to be disclosed on a consolidated basis.

5 Employee benefit expense

	2014 £m	2013 £m
Group		
Wages and salaries	162.1	151.4
Social security costs	17.4	16.2
Pension costs (Note 20)	7.8	7.1
Share-based payments expense (Note 20)	2.2	2.7
	189.5	177.4

	2014 Number	2013 Number
Average number of persons employed		
Natural Resources	1,139	1,397
Infrastructure	2,746	2,201
Central	24	22
	3,909	3,620

Of the above employees nine were employed overseas (2013: 292).

Company

The Company does not employ any personnel, except for the Directors considered in Note 6.

6 Remuneration of Directors

Details of the Directors' remuneration, pension entitlements, interest in the Long-Term Incentive Plans, Annual Incentive Plans, Deferred Share Bonus Plans and share options are included in the Directors' remuneration report.

For the purpose of the disclosure required by Schedule 5 to the Companies Act 2006, the total aggregate emoluments of the Directors in respect of 2014 and 2013 are detailed below.

	2014 £m	2013 £m
Remuneration	1.5	1.6
Post-employment benefits	0.2	0.1
Gains made on the exercise of share-based plans	0.9	0.7
	2.6	2.4

7 Net finance expense

	2014 £m	2013 £m
Interest income from bank deposits	0.2	0.1
Interest income on loans to related parties	0.5	0.6
Finance income	0.7	0.7
Interest payable on bank overdrafts, interest bearing loans, borrowings and other similar charges	(2.2)	(2.6)
Unwind of discount on deferred consideration	(0.7)	–
Interest cost on the net liabilities of the defined benefit pension scheme (Note 20)	(1.4)	(2.1)
Finance expense	(4.3)	(4.7)
Net finance expense	(3.6)	(4.0)

Interest income on loans to related parties relates to shareholder loan interest receivable from investments in equity accounted joint ventures and associates.

Notes to the financial statements
continued

8 Income tax

	2014 £m	2013 £m
On profit for the year		
United Kingdom corporation tax at 21.5% (2013: 23.25%)	–	–
Adjustment in respect of prior years	–	0.1
Current tax credit for the year	–	0.1
Deferred tax charge for current year	(2.2)	(1.4)
Adjustment in respect of prior years	0.6	0.9
Deferred tax charge for the year	(1.6)	(0.5)
Income tax expense in the consolidated income statement	(1.6)	(0.4)

	2014 £m	2013 £m
Tax reconciliation		
Profit before tax	22.6	12.9
Income tax at 21.5% (2013: 23.25%)	(4.9)	(3.0)
Share of results of joint ventures and associates at 21.5% (2013: 23.25%)	(0.3)	(2.6)
Disallowed provisions and expenses charged to reserves	0.2	(0.1)
Non-taxable gains	0.9	2.2
Utilisation of previously unrecognised temporary differences	0.3	0.7
Research and Development tax relief for current year	0.7	–
Rate adjustment relating to deferred taxation and overseas profits and losses	0.9	1.4
Adjustments in respect of prior years, mainly Research and Development tax relief claims	0.6	1.0
Income tax expense in the consolidated income statement	(1.6)	(0.4)
Effective rate of tax	7.1%	3.1%

The income tax above does not include any amounts for equity accounted joint ventures and associates, whose results are disclosed in the consolidated income statement net of tax.

The current tax liabilities of £1.5 million (2013: £1.6 million) for the Group and £1.5 million (2013: £1.5 million) for the Company represent the amount of income taxes in respect of all outstanding periods.

Accumulated tax losses carried forward, mainly in the United Kingdom, were £5.1 million (2013: £5.3 million).

	2014 £m	2013 £m
Deferred tax asset recognised at 20.0% (2013: 21.0%)		
Accelerated capital allowances	1.8	1.6
Short-term temporary differences	(1.1)	–
Retirement benefit obligations	8.4	7.9
Tax losses	0.1	0.3
Deferred tax asset	9.2	9.8

The Company had no deferred tax asset at either year end.

8 Income tax continued

	2014 £m	2013 £m
Analysis of deferred tax movements		
At 1 January	9.8	17.4
Deferred tax relating to business combinations		
Transfer in respect of acquired intangible assets	–	(1.3)
Deferred tax in consolidated income statement		
Accelerated capital allowances	0.1	(0.4)
Short-term temporary differences	(0.5)	(1.2)
Trading tax losses	(0.2)	–
Retirement benefit obligations	(1.0)	1.1
	(1.6)	(0.5)
Deferred tax in other comprehensive income and expense statement		
Retirement benefit obligations	1.5	(5.3)
Deferred tax recognised directly in the consolidated statement of changes in equity		
Short-term temporary differences	(0.5)	(0.5)
At 31 December	9.2	9.8

Factors that may affect future tax charges

The Group and Company have potential deferred tax assets in their United Kingdom operations that have not been recognised at the year end on the basis that their future economic benefits were not assured at the statement of financial position date.

Gross deferred tax assets not recognised at the statement of financial position date were as follows:

	Group		Company	
	2014 £m	2013 £m	2014 £m	2013 £m
Accelerated capital allowances	3.3	3.3	–	–
Short-term temporary differences	22.6	22.0	–	–
Trading tax losses	4.4	3.8	–	–
Temporary differences	30.3	29.1	–	–
In addition to the above temporary differences, the following gross deferred tax assets are available.				
Management expenses and charges incurred by parent Company	56.9	56.9	56.9	56.9
Capital losses	275.0	275.0	241.0	241.0

The current year tax effect, at 21.5%, of claiming short-term temporary differences and trading tax losses was £0.3 million (2013: £0.7 million) as shown in the tax reconciliation above.

There are no expiry dates associated with the deferred tax assets, recognised and not recognised, and tax relief will be obtained if suitable profits arise in the future in the relevant entities.

Notes to the financial statements
continued

9 Earnings per share

The calculation of earnings per share is based on profit of £21.0 million (2013: £12.5 million) and the number of shares set out below.

	2014 Number (millions)	2013 Number (millions) restated*
Weighted average number of ordinary shares in issue for basic earnings per share calculation	94.6	71.2
Dilutive potential ordinary shares arising from employee share schemes	2.1	2.9
Weighted average number of ordinary shares in issue for diluted earnings per share calculation	96.7	74.1

* The number of shares has been adjusted for the bonus element within the 2014 capital raise detailed in Note 21.

At 31 December 2014, 0.6 million options were excluded from the weighted average number of ordinary shares calculation as they were anti-dilutive (2013: all options were included).

10 Dividends

	Dividend per share pence	2014 £m	2013 £m
Final dividend for the year ended 31 December 2012	7.25	–	4.7
Interim dividend for the year ended 31 December 2013	3.75	–	2.5
Final dividend for the year ended 31 December 2013	7.75	5.2	–
Interim dividend for the year ended 31 December 2014	3.25	3.2	–
Amount recognised as distributions to equity holders in the year		8.4	7.2
Dividends settled in shares		(0.7)	(0.5)
Dividends settled in cash		7.7	6.7

A final dividend in respect of the year ended 31 December 2014 of 6.25p per share, amounting to a dividend of £6.3 million, is to be proposed at the Annual General Meeting. If approved, the dividend is expected to be paid on 22 May 2015 to shareholders registered at the close of business on 17 April 2015 and a scrip dividend alternative will be offered. These financial statements do not reflect the final dividend payable.

11 Intangible assets

Group	Goodwill £m	Customer relationships £m	Other acquired intangibles £m	Software & development £m	Total £m
Cost					
At 1 January 2013	15.2	4.1	1.7	5.3	26.3
Acquired through business combinations	7.1	4.5	1.4	–	13.0
Additions	–	–	2.4	1.2	3.6
At 31 December 2013	22.3	8.6	5.5	6.5	42.9
At 1 January 2014	**22.3**	**8.6**	**5.5**	**6.5**	**42.9**
Reclassifications from property, plant and equipment	**–**	**–**	**–**	**0.6**	**0.6**
Additions	**–**	**–**	**–**	**0.8**	**0.8**
Disposals	**–**	**–**	**–**	**(0.2)**	**(0.2)**
At 31 December 2014	**22.3**	**8.6**	**5.5**	**7.7**	**44.1**
Amortisation					
At 1 January 2013	–	2.2	0.4	5.0	7.6
Provided in year	–	0.4	1.4	0.5	2.3
At 31 December 2013	–	2.6	1.8	5.5	9.9
At 1 January 2014	**–**	**2.6**	**1.8**	**5.5**	**9.9**
Provided in year	**–**	**1.5**	**1.5**	**0.4**	**3.4**
Disposals	**–**	**–**	**–**	**(0.2)**	**(0.2)**
At 31 December 2014	**–**	**4.1**	**3.3**	**5.7**	**13.1**

Net book value					
At 31 December 2014	**22.3**	**4.5**	**2.2**	**2.0**	**31.0**
At 31 December 2013	22.3	6.0	3.7	1.0	33.0
At 1 January 2013	15.2	1.9	1.3	0.3	18.7

In December 2013, the Group acquired the outstanding 27% interest from its partner Serco plc in their Managed Motorway Technology joint venture arrangement for a cash consideration of £2.4 million paid January 2014.

The net book value of other acquired intangible assets includes £2.1 million (2013: £3.6 million) relating to order book.

Goodwill has been allocated to the applicable cash generating units identified within the Infrastructure (£5.5 million) and Natural Resources (£16.8 million) reporting segments.

As described in Note 2, the Group reviews the value of goodwill and in the absence of any identified impairment risks, tests are based on internal value in use calculations of the cash generating unit ('CGU'). The key assumptions for these calculations are: discount rates, growth rates and expected changes to revenue and direct costs during the period.

Discount rates have been estimated based on pre-tax rates that reflect current market assessments of the Group's weighted average cost of capital and the risks specific to the CGU. The rate used to discount the forecast cash flows for the CGU in Infrastructure was 10.5% and for the CGU in Natural Resources was 12.5%.

The Group prepares cash flow forecasts derived from the most recent financial forecasts for the following two years and extrapolates those cash flows based on the following internal assessments of the annual growth rates attributable to the CGUs:

Growth rates	Infrastructure %	Natural Resources %
Years 3-4	2.5	2.5
Year 5	1.5	2.5
Long-term average	1.5	1.5

As at 31 December 2014, based on these internal valuations, the recoverable value of goodwill exceeded the carrying amounts by a comfortable amount.

Notes to the financial statements
continued

12 Property, plant and equipment

	Land and buildings £m	Plant and equipment £m	Total £m
Group			
Cost			
At 1 January 2013	0.9	22.3	23.2
Additions	–	1.3	1.3
Disposals	–	(1.3)	(1.3)
Acquired through business combinations	–	0.1	0.1
At 31 December 2013	0.9	22.4	23.3
At 1 January 2014	0.9	22.4	23.3
Reclassifications to intangible assets	–	(0.6)	(0.6)
Additions	–	5.3	5.3
Disposals	–	(6.4)	(6.4)
At 31 December 2014	0.9	20.7	21.6
Depreciation			
At 1 January 2013	0.6	13.5	14.1
Provided in year	–	2.4	2.4
Disposals	–	(1.1)	(1.1)
At 31 December 2013	0.6	14.8	15.4
At 1 January 2014	0.6	14.8	15.4
Provided in year	0.1	1.9	2.0
Disposals	–	(5.8)	(5.8)
At 31 December 2014	0.7	10.9	11.6
Net book value			
At 31 December 2014	0.2	9.8	10.0
At 31 December 2013	0.3	7.6	7.9
At 1 January 2013	0.3	8.8	9.1

13 Investments and loans in subsidiaries, equity accounted joint ventures and associates

	Investments		Loans	
	Joint ventures £m	Associates £m	Associates £m	Total £m
Group				
Cost or fair value				
At 1 January 2013	54.9	0.2	3.6	58.7
Currency realignment	(0.3)	–	–	(0.3)
Additions	2.7	–	2.2	4.9
Disposal	–	(0.1)	(1.0)	(1.1)
At 31 December 2013	57.3	0.1	4.8	62.2
At 1 January 2014	**57.3**	**0.1**	**4.8**	**62.2**
Currency realignment	**(2.9)**	**–**	**–**	**(2.9)**
Additions	**1.7**	**–**	**–**	**1.7**
Repayments	**–**	**–**	**(0.1)**	**(0.1)**
Disposal	**–**	**–**	**(3.0)**	**(3.0)**
At 31 December 2014	**56.1**	**0.1**	**1.7**	**57.9**
Share of post-acquisition reserves				
At 1 January 2013	(18.8)	0.1		(18.7)
Currency realignment	0.1	–		0.1
Disposals	–	0.1		0.1
Dividends	–	(1.3)		(1.3)
(Loss)/profit for the year	(11.5)	0.2		(11.3)
Cash flow hedges – change in fair value	–	(0.2)		(0.2)
Cash flow hedges – disposals	–	1.2		1.2
At 31 December 2013	(30.2)	0.1		(30.1)
At 1 January 2014	**(30.2)**	**0.1**		**(30.1)**
Currency realignment	**1.0**	**–**		**1.0**
Disposals	**–**	**0.1**		**0.1**
Dividends	**–**	**(0.1)**		**(0.1)**
(Loss)/profit for the year	**(1.4)**	**0.1**		**(1.3)**
At 31 December 2014	**(30.6)**	**0.2**		**(30.4)**
Reclassifications				
At 1 January 2013	–	1.3	(0.9)	0.4
Adjustment in the year	–	(1.3)	0.9	(0.4)
At 31 December 2013	–	–	–	–
At 1 January 2014	–	–	–	–
At 31 December 2014	**–**	**–**	**–**	**–**
Net book value				
At 31 December 2014	**25.5**	**0.3**	**1.7**	**27.5**
At 31 December 2013	27.1	0.2	4.8	32.1
At 1 January 2013	36.1	1.6	2.7	40.4

Notes to the financial statements
continued

13 Investments and loans in subsidiaries, equity accounted joint ventures and associates
continued

Analysis of Group share of joint ventures and associates revenue, income and assets and liabilities

	2014				2013			
	Alcaidesa Holding SA £m	Other joint ventures £m	Associates £m	Total £m	Alcaidesa Holding SA £m	Other joint ventures £m	Associates £m	Total £m
Revenue	2.3	41.7	6.7	50.7	1.8	43.1	29.9	74.8
(Loss)/profit before tax	(0.8)	(0.2)	0.2	(0.8)	(11.9)	0.4	0.3	(11.2)
Income tax	(0.5)	–	–	(0.5)	–	–	(0.1)	(0.1)
(Loss)/profit for the year	(1.3)	(0.2)	0.2	(1.3)	(11.9)	0.4	0.2	(11.3)
Non-current assets	16.1	–	–	16.1	18.4	–	0.8	19.2
Current assets	18.6	12.0	3.5	34.1	19.6	18.3	41.2	79.1
Current liabilities	(1.8)	(11.7)	(1.8)	(15.3)	(2.6)	(17.8)	(15.9)	(36.3)
Non-current liabilities	(7.7)	–	(1.4)	(9.1)	(8.8)	–	(25.9)	(34.7)
Investments in joint ventures and associates	25.2	0.3	0.3	25.8	26.6	0.5	0.2	27.3
Dividends received by Group	–	–	0.1	0.1	–	–	1.3	1.3

Net interest payable by joint ventures and associates in 2014 was £0.6 million (2013: £1.0 million). The applicable interest rates during the year are income of 0.2% to 6.5% per annum (2013: 0.2% to 6.5%) and expense of 1.7% to 11.5% per annum (2013: 1.7%to 11.5%).

Analysis of the total revenue, income, assets and liabilities of joint ventures and associates

	2014				2013			
	Alcaidesa Holding SA £m	Other joint ventures £m	Associates £m	Total £m	Alcaidesa Holding SA £m	Other joint ventures £m	Associates £m	Total £m
Revenue	4.7	111.1	16.9	132.7	3.7	105.1	93.6	202.4
(Loss)/profit before tax	(1.6)	(0.4)	0.4	(1.6)	(23.7)	0.8	0.7	(22.2)
Income tax	(1.0)	–	(0.1)	(1.1)	–	–	(1.0)	(1.0)
(Loss)/profit for the year	(2.6)	(0.4)	0.3	(2.7)	(23.7)	0.8	(0.3)	(23.2)
Non-current assets	32.2	–	0.1	32.3	36.8	–	2.1	38.9
Current assets	37.2	29.6	8.6	75.4	39.3	43.1	103.1	185.5
Current liabilities	(3.7)	(28.9)	(4.5)	(37.1)	(5.3)	(41.9)	(39.6)	(86.8)
Non-current liabilities	(15.4)	–	(3.4)	(18.8)	(17.6)	–	(64.8)	(82.4)
Equity	50.3	0.7	0.8	51.8	53.2	1.2	0.8	55.2

Details of the principal subsidiary undertakings, joint ventures, joint operations and associates are shown in Note 24.

The loss for the year of Alcaidesa Holding SA includes depreciation and amortisation of £1.3 million (2013: £1.4 million) and interest expense of £1.2 million (2013: £1.4 million). There is no other comprehensive income / (expense). Current assets of Alcaidesa Holding SA includes cash and cash equivalents of £0.5 million (2013: £0.4 million). Current financial liabilities (excluding trade and other payables and provisions) comprises borrowings of £1.6 million (2013: 2.5 million). Non-current liabilities comprises borrowings.

There is no other comprehensive income / (expense) in respect of other joint ventures and the associates.

13 Investments and loans in subsidiaries, equity accounted joint ventures and associates continued

Company	
Investments in subsidiaries	£m
Cost	
At 1 January 2013	364.4
Additions	2.7
At 31 December 2013	367.1
At 1 January 2014	**367.1**
Additions	**2.2**
At 31 December 2014	**369.3**
Amounts written off	
At 1 January 2013	(269.2)
At 31 December 2013	(269.2)
At 1 January 2014	**(269.2)**
At 31 December 2014	**(269.2)**

Net book value	
At 31 December 2014	**100.1**
At 31 December 2013	97.9
At 1 January 2013	95.2

Additions relate to the increase in the cost of investments in subsidiaries by the equivalent amount of the equity settled share-based payment charge in relation to employees of subsidiaries included in the income statement.

Details of the principal subsidiaries in which the Company has an interest are set out in Note 24.

14 Trade and other receivables

	Group		Company	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Amounts included in current assets				
Trade receivables	**95.5**	87.4	**–**	–
Other receivables	**16.8**	5.3	**–**	–
Amounts due from customers for contract work	**71.1**	80.3	**–**	–
Prepayments and accrued income	**12.9**	15.2	**1.4**	1.0
Amounts owed by joint ventures and associates	**0.8**	2.4	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**56.8**	50.3
	197.1	190.6	**58.2**	51.3
Amounts included in non-current assets				
Other	**31.8**	22.0	**–**	–

At 31 December 2014, amounts due from customers for contract work falling due within one year include retentions of £1.4 million (2013: £20.6 million) relating to long-term contracts in progress. Other receivables falling due after more than one year include retentions of £31.1 million (2013: £21.5 million) relating to long-term contracts in progress.

With respect to trade receivables that are neither impaired nor past due, there are no indications at the reporting date that the payment obligations will not be met. The Directors consider that the carrying amount of trade, other receivables and amounts owed by joint ventures and associates approximates to their fair value.

Notes to the financial statements
continued

14 Trade and other receivables continued

The average credit period within trade receivables on amounts billed for construction work and on sales of goods is 33 days (2013: 33 days). The analysis of the due dates of the trade receivables was £68.5 million (2013: £76.1 million) due within 30 days, £25.6 million (2013: £8.8 million) due between 30 and 60 days and £1.4 million (2013: £2.5 million) due after 60 days.

These balances include receivables, with a carrying amount of £4.3 million (2013: £5.0 million), which are past due at the reporting date and for which no provision has been made as there has been no significant change in credit quality and the amounts are considered recoverable. No collateral is held over these balances. The analysis of the overdue amounts was £2.9 million (2013: £2.8 million) overdue by less than 30 days, £0.3 million (2013: £0.5 million) overdue by between 30 and 60 days and £1.1 million (2013: £1.7 million) overdue by more than 60 days.

The provision for impairment of trade and other receivables is £7.4 million (2013: £6.9 million).

The aggregate amount of costs incurred plus recognised profits, less recognised losses, for all contracts in progress at the statement of financial position date was £2,927.6 million (2013: £2,782.6 million). Progress billings and advances received from customers under open construction contracts amounted to £2,915.9 million (2013: £2,728.8 million). Advances for which work has not started, and billings in excess of costs incurred and recognised profits are included in credit balances on long-term contracts.

15 Cash and cash equivalents

Cash and cash equivalents are analysed below, and include the Group’s share of cash held by joint operations of £24.1 million (2013: £25.6 million).

	Group		Company	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Cash and cash equivalents	**148.5**	84.3	**10.2**	–
Bank overdrafts	**–**	(1.6)	**–**	–
Cash, cash equivalents and overdrafts in the cash flow statement	**148.5**	82.7	**10.2**	–

16 Interest bearing loans and borrowings

	Group		Company	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Revolving Credit Facility	**–**	25.0	**–**	25.0

The Group’s borrowings facilities are described in Note 17.

17 Financial instruments – Fair values and risk management

a) Risk management

The Group's centralised treasury function manages financial risk, principally arising from liquidity and funding risks and movements in foreign currency rates, interest rates and inflation rates, in accordance with policies agreed by the Directors.

The Group does not enter into speculative transactions.

The Company does not have any forward foreign currency contracts or other derivatives.

i) Capital management

The Group's objectives when managing capital are to safeguard its ability to continue as a going concern and to provide resources to grow the business, in order to provide returns for shareholders and other stakeholders. The current capital base of the Group is driven by equity capital from shareholders and retained earnings. During the year, the Group raised £70.3 million (net of expenses) through a capital raise (Note 21). The proceeds will demonstrate to customers the Group's financial capacity to support further increases in contract size and duration and fund likely increased working capital requirements arising from the move to target-cost, cost-reimbursable contracts. The Board of Directors ('Board') continues to seek to strengthen the Group by growing the business and improving profitability; the Strategic report describes the Group's strategy and its operations. It is the Board's policy to progressively increase dividends paid to shareholders based on growth in underlying earnings per share after taking account of the investment and capital needs of the business. There were no changes in the Board's approach to capital management during the year.

ii) Liquidity and funding risk

Ultimate responsibility for liquidity and funding risk rests with the Board, which has put in place a monitoring and reporting framework to manage funding requirements.

Liquidity risk is managed by monitoring actual and forecast short and medium-term cash flows and the maturity profile of financial assets and liabilities and by maintaining adequate cash reserves. The nature and timing of the contract cash flows causes the cash balances to vary over the month with the balance usually highest at month end.

The average month end net cash balance during the year was £95.6 million (2013: £50.7 million).

Customers awarding long-term contracting work may, as a condition of the award, require the contractor to provide performance and other bonds. Consequently, the Group is reliant on its ability to secure bank and surety bonds. It has facilities in place to provide these bonds and monitors the usage and regularly updates the forecast usage of these facilities.

At 31 December 2014, the Group had banking and bonding facilities, including a £95.0 million (2013: £95.0 million) Revolving Credit Facility, extending to 30 June 2017. The facilities have financial covenants based on profit, interest cover and leverage measured quarterly.

Unsecured bonding facilities

	Group and Company	
	2014 £m	2013 £m
Expiring between two and five years*	400.0	400.0
* Element of above facilities available for borrowings	2.5	2.5

At 31 December 2014, the utilisation of these bonding facilities amounted to £146.8 million (2013: £157.1 million).

iii) Credit risk

The Group focuses on major blue-chip private sector and large public sector customers. It uses an external credit scoring system to assess a potential customer's credit quality and will enter into a contract only if that assessment is satisfactory. Deposits in the United Kingdom are placed with the bank facility providers or, in joint operations, with banks agreed by the partners. Overseas deposits are placed with major banks operating in those countries. Transactions involving derivative financial instruments are with bank or insurance company counterparties with high credit ratings that are monitored regularly and with whom there are signed netting agreements. Given the high credit ratings of the banks and insurance companies used, management does not expect any counterparty will fail to meet its obligations.

At the year end date, there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amounts of each financial asset, including derivative financial instruments, and the individual constituents of amounts due from customers for contract work in the statement of financial position. Further information on the exposure to credit risk is set out in Note 14.

Notes to the financial statements
continued

17 Financial instruments – Fair values and risk management continued

a) Risk management continued

iv) Interest rate risk
The Group has cash balances in the United Kingdom and overseas and until late 2014 bank borrowings overseas. The largest constituents are United Kingdom balances denominated in pounds sterling. A 1% rise in interest rates would have increased the annual interest income on net cash balances by £1.0 million (2013: £0.5 million).

No interest rate hedging is currently undertaken by the Group.

v) Foreign currency risk
Transactional currency exposures arise from sales or purchases by operating companies in currencies other than their functional currency. The current strategy is to hedge both committed and forecast foreign currency exposures, where applicable, and where the transaction timing and amount can be determined reliably and no natural hedge exists. The Group only enters into forward contracts when a contractual commitment exists in respect of the foreign currency transaction and the Group's policy is to negotiate the terms of the hedge derivative to match the terms of the hedged item to maximise hedge effectiveness.

Investments in joint ventures includes the Group's investment in Alcaidesa Holding SA, a company based in Spain and denominated in euro. At the year end, the net carrying value of the equity investment was £25.2 million (2013: £26.6 million). A 10% strengthening in the euro would have favourably impacted the statement of financial position by £2.8 million (2013: £3.0 million). A 10% strengthening in the euro would have adversely impacted the results by £0.2 million (2013: £1.3 million).

In addition, a 10% strengthening in the UAE dirham would have adversely impacted the results by £0.1 million (2013: £0.2 million). At 31 December 2014, the net monetary assets denominated in currencies other than the functional currency of the operation involved were Euro denominated net monetary assets of £0.2 million (2013: £0.1 million), US dollar denominated net monetary assets of £0.2 million (2013: £Nil) and UAE dirham denominated net monetary assets of £0.6 million (2013: £Nil) in members of the Group with pounds sterling as their functional currency.

b) Cash flow hedges

Forward currency contracts that hedge forecast transactions are classified as cash flow hedges and stated at fair value based on a Level 2 valuation method, using quoted forward exchange rates. The terms of the foreign currency contracts match the terms of the commitments.

At 31 December 2014, the Group had foreign currency contracts (five sale contracts (2013: five), no purchase contracts (2013: seven)) designated as hedges of future transactions and summarised below. The carrying value represents the fair value of the contract; the contractual cash flows represent the pounds sterling commitments. There were no ineffective hedges at the year end (2013: Nil).

Foreign exchange contracts

	2014				2013			
	Carrying amount £m	Contractual cash flows £m	Within one year £m	Between one and 5 years £m	Carrying amount £m	Contractual cash flows £m	Within one year £m	Between one and 5 years £m
Purchases	–	–	–	–	–	(1.8)	(1.8)	–
Sales	–	1.4	0.7	0.7	(0.1)	1.4	–	1.4
	–	1.4	0.7	0.7	(0.1)	(0.4)	(1.8)	1.4

The expected impact on the income statement of the foreign exchange contracts is £Nil in 2015.

c) Financial assets and liabilities

The Group has grouped its financial instruments into 'classes'. Although IFRS 7 does not define 'classes', as a minimum instruments measured at amortised cost should be distinguished from instruments measured at fair value.

17 Financial instruments – Fair values and risk management continued

c) Financial assets and liabilities continued

i) Currency and maturity of financial assets

Financial assets not measured at fair value

	2014				2013			
	Total £m	Within one year £m	Between one and five years £m	After five years £m	Total £m	Within one year £m	Between one and five years £m	After five years £m
Cash and cash equivalents:								
Pounds sterling	147.4	147.4	–	–	83.8	83.8	–	–
Other	1.1	1.1	–	–	0.5	0.5	–	–
	148.5	148.5	–	–	84.3	84.3	–	–
Loans to joint ventures and associates:								
Pounds sterling	1.7	0.1	0.3	1.3	4.8	0.2	0.9	3.7
Trade, other receivables and amounts owed by joint ventures and associates:								
Pounds sterling	143.9	112.1	31.8	–	114.9	92.9	22.0	–
Other	1.0	1.0	–	–	2.2	2.2	–	–
	144.9	113.1	31.8	–	117.1	95.1	22.0	–
Total financial assets not measured at fair value	295.1	261.7	32.1	1.3	206.2	179.6	22.9	3.7

The Group has not disclosed the fair values for short-term trade receivables and amounts due from joint ventures and associates within financial assets, because their carrying amounts are a reasonable approximation of fair values. The fair values of loans carrying interest rates above 10% may be higher than their carrying values of £1.7 million (2013: £4.8 million), but not by a material amount.

Financial assets measured at fair value

The Group does not have any financial assets measured at fair value.

ii) Currency and maturity of financial liabilities

Financial liabilities not measured at fair value

	2014			2013		
	Total £m	Within one year £m	Between one and five years £m	Total £m	Within one year £m	Between one and five years £m
Bank overdrafts – UAE dirham	–	–	–	1.6	1.6	–
Revolving Credit Facility – pounds sterling	–	–	–	25.0	25.0	–
Trade and other payables:						
Pounds sterling	133.0	129.8	3.2	112.1	111.0	1.1
Other	0.2	0.2	–	0.4	0.4	–
	133.2	130.0	3.2	112.5	111.4	1.1
Total financial liabilities not measured at fair value	133.2	130.0	3.2	139.1	138.0	1.1

The Group has not disclosed the fair values for short-term trade and other payables and bank overdrafts within financial liabilities, because their carrying amounts are a reasonable approximation of fair values.

Notes to the financial statements
continued

17 Financial instruments – Fair values and risk management continued

c) Financial assets and liabilities continued

Financial liabilities measured at fair value

	2014			2013		
	Total £m	Within one year £m	Between one and five years £m	Total £m	Within one year £m	Between one and five years £m
Deferred consideration – pounds sterling	6.5	5.2	1.3	6.9	3.7	3.2

The deferred consideration is valued at a Level 3 valuation method. The fair value is the same as the carrying value. See (d) 'Measurement of fair value' below.

iii) Reconciliation of trade and other receivables and trade and other payables to the statement of financial position

	2014		2013	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other receivables (as above)	113.1	31.8	95.1	22.0
Amounts due from customers	71.1	–	80.3	–
Prepayments and accrued income	12.9	–	15.2	–
	197.1	31.8	190.6	22.0

	2014		2013	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other payables (as above)	130.0	3.2	111.4	1.1
Deferred consideration (as above)	5.2	1.3	3.7	3.2
Credit balances on long-term contracts	3.6	–	6.0	–
Accruals and deferred income	157.5	–	145.0	–
	296.3	4.5	266.1	4.3

iv) Effective interest rates of financial assets and liabilities

	2014	2013
Financial assets		
Cash and cash equivalents	0.0% to 0.5%	0.0% to 0.5%
Loans to joint ventures and associates	10.0% to 11.5%	10.0% to 11.5%

Financial liabilities

The Group has overdraft facilities and a Revolving Credit Facility, both undrawn at the year end (2013: £1.6 million and £25.0 million respectively). These are unsecured and carry interest at floating rates at a margin over Base or LIBOR.

The Company's financial assets comprised cash at bank of £10.2 million (2013: £Nil) and trade and other receivables of £58.2 million (2013: £50.3 million) denominated in pounds sterling and maturing within one year.

The Company's financial liabilities comprised trade and other payables of £27.5 million (2013: trade and other payables of £49.3 million and a Revolving Credit Facility of £25.0 million) denominated in pounds sterling and maturing within one year.

17 Financial instruments – Fair values and risk management continued

d) Measurement of fair value

Valuation techniques and significant unobservable inputs
The following tables show the valuation techniques used in measuring Level 3 and Level 2 fair values, as well as the significant unobservable inputs used. There are no financial instruments whose value could be determined under Level 1.

Financial instruments measured at fair value

Type	Valuation technique	Significant unobservable inputs	Inter relationship between significant unobservable inputs and fair value measurement
			The estimated fair value would increase (decrease) if:
Deferred consideration	Discounted cash flows: The valuation models consider the present value of the expected payment, based on forecast EBITDA for 2015 discounted using a risk-adjusted discount rate.	Forecast annual revenue growth rate (2015: 36%)	the annual revenue growth rate were higher (lower)
		Forecast EBITDA margin (2015: 17.5%)	the EBITDA margin were higher (lower); or
		Risk-adjusted discount rates (12.5%)	the risk-adjusted discount rate were lower (higher).
			Generally, a change in the annual revenue growth rate is accompanied by a directionally similar change in EBITDA.
Cash flow hedges	Market comparison technique: The fair values are based on broker quotes. Similar contracts are traded in an active market and quotes reflect the actual transactions in similar instruments.	Not applicable.	Not applicable.

Financial instruments not measured at fair value

Type	Valuation technique	Significant unobservable inputs
Other financial liabilities (as above)	Discounted cash flow.	Not applicable.
Revolving Credit Facility	Discounted cash flow.	Not applicable.

Level 3 fair values
The following table shows a reconciliation from the opening to closing balances for Level 3 fair values:

	Deferred consideration £m
At 1 January 2013	3.9
Assumed within a business combination	3.2
Addition charged to income statement	2.8
Payments	(3.0)
At 31 December 2013	6.9
At 1 January 2014	**6.9**
Addition charged to income statement (including unwind of discount)	**2.9**
Payments	**(3.3)**
At 31 December 2014	**6.5**

There were no transfers out of Level 3 other than the payments made during the year.

Notes to the financial statements
continued

17 Financial instruments – Fair values and risk management continued

d) Measurement of fair value continued

Sensitivity analysis

For the fair value of the £1.3 million non-current deferred consideration, reasonably possible changes at the reporting date to one of the significant unobservable inputs, holding other inputs constant, would have effects to profit or loss as set out in the table below.

	Profit/(Loss)	
	Increase £m	Decrease £m
31 December 2014		
Annual revenue growth rate (2.0% movement)	(0.1)	0.1
EBITDA margin (2.0% movement)	(0.1)	0.1
Risk-adjusted discount rate (4.0% movement)	0.1	(0.1)

The fair value of the current deferred consideration will not change.

18 Trade and other payables

	Group		Company	
	2014 £m	2013 £m	2014 £m	2013 £m
Current liabilities				
Trade payables	101.5	90.5	–	–
Other payables	16.7	10.9	–	–
Social security	5.5	5.3	–	–
Credit balances on long-term contracts	3.6	6.0	–	–
Accruals and deferred income	157.5	145.0	0.4	–
Deferred consideration	5.2	3.7	–	–
Amounts owed to joint ventures and associates	6.3	4.7	–	–
Amounts owed to subsidiary undertakings	–	–	27.5	49.3
	296.3	266.1	27.9	49.3
Non-current liabilities				
Other payables	3.2	1.1	–	–
Deferred consideration	1.3	3.2	–	–
	4.5	4.3	–	–

Accruals and deferred income include subcontract liabilities (not yet payable), subcontract retentions and other accruals and deferred income.

The Directors consider that the carrying amount of trade payables, other payables, social security and amounts owed to joint ventures and associates approximates to their fair value.

Financial risk management policies are in place that seek to ensure that all payables are paid within their credit timeframes.

19 Provisions for other liabilities and charges

Group	Property £m	Other £m	Total £m
Current			
At 1 January 2013	1.0	1.1	2.1
Provided	0.1	0.4	0.5
Utilised	(0.4)	–	(0.4)
Released	(0.1)	(0.3)	(0.4)
At 31 December 2013	0.6	1.2	1.8
At 1 January 2014	**0.6**	**1.2**	**1.8**
Provided	**0.3**	**–**	**0.3**
Utilised	**(0.5)**	**(0.1)**	**(0.6)**
Released	**(0.1)**	**(0.1)**	**(0.2)**
Reclassified from non-current	**–**	**0.2**	**0.2**
At 31 December 2014	**0.3**	**1.2**	**1.5**

Group	Property £m	Other £m	Total £m
Non-current			
At 1 January 2013	0.1	1.8	1.9
Provided	–	0.3	0.3
Transfer	(0.1)	(1.7)	(1.8)
At 31 December 2013	–	0.4	0.4
At 1 January 2014	**–**	**0.4**	**0.4**
Utilised	**–**	**(0.1)**	**(0.1)**
Reclassified to current	**–**	**(0.2)**	**(0.2)**
At 31 December 2014	**–**	**0.1**	**0.1**

Company	Funding obligations £m
Current	
At 1 January 2013	0.2
Utilised	(0.1)
At 31 December 2013	0.1
At 1 January 2014	**0.1**
Utilised	**(0.1)**
At 31 December 2014	**–**
Non-current	
At 1 January 2013	1.3
At 31 December 2013	1.3
At 1 January 2014	**1.3**
At 31 December 2014	**1.3**

Group

Property provisions relate to costs of vacant properties and will be utilised over the next three years.

Other provisions, mainly comprise a provision for staff benefits payable to the staff of an overseas subsidiary, insurance provisions and remedial costs, most of which will be utilised over the next year.

Company

Provisions in the Company relate to funding obligations to a non-trading overseas subsidiary, which eliminates on consolidation.

Notes to the financial statements
continued

20 Employee benefits

(a) Pensions

A defined benefit pension scheme is operated in the United Kingdom and a number of defined contribution pension schemes are in place in the United Kingdom and overseas. Contributions are paid by subsidiary undertakings and employees. The total pension charge in the income statement was £9.2 million comprising £7.8 million included in operating costs plus £1.4 million included in net finance expense (2013: £9.2 million, comprising £7.1 million in operating costs plus £2.1 million in net finance expense).

The Company does not operate a pension scheme.

Defined benefit scheme

The defined benefit scheme was closed to new members on 31 May 2005 and from 1 April 2006 future benefits were calculated on a Career Average Revalued Earnings basis. The scheme was closed to future accrual of benefits to members on 30 September 2009. A full actuarial valuation of the scheme was carried out as at 31 March 2013 and this was updated to 31 December 2014 by a qualified independent actuary.

	2014 £m	2013 £m	2012 £m
Present value of defined benefit obligations	(701.0)	(629.7)	(610.7)
Fair value of scheme assets	659.3	592.5	558.8
Recognised liability for defined benefit obligations	(41.7)	(37.2)	(51.9)

Movements in present value of defined benefit obligations

	2014 £m	2013 £m
At 1 January	629.7	610.7
Interest cost	28.3	26.2
Remeasurements	71.2	21.6
Benefits paid	(28.2)	(28.8)
At 31 December	701.0	629.7

Movements in fair value of scheme assets

	2014 £m	2013 £m
At 1 January	592.5	558.8
Interest income	26.9	24.1
Remeasurements	55.5	30.2
Contributions by employer	12.6	8.2
Benefits paid	(28.2)	(28.8)
At 31 December	659.3	592.5

Contributions by the employer in 2014 included the transfer of two PFI investments, Lewisham Schools for the Future Holdings 3 Limited and Lewisham Schools for the Future Holdings 4 Limited, at an agreed amount of £7.4 million.

Expense recognised in the income statement

	2014 £m	2013 £m
Administrative expenses	(0.8)	(1.1)
Interest cost on the net liabilities of the defined benefit pension scheme	(1.4)	(2.1)
	(2.2)	(3.2)

20 Employee benefits continued

(a) Pensions continued

Fair value of scheme assets

	2014 £m	2013 £m
Equities	146.1	175.6
Multi-credit	66.8	65.7
Government bonds	307.5	212.4
Infrastructure and property	73.6	64.8
Absolute return funds and cash	65.3	74.0
	659.3	592.5

The infrastructure holding includes the portfolio of ten PFI investments transferred by the Group to The Costain Pension Scheme in 2010, 2012 and 2014.

The pension scheme does not have any assets invested in the Group's financial instruments or in property or other assets used by the Group.

Principal actuarial assumptions (expressed as weighted averages)

	2014 %	2013 %	2012 %
Discount rate	3.60	4.60	4.40
Future pension increases	2.85	3.20	2.85
Inflation assumption	2.90	3.30	2.95

Weighted average life expectancy from age 65 as per mortality tables used to determine benefits at 31 December 2014 and 31 December 2013 is:

	2014		2013	
	Male (years)	Female (years)	Male (years)	Female (years)
Currently aged 65	22.1	24.6	22.0	24.5
Non-retirees	23.9	26.5	23.8	26.4

The discount rate, inflation and pension increase and mortality assumptions have a significant effect on the amounts reported. Changes in these assumptions would have the following effects on the defined benefit scheme:

	Pension liability £m	Pension cost £m
Increase discount rate by 0.25%, decreases pension liability and reduces pension cost by	27.5	1.0
Decrease inflation, pension increases by 0.25%, decreases pension liability and reduces pension cost by	24.0	0.9
Increase life expectancy by one year, increases pension liability and increases pension cost by	21.2	0.8

The Group expects to make contributions of approximately £7.0 million, plus an element of dividend matching and the expenses of administration to its defined benefit scheme in the next financial year.

Defined contribution schemes

Several defined contribution pensions are operated. The total expense relating to these plans was £7.0 million (2013: £6.0 million).

Notes to the financial statements
continued

20 Employee benefits continued

(b) Share-based payments

The Company operates a number of share-based payment plans as described below.

Long-Term Incentive Plans (LTIP)
Shareholders approved a new Long-Term Incentive Plan at the 2012 AGM that allows for conditional awards with a maximum face value of up to 100% of base salary with a performance condition based on earnings per share.

Annual Incentive Plan (AIP)
Executive Directors and other senior management are eligible to participate in the Company's Annual Incentive Plan, under which one third of the award is payable in shares. The total AIP award of up to 150% of base salary has performance conditions based on adjusted EBIT (Earnings before interest, tax and other items) (at least 50% of the award) and other measures. The share award element vests on the second anniversary of the date of grant and will be satisfied by shares purchased by a trust on behalf of the Group. It will not lead to any dilution of shareholder interest. Participants must be in employment with the Company and not under notice of termination (either given or received) on the date of vesting.

Deferred Share Bonus Plan (DSBP)
Prior to 2014, Executive Directors and other senior management were eligible to participate in the Company's Deferred Share Bonus Plan which allowed for conditional awards with a face value of up to 50% of base salary with a performance condition based on adjusted EBIT (Earnings before interest, tax and other items). The deferred bonus award vests on the second anniversary of the date of grant and is satisfied by shares purchased by a trust on behalf of the Group, so does not lead to any dilution of shareholder interest. Participants must be in employment with the Company and not under notice of termination (either given or received) on the date of vesting.

Save As You Earn Plans (SAYE)
The Company operates a number of SAYE plans that are open to all employees who pay a fixed amount from salary into a savings account each month and may elect to save over three or five years. At the end of the savings period, employees have six months in which to exercise their options (after which the options expire) using the funds saved. If employees decide not to exercise their options, they may withdraw the funds saved. Exercise of options is subject to continued employment within the Group (except where permitted by the rules of the scheme).

Share-based payment expense
The amounts recognised in the income statement, before income tax, for share-based payment transactions with employees was £2.2 million (2013: £2.7 million); the entire charge relates to subsidiaries.

Options outstanding at the end of the year
The outstanding LTIPs (exercise price £1 per individual grant), AIP (Nil-cost option) and DSBPs (Nil-cost option), which arrange for the grant of shares to Executive Directors and senior management, and the outstanding SAYE schemes are shown below.

	LTIP	DSBP	AIP	SAYE	
	Number (m)	Number (m)	Number (m)	Number (m)	Weighted average exercise price (p)
Outstanding at 1 January 2013	2.2	2.2	–	1.5	199.0
Adjusted during the year	–	(0.2)	–	–	–
Forfeited during the year	–	–	–	(0.1)	186.7
Exercised during the year	(0.6)	(0.9)	–	(0.6)	195.8
Granted during the year	0.7	0.3	–	1.2	222.0
Outstanding at 31 December 2013	2.3	1.4	–	2.0	207.6
Adjusted during the year	0.2	0.2	–	–	–
Forfeited during the year	(0.4)	(0.3)	–	(0.2)	208.8
Exercised during the year	(0.5)	(0.5)	–	(0.2)	203.7
Granted during the year	0.8	–	0.5	1.3	231.9
Outstanding at 31 December 2014	**2.4**	**0.8**	**0.5**	**2.9**	**218.6**
Exercisable at the end of the period	**0.1**	–	–	–	–

Share options outstanding at the end of the year had a weighted average remaining contractual life of 5.8 years (2013: 5.8 years).

20 Employee benefits continued

(b) Share-based payments continued

The fair value of options granted is calculated using the Black-Scholes option pricing model. The aggregate fair value of options granted during the year was £1.4 million (2013: £2.8 million). The assumptions used in valuing the grants were:

	2014	2013
Expected volatility	20%	20%
Expected life (years)	2.7 – 5.0	2.7 – 5.0
Risk-free interest rate	2.1%	3.5%
Expected dividend yield	3.5%	4.0%

The expected volatility is based on the historical share price volatility over a term matching the expected life. The expected life is based on management's best estimate having regard to the effect of non-transferability, exercise restrictions and behavioural considerations.

21 Share capital

	2014		2013	
	Number (millions)	Nominal value £m	Number (millions)	Nominal value £m
Issued share capital				
Shares in issue at beginning of year – ordinary shares of 50p each, fully paid	66.8	33.4	65.5	32.8
Issued in year (see below)	34.4	17.2	1.3	0.6
Shares in issue at end of year – ordinary shares of 50p each, fully paid	101.2	50.6	66.8	33.4

The Company's issued share capital comprised 101,202,693 ordinary shares of 50 pence each as at 31 December 2014.

On 27 February 2014, the Group announced a capital raise of £70.3 million (net of expenses) by way of an issue of 33,382,068 ordinary shares of 50 pence each at 225 pence per share. 11,111,112 shares were to be issued through a firm placing and 22,270,956 through a placing and open offer. The capital raise was completed successfully on 18 March 2014.

The capital raise was effected through a structure, which resulted in a merger reserve arising under Section 612 of the Companies Act 2006. Following the receipt of the cash proceeds through the structure, the excess of the net proceeds over the nominal value of the share capital issued has been transferred to retained earnings.

On 16 April 2014, the Company issued 603,275 shares in respect of the exercise of options granted under the 2011 LTIP.

On 25 April 2014, pursuant to the Scrip Dividend Scheme, shareholders elected to receive 191,503 ordinary shares of 50 pence each in the Company in lieu of cash in respect of all or part of their final dividend for the year ended 31 December 2013, and shareholders elected to receive a further 73,270 ordinary shares on 24 October 2014 in lieu of cash in respect of all or part of their interim dividend for the year ended 31 December 2014.

During the year, the Company issued 159,636 shares on exercise of options granted under the 2008 5-year and 2011 3-year SAYE schemes.

All shares rank pari passu regarding entitlement to capital and dividends.

The share options outstanding at the year end are detailed in Note 20. Details of the performance conditions and the options granted to Executive Directors are given in the Directors' remuneration report.

Notes to the financial statements
continued

22 Contingent liabilities

	Group 2014 £m	Group 2013 £m	Company 2014 £m	Company 2013 £m
Under guarantees of bank overdrafts to subsidiary companies	–	–	–	1.6

Group

There are contingent liabilities in respect of:

- creditors of joint operations, which are less than the book value of their assets;
- performance bonds and other undertakings entered into in the ordinary course of business; and
- legal claims arising in the ordinary course of business.

It is not anticipated that any material liabilities will arise from the contingent liabilities other than those provided for (Note 19).

Company

The Company has guaranteed the obligations of the subsidiary companies that are participating employers of The Costain Pension Scheme, the defined benefit pension scheme in the United Kingdom. At 31 December 2014, the potential liability was £41.7 million (2013: £37.2 million) on an IAS 19 basis and is included in these financial statements as disclosed in Note 20.

23 Other financial commitments

Group

Operating lease commitments

Leases as lessee	2014 Land and buildings £m	2014 Other operating leases £m	2013 Land and buildings £m	2013 Other operating leases £m
Future aggregate minimum lease payments under non-cancellable leases:				
Within one year	4.1	3.4	3.5	3.4
Between one and five years	11.6	4.1	8.9	3.4
Later than five years	7.0	–	7.0	–
	22.7	7.5	19.4	6.8

Leases as lessor	Land and buildings 2014 £m	Land and buildings 2013 £m
Future aggregate minimum lease income under non-cancellable leases:		
Within one year	0.2	0.3
Between one and five years	–	0.3
	0.2	0.6

The Group has various offices under non-cancellable operating lease agreements. The leases have various terms, escalation clauses and renewal rights. The Group also leases vehicles under non-cancellable operating leases. None of the leases include contingent rents.

Company

The Company does not have any other financial commitments (2013: £Nil).

24 Principal subsidiary undertakings, joint ventures, associates and joint operations

	Activity	Percentage of equity held	Country of incorporation
Subsidiary undertakings			
Costain Ltd	Engineering, Construction and Maintenance	100	UK
Costain Abu Dhabi Co WLL	Process Engineering	49	UAE
Costain Building & Civil Engineering Ltd	Engineering and Construction	100	UK
Costain Engineering & Construction Ltd	Holding and Service Company	100	UK
Costain Oil, Gas & Process Ltd	Process Engineering	100	UK
Costain Upstream Ltd	Engineering and Design Services	100	UK
Promanex (Civils & Industrial Services) Ltd	Support Services	100	UK
Promanex (Construction & Maintenance Services) Ltd	Support Services	100	UK
Promanex (Total FM & Environmental Services) Ltd	Support Services	100	UK
Richard Costain Ltd	Service Company	100	UK

	Activity	Issued share capital £m	Percentage of equity held %	Country of incorporation	Reporting date
Joint ventures					
ABC Electrification Ltd	Rail Electrification	–	33.3	UK	31 March
Alcaidesa Holding SA	Land Development	10.6	50	Spain	31 December
Brighton & Hove 4Delivery Ltd	Civil Engineering	–	49	UK	31 March
4Delivery Ltd	Civil Engineering	–	40	UK	31 March
Associates					
Integrated Bradford LEP Ltd	Construction and Operation of Schools	–	40	UK	31 December
Lewisham Schools for the Future LEP Ltd	Construction and Operation of Schools	0.1	40	UK	31 March

The equity capital of the above are held by subsidiary undertakings with the exception of Richard Costain Limited and Costain Engineering & Construction Ltd.

Costain Abu Dhabi Co WLL has been treated as a subsidiary undertaking due to Costain having power to influence and control the composition of the board of directors and the beneficial right to all the net income.

All undertakings operate mainly in the country of incorporation.

All holdings are of ordinary shares except Richard Costain Ltd, where Costain Group PLC holds 100% of the ordinary and preference shares.

Notes to the financial statements
continued

24 Principal subsidiary undertakings, joint ventures, associates and joint operations
continued

A full list of Group companies will be included in the Company's annual return.

	Activity	Percentage of equity held %	Country of incorporation
Major joint operations			
A-one+ Integrated Highway Services – MAC 7	Engineering & Maintenance	33.3	UK
A-one+ Integrated Highway Services – MAC 12	Engineering & Maintenance	33.3	UK
A-one+ Integrated Highway Services – MAC 14	Engineering & Maintenance	33.3	UK
ATC Joint Venture – C610 – Crossrail	Engineering	32.5	UK
Costain-Carillion Joint Venture – M1 Widening and A5/M1 Link	Civil Engineering	50	UK
Costain-Hochtief Joint Venture – Reading station	Civil Engineering	50	UK
Costain-Laing O'Rourke Joint Venture – Bond Street station	Civil Engineering	50	UK
Costain-Laing O'Rourke Joint Venture – Farringdon station	Civil Engineering	50	UK
Costain-Skanska C360 Joint Venture – Eleanor Street – Crossrail	Civil Engineering	50	UK
Costain-Skanska C405 Joint Venture – Paddington – Crossrail	Civil Engineering	50	UK
Costain-Skanska C411 Joint Venture – Bond Street – Crossrail	Civil Engineering	50	UK
Costain-Skanska C412 Joint Venture – Bond Street – Crossrail	Civil Engineering	51	UK
Costain-Veolia-Atkins Joint Venture – Thames Water AMP6	Civil Engineering	44	UK
Costain-Vinci Construction Joint Venture – Shieldhall	Civil Engineering	50	UK
Educo UK Joint Venture – Bradford Schools	Construction	50	UK
Galliford-Costain-Atkins Joint Venture – United Utilities	Civil Engineering	42	UK
Lagan-Ferrovial-Costain – A8	Civil Engineering	45	UK
The e5 Joint Alliance Severn Trent Framework	Civil Engineering	25	UK

25 Acquisitions

There were no acquisitions during the year and there were no changes to the acquisition fair values of EPC Offshore Limited disclosed in the 2013 financial statements.

26 Related party transactions

Group

A related party relationship exists with its major shareholders, subsidiaries, joint ventures and associates, joint operations, The Costain Pension Scheme and with its Directors and executive officers.

Sales of goods and services

	2014			2013		
	Joint ventures and associates £m	Joint operations £m	Total £m	Joint ventures and associates £m	Joint operations £m	Total £m
Services of Group employees	40.4	73.3	113.7	13.8	70.6	84.4
Construction services and materials	0.9	12.9	13.8	11.7	16.6	28.3
	41.3	86.2	127.5	25.5	87.2	112.7

There were no sales of goods and services to major shareholders during the year (2013: £Nil).

An amount due from a major shareholder has been fully provided against since 2006. It relates to work carried out under a subcontract. Discussions among all the parties continue but recovery is uncertain.

Balances with joint ventures and associates are disclosed in Notes 14 and 18. Balances with joint operations are eliminated on consolidation.

Major shareholders
Mohammed Abdulmohsin Al-Kharafi & Sons Co W.L.L. and York Place Limited are regarded as related parties of the Company.

The Costain Pension Scheme
Details of transactions between the Group and The Costain Pension Scheme are included in Note 20 and, in respect of the transfer of two PFI investments in 2014, also Note 4.

Transactions with key management personnel
Disclosures related to the remuneration of key personnel as defined in IAS24 'Related Party Disclosures' are given in Note 6. Key management personnel, as defined under IAS24 'Related Party Disclosures', have been identified as the Board of Directors as the controls operated by the Group ensure that all key decisions are reserved for the Board.

The Directors of the Company and their immediate relatives control 622,165 ordinary shares in Costain Group PLC, which expressed as a percentage of the issued share capital is 0.61% (2013: 0.73%) of the voting shares of the Company.

In addition to their salaries, in respect of the Executive Directors and executive officers, the Group provides non-cash benefits and contributes to defined contribution pension plans. Executive Directors and executive officers also participate in the Group's LTIP, DSBP and SAYE plans, which are detailed in Note 20.

The compensation of key management personnel, including the Directors, is as follows:

	Group	
	2014 £m	2013 £m
Directors' emoluments	2.4	1.6
Executive officers' emoluments	1.7	2.0
Post-employment benefits	0.1	0.3
Share-based payments	1.0	1.1
	5.2	5.0

The above amounts are included in employee benefit expense (Note 5).

Company

The Company has no transactions with related parties other than the charge in relation to share-based payments (Note 20) (2013: none).

Five-year financial summary

	2014 £m	2013 £m	2012 £m	2011 £m	2010 £m
Revenue and profit					
Revenue (Group and share of joint ventures and associates)	**1,122.5**	960.0	934.5	986.3	1,022.5
Less: Share of joint ventures and associates	**(50.7)**	(74.8)	(86.1)	(117.8)	(98.0)
Group revenue	**1,071.8**	885.2	848.4	868.5	924.5
Group operating profit before other items	**28.7**	27.4	21.7	24.1	17.4
Other items:					
Exceptional transaction costs	**–**	(3.7)	–	–	–
Amortisation of acquired intangible assets	**(3.0)**	(1.8)	(1.7)	(0.9)	–
Employment related and other deferred consideration	**(2.2)**	(2.8)	(1.7)	(0.7)	–
Group operating profit	**23.5**	19.1	18.3	22.5	17.4
Profit on sales of investments	**–**	–	–	0.5	–
Profit on sales of interests in joint ventures and associates	**4.0**	9.1	10.5	0.3	11.2
Profit on sale of land and property	**–**	–	–	–	1.3
Share of results of joint ventures and associates	**(1.3)**	(11.3)	(1.4)	(1.3)	(0.5)
Profit from operations	**26.2**	16.9	27.4	22.0	29.4
Finance income	**0.7**	0.7	1.0	34.1	30.7
Finance expense	**(4.3)**	(4.7)	(3.7)	(32.2)	(32.2)
Net finance (expense)/income	**(3.6)**	(4.0)	(2.7)	1.9	(1.5)
Profit before tax	**22.6**	12.9	24.7	23.9	27.9
Income tax	**(1.6)**	(0.4)	(1.6)	(5.2)	(4.8)
Profit for the year attributable to equity holders of the parent	**21.0**	12.5	23.1	18.7	23.1
Earnings per share – basic *	**22.2p**	17.6p	32.9p	27.2p	33.9p
Earnings per share – diluted *	**21.7p**	16.9p	31.8p	26.2p	32.9p
Dividends per ordinary share					
Final	**6.25p**	7.75p	7.25p	6.75p	6.25p
Interim	**3.75p**	3.75p	3.50p	3.25p	3.00p
Summarised consolidated statement of financial position					
Intangible assets	**31.0**	33.0	18.7	20.3	0.1
Property, plant and equipment	**10.0**	7.9	9.1	11.4	9.7
Investments in equity accounted joint ventures and associates	**27.5**	32.1	40.4	42.9	37.4
Other non-current assets	**41.0**	31.8	34.9	33.8	39.8
Total non-current assets	**109.5**	104.8	103.1	108.4	87.0
Current assets	**346.9**	276.5	290.6	332.0	309.3
Total assets	**456.4**	381.3	393.7	440.4	396.3
Current liabilities	**299.3**	296.1	303.1	348.3	311.4
Retirement benefit obligations	**41.7**	37.2	51.9	52.9	39.6
Other non-current liabilities	**4.6**	4.7	6.9	8.4	7.7
Total liabilities	**345.6**	338.0	361.9	409.6	358.7
Equity attributable to equity holders of the parent	**110.8**	43.3	31.8	30.8	37.6

* The earnings per share figures for 2010 to 2013 have been restated for the bonus element in the 2014 capital raise.

Financial calendar and other shareholder information

Financial calendar[1]

Full year results	3 March 2015
Annual Report mailing	20 March 2015
Ex-dividend date for final dividend	16 April 2015
Final dividend record date	17 April 2015
Annual General Meeting	6 May 2015
Final dividend payment date[2]	22 May 2015
Half-year end	30 June 2015
Half-year results 2015	20 August 2015
Ex-dividend date for interim dividend	17 September 2015
Interim dividend record date	18 September 2015
Interim dividend payment date	23 October 2015
Financial year end	31 December 2015

[1] The financial calendar may be updated from time to time throughout the year. Please refer to our website **www.costain.com** for up-to-date details.

[2] Subject to shareholder approval at the Annual General Meeting to be held on 6 May 2015.

Scrip dividend scheme

A scrip dividend scheme will be offered in respect of the final dividend. Those shareholders who have already elected to join the scheme will automatically have their dividend sent to them in this form.

Shareholders wishing to join the scheme for the final dividend (and all future dividends) should return a completed mandate form to the Registrar, Equiniti, by 30 April 2015. Copies of the mandate form and the scrip dividend brochure can be downloaded from the Company's website at **www.costain.com** or obtained from Equiniti by telephoning 0871 384 2268* or +44 (0)121 415 7173 if calling from outside the United Kingdom.

Analysis of shareholders

as at 2 March 2015

	Accounts	Shares	%
Institutions, companies, individuals and nominees:			
Shareholdings 100,000 and more	109	89,152,633	88.09
Shareholdings 50,000-99,999	43	2,939,577	2.90
Shareholdings 25,000-49,999	54	1,831,819	1.81
Shareholdings 5,000-24,999	358	3,511,611	3.47
Shareholdings 1-4,999	9,574	3,772,310	3.73
Totals	10,138	101,207,950	100.00

Secretary

Tracey Wood

Registered Office

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Telephone 01628 842 444
www.costain.com
info@costain.com
Company Number 1393773

Registrar

Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA

Telephone 0871 384 2250* or +44 (0)121 415 7047 if calling from outside the United Kingdom.

* Calls to 0871 numbers cost 8p per minute plus network extras. Lines are open Monday to Friday 08.30am to 05.30pm, excluding UK bank holidays.

Financial calendar and other shareholder information

continued

Dividend mandate

Shareholders can arrange to have their dividends paid directly into their bank or building society account, by completing a bank mandate form. The advantages to using this service are:

- the payment is more secure as you can avoid the risk of cheques getting lost in the post;
- it avoids the hassle of paying in a cheque; and
- there is no risk of lost, stolen or out-of-date cheques.

A mandate form can be obtained from the Company's website, or by contacting Equiniti on 0871 384 2250* (+44 (0) 121 415 7047 if calling from outside the United Kingdom) who will be pleased to assist you and can also be obtained via the shareholder website at **www.shareview.co.uk** (see below for further details). Alternatively, you will find one attached to the tax voucher of your last dividend payment. Overseas shareholders can arrange for their dividends to be paid in their local currency and more information can be obtained from **www.shareview.com/overseas**

Shareview service

The Shareview service from our Registrar, Equiniti, allows shareholders to manage their shareholding online, giving:

- direct access to data held on their behalf on the share register including recent share movements and dividend details; and
- the ability to change their address or dividend payment instructions online.

To sign up for Shareview you need the 'shareholder reference' printed on your proxy form or dividend stationery. There is no charge to register.

When you register with the site, you can register your preferred format (post or email) for shareholder communications. If you select email as your mailing preference, you will be notified of various shareholder communications, such as annual results, by email instead of post.

If you have your dividends paid straight to your bank account, and you have selected email as your mailing preference, you can also collect your tax voucher electronically. Instead of receiving the paper tax voucher, you will be notified by email with details of how to download your electronic version. Visit the website at **www.shareview.co.uk** for more details.

Details of software and equipment requirements are given on the website.

Unsolicited mail

The Company is legally obliged to make its share register available to the general public. Consequently, some shareholders may receive unsolicited mail, including correspondence from unauthorised investment firms. Shareholders who wish to limit the amount of unsolicited mail they receive can contact:

The Mailing Preference Service
Freepost 29
LON20771
London W1E OZT

Further guidance on this issue can also be found on the Company's website at **www.costain.com**

ShareGift

The Orr Macintosh Foundation (ShareGift) operates a charity share donation scheme for shareholders with small parcels of shares whose value makes it uneconomic to sell them. Details of the scheme are available on the ShareGift website at **www.sharegift.org**. Equiniti can provide stock transfer forms on request. Donating shares to charity in this way gives rise neither to a gain nor a loss for Capital Gains Tax purposes. This service is completely free of charge.

* Calls to 0871 numbers cost 8p per minute plus network extras. Lines are open Monday to Friday 08.30am to 05.30pm, excluding UK bank holidays.

Disclaimer

The purpose of this document is to provide information to the members of Costain Group PLC. This document contains certain statements that are forward-looking statements. They appear in a number of places throughout this document and include statements regarding our intentions, beliefs or current expectations and those of our officers, directors and employees concerning, amongst other things, our results of operations, financial condition, liquidity, prospects, growth, strategies and the business we operate. By their nature, these statements 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 document and unless otherwise required by applicable law the Company undertakes no obligation to update or revise these forward-looking statements. Nothing in this document should be construed as a profit forecast. The Company and its directors accept no liability to third parties in respect of this document save as would arise under English law.

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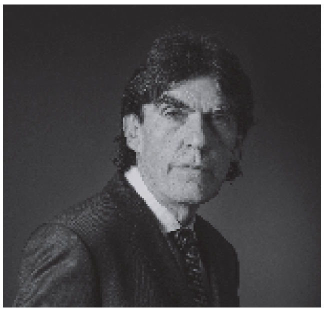

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We welcome your views

Costain is committed to engaging in dialogue with all its stakeholders. We are actively encouraging feedback on our Annual Report and would welcome any views you may have.

Useful links

www.costain.com
www.costain.com/investors
www.costain.com/our-culture
www.costain.com/annual-report-2014
www.costain.com/news

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This report has been printed on Cocoon Silk recycled papers. By using this material rather than non-recycled papers, we have reduced the environmental impact by:

2,116 kg of landfill
284 kg CO_2 and greenhouse gases
2,842 km travel in the average European car
58,675 litres of water
5,407 kWh of energy
3,438 kg of wood

Source: Carbon footprint data evaluated by Labelia Conseil in accordance with the Bilan Carbone® methodology. Calculations are based on a comparison between the recycled paper used versus a virgin fibre paper according to the latest European BREF data (virgin fibre paper) available. Results are obtained according to technical information and subject to modification.

Design and production

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