COSTAIN

Smart thinking, improving lives

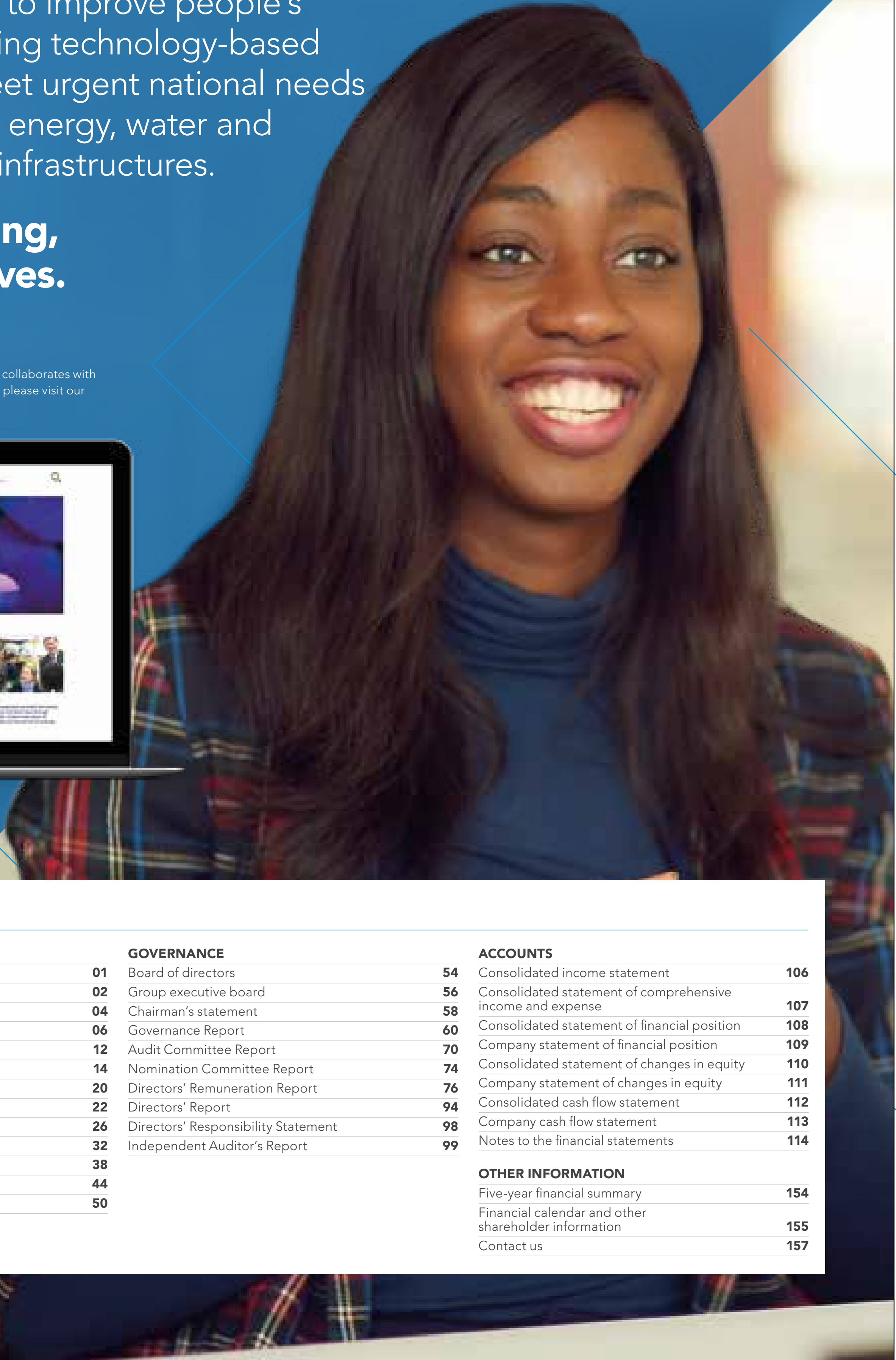
Costain Group PLC
Annual Report 2017

Costain is a smart infrastructure solutions company.

Our purpose is to improve people's lives by deploying technology-based solutions to meet urgent national needs across the UK's energy, water and transportation infrastructures.

Smart thinking, improving lives.

→ To find out more about how Costain collaborates with clients on a wide range of contracts, please visit our website **www.costain.com**



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HIGHLIGHTS

Another strong performance

- revenue, including share of joint ventures and associates, increased to £1,728.9 million (2016: £1,658.0 million)
- underlying[1] operating profit up 18% to £48.7 million (2016: £41.1 million)
- net cash[2] position increased to £177.7 million (2016: £140.2 million). Average month-end net cash[2] for the year increased to £96.7 million (2016: £69.1 million).

Clear purpose and strategy

- proactively aligning the Group with the fast changing market environment and rapidly evolving client requirements in energy, water and transportation infrastructures
- transforming Costain into the UK's leading smart infrastructure solutions company
- providing an integrated offering of technology, consultancy, asset optimisation and delivery services to meet increasingly complex and urgent national needs.

Positive outlook

- maintained forward order book at £3.9 billion, with over £1.1 billion of revenue secured for 2018
- well positioned, through long-term strategic client relationships and an increase to over 1,300 people in consultancy and technology roles, to deliver multi-billion pound programmes
- recommended final dividend of 9.25 pence per share (2016: 8.4 pence), increasing the total dividend for the year by 10% to 14.0 pence per share (2016: 12.7 pence).

FINANCIAL HIGHLIGHTS

REVENUE (including share of joint ventures and associates) £m

£1,728.9m

2017	**1,728.9**
2016	1,658.0
2015	1,316.5

UNDERLYING[1] OPERATING PROFIT £m

£48.7m

2017	**48.7**
2016	41.1
2015	33.2

UNDERLYING[1] PROFIT BEFORE TAX £m

£43.4m

2017	**43.4**
2016	37.5
2015	29.9

NET CASH BALANCE[2] £m

£177.7m

2017	**177.7**
2016	140.2
2015	108.2

UNDERLYING[1] BASIC EARNINGS PER SHARE pence

34.8p

2017	**34.8**
2016	31.5
2015	25.1

TOTAL DIVIDEND PER SHARE pence

14.0p

2017	**14.0**
2016	12.7
2015	11.0

	2017	2016
Revenue		
– including share of JVs and associates	**£1,728.9m**	£1,658.0m
– reported	**£1,684.0m**	£1,573.7m
Operating profit		
– underlying[1]	**£48.7m**	£41.1m
– reported	**£44.3m**	£34.9m
Profit before tax		
– underlying[1]	**£43.4m**	£37.5m
– reported	**£38.9m**	£30.9m
Basic earnings per share		
– underlying[1]	**34.8p**	31.5p
– reported	**31.1p**	25.7p
Net cash balance[2]	**£177.7m**	£140.2m
Dividend per share	**14.0p**	12.7p

1 Before other items; amortisation of acquired intangible assets and employment related and other deferred consideration

2 Net cash balance is cash and cash equivalents less interest-bearing loans and borrowings

Improving people's lives

What we do

We offer a broad range of innovative services across the whole life-cycle of our clients' assets, through the delivery of integrated consultancy, technology, asset optimisation and complex delivery services.

2017 Revenue

Revenue, including the Group's share of joint ventures and associates, for the year increased 4% to £1,728.9 million (2016: £1,658.0 million).

Strong market focus

Our focus is on meeting urgent national needs across three major markets where our work helps to safeguard the security, increase the capacity, improve customer service and drive efficiency in our clients' infrastructure programmes.

- ENERGY
- WATER
- TRANSPORTATION

TOTAL SPEND ACROSS ALL MARKETS

£90.0bn/annum

Read more on pages 22 to 25

Our work in action

Costain has been shaping the world in which we live for over 150 years by continuing to transform. Our people are committed to high performance and safe delivery.

HOW WE HELP TO KEEP THE UK MOVING

See pages 06 to 07

HOW WE HELP TO KEEP THE WATER FLOWING

See pages 08 to 09

HOW WE HELP TO POWER COMMUNITIES

See pages 10 to 11

Our values

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.

Clear set of priorities

By positioning ourselves as the leading smart infrastructure solutions company we will enhance our growth and market position as we continue to drive value for our stakeholders. We will achieve this by focusing on four priorities:

- BROADEN OUR INTEGRATED SERVICE DELIVERY
- ATTRACT AND DEVELOP NEW SKILLS
- ACHIEVE SUSTAINABLE GROWTH IN PROFIT
- WORK RESPONSIBLY AND SAFELY

Read more on pages 26 to 31

Proven track record

We have a proven track record of delivering results for our stakeholders and we continue to create value for our clients, society, our people and shareholders.

ORDER BOOK

£3.9bn

2017	**3.9**
2016	3.9
2015	3.9

Read more on pages 15 and 29

Focused strategy and robust business management system delivering results

Focused strategy and growth opportunities

Successful leadership

Track record of sustainable growth

Focus on blue-chip clients
Our clients' major spending plans are underpinned by regulation, legislation or strategic national needs.

Chosen UK markets that offer significant opportunities for Costain
Energy, water, transportation.

Growing by broadening and integrating our services
We will continue to grow through the delivery of integrated consultancy, asset optimisation, technology and complex delivery services.

Skilled and experienced leadership team
We have a proven management team with a diverse range of skills and experience who ensure the safe and effective delivery of our strategy.

Committed to attracting new skills and capabilities
We are increasing the number of employees in consulting and technology roles.

Investing in the development of our people
We invest significantly in our people to grow skills and capabilities in line with client requirements.

Delivering seven years of sustainable growth
Strong revenue and profit growth due to our client focus and long-term strategic relationships.

UNDERLYING OPERATING PROFIT[1] £m

£48.7m

2017	**48.7**
2016	41.1
2015	33.2
2014	28.7
2013	27.4
2012	24.5
2011	24.1
2010	17.4

REPEAT BUSINESS

90%+

INVESTMENT IN TRAINING

£4.0m

SUSTAINABLE GROWTH

7 years

1 Before other items; amortisation of acquired intangible assets and employment related and other deferred consideration

Strong balance sheet

Technology-led solutions

Responsible business

Strong net cash position
Our strong operational performance and focus on cash control and management has increased our net cash position.

Banking facilities
In addition we have increased our debt facilities to support future growth and extended the term to 2022.

Delivering technology-led solutions
We deliver technology-led solutions to our clients to help meet their needs to increase network capacity, improve customer service and ensure security of supply.

We are transforming Costain into the UK's leading smart infrastructure solutions company.

Robust risk management, governance and ethics
We have the highest standards of risk management, corporate governance and business ethics.

Selective bidding process
Our 'One Costain' philosophy enables us to focus our resources on identifying and securing the most attractive opportunities across the markets in which we operate.

Responsible business practices
Our purpose is to improve people's lives. We embed responsible business practices across the whole of our business, our values and our culture.

NET CASH BALANCE[2]

£177.7m

CONSULTANCY AND TECHNOLOGY

1,300 employees

ACCIDENT FREQUENCY RATE

0.07

2 Net cash balance is cash and cash equivalents less interest-bearing loans and borrowings

Smart thinking, **improving lives**

Transportation

How we help to keep the UK moving

IMPROVING CONNECTIVITY THROUGH TRANSPORT INVESTMENT

To keep up with growing demand and the need for improved connectivity, commitment to transport infrastructure is vital for our economy to thrive. It is positive to see Government pledging to increase transport investment by 50% between 2015 and 2020 as this will ultimately drive growth and productivity across the UK. It is crucial however that this additional support is put towards projects that make a positive impact on people's lives.

Government's efforts to drive forward the use of electric vehicles, for example, is encouraging. Not only will pure electric cars have much lower running costs than diesel vehicles, but they will also produce far lower levels of carbon emissions. London recently welcomed the first electric taxi, which is set to be one of more than 9,000 in service by 2021. Oxford is also paving the way for electric cars, as it strives to be the world's first zero emissions zone. These initiatives, which use the latest technology, will provide long-term benefits for the UK but also those travelling every day.

From Connected and Autonomous Vehicle testing and HGV platooning to 24/7 surveillance of London's transport network, innovative technology is shaping the way people live their daily lives. Travelling across the UK is becoming increasingly more efficient and with each project, hundreds more road users are benefitting from improved journeys.

SAFETY IN NUMBERS

Working as part of a Highways England/DfT project being led by TRL, the global centre of innovation and transport mobility, Costain is working on the first real-world operational trial of platooning vehicles on UK roads. The trial will go beyond demonstrations to showcase the real-world benefits of connected vehicle platoons in tackling fuel efficiency, driver behaviour, traffic flow and safety. Costain will be working across all four phases of the project, which concludes in 2019, and will be supplying advisory services of safety, risk and Strategic Road Network (SRN) analysis.

Platooning involves two or more HGVs connected through wireless 'vehicle-to-vehicle communication' with the lead vehicle controlling the speed, acceleration and braking of the following vehicles. The technology effectively allows them to communicate with each other and operate as a single unit. The pilot will explore whether this autonomous driver technology can improve the fuel efficiency of HGVs to reduce emissions output and increase traffic flow and road capacity. It is also hoped the trial will boost acceptance and understanding by road users ahead of mapping out potential future infrastructure considerations and looking at the commercial case for the adoption of the technology.

www.costain.com/solutions/case-studies

Smart thinking, **improving lives**

Water

How we help to keep the water flowing

THE FUTURE LOOKS RENEWABLE FOR THE WATER MARKET

Climate change, population growth and changes in consumer behaviour are putting increasing pressure on the water sector. With clients going through the latest round of regulatory change, there is an even greater need for innovation to ensure the industry can continue to meet the needs of people, businesses and the environment. Using the latest technology to improve the management of assets is and will continue to be vital; it will allow the industry to continue cutting wastage and preserving an increasingly valuable resource, while protecting consumers from higher water bills. Technology such as 3D modelling, building information modelling (BIM) and virtual reality act as a simulator to practice operations. This allows for processes to be tested and modified more efficiently, thus reducing the cost and time of projects.

INCREASING EFFICIENCY THROUGH 'PLUG AND PLAY' SYSTEMS

Climate change pressures and increased strains on the energy network mean Costain and our clients need to focus on increased efficiency across large energy intensive networks – with the aim of getting the most out of existing systems through increased intelligence and smarter technologies. One way this can be achieved is through Intelligent Asset Optimisation (IAO), which will prepare water companies for the future by addressing efficiency and resilience through data, analytics and in-built responses.

To better secure the supply of water for our clients and the end users, Costain is using IAO at Hopwood Services with Severn Trent Water. Costain developed a standalone system that was installed on site to enhance the monitoring and data collection of the existing pumping station. The standalone 'plug and play' system is installed in between the existing control infrastructure and equipment. This means that no modifications to the existing system were required. Data is transmitted to the Costain cloud, where machine learning and analytics take place. By altering the set points for the pumps, Costain is able to generate additional live data to provide an ongoing self-learning approach.

The result of the enhanced monitoring and control of the pumps has reduced energy consumption by 15%. By reducing energy consumption, more water can be pumped for the same amount of energy, alleviating wear and tear. Pumps last longer and are subject to fewer breakdowns which also reduces the cost of water services over longer periods of sustainable operation.

www.costain.com/solutions/case-studies

Smart thinking, improving lives

Energy

How we help to power communities

RENEWABLE ENERGY OPENING DOORS FOR UK INFRASTRUCTURE

Alternative energy sources and advances in digital technology are creating a more competitive and dynamic energy market by providing consumers access to greater choice. According to Ofgem, renewables produced 26% of all electricity in 2017, with this figure expected to increase as associated technology costs decrease.

Reducing the environmental impact of electricity generation and gas to heat homes and businesses is one of the UK's top energy priorities. This is because the UK is committed to reducing carbon emissions by 80% by 2050, relative to levels in 1990. Ofgem states that since the Climate Change Act 2008, over half the reduction in the UK's greenhouse gas emissions resulted from cleaner electricity. However, there has been limited progress in reducing emissions from heat (gas) and transport.

The transition toward more renewable energy and diversified supplies is creating opportunities and challenges for the flexibility of existing supply infrastructure. We can therefore expect to see increased investment to upgrade and replace ageing infrastructure that will supply energy at a reduced environmental impact. A good example of this is the work we are doing to support National Grid by upgrading their electricity interconnector cables and compressor units at Peterborough and Huntingdon.

MEETING ENVIRONMENTAL LEGISLATION

Driven by the need for National Grid's gas turbine compressors to comply with the European Industrial Emissions Directive, Costain was awarded a contract by National Grid to upgrade its existing compressor stations at Peterborough and Huntingdon, which form part of the National Gas Transmission System. The project was to install two modern and efficient gas-turbine compressors at each site, enabling a more reliable supply of energy for consumers, while at the same time reducing carbon emissions.

New compressors mean more reliable gas supplies, less unforeseen breakdowns and reduced maintenance costs. The result is maintaining safe, reliable and efficient delivery of an energy source used by over 80% of UK households.

Costain began working on the project in January 2014, completing a Front End Engineering Design (FEED) study of each site at the end of 2015. The FEED focused on the technical requirements, as well as the estimated investment for the projects. With Costain undertaking the FEED, we were able to offer National Grid technology solutions which produced cost efficiencies and reduced learning curves, along with an awareness of the design and build requirements for the main works phase.

www.costain.com/solutions/case-studies

Another strong performance driven by ongoing transformation and differentiation

"I am pleased to report that Costain has delivered another strong performance in the year, with continued growth in both revenue and profit."

Dr Paul Golby CBE
Chairman

FINAL DIVIDEND

9.25p per share

BRINGING THE TOTAL FOR THE FULL YEAR TO

14.0p per share

I am pleased to report that Costain has delivered another strong performance in the year, with continued growth in both revenue and profit.

I have previously commented on Costain's position as a great British engineering success story with an outstanding brand and leading market positions. This has been reinforced further during the year by the ongoing strategic transformation of the business to establish a clearly differentiated position as the UK's leading smart infrastructure solutions company.

This transformation keeps Costain relevant to our clients, who are faced with ever greater urgency and complexity in meeting the UK's infrastructure needs, and who require our technology-led offering to help deliver their multi-billion pound programmes and service enhancements.

To maintain our competitive advantage, we are placing greater focus on smart thinking across everything we do, both internally and externally. We are always asking how we can do things better, quicker, faster, safer and more effectively. Above all, how we can add and deliver further value to our clients. A critical element of this will be our relentless pursuit of new skills and capabilities to ensure that we have the brightest people and the broadest range of services to meet our clients' increasingly urgent and complex needs.

Dividend

The Group has a progressive dividend policy, targeting an ongoing dividend cover of around two times underlying earnings, translating strong performance directly into shareholder returns.

Our performance this year, and our confidence in the opportunities for future growth, have resulted in the Board recommending a final dividend of 9.25 pence per share (2016: 8.4 pence) which, if approved, will be paid on 18 May 2018 to shareholders on the register as at the close of business on 13 April 2018. This represents an increase of 10% in the total dividend for the year to 14.0 pence per share (2016: 12.7 pence).

Governance

We measure the Board's effectiveness by holding an externally facilitated evaluation of Board performance every three years and take appropriate action where required.

In 2017, an external evaluation concluded that the Board is well-functioning and effective, and recommended agreed actions to help ensure the speed of transformation and organisational development is maintained. I am pleased that the evaluation also confirmed that we have a Board committed to the highest standards of governance.

Our annual report will set out and explain the processes we have put in place to deliver long-term success while also ensuring that the Company complies with all applicable laws and regulations and meets the requirements of our stakeholders.

Board and people

I was pleased to welcome Jacqueline de Rojas CBE to the Board as a non-executive director with effect from 20 November 2017. Jacqueline is a recognised and highly regarded technology leader in the UK and has brought an additional perspective to our Board as we continue to transform into the UK's leading smart infrastructure solutions company.

As part of our planned Board succession, James Morley will retire as a non-executive director of the Company, and as senior independent director, on 8 May 2018 after the conclusion of the Group's Annual General Meeting (AGM). Jane Lodge has been appointed to act as the Company's senior independent director with effect from the conclusion of the 2018 AGM. I would like to thank James for more than 10 years of dedicated service to Costain, during which time he has made a significant contribution, and wish him well for the future.

The success of any company is down to the quality of its leadership and the depth of talented and skilled people throughout the organisation. On behalf of the Board, I would also like to thank all Costain's people for their commitment, dedication and hard work. The strong result we have achieved this year would not be possible without them.

Corporate citizenship

Driven by our values, Costain takes seriously our wider corporate responsibility and the role the business plays in society. That corporate perspective is also integral to the development of long-term relationships with our blue-chip clients who increasingly place a demonstrable commitment to corporate responsibility high on their selection criteria for preferred suppliers.

Outlook

Our major clients, who are committed to spending billions of pounds to improve people's lives by enhancing the UK's energy, water and transportation infrastructures, are facing increasingly complex and urgent challenges. In response, and to help them meet those challenges better, we are transforming the business into the UK's leading smart infrastructure solutions company.

This transformation is an ongoing process and will ensure that our integrated offering of technology, consultancy, asset optimisation and complex delivery services, keeping Costain relevant to our clients as they deliver their multi-billion pound programmes and service enhancements.

The rapidly changing environment in which we operate presents new and attractive opportunities for Costain and we are well-positioned to take advantage of these. This, along with the good visibility we have over the medium-term, reinforces our confidence for the future and I look forward to reporting on further progress.

Dr Paul Golby CBE
Chairman
1 March 2018

A clear purpose and strategy is transforming Costain into the UK's leading smart infrastructure solutions company

"We are looking to the future with confidence."

Andrew Wyllie CBE
Chief Executive

4,000+ people

Over 1,300 people in consultancy and technology roles, up 300% in three years.

800+

chartered professionals across a wide range of disciplines. 18% of senior managers are female, up from 10% in 2014.

REVENUE (including share of joint ventures and associates) £m

£1,728.9m

2017	**1,728.9**
2016	1,658.0
2015	1,316.5

UNDERLYING[1] PROFIT BEFORE TAX £m

£43.4m

2017	**43.4**
2016	37.5
2015	29.9

1 Before other items; amortisation of acquired intangible assets and employment related and other deferred consideration

I am pleased to report that Costain had another very good year.

We are fulfilling our purpose by improving millions of people's lives across the UK by deploying technology-based engineering solutions to address urgent national infrastructure needs in energy, water and transportation.

We have benefited from proactively aligning the business in a rapidly changing market environment and evolving client requirements, allowing us to differentiate Costain and deliver another strong trading result.

There is a revolution taking place in the use of technology and innovation across infrastructure which is having a profound impact on the market, and creating a wide range of exciting new opportunities for Costain. We are transforming Costain into the UK's leading smart infrastructure solutions company and are looking to the future with confidence.

Another strong trading performance

Results

Our performance reflects the rigorous implementation of the Costain Way business management system that sets out our policies and procedures which are applied consistently across the Group. This also governs our robust approach to assessing opportunities, as well as a continual monitoring of contract and operational performance.

Revenue, including the Group's share of joint ventures and associates, for the year increased 4% to £1,728.9 million (2016: £1,658.0 million).

Group underlying operating profit increased 18% to £48.7 million (2016: £41.1 million). The reported operating profit increased 27% to £44.3 million (2016: £34.9 million). The term 'underlying' throughout this document excludes other items; amortisation of acquired intangible assets and employment related and other deferred consideration.

Underlying profit before tax was £43.4 million (2016: £37.5 million), and underlying basic earnings per share increased to 34.8 pence (2016: 31.5 pence). Reported profit before tax was £38.9 million (2016: £30.9 million) and reported earnings per share were 31.1 pence (2016: 25.7 pence).

Although we have two core operating and reporting divisions within our business (Infrastructure and Natural Resources) we have continued to implement our 'One Costain' philosophy which enables us to constantly focus our resources on identifying and securing the most attractive business opportunities across the markets in which we operate. Further detail on our reporting divisions' performance is set out in the operational review.

Order book

Costain's strong market positions, reputation for innovation and wide range of integrated services enabled us to secure over £2 billion of new contract awards and extensions to existing contracts during the year. As announced in August, we were unable to agree final terms and conditions for the completion of the marine works contract at Hinkley Point C, and therefore £350 million was removed from the order book at that time.

Consequently, the Group's high-quality order book at 31 December 2017 was maintained at £3.9 billion (31 December 2016: £3.9 billion), providing good visibility for the Group's future performance.

The strategic nature of Costain's long-term client relationships has once again ensured that over 90% of the order book comprises repeat business.

As at 31 December 2017, the Group had secured over £1.1 billion of revenue for 2018 (31 December 2016: over £1.2 billion secured for 2017). In addition, the Group has a preferred bidder position of circa £400 million (2016: £500 million).

Cash and banking facilities

Costain finished the year with an increased strong net cash position of £177.7 million (2016: £140.2 million) reflecting very good cash collection towards the end of the period. As previously, some of this increase will reverse during the year ahead. The average month-end net cash during the year also increased to £96.7 million (2016: £69.1 million).

During the year the Group increased total banking debt facilities, in place to support its future growth, from £155.0 million to £191.0 million and extended the term to June 2022.

Investing in smart people to deliver smart solutions

TRAINING & DEVELOPMENT

78,000 hours

ORDER BOOK £bn

£3.9bn

MONEY RAISED FOR CHARITABLE CAUSES

£200,000

A dynamic and rapidly changing market environment

Costain is playing a major role in meeting urgent national infrastructure needs, which are being driven by significant demographic, economic and social trends, across the UK's energy, water and transportation sectors.

We must deliver solutions, in highly regulated and legislated environments, that increase network capacity, improve customer service and ensure security of supply. Our solutions must also demonstrate value-for-money and be deliverable within clients' budgets.

In response to some of the challenges of the 21st century - including global warming, the impact of pollution on human health, the need for improved productivity, and the requirement to stimulate regional economic development - there is rapidly-building momentum across both central and local Government to take the bold decisions which will improve both the country and peoples' lives.

Examples of some of the policy decisions taken in 2017 include:

- the proposal by the UK Government for a complete ban on the sale of all new petrol and diesel-engine cars and vans from 2040 and a subsequent pledge by the Scottish Government to ban such vehicles from 2032
- Oxford City Council announced that it plans to start phasing out polluting vehicles including taxis, cars and buses from the city-centre area in only two years' time by 2020, in what officials believe would be the world's first zero-emissions zone
- the announcement of the final route of the second phase of HS2 linking London and Birmingham with Manchester and Leeds, with services running from 2032
- a proposal from The National Infrastructure Commission to develop the arc spanning Cambridge, Milton Keynes and Oxford, an area which attracts and links cutting-edge industries with world-leading academia, which would deliver new integrated transport infrastructure, helping to provide over one million homes and jobs by 2050, including the country's first new towns in 50 years
- the further roll-out of contactless payment across the UK transport infrastructure, following on from Transport for London's announcement that over a billion journeys have now been made by contactless payment methods, to ensure that customers automatically pay the lowest fare
- the commencement of retail competition for non-domestic users in the water market.

This rapidly-changing environment is having a profound impact on all market participants, not least our clients and the demands they, in turn, are placing on Costain. This is creating a wide range of tremendous new opportunities for us as we look to deliver ever more innovative solutions to meet the challenges ahead.

Transforming Costain into the UK's leading smart infrastructure solutions company

As the pace of change continues to build, we are seeing an acceleration in the rate at which new opportunities are being created. The single biggest factor in our continuing success will be our ability further to embrace the revolution taking place in the use and deployment of technology. We have therefore been transforming Costain into the UK's leading smart infrastructure solutions company, embedding technology across everything we do and, while this transformation is ongoing, we are looking to the future with confidence.

This differentiation is making sure that Costain remains an essential choice for the strategic relationships required by our clients on their long-term collaborative multi-billion pound investment programmes. Our offering, comprising integrated technology, consultancy, asset optimisation and complex delivery services, keeps Costain relevant to our clients, and their rapidly changing requirements.

Our clients are required, often by consequence of a regulatory determination or enhanced legislation, to improve significantly the performance, capacity and service provided by the UK's energy, water and transportation infrastructure. Although billions of pounds are being invested, there is also a finite amount of money available, and therefore the heightened infrastructure performance also needs to be achieved through materially improved financial efficiency.

We believe that the only way that these potentially conflicting objectives can be achieved effectively is through the deployment of innovation and the revolution that is taking place in the use of technology is in every aspect of our service delivery. Examples of our recent activity include the Group's involvement in the operational trials of HGV platooning vehicles, the development of testbeds for connected and autonomous vehicles and asset optimisation for a number of water utilities.

Our clients are also developing long-term strategic relationships with suppliers who can mobilise the required range of innovative integrated services. These dynamic market trends are having a profound impact on the competitive environment and are driving supply-side consolidation.

That is why we are continuing to invest in our skills, services and capabilities both organically and by targeted acquisition to embed these across our entire contract portfolio and, consequently, why we are successfully developing and strengthening our long-term strategic supply chain relationships.

Smart people

The success of Costain is built on the strength and experience of our team.

During the year, we increased the number of people in the business working across consultancy and technology roles to 1,300 (2016: 1,200), representing over 30% of the total head count. Additionally, we now have over 800 chartered professionals across a wide range of disciplines, over 250 graduates working towards becoming chartered and over 120 apprentices on a structured development programme undergoing training across the business.

To ensure we continue to generate thought leadership on key issues, we have increased the number of PhD students we are sponsoring to 21. They are undertaking leading-edge research at renowned universities including Cambridge, Imperial College and Edinburgh.

Along with our engineering centre in Manchester, where over 300 of our people are based, we currently have research and development relationships with 15 leading universities and with which we continue to progress a number of patent applications.

Across the Group, there have been over 78,000 hours of training and development in the year, a significant increase year on year following the roll-out of several new e-learning programmes. A number of the members of the senior leadership team have participated in executive education programmes during the year at leading business schools including Stanford and INSEAD.

We continue to enhance our performance and service delivery by improving the diversity within our teams, including an increase to 18% of the number of women now in senior leadership roles.

Smart thinking

To keep differentiating Costain and develop our competitive advantage, we are ensuring that we deploy smart thinking across every aspect of the organisation and the way in which we do business, both internally and externally.

The Costain ethos is always to ask how we can do things better, quicker, faster, safer and more effectively, deploying innovation and technology at every appropriate opportunity.

Just some examples of the result of smart thinking deployed across the seven elements of our business model include:

Unique client focus

- Over 50% of the Group's order book growth derives from contract extensions and enhancements where we have increased our service offering to clients.
- Strong market positions with a range of clients including becoming the largest supplier to Network Rail.

Skills and experience of the team

- Increasing the number of employees in consultancy and technology roles to 1,300, up 300% in the last three years.
- The appointment of Jacqueline de Rojas CBE as a non-executive director. Jacqueline is a leader in the UK technology sector and an experienced non-executive director.

Technology integration capability

- HGV platooning trial: working on the first real-world operational trial of platooning vehicles on UK roads.
- Connected autonomous vehicles: participation in the development of testbeds for connected and autonomous vehicles.

Range of integrated innovative services

- The introduction of Intelligent Asset Optimisation to address efficiency and resilience in the water sector through data, analytics and in-built responses.
- The appointment by the Crown Commercial Service (CCS) to provide consulting services as part of its Management Consultancy Framework.

Financial strength

- A robust balance sheet with an average month end net cash balance of £96.7 million up 40% from last year.
- We have also increased our debt facilities to £191.0 million and extended their term to 2022.

Proven track record

- 90% repeat business.
- On time completion of a significant capacity enhancement at London Bridge station.

Reputation, values and responsibility

- Demonstrating our commitment to change the way we all think and act about mental health in the workplace by signing the Time to Change employer pledge.
- Being named top of our sector in Management Today magazine's annual Britain's Most Admired Companies assessment, improving our ranking to 27 overall, up from 69 in the previous year.

Costain Cares

The management of Safety, Health and Environment is a core value at Costain. The Group's Accident Frequency Rate (AFR) in the year was 0.07, which is our best-ever performance and compares well with our industry peer group.

We also received a total of 18 RoSPA awards in 2017 including one Patron's Award, one President's Award and two Gold Medals.

Notwithstanding this industry leading safety performance, the Group still had a number of serious safety incidents in the year, including high-potential near-miss events, which reinforced the need for continuous learning, vigilance and improvement in our safety performance.

We remain committed to further improvement in our safety performance and are implementing a strategy to reduce by a further 50% the number of incidents in the business by the end of 2018.

www.costain.com/solutions/case-studies/travel

TRANSPORT

Improving the way the UK travels

Costain is helping to create a world-class UK testbed for developing the next generation of connected and autonomous (CAV) vehicles as part of a consortium led by WMG, University of Warwick. The team, funded through a new £25m programme of investment from the Government, will be helping to create a world-leading connected infrastructure and eco-system, positioning the Midlands as a centre for cutting-edge automotive and communication technologies. The testbed will be based on 80 kilometres of urban roads in Coventry and Birmingham and the technology will enable live trials of CAVs in real world scenarios alongside live traffic.

This exciting and ambitious project focusses on deploying a testbed in a challenging public environment, capable of demonstrating and commissioning the safe use of CAV technology and mobility services in an accessible and globally recognisable context. Vehicle manufacturers will use the testbed to trial their CAVs. The testbed will provide valuable data on CAV performance with particular interest in how CAVs interact with existing vehicles and road infrastructure. This information will be used by manufacturers and road authorities to accelerate widescale deployment of CAVs on UK roads. Costain brings technology expertise in surveillance, analytics and vehicle-to-infrastructure communication, which will be used heavily in this testbed.

Smart thinking, improving lives

Our clients place great emphasis on the good citizen credentials of their strategic 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, clients insist that their tier-one providers share their corporate and social responsibility values and failure to do this would mean a failure to pre-qualify for future work.

During the year we have been placing an increased emphasis on the health and wellbeing of the Costain team. Initiatives include recognising and supporting improved mental health, encouraging flexible working and fundamentally re-evaluating traditional working practices.

From April 2017, the Government has introduced gender pay gap reporting for all companies with more than 250 employees. We fully support this legislation as we believe it will help businesses to tackle gender equality in the workplace.

We have conducted an in-depth review into our employee remuneration and are confident that men and women are paid equally for doing equivalent roles across our business. Our gender pay gap however is 23.8% as a result of having fewer women in senior leadership positions. We are working hard to address this and are confident that as we make progress in our gender balance, our gender pay gap will decrease. For more information please download our report from our website www.costain.com.

The Costain Charitable Foundation is the focus of the range of charitable and community work we undertake, both individually and as a Group. I am pleased to report that we raised over £200,000 for charitable causes in 2017.

Outlook

Costain delivered a strong performance in a dynamic and rapidly changing market environment. Our clients are facing increasingly complex challenges and we have transformed our business to ensure that we remain relevant to them in meeting those challenges.

We have an exciting opportunity ahead to grow our business. To realise it, we will continue to invest in our people and innovative technologies to ensure that we maintain our offering comprising integrated technology, consultancy, asset optimisation and complex delivery services.

The current year has started well and we continue to look forward to the future with confidence.

Andrew Wyllie CBE
Chief Executive
1 March 2018

www.costain.com/solutions/case-studies/equality

PEOPLE

Equality, diversity and inclusion

We believe that greater diversity will make us a better business, a more creative, innovative, agile and efficient organisation. It is our goal to have a workforce that is representative of society and to achieve this, we are committed to meeting the FTSE 350 target of at least 33% of our senior management positions being filled by women by 2020. We are also committed to the FTSE 250 target to have at least one BAME (Black, Asian or Minority Ethnic) board director by 2024.

We launched our latest Equality, Diversity and Inclusion (EDI) strategy in March 2017, and have implemented a number of initiatives that we believe will help us meet our goal. Our focus has been on line manager training, removing barriers to flexible working and ensuring our policies are inclusive.

Over 1,000 line managers have completed unconscious bias training since its launch in 2016. We have also made this training available to our supply chain partners.

We have made a significant investment in new IT systems and software, which is supporting employees to work flexibly; currently 9.8% of our employees are on a formal flexible working arrangement. We estimate that approximately an additional 30% of employees work flexibly through informal arrangements.

Following employee feedback, we launched an update to our planned absence process to allow employees who wish to observe holy holidays the flexibility to work on bank holidays and take this time owed to mark their own holy festivals, eliminating the need to take annual leave. For example, this means that an employee might choose to work on Good Friday and swap the leave entitlement for a different holy festival such as Eid or Diwali.

We are pleased to be seeing progress towards our goal and an encouraging indicator is that our senior female population has grown from 10% to 18% over the last three years.

Smart thinking, improving lives

Creating value for our stakeholders

Our purpose at Costain is to improve people's lives by deploying technology-based solutions to meet urgent national needs across the UK's energy, water and transportation infrastructures.

OUR KEY INPUTS:
Sources of competitive advantage

OUTSTANDING REPUTATION
We are recognised in the industry for our outstanding delivery, technical excellence, health, safety and sustainability performance.

SKILLED AND EXPERIENCED TEAM
The skills, productivity and expertise of our people, along with investment in research and development, enable us to deliver optimal solutions for our clients.

SMART TECHNOLOGY
Investment in research, innovation and technology is crucial to deliver value in the services we provide to meet the needs of our clients.

STRATEGIC PARTNERSHIPS
We are a trusted delivery partner that collaborates strategically at all levels with our clients. We develop strategic relationships with all our stakeholders to support the development of broader services and technology solutions for our clients.

FINANCIAL STRENGTH
The financial resources (through shareholder capital, retained profits and cash generation) we need to run our business.

WHAT WE DO:
How we create value

OUR INTEGRATED, SMART INFRASTRUCTURE SOLUTIONS
We are 100% focused on UK blue-chip infrastructure clients, specialising in projects requiring technology-based integrated services across the asset lifecycle.

CONSULTANCY
Concept, design and programme management consultancy

COMPLEX DELIVERY
Construction and implementation of technology led service solutions

ASSET OPTIMISATION
Maintenance support and upgrading, and advice on asset portfolio investments

TECHNOLOGY INTEGRATION

OUR MARKETS
We focus on markets where there is committed spend, underpinned through legislation, regulation or essential national need.

ENERGY

WATER

TRANSPORTATION

OUR AMBITION
By positioning ourselves as the UK's leading smart infrastructure solutions company we will enhance our growth and market position as we continue to drive value for our stakeholders.

OUR STRATEGY:
How we maximise value

- BROADEN OUR INTEGRATED SERVICE DELIVERY
- ATTRACT AND DEVELOP NEW SKILLS
- ACHIEVE SUSTAINABLE GROWTH IN PROFIT
- WORK RESPONSIBLY AND SAFELY

OUR OUTPUTS:
The value we create

SHAREHOLDERS
We deliver sustainable, profitable growth and attractive returns for our shareholders. We continue to invest in the Group to support our strategy for growth.

9.25p final dividend

14.0p total dividend for the year

SOCIETY
Our projects bring productivity benefits from enhanced infrastructure, and employment opportunities.

135 STEM ambassadors

16,000+ young people engaged in STEM

CLIENTS
Our trusted relationships with our clients enable a better understanding of their needs, allowing us to identify, create and deliver the best solutions.

90%+ repeat business

85% client satisfaction

EMPLOYEES
We provide a safe and rewarding environment for employees and subcontractors.

200+ mental health first aiders

78,000 training days

HOW WE OPERATE

RESPONSIBLE WORKING
Costain Cares is our long-term strategy to build a longer-term sustainable business that creates economic, environmental and social value and delivers tangible benefits for stakeholders.

Find out more on pages 38 to 43

EMBEDDED VALUES
Underpinning everything we do are the Costain values and a culture where all our employees embody our values.

Find out more at costain.com/values

ROBUST CORPORATE GOVERNANCE
We have rigorous policies, procedures and mandatory training to ensure we have a responsible business culture.

Read more on pages 54 to 105

EFFECTIVE RISK MANAGEMENT
Our robust risk management processes identify, manage and mitigate potential risk to the success of the business.

Read more on pages 44 to 49

Smart infrastructure solutions for rapidly changing client requirements

Costain's strategy is focused on meeting the infrastructure needs of our clients in water, energy and transportation. These markets have common requirements, typically set out in legislation or regulation, to improve capacity, increase resilience and enhance customer service. By focusing on the UK market, and a defined set of blue-chip client organisations, we can ensure that our technology-led services can meet their complex needs.

We estimate that our clients will spend around £90 billion per annum, of which approximately £19 billion per annum is on the technology-led services that we deliver. We believe the nature and mix of client expenditure will change, with less spent on the construction of new assets and a greater proportion on the optimisation and enhanced use of existing infrastructure, using technology to provide insight and efficient delivery.

WATER

Market dynamics

- End of the third year of the current regulatory cycle (AMP6); typically, the peak of activity in the water company frameworks.
- Activity is increasing on preparation for the 2019 price review, which will lead to the next regulatory period beginning in April 2020 (AMP7).
- Increased focus on:
  - outcome-based frameworks, where the success is measured not on what has been built, but on what has been achieved by way of measurable outcomes
  - the total amount being spent by the regulated companies (TOTEX) rather than regarding operating and capital expenditures as discrete areas
  - asset resilience, and making sure that water and wastewater networks work reliably and predictably
  - use of smart water infrastructure, which underpins the efficient delivery of water and wastewater services, using technology-led insight.

Client spend **£10bn**

Addressable **£3bn**

Our opportunity

- Costain is already working with our clients to shape the future of the water industry, and we are well positioned to offer technology-led integrated services that support the need for reliable water and wastewater services in the UK.
- We have short-term opportunities through the efficient delivery of those frameworks where we have a position, as well as in securing discrete non-framework opportunities, where these arise.

→ See case study on page 08 to 09

POWER

Market dynamics

- The generation, transmission and customer distribution of electricity and gas in the UK needs a secure and reliable infrastructure to guarantee the supply.
- Growth in renewable electricity sources creates new challenges in matching supply with demand.
- Continued regulatory focus on reducing carbon emissions from power generation and transmission.

Client spend **£16bn**

Addressable **£3bn**

Our opportunity

- Our experience creates opportunities for Costain to support our clients in upgrading and optimising their existing assets to meet these challenges.
- The move to smart cities and the greater use of non-carbon fuels in transport will create challenges for the UK, requiring innovative solutions for energy generation and storage.

→ See case study on page 10 to 11

Addressable market is based on the spend by our clients or potential clients, on the technology-led services we deliver in our chosen markets.

OIL & GAS

Market dynamics
- The oil and gas market continues to be challenged by the low oil price, reflecting over-supply in a market with relatively weak demand.
- Conventional North Sea reserves are diminishing, with new operators entering the market to replace some established companies.
- New sources of gas supply are being identified and the process for extraction safely and reliably is being explored.
- The potential of hydrogen as an alternative fuel is being developed in earnest.

Client spend **£23bn** Addressable **£2bn**

Our opportunity
- Costain offers technology-led design and advisory services to on and off-shore clients, focussed on efficient and reliable delivery of oil and gas to the UK.
- Advisory services supporting the prioritisation of activities for our UK-based clients.
- Our capabilities are ideally suited to supporting clients that are developing hydrogen and non-conventional gas solutions to meet the UK's energy needs in the future.

NUCLEAR

Market dynamics
- New sources of nuclear power continue to be a critical part of meeting the UK's energy needs, and progress on new facilities is being made.
- Safely decommissioning existing power plants continues to require significant investment.

Client spend **£14bn** Addressable **£2bn**

Our opportunity
- Our clients require technology-led, innovative solutions to meet the complex challenges of building new and retiring old nuclear assets.
- Our experience with Magnox and Sellafield demonstrate our ability to meet the needs of this demanding market.

HIGHWAYS

Market dynamics
- Highways England are in the third year of their current regulatory period (Road Investment Strategy) and the focus for them remains on delivering the agreed targets.
- The next Road Investment Strategy (RIS2) is being developed ahead of the next regulatory period in 2020, and this will include revised funding methods for Highways England.
- Improving the road connections away from the trunk network is important to the overall traffic infrastructure of the UK.
- There is a move towards autonomous vehicles, and connecting public transport more effectively with the roads infrastructure.

Client spend **£11bn** Addressable **£5bn**

Our opportunity
- Our integrated, technology-led service offering has demonstrably supported Highways England in meeting their targets, and those same services have also been recognised as being useful to the Welsh Government, Transport for London and East Sussex County Council.
- Connected and autonomous vehicles are already being trialled, and Costain's technology and advisory skills are supporting the UK's leading companies in this field. We see significant growth in this market, as the UK accelerates to a modern, efficient highways model.

→ See case study on page 06 to 07

RAIL

Market dynamics
- Rail remains an integral part of the infrastructure development in the UK.
- In addition to the delivery of new rail systems such as HS2 and Crossrail, significant upgrades are required to meet customer demand for improved services across the network.
- Increased use of technology will allow greater capacity and service reliability to the benefit of our rail clients and their customers.
- The management structure of the rail network is under review, although the requirement for significant investment is unchanged.

Client spend **£16bn** Addressable **£5bn**

Our opportunity
- We have secured several HS2 contracts covering consultancy, enabling works and delivery with further opportunities being considered.
- We provide advisory support on many developing rail activities, and we see our expertise in this area as an opportunity to broaden our market positioning.
- Being able to demonstrate our skills and track record to a broader client base should open further opportunities to us.

Addressable market is based on the spend by our clients or potential clients, on the technology-led services we deliver in our chosen markets.

Enhancing growth and market position while driving shareholder value

Our strategic ambition: By positioning ourselves as the UK's leading smart infrastructure solutions company we will enhance our growth and market position as we continue to drive value for our stakeholders. We will achieve this through four objectives, focusing on our seven strategic priorities. We will:

BROADEN OUR INTEGRATED SERVICE DELIVERY

ATTRACT AND DEVELOP NEW SKILLS

ACHIEVE SUSTAINABLE GROWTH IN PROFIT

WORK RESPONSIBLY AND SAFELY

Focusing on our seven strategic priorities

- a Unique client focus
- b Skills and experience of the team
- c Technology integration capability
- d Range of integrated innovative services
- e Financial strength
- f Proven track record
- g Reputation, values and responsibility

BROADEN

Broaden our integrated service delivery – we will continue to broaden our range of integrated services by increasing the profit being derived from consultancy and technology services, as part of our integrated offering.

c

Technology integration capability

- Ensure all our activities are technology-led.
- Greater allocation of resources to research and development.

d

Range of integrated, innovative services

- A full range of services meeting client needs across the lifecycle of their infrastructure assets.
- Leading advisory and design expertise, established delivery reputation and proven skills in asset optimisation.
- Accelerate the development of new skills and capabilities through research and targeted acquisitions.

Examples of progress in 2017 include:	Performance	2018 focus	Associated risks
• Working on the first real-world operational trial of platooning vehicles on UK roads. • Participation in the Government funded testbeds for connected and autonomous vehicles.	TOTAL VALUE OF COLLABORATIVE RESEARCH GRANTS* £51m 2017 51 2016 46 NUMBER OF COSTAIN SPONSORED PHDS 21 2017 21 2016 13 2015 8	• Expand and enhance our key technology partnerships. • Increase the number of sponsored PhD students working on research and development activities.	• Failure to deliver the business strategy. • Failure to attract and transform the skills, capabilities and competence of our resources. • Failure to ensure that our technology is robust, our systems are secure and our data protected.
• The introduction of Intelligent Asset Optimisation (IAO) to address efficiency and resilience in the water sector through data, analytics and in-built responses. • The appointment by the Crown Commercial Service (CCS) to provide consulting services as part of its Management Consultancy Framework.	NUMBER OF INNOVATIONS 178 2017 178 2016 132 2015 97 RESEARCH GRANTS SECURED 22 2017 22 2016 14	• Appointment of capability leads responsible for the development and utilisation of our Group-wide capability in consultancy, technology and complex delivery. • Continue to grow the delivery of our consultancy and technology service.	• Failure to deliver the business strategy. • Failure to attract and transform the skills, capabilities and competence of our resources.

*The total collaborative research funding we manage in collaboration with our university partners and clients.

DEVELOP

Attract and develop new skills – we will increase the number of our employees acting in consultancy or technology advisory services.

b

Skills and experience of our team

- Identify and recruit the different mix of skills sets required to deliver our strategy.
- Develop our teams through internal and external programmes designed to support the future activities of the Group.
- Continue to drive our equality, diversity and inclusion strategy through our agreed action plan.
- Enhance and add to our capabilities through targeted acquisitions.

Examples of progress in 2017 include:	Performance	2018 focus	Associated risks
• Increasing the number of employees in consultancy and technology roles to 1,300, up 300% in the last three years. • The appointment of Jacqueline de Rojas CBE as a non-executive director. Jacqueline is a leader in the UK technology sector and an experienced non-executive director.	**HEADCOUNT** **4,008** 2017: 4,008 2016: 4,180 2015: 4,115 **EMPLOYEE TURNOVER %** **10.4%** 2017: 10.4 2016: 9.4 2015: 10.1 **INVESTMENT IN LEARNING & DEVELOPMENT £m** **£4.0m** 2017: 4.0 2016: 4.0 2015: 3.9 **EQUALITY, DIVERSITY AND INCLUSION** Employees **3,112** male **896** female **4,008** total 2017: 4,008 total; 3,112; 896 2016: 4,180 total; 3,291; 889 2015: 4,115 total; 3,291; 824 Board Members **5** male **3** female **8** total 2017: 8 total; 5; 3 2016: 8 total; 6; 2 2015: 8 total; 6; 2 Senior management **41** male **9** female **50** total 2017: 50 total; 41; 9 2016: 53 total; 45; 8 2015: 43 total; 38; 5	• Increase the number of employees in consultancy and technology roles via upskilling existing employees and hiring new recruits with consultancy and technology skills. • Launch our executive development programme to accelerate board succession pipeline.	• Failure to deliver the business strategy. • Failure to attract and transform the skills, capabilities and competence of our resources.

GROW

Sustainable growth in profit – our ambition is to achieve sustainable growth, organically and through targeted acquisition, in reported earnings.

a

Unique client focus

- Clear focus on blue-chip clients based in the UK, with over 90% repeat business.
- Client-centric business model delivering integrated services.

e

Financial strength

- Track record of profitable growth.
- Strong balance sheet.
- Disciplined cost control throughout the business.

f

Proven track record

- Continuing to provide the highest standards of client service.
- Focused on meeting clients' complex and evolving needs.

Examples of progress in 2017 include:	Performance	2018 focus	Associated risks
• Over 50% of the Group's order book growth derives from contract extensions and enhancements where we have increased our service offering to clients. • Becoming the largest supplier to Network Rail.	**ORDER BOOK £bn** **£3.9bn** 2017: 3.9 2016: 3.9 2015: 3.9	• Continue to enhance strategic relationships with clients. • Accelerate the development of client-led technology solutions.	• Failure to deliver the business strategy. • Failure to respond to changes in client circumstances resulting from different market, regulatory or political conditions.
• A robust balance sheet with a net cash position of £177.7 million, up 27% from last year. • We have also increased our debt facilities to £191.0 million and extended the term to 2022.	**UNDERLYING OPERATING PROFIT[1] £m** **£48.7m** 2017: 48.7 2016: 41.1 2015: 33.2 **NET CASH BALANCE[2] £m** **£177.7m** 2017: 177.7 2016: 140.2 2015: 108.2 **REVENUE (INCLUDING SHARE OF JOINT VENTURES AND ASSOCIATES) £m** **£1,728.9m** 2017: 1,728.9 2016: 1,658.0 2015: 1,316.5	• Maintain focus on good cash management. • Continue with disciplined risk management and with cash conversion in excess of 80%.	• Failure to deliver the business strategy. • Failure to maintain a strong balance sheet may limit our ability to grow. • Failure to identify and secure new work. • Failure to deliver projects effectively. • Failure to manage the legacy defined benefit pension scheme so that the liabilities are within a range appropriate to its capital base.
• 90% repeat business. • On time completion of a significant capacity enhancement at London Bridge station.	**CLIENT SATISFACTION %** **85%** 2017: 85 2016: 85 2015: 82 **REPEAT BUSINESS %** **90%+** 2017: 90+ 2016: 90+ 2015: 90+	• Maintain our win rate of better than one in three. • Enhance our customer service by continuing to deliver safely, on time and to budget.	• Failure to deliver the business strategy. • Failure to identify and secure new work. • Failure to deliver projects effectively. • Failure to ensure that our technology is robust, our systems are secure and our data protected.

1 Before other items; amortisation of acquired intangible assets and employment related and other deferred consideration
2 Net cash balance is cash and cash equivalents less interest-bearing loans and borrowings

RESPONSIBLE

Work responsibly and safely – building a long-term sustainable business that creates economic, environmental and social value for our stakeholders.

g

Reputation, values and responsibility

- Ensuring Costain is a safe and great place to work.
- Creating a better environment.
- Supporting local communities, providing a positive and lasting legacy.
- Providing sustainable solutions and services.

Examples of progress in 2017 include:	Performance	2018 focus	Associated risks
• Demonstrating our commitment to change the way we all think and act about mental health in the workplace by signing the Time to Change employer pledge.	**ACCIDENT FREQUENCY RATE (AFR)** 0.07 2017 0.07 2016 0.09 2015 0.08 **CO_2 EQUIVALENT EMISSIONS (tCO_2e)** 18,579 Total emissions 2017 18,579 2016 18,523 2015 25,094 17,001 Scope 1 2017 17,001 2016 15,255 2015 19,488 1,578 Scope 2 2017 1,578 2016 3,267 2015 5,606 10.7 Emissions intensity (tCO_2e/£m) 2017 10.70 2016 11.19 2015 19.06 **NON OPERATIONAL CARBON (tCO_2e/£m)** 3.2 2017 3.2 2016 4.3 2015 5.05	• Halve both the number of people injured at work, the incidence of work related ill health and the number of environmental incidents by the end of 2018.	• Failure to prevent a major accident or incident for which Costain is held primarily accountable. • Failure to deliver the business strategy. • Failure to ensure that our technology is robust, our systems are secure and our data protected.

CO2 equivalent emissions

Scope 1 – Carbon emissions include those resulting from the combustion of fuel and operation of facilities and owned assets such as company vehicle fleet (global operations and assets).

Scope 2 – Carbon emissions resulting from the purchase of electricity, heat, steam and cooling for own use (global operations).

Non operational carbon

Scope:
Business mileage from Costain company car fleet and grey fleet (car allowance, car hire, travel allowance).

Carbon emissions resulting from the purchase of electricity and gas for our permanent offices only.

Methodology – All data is independently verified and accreditation to the recognised standard Certificated Emission Measurement and Reduction Scheme (CEMARS) awarded by Achilles.

Examples of progress in 2017 include:	Performance	2018 focus	Associated risks
• Being named top of our sector in Britain's Most Admired Companies (Management Today), improving our ranking to 27 overall, up from 69 the previous year.	**CONSIDERATE CONSTRUCTORS SCORE** 43.8 out of 50 average score 2017 43.8 2016 42.7 2015 41.3 **SUPPLY CHAIN PERFORMANCE %** 71% 2017 71 2016 68 2015 68	• Increase the diversity of our workforce.	

PEOPLE

Wellbeing

Wellbeing is about creating and maintaining the right culture where our employees can be happy, healthy and fulfil their potential. In turn, absenteeism will reduce, morale will increase and our general working environment will feel like a great place to work where healthy lifestyle choices are available for all. This is key to helping us to attract and retain the very best talent by ensuring Costain is a great place to work.

We believe in giving our employees the tools to promote, maintain and maximise their wellbeing to support them in being the best they can be. In 2018, we will launch our new Wellbeing strategy which will help us build on the strong progress made in 2017.

We are proud that there are over 200 trained mental health first aiders within our business, providing support to every contract and office. In addition to this, over 300 of our line managers have completed mental health awareness training, building understanding of mental health and ensuring our managers are equipped to support their teams.

3,500 employees have completed a medical in the past two years as part of our commitment that every employee completes at least biennial medicals.

We were also delighted to open up our employee assistance programme to the supply chain, providing help to anyone experiencing worry, stress or anxiety caused by health, family, work, legal or other issues. The service offers confidential advice via a free 24/7 helpline and provides additional emotional support through telephone or face-to-face counselling sessions.

Smart thinking, improving lives

→ For more detailed information about our sustainability performance please visit our website: costain.com/sustainability

Client-aligned divisions that deliver technology based solutions.

Our client-aligned Infrastructure and Natural Resources divisions have continued to deliver technology-based solutions to meet urgent national needs across the UK's energy, water and transportation infrastructures.

Operational review

Under our 'One Costain' operating model the Group has two core operating and reporting divisions within the business: Infrastructure and Natural Resources.

Infrastructure

The division, which operates in the highways, rail and nuclear markets, delivered another solid performance in the year. The full year revenue (including share of joint ventures and associates) increased to £1,379.7 million (2016: £1,276.1 million and underlying operating profit was £52.2 million (2016: £56.6 million). The margin in the year was 3.8% (2016: 4.4%), which is just below our 4%–5% target range, reflecting a high level of bid costs and the timing of returns on contracts. We expect the division's margin to return to the target range in 2018.

The forward order book for the division has increased to £3.0 billion (2016: £2.9 billion) and the level of tendering activity remains high.

www.costain.com/solutions

Keeping East Sussex connected

As part of a partnership between Costain, CH2M and East Sussex County Council, we maintain more than 2,000 miles of highway in East Sussex – looking after roads, pavements, street lights, grass and winter maintenance. To improve access to these services and enable open communication between the council and the public in East Sussex, an interactive customer service portal has been created. More than 80,000 highway-related cases are reported each year, and so the portal, which connects real-time data with geography for the local authority, provides access to information on programmes of work to allow for them to be monitored and maintained. Using GIS technology, the system is multi-modal accessible, and can be used in various disciplines from environmental, scheme planning and community engagement to data capture and road inspection. Better capture of data and accurate record keeping has played a part in reducing the cost of claims significantly for the client from £1.6 million to £26,000. This technology has led to an 82% reduction in corporate complaints, with compliments shifting from 2:1 to 1:3 and these successes have assisted the team in winning the European Contact Centre of the Year award for 2017.

Smart thinking, improving lives

Highways

Costain is a leading player in the highways market and has again delivered a wide range of strategic highway programmes in the year which have made a considerable contribution increasing network capacity, reducing congestion and improving the movement of people and goods across the UK.

We are providing a range of consultancy services for Highways England including commissions to support the roll out of their Building Information Modelling programme, customer experience enhancement, HGV platooning studies and several strategic impact studies.

During the year we have continued to provide asset management services to Highways England through their Asset Support Contracts on Area 4 (Kent and Sussex) and Area 12 (Yorkshire and Humberside) in addition to our maintenance and response contract for Area 14 (the North East). Our first local authority integrated services contract for East Sussex County Council continues to perform well, achieving efficiency savings and record customer feedback through our digitalised approach and award-winning customer experience centre.

We have successfully completed a number of capital schemes on programme and within budget including the A556 Knutsford to Bowden Link, the A5-M1 Link and the A160/A180 Port of Immingham. We are leading Highway England's largest ever contract, the A14 upgrade, and we continue to provide innovative solutions across the Smart Motorway Programme, currently delivering four schemes on the M1 corridor.

We continue to progress the technically-complex A465 Heads of the Valleys road upgrade for the Welsh Government. We are in a process with our client to resolve the impact from additional scope on the cost and programme, which we anticipate being agreed in line with our estimated outcome on the project.

In addition, for the Welsh Government, we are delivering the refurbishment and technology system fit out on the critical M4 Brynglas Tunnel, the All Wales Technology contract and continue to provide professional services in support of the M4 Corridor around Newport which is currently going through public inquiry.

Rail

Costain has continued to contribute to improving the UK's rail infrastructure providing much needed capacity enhancement at London Bridge Station for Network Rail. Over one million passengers a week now experience the enlarged concourse and benefit from an enhanced service experience.

In Scotland's central belt, the first electrified rail link between Edinburgh and Glasgow has been successfully commissioned allowing new faster passenger trains to meet the growing transport needs in the region. We are pleased to have secured the extension contract that will see the electrification of the Stirling, Dunblane and Alloa route.

Good progress has been made in the year on Crossrail, Europe's largest infrastructure programme, where Costain is playing a leading part in delivering this much-needed boost to London's rail capacity. Track construction is now complete and on our railway systems contract we are focusing on delivering the remaining power and ventilation works to support the planned commissioning of the Elizabeth Line in 2018. Our contracts at Paddington and Bond Street station continue to progress well. Costain is also supporting Network Rail through the Crossrail Anglia contract which connects Crossrail to the existing mainline between Liverpool Street and Shenfield.

On HS2 we have been awarded further contracts including two of the main civil engineering works contracts on the Southern section of this high-speed railway. This includes section one and two main works contracts taking the railway from Euston out to the edge of Greater London. This complements the enabling works contract, previously secured, for the same sections which are also progressing well.

The upgraded Bond Street underground station was opened as planned in time for the Oxford Street Christmas shopping season.

Nuclear

Costain continues to play an important role in nuclear new-build and decommissioning, ensuring security of supply of new nuclear power, a vital component of the UK's commitment to delivering sustainable low carbon energy sources.

We have secured a range of significant consultancy contracts during the year including the major construction and programme management appointment for the development of one of AWE's nuclear facilities. In addition, we have deployed a team of experienced nuclear professionals across EDF's UK reactor fleet to support their project control capabilities.

The final commissioning phase on the complex Evaporator D at Sellafield was completed, and the new facility was handed over to the operations team and is now providing a long-term solution for the reduction in Highly Active Liquor stocks. This facility is a key component in the UK's nuclear waste reduction and decommissioning programme and its successful completion has enhanced Costain's reputation in the market. We continue to support this client through our Decommissioning Delivery Partnership Framework contract across several decommissioning, engineering and construction contracts.

www.costain.com/solutions

INFRASTRUCTURE:

REVENUE (including share of joint ventures and associates) £m

£1,379.7m

ORDER BOOK £bn

£3.0bn

For EDF NNB at Hinkley Point C we concluded our obligations on the Marine Cooling Water contract at the year end. We have also completed the infrastructure works on Junction 23 and 24 of the M5 for this project. We continue to deliver the large temporary aggregate jetty on the site which has been impacted by a number of technical issues and is due to be completed in 2018.

Keeping the lights on: growing the UK's grid capacity

UK electricity demand has peaks and troughs throughout the year and National Grid ensure that there is sufficient supply to meet the country's demands. To ensure flexibility in the supply and demand modelling, and to take advantage of competitive pricing from Europe, sub-sea cables are used to buy and sell electricity from the Continent. Costain were successful in securing work with National Grid in May 2017 to help deliver the Richborough Connection Project in Kent, for a new interconnector with Belgium. Costain people are supporting the National Grid UK construction team through the provision of project controls, consultancy services and technology solutions, including drone survey services.

National Grid's challenges for this project were numerous and Costain helped with two key areas. Firstly, managing the documentation for the project across all stakeholder interfaces and secondly, supporting the construction with the mapping of the route for the pylons to carry the overhead cables to Sandwich from the interconnector in Richborough. We used our consultancy expertise to work with National Grid to develop a bespoke documentation management system. To assist the construction further, we offered an innovative approach to mapping the route by using drones to accurately survey in 3D and video format, to baseline the existing environment. A key benefit being to minimise any landownership challenges during and after construction. Through our unique blend of consultancy and technology solutions, we are helping ensure that the UK's electricity needs are met well into the future.

Smart thinking, improving lives

Natural Resources

The Natural Resources division, which operates in the water, power and oil and gas markets, returned to profitability with an underlying operating profit of £4.8 million (2016: £8.6 million loss). Revenue (including share of joint ventures and associates) was £343.9 million (2016: £377.3 million).

The significant improvement in the performance reflects growth in the water sector and the successful consensual termination of the legacy Greater Manchester Waste PFI contract. However, the margin was impacted by the timing and quantum of returns across a number of contracts and a lower contribution from oil and gas operations, where we have retained skills and capabilities in anticipation of an expected improvement in market conditions. The division is progressing towards a medium term underlying target margin of 4%–5%.

The division has a forward order book of £0.9 billion (2016: £1.0 billion).

Water

The Group is now in year three of the AMP6 five-year programmes for Thames Water, Severn Trent and Southern Water with a focus on improving and maintaining water quality standards, supply resilience and meeting anticipated demographic shifts. These programmes are performing well and are using the full range of integrated capabilities available in the Group to deliver improved customer service, innovative solutions, and achieve significant total whole life expenditure efficiency savings.

Costain is improving water quality and resilience of supply through the delivery of the Shieldhall Tunnel for Scottish Water in Glasgow, reducing flooding issues in the city's wastewater network. This is one of the largest infrastructure investments in Scotland and the main tunnel drive was successfully completed in October and the associated works are progressing well. Commercial discussions continue with the client regarding some programme, scope and cost changes on the contract.

The Thames Tideway project, on which the Group is delivering the east section, is progressing well and will form an integral part of the modernisation of London's Victorian sewerage system and significantly improve water quality in the River Thames, providing capacity to cope with the demands of the city well into the 22nd century.

Bid activity for AMP7 is well underway, with several clients seeking contracts with early engagement from the supply chain to help develop robust business plans ahead of AMP7 formally commencing in 2020.

Power

Ensuring that the UK has a secure and resilient energy mix is another area of national need in which Costain is playing a key role.

The contract for the upgrade of National Grid's Peterborough and Huntingdon compressor stations is progressing well. This programme of work is part of National Grid's Emissions Reduction Project to ensure that both compressor stations comply with the Industrial Emissions Directive and Pollution Prevention and Control regulations. The project will also increase system resilience and reduce overall risk on the National Transmission System by replacing ageing assets with modern, efficient equipment.

www.costain.com/solutions

Drone pilots speed up the delivery of infrastructure

Surveying an area and modelling infrastructure is, by necessity, time-consuming. However, innovative technology is entering the market and enabling businesses, such as Costain, to make the process more efficient. We have begun to deploy drones to assist our teams on site to do exactly this, producing more accurate 3D models, at speed, of how new projects will look and function upon completion. To ensure we can deploy drones at a moment's notice, we have trained our own cadre of inhouse pilots who are able to get to our sites across the country.

These pilots' expertise has been put to good use on a portfolio of different challenges. These include flying drones into sewage tunnels through to mapping the route for the expansion of the A465 in Wales. Using drones not only enables our engineers to develop models more quickly than traditional methods, but it is also much safer as fewer team members need to be put in potentially risky situations.

Our ambition is to train even more drone pilots over the coming years so that they can help us efficiently deliver the infrastructure required to keep the country growing.

Smart thinking, improving lives

NATURAL RESOURCES:

REVENUE (including share of joint ventures and associates) £m

£343.9m

ORDER BOOK £bn

£0.9m

Costain is providing the project services to deliver the replacement of the Humber Estuary Crossing for National Grid. The River Humber pipeline is a strategically important asset, connecting the gas import facility at Easington on the Yorkshire coast and which provides 70–100 million cubic metres of natural gas per day to the national network. Costain also continues to provide asset management services and programme management services for Interconnector Contracts with National Grid.

Oil and Gas

The Hydrochloric Acid Dosing Plant Construction Contract and Condensate Mercury Removal System for Total's Edradour-Glenlivet facility continue to progress to programme with key shut down activities completed to plan.

Costain's programme management services to Ithaca on the Stella field development continue to programme, as well as the ongoing support services to Total and Phillips 66 at their Immingham refineries.

In the period, we have secured new contracts for our gas process technology service offering, together with our first decarbonisation contract, and several strategic development consultancy services.

The ongoing market conditions continue to be uncertain, recognising an increase in new business opportunities during 2017 as clients restructure their operations and investment projects to accommodate prevailing market conditions. However, several clients continue to defer investment decisions for key programmes.

Greater Manchester Waste PFI

We announced in September 2017 that all the conditions to the consensual termination of the legacy Greater Manchester Waste contract were satisfied. In accordance with the terms of the consensual termination, Costain fully demobilised its remaining activities and settled all of its obligations under the contract within the provisions we have previously taken for the project.

Alcaidesa

Costain owns the Alcaidesa group, which incorporates the operating assets of two golf courses, an associated consented parcel of land and the 624-berth marina concession, adjacent to Gibraltar.

Revenue in the year was £5.3 million (2016: £4.6 million). While there has been an improvement in the trading returns from the operations and some early improvement in market conditions in Spain for this non-core activity, the overall result has been impacted by a foreign exchange loss arising from an adjustment to the Group's hedging position. The loss before tax was £1.4 million (2016: £0.7 million loss).

SUSTAINABILITY

Working responsibly

Responsible business underpins our business model and is one of our strategic ambitions. We are committed to building a long-term sustainable business that creates economic and social value for our stakeholders.

Our culture and values influence how we behave, and run through everything that we do, helping us improve people's lives.

In 2016, we launched our 2025 sustainability strategy, the next phase of our Costain Cares journey: our commitment to our stakeholders to focus on the issues they care about.

Sustainability governance and ethics

The Board is responsible and the Executive Board of Costain is accountable for all aspects of corporate responsibility/sustainability, including setting policy, developing the strategy and providing leadership to drive our performance.

We have an established Sustainability Committee, consisting of directors and senior managers with direct responsibilities for key aspects of our sustainability performance. The Committee is responsible for implementing and delivering policy and reports to the Executive Board.

Supporting our sustainability strategy

Every employee, supplier and partner is responsible for working responsibly and sustainably and we have implemented a suite of policies designed to support them in ensuring that we always champion best practices, these include:

- Corporate Responsibility
- Environmental
- Health and wellbeing
- Ethical business conduct
- Modern slavery and human trafficking
- Equality, diversity and inclusion
- Anti-bribery

To support these policies, we have procedures and practices to ensure we truly live our principles. In particular, audit and training programmes ensure that these policies are kept at the front of mind for our employees and partners. This year we trained over 1,000 line managers in unconscious bias, more than 200 of our colleagues have trained as mental health first aiders and over 450 employees have received mental health awareness training.

We continually assess our anti-corruption and anti-bribery processes including having in place appropriate whistleblowing procedures to ensure their continued effectiveness. Compliance with our anti-bribery policy is reviewed on an annual basis by all relevant officers, employees and partners and associated persons within our supply chain.

We are committed to operating responsibly and with high ethical standards, particularly with regard to human rights issues. We will not tolerate human trafficking and other kinds of slavery within our operations, and expect equally high standards from our supply chain.

In the year, we published our modern slavery statement setting out the steps taken to ensure that slavery and human trafficking is not taking place in any part of our business or that of our supply chain. We have continued to expand the provision of training across front line supervisors and high-risk labour suppliers through the Supply Chain Sustainability School, an award-winning industry-wide collaboration designed to ensure the sharing of best practices, as well as Costain's own Supply Chain Academy.

In March 2018, we published our first gender pay report. We conducted an in-depth review into our pay levels and are confident that we have equal pay conditions, however like many other organisations we do have a gender pay gap.

The main reason for our gender pay gap, is that there are fewer women in senior leadership positions. We are already taking action to address the gender balance within Costain and we are confident that as we make progress in our gender balance, our gender pay gap will decrease. We have made encouraging progress, seeing our senior female population growing from 10% to 18% over the last two years, but we recognise that there is more to do.

For more information on any of our policies or statements please visit our website www.costain.com.

Our strategy is based upon our four pillars of responsible business

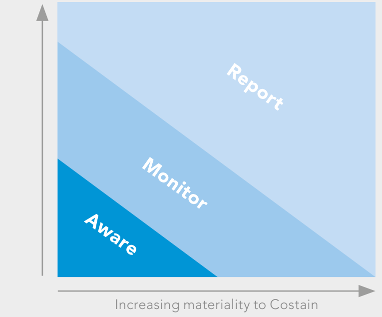
- **Ensuring Costain is a safe and great place to work**
- **Creating a better environment**
- **Supporting our local communities and providing a positive lasting legacy**
- **Providing better solutions for the marketplace**

Materiality and issues overview

To ensure we remain focused on the right issues, we conduct detailed stakeholder research, which includes meeting with clients, suppliers, employees, NGOs, Government and our local communities. The intelligence we gather helps to shape our targets and ensure we place appropriate resources on the important issues we can influence.

Our stakeholders told us that there are over 100 different issues of importance to them, with 25 being materially important to Costain. Seventeen of which form our targets which we are measured against and eight of which we are monitoring closely.

Materially important to Costain



We aim to report only on the issues that are relevant and important to Costain and our stakeholders.

We have categorised the issues that are materially important to Costain under our four pillars of responsible business. For further information about our materiality assessment and our material issues please see our Sustainability Report.

www.costain.com/case-studies/Sustainability

SUSTAINABILITY

London Design and Engineering University Technical College sponsorship

We are proud founding sponsors to the London Design and Engineering University Technical College (LDE UTC), a brand new school which opened in September 2016 with 180 students with a near 50:50 gender split. The school is one of 48 UTC's across the country whose key features are Employer and University leadership supported by the Baker Dearing Trust. The school is non-selective and DfE funded.

Through the school we are contributing to a fundamental shift in the provision of Science, Technology, Engineering and Maths (STEM) education in London moving it into the digital age and addressing at root the lack of Black, Asian & Minority Ethic (BAME) people, along with gender representation in the engineering industry. Through the school we are recruiting diverse apprentices and graduates, equipped with the digital, engineering and project skills that the employer led curriculum will provide.

In addition to financial support we have provided opportunities for our STEM ambassadors to volunteer, developing lesson plans, projects, site visits and work experience. We are very pleased to be sponsoring the Pure Maths A-level, to support the school with a subject which will greatly benefit the students. This is being delivered outside of school hours and despite this, is fully subscribed.

Smart thinking, improving lives

A year in highlights

- **0.07** Lowest ever accident frequency rate
- **1,000+** Employees completed unconscious bias training
- **1st** Our people marched at London Pride festival for the first time
- **Launched** New Equality, Diversity and Inclusion strategy
- **26%** Reduction in non-operational carbon footprint
- **9** Environmental awards received
- **Launched** Our employee Gender Network
- **200+** Colleagues trained as mental health first aiders
- **450+** Employees completed mental health awareness training
- **Signed up** To the 'Ban the box' campaign
- **0.15** Lowest ever environmental incident frequency rate
- **95%** Percentage of all our waste diverted from landfill
- **16,000+** Young people engaged through Science, Technology, Engineering and Maths (STEM) activities
- **5,000 hours** Employees volunteered over 5,000 hours in our local communities
- **Award** Business In The Community Wales' Responsible Large Business of the Year Award, in 2017
- **1,800+** Managers completed modern slavery awareness training
- **46%** The percentage of our total expenditure going to SMEs
- **43.8** Average Considerate Constructors Scheme score, 22% higher than the industry average
- **£200k+** Charitable donations
- **700+** Days of work experience completed
- **140th** The 140th SME graduated from our supply chain academy
- **71%** Highest ever average supply chain performance score

www.costain.com/case-studies/Sustainability

SUSTAINABILITY

Protecting the environment

We are committed to protecting the environment and leaving a legacy of enhanced biodiversity on our contracts. Our A465 Heads of the Valleys contract is an excellent example of how we are meeting this commitment, with the team winning a Green Apple Award for their dedication.

The highways scheme in South Wales is being delivered for the Welsh Government, improving the A465 Heads of the Valleys Road between Gilwern and Brynmawr, upgrading from a single three-lane carriageway to dual two-lane carriageway.

The scheme is located in the Brecon Beacons National Park, passing through the Usk Bat Sites Special Area of Conservation (SAC – the highest order of protected ecological site under European legislation) and Mynydd Llangatwg SSSI, renowned for an extensive karst limestone cave system, part of which passes directly under the road, allowing each passing car overhead to be easily heard!

Two new permanent bat crossings have been installed in addition to pre-existing road subways, which are being transformed into specialised bat roosts. Monitoring data during 2017 found that the new crossings are well used by the bat population, despite the road still being under construction.

The team successfully translocated very rare (100 in existence) Welsh Whitebeam Trees away from the site, to locally acquired land where the trees are being nurtured.

An additional 36 hectares of land located strategically around the gorge was acquired for the planting of several hundred native Beech seedlings, propagated from within a National Nature Reserve. This is assisting the team to protect and conserve the native provenance of the locality. Once planting has finished, over 12,000 trees will have been planted throughout the duration of this contract.

Artificial hibernaculum is being created throughout the length of the scheme, using felled trees to provide habitats for reptiles and small mammals.

Smart thinking, improving lives

Our goals for 2025

Our goals for 2025

As a responsible business we are continually looking to improve our performance and the service we provide our stakeholders. We set ourselves ambitious publicised targets which we are pleased to report our progress against.

The table on page 43 gives a high-level overview of our performance against the 2017 targets, for more detailed information please visit our website to view our Sustainability Report. We are pleased to report that 85% of our targets were fully met. Many of our highlights have already been shared on the previous pages.

2018 priorities

Our journey towards our 2025 goals continues in 2018, proactively developing our stakeholder relationships and continuing to focus on the issues that matter.

We have made big strides in recent years on our employee diversity and will be looking to accelerate our progress by focussing harder on inclusive behaviours to ensure we create the best environment for a workforce that is representative of society.

We will be doing more to measure our social value, reinforcing to our clients and stakeholders that Costain is committed to supporting local communities and small businesses.

Sustainable and ethical procurement remains a priority and we will be maintaining our rigor when it comes to preventing modern slavery and human trafficking occurring within our operations or supply chain. We will be working hard to reach the new ISO 20400 standard for sustainable procurement and publishing our second modern slavery and human trafficking statement.

SUSTAINABILITY

Nanotechnology in infrastructure

Recent advances in nanotechnology can transform the infrastructure sector by bringing resilience and improving the sustainability of structures. Costain has been working with leading universities and our supply chain to develop advanced construction materials. The business case for advanced materials is clear, with almost half of a construction budget spent on infrastructure repair and maintenance rather than building new structures, while at the same time these repairs are usually very ineffective. In the EU, 20% of the repairs are considered to fail in five years, 55% in 10 years and most will fail within 25 years. These repairs have a huge impact, not only on the environment, but also on the local communities affected by the works.

Smart, biomimetic materials that are inspired by natural biological systems can completely change the way our infrastructure behaves. Costain funded a PhD at Cardiff University as part of the Materials for Life (M4L) project, researching and upscaling self-healing concrete. This concrete can heal cracks with a variety of mechanisms, such as releasing healing agents from microcapsules, filling cracks with bacterial action and closing cracks with shape memory polymers, thus significantly reducing the need for frequent repairs and maintenance.

Following the early successes of the M4L programme, Costain has funded a second PhD at the University of Cambridge, looking into the possibility of generating a self-sensing mechanism in concrete products. This research uses nanotechnology and in particular a 'wonder' material called graphene which is the strongest material on earth (200 times stronger than steel) yet the most lightweight material.

The implications of self-healing and self-sensing materials are immense and when fully developed, they will reduce the burden on the environment and the local communities that constant repairs and maintenance of infrastructure imposes.

Ioanna Papanikolaou
PhD in nanomaterials for infrastructure, University of Cambridge

www.costain.com/case-studies/Sustainability

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2017 sustainability target performance

Status: Achieved / Partly Achieved / Unachieved

	Commitment	2017 Target	Status
Costain is a safe and great place to work	Never compromising safety.	Group Accident Frequency Rate (AFR) of 0.07	Achieved
	Always prioritising the health of our people.	100% of projects and permanent offices to achieve bronze level status in the Costain health maturity matrix. With 50% of projects to achieve silver status.	Achieved
		All project and office colleagues to have access to Mental Health First Aiders.	Achieved
	Ensuring all employees are treated and valued equally and we actively promote diversity and inclusion.	A further 250 managers to complete unconscious bias training.	Achieved
	Investing in tomorrow's leaders today.	100% of our senior leaders (Executive Board, divisional senior leadership team, contract leaders) to attend and complete the new Costain SHE leadership development course.	Achieved
	Communicating openly and by engaging with our employees, listening to their views on the Company and the issues that affect them.	Visible company action plan from 2016 engagement survey.	Achieved
Creating a better environment	Enhancing biodiversity.	All relevant projects to achieve an environmental engagement score of green or above by the end of 2017.	Achieved
	Using natural resources efficiently.	All projects to trial the resource efficiency matrix.	Achieved
		5% reduction in non-operational carbon per £1m turnover in 2017, contributing to a 35% reduction by 2020 against the 2013 baseline.	Achieved
	Protecting the environment.	Environmental incident frequency rate of 0.18 or below.	Achieved
Supporting our local communities and providing a positive lasting legacy	Respecting the communities that we serve.	Average Considerate Constructors score of 41.	Achieved
	Investing in the communities where we operate.	30% of Costain employees undertake a volunteering opportunity in 2017.	Partly Achieved
	Inspiring the next generation.	10,000 young people engaged through Costain supported STEM activities.	Achieved
		Roll-out Costain's inspirational work experience programme.	Achieved
	Generating local social value.	Implementation of supply chain mapping tool across all major Costain contracts.	Partly Achieved
	Supporting charity.	Charitable donations equal 0.5% of Costain profit.	Achieved
Providing better solutions for the marketplace	Providing clients with sustainable solutions that enhance their businesses.	Develop and implement a bespoke sustainability themed client engagement survey.	Achieved
	Supply chain collaboration.	Implement action plan to achieve ISO 20400 in 2018.	Achieved
		100% of strategic partners registered with the Supply Chain Sustainability School and achieving silver standard.	Partly Achieved
	Providing a sustainable return for our shareholders.	A sustainable return for our shareholders.	Achieved

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

Risk management processes are incorporated within the Group's normal management and governance systems at all levels.

Risk Management Framework

During 2017, we continued to take steps to evolve and enhance our risk management processes, further embedding into business as usual activity and leading to a better understanding of the principal risks and opportunities we face. Focus has been placed on consistent assessment of risk, ensuring measures are in place to monitor risks and to facilitate informed decision making.

The Group Risk and Assurance team oversee and provide practical guidance on the implementation of risk management across the company. Processes are incorporated into day to day activity and governance systems. This team also leads the process to review and assess risk, focusing on the strategic objectives of the Group which supplements the processes already established at contract level, providing a consistent approach to risk management across the company.

Oversight

The Board has overall responsibility for risk management. During the year, through the delegated authority of the Audit Committee, the Board assessed the effectiveness of the risk management and internal controls systems in place to identify, assess, manage and mitigate the impact of our principal risks.

In 2017, at an operational level, the Executive Board has undertaken a comprehensive review and redraft of the Group risk register considering our three year plan and strategic direction. These risks are regularly reviewed and monitored by the Executive Board. The Audit Committee, on behalf of the Board, have reviewed and approved the appropriateness and relevance of the risk register and will monitor implementation of key actions to reduce the impact of the risks.

Risk appetite

The ongoing evolution and enhancement of our risk management processes in 2017 has also included a revised approach to the evaluation of the Group's willingness to take on risk in order to meet our strategic objectives.

We have simplified and standardised the terms we have used to describe our risk appetite. Please refer to the key on page 46 and 48.

The Costain risk assessment process is closely aligned with the planning process to enable decisions to be made in connection with how much and which risks to take in pursuit of our strategic priorities.

Our approach to risk appetite remains dynamic and any changes to the business environment in which we operate and/or our strategic priorities will require a reassessment of our tolerances which would be led by the Board.

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 the financial statements and in note 18 to the financial statements.

The directors have acknowledged the guidance in respect of going concern published by the Financial Reporting Council. 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. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Risk management and control responsibility framework

BOARD OF DIRECTORS

The Board

Key responsibilities:

- sets strategic objectives and defines the risk appetite
- maintains overall responsibility of the Group's risk management and internal control systems
- considers the variety and extent of risk exposure against the risk appetite for our principal risks
- provides leadership to ensure an effective risk management culture.

Top-down

Oversight, identification, assessment and mitigation at corporate level.

GROUP EXECUTIVE BOARD

Group Executive Board

Responsible for:

- assessing and mitigating risk
- monitoring the implementation of risk management processes and internal controls
- directing resources to effectively implement controls.

AUDIT COMMITTEE

Audit Committee

Responsible for:

- reviewing the effectiveness of risk management and internal control systems
- supporting the Board in monitoring exposure against the risk appetite.

INTERNAL AUDIT

Internal Audit

Responsible for:

- reviewing the effectiveness of risk management and internal control systems in order to support the Audit and Executive Committees.

Bottom-up

Identification, assessment and mitigation at contract and functional level.

OPERATIONAL LEVEL

Operational level

Key responsibilities:

- implements the risk management processes to ensure internal controls are embedded throughout operational management
- identifies, manages and maintains accountability for risk within local areas of responsibilities
- embeds a culture of awareness to develop and enhance the quality of risk management.

Viability statement

In accordance with provision C.2.2 of the 2014 revision of the UK Corporate Governance Code, the Board has assessed the viability of the Group over a three-year period taking into account its current financial position and the principal risks.

The period of three years has been considered appropriate and relevant as the Group has reasonable visibility of secured work and pipeline of opportunities over this period and also aligns with the period reviewed by the Board in the normal business planning process.

The Risk Management Framework described on page 45 outlines the approach the Board has taken to identifying and managing risk. As detailed on pages 46 to 49 the Board has carried out an assessment of the principal risks facing the Group including those that would threaten its business model, future performance, solvency or liquidity.

The assessment of viability has been made taking into account these principal risks and testing a number of plausible, but severe scenarios which are not included in the corporate plan. The scenarios include various combinations of the following:

- A major health and safety incident, leading to a fine and loss of future work.
- Project delivery issues, leading to a downward revision to profit and loss of future work.
- Failure to achieve the speed of transformation of the Group's service offering, leading to lower future profits.
- A major IT data breach, leading to increased operational costs and loss of future work.
- Working capital issues experienced on a number of key contracts or unforeseen increase in pension contributions, leading to a loss of balance sheet strength.
- Reduction in the level of new work secured, leading to lower future profit.
- Loss of key people leading to a reduction in future work.
- Failure of the Group to respond to changing client buying circumstances, leading to a reduction in current and future work.

Based on an assessment of the financial impact of the scenarios on the corporate plan, the Board confirm that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three-year period to 31 December 2020.

Principal Risks

The Board has undertaken a robust assessment of the principal risks facing the Group through the controls and mitigation plans in place to manage these within our risk appetite.

The principal risks and uncertainties facing the Group and its ability to achieve its strategic objectives are set out below.

Overall the Board has assessed that the risk profile of the Group is broadly in line with the 2016 position with some small movements in individual risks. The number of principal risks considered by the Board to be those which would have the greatest impact on the achievement of strategy remains nine.

However, to better recognise and monitor these risks there have been some changes to how they are reported:

- A new risk 'Failure to deliver the business strategy' replaces the previous 'Acquisitions' risk to reflect our broader strategic objectives.
- 'Failure to respond to changes in client circumstances' has been redefined from 'Political, economic and market conditions' to better reflect the nature of the risk in responding to changing buying behaviours because of different market, regulatory or political conditions.

Title	Change in 2017	Appetite	Link to Strategic priority	Strategic assumption	What is the risk?	How we manage it	How we further mitigate it
Failure to prevent a major accident or incident for which Costain is held primarily accountable.	No change to risk	A	g	Costain has an Accident Frequency Rate of 0.07, a record low, and is the result of continuous improvement in our approach to safety, health and environment (SHE).	Costain operates in complex and hazardous environments, which have the potential to result in significant loss including the loss of life, widespread acute ill health or damage to the environment. Failure to manage these risks has the potential to result in personal or environmental harm, or operational loss. Significant SHE events could also have regulatory, legal, financial and reputational impacts with all stakeholders.	SHE policies and procedures. SHE strategy and plans. Costain behavioural safety programme (CBS). SHE monitoring and assurance.	Ongoing evaluation and improvement of assurance processes. Review of performance against SHE targets. Proactive monitoring of SHE standards at site and offices including regular visits by senior leaders. Ongoing roll-out and certification of CBS strategy and behavioural approach.
Failure to deliver the business strategy.	No change to risk	T	a, b, c, d, e, f, g	The delivery of the future strategy involves growth in many business areas. Specifically, transforming our integrated service offering of consultancy, technology, complex delivery and asset optimisation which is fundamental to our future success and incorporates both controllable and uncontrollable risk elements which require monitoring. We must do this with pace to meet our strategic objectives. Organic growth alone may not be sufficient to deliver on the 2020 plan, and therefore we may need to identify suitable acquisition targets.	Failure to manage this risk could result in the transformation and diversification of the business being unsuccessful, new market opportunities may be missed, work in diversified markets may not be won and/or loss of stakeholder confidence.	Technology & Consultancy strategy and implementation plans. Strengthening of our leadership team to deliver in growth areas. A pipeline of acquisition opportunities which are robustly evaluated at Board and Executive level. Rapid integration plans for acquired businesses.	Implementation of Technology and Consultancy operating model and organisation. Allocating additional work winning spend to Technology and Consultancy opportunities. Define and implement annual corporate and internal communication plans. Appointing account directors for all major clients (and potential clients).
Failure to maintain a strong balance sheet may limit our ability to grow.	No change to risk	A	e	Events and activities can have a direct impact on our credit ratings and liquidity which could increase the cost of, and access to, financing. In a changing external environment, we need to respond to macro-economic or political influences. Fraud or other financial loss may impact our ability to meet our financial commitments.	We may fail to win work due to an inability to demonstrate the required level of financial resource. We may not be able to maintain a competitive scale in a consolidating market. We may fail to maintain adequate working capital to operate the business.	Treasury function experienced in the management and oversight of investments. Bank and surety bonding facilities to deliver finance requirements. Strategic collaborations with joint venture partners to help achieve the required financial and operational strength. Robust joint venture partner selection criteria; all partnerships and alliances signed off by the PLC Board. Zero tolerance to fraud or bribery, supported by online training.	We may utilise banking and bonding facilities if required. We continue to maintain robust cash control and forecasting processes.
Failure to identify and secure new work.	No change to risk	T	e, f	Costain's business strategy depends on winning work in both current, changing and diversified markets, to maintain, grow and diversify a profitable future business which delivers stakeholder value. We have secured approximately 73% of our contract profit planned for 2018, broadly in line with the previous year. The risk is that we fail to secure the balance of 27%.	Failure to manage this risk could mean that we do not win work from current clients, new clients/markets and may therefore fail to demonstrate our capabilities to diversify. We may miss our profit targets if we are unable to secure sufficient new work.	Focus on key, blue-chip clients, and understanding their needs. Monitoring our pipeline of opportunities. Bid compliance and governance processes. Centralised allocation of resources to the most advantageous business development activities. Broadening the skills and breadth of our capability organically and by acquisition.	Appointing account directors for all major clients (and potential clients). Developing pursuit plans for every opportunity. Allocating a greater proportion of our work winning expenditure to technology and consultancy opportunities. Delivery of consultancy and technology services via strategic acquisitions. Increased work winning expenditure planned for 2018.
Failure to attract and transform the skills, capabilities and competence of our resources.	No change to risk	T	b, d	The attraction, retention and succession of the right people with the right skills in the right role at the right time, underpins the achievement of the Costain business strategy. The development and motivation of our people and leaders are critical factors in the successful execution of our strategy. In addition, we require the right behaviours from our leaders and employees to deliver our business strategy in accordance with our values. Where appropriate, we seek to supplement our internal skills with those of selected partners, and ensuring that our supply chain have the correct competencies and share our values is important to our delivery.	Failure to manage our skills and capabilities risk may result in an inability to grow the business as anticipated and consequently in a short term, impact on performance.	An attractive and fair remuneration policy. High staff retention rate and engaged workforce. Comprehensive induction process for new staff. A defined people strategy based on culture, equality, wellbeing, training, reward and recognition. Active liaison with employees is achieved through the Costain Ground Force employee committee and engagement surveys. An ongoing process of competency identification and management, and linking this to our resource planning. Careful selection of partners and suppliers, with robust monitoring of their performance against criteria.	Recruitment strategy to hire from a broad range of backgrounds and experience. Develop our team through internal and external programmes designed to support the future activities of the Group. Continue to drive our equality, diversity and inclusivity strategy. Evolve and drive our wellbeing strategy. We will undertake a company-wide engagement survey in 2018.

Change in 2017

- Increased risk
- No change to risk
- Decreased risk

Risk Appetite

- A **Averse** We are cautious in this area, and therefore will stay away from adding high-risk opportunities in to our portfolio.
- N **Neutral** We take a balanced approach to the financial and reputational risk-return trade-offs.
- T **Tolerant** We are open to taking risk within a defined set of parameters to achieve our strategic objectives.

Strategic priorities

- a Unique client focus
- b Skills and experience of the team
- c Technology integration capability
- d Range of innovative services
- e Financial strength
- f Proven track record
- g Reputation, values and responsibility

Title	Change in 2017	Appetite	Link to Strategic priority	Strategic assumption	What is the risk?	How we manage it	How we further mitigate it
Failure to deliver projects effectively.	No change to risk	T	e f	Costain has a strong reputation for project delivery, with 90% repeat orders. We believe we have robust processes, skilled employees and carefully selected supply chain partners to support our continued delivery of projects in line with expectations. Entering new business areas may involve new ways of working, in which we have less expertise.	Failure to maintain discipline in delivering projects could result in: • contract disputes • design faults that result in additional works to rectify • failure of our supply chain to complete the works • refusal of claims by insurers following a loss • compensation events or increase in scope not being fully reimbursed by our clients. Failure to deliver projects in line with the judgements and estimates made.	Work winning Gate process, Executive Investment Panel (EIP) and Board approval of projects. Partner selection aligned to capability criteria. Project controls framework, as part of a robust programme management process. Supply Chain management processes and utilisation of performance bonds where appropriate. Consistence of approach through application of the Costain Way. Regular detailed review meetings at sector, divisional and Group level. Risk-based assurance and audit activities.	Further enhancements to process standardisation though upgrades to the Costain Way. Standardisation of our online timesheet and expense system. Further definition of Joint Venture Board members roles and responsibilities. Implementation of standardised and consistent project performance reviews. Further roll out of in-depth commercial reviews on key projects. Continued review of strategic partners to ensure alignment.
Failure to manage the legacy defined benefit pension scheme so that the liabilities are within a range appropriate to its capital base.	No change to risk	N	e	The pension scheme has a deficit of £23.9m on an accounting basis at 31 December 2017. The defined benefit pension scheme was closed to new members from 1 June 2005 and to future accrual on 30 September 2009.	Failure to manage this exposure adequately could lead to Costain being exposed to significant additional liabilities under the legacy defined benefit pension scheme and hence significantly higher deficit contributions adversely impacting the Group's operational results.	Funding arrangement agreed with Trustees. Regular reviews of funding position are undertaken. Investment performance is monitored and the Company provides input into the scheme's investment strategy. A third-party pensions expert provides independent advice.	Embed regular reviews to identify further opportunities to mitigate long-term risks. Providing input to current investment strategy review being undertaken by Pension Scheme Trustees.

Change in 2017

- Increased risk
- No change to risk
- Decreased risk

Risk Appetite

- **A** **Averse** We are cautious in this area, and therefore will stay away from adding high-risk opportunities in to our portfolio.
- **N** **Neutral** We take a balanced approach to the financial and reputational risk-return trade-offs.
- **T** **Tolerant** We are open to taking risk within a defined set of parameters to achieve our strategic objectives.

Title	Change in 2017	Appetite	Link to Strategic priority	Strategic assumption	What is the risk?	How we manage it	How we further mitigate it
Failure to ensure that our technology is robust, our systems are secure and our data protected.	Increased risk	A	c f g	Costain's strategic requirement to be at the forefront of technology development means that it is critical that our technology is robust, our systems are secure and our data protected. Effectiveness, availability, integrity and security of IT systems and data are essential for Costain's operations. Sensitive data faces the threat of misappropriation from hackers, viruses and other sources, including disaffected employees. The risk has increased in 2017 reflecting the continued rise in cyber threats.	Failure to manage our technology and data risks could result in: • loss of confidential client or personal data • breaches of legislation and subsequent fines • breach of contract • inappropriate release of commercially sensitive data • business systems suffer a cyber attack.	An information security strategy which integrates information systems, personnel and physical aspects in order to prevent, detect and investigate threats and incidents. Engaging with key technology partners and suppliers, to ensure potential vulnerabilities are identified. Annual penetration tests and 24 hour threat monitoring by an external security company. Business continuity systems and procedures, routinely tested and developed, to ensure rapid recovery and data retrieval. Accreditation to ISO 27001:2013 Information Security Management System. Up to date information security procedures, including regular password changes for system access. A major upgrade to our hardware and software in 2017, migrating most of our key systems to the cloud.	Full implementation of a behavioural training course for information security, with further testing of employees' understanding. Development of a data classification model. Successful completion of the GDPR compliance programme. Continued improvement of physical access controls on site. Migration to the cloud for remaining key systems. Attain full Cyber Essentials Plus certification.
Failure to respond to changes in client circumstances resulting from different market, regulatory or political conditions.	No change to risk	T	a	This risk would arise if we failed to recognise or understand clients' and prospects' changing buying behaviours, particularly where we have new clients. Failure to understand and respond to the changing marketplace might result in a loss of market share as existing clients move to competitors and future client needs are not met by our service offering. Clients may implement new contract conditions which might adversely impact our business and financial results.	Failure to adequately understand and respond to our clients' needs may result in a reduction in work won, loss of repeat clients, an inability to win work in diversified markets and/or a reduction in profitability and cash flow.	A track record of strong client relationships in target markets. Executive Board members actively engage in discussions with regulatory authorities. Actively monitoring policy development via industry groups.	Appointing account directors for all major clients (and potential clients). Greater Board engagement with clients. Focus on major clients in key UK markets.

Strategic priorities

- a Unique client focus
- b Skills and experience of the team
- c Technology integration capability
- d Range of innovative services
- e Financial strength
- f Proven track record
- g Reputation, values and responsibility

CHIEF FINANCIAL OFFICER'S REVIEW

Positive outlook with an increase in dividend, reflecting the Board's confidence for the future

"Our performance reflects the effective implementation of the Group's focused strategy."

Anthony Bickerstaff
Chief Financial Officer

£1,728.9m
Revenue (including share of joint ventures and associates)

£48.7m
Underlying[1] operating profit

34.8p
Underlying[1] basic earnings per share

REVENUE (including share of joint ventures and associates) £m

£1,728.9m

2017	**1,728.9**
2016	1,658.0
2015	1,316.5

UNDERLYING[1] OPERATING PROFIT £m

£48.7m

2017	**48.7**
2016	41.1
2015	33.2

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

Overview

In 2017, the Group had another year of strong financial performance with increases in revenue and profit and finished the year with an excellent net cash position. This performance reflects the effective implementation of the Group's focused strategy which has continued to deliver good financial results over several years.

In addition, the Group continues to attract good support from its banking partners and has enhanced and extended its debt facilities during the year.

Revenue, including share of joint ventures and associates, was £1,728.9 million for the year to 31 December 2017 (2016: £1,658.0 million). Reported revenue, excluding share of joint ventures and associates, was £1,684.0 million for the year to 31 December 2017 (2016: £1,573.7 million).

The Group generated an 18% increase in underlying operating profit to £48.7 million (2016: £41.1 million). The increased profit reflects the Group's focus on long-term repeat orders with blue-chip clients.

Profit before tax, before other items, for the year was £43.4 million (2016: £37.5 million). Basic earnings per share, before other items, amounted to 34.8 pence (2016: 31.5 pence).

Reported profit before tax for the year was £38.9 million (2016: £30.9 million). Reported basic earnings per share were 31.1 pence (2016: 25.7 pence).

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

Other items

To aid understanding of the underlying performance of the Group, throughout the annual report underlying operating profit and underlying profit before tax have been used. These measures exclude 'other items' which are acquisition related charges including amortisation of intangible assets and deferred consideration treated as an employment expense. These 'other items' are shown in a separate column in the consolidated income statement.

1 Before other items; amortisation of acquired intangible assets and employment related and other deferred consideration

Net Finance Expense

Net finance expense amounted to £5.7 million (2016: £4.2 million). The interest payable on bank overdrafts, loans and other similar charges was £4.2 million (2016: £3.3 million) and the interest income from bank deposits and other loans and receivables amounted to £0.4 million (2016: £0.6 million). In addition, the net finance expense includes the interest cost on the net liabilities of the pension scheme of £1.8 million (2016: £1.1 million) and £0.1 million (2016: £0.4 million) unwind of discount on deferred consideration. The interest payable element of the net finance expense includes £2.3 million (2016: £2.1 million) for the cost associated with the arrangement of the Group's banking facilities and the fees for the committed bonding facilities.

Tax

The Group's effective rate of tax was 16.2% of the profit before tax (2016: 14.6%). The lower than normal rate of tax arose owing to prior year adjustments in respect of research and development tax relief and the reversal of timing differences including the use of tax losses not previously recognised as deferred tax assets.

Dividend

The Board has recommended a final dividend for the year of 9.25 pence per share (2016: 8.4 pence per share) to bring the total for the year to 14.0 pence per share (2016: 12.7 pence per share).

In accordance with the pension deficit recovery plan agreed with the Trustee of The Costain Pension Scheme (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 £154.0 million (2016: £99.6 million). The movements are detailed in the consolidated statements of comprehensive income and expense and changes in equity in the financial statements. The increase in the year includes a positive movement following the re-measurement of the Group's legacy pension scheme defined benefit obligations to reflect current market-based assumptions.

New accounting standard – IFRS15

The new accounting standard, IFRS15 revenue recognition, will be applicable to Costain's financial statements in 2018. Full details of the impact of the standard are included in a note to the 2017 financial statements. In summary, the main impact arises from the Group having a small number of long-term frameworks which have separate performance obligations within them and under IFRS15 must be accounted for as separate contracts rather than one long-term framework contract. Application of IFRS15, which has no impact on the Group's cash flow, will reduce the net assets of the Group by £4.6 million on 1 January 2018. As the frameworks complete, which is anticipated to be by 2020, it is forecast that this amount will be generated and therefore reverse this impact on net assets.

Pensions

As at 31 December 2017, the Group's pension scheme deficit in accordance with IAS19, was £23.9 million (2016: £73.5 million). The scheme deficit position has reduced significantly in the year due to returns on assets greater than assumed, a fall in liabilities arising from favourable experience over the period since the last triennial valuation and company contributions.

The table below sets out the key details of the pension scheme deficit calculation:

	2017 £m	2016 £m
Present value of defined benefit obligations	(803.4)	(827.5)
Fair value of scheme assets	779.5	754.0
Recognised liability for defined benefit obligations	(23.9)	(73.5)
Principal actuarial assumptions (expressed as weighted averages)	%	%
Discount rate	2.50	2.70
Future pension increases	2.90	3.10
Inflation assumption	3.10	3.20

In accordance with the pension regulations, a triennial actuarial review of the Costain defined benefit pension scheme was carried out as at 31 March 2016. In February 2017, an updated deficit recovery was agreed with the scheme Trustee resulting in cash contributions of £10.0 million for the 12 months to 31 March 2017 and then £9.6 million per annum (increasing annually with inflation) until the deficit is cleared, which would be in 2031 on the basis of the assumptions made in the valuation and agreed recovery plan.

In addition, as previously implemented, the Group will continue to make an additional contribution so that the total deficit contributions match the total dividend amount paid by the Company each year. Consequently, the total amount of contribution is anticipated to be at the same overall level to that under the previous plan. Any additional payments in this regard would have the effect of reducing the recovery period in the agreed plan.

Cash flow and borrowings

The Group has a positive cash balance, which was £248.7 million as at 31 December 2017 (2016: £210.2 million) which included cash held by joint operations of £87.8 million (2016: £68.1 million). The Group had borrowings of £71.0 million (2016: £70.0 million).

The increase in the net cash position reflects positive operating cash flow and working capital, in particular benefiting from the timing of substantial contract receipts at the year-end. These positive movements have been partially offset by dividend payments and pension deficit contributions made during the year. The average month-end net cash balance during 2017 was £96.7 million (2016: £69.1 million).

NET CASH BALANCE[2]

£177.7m

BANKING FACILITIES

£191.0m

ORDER BOOK

£3.9bn

Order Book

During the year, the Group secured several new contracts and extensions and the Group's order book was maintained at £3.9 billion (31 December 2016: £3.9 billion). The new accounting standard, IFRS15 revenue recognition, sets out a basis for reporting a company's 'backlog' which is a form of order book although different to the Group's reported order book figures. In 2018, the backlog in accordance with IFRS15 will be reported as part of the Group's overall order book.

Contract bonding and banking facilities

The Group has in place banking and bonding facilities from banks and surety bond providers to meet the current and projected usage requirements. In December, the Group increased its banking facilities to £191.0 million and extended the maturity date to 25 June 2022 with its relationship banks. These facilities are made up of a £131 million revolving credit facility and a £60.0 million term loan.

In addition, the Group has in place committed and uncommitted bonding facilities of £320.0 million. In December, the committed element of the bonding facility was reduced to £45.0 million from £125.0 million, lowering the carrying cost of the facilities and reflecting the low level of utilisation, which on the 31 December 2017 was only £5.0 million. Utilisation of the total bonding facilities on the 31 December 2017 was £108.0 million and has not been higher than £161.0 million in the last three years.

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 and 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.

Foreign currency exposure

Translation exposure: the results of the Group's overseas activities, mainly non-core activities 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. The Group holds a currency hedge against the assets held in its Spanish subsidiary.

Transaction exposure: the Group has transactional currency exposures arising from overseas supply purchases for business in the UK and from subsidiaries' commercial activities overseas. 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 against which the Group holds the appropriate hedging arrangements.

Anthony Bickerstaff
Chief Financial Officer
1 March 2018

2 Net cash balance is cash and cash equivalents less interest-bearing loans and borrowings

Experience and effective leadership

Dr Paul Golby

CBE, FREng, FIET, FIMechE, FEI, FCGI

Non-Executive Chairman

Appointment
May 2016

Skills and experience
Paul Golby was appointed as chairman of Costain in May 2016. A fellow of the Royal Academy of Engineering, Paul has held a variety of roles within the engineering and energy industries. Following an early career with Dunlop Holdings plc and BTR plc he joined Clayhithe plc, becoming an executive director in 1992. In 1998, Paul joined East Midlands Electricity plc as managing director and following its acquisition by PowerGen (subsequently E.ON UK plc) was appointed executive director, UK operations. In 2002, Paul became chief executive and later executive chairman, stepping down from the E.ON Board in December 2011.

Paul was also non-executive chairman of AEA Technology Group plc (2009–2012), chairman of Engineering UK (2010–2016) and pro chancellor, and chair of council, of Aston University (2009–2017).

External appointments
Non-executive director of National Grid plc and non-executive chairman of the National Air Traffic Services (NATS Holdings Ltd). Paul is also chairman of the Engineering and Physical Sciences Research Council and a member of the Prime Minister's Counsel for Science and Technology.

Andrew Wyllie

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 (2001–2005) 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, Asia and the UK.

Andrew has a MBA from the London Business School, is a fellow of the Royal Academy of Engineering, senior vice president of the Institution of Civil Engineers, is a fellow of the Institute of Directors and the British American Project. He is also a member of the CBI Infrastructure Board and a companion of the Chartered Management Institute. He held the position of non-executive director of Scottish Water from April 2009 until March 2017. Andrew was awarded a CBE for services to engineering and construction in the 2015 New Year's Honours list.

External appointments
Non-executive director of Yorkshire Water Services Limited.

Anthony Bickerstaff

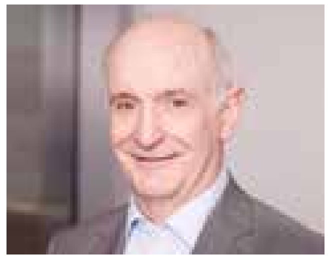
FCCA

Chief Financial Officer

Appointment
June 2006

Skills and experience
Tony Bickerstaff was appointed chief financial officer in June 2006. Tony has extensive knowledge of the infrastructure 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 and Electricity Settlements Company Limited.



James Morley

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 chair of the audit committee from January 2008 until the end of October 2012. He is a chartered accountant with some 30 years' experience as a Board member of both listed and private companies. Previous roles include chief operating officer of Primary Group Ltd (2006–2007), group finance director of Cox Insurance Holdings plc (2002–2005), group finance director of Arjo Wiggins Appleton plc (1999–2001), group executive director finance of Guardian Royal Exchange plc (1990–1999), deputy chief executive and finance director of Avis Europe plc (1976–1989), non-executive director of the Banker's Investment Trust plc (1994–2008), non-executive director of WS Atkins plc (2001–2009), non-executive director of Trade Indemnity Group plc (1991–1996), non-executive director of The Innovation Group plc (2007–2015), non-executive chairman of Acumus Ltd. (2011–2012), non-executive director of Speedy Hire plc (2009–2015) and non-executive director of BMS Group Ltd. (2011–2015).

External appointments
Non-executive director of Minova Insurance Holdings Ltd.

Committee membership

Member of the Remuneration Committee | Member of the Audit Committee | Member of the Nomination Committee | Chair of Committee

Jane Lodge

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. Jane was previously a non-executive director and chair of the Audit Committee, Moorgate Industries Limited (2014–2015) and a non-executive director of Black Country Living Museum Trust Limited.

External appointments
Non-executive director and chair of the Audit Committee at Devro PLC, DCC plc and Sirius Minerals plc. Non-executive director of the Bromsgrove School Foundation.

Alison Wood

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).

Alison is chair of the Costain Charitable Foundation.

External appointments
Non-executive director and chair of the Remuneration Committee at Cobham plc and TT Electronics plc. Senior independent director at e2v technologies plc and a non-executive director of the British Standards Institute.

David McManus

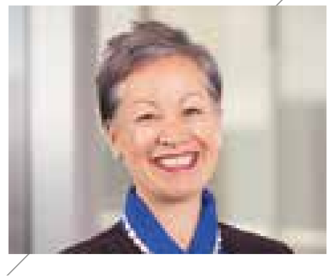
BSc

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), where he served as chairman from 2006 to 2008 and was also a non-executive director of Caza Oil & Gas Inc. (2011–2015).

External appointments
Non-executive chairman of Rockhopper Exploration plc and of FlexLNG and a non-executive director at the Hess Corporation.



Jacqueline de Rojas

CBE

Independent Non-Executive Director

Appointment
November 2017

Skills and experience
Jacqueline de Rojas was appointed as a non-executive director with effect from 20 November 2017. She is a leader in the UK technology sector and an experienced non-executive director who has held executive positions at global blue-chip software companies such as Citrix Systems, CA Technologies, McAfee and Novell. Jacqueline was previously a non-executive director of Home Retail Group prior to the divestment of this group. She was awarded a CBE for services to international trade in the 2018 New Year's Honours list.

External appointments
Non-executive director at Rightmove plc and AO World plc, chair of the Advisory Board at the Digital Leaders Technology Group and president of techUK.

Group Executive Board
See pages 56 to 57

Committee activities
See pages 71 to 73, 75 and 82

An experienced leadership team to deliver the strategy

The Group Executive Board, chaired by Andrew Wyllie, focuses on running the business and delivering the Group strategy. The members are:

Andrew Wyllie
CBE, FREng, MBA, BSc, CEng, FICE, CCMI

Chief Executive

Board of directors profiles
See page 54

Anthony Bickerstaff
FCCA

Chief Financial Officer

Board of directors profiles
See page 54

Sally Austin
BSc (Hons), FCIPD

Group HR Director

Appointment
July 2015

Skills and experience
Sally Austin joined Costain in 2005 and is currently Group HR director. She began her career with BAE Systems, moving to Eaton Corporation in 2000 where she held a number of HR management roles supporting US, EMEA and European facilities. In her current role she holds responsibility for executive remuneration, Group-wide HR operations, recruitment, learning and development, HR shared services and pensions. Sally holds a BSc(Hons) in psychology and is a fellow of the CIPD.

External appointments
Non-executive director of Warwick Independent Schools Foundation.

Matthew Harris
BSc, FCA

Group Strategy and Risk Director

Appointment
December 2016

Skills and experience
Matthew Harris was appointed Group strategy and risk director in 2016. He is a fellow of the Institute of Chartered Accountants in England and Wales, achieved a BSc in management science at the University of Warwick and qualified as a chartered accountant with Price Waterhouse. Matthew gained finance and management experience with BMW, Thames Water, American Water and Hanson. He joined Costain in 2012 as finance director for the Natural Resources division and has led a number of Group-wide projects since then.

Nigel Curry
CEng, BEng, MBA

Group Capability Development Director

Appointment
August 2015

Skills and experience
Nigel Curry is an Executive Board director responsible for Group capability including technology, consultancy, complex delivery and asset optimisation. He is a qualified chartered mechanical engineer with an executive MBA and has attended Harvard and INSEAD on their director programmes. Nigel was granted the Freedom of the City of London in 2008 and has been a trustee of IGEM. Nigel has extensive experience managing the construction of complex programmes in the energy, power and defence sectors. He joined Costain when it acquired the Rhead Group in 2015.

Martin Hunter
BA, ACA

Group Financial Controller

Appointment
April 1999

Skills and experience
Martin Hunter holds the position of Group financial controller and has held a number of head office finance positions since 1984. Previously, Martin worked for Stoy Hayward, a London based firm of chartered accountants.

He is a member of the Institute of Chartered Accountants in England and Wales.

Darren James
BEng (Hons), CEng, FICE, FCIHT, FIoD

Managing Director Infrastructure

Appointment
September 2008

Skills and experience
Darren James has held the position of managing director of the Infrastructure division since 2008. He initially joined as an industrial placement student during his undergraduate studies at the University of Surrey, where he obtained a degree in civil engineering. He has held a number of positions in the Group. In his current role Darren has profit and loss responsibility for the division which provides services to clients in the rail, highways and nuclear sectors. Additionally Darren has Group-wide responsibility for Health, Safety and Environment.

External appointments
Non-executive director of the Port of London Authority and a director of the Rail Industry Association.

Alex Vaughan
BSc (Hons) MRICS, Dip IoD, FIoD

Managing Director Natural Resources

Appointment
October 2006

Skills and experience
Alex Vaughan is managing director of the Natural Resources division, where he is responsible for our services to water, oil and gas and power clients. He has held this position since 2013. He is qualified as a chartered quantity surveyor. He has worked on infrastructure projects in the UK and internationally, as well as having held a number of corporate roles including Group HR director and corporate development director. In 2009 he completed the Harvard Business School AMP. Alex is a member of the CBI regional council and is currently also responsible for the development of client-facing technology solutions across the Group.

David Taylor
FRICS, FIoD

Group Commercial Director

Appointment
January 2015

Skills and experience
David Taylor joined the Company in 2009 and was appointed Group commercial director in January 2015. He has held a number of senior leadership roles within the business and is currently responsible for the commercial, supply chain and design management functions.

Prior to joining Costain, David acquired more than 25 years' experience with Taylor Woodrow where he held the position of commercial director for its UK operations.

Tracey Wood
LLB

Legal Director and Company Secretary

Appointment
July 2008

Skills and experience
Tracey Wood joined the Company in February 2006 as head of legal. She has a construction and commercial law background and was formerly a partner at Hammonds. She has had a number of senior roles and was appointed to the Executive Board as HR director in July 2008. She became legal director and company secretary in June 2010 and currently also has responsibility for human resources across the Group. Tracey is a director of the Costain Charitable Foundation.

External appointments
Non-executive director and chair of Remuneration Committee of Bristol Water PLC.

Chairman's Statement

Governance Highlights

Board Evaluation
→ See more on pages 63 to 64.

Board Activity
→ See more on pages 65 to 69.

Diversity Policy
→ See more on pages 59, 62 and 75.

Dear Shareholder

Over the past year, the Board has continued its focus to maintain the highest standards of corporate governance.

Recognising the need to continue to develop the effectiveness of the Board and add value beyond the statutory requirements, I commissioned an independent evaluation of the functioning of the Board.

Dr Tracy Long from Boardroom Review Limited conducted the review which reported that the Board was well-functioning and effective, with a commitment to the highest standards of governance. The review also provided useful insight and practical actions to help us continue to build on these strengths. More details about the evaluation process and outputs can be found on pages 63 and 64.

During 2018, the Board will continue to promote this robust governance framework that encourages transparency and accountability, as well as a meticulous and efficient approach to internal control and risk management.

Some of the main priorities during the year were:

Board composition

Given the ongoing transformation of the business into the UK's leading smart infrastructure solutions company, the Board identified the requirement for an additional non-executive director with technology sector expertise. Following a comprehensive search led by the Nominations Committee, Jacqueline de Rojas CBE, joined the Board on 20 November 2017. Jacqueline is a recognised and highly regarded technology leader in the UK.

The report from the Nomination Committee on page 74 explains the process the Board and Nominations Committee followed to undertake this search.

On 26 February 2018, the Board announced that as part of its planned Board succession James Morley will be retiring as non-executive director of the Company, and as senior independent director, with effect from the conclusion of the Annual General Meeting on 8 May 2018 (the 2018 AGM). James joined the Board in January 2008 and was appointed as senior independent director in January 2013.

Jane Lodge will succeed James Morley as senior independent director with effect from the conclusion of the 2018 AGM whilst maintaining her role as chair of the Audit Committee.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE

As a premium listed company on the London Stock Exchange, the Company is reporting in accordance with the UK Corporate Governance Code published in April 2016 (the Code), which sets out standards of good practice in relation to board leadership, effectiveness, accountability, remuneration and relations with shareholders. Throughout the entire year, the Company complied with all the provisions of the Code. The Audit Committee Report on pages 70 to 73, the Nomination Committee Report on pages 74 to 75 and the Directors' Remuneration Report on pages 76 to 93 are also incorporated into this report by reference.

Board diversity

Board and Group-wide diversity continues to be an important focus for Costain. With the appointment of Jacqueline de Rojas, the Board currently has 37.5% female representation which exceeds the Hampton-Alexander Review voluntary target for women on boards of FTSE 350 companies.

Talent, development and succession

During the year, the Nominations Committee continued to concentrate on executive and senior leadership succession planning. We spent considerable time assessing the talent pipeline and identifying what skills are needed to support our strategy and business long-term.

Strategy

This year, the Board has again undertaken wide-ranging discussions on the Group's strategic priorities. This has included a number of workshops attended by members of the Group Executive Board and third-party advisers. These conversations continued to be focused on the ongoing strategic transformation of the business. A three-year business plan was approved by the Board in December 2017.

Risk and controls

Protecting the business from operational, financial and reputational risk is a key part of the Board's role. As such the Board continues to enhance the level of risk debate and setting of the Group's risk appetite by undertaking thorough reviews of each of the principal risks. The Audit Committee continues to be focused on ensuring the correct controls are in place to manage these principal risks.

On the following pages, we explain our approach to corporate governance, demonstrating how the Board and its Committees have fulfilled their responsibilities to ensure robust governance practices are embedded throughout the Company.

Dr Paul Golby CBE
Chairman
1 March 2018

GOVERNANCE REPORT CONTINUED

Our governance structure

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 below:

Our Board

Key responsibilities:

The Board is collectively responsible for the management of the Company. The Board's main role is to create long-term value for shareholders by providing entrepreneurial and prudent leadership of the Company. It does this by setting the Company's strategic aims and overseeing their delivery, ensuring that the necessary financial and other resources are available, and by maintaining a balanced approach to risk within a framework of effective controls.

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 costain.com.

Chairman

– The chairman, Dr Paul Golby, is responsible for the effective leadership and operation of the Board.

Chief executive

– The chief executive, Andrew Wyllie, is responsible for managing the business of the Company through the implementation of policies and strategies as determined by the Board.

The role of the chairman and chief executive are separately held and responsibilities clearly established.

See Board biographies on pages 54 and 55.

Non-executive directors

– Comprises five independent non-executive directors.

– The non-executive directors all bring valuable experience, insight and perspective to the Board, through their former executive roles and their other non-executive positions, which are held across a wide range of businesses and disciplines, and this facilitates robust decision-making by the Board as a whole.

– The non-executive directors, together with the chairman, also meet without the executive directors being present from time to time as a matter of good corporate governance.

Specific responsibilities of the senior independent director:

– The role of the senior independent director involves providing a sounding board for the chairman, acting as a point of contact for shareholders to raise concerns, should they arise and meeting with the other non-executive directors, without the presence of the chairman or executive directors, to discuss such matters as the appraisal of the chairman's performance.

– The current senior independent director is James Morley. As James Morley will be retiring as a non-executive director at the conclusion of the Company's 2018 AGM, the role of senior independent director will be taken on by Jane Lodge.

Board Committees

Key responsibilities:

The Board has established Committees which are responsible for audit, remuneration, and appointments 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 62.

Audit Committee

Key responsibilities:

– Monitors and reviews the integrity of Costain's financial statements.

– Manages the relationship with the external auditor.

– Oversees the Company's systems for internal control and risk management.

Nomination Committee

Key responsibilities:

– Monitors and reviews the composition and balance of the Board and its Committees to ensure Costain has the right structure, skills and experience in place for the effective management of the Group.

– Undertakes the management of Board effectiveness reviews.

– Reviews management training and succession planning in respect of the Company's senior executives.

Remuneration Committee

Key responsibilities:

– Determines the remuneration for executive directors and the Executive Committee members.

– Oversees Costain's overall remuneration policy, strategy and implementation.

Group Executive Board

Key responsibilities:

– The Group Executive Board is accountable for the day to day running of the business and delivering the Group strategy following policies laid down by the Board. 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.

See Executive Board biographies on pages 56 and 57.

Investments Committee

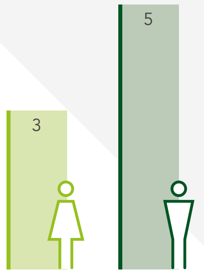
Key responsibilities:

– Responsible for allocating the Group's work winning resources and other investments.

Health & Safety Committee

Key responsibilities:

– Responsible for setting and monitoring compliance with the Group's health and safety policies.



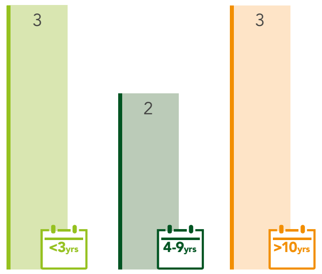
Board membership

- Female
- Male

62.5% male

37.5% female

There are eight members of the Board, five male and three female.



Board tenure

- 3 months to 3 years (3 directors)
- 4 to 9 years (2 directors)
- 10+ years (3 directors)

37.5% +10yrs

Board Expertise (directors)

Construction/Engineering	5
Energy/Oil & Gas/Utilities	5
Finance	3
Consultancy	3
Housebuilding/Property	2
Technology	1
Insurance	1

Leadership

Role of the Board

For more information please refer to diagram on pages 60 and 61.

Board composition and attendance

The Board currently comprises the chairman, two executive directors and five independent non-executive directors. The membership of the Board and biographical details of all the directors can be found on pages 54 and 55.

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 relevant experience and expertise of the Board was further enhanced by the recent appointment of Jacqueline de Rojas as a non-executive director in November 2017 who is a leader in the UK technology sector. 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, gender balance and expertise of the non-executive directors which is depicted in the pie charts on this page.

The Board meets regularly, with eight scheduled meetings having taken place during the year. The directors' attendance record at the scheduled Board meetings and Board Committee meetings for the year ended 31 December 2017 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 roles

For more information please refer to diagram on pages 60 and 61.

Board independence

The Board considers each of its non-executive directors to be independent in character and judgement and there are no relationships or circumstances which are likely to affect (or could appear to affect) the judgement of such non-executive directors, notwithstanding that, in the case of James Morley, the senior independent director, he has served on the Board for more than nine years as at the date of this report. James will be retiring as a non-executive director at the conclusion of the 2018 AGM.

At the time of his original appointment in May 2016, 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 is a member of the FTSE SmallCap Index.

Board attendance	Board Maximum 8	Audit Committee Maximum 4	Remuneration Committee Maximum 3	Nomination Committee Maximum 4
Executive directors				
Andrew Wyllie	8/8	4[a]	1[a]	4[a]
Anthony Bickerstaff	8/8	4[a]	2[a]	3[a]
Non-executive directors				
Paul Golby	8/8	4[a]	3[a]	4/4
James Morley	7/8	4/4	3/3	3/4
Jane Lodge	8/8	4/4	3/3	4/4
Alison Wood	8/8	4/4	3/3	4/4
David McManus	8/8	4/4	3/3	4/4
Jacqueline de Rojas[b]	1/1[b]	1/1[b]	1/1[b]	1/1[b]

(a) Not a member of the Committee – attendance at meeting by invitation.

(b) Appointed to the Board with effect from 20 November 2017.

JULY 2017 BOARD VISIT TO SOUTH WALES:

Offsite visits and Board meetings give the Board further insights into the business. In July 2017, a three day Board visit to South Wales included:

- Six 'show and tell' demonstrations providing insight into the development and application of innovative technologies in the operation of the UK's national infrastructure.
- Tour around the South Wales Traffic Management Centre.
- Site visit to the A465 project.
- Presentations by participants in the Senior Leadership Programme.

Appointments to the Board and retirement of directors

Jacqueline de Rojas was appointed to the Board as a non-executive director with effect from 20 November 2017. At the conclusion of the forthcoming AGM, to be held on 08 May 2018, James Morley will be retiring as a non-executive director and his position as senior independent director will be taken over by Jane Lodge. Biographies of all the directors can be found on pages 54 and 55.

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 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.

The executive directors have contracts of employment with the Company, terminable on 12 months' notice, whilst the Chairman and non-executive directors all have letters of appointment with the Company. 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. All contracts and letters of appointment are available for inspection at the Company's registered office during normal business hours.

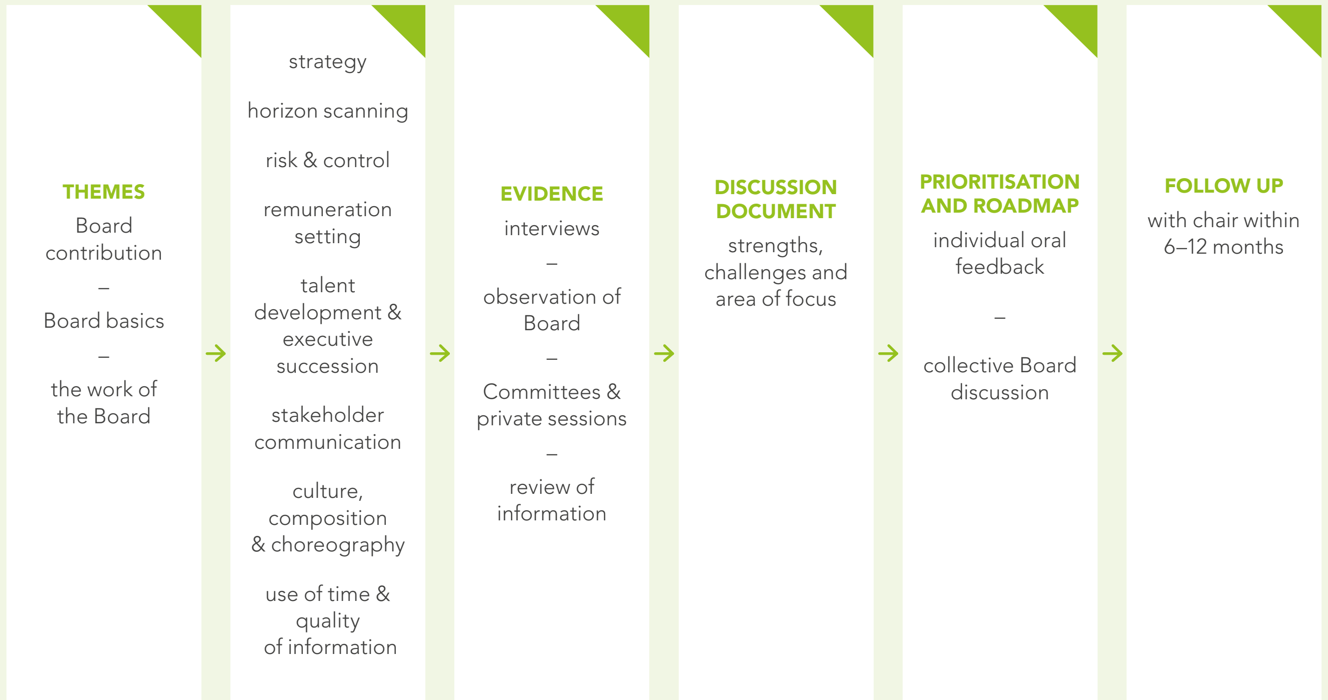
The Company therefore complied with provision B.2.3 of the Code throughout the whole of the year, which requires that all non-executive directors should be appointed for a specific term.

Board effectiveness

Board Effectiveness Evaluation

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

During the year, the Chairman engaged Dr Tracy Long of Boardroom Review Limited, to conduct an externally facilitated Board evaluation. Neither Dr Tracy Long nor Boardroom Review Limited have any other connection with the Company aside from the provision of Board evaluations.



Board effectiveness continued

Outputs from the 2017 Evaluation

Strengths identified:

A positive Board culture, led by the chair and CEO, which is focussed on adding value to the Company.	An increasingly effective use of formal and informal Board and Committee time.	The work of the Board, including: • strong financial management and Audit Committee leadership • attention to the risk and control framework and crisis management • visibility of, and confidence in, the lines of defence • attention to corporate values and principles • setting the tone through the Remuneration Committee • consideration of talent management • effective shareholder communication.

Areas of focus identified:

The need to develop the model through: • better visibility of the market landscape • aligning expectations of pace and change • continued focus on diversity of perspective.	The need to continue the work on executive talent management and succession planning through the Nomination Committee.

Board induction

On appointment, new members of the Board take part in a tailored induction programme, organised by the company secretary and general counsel.

The induction programme for Jacqueline de Rojas covered the following activities and meetings:

01

Meeting with the Board, its Committees and other external stakeholders

As part of the appointment process, Jacqueline had meetings with the chairman, the senior independent director and Committee chairs in order to build up her understanding of the Costain business and its markets. Additionally, Jacqueline had the opportunity to meet with other key advisers and stakeholders, including the Company's financial advisers/brokers.

02

Meeting with senior management and staff

Jacqueline has spent time at the Group's headquarters meeting the chief executive and chief financial officer. She also had meetings with all the members of the Executive Board. In January 2018, Jacqueline attended the Costain awards ceremony during which she had the opportunity to speak to members of staff from across the business.

03

Understanding the business

Jacqueline (accompanied by the relevant managing director) has carried out engagement tours at three operational sites. These tours have involved Jacqueline meeting with various members of the project team, including the supply chain, and learning about the nature of each of the projects.

04

Training

An electronic induction pack has been provided to ensure a thorough understanding of the role of director and the framework within which the Board operates. This has been coupled with a training session with the company secretary and general counsel covering director's duties and the Group's corporate governance practices and procedures.

How the non-executive directors are kept informed

- Deep dive presentations from business sectors or functions.
- Visits to regional offices or operational sites.
- Access to key executive personnel between meetings.
- Weekly reports from the chief executive.
- Regular management accounts and internal reports.
- Updates on legal, regulatory and governance matters.
- Presentations from external advisers.

Directors due to offer themselves for election/re-election at the 2018 AGM

Andrew Wyllie

David McManus

Jacqueline de Rojas

Health and Safety

The Board considers health and safety its number one priority.

- All Board members hold a Construction Site Visitor Card certificated under the Construction Skills Certification Scheme.
- The Board also take part in twice yearly health and safety impact days which take place across all our sites.
- As part of the Company's commitment to health and wellbeing the Board have also recently undertaken mental health training.

Board training

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 sessions.

Operation of the Board

The chairman sets the Board's agenda and ensures that adequate time is available for discussion of all agenda items. 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 have access to all information relating to the Group and are free to seek any further information they consider necessary. After each meeting, the company secretary operates a comprehensive follow-up procedure to ensure that actions are completed as agreed by the Board.

Senior executives below Board level are invited to attend Board meetings from time to time in order to deliver presentations on issues that are relevant to their particular business sector or function. During the year, the directors set aside several days to combine scheduled Board and Committee meetings with visiting regional offices and operational sites in order to provide the non-executives with an opportunity to meet both senior managers and other members of staff and to obtain a greater insight into particular aspects of the business and projects that the Company is engaged in.

In July 2017, the Board travelled to South Wales in order to visit the Company's projects and the highlights of their visit are detailed in the table shown on page 63.

In addition, between Board meetings, the chairman and non-executive directors have access to the chief executive, chief financial officer 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. The Board is also kept up to date on legal, regulatory and governance matters by both the company secretary and external advisers.

All Board members have access to the advice and services of the company secretary, who is responsible for ensuring that Board procedures are followed and applicable rules and regulations are followed, and who is also the Company's general counsel. 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.

Re-election of directors

In accordance with Article 78 of the Company's articles of association and provision B.7.1 of the Code, Jacqueline de Rojas, Andrew Wyllie and David McManus are due to offer themselves for election/re-election at the 2018 Annual General Meeting (AGM). Jacqueline, having been appointed by the Board since the last AGM, is required to stand for election. Andrew and David, having served on the Board at the time of the two preceding AGMs without retiring, are also both required to stand for re-election at the 2018 AGM. Jacqueline and David have letters of appointment with the Company, and the current terms of appointment of all the directors are set out in the Directors' Remuneration Report on page 90.

Having due regard to the results of the externally facilitated review of the Board's performance conducted by Boardroom Review Limited, and to periodic internal evaluations (further details provided on pages 63 and 64), the Board confirms that it is of the opinion that each of the non-executive directors standing for election/re-election continues to be independent in character and judgement. The Board also confirms that these directors continue to perform effectively, that they demonstrate commitment to their particular roles, that they ensure proper time is devoted to Board and Committee meetings and should therefore be re-elected at the forthcoming AGM.

Directors' conflicts of interest and external appointments

The non-executive directors may serve on a number of other company boards provided they continue to demonstrate the requisite commitment to discharge their duties to the Company effectively and such external appointments are seen as being beneficial to the overall decision-making process of the Board as a whole. The Company also encourages the executive directors to take up non-executive positions, with the prior consent of the Company, in the belief that such appointments broaden their skills and enhance the contribution which they can make to the Company's performance. Generally, no more than one such appointment may be undertaken by the executive directors. The Company has procedures in place for managing conflicts of interest. Directors are required to declare all external appointments or relationships with other companies and the Board has adopted appropriate processes to manage and, if appropriate, approve any such appointment or relationship which could result in a possible conflict 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.

Corporate Responsibility (CR)

The Board receives reports from the Company's corporate responsibility director and monitors progress on a regular basis.

Diversity

Details of the Company's diversity policy, in relation to the Board and senior executives, can be found on page 75 of the Nomination Committee Report.

Details of the Company's Group-wide approach to issues of diversity and equality can also be found on page 19 of this annual report.

Remuneration

Details of the Company's remuneration policy and how it has been implemented, together with the activities of the Remuneration Committee are to be found on pages 76 to 93 of the Directors' Remuneration Report.

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.

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 on 4 July 2017 the hosting of a site visit for analysts to its technology facility in Yatton, North Somerset. The visit provided insight into the development and application of innovative technologies in the operation of the UK's national infrastructure.

The chairman is available to discuss strategy and governance issues with shareholders. The senior independent director, who is currently James Morley, is available to shareholders if they have any concerns that have not been, or cannot be, addressed through the normal channels of chairman, chief executive or chief financial officer.

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 AGM as an important opportunity to communicate directly with shareholders. The AGM provides shareholders with an opportunity to ask questions of the directors during the meeting and also on a more informal basis following the conclusion of the meeting, at which senior members of staff are also present. The AGM also gives shareholders an opportunity to listen to a presentation from the chief executive on the current trading performance and developments within the business. Board members, including the chairs of the Remuneration, Nomination and Audit Committees, attended the 2017 AGM and propose to attend the 2018 AGM, 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.

Accountability

Financial and business reporting

The Board is required by the Code to present a fair, balanced and understandable assessment of the Company's position and prospects and reference is made to the statement of directors' responsibilities on page 98 together with the statement on the status of the Company as a going concern and the financial viability statement on pages 44 and 45.

The preparation of this annual report involved input from a number of functions across the Group and the Board was involved at an early stage to enable review, challenge and discussion ahead of approving the final publication.

The Board also recognises that its responsibility to present a fair, balanced and understandable assessment also extends to interim and other price-sensitive reports that the Company may publish from time to time.

Business model

The Strategic Report on pages 1 to 53 gives details of the Company's business model and the strategy for delivering the objectives of the Company.

Risk management and internal control

Risk management

Risk management is firmly established and plays a critical role in ensuring the Group continues to deliver its strategic objectives and in meeting the requirements of the Code. The Board is responsible for undertaking a robust assessment of the principal risks facing the Group, as described on pages 44 to 49 of the Strategic Report, including those that would threaten its business model, future performance, solvency and liquidity and ensuring that appropriate mitigating actions are in place to manage them.

The Group's approach to risk management ensures that, on an ongoing basis, the most significant risks to the Group's objectives are identified, assessed and managed.

Policy and procedures require that all divisions and functions undertake effective risk management ensuring that controls are in place and operating as intended in order to manage risks. Whilst enterprise level risk management is coordinated and supported by the Group risk and assurance function ownership of risk is maintained at the business unit level.

GOVERNANCE REPORT CONTINUED

At all levels within the business, risk events and their potential impact are identified and captured in risk registers. Using a standard assessment matrix, risks are assessed for their likelihood and impact of occurrence together with identification of controls in place to manage them. Considering the Group's risk appetite, as defined by the Board, further mitigating action plans are developed to mitigate the risk to an acceptable level. The Group risk and assurance team then provide ongoing oversight of the implementation of mitigating actions reporting to the Executive Board and Audit Committee regularly.

The Costain Way, which forms the basis of the Group's control framework, contains all policies, procedures and controls and is regularly updated to reflect the output of risk and assurance activity to ensure that there is continuous improvement to the control environment.

Improvements to the risk management system have been implemented throughout 2017, in particular in the way risks are aggregated, escalated and reported up to the Executive Board and subsequently the Audit Committee. Strengthening of the process will continue in 2018 including further consistency in approach, training of personnel, establishment of a cross functional risk forum and improving processes to capture and escalate contract risks to Group level.

Internal control

The Board is responsible for the Group's systems of risk management and internal control and is required to regularly review their effectiveness. The Audit Committee has undertaken this review in accordance with the requirements of the *Guidance on Risk Management, Internal Control and Related Financial and Business Reporting*, published by the FRC, throughout the year and up to the date of this annual report. Further details can be found on page 72 of the Audit Committee Report.

The Group uses the Costain Way, its operational management system, as the framework for the systems and controls in place to ensure that exposure to significant risks is managed appropriately. The Board recognises that such a system 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 Costain Way is certified by BSI as compliant to management standards including ISO 9001 (quality), ISO 14001 (environment), OHSAS 18001 (health and safety), ISO 22301 (business continuity), ISO 27001 (information security) and BS 11000 (collaboration).

Guidance, policies, processes and controls within the Costain Way include but are not limited to:

- a clear and regularly updated delegation of authority including matters reserved for the Board
- clear procedures regarding the review and approval of investment decisions by management, the Board and its Committees
- a robust annual strategy and planning cycle across all business units and the interaction with the risk management system to identify and mitigate the risks that pose the greatest threat or opportunity in achievement of our strategic objectives
- a comprehensive annual budgeting system, linked to the annual strategy review, for each business unit which is reviewed and approved by the Board in December of each year
- robust financial reporting procedures designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes
- monthly divisional performance reviews by management and reported against budget to the Executive Board and the PLC Board. This report covers profit and loss and cashflow with accompanying narrative on any significant issues

> "Internal Audit monitors compliance against the Costain Way using a risk-based approach to ensure the focus is on high-risk activities and thus verify the appropriate implementation of controls."

- clear and established escalation and reporting from the Group treasurer and Group tax manager, via the chief financial officer, to the Audit Committee on any issues of significance to the Group
- Group wide risk management policy and standards which are embedded across the Group
- comprehensive contract level reporting to management on a monthly basis including detailed information on safety, health and environmental performance, cash flow, value, cost and profit, claims and variations, risk management, progress and staffing levels. This enables management to monitor performance, taking action as necessary
- third line of defence reviews performed by internal audit providing assurance over areas of the highest perceived risk
- legal compliance risks are addressed through clearly communicated policies, associated procedures e.g. for the declaration of gifts and hospitality, and regular training over such matters as, competition, data security and ethics
- regular Board reporting and monitoring of the effectiveness of safety, health and environment processes.

The Group also has an independent internal audit function who undertake a programme of risk based audits across all operations throughout the year. All audit reports are shared with the relevant business owners who are expected to implement appropriate measures to address any risks or controls weaknesses. The results of all internal audit activity are also shared with the chief executive, chief financial officer and scrutinised by the Executive Board and Audit Committee on a regular basis, further details of which can be found on page 72 of the Audit Committee Report.

AUDIT COMMITTEE

Audit Committee Report

Governance of the Committee

The Audit Committee (the Committee) is comprised exclusively of independent non-executive directors, with myself acting as chairman. The members of the Committee and details of their attendance at Committee meetings are given on page 62 and their biographies are shown on pages 54 and 55.

The company secretary is secretary to the Committee.

The Company considers that I, as chairman, possess the necessary recent and relevant financial experience to effectively chair the Committee. In addition, the Company considers that all the members of the Committee possess relevant skills and experience to meaningfully support the activities of the Committee.

During 2017, the Committee held four meetings. The meetings of the Committee are normally also attended by the chairman, the chief executive, the chief financial officer, the group strategy and risk director, the head of risk and assurance, the financial controller and the external auditor. Other senior executives will attend as required to provide information on matters being discussed which fall into their area of responsibility. The Committee also regularly meets privately with the external auditor and the head of risk and assurance.

Role of the 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 announcements relating to the Group's performance, and reviewing significant financial judgements contained in them
- reviewing the effectiveness of the Group's system of internal controls and the processes for management of the principal risks facing the Group
- reviewing the effectiveness of the risk and assurance function and approving, in consultation with the chief executive, the appointment and termination of employment of the head of that function
- 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 systems for detecting fraud, preventing bribery and allowing employees to raise concerns in a safe and confidential manner 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.

SIGNIFICANT ACCOUNTING MATTERS THIS YEAR

- Key contract judgements.
- Pension deficit measurement.
- Thematic review of pension disclosures.
- The carrying value of goodwill and intangible assets.
- Going concern and viability statement.
- Future IFRS and UK GAAP developments.

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 following the review this year no amendments were considered to be required at this time.

Activities

In 2017, the principal activities of the Committee and the manner in which it discharged its responsibilities were as follows:

Financial statements

The Committee reviewed and evaluated 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 2017. At the Board's request, it also considered whether the annual report and accounts, taken as a whole, was fair, balanced and understandable and provided the information necessary for shareholders to assess the Company's performance, business model and strategy.

Significant accounting matters

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

(A) Key contract judgements

As detailed in note 2 on pages 114 to 121 of the financial statements, a significant proportion of the Group's activities are undertaken via long-term contracts. 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 uses detailed contract valuations and cost forecasts when formulating its judgements of costs and revenues and its assessments of the expected outcome of each long-term contractual obligation. Given the Company's portfolio of contracts, the Committee spent time during the year reviewing the positions and judgements taken by management on a number of material contracts across the Group. This was mainly achieved through discussions with, and reviewing reports presented by, management and the external auditor.

This review included, amongst other things, consideration of the Greater Manchester Waste Disposal Authority PFI contract awarded in 2007 which in September 2017 was successfully terminated by consensual agreement. In accordance with the terms of the termination, Costain fully demobilised its remaining activities and settled all of its obligations under the contract within the provisions we had previously taken for the project.

On the basis of its review of material contracts, the Committee concluded that it was content with the judgements that had been made by management and that appropriate disclosures had been made at the relevant times.

(B) Pension

The Group's defined benefit pension scheme requires significant judgements to be made 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 Company takes written advice from an independent qualified actuary. These assumptions and sensitivities are set out in note 20 on page 141 of the financial statements.

The triennial actuarial review was carried out as at 31 March 2016 and in February 2017, an updated deficit recovery plan was agreed with the scheme trustee.

(C) Thematic review of pension disclosures

The Committee considered the outcome of the Financial Reporting Council (FRC) thematic review of the Group's reporting relating to pension disclosures in respect of the year ended 31 December 2016. It was noted that the FRC had no substantive issues to raise. The FRC did note one matter relating to disclosure of the approach used to value assets that do not have a quoted market price in an active market. The Committee agreed the changes that needed to be made to the 2017 annual report as regards this one matter.

(D) The carrying value of goodwill and intangible assets

As set out in note 11 on pages 129 and 130 of the financial statements, the goodwill and acquired intangible balances within the Group relate to companies acquired by the Group. In particular, the Committee reviewed the carrying value of the goodwill within the Natural Resources division. The Committee also critically reviewed the impairment considerations in respect of the goodwill and intangibles. The Committee agreed with the amortisation charge in respect of intangibles, and the conclusion that no impairment to goodwill was necessary.

(E) Going concern and viability statement

The Committee reviewed the Group's processes for the management of cash flow and working capital, committed funding, its ability to generate cash and its ability to raise further funding. It also challenged management's sensitivity analysis including in relation to mitigating actions. The Committee also considered the period over which the Viability Statement (set out on page 44 and 45) should apply. Based on this analysis, the Committee recommended to the Board that it could approve and make the Viability Statement and that the Group can adopt the going concern basis in preparing its financial statements.

(F) Future IFRS and UK GAAP developments

During the year, the Committee received reports from both the external auditor and the financial controller regarding the future accounting developments likely to affect the presentation of the Group's financial statements, including IFRS 15 (Revenue from Contracts with Customers) and IFRS 9 (Financial Instruments).

The impact on the Group of these standards is explained on page 121 of the notes to the Financial Statements.

> "The Committee, on behalf of the Board, has evaluated the effectiveness of the systems of risk management and internal controls operated within the Group pursuant to the FRC's guidance on internal control."

Evaluation of effectiveness of the Committee

An external effectiveness review of the Committee's performance has been carried out in respect of the year ended 31 December 2017 as part of the review into the effectiveness of the Board conducted by Dr Tracy Long of Boardroom Review Limited. The effectiveness of the Committee and its chairman was commended and the review concluded that there were no significant areas for concern in respect of the performance of the Committee or any of its members.

Risk management and internal control

Details of the Group's internal controls and risk management framework are more fully set out on pages 44 to 49 in the Strategic Report and pages 67 to 69 in the Governance Report.

The Committee, on behalf of the Board, has evaluated the effectiveness of the systems of risk management and internal controls operated within the Group pursuant to the FRC's guidance on internal control. The evaluation covered all material controls, including financial, operational and compliance controls. The review did not identify any significant weaknesses in the system of internal control and risk management.

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

Internal audit

The Group has an internally resourced risk and assurance function which reports directly to the Committee. The Committee is responsible for monitoring and reviewing the operation and effectiveness of this function and approves the scope of its annual plan. Following feedback from last year's review of the internal audit function, a new head of risk and assurance was appointed in February 2017.

During the year, the Committee undertook another internal assessment of the effectiveness and independence of the internal audit function which evidenced continued improvement across all areas, including better alignment between audit planning and the Group's strategic objectives, resulting in the improved effectiveness of internal audit reporting. Accordingly, the Committee is satisfied that the quality, experience and expertise of the function is appropriate for the business.

The Committee has received regular reports on the internal audit function's programme and findings at each of its meetings during the course of the year, and has been presented with action plans to resolve any highlighted areas.

External auditor

The Company's external auditor is PricewaterhouseCoopers LLP (PwC). The audit partner is Jonathan Hook.

Independence

During 2016, the Committee conducted a competitive tender process, the details of which were reported in last year's annual report. The Board approved the Committee's recommendation to appoint PwC as auditors of the Company in respect of the year ending 31 December 2017 replacing KPMG LLP. A resolution was approved by the shareholders at the Annual General Meeting held on 8 May 2017.

A thorough conflict of interest check was undertaken as part of the tender process and the ability of PwC to meet strict independence and objectivity requirements was one of the key considerations of the Committee when making its recommendation. Therefore the Committee considers that the appointment of PwC has ensured that a high level of independence is maintained and the Committee will continue to monitor this area.

Audit effectiveness procedure

Questionnaires
Questionnaires completed by members

Report compiled
Company secretary produces report for consideration by Committee

Decision made
Efficiency and effectiveness of the external audit 2016 was deemed satisfactory

Effectiveness

Following the end of the 2016 financial year, the Committee considered the effectiveness of KPMG as external auditor. As part of this process, external audit effectiveness questionnaires were completed by members of the Committee, the executive directors, other members of the Executive Board and certain members of the finance team. Based on the responses to the questionnaires, the company secretary produced a report for detailed consideration by the Committee. The Committee confirms that it remained satisfied with the efficiency and effectiveness of the external audit in respect of the year ended 31 December 2016.

During the year, the Committee has also kept under review the ongoing effectiveness of PwC as the Company's new external auditor, for example, through the quality of the external auditor's reports and the audit partner's interaction with the Committee. The Committee confirms that it believes that the independence and objectivity of PwC and the effectiveness of the audit process remains strong and has therefore recommended the re-appointment of PwC for 2018.

Non-audit fees

The Company has 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 as to ensure that these are not impaired by the provision of permissible non-audit services.

In 2017, other than the interim review, the external auditor performed very limited non-audit services and fees payable to the external auditor were less than £0.1 million (2016: less than £0.1 million).

Planning

At its meeting in December 2017, the Committee considered and approved the external audit plan for the audit of the Group for the year ended 31 December 2017. The Committee considered significant risk areas for the audit, the proposed scope, the materiality threshold, and the transition from KPMG LLP to PwC.

Jane Lodge
Chair
1 March 2018

Nomination Committee Report

NOMINATION COMMITTEE

Governance of the Committee

The Nomination Committee (the Committee) is comprised exclusively of independent non-executive directors, with myself acting as chairman. The members of the Committee and details of their attendance at Committee meetings are given on page 62 and their biographies are shown on pages 54 and 55.

The company secretary is secretary to the Committee.

Only members of the Committee have the right to attend Committee meetings. Other individuals, such as the chief executive, Group HR director, members of senior management and external advisors, may be invited to attend meetings as and when it is considered appropriate.

The outcome of all Committee meetings are reported to the Board for its consideration. The senior independent director of the Company will chair any meetings of the Committee that may deal with the appointment of my successor as chairman of the Company. The Committee may take independent professional advice on any matters covered by its terms of reference at the Company's expense.

Role of the Committee

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

- reviewing the overall size, structure and composition of the Board
- identifying and nominating for the Board's approval, candidates to fill Board vacancies as and when they arise
- receiving notifications from directors of situations, such as proposed external appointments, in which a potential conflict of interest might arise and/or their time commitment to the Board could be compromised
- 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 arrangements and management training in respect of the executive directors and other senior employees
- directing periodic Board effectiveness reviews, both internal and external, which form part of the regular evaluation and development work conducted by the Board to ensure it continues to improve its overall effectiveness.

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 following the review this year no amendments were considered to be required at this time.

Activities

In 2017, the principal activities of the Committee and the manner in which it discharged its responsibilities were as follows:

Succession planning

Succession planning has continued to be a key area of focus during the year, both in respect of the Board and for those high performing individuals below Board level, together with an ongoing review of the structure and composition of the Board. This focus is aligned and supportive of the Group's key strategic objective of enhancing its ability to deliver a range of innovative technology based solutions for its customers.

As part of this process a working group, led by myself as chairman and Ms Jane Lodge, was established to oversee the recruitment of an additional non-executive director who could demonstrate an appropriate set of skills and background gained within the technology sector. The Lygon Group was appointed to help facilitate this process who, having no other connection with the Company and being a signatory to the voluntary Code of Conduct of Executive Search Firms, was considered to be independent.

Having considered a number of potential candidates, from a gender-balanced list of individuals with a range of backgrounds and experiences, this process culminated in the nomination, and subsequent approval by the Board in November 2017, of the appointment as non-executive director of Ms Jacqueline de Rojas CBE. Jacqueline, whose biographical details can be found on page 55 of this annual report, brings to her role significant experience gained within the technology sector and in the delivery of innovative IT solutions.

On 26 February 2018, the Board announced that as part of its planned Board succession James Morley will be retiring as non-executive director of the Company, and as senior independent director, with effect from the conclusion of the Annual General Meeting on 8 May 2018 (the 2018 AGM). James Morley joined the Board in January 2008 and was appointed as senior independent director in January 2013.

Jane Lodge will succeed James Morley as senior independent director with effect from the conclusion of the 2018 AGM while remaining chair of the Audit Committee.

In order to develop future executive talent, and to ensure that appropriate succession is in place, specific actions have been undertaken during the year in respect of certain members of the Executive Board. This process has been conducted with the assistance of external consultants, The Zygos Partnership, who undertook both a benchmarking exercise and facilitated personal assessments to ascertain the executives' skills, potential and further development requirements.

In the year under review, the Committee received updates from Sally Austin, the Group HR director, on the talent management and succession planning activities within the wider Group.

Board diversity

The Company remains committed to ensuring a diverse and representative Board and to ensuring that appointments are based on merit. Boardroom diversity continues to be an important area of focus for the Committee with the aim of attracting and maintaining a Board which has a broad range of skills, backgrounds and experience, whilst ensuring that the best people are appointed. Within this context, and as part of the ongoing process of refreshing the Board, the Company continues to encourage and welcome interest from a wide range of candidates who will add to the Board's diversity.

The Hampton-Alexander Review (the Review), published in November 2016, regarding gender balance within the leadership structure of listed companies, has recommended (amongst other things) a voluntary target for women represented on FTSE 350 Boards of 33% by 2020. The Board currently has a 37.5% female representation which exceeds the recommendation of the Review and with effect from the conclusion of the 2018 AGM will have a female senior independent director.

The Committee is also mindful of the Review's recommendation for a 33% female representation on executive boards and the direct reports to the executive committees of FTSE 250 companies by 2020. The Committee continues to monitor gender diversity within the Company's senior management including that of the Group Executive Board. This currently stands at 18%.

The Committee also acknowledges the target set by the Parker Review for FTSE 250 companies to have at least one non-white director on their Boards by 2024. Diversity in all its forms, including ethnic diversity, is an area of increased focus for the Group at both Board level and throughout the business.

A copy of the Board's Diversity Policy relating to appointments to the Board can be found on the Company's website at: www.costain.com.

The composition of our Board and Group Executive Board can be found on pages 54 and 55, 56 and 57 of this annual report respectively.

Dr Paul Golby CBE
Chairman

1 March 2018

HOW DID WE PERFORM IN THE YEAR?

GROUP EBITA

£49.0m

2017	**49.0**
2016	41.1
2015	33.2
2014	28.7

GROUP HEALTH & SAFETY

0.07AFR

2017	**0.07**
2016	0.09
2015	0.08
2014	0.10

UNDERLYING EARNINGS PER SHARE

34.8p

2017	**34.8**
2016	31.5
2015	25.1
2014	27.8

CASH FLOW (average month end cash balance)

£96.7m

2017	**96.7**
2016	69.1
2015	103.7
2014	95.6

HOW WAS OUR PERFORMANCE REFLECTED IN OUR PAY?

AIP – Award achieved by executive directors

	GROUP EBITA[1] (maximum opportunity: 55%)	GROUP HEALTH AND SAFETY (maximum opportunity: 10%)	ORDER BOOK (maximum opportunity: 10%)	CASH FLOW[3] (maximum opportunity: 10%)	PERSONAL PERFORMANCE (maximum opportunity: 15%)	TOTAL ACHIEVED
Andrew Wyllie	40%	7%	9%	10%	15%	81%
Anthony Bickerstaff	40%	7%	9%	10%	15%	81%

LTIP – Award achieved by executive directors

	AGGREGATE EPS[2] (for financial years ended 31 December 2015, 2016 and 2017)	TOTAL ACHIEVED
Andrew Wyllie	93.7 pence (Maximum vesting level: 96.9p or more)	79.1%
Anthony Bickerstaff	93.7 pence (Maximum vesting level: 96.9p or more)	79.1%

ENSURING SHAREHOLDER ALIGNMENT

33% of AIP bonus is automatically deferred into Costain shares with a two year holding period

50% Subject to performance targets being met, 50% of LTIP shares vest after three years; the remaining 50% vest after five years

100% Shareholder guidelines are currently set at 100% of salary for the executive directors, both of whom have exceeded this target

1 Earnings before interest, tax and amortisation; calculated on an adjusted basis
2 Adjusted to take account of relevant events such as acquisitions and disposals
3 Measured pre-acquisition and investments; adjusted to remove exceptional cash inflow at the end of 2016 and 2017

ANNUAL STATEMENT BY CHAIR OF THE REMUNERATION COMMITTEE

Remuneration Committee Report

REMUNERATION COMMITTEE

AT A GLANCE SUMMARY: EXECUTIVE DIRECTORS' REMUNERATION

2017 variable pay outcomes

2017 AIP outcome of 81% (chief executive) and 81% (chief financial officer) of maximum (see page 84).

One third of the amount earned under the 2017 AIP deferred in shares for two years.

Vesting of the 2015 LTIP award at 79.1% of maximum supported by aggregate EPS of 93.7 pence for the three years ended 31 December 2017 (see page 85).

50% of the 2015 LTIP award vesting is subject to a two year holding period.

Implementation in 2018

Salary increases of 2.5% with effect from 1 April 2018.

Maximum 2018 AIP opportunity equal to 150% of salary subject to a mixture of financial and non-financial performance measures (see page 87).

Maximum 2018 LTIP award opportunity equal to 100% of salary subject to aggregate EPS performance and cash conversion performance over the three financial years ending 31 December 2020 (see page 88).

I am pleased to present our Directors' Remuneration Report, on behalf of the Board, for the year ended 31 December 2017.

Performance and variable pay outcomes for the year ended 31 December 2017

The Company has had another strong year, with continued growth in revenue, profit and cash, and maintaining the high quality forward order book at £3.9 billion of revenue. Performance against the strategic priorities underpinning our strategy is set out on pages 26 to 31 of the Strategic Report.

The 2017 AIP award, one third of which is deferred in shares for two years, was subject to a mixture of financial and non-financial performance measures aligned with key strategic priorities. 55% was linked to EBITA and the remainder to continued improvement of our health and safety performance, order book profitability, cash management and the delivery of critical project and corporate activities which were the personal responsibility of our executive directors.

Based on 2017 EBITA of £49 million and taking into account performance in the year against the non-financial performance measures, the chief executive and chief financial officer will both receive 81% of their maximum AIP opportunity respectively one third of which is deferred in shares for two years. Further details are set out on page 84.

The LTIP award granted on 9 March 2015 was subject to an aggregate EPS target for the three financial years ended 31 December 2017 of 83.9 pence (15% vests) to EPS of 96.9 pence (100% vests). Based on aggregate EPS performance of 93.7 pence over the three years, 79.1% of the LTIP award is due to vest in March 2018. 50% of the amount vesting is subject to a two year holding period for the executive directors. Further details are set out on page 85.

DEFINITIONS USED IN THIS REPORT

AIP: Annual Incentive Plan

EBITA: Earnings Before Interest, Tax and Amortisation as adjusted by the Remuneration Committee to take account of relevant events (such as acquisitions or disposals) and ensure that the performance measures are assessed on a consistent basis year-to-year

EPS: Earnings Per Share as adjusted by the Remuneration Committee to take account of relevant events (such as acquisitions or disposals) and ensure that the performance measures are assessed on a consistent basis year-to-year

LTIP: Long-Term Incentive Plan

SDP: Share Deferral Plan

DIRECTORS' REMUNERATION REPORT CONTINUED

Remuneration policy

Our remuneration policy was approved by shareholders at our 2017 AGM, supported by over 98% of the votes cast. The following is an overview of how our remuneration policy supports the strategic priorities of the business:

Health and safety remains our highest priority.	• AIP includes health and safety performance metrics.
Encourage behaviours which facilitate the delivery of innovative and sustainable solutions to increasingly complex and large-scale national needs, to ensure we remain competitive and continue to deliver shareholder value.	• Performance targets are set to reward sustainable business performance, while not encouraging inappropriate business risks to be taken. • AIP performance measures aim to balance earnings growth and other key financial objectives with non-financial indicators. • One-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 LTIP captures long-term growth in earnings and cash conversion. An additional two years' deferral on 50% of any LTIP award which vests further supports longer term alignment between executives and shareholders.
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.
Building a long-term sustainable business.	• Our remuneration policy ensures further alignment of interests between the Costain Board and shareholders by expecting the executive directors to build and maintain a shareholding worth not less than 100% of base salary (or 200% of salary should the annual LTIP opportunity exceed 100% of salary). Both executive directors have exceeded their shareholding guidelines.

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) Regulations 2008 (as amended). 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 remuneration policy. This section contains the policy table summarising the remuneration policy approved at the 2017 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 2017 and how we intend for the policy to apply for the year ending 31 December 2018 and is the subject of an advisory shareholder vote at the 2018 AGM.

Reward for the year ending 31 December 2018

We approved salary increases for the executive directors of 2.5% with effect from 1 April 2018 after carefully considering their performance and the range of salary increases awarded to other employees.

No changes are proposed to the quantum or structure of the AIP or LTIP for 2018. The AIP will be weighted 70% as regards financial measures, 10% as regards health and safety measures and 20% as regards other non-financial group and personal strategic measures including targets to specifically address growth in consultancy, advisory and technology capability. The Committee considers that this weighting appropriately aligns the AIP performance measures with key financial and strategic areas of the business. Details of the AIP performance measures are provided on page 87 and the targets with performance against them will be provided in the 2018 Directors' Remuneration Report. Details of the LTIP performance measures and targets are provided on page 88.

The non-executives' and the chairman's fee for 2018 is to increase by 2.5%.

Conclusion

We remain committed to a responsible approach to executive pay. Overall, given the Company's performance over the one and three-year periods ended 31 December 2017, we believe that the remuneration of the executive directors in respect of 2017 continues to reflect our success in the delivery of our strategy and the drive for profitable and sustainable long-term growth for our shareholders. The following pages describe in further detail how we have implemented our remuneration policy in 2017, together with our approach for 2018, the agenda of which will continue to focus on aligning reward with our strategy. We do not envisage any significant changes.

The remuneration policy approved at our 2017 AGM remains in force and we have therefore published the policy table only. The remuneration policy in its entirety is available in the 2016 annual report on our website.

Alison Wood
Chair
1 March 2018

EXTRACT FROM THE REMUNERATION POLICY

The remuneration policy was approved by shareholders under a binding vote at the AGM on 8 May 2017. We have set out below the policy table and the full remuneration policy is available in the 2016 annual report on the Company's website at costain.com.

Remuneration policy for executive directors is set out below.

Element	Purpose and link to strategy	Operation	Performance metrics	Maximum opportunity
Salary	• To attract and retain high-calibre individuals. • Reflects skills, experience and performance in role. • Provides an appropriate level of basic fixed income while avoiding excessive risk arising from over reliance on variable income.	• Generally reviewed annually (with any change usually effective from 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. • Increases will usually be in line with average salary increases for the wider workforce (in percentage terms). • Higher increases may be appropriate in certain circumstances, which include but are not limited to, where an individual is promoted, changes role or where an individual is appointed on a below market salary with the expectation that their salary will increase with experience and performance.	• N/A	• To avoid setting expectations of future salary increases there is no maximum salary value set under the policy.
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.	• 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, ordinarily, to continued employment and not being under notice of termination, either given or received, on the date of vesting). Deferred share awards may be granted as conditional awards or nil or nominal cost options. • The Committee may decide not to operate deferral where the amount of the bonus otherwise to be deferred would, in the opinion of the Committee be so small as to make deferral unduly administratively burdensome. Executives may, with the approval of the Committee, elect for a greater proportion of the AIP award to be deferred into shares. • Deferred share awards may include the right to receive a benefit (in cash or in shares) determined by reference to the value of dividends that would have been paid by reference to dividend record dates in the period from grant to vesting. The benefit may assume the reinvestment of dividends. • 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 malus and clawback as described on page 80.	• The Committee considers and approves the performance measures and targets at the start of each year and ensures they are aligned with business strategy and are sufficiently stretching. • Financial metrics will comprise at least 50% of AIP opportunity. The balance of the AIP opportunity will be based on financial metrics and/or non-financial metrics such as 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 between 0% and 100%. Up to 60% of the maximum potential will be earned for on-target performance. • The Committee may amend the pay-out if the formulaic output does not reflect its assessment of overall business performance.	• Maximum: 150% of salary. • The combined AIP and LTIP maximum opportunities for any year may not exceed 250% of salary.

Element	Purpose and link to strategy	Operation	Performance metrics	Maximum opportunity
Long-Term Incentive Plan (LTIP)	• Aligned to main strategic objectives of delivering sustainable performance which in turn should deliver enhanced returns.	• Annual grant of performance shares, half of which vest after three years subject, ordinarily, to continued service and subject to performance targets, and half of which vest after five years (the final two years being subject only to continued service). Awards may be granted as conditional awards or nil or nominal cost options. • LTIP performance will be measured over three years. • LTIP awards may include the right to receive a benefit (in cash or in shares) determined by reference to the value of dividends that would have been paid on vested shares by reference to dividend record dates in the period from grant to vesting. The benefit may assume the reinvestment of dividends. • Awards may be subject to malus and clawback as described below.	• The performance condition will be based on key metrics aligned to the business strategy, including but not limited to EPS, return measures and cash-based measures. • At least 50% of the opportunity will be subject to an EPS performance measure. • Up to 25% of the maximum is earned for threshold performance, 100% for maximum with straight line vesting usually applying between these points.	• LTIP awards with a face value of not more than 150% of salary. • The combined AIP and LTIP maximum opportunities for any year may not exceed 250% of salary.
SAYE Scheme	• Offered to all 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. • Operated under HMRC requirements as a tax qualifying plan.	• N/A	• Participation on the same basis as all 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, personal pension arrangements and/or a cash supplement.	• N/A	• 22% of base salary.
Other Benefits	• To aid retention and be competitive in the market place. • Healthcare benefits in order to minimise business disruption.	• Company car (or car allowance) and fuel allowance. • Medical insurance. • Life assurance. • Other benefits as appropriate, for example, relocation expenses and travel and subsistence.	• N/A	• N/A
Share Ownership Guidelines	• Further alignment of interests between Costain Board and shareholders.	• Executive directors are expected to build and maintain a shareholding of not less than 100% of base salary (or 200% of salary should the annual LTIP opportunity exceed 100% of salary). Shares subject to LTIP awards for which the performance period has ended and which are subject, ordinarily, only to continued employment (or subject to an LTIP or SDP award where the award is exercisable but not exercised) count towards the shareholding guideline, on a net of assumed tax basis. Executive directors are required to retain half of the shares acquired pursuant to the LTIP and SDP (after sales to cover tax) until the shareholding guideline is met.	• N/A	• N/A

NOTES

Performance measures

The choice of the performance metrics applicable to the AIP reflects the Committee's aim that our annual incentives should balance the delivery of stretching financial performance with non-financial indicators, particularly health and safety targets, and specific individual objectives. The LTIP financial metrics capture long-term earnings performance and if appropriate, may be extended to include return based and cash measures which we believe are closely aligned with the financial performance expected by our shareholders. LTIP measures may also include strategic measures to incentivise the behaviours needed to deliver the Company's overall strategy.

AIP and LTIP performance measures may be adjusted if an event occurs which causes the Committee to consider that it would be appropriate to amend the performance measures (e.g. a material acquisition or divestment) so that they achieve their original purpose.

Recovery provisions

The AIP (including the deferred awards delivered under the SDP) and LTIP awards are subject to 'malus' and 'clawback' provisions as follows.

For up to two years following the payment of the cash element of an AIP award, the Committee may require repayment of all or part of the bonus in the event of a material misstatement or error in assessing performance measures which has led to an overpayment of the bonus or in the event of dismissal due to gross misconduct in the bonus year or in the event of criminal behaviour. Some or all of a deferred share award under the SDP may be clawed back (via a cancellation of the award) prior to vesting in equivalent circumstances.

For up to two years following the vesting of an LTIP award (or part of an LTIP award) the Committee may require the repayment of all or part of the award (which may be effected by the cancellation of unvested LTIP awards) in the event of a material misstatement or error in assessing performance measures which has led to an award vesting to a greater degree than would otherwise have been the case or in the event of dismissal due to gross misconduct.

Incentive plan operation

The Committee will operate the AIP, SDP and LTIP according to their respective rules.

Share awards under the SDP and LTIP (and any applicable performance conditions) may be adjusted in the event of a variation of the Company's share capital or a demerger, special dividend or other event which affects the market price of a share. Share awards under the SDP and LTIP may be satisfied in cash and may vest early, in accordance with the plan rules, in the event of a change of control or other relevant event (such as a winding-up or demerger). Where an LTIP award vests early, the extent of vesting will be determined taking into account the extent to which the performance condition has been satisfied (as assessed by the Committee) and, unless the Committee determines otherwise, the proportion of the vesting period that has elapsed. A copy of the plan rules is available on request from the company secretary.

Remuneration policy for chairman and non-executive directors is set out below.

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 usually 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. • Overall fees will remain within the limit set out in the Company's articles of association. • The chairman and non-executive directors do not participate in any variable pay or share scheme arrangement, although their fees may be paid in cash or shares. • May be entitled to benefits such as travel and subsistence and secretarial support, or other benefits as appropriate.	N/A
Share Ownership Guidelines	• Alignment of interests between Costain Board and shareholders.	• Non-executive directors are expected to build and maintain a shareholding of not less than 100% of their annual fee.	N/A

DIRECTORS' REMUNERATION REPORT CONTINUED
ANNUAL REPORT ON REMUNERATION

Governance of the Committee

The Remuneration 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 62. Biographies are shown on pages 54 and 55. The Committee is chaired by Alison Wood. The company secretary is 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. 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
10 February 2017	Consideration given to the extent to which the performance measures were likely to have been met with regard to the LTIP granted in 2014
	Approved the 2016 AIP annual cash bonuses subject to final audit of the 2016 accounts
	Approved the 2017 AIP performance measures and list of participants
	Approved indicative performance targets for the 2017 LTIP grant
	Noted the automatic vesting of the 2015 SDP Share Awards on 09 March 2017
	Reviewed the chairman's and non-executive directors' fees for 2017
	Approved the executive directors and senior executives salaries for 2017
	Reviewed risk and remuneration
	Approved revised shareholder guidelines
	Reviewed the Directors' Remuneration Report
05 April 2017	Granted awards under the 2017 LTIP
	Granted awards under the SDP relating to the 2016 year end AIP bonus
18 December 2017	Reviewed the performance targets and participants in respect of the proposed 2018 LTIP
	Reviewed the proposed 2018 AIP performance measures and list of participants
	Reviewed the 2018 annual salary increases for the executive directors, Executive Committee and the wider workforce

Advice provided to the Committee

Advice was sought, where appropriate, from a number of sources. During the course of the year, the chief financial officer, 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).

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 was appointed in place of New Bridge Street (a trading name of Aon Hewitt Limited) to act as the Company's remuneration consultants. Deloitte LLP received fees of £29,040 for the year ended 31 December 2017 in respect of services provided to the Committee.

Deloitte LLP is a founder signatory to the Remuneration Consulting Group's Code of Conduct and is considered by the Committee to be independent. During the year, Deloitte LLP also provided advice to the Company in relation to the operation of the Company's share plans, VAT and employment tax.

Voting on the Remuneration Report at the AGM in 2017

Last year's Remuneration Report was approved by shareholders with a 99.74% (2016 AGM: 99.68%) vote in favour (including discretionary votes).

Voting on the remuneration policy at the AGM in 2017

The current remuneration policy was approved by shareholders with a 98.24% vote in favour (including discretionary votes) at the Company's 2017 AGM.

Implementation of policy in the year to 31 December 2017

Single total figure of remuneration for each director

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

	2017						2016					
	Salary & fees £	Taxable benefits £	Pension * £	Annual Incentive £	LTIP ** £	Total £	Salary & fees £	Taxable benefits £	Pension *** £	Annual Incentive £	LTIP **** £	Total £
Executive directors												
A Wyllie	468,013	13,252	102,963	572,125	510,410	1,666,763	456,590	13,322	100,450	519,581	–	1,089,943
A O Bickerstaff	310,107	11,752	68,224	379,092	338,144	1,107,319	302,526	11,822	66,556	344,276	–	725,180
Non-executive chairman												
P Golby[1]	160,000	–	–	–	–	160,000	105,025	–	–	–	–	105,025
Non-executive directors												
J A Lodge	54,400	–	–	–	–	54,400	54,061	–	–	–	–	54,061
D McManus	45,000	–	–	–	–	45,000	44,823	–	–	–	–	44,823
J Morley	51,600	–	–	–	–	51,600	51,292	–	–	–	–	51,292
A J Wood	52,000	–	–	–	–	52,000	51,592	–	–	–	–	51,592
J de Rojas[2]	5,308	–	–	–	–	5,308	–	–	–	–	–	–
D P Allvey[3] (former chairman)	–	–	–	–	–	–	34,014	–	–	–	–	34,014

* A pension contribution of £12,500 was paid to Andrew Wyllie's chosen pension arrangement and the balance was paid to him directly as a taxable benefit. The amount quoted for Anthony Bickerstaff was paid to him directly as a taxable benefit.

** The value of the 2015 LTIP which is due to vest in 2018, subject to the Committee's determination (see note (c) below), is based on the average share price over the final three months of 2017, being 438 pence per share.

*** A pension contribution of £40,000 was paid to Andrew Wyllie's chosen pension arrangement and the balance was paid to him directly as a taxable benefit. The amount quoted for Anthony Bickerstaff was paid to him directly as a taxable benefit.

**** The 2014 LTIP did not vest in May 2017 as the performance measures were not met.

1 Appointed as non-executive chairman w.e.f. 05 May 2016.
2 Appointed as non-executive director w.e.f. 20 November 2017.
3 Retired as non-executive chairman w.e.f. 05 May 2016.

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 2017 (and their approximate values) were a car allowance of £12,000 (2016: £12,000) for Andrew Wyllie and £10,500 (2016: £10,500) for Anthony Bickerstaff, together with private medical insurance for both executive directors of £1,252 (2016: £1,322). This package of benefits was unchanged from 2016.

(b) Determination of the 2017 annual incentive

The maximum AIP opportunity for the chief executive and the chief financial officer for the year ended 31 December 2017 remained unchanged from 2016 at 150% of base salary, with one third of the earned AIP award to be deferred into shares for a further two years and two thirds of the earned AIP award paid in cash. Grants will be made under the SDP in April 2018.

The performance measures established by the Committee for the 2017 AIP continued to align reward with the Company's strategy while not encouraging inappropriate business risks to be taken. These included inter alia a maximum target of £52.3 million for Group EBITA.

DIRECTORS' REMUNERATION REPORT CONTINUED

The achievement of the performance measures has been reviewed, with appropriate input from the Audit Committee, following the end of the 2017 financial year. The maximum 2017 AIP opportunity against each of the performance measures is shown below, together with the AIP award actually achieved.

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

	AIP opportunity – maximum percentage of bonus		AIP award – as a percentage of bonus		AIP performance measure		
Performance measures	Andrew Wyllie	Anthony Bickerstaff	Andrew Wyllie	Anthony Bickerstaff	Threshold	Maximum	Actual performance
Group EBITA[1]	55%	55%	40%	40%	£43.8m	£52.3m	£49.0m
Group Health and Safety[2]	10%	10%	7%	7%	n/a	AFR 0.06	AFR 0.07[4]
Order Book (percentage of target gross profit)	10%	10%	9%	9%	£72.6m	£88.7m	£86.6m
Cash Flow[3] (average month end cash balance)	10%	10%	10%	10%	£54.8m	£67m	£86m
Personal Performance	15%	15%	15%	15%	see personal performance section below		
Total	100%	100%	81%	81%			

1 Calculated on an adjusted basis as approved by the Committee.
2 Includes leadership of health and safety engagement and culture.
3 Measured pre-acquisition and investments. The cash flow for assessing AIP performance was adjusted to remove exceptional cash inflow at the end of 2016 and 2017.
4 AFR of 0.07 represents a record safety performance for the Group.

Personal performance

Personal performance was based on the delivery of project and corporate activities critical to the strategic development of the business which were the personal responsibility of the executive directors. Details of the executive directors' performance against their personal objectives is set out below.

Andrew Wyllie

Personal objective	Actual performance	Personal weighting	Award
Increase the strategic development of the business through appropriate activity, in particular: • meeting technology and consulting objectives across the Group and • progression with closing out obligations on Greater Manchester Waste.	A number of key strategic and corporate activity objectives have been met in 2017 including: • the development of the Group's smart infrastructure solutions company positioning • the consulting, advisory and technology activities have grown by over 25% as targeted and • a successful consensual termination was achieved on the legacy Greater Manchester Waste PFI contract. In addition, the Group has put in place an industry leading wellbeing programme including the training and introduction of over 200 mental health first aiders in the Company. The Company is highly regarded by the analysts, all with BUY recommendations and an increasing understanding of the Company's differentiation and clear focused strategy.	15%	15%

Anthony Bickerstaff

Personal objective	Actual performance	Personal weighting	Award
Increase the strategic development of the business through appropriate activity, in particular: • corporate activity • development of consulting and advisory services across the Group and • senior leadership succession and personal development.	A number of key strategic and corporate activity objectives have been met in 2017 including: • the development of the Group's smart infrastructure solutions company positioning • the consulting, advisory and technology activities have grown by over 25% as targeted and • a number of successful internal appointments have been made in the year. In addition, the Group has put in place an industry leading wellbeing programme including the training and introduction of over 200 mental health first aiders in the Company. The Company is highly regarded by the analysts, all with BUY recommendations and an increasing understanding of the Company's differentiation and clear focused strategy.	15%	15%

(c) Vesting of the 09 March 2015 LTIP award

The LTIP award granted on 09 March 2015 was based on performance to the year ended 31 December 2017.

100% of this award is subject to the following performance measure:

Aggregate EPS for the financial years ended 31 December 2015, 2016 and 2017	Vesting level
Below 83.90 pence	0%
83.90 pence	15%
Between 83.90 pence and 96.9 pence	15% – 100% pro rata
96.9 pence or more	100%

For the purposes of the LTIP, EPS is adjusted by the Committee to take account of relevant events (such as acquisitions or disposals) and to ensure that the performance measures are assessed on a consistent basis year-to-year. Aggregate EPS for the financial years ended 31 December 2015, 2016 and 2017, calculated on an adjusted basis approved by the Committee, was 93.7 pence. As a result of which the LTIP award granted on 09 March 2015 is due to vest by 79.1%.

	Number of shares granted	Number of shares due to vest 1 and 2	Number of shares due to lapse 1	Number of dividend shares due to vest 3 and 4	Total shares due to vest 1 and 2	Estimated value 3
Andrew Wyllie	141,710	112,092	29,618	4,440	116,532	£510,410
Anthony Bickerstaff	93,883	74,261	19,622	2,941	77,202	£338,144

1 Subject to the Committee's official determination that the performance measure has been met and to any other adjustment.
2 50% of the award is subject to a two-year holding period.
3 Value based on the average share price over the final three months of the financial year ended 31 December 2017, being 438 pence per share.
4 Relating to 50% of the award vesting and capable of exercise three years after grant only. Additional dividend shares will also be payable on the 50% of the award subject to a two-year holding period.

(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 £2,392 (2016: £2,236) and £1,585 (2016: £1,482) 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 of £160,000.

(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 Committees. The annual fees set with effect from 1 April 2017 were as follows:

2017 Fees	Basic Fee	Senior independent director	Audit Committee chair	Remuneration Committee chair
Fees	£45,000	£6,600	£9,400	£7,000

Grants made during the year

These tables and the associated footnotes have been audited by PwC LLP.

2017 LTIP Grant

Grants were made under the LTIP on 05 April 2017. 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 the achievement of performance measures (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 2017 LTIP are as follows:

(A) EPS performance measures (relating to 75% of the award):

Aggregate EPS over the financial years ended 31 December 2017, 2018 and 2019	Vesting level
Below 101.4 pence	0%
101.4 pence	15%
113.6 pence or more	100%
Between 101.4 pence and 113.6 pence	Between 15% and 100% pro rata on a straight-line basis

(B) Cash conversion performance measures (relating to 25% of the award)

Cash conversion	Vesting level for awards
Below 80%	0%
80%	15%
100%	100%
Between 80% and 100%	Between 15% and 100% pro rata on a straight-line basis

The share awards granted under the 2017 LTIP are as follows:

	Number of shares	Face value[1]	End of performance period	Threshold vesting	Weighting (% of award)
Andrew Wyllie	103,491	£470,884	31 December 2019	15%	100%
Anthony Bickerstaff	68,573	£312,007	31 December 2019	15%	100%

1 Valued using the share price on the business day prior to the date of grant (04 April 2017), being 455 pence per share.

2017 SDP Grant

The Company granted awards under the Costain Share Deferral Plan (SDP) to the executive directors during 2017, details of which are shown on page 92.

All-employee share plan

The Company granted options under the Costain SAYE scheme to the executive directors during 2017, details of which are shown on page 92.

Implementation of policy in the year to 31 December 2018

Salary

For 2018, the Committee approved a 2.5% increase for the executive directors, effective 1 April 2018. A 2.5% salary increase budget will also be applied across the Company in 2018. The results of the salary review are set out in the table below:

	Salary 2018	Salary 2017	% change
Andrew Wyllie	£482,700	£470,885	2.5%
Anthony Bickerstaff	£319,800	£312,010	2.5%

Non-executive director fees

Non-executive directors' fees (basic fees only) are to increase by 2.5%, with effect from 1 April 2018, as shown in the table below:

2018 Fees	Basic Fee	Senior Independent director	Audit Committee chair	Remuneration Committee chair
Fees	£46,125	£6,600	£9,400	£7,000

2018 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 are clearly aligned with the delivery of our strategy. Their achievement will be reviewed, with appropriate input from the Audit Committee, at the end of the year.

The maximum bonus opportunity for the chief executive and the chief financial officer for the year ending 31 December 2018 will remain unchanged from 2017 at 150% of base salary, with one third of earned bonus deferred into shares for a further two years, to be awarded under the SDP, and two thirds of earned AIP paid in cash.

The performance measures for the 2018 AIP are as follows:

Performance measures	2018 AIP opportunity – maximum percentage of bonus	
	Andrew Wyllie	Anthony Bickerstaff
Group EBITA	50%	50%
Group health and safety	10%	10%
Order book percentage of target gross profit	10%	10%
Cash flow (average month end cash balances)	10%	10%
Personal performance	20%	20%
Total	100%	100%

The Committee has chosen not to disclose in advance the performance targets for the year ending 31 December 2018, as these include items which the Committee considers commercially sensitive. The Committee will continue to provide retrospective disclosure of performance targets in next year's Annual Report on Remuneration to the extent the Committee determines these targets are not commercially sensitive.

2018 LTIP Grant

The grant level for the executive directors remains at 100% of salary. Subject to the achievement of performance measures 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 anticipated that the grant of the 2018 LTIP award will take place in April 2018.

It is proposed that the 2018 LTIP awards will be subject to EPS performance (75% of the award) and cash conversion performance (25% of the award).

It is proposed that the targets for the 2018 LTIP award will be as follows:

EPS performance measure

Sum of the EPS for the financial years ending 31 December 2018, 2019 and 2020	Vesting level for awards
Below 117.2 pence	0%
117.2 pence	15%
128.9 pence or more	100%
Between 117.2 pence and 128.9 pence	Between 15% and 100% pro rata on a straight-line basis

The Committee believes that EPS remains an 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 shall be calculated on an adjusted basis as determined by the Committee to take account of relevant events (such as acquisitions or disposals) and ensure that the performance measures are assessed on a consistent basis year-to-year.

Cash conversion performance measure

Cash conversion	Vesting level for awards
Below 80%	0%
80%	15%
100%	100%
Between 80% and 100%	Between 15% and 100% pro rata on a straight-line basis

Cash conversion is adjusted cash flow from operations (excluding cash movements in provisions and pension deficit) divided by EBITDA. It is measured as average cash flow conversion over the three-year period ending 31 December 2020.

Adjusted cash flow from operations for the year ending 31 December 2018 will be adjusted to recognise the timing of cash inflows at the end of 2017.

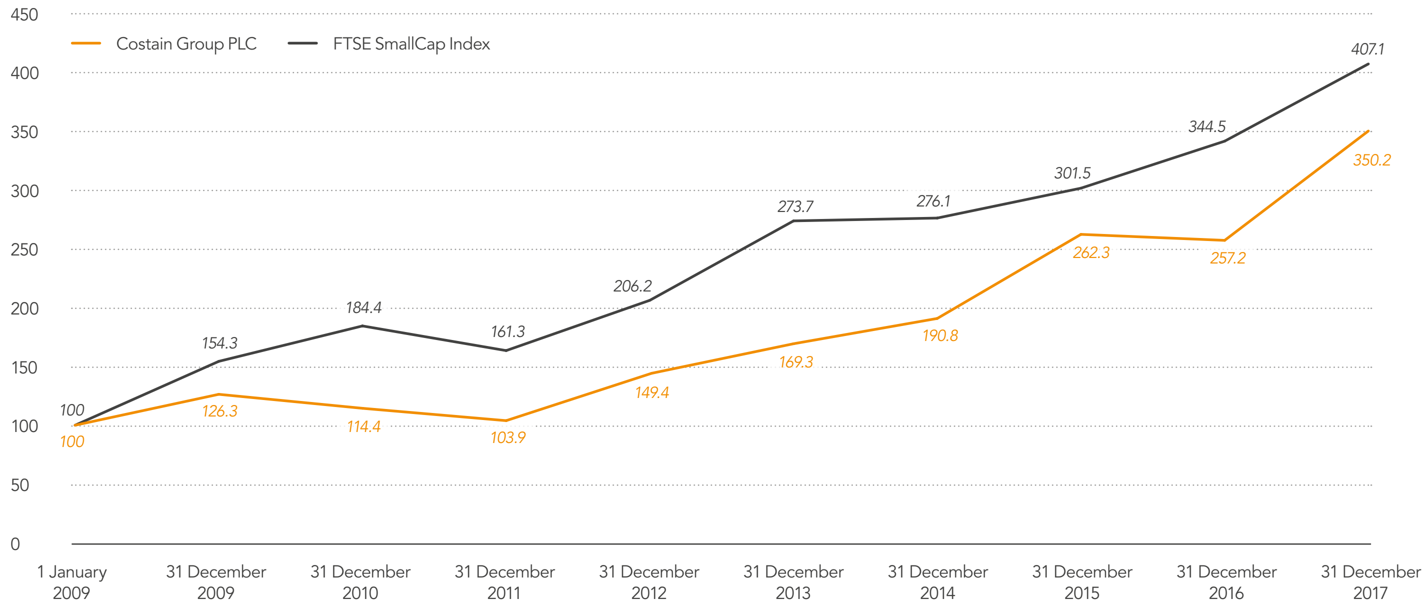
The Committee has the discretionary power to vary these targets, should circumstances change, so that the original targets are no longer considered appropriate, for example in the case of a material acquisition or divestment in the Group.

A clawback and malus provision is incorporated in the AIP and the LTIP 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, to 31 December 2017, of £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 a more appropriate index to use than the FTSE All-Share Index as it is the index in which the Company is a constituent and comprises companies of a similar size to Costain.



Source: Thomson Reuters Datastream

Change in chief executive's remuneration

	Year ending 31 December								
	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total remuneration	£887,814	£1,603,014	£1,228,332	£1,089,337	£1,251,239	£1,329,007	£1,414,381	£1,089,943	£1,666,763
AIP (%)	84%	94%	86%	55%	75%	71.6%	79.8%	75.4%	81%
LTIP vesting (%)	Nil%	96%	100%	100%	50%	50%	50%	nil%	79.1%

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.

	2017	2016	% change
Chief executive			
– salary	£468,013	£456,590	2.5%
– benefits	£13,252	£13,322	0%
– bonus (annual incentive)[1]	£572,125	£519,581	10.1%
Average per employee			
– salary[2]	£45,893	£43,936	4.5%
– benefits[3]	£5,090	£4,735	7.4%
– bonus (annual incentive)[4]	£3,485	£3,148	10.7%

1 Bonus figures for the chief executive are calculated on the basis of the combined cash bonus actually achieved and the value of the share options that were granted/to be granted under the AIP.

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 are calculated on the total bonus payments made to monthly paid employees.

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 ended 31 December 2016 to the financial year ended 31 December 2017.

	2017 £m	2016 £m	% change
Overall expenditure on pay	222.0	216.1	3.5%
Dividend	13.7	11.8	16%

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]	Next AGM at which the director is required to stand for re-election
Andrew Wyllie	25 April 2005	Terminable on 12 months' notice	2018 AGM
Anthony Bickerstaff	3 March 2006	Terminable on 12 months' notice	2019 AGM
Paul Golby	5 May 2016	5 May 2019	2020 AGM
James Morley	9 January 2008	Close of 2018 AGM [2]	2018 AGM [2]
Jane Lodge	1 August 2012	1 August 2018	2019 AGM
Alison Wood	1 February 2014	1 February 2020	2020 AGM
David McManus	12 May 2014	12 May 2020	2018 AGM
Jacqueline de Rojas	20 November 2017	20 November 2020	2018 AGM

1 Expiry of Current Term is subject to:

(a) the appointment of a non-executive director can be terminated by reasonable notice on either side (of not less than one month)

(b) election is required at the AGM following their appointment, subsequent re-election at intervals of no more than three years and, for non-executive directors, re-election at each AGM if having served on the Board for more than nine years, in accordance with the Code and the Company's articles of association. Jacqueline de Rojas is therefore subject to election at the 2018 AGM following her appointment to the Board in November 2017, while Andrew Wyllie and David McManus are due to offer themselves for re-election at the 2018 AGM having served on the Board at the two proceeding AGMs without retiring.

2 James Morley will be retiring as a non-executive director at the conclusion of the 2018 AGM and will not therefore be seeking re-election to the Board.

External directorships

Andrew Wyllie was appointed as a non-executive director of Scottish Water in April 2009 and after completing two full terms of four years each stepped down as a non-executive director in April 2017. In respect of his appointment for the year ended 31 December 2017 he was paid £5,112 (2016: £20,400).

Andrew Wyllie was appointed as a non-executive director of Yorkshire Water Services Limited on 01 September 2017 and, in respect of his appointment for the year ended 31 December 2017, he was paid £16,667.

Anthony Bickerstaff was re-appointed, with effect from 12 November 2017, for a second three year term as a non-executive director and chair of the Audit Committee of Low Carbon Contracts Company Limited and Electricity Settlements Company Limited and, in respect of his appointment for the year ended 31 December 2017, he was paid £31,000 (2016: £31,000).

The executive directors have retained these fees in accordance with the policy set out in the Policy Report.

The following tables and the associated footnotes have been audited by PwC LLP.

Share awards under the Long-Term Incentive Plan (LTIP)

Details of the executive directors' participation in the LTIP are as follows:

Director	Date granted	Balance at 1 January 2017	Granted during year	Share price at date of grant	Vested during year	Lapsed during year	Market price at date of exercise	Average market price at date of sale/ retention of balance	Value of shares at date of sale/ retention of balance (excluding shares deducted to settle tax sold at market price on date of exercise)	Balance at 31 December 2017	Actual/ expected vesting date
Andrew Wyllie	07.05.14[1]	164,467	–	265p	–	164,467	n/a	n/a	n/a	–	n/a
	09.03.15[2]	141,710	–	316p	–	–	–	–	–	141,710	March 2018 March 2020
	06.04.16[3]	132,678	–	346.25p	–	–	–	–	–	132,678	April 2019 April 2021
	05.04.17[4]	–	103,491	455p	–	–	–	–	–	103,491	April 2020 April 2022
Anthony Bickerstaff	07.05.14[1]	108,959	–	265p	–	108,959	n/a	n/a	n/a	–	n/a
	09.03.15[2]	93,883	–	316p	–	–	–	–	–	93,883	March 2018 March 2020
	06.04.16[3]	87,913	–	346.25p	–	–	–		–	87,913	April 2019 April 2021
	05.04.17[4]	–	68,573	455p	–	–	–		–	68,573	April 2020 April 2022

1 100% of the award was 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. This award lapsed as the aggregate EPS performance target during the period was not met.

2 100% of the award is subject to an aggregate EPS target for the financial years ended 31 December 2015, 2016 and 2017 of 83.9 pence (15% vests) to EPS of 96.9 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 2017, while 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, ordinarily, the individual remains an employee or officer of the Company. This award is due to vest by 79.1% based on aggregate EPS performance during the period.

3 100% of the award is subject to an aggregate EPS target for the financial years ended 31 December 2016, 2017 and 2018 of 91.7 pence (15% vests) to EPS of 101.7 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 2018, while 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, ordinarily, the individual remains an employee or officer of the Company.

4 Performance targets are as follows:

(a) an EPS target (relating to 75% of the award) of 101.4p (for 15% vesting) and 113.6p (for 100% vesting), with vesting on a straight-line basis between the two; and

(b) a cash conversion target (relating to 25% of the award) of 80% (for 15% vesting) and 100% (for 100% vesting), with vesting on a straight-line basis between the two.

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 2019, while 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, ordinarily, the individual remains an employee or officer of the Company.

The LTIP awards, which are expressed as options, have a nil exercise price. At 29 December 2017, the derived mid-market price of the ordinary shares in the Company, as advised by the Company's brokers, was 467.75 pence. The range of the share price of the ordinary shares during 2017 was 357 pence to 489.75 pence.

DIRECTORS' REMUNERATION REPORT CONTINUED

Share awards under the Share Deferral Plan (SDP)

Details of the executive directors' participation in the SDP are as follows:

Director	Date granted	Balance at 1 January 2017	Granted during year	Share price at date of grant	Vested during year	Lapsed during year	Market price at date of exercise	Average market price at date of sale/retention of balance	Value of shares at date of sale/retention of balance (excluding shares deducted to settle tax sold at market price on date of exercise)	Balance at 31 December 2017	Actual/expected vesting date
Andrew Wyllie	09.03.15	48,999[1]	–	316.25p	48,999[3]	–	415p	413p	£112,815	–	March 2017[2]
	06.04.16	51,643[1]	–	346.25p	–	–	–	–	–	51,643[1]	April 2018[2]
	05.04.17	–	38,064[1]	455p	–	–	–	–	–	38,064[1]	April 2019[2]
Anthony Bickerstaff	09.03.15	34,140[1]	–	316.25p	34,140[3]	–	415p	413p	£78,602	–	March 2017[2]
	06.04.16	34,428[1]	–	346.25p	–	–	–	–	–	34,428[1]	April 2018[2]
	05.04.17	–	25,221[1]	455p	–	–	–	–	–	25,221[1]	April 2019[2]

1 Awards under the SDP are structured as options with a nil exercise price.

2 Awards become exercisable on or around the second anniversary of the date of grant in accordance with the Rules of the SDP and subject, ordinarily, to the continued employment of the participants. To the extent that the awards become exercisable, they will remain exercisable until the tenth anniversary of the date of grant.

3 In addition, dividend shares were awarded upon vesting – Andrew Wyllie: 2,541 shares; Anthony Bickerstaff: 1,770 shares.

Share Options under the SAYE Scheme (SAYE)

Details of the executive directors' SAYE options are as follows:

Director	Date granted	Balance at 1 January 2017	Granted during year	Exercise price	Exercised during year	Lapsed during year	Market price at date of exercise	Market price at date of retention	Value of shares at date of retention	Balance at 31 December 2017	Exercised/exercisable from/to
Andrew Wyllie	29.09.14	2,253	–	234.80p	2,253	–	431p	431p	£9,710	–	Nov 2017 May 2018
	28.09.15	1,834	–	314p	–	–	–	–	–	1,834	Nov 2018 May 2019
	26.09.16	645	–	279p	–	–	–	–	–	645	Nov 2019 May 2020
	25.09.17	–	1,319	357.40p	–	–	–	–	–	1,319	Nov 2020 May 2021
Anthony Bickerstaff	29.09.14	2,253	–	234.80p	2,253	–	431p	431p	£9,710	–	Nov 2017 May 2018
	28.09.15	1,834	–	314p	–	–	–	–	–	1,834	Nov 2018 May 2019
	26.09.16	1,251	–	279p	–	–	–	–	–	1,251	Nov 2019 May 2020
	25.09.17	–	1,289	357.40p	–	–	–	–	–	1,289	Nov 2020 May 2021

Directors' shareholdings

Details of the directors' share interests in the Company as at 31 December 2017, and at the date of this report, are as follows:

Director	Beneficially owned	Outstanding SDP awards	Outstanding LTIP awards	Outstanding SAYE awards	Shareholding guidelines (% of salary/fee)	Actual shareholding (% of salary/fee)
Andrew Wyllie[1]	422,419	89,707	377,879	3,798	100%	226.25%
Anthony Bickerstaff[1]	236,595	59,649	250,369	4,374	100%	190.71%
Paul Golby[2]	35,000	–	–	–	100%	69.44%
James Morley	47,111	–	–	–	100%	197.45%
Jane Lodge	24,658	–	–	–	100%	103.55%
Alison Wood	6,666	–	–	–	100%	28.84%
David McManus	0	–	–	–	100%	0%
Jacqueline de Rojas[3]	0	–	–	–	100%	0%

1 Part held by persons closely associated.

2 Held by persons closely associated.

3 Appointed as non-executive director w.e.f. 20 November 2017.

The executive directors are expected to build and maintain a shareholding of not less than 100% of base salary through the retention of vested share awards or through open market purchases. This increases to 200% of salary should the annual LTIP opportunity exceed 100% of salary. The non-executive directors are also expected to build and maintain a shareholding of 100% of their fee.

DIRECTORS' REPORT

The directors submit to the members their report and accounts of the Company for the year ended 31 December 2017.

The Governance Report on pages 54 to 93 and the Strategic Report on pages 1 to 53 (and in particular pages 28 and 30 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 dividend payments

Profit after tax for the financial year ended 31 December 2017 amounted to £32.6 million (2016: £26.4 million). An interim dividend of 4.75 pence per share (2016: 4.3 pence) amounting to £5.0 million (2016: £4.4 million) was paid on 20 October 2017. A final dividend at the rate of 9.25 pence per share (2016: 8.4 pence) amounting to £9.8 million (2016: £8.8 million) will also be recommended to shareholders at the Annual General Meeting (AGM) to be held on 8 May 2018. If approved, the dividend will be paid on 18 May 2018 to shareholders registered at close of business on 13 April 2018.

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.

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 2017 was £52,776,661.50, consisting of 105,553,323 ordinary shares of 50 pence each.

Further details of the share capital of the Company can be found in note 22 on page 145.

The awards granted in May 2014 under the 2012 Long-Term Incentive Plan (LTIP) matured as at 31 December 2016 but did not vest in May 2017 as the performance conditions had not been achieved. Details regarding the 2015 LTIP awards that are due to vest in March 2018 can be found in the Directors' Remuneration Report on page 85.

Share options granted under the Company's Save As You Earn Scheme (SAYE) in November 2014 (at an option price of 234.80p) matured as at 1 November 2017, resulting in the exercise of options as at 31 December 2017 over 702,223 ordinary shares of 50 pence each. Further details of the SAYE Scheme can be found on page 92 of the Directors' Remuneration Report.

At the 2016 AGM, 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. This authority was granted for a period of three years (until the conclusion of the 2019 AGM), which is in line with the guidelines of the Investment Association (IA) which requires shareholder approval to be sought to renew the directors' authority to offer a scrip dividend scheme at least once every three years.

In May 2017, 382,406 ordinary shares of 50 pence each were allotted to shareholders in respect of the final dividend for 2016 and, in October 2017, 63,867 ordinary shares of 50 pence each were allotted to shareholders in respect of the interim dividend for 2017. Further information on the scrip dividend scheme is set out on page 155. 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 Company's Share Dealing Code, whereby the directors and 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 31 December 2017 the Company had been notified, under the Disclosure Guidance and Transparency Rules issued by the Financial Conduct Authority (DTR5), of the following voting interests in its ordinary share capital:

Shareholder	Date of notification	Number of shares/ voting rights	% of voting rights	Number of shares/ voting rights attaching to financial instruments	% of voting rights	Aggregate % of voting rights
BlackRock Inc*	27/11/2017	5,684,695	5.39	1,489,803	1.41	6.80
JO Hambro Capital Management Group Limited*	23/11/2017	5,345,750	5.07	n/a	n/a	5.07

* Subsequent notifications received from JO Hambro Capital Management Limited that, with effect from 10 January 2018, they held a total interest in 5,186,629 shares representing 4.91% of the Company's issued share capital and from BlackRock Inc that, with effect from 26 February 2018, they held a total interest in 7,060,902 shares representing 6.68% of the Company's issued share capital.

Save as noted above in respect of JO Hambro Capital Management Limited and BlackRock Inc, the Company did not receive any further notifications pursuant to DTR5 in the period from 31 December 2017 to the date of this report (being a date not more than one month prior to the date of the Company's Notice of AGM).

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.

Authority to issue shares

The directors may only issue shares if authorised to do so by the articles of association or the shareholders in general meeting. At the Company's AGM held on 8 May 2017, shareholders granted an authority to the directors to allot ordinary shares up to an aggregate nominal amount of £17.3 million. As at 31 December 2017, the only shares that had been allotted were in order to satisfy awards under the Company's share schemes and scrip dividends.

As this authority is due to expire on 8 May 2018, shareholders will be asked to renew and extend the authority, given to the directors at the last AGM, to allot shares in the Company, or grant rights to subscribe for, or to convert any security into, shares in the Company for the purposes of Section 551 of the Companies Act 2006. Further details on the resolution are provided in the Notice of this year's AGM.

Disapplication of pre-emption rights

If the directors wish to allot new shares and other equity securities, or sell treasury shares, for cash (other than in connection with an employee share scheme) company law requires that these shares are offered first to shareholders in proportion to their existing holdings. There may be occasions, however, when the directors need the flexibility to finance business opportunities by the issue of shares without a pre-emptive offer to existing shareholders. This cannot be done under the Companies Act 2006 unless the shareholders have first waived their pre-emption rights.

At the forthcoming AGM, shareholders will be asked to pass two special resolutions to grant the directors powers to disapply shareholders' pre-emption rights under certain circumstances. Further details on the resolutions are provided in the Notice of this year's AGM.

Power in relation to the Company buying back its own shares

The directors may only buy back shares if authorised to do so by the articles of association or by a special resolution of the shareholders at a general meeting. Any shares which have been bought back may be held as treasury shares, and either be resold for cash, cancelled (either immediately or in the future), or used for the purposes of the Company's share schemes. Any cancelled treasury shares will thereby reduce the amount of the Company's issued share capital. The Company did not buy back any of its shares during the year ended 31 December 2017 or during the period from 1 January 2018 to the date of this report.

At the forthcoming AGM authority will be sought from the shareholders to grant authority for the Company to repurchase up to 10% of the issued share capital of the Company. Further details on the resolution are provided in the Notice of this year's AGM.

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.

DIRECTORS' REPORT CONTINUED

Employee Share Trust

As at 31 December 2017, ACS HR Solutions Share Plan Services (Guernsey) Limited, as Trustee of the Costain Group Employee Trust, held 0.32% of the issued share capital of the Company 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 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 2017 (2016: nil). The Company has a policy of not making donations to political organisations. As a precautionary measure, shareholder approval is being sought at the forthcoming AGM for the Company and its subsidiaries to make donations and/or incur expenditure which may be construed as 'political' by the wide definition of that term included in the relevant legislation. Further details on the resolution are provided in the Notice of this year's AGM.

Directors' interests

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 2017, are contained in the Directors' Remuneration Report, which appears on pages 76 to 93.

Independent auditors

PricewaterhouseCoopers LLP (PwC) were appointed as auditor of the Company at the 2017 AGM. The Board is proposing the re-appointment of PwC as auditor from the conclusion of the AGM in May 2018 until the conclusion of the next general meeting at which the accounts are laid before the Company. See pages 72 and 73 of the Audit Committee Report and the Notice of this year's 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 become terminable 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 as a result of a successful 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 30 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

Brief biographies of the present members of the Board are given on pages 54 and 55.

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.

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 AGM of the Company and is then eligible for reappointment.

At every AGM of the Company, any director who has been appointed by the Board since the last AGM, or who held office at the time of the two preceding AGMs 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 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.

The Company may, by special resolution, remove any director before the expiration of his/her period of office. The office of a director shall also be vacated under a number of situations which are set out in the articles of association of the Company. These include a director wishing to resign, being required to step down due to ill health, becoming bankrupt or being prohibited by law from being a director.

Diversity

Details of the Company's policy on diversity within the business (including at Board level), is provided in the Nomination Committee Report on page 75 and the Strategic Report on page 19.

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.

Employee information

The average number of employees within the Company and Group is shown in note 5 to the financial statements on page 125.

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. Regular staff engagement surveys are run by the Company, the results of which are communicated to employees.

Employees are also 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.

The Company also operates an all employee share plan enabling employees to become shareholders and build a stake in the future success of the Company.

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 auditor

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 auditor is 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

Tracey Wood
Company Secretary
1 March 2018

DIRECTORS' RESPONSIBILITY STATEMENT

The directors are responsible for preparing the annual report, the Directors' Remuneration Report and the 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 judgements 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 Directors' 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 which 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 for shareholders to assess the Company's and the Group's position and 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 or 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

Dr Paul Golby CBE	Andrew Wyllie CBE
Chairman	Chief Executive
1 March 2018	1 March 2018

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF COSTAIN GROUP PLC

Report on the audit of the financial statements

Opinion

In our opinion, Costain Group PLC's Group financial statements and Company financial statements (the financial statements):

- give a true and fair view of the state of the Group's and of the Company's affairs as at 31 December 2017 and of the Group's profit and the Group's and the Company's cash flows for the year then ended
- have been properly prepared in accordance with IFRSs as adopted by the European Union and, as regards the Company's financial statements, as applied in accordance with the provisions of the Companies Act 2006 and
- 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.

We have audited the financial statements, included within the annual report, which comprise: the consolidated statement of financial position as at 31 December 2017; the consolidated income statement; consolidated statement of comprehensive income and expense; consolidated statement of changes in equity; and consolidated cash flow statement for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

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

Independence

We remained independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Company.

Other than those disclosed in note 4 to the financial statements, we have provided no non-audit services to the Group or the Company in the period from 1 January 2017 to 31 December 2017.

Our audit approach

Overview

Materiality

- Overall Group materiality: £1.9 million (2016: £1.5 million), based on 5% of profit before tax.
- Overall Company materiality: £1.5 million (2016: £1.5 million), based on the lower of component materiality and statutory materiality (1% of total assets).

Audit scope

- We identified four reporting units, all UK based, which accounted for 97% of Group revenues and 70% of Group profit before tax.

Key audit matters

- Timing and accuracy of contract revenue and profit recognition including recoverability of amounts due from customers.
- Impairment of goodwill and other intangible assets.
- Valuation of defined benefit pension schemes' obligation.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF COSTAIN GROUP PLC CONTINUED

Our audit approach continued

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

We gained an understanding of the legal and regulatory framework applicable to the Group and the industry in which it operates, and considered the risk of acts by the Group which were contrary to applicable laws and regulations, including fraud. We designed audit procedures at Group and significant component level to respond to the risk, recognising that the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. We focused on laws and regulations that could give rise to a material misstatement in the Group and Company financial statements, including, but not limited to, the Companies Act 2006, the Listing Rules, pensions legislation and UK tax legislation. Our tests included, but were not limited to, review of the financial statement disclosures to underlying supporting documentation, review of correspondence with the regulators, review of correspondence with legal advisors and enquiries of management. There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it.

We did not identify any key audit matters relating to irregularities, including fraud. As in all of our audits we also addressed the risk of management override of internal controls, including testing journals and evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.

Key audit matter	How our audit addressed the key audit matter
Group *Timing and accuracy of contract revenue and profit recognition including recoverability of amounts due from customers* The valuation of amounts recoverable on construction contracts is dependent on judgements around stage of completion and remaining costs to complete, as well as the associated provisions. In a number of the Group's projects there are assumptions within either revenue or cost of sales regarding recovery of contractual entitlement from clients or subcontractors, and value can be recorded within work in progress which is not yet certified or formally agreed. Provisions are recorded by the Group where there are concerns over recoverability. Refer to note 2 Accounting Policies on pages 114 to 121 of the annual report and the Audit Committee Report on pages 70 to 73 of the annual report.	We obtained an understanding of and evaluated management's own process and controls for reviewing long term contracts and gained an understanding of the key judgements involved and background to the specific contracts selected in our sample. We selected a sample of contracts for our testing, based on both quantitative and qualitative criteria including: • high levels of revenue recognised in the year • low margin or loss making contracts and • contracts with significant balance sheet exposure. For our sample, we focused on the significant judgements adopted by management in relation to the revenue and margin recognition, and, in particular, judgements with respect to the percentage completion, by: • obtaining an understanding of the contract and its particulars • agreeing forecast revenue to signed contracts, signed variations or other supporting documentation • tracing a sample of variations to supporting certifications or instructions from clients • holding discussions with management to understand and challenge areas of judgement taken • where necessary, reviewing legal correspondence and expert advice obtained in respect of those judgements • reconciling revenue recognised with amounts applied for and amounts certified by clients and confirming, using our industry knowledge and experience, that the reconciling items were appropriate
Group *Timing and accuracy of contract revenue and profit recognition including recoverability of amounts due from customers* continued	• re-performing the key calculations behind the margin applied, the profit taken and the stage of completion, as well as balance sheet exposure • assessing the recoverability of balance sheet items by comparing to external certification of the value of work performed and • agreeing forecast costs to complete to documentary evidence (such as orders signed with subcontractors or supporting calculations) and applying industry knowledge and experience to challenge the completeness of the forecast costs to completion. In addition, for the remaining contract population we performed the following: • reviewed the forecast margins for the population of contracts and for those which had moved significantly since tender and / or prior reporting periods, we obtained explanations from management • considered management provisions across all contracts and • recalculated the percentage completion based on costs to date and recalculated revenue to agree to those reported by management. Based on all of the evidence obtained in the above procedures, we are satisfied the values that have been determined by management as recoverable on contracts is supportable. Given the degree of estimation, we are also satisfied with the disclosures included on pages 32 to 37.
Group *Impairment of goodwill and other intangible assets* The assessment of the carrying value of goodwill and intangible assets involves complex and subjective judgements about the future results of the business.	We obtained the directors' future cash flow forecasts, which were prepared to a sufficiently detailed level. Initially, we evaluated management's basis of determination of the CGU's between Infrastructure and Natural Resources. The Natural Resources CGU has historically been loss making. We performed the following testing: • comparing the cash flows to the latest Board approved budgets, testing the integrity of the underlying calculations and assessed how both internal and external drivers of performance were incorporated into the projections • we challenged the discount rate used by independently recalculating the cost of capital, which was consistent with the discount rate used • we tested the level of secured work by tracing it to supporting orders • we tested the cost forecasts by comparing a sample to tenders from subcontractors or calculations of man hours required, noting that 90% of the 2018 forecast revenue has been secured • we compared 2017 financial performance to budget and understood the drivers of improvement in profitability and • we performed sensitivity analysis around the key drivers of the cash flow forecasts, in particular the revenue growth and margin assumptions. We concluded management's assessment was reasonable.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF COSTAIN GROUP PLC CONTINUED

Our audit approach continued

Key audit matter	How our audit addressed the key audit matter
Group *Valuation of defined benefit pension schemes' obligation* The pension obligation is material to the Group and subject to a number of assumptions which require expert involvement, are judgemental and subject to specific accounting standards (to determine the methodology).	We obtained the actuarial valuation at 31 December 2017 and tested the valuation of the pension liabilities as follows: We agreed the discount and inflation rates used in the valuation of the pension liability to our internally developed benchmarks, finding these to be within an acceptable range. Our benchmarks are based on our view of relevant economic indicators. • we discussed with the directors the rationale for the discount rate they used, the methodology used to derive it was appropriate • we tested the directors' assumptions around inflation and mortality rates by comparing them to, and finding them consistent with, national and industry averages, recognising the particular economic and health and safety factors that affect the construction industry • we tested the underlying census data to supporting documents to confirm completeness and accuracy and • we performed a reconciliation of the valuation results to the IAS 19 liability at 31 December 2017. We did not identify any issues within our testing and were satisfied the assumptions applied are within an appropriate range.

We determined that there were no key audit matters applicable to the Company to communicate in our report.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the Group and the Company, the accounting processes and controls, and the industry in which they operate.

The Group is primarily UK based and has two main segments; Infrastructure and Natural Resources. There is also a non-core overseas segment Alcaidesa, based in Spain. In establishing the overall approach to the Group audit, we determined the type of work needed to be performed at these reporting units. Making up the Group's reporting segments, we identified the following legal entities required a full scope audit; Costain Limited, Costain Oil and Gas Process Limited, Costain Engineering & Construction Limited and Costain Group PLC, which in our view, required an audit of their entire financial information, either due to their size or their risk characteristics. In addition to this we performed work over specific balances in other Group entities, which in our view, required an audit of such balances, either due to their size or their risk characteristics. The required work was performed by the Group team. Alcaidesa was audited by a local component team, based on full scope instructions issued by the Group engagement team. The Group engagement team remained in contact throughout the component team's work. All component materiality allocations were based on the Group profit before tax.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Company financial statements
Overall materiality	£1.9 million (2016: £1.5 million).	£1.5 million (2016: £1.5 million).
How we determined it	5% of profit before tax.	5% of profit before tax.
Rationale for benchmark applied	Based on the benchmarks used in the annual report, profit before tax is the primary measure used by the shareholders in assessing the performance of the Group, and is a generally accepted auditing benchmark.	We believe that profit before tax is the primary measure used by the shareholders in assessing the performance of the entity, and is a generally accepted auditing benchmark.

For each component in the scope of our Group audit, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £0.9m and £1.9m. Certain components were audited to a local statutory audit materiality that was also less than our overall Group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £100,000 (Group audit) (2016: £74,500) and £100,000 (Company audit) (2016: £74,500) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Going concern

In accordance with ISAs (UK) we report as follows:

Reporting obligation	Outcome
We are required to report if we have anything material to add or draw attention to in respect of the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the directors' identification of any material uncertainties to the Group's and the Company's ability to continue as a going concern over a period of at least twelve months from the date of approval of the financial statements.	We have nothing material to add or to draw attention to. As not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's and Company's ability to continue as a going concern.
We are required to report if the directors' statement relating to Going Concern in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.	We have nothing to report.

Reporting on other information

The other information comprises all of the information in the annual report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report, Directors' Report and Corporate Governance Statement, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, the Companies Act 2006, (CA06), ISAs (UK) and the Listing Rules of the Financial Conduct Authority (FCA) require us also to report certain opinions and matters as described below (required by ISAs (UK) unless otherwise stated).

Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 31 December 2017 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the Group and Company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report. (CA06)

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF COSTAIN GROUP PLC CONTINUED

Reporting on other information continued

Corporate Governance Statement

In our opinion, based on the work undertaken in the course of the audit, the information given in the Corporate Governance Statement (on pages 67 to 69) about internal controls and risk management systems in relation to financial reporting processes and about share capital structures in compliance with rules 7.2.5 and 7.2.6 of the Disclosure Guidance and Transparency Rules sourcebook of the FCA (DTR) is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the group and company and their environment obtained in the course of the audit, we did not identify any material misstatements in this information. (CA06)

In our opinion, based on the work undertaken in the course of the audit, the information given in the Corporate Governance Statement (on page 59) with respect to the Company's corporate governance code and practices and about its administrative, management and supervisory bodies and their committees complies with rules 7.2.2, 7.2.3 and 7.2.7 of the DTR. (CA06)

We have nothing to report arising from our responsibility to report if a corporate governance statement has not been prepared by the Company. (CA06)

The directors' assessment of the prospects of the group and of the principal risks that would threaten the solvency or liquidity of the group

We have nothing material to add or draw attention to regarding:

- The directors' confirmation on page 46 of the annual report that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity.
- The disclosures in the annual report that describe those risks and explain how they are being managed or mitigated.
- The directors' explanation on pages 44 and 45 of the annual report as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We have nothing to report having performed a review of the directors' statement that they have carried out a robust assessment of the principal risks facing the Group and statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the UK Corporate Governance Code (the Code); and considering whether the statements are consistent with the knowledge and understanding of the Group and Company and their environment obtained in the course of the audit (Listing Rules).

Other Code provisions

We have nothing to report in respect of our responsibility to report when:

- The statement given by the directors, on page 98, that they consider the annual report taken as a whole to be fair, balanced and understandable, and provides the information necessary for the members to assess the Group's and Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and Company obtained in the course of performing our audit.
- The section of the annual report on pages 70 to 73 describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.
- The directors' statement relating to the Company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified, under the Listing Rules, for review by the auditors.

Directors' remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006. (CA06)

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Directors' Responsibilities Statement set out on page 98, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group's and the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or the Company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an Auditors' Report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our Auditors' Report.

Use of this report

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

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

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

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the Audit Committee, we were appointed by the members on 8 May 2017 to audit the financial statements for the year ended 31 December 2017 and subsequent financial periods. This is therefore our first year of uninterrupted engagement.

Jonathan Hook

(Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP Chartered Accountants and Statutory Auditors London

1 March 2018

CONSOLIDATED INCOME STATEMENT YEAR ENDED 31 DECEMBER

	Notes	2017 Before other items £m	2017 Other items £m	2017 Total £m	2016 Before other items £m	2016 Other items £m	2016 Total £m
Continuing operations							
Revenue including share of revenue of joint ventures and associates	3	**1,728.9**	**–**	**1,728.9**	1,658.0	–	1,658.0
Less: Share of revenue of joint ventures and associates	13	**(44.9)**	**–**	**(44.9)**	(84.3)	–	(84.3)
Group revenue		**1,684.0**	**–**	**1,684.0**	1,573.7	–	1,573.7
Cost of sales		**(1,596.2)**	**–**	**(1,596.2)**	(1,497.7)	–	(1,497.7)
Gross profit		**87.8**	**–**	**87.8**	76.0	–	76.0
Administrative expenses before other items		**(39.1)**	**–**	**(39.1)**	(34.9)	–	(34.9)
Amortisation of acquired intangible assets		**–**	**(3.2)**	**(3.2)**	–	(4.6)	(4.6)
Employment related and other deferred consideration		**–**	**(1.2)**	**(1.2)**	–	(1.6)	(1.6)
Group operating profit		**48.7**	**(4.4)**	**44.3**	41.1	(6.2)	34.9
Share of results of joint ventures and associates	13	**0.3**	**–**	**0.3**	0.2	–	0.2
Profit from operations	3	**49.0**	**(4.4)**	**44.6**	41.3	(6.2)	35.1
Finance income	7	**0.4**	**–**	**0.4**	0.6	–	0.6
Finance expense	7	**(6.0)**	**(0.1)**	**(6.1)**	(4.4)	(0.4)	(4.8)
Net finance expense		**(5.6)**	**(0.1)**	**(5.7)**	(3.8)	(0.4)	(4.2)
Profit before tax	3/4	**43.4**	**(4.5)**	**38.9**	37.5	(6.6)	30.9
Taxation	8	**(6.9)**	**0.6**	**(6.3)**	(5.1)	0.6	(4.5)
Profit for the year attributable to equity holders of the parent		**36.5**	**(3.9)**	**32.6**	32.4	(6.0)	26.4
Earnings per share							
Basic	9	**34.8p**	**(3.7)p**	**31.1p**	31.5p	(5.8)p	25.7p
Diluted	9	**34.2p**	**(3.6)p**	**30.6p**	30.7p	(5.7)p	25.0p

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

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME AND EXPENSE
YEAR ENDED 31 DECEMBER

	2017 £m	2016 £m
Profit for the year	**32.6**	26.4
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of foreign operations	**0.5**	4.2
Net investment hedge:		
* Effective portion of changes in fair value during year	**(0.7)**	(3.7)
* Net changes in fair value transferred to the income statement	**0.2**	–
Cash flow hedges:		
* Effective portion of changes in fair value during year	**(1.4)**	1.9
* Net changes in fair value transferred to the income statement	**0.3**	–
Total items that may be reclassified subsequently to profit or loss	**(1.1)**	2.4
Items that will not be reclassified to profit or loss:		
Remeasurement of defined benefit obligations	**39.2**	(49.8)
Tax recognised on remeasurement of defined benefit obligations	**(7.4)**	7.6
Total items that will not be reclassified to profit or loss	**31.8**	(42.2)
Other comprehensive income/(expense) for the year	**30.7**	(39.8)
Total comprehensive income/(expense) for the year attributable to equity holders of the parent	**63.3**	(13.4)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER

	Notes	2017 £m	2016 £m
Assets			
Non-current assets			
Intangible assets	11	**62.5**	65.9
Property, plant and equipment	12	**43.0**	42.2
Investments in equity accounted joint ventures	13	**0.3**	0.3
Investments in equity accounted associates	13	**0.8**	0.6
Loans to equity accounted associates	13	**1.6**	1.7
Other	14	**4.9**	7.7
Deferred tax	8	**10.1**	14.9
Total non-current assets		**123.2**	133.3
Current assets			
Inventories		**1.4**	3.6
Trade and other receivables	14	**287.8**	299.1
Cash and cash equivalents	15	**248.7**	210.2
Total current assets		**537.9**	512.9
Total assets		**661.1**	646.2
Equity			
Share capital	22	**52.8**	52.1
Share premium		**12.1**	8.8
Foreign currency translation reserve		**2.3**	2.3
Hedging reserve		**0.8**	1.9
Retained earnings		**86.0**	34.5
Total equity attributable to equity holders of the parent		**154.0**	99.6
Liabilities			
Non-current liabilities			
Retirement benefit obligations	21	**23.9**	73.5
Other payables	19	**1.3**	1.0
Interest bearing loans and borrowings	16	**60.6**	30.1
Provisions for other liabilities and charges	20	**–**	0.4
Total non-current liabilities		**85.8**	105.0
Current liabilities			
Trade and other payables	19	**402.5**	397.2
Taxation	8	**7.1**	3.4
Interest bearing loans and borrowings	16	**10.4**	39.9
Provisions for other liabilities and charges	20	**1.3**	1.1
Total current liabilities		**421.3**	441.6
Total liabilities		**507.1**	546.6
Total equity and liabilities		**661.1**	646.2

The financial statements were approved by the Board of directors on 1 March 2018 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	2017 £m	2016 £m
Assets			
Non-current assets			
Investments in subsidiaries	13	**108.1**	105.4
Total non-current assets		**108.1**	105.4
Current assets			
Trade and other receivables	14	**139.3**	134.4
Cash and cash equivalents	15	**–**	–
Total current assets		**139.3**	134.4
Total assets		**247.4**	239.8
Equity			
Share capital	22	**52.8**	52.1
Share premium		**12.1**	8.8
Other reserves		**22.2**	19.5
Hedging reserve		**(0.2)**	–
Retained earnings		**59.3**	59.7
Total equity attributable to equity holders of the parent		**146.2**	140.1
Liabilities			
Non-current liabilities			
Interest bearing loans and borrowings	16	**60.0**	30.0
Provisions for other liabilities and charges	20	**0.9**	1.1
Total non-current liabilities		**60.9**	31.1
Current liabilities			
Trade and other payables	19	**28.5**	27.2
Taxation	8	**1.5**	1.5
Interest bearing loans and borrowings	16	**10.2**	39.9
Provisions for other liabilities and charges	20	**0.1**	–
Total current liabilities		**40.3**	68.6
Total liabilities		**101.2**	99.7
Total equity and liabilities		**247.4**	239.8

The financial statements were approved by the Board of directors on 1 March 2018 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	Retained earnings £m	Total equity £m
At 1 January 2016	51.1	6.2	1.8	–	61.5	120.6
Profit for the year	–	–	–	–	26.4	26.4
Other comprehensive income/(expense)	–	–	0.5	1.9	(42.2)	(39.8)
Issue of ordinary shares under employee share option plans	0.9	1.9	–	–	(0.3)	2.5
Shares purchased to satisfy employee share schemes	–	–	–	–	(1.4)	(1.4)
Equity-settled share-based payments	–	–	–	–	2.3	2.3
Dividends paid	0.1	0.7	–	–	(11.8)	(11.0)
At 31 December 2016	52.1	8.8	2.3	1.9	34.5	99.6
At 1 January 2017	**52.1**	**8.8**	**2.3**	**1.9**	**34.5**	**99.6**
Profit for the year	**–**	**–**	**–**	**–**	**32.6**	**32.6**
Other comprehensive income/(expense)	**–**	**–**	**–**	**(1.1)**	**31.8**	**30.7**
Issue of ordinary shares under employee share option plans	**0.6**	**1.6**	**–**	**–**	**–**	**2.2**
Shares purchased to satisfy employee share schemes	**–**	**–**	**–**	**–**	**(1.4)**	**(1.4)**
Equity-settled share-based payments	**–**	**–**	**–**	**–**	**2.2**	**2.2**
Dividends paid	**0.1**	**1.7**	**–**	**–**	**(13.7)**	**(11.9)**
At 31 December 2017	**52.8**	**12.1**	**2.3**	**0.8**	**86.0**	**154.0**

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 after 1 January 2004, the date of adoption of IFRS, 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 foreign subsidiaries, including fair value movements on investment hedges.

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.

COMPANY STATEMENT OF CHANGES IN EQUITY

	Share capital £m	Share premium £m	Other reserve £m	Hedging reserve £m	Retained earnings £m	Total equity £m
At 1 January 2016	51.1	6.2	16.6	–	59.8	133.7
Comprehensive income	–	–	–	–	12.0	12.0
Issue of ordinary shares under employee share option plans	0.9	1.9	–	–	(0.3)	2.5
Equity-settled share-based payments granted to employees of subsidiaries	–	–	2.9	–	–	2.9
Dividends paid	0.1	0.7	–	–	(11.8)	(11.0)
At 31 December 2016	52.1	8.8	19.5	–	59.7	140.1
At 1 January 2017	**52.1**	**8.8**	**19.5**	**–**	**59.7**	**140.1**
Comprehensive income/(expense)	**–**	**–**	**–**	**(0.2)**	**13.3**	**13.1**
Issue of ordinary shares under employee share option plans	**0.6**	**1.6**	**–**	**–**	**–**	**2.2**
Equity-settled share-based payments granted to employees of subsidiaries	**–**	**–**	**2.7**	**–**	**–**	**2.7**
Dividends paid	**0.1**	**1.7**	**–**	**–**	**(13.7)**	**(11.9)**
At 31 December 2017	**52.8**	**12.1**	**22.2**	**(0.2)**	**59.3**	**146.2**

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.

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.

CONSOLIDATED CASH FLOW STATEMENT YEAR ENDED 31 DECEMBER

	Notes	2017 £m	2016 £m
Cash flows from/(used by) operating activities			
Profit for the year		**32.6**	26.4
Adjustments for:			
Share of results of joint ventures and associates	13	**(0.3)**	(0.2)
Finance income	7	**(0.4)**	(0.6)
Finance expense	7	**6.1**	4.8
Taxation	8	**6.3**	4.5
Depreciation of property, plant and equipment	4	**3.9**	6.4
Amortisation of intangible assets	4	**3.7**	5.2
Employment related and other deferred consideration		**1.2**	1.6
Shares purchased to satisfy employee share schemes		**(1.4)**	(1.4)
Share-based payments expense	5	**2.7**	2.9
Cash from operations before changes in working capital and provisions		**54.4**	49.6
Decrease/(increase) in inventories		**0.2**	(0.7)
Decrease/(increase) in receivables		**14.2**	(24.0)
Increase in payables		**3.4**	61.1
Movement in provisions and employee benefits		**(12.4)**	(14.7)
Cash from operations		**59.8**	71.3
Interest received		**0.3**	0.4
Interest paid		**(3.2)**	(2.4)
Taxation paid		**(5.3)**	(2.2)
Net cash from operating activities		**51.6**	67.1
Cash flows from/(used by) investing activities			
Dividends received from joint ventures and associates	13	**0.1**	0.2
Additions to property, plant and equipment	12	**(1.8)**	(7.0)
Additions to intangible assets	11	**(0.3)**	(0.1)
Proceeds of disposal of property, plant and equipment		**0.2**	0.1
Repayment of loans to joint ventures and associates	13	**0.1**	–
Acquisition related deferred consideration	18	**(2.4)**	(2.0)
Acquisition of subsidiaries (net of acquired cash and cash equivalents)	26	**–**	(16.3)
Net cash used by investing activities		**(4.1)**	(25.1)
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		**2.2**	2.5
Ordinary dividends paid	10	**(11.9)**	(11.0)
Drawdown of loans	16/17	**70.7**	90.1
Repayment of loans	16/17	**(70.0)**	(60.0)
Net cash (used by)/from financing activities		**(9.0)**	21.6
Net increase in cash, cash equivalents and overdrafts		**38.5**	63.6
Cash, cash equivalents and overdrafts at beginning of the year	15	**210.2**	146.7
Effect of foreign exchange rate changes		**–**	(0.1)
Cash, cash equivalents and overdrafts at end of the year	15	**248.7**	210.2

COMPANY CASH FLOW STATEMENT YEAR ENDED 31 DECEMBER

	Notes	2017 £m	2016 £m
Cash flows from/(used by) operating activities			
Profit for the year		**13.1**	12.0
Adjustments for:			
Finance income		**(14.9)**	(13.0)
Finance expense		**2.9**	2.3
Taxation		**(0.4)**	–
Cash from operations before changes in working capital and provisions		**0.7**	1.3
Increase in receivables		**(4.9)**	(34.5)
Increase in payables		**1.6**	1.0
Movement in provisions		**(0.1)**	(0.1)
Cash used by operations		**(2.7)**	(32.3)
Interest received		**0.6**	0.5
Interest paid		**(2.9)**	(2.3)
Taxation received		**0.4**	–
Net cash used by operating activities		**(4.6)**	(34.1)
Cash flows from investing activities			
Dividends received		**14.3**	12.5
Net cash from investing activities		**14.3**	12.5
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		**2.2**	2.5
Ordinary dividends paid	10	**(11.9)**	(11.0)
Drawdown of revolving credit facility	16/17	**70.0**	90.0
Repayment of loans	16/17	**(70.0)**	(60.0)
Net cash (used by)/from financing activities		**(9.7)**	21.5
Net decrease in cash and cash equivalents		**–**	(0.1)
Cash and cash equivalents at beginning of the year	15	**–**	0.1
Cash and cash equivalents at end of the year	15	**–**	–

NOTES TO THE FINANCIAL STATEMENTS

1 General information

Costain Group PLC (the Company) is a public limited company incorporated in the UK. The address of its registered office and principal place of business is disclosed on page 155 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 2017 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 1 March 2018.

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 judgements, 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 these form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. Judgements 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 18.

The Group's principal business activity involves delivering long-term contracts with a number of customers, virtually all in the UK. 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 in respect of going concern published by the Financial Reporting Council. 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. 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 2017:

- Recognition of Deferred Tax Assets for Unrealised Losses – amendments to IAS 12, and
- Disclosure initiative – amendments to IAS 7

The impact of these standards is limited to minor disclosure changes and the insertion of a net cash/(debt) reconciliation (note 17).

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, generally accompanied by a share of between 20% and 50% of the voting rights. 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.

(e) Joint operations are those joint arrangements over which joint control exists, established by contractual agreement, which are not legal entities 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, to the extent that the hedge is effective, are recognised directly in equity. Those exchange differences 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. Over 95% of the Group's revenue arises from long-term contracts.

(a) Long-term contracts

Revenue arises from increase in the value of work performed and 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.

Compensation events, variations and claims, gain from pain/gain arrangements and other bonus assessments are included in revenue where it is probable that the amount, which can be measured reliably, will be recovered from the customer and pain from pain/gain arrangements is included where incurred or expected to be incurred. 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

Contract 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, this includes amortisation of acquired intangibles and employment related and other deferred consideration. These are adjusted because they are not long term in nature and, hence, will not reflect the long-term performance of the Group.

Pre-contract costs

Costs associated with bidding for contracts are written off as incurred.

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, brand and intellectual property), computer software and patents. Customer relationships and other acquired intangibles are measured at the present value of cash flows attributable to the relationship less an appropriate contributory asset charge. Computer software and patents are 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
Other intangibles	– 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)
Marina (Alcaidesa)	– concession period (20 years remaining)
Golf courses (Alcaidesa)	– 50 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.

Impairment of non-financial assets

For the purposes of impairment testing, goodwill is allocated to 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.

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 (other than in relation to goodwill) 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 UK 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.

2 Summary of significant accounting policies continued

Taxation continued

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.

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 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 UK, which provides benefits based on pensionable salary. The details are included in note 21. 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.

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.

Certain derivative financial instruments are designated as cash flow hedges in line with established risk management policies. These 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. 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.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

2 Summary of significant accounting policies continued

Financial assets and liabilities continued

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 (ie 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.

Significant areas of judgement 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 judgement and estimation arise from the accounting for long-term contracts under IAS 11 'Construction Contracts', 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'.

Long-term contracts

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. Both cost and revenue forecasts 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. Cost forecasts take into account the expectations of work to be undertaken on the contract. Revenue forecasts take into account compensation events, variations and claims to the extent that the amounts the Group expects to recover can be reliably estimated and the receipt is probable and assessments of the impact of pain/gain arrangements.

Management bases its judgements 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, progress on discussions over compensation events, variations and claims with clients and forecasts of the costs to complete and, in certain limited cases, assessments of recoveries from insurers. 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.

Management believes it is reasonably possible, on the basis of existing knowledge, that outcomes within the next financial year could require material adjustment. Given the pervasive impact of judgements and estimates on revenue, cost of sales and related balance sheet amounts, it is difficult to quantify the impact of taking alternative assessments on each of the judgements above.

Carrying value of goodwill and intangible assets

Reviewing the carrying value of goodwill and intangible assets recognised on acquisition requires judgements, 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

Defined benefit pension schemes require significant judgements 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 21.

IFRSs not applied

The following IFRSs having been endorsed, will be applicable as stated below:

- IFRS 9 'Financial Instruments' – Published in July 2014 and replacing the existing guidance in IAS 39 'Financial Instruments: Recognition and Measurement' will be effective for the accounting period beginning 1 January 2018. 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.

  There is no material impact on the Group's consolidated financial statements resulting from the application of IFRS 9.

- IFRS 15 'Revenue from Contracts with Customers' was issued in May 2015 and will be effective for the Group for the accounting period beginning 1 January 2018.

  IFRS 15 replaces existing revenue recognition standards: IAS 11 'Construction Contracts' and IAS 18 'Revenue', and moves away from the 'risks and rewards' concept of revenue recognition used by IAS 18 to a concept of 'transfer of control'. Its core principle is that revenue should be recognised when (or as) an entity transfers control of goods or services to a customer. The standard is intended to bring greater transparency and comparability to financial reporting. The Group will adopt the modified retrospective transition approach to the standard.

  The main change for Costain from the adoption of IFRS is the separation of individual, distinct performance obligations within its framework and multiple revenue stream type contracts. Where the outcome of a long-term contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the whole contract. 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.

  Under IFRS 15, revenue will be spread over the expected life of each individual performance obligation rather than in line with the total costs profile. This results in a reduction in revenue recognised in periods prior to 1 January 2018 and a corresponding decrease in amounts due from customers for contract work in the statement of financial position of £5.7 million.

  This will be reflected by a decrease in opening retained earnings as at 1 January 2018 of £4.6 million, net of tax. It will reverse over the remaining periods of the contracts.

  There is no impact on the commercial activities, lifetime profitability or cash flows of the Group, as a result of the adoption of this accounting standard.

- IFRS 16 'Leases' replaces the existing accounting requirements in IAS 17 'Leases'. The adoption of IFRS 16 is mandatory for the Group for the accounting period beginning 1 January 2019. A single model for lessees will be required, eliminating off balance sheet accounting for non-exempt operating leases. As a result, lease liabilities and corresponding right of use lease assets will come onto the balance sheet and be unwound and depreciated over the term of the lease. The presentation and timing of income and expense recognition in the income statement will change, although the total income and expense over the term of the lease remains the same. There will be no impact on cash flows as the payments received or paid under the leases remain the same, although there will be a change in presentation of cash flows. The application of the new standard will have a varying impact on opening retained earnings at the initial date of adoption dependent upon which transition method is chosen.

  The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 16 and expects to disclose a range of estimates for the quantitative impact prior to initial adoption. It is not practicable to provide a reasonable estimate of the effect of IFRS 16 or to conclude on the transition approach to be taken until the detailed reviews have been completed.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

3 Operating segments

The Group has two core business segments: Natural Resources and Infrastructure plus the non core business Alcaidesa 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 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.

2017	Natural Resources £m	Infrastructure £m	Alcaidesa £m	Central costs £m	Total £m
Segment revenue					
External revenue	**333.5**	**1,345.2**	**5.3**	**–**	**1,684.0**
Share of revenue of joint ventures and associates	**10.4**	**34.5**	**–**	**–**	**44.9**
Total segment revenue	**343.9**	**1,379.7**	**5.3**	**–**	**1,728.9**
Segment profit/(loss)					
Operating profit/(loss)	**4.8**	**52.2**	**(1.4)**	**(6.9)**	**48.7**
Share of results of joint ventures and associates	**0.3**	**–**	**–**	**–**	**0.3**
Profit/(loss) from operations before other items	**5.1**	**52.2**	**(1.4)**	**(6.9)**	**49.0**
Other items:					
Amortisation of acquired intangible assets	**(1.1)**	**(2.1)**	**–**	**–**	**(3.2)**
Employment related and other deferred consideration	**(1.2)**	**–**	**–**	**–**	**(1.2)**
Profit/(loss) from operations	**2.8**	**50.1**	**(1.4)**	**(6.9)**	**44.6**
Net finance expense					**(5.7)**
Profit before tax					**38.9**
Segment profit/(loss) is stated after charging the following:					
Depreciation	**2.8**	**–**	**1.1**	**–**	**3.9**
Amortisation (including acquired intangible assets)	**1.9**	**1.7**	**0.1**	**–**	**3.7**
Segment assets					
Reportable segment assets	**117.6**	**248.0**	**35.1**	**1.6**	**402.3**
Unallocated assets:					
Deferred tax					**10.1**
Cash and cash equivalents					**248.7**
Total assets					**661.1**
Expenditure on non-current assets					
Property, plant and equipment	**0.4**	**0.6**	**0.8**	**–**	**1.8**
Intangible assets	**0.1**	**0.2**	**–**	**–**	**0.3**
Segment liabilities					
Reportable segment liabilities	**93.2**	**284.0**	**3.6**	**24.3**	**405.1**
Unallocated liabilities:					
Retirement benefit obligations					**23.9**
Borrowings					**71.0**
Taxation					**7.1**
Total liabilities					**507.1**

2016	Natural Resources £m	Infrastructure £m	Alcaidesa £m	Central costs £m	Total £m
Segment revenue					
External revenue	361.9	1,207.2	4.6	–	1,573.7
Share of revenue of joint ventures and associates	15.4	68.9	–	–	84.3
Total segment revenue	377.3	1,276.1	4.6	–	1,658.0
Segment profit/(loss)					
Operating profit/(loss)	(8.6)	56.6	(0.7)	(6.2)	41.1
Share of results of joint ventures and associates	0.2	–	–	–	0.2
Profit/(loss) from operations before other items	(8.4)	56.6	(0.7)	(6.2)	41.3
Other items:					
Amortisation of acquired intangible assets	(2.8)	(1.8)	–	–	(4.6)
Employment related and other deferred consideration	(1.4)	(0.2)	–	–	(1.6)
Profit/(loss) from operations	(12.6)	54.6	(0.7)	(6.2)	35.1
Net finance expense					(4.2)
Profit before tax					30.9
Segment profit/(loss) is stated after charging the following:					
Depreciation	3.6	1.7	1.1	–	6.4
Amortisation (including acquired intangible assets)	3.2	1.9	0.1	–	5.2
Segment assets					
Reportable segment assets	185.3	200.4	34.2	1.2	421.1
Unallocated assets:					
Deferred tax					14.9
Cash and cash equivalents					210.2
Total assets					646.2
Expenditure on non-current assets					
Property, plant and equipment	6.0	0.6	0.4	–	7.0
Intangible assets	0.1	–	–	–	0.1
Segment liabilities					
Reportable segment liabilities	127.8	244.2	3.4	24.3	399.7
Unallocated liabilities:					
Retirement benefit obligations					73.5
Borrowings					70.0
Taxation					3.4
Total liabilities					546.6

3 Operating segments continued

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.

2017	External revenue £m	Share of revenue of JVs and assoc's £m	Total segment revenue £m	Non-current assets £m
UK	**1,674.7**	**44.9**	**1,719.6**	**78.9**
Spain	**5.3**	**–**	**5.3**	**34.1**
Rest of the world	**4.0**	**–**	**4.0**	**0.1**
	1,684.0	**44.9**	**1,728.9**	**113.1**

2016	External revenue £m	Share of revenue of JVs and assoc's £m	Total segment revenue £m	Non-current assets £m
UK	1,564.4	84.3	1,648.7	86.9
Spain	4.6	–	4.6	31.4
Rest of the world	4.7	–	4.7	0.1
	1,573.7	84.3	1,658.0	118.4

Customers accounting for more than 10% of revenue

Three customers (2016: three) in the Infrastructure segment accounted for revenue of £1,005.7 million (2016: £1,028.2 million).

4 Other operating expenses and income

	2017 £m	2016 £m
Profit before tax is stated after charging:		
Amortisation of intangible assets (note 11)	**3.7**	5.2
Depreciation of property, plant and equipment (note 12)	**3.9**	6.4
Hire of plant and machinery	**46.9**	48.4
Rent of land and buildings	**4.6**	5.2
and after crediting:		
Income from sub-leases of land and buildings	**0.1**	0.1

Auditor's remuneration

	2017 £m	2016 £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	**0.4**	0.4
	0.5	0.5

An amount of less than £0.1 million was paid to the Group's auditor in 2017 (2016: less than £0.1 million) with regards to the independent review of the interim results and other non-audit services.

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

Group	2017 £m	2016 £m
Wages and salaries	**222.0**	216.1
Social security costs	**24.5**	23.5
Pension costs (note 21)	**8.9**	8.5
Share-based payments expense (note 21)	**2.7**	2.8
	258.1	250.9

	2017 Number	2016 Number
Average number of persons employed		
Natural Resources	**1,205**	1,555
Infrastructure	**2,825**	2,545
Alcaidesa	**67**	64
Central	**21**	26
	4,118	4,190

Of the above employees 93 were employed overseas (2016: 104).

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 2017 and 2016 are detailed below.

	2017 £m	2016 £m
Remuneration	**1.8**	1.7
Post-employment benefits	**0.2**	0.2
Gains made on the exercise of share-based plans	**1.2**	0.3
	3.2	2.2

7 Net finance expense

	2017 £m	2016 £m
Interest income from bank deposits	**0.2**	0.3
Interest income on loans to related parties	**0.2**	0.3
Finance income	**0.4**	0.6
Interest payable on bank overdrafts, interest bearing loans, borrowings and other similar charges	**(4.2)**	(3.3)
Unwind of discount on deferred consideration	**(0.1)**	(0.4)
Interest cost on the net liabilities of the defined benefit pension scheme (note 21)	**(1.8)**	(1.1)
Finance expense	**(6.1)**	(4.8)
Net finance expense	**(5.7)**	(4.2)

Other similar charges includes arrangement and commitment fees payable. Interest income on loans to related parties relates to shareholder loan interest receivable from investments in equity accounted joint ventures and associates.

8 Taxation

	2017 £m	2016 £m
On profit for the year		
UK corporation tax at 19.25% (2016: 20%)	**(10.7)**	(2.8)
Adjustment in respect of prior years	**1.8**	–
Current tax expense for the year	**(8.9)**	(2.8)
Deferred tax expense for the current year	**2.5**	(1.7)
Adjustment in respect of prior years	**0.1**	–
Deferred tax credit/(expense) for the year	**2.6**	(1.7)
Tax expense in the consolidated income statement	**(6.3)**	(4.5)

	2017 £m	2016 £m
Tax reconciliation		
Profit before tax	**38.9**	30.9
Taxation at 19.25% (2016: 20%)	**(7.5)**	(6.2)
Share of results of joint ventures and associates	**0.1**	0.1
Disallowed expenses and amounts qualifying for tax relief	**(1.9)**	(0.3)
Utilisation of previously unrecognised temporary differences	**0.9**	0.1
Research and development tax relief for the current year	**0.4**	0.5
Rate adjustment relating to deferred taxation and overseas profits and losses	**(0.2)**	1.3
Adjustments in respect of prior years, mainly research and development tax relief claims	**1.9**	–
Tax expense in the consolidated income statement	**(6.3)**	(4.5)
Effective rate of tax	**16.2%**	14.6%

The 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 £7.1 million (2016: £3.4 million) for the Group and £1.5 million (2016: £1.5 million) for the Company represent the amount of tax in respect of all outstanding periods.

Accumulated trading tax losses carried forward in the UK were £0.1 million (2016: £5.1 million).

Accumulated tax losses carried forward in Spain were £58.8 million (2016: £55.9 million).

	2017 £m	2016 £m
Deferred tax asset recognised		
Accelerated capital allowances	**1.6**	2.0
Short-term temporary differences	**0.6**	(4.3)
Retirement benefit obligations	**4.5**	14.0
Tax losses	**3.4**	3.2
Deferred tax asset	**10.1**	14.9

UK deferred tax assets have been recognised at 19.0% or 17.0% as applicable (2016: 19.0%) and Spanish tax losses have been recognised at 25.0% (2016: 25.0%).

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

	2017 £m	2016 £m
Analysis of deferred tax movements		
At 1 January	**14.9**	10.6
Deferred tax relating to business combinations		
Transfer in respect of acquired intangible assets	**–**	(1.1)
Currency realignment	**–**	0.5
	–	(0.6)
Deferred tax in consolidated income statement		
Accelerated capital allowances	**(0.4)**	0.4
Short-term temporary differences	**4.7**	(1.1)
Retirement benefit obligations	**(2.1)**	(1.0)
Tax losses	**0.4**	–
	2.6	(1.7)
Deferred tax in other comprehensive income and expense statement		
Retirement benefit obligations	**(7.4)**	7.6
Short-term temporary differences	**0.5**	–
	(6.9)	7.6
Deferred tax recognised directly in the consolidated statement of changes in equity		
Short-term temporary differences	**(0.5)**	(1.0)
At 31 December	**10.1**	14.9

Factors that may affect future tax charges

The rate of UK corporation tax reduces to 17% with effect from 1 April 2020. The deferred tax assets are reflected at the 17% rate or at 19% where the asset will unwind prior to April 2020.

The Group and Company have potential deferred tax assets in their UK 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	
	2017 £m	2016 £m	2017 £m	2016 £m
Accelerated capital allowances	**1.9**	2.2	**–**	–
Short-term temporary differences	**25.4**	19.9	**–**	–
Trading tax losses	**0.1**	4.9	**–**	–
Total temporary differences	**27.4**	27.0	**–**	–
In addition to the above temporary differences, the following gross deferred tax assets are available:				
Management expenses and charges incurred by Parent Company	**54.7**	55.6	**54.7**	55.6
Spanish tax losses carried forward	**40.7**	39.2	**–**	–
Capital losses	**270.6**	275.0	**241.0**	241.0

The current year tax effect, at 19.25%, of claiming short-term temporary differences and trading tax losses was £0.9 million (2016: £0.1 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.

9 Earnings per share

The calculation of earnings per share is based on profit of £32.6 million (2016: £26.4 million) and the number of shares set out below.

	2017 Number (millions)	2016 Number (millions)
Weighted average number of ordinary shares in issue for basic earnings per share calculation	**104.7**	102.8
Dilutive potential ordinary shares arising from employee share schemes	**2.0**	2.6
Weighted average number of ordinary shares in issue for diluted earnings per share calculation	**106.7**	105.4

At 31 December 2017, no options were excluded from the weighted average number of ordinary shares calculation because they were anti-dilutive (2016: 0.7 million options were excluded).

10 Dividends

	Dividend per share pence	2017 £m	2016 £m
Final dividend for the year ended 31 December 2015	7.25	**–**	7.4
Interim dividend for the year ended 31 December 2016	4.30	**–**	4.4
Final dividend for the year ended 31 December 2016	8.40	**8.7**	–
Interim dividend for the year ended 31 December 2017	4.75	**5.0**	–
Amount recognised as distributions to equity holders in the year		**13.7**	11.8
Dividends settled in shares		**(1.8)**	(0.8)
Dividends settled in cash		**11.9**	11.0

A final dividend in respect of the year ended 31 December 2017 of 9.25 pence per share, amounting to a dividend of £9.8 million, is to be proposed at the Annual General Meeting. If approved, the dividend is expected to be paid on 18 May 2018 to shareholders on the register as at 13 April 2018 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	Other intangibles £m	Total £m
Cost					
At 1 January 2016	40.8	12.6	7.2	8.6	69.2
Currency realignment	–	–	–	0.1	0.1
Acquired through business combinations	13.3	2.8	2.5	–	18.6
Additions	–	–	–	0.1	0.1
Disposals	–	–	–	(0.7)	(0.7)
At 31 December 2016	54.1	15.4	9.7	8.1	87.3
At 1 January 2017	**54.1**	**15.4**	**9.7**	**8.1**	**87.3**
Additions	**–**	**–**	**–**	**0.3**	**0.3**
At 31 December 2017	**54.1**	**15.4**	**9.7**	**8.4**	**87.6**
Amortisation					
At 1 January 2016	–	5.6	5.0	6.3	16.9
Provided in year	–	2.3	2.3	0.6	5.2
Disposals	–	–	–	(0.7)	(0.7)
At 31 December 2016	–	7.9	7.3	6.2	21.4
At 1 January 2017	**–**	**7.9**	**7.3**	**6.2**	**21.4**
Provided in year	**–**	**2.3**	**0.9**	**0.5**	**3.7**
At 31 December 2017	**–**	**10.2**	**8.2**	**6.7**	**25.1**
Net book value					
At 31 December 2017	**54.1**	**5.2**	**1.5**	**1.7**	**62.5**
At 31 December 2016	54.1	7.5	2.4	1.9	65.9
At 1 January 2016	40.8	7.0	2.2	2.3	52.3

The net book value of other acquired intangible assets includes £0.9 million (2016: £1.3 million) relating to order book.

Goodwill has been allocated to the applicable cash generating units of the Infrastructure segment (£15.5 million) and the Natural Resources segment (£38.6 million).

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 Infrastructure CGU was 9.8% and for the Natural Resources CGU was 10.2%.

The value in use calculations use the Group's three-year cash flow forecasts, which are based on the expected revenues of each CGU taking into account the current level of secured and anticipated orders, extrapolated for future years by the expected growth applicable to each CGU as follows:

Growth rates	Infrastructure %	Natural Resources %
Year 4	2.5	2.5
Year 5	1.5	2.5
Long-term average	1.5	1.5

11 Intangible assets continued

At 31 December 2017, based on the internal value in use calculations, management concluded that the recoverable value of the cash generating units exceeded their carrying amount.

There is substantial headroom on goodwill for both CGUs. Sensitivity analysis has been performed on the goodwill in relation to each CGU by changing the key assumptions applicable to each CGU. In respect of the Natural Resources segment, which has the smaller headroom, the assumptions would have to change as follows for any single assumption change to bring headroom down to £nil:

- Discount rate – increase from 10.2% to 16.5%;
- Growth rate – reduce from positive 2.5% to a negative value;
- Underlying operating margin – reduce forecast margin by 1.1%.

12 Property, plant and equipment

Group	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 January 2016	26.0	24.7	50.7
Currency realignment	4.2	0.5	4.7
Additions	0.2	6.8	7.0
Acquired through business combinations	–	0.1	0.1
Disposals	(0.5)	(0.4)	(0.9)
At 31 December 2016	29.9	31.7	61.6
At 1 January 2017	**29.9**	**31.7**	**61.6**
Reclassification from inventories	**2.0**	**–**	**2.0**
Currency realignment	**1.0**	**0.1**	**1.1**
Additions	**–**	**1.8**	**1.8**
Disposals	**–**	**(0.9)**	**(0.9)**
At 31 December 2017	**32.9**	**32.7**	**65.6**
Depreciation			
At 1 January 2016	1.3	12.1	13.4
Currency realignment	0.3	0.1	0.4
Provided in year	0.9	5.5	6.4
Disposals	(0.5)	(0.3)	(0.8)
At 31 December 2016	2.0	17.4	19.4
At 1 January 2017	**2.0**	**17.4**	**19.4**
Provided in year	**0.9**	**3.0**	**3.9**
Disposals	**–**	**(0.7)**	**(0.7)**
At 31 December 2017	**2.9**	**19.7**	**22.6**
Net book value			
At 31 December 2017	**30.0**	**13.0**	**43.0**
At 31 December 2016	27.9	14.3	42.2
At 1 January 2016	24.7	12.6	37.3

A piece of land at Alcaidesa in Spain was reclassified from inventories to land and buildings in 2017.

The £5.5 million provided in the prior year for plant and equipment includes an impairment of £1.4 million relating to a tunnel boring machine.

13 Investments and loans in subsidiaries, equity accounted joint ventures and associates

	Investments		Loans	
Group	Joint ventures £m	Associates £m	Associates £m	Total £m
Cost or fair value				
At 1 January 2016	14.4	0.1	1.7	16.2
At 31 December 2016	14.4	0.1	1.7	16.2
At 1 January 2017	**14.4**	**0.1**	**1.7**	**16.2**
Repayments	**–**	**–**	**(0.1)**	**(0.1)**
At 31 December 2017	**14.4**	**0.1**	**1.6**	**16.1**
Share of post-acquisition reserves				
At 1 January 2016	(14.0)	0.4		(13.6)
Dividends	(0.1)	(0.1)		(0.2)
Profit for the year	–	0.2		0.2
At 31 December 2016	(14.1)	0.5		(13.6)
At 1 January 2017	**(14.1)**	**0.5**		**(13.6)**
Dividends	**–**	**(0.1)**		**(0.1)**
Profit for the year	**–**	**0.3**		**0.3**
At 31 December 2017	**(14.1)**	**0.7**		**(13.4)**
Net book value				
At 31 December 2017	**0.3**	**0.8**	**1.6**	**2.7**
At 31 December 2016	0.3	0.6	1.7	2.6
At 1 January 2016	0.4	0.5	1.7	2.6

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

	2017			2016		
	Joint ventures £m	Associates £m	Total £m	Joint ventures £m	Associates £m	Total £m
Revenue	**44.0**	**0.9**	**44.9**	83.4	0.9	84.3
Profit before tax	**–**	**0.4**	**0.4**	–	0.3	0.3
Taxation	**–**	**(0.1)**	**(0.1)**	–	(0.1)	(0.1)
Profit for the year	**–**	**0.3**	**0.3**	–	0.2	0.2
Non-current assets	**0.1**	**–**	**0.1**	–	–	–
Current assets	**11.4**	**2.4**	**13.8**	15.7	2.5	18.2
Current liabilities	**(11.1)**	**(0.4)**	**(11.5)**	(15.4)	(0.6)	(16.0)
Non-current liabilities	**–**	**(1.3)**	**(1.3)**	–	(1.3)	(1.3)
Investments in joint ventures and associates	**0.4**	**0.7**	**1.1**	0.3	0.6	0.9
Dividends received by Group	**–**	**0.1**	**0.1**	0.1	0.1	0.2

Net interest payable by joint ventures and associates in 2017 was £nil (2016: £nil). The applicable interest rates during the year are income of 0.2% to 13.6% per annum (2016: 0.2% to 6.5%) and expense of 10.7% to 13.6% per annum (2016: 11.5%).

Analysis of the total revenue, income, assets and liabilities of joint ventures and associates

	2017			2016		
	Joint ventures £m	Associates £m	Total £m	Joint ventures £m	Associates £m	Total £m
Revenue	**127.4**	**2.2**	**129.6**	242.9	2.2	245.1
Profit/(loss) before tax	**–**	**1.0**	**1.0**	–	0.8	0.8
Taxation	**–**	**(0.2)**	**(0.2)**	–	(0.1)	(0.1)
Profit/(loss) for the year	**–**	**0.8**	**0.8**	–	0.7	0.7
Non-current assets	**0.2**	**–**	**0.2**	0.2	–	0.2
Current assets	**31.4**	**6.1**	**37.5**	44.9	6.1	51.0
Current liabilities	**(30.7)**	**(1.0)**	**(31.7)**	(44.2)	(1.4)	(45.6)
Non-current liabilities	**–**	**(3.2)**	**(3.2)**	–	(3.3)	(3.3)
Equity	**0.9**	**1.9**	**2.8**	0.9	1.4	2.3

Details of subsidiary undertakings, joint ventures, joint operations and associates are shown in note 25.

There is no other comprehensive income/(expense) in respect of joint ventures and the associates.

Company

Investments in subsidiaries	£m
Cost	
At 1 January 2016	371.7
Additions	2.9
At 31 December 2016	374.6
At 1 January 2017	**374.6**
Additions	**2.7**
At 31 December 2017	**377.3**
Amounts written off	
At 1 January 2016	(269.2)
At 31 December 2016	(269.2)
At 1 January 2017	**(269.2)**
At 31 December 2017	**(269.2)**
Net book value	
At 31 December 2017	**108.1**
At 31 December 2016	105.4
At 1 January 2016	102.5

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 subsidiaries in which the Company has an interest are set out in note 25.

14 Trade and other receivables

	Group		Company	
	2017 £m	2016 £m	2017 £m	2016 £m
Amounts included in current assets				
Trade receivables	**110.9**	101.8	**–**	–
Other receivables	**15.6**	44.3	**–**	–
Amounts due from customers for contract work	**140.8**	125.2	**–**	–
Prepayments and accrued income	**19.2**	24.2	**0.3**	1.0
Amounts owed by joint ventures and associates	**1.3**	3.6	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**139.0**	133.4
	287.8	299.1	**139.3**	134.4
Amounts included in non-current assets				
Other	**4.9**	7.7	**0.7**	–

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

14 Trade and other receivables continued

At 31 December 2017, amounts due from customers for contract work falling due within one year include retentions of £8.2 million (2016: £27.1 million) relating to long-term contracts in progress. Other receivables falling due after more than one year include retentions of £4.3 million (2016: £7.1 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.

The average credit period within trade receivables on amounts billed for contract work and on sales of goods is 33 days (2016: 35 days). The analysis of the due dates of the trade receivables was £93.5 million (2016: £82.4 million) due within 30 days, £16.7 million (2016: £19.3 million) due between 30 and 60 days and £0.7 million (2016: £0.1 million) due after 60 days.

These balances include receivables, with a carrying amount of £6.2 million (2016: £5.6 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 £2.3 million (2016: £1.0 million) overdue by less than 30 days, £0.9 million (2016: £0.7 million) overdue by between 30 and 60 days and £3.0 million (2016: £3.9 million) overdue by more than 60 days.

The provision for impairment of trade and other receivables is £0.6 million (2016: £0.3 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 £4,459.7 million (2016: £3,776.3 million). Progress billings and advances received from customers under open contracts amounted to £4,328,5 million (2016: £3,672.0 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 £87.8 million (2016: £68.1 million).

	Group		Company	
	2017 £m	2016 £m	2017 £m	2016 £m
Cash and cash equivalents	**248.7**	210.2	**–**	–
Cash and cash equivalents in the cash flow statement	**248.7**	210.2	**–**	–

16 Interest bearing loans and borrowings

	Group		Company	
	2017 £m	2016 £m	2017 £m	2016 £m
Current				
Revolving Credit Facility	**10.2**	39.9	**10.2**	39.9
Other loans	**0.2**	–	**–**	–
	10.4	39.9	**10.2**	39.9
Non-current				
Term Loan	**60.0**	30.0	**60.0**	30.0
Other loans	**0.6**	0.1	**–**	–
	60.6	30.1	**60.0**	30.0

The Group's borrowings facilities are described in note 18.

17 Cash flow information

Net cash/(debt) reconciliation

This section sets out an analysis of net cash/(debt) and movements in net cash/(debt) during the year.

	Group		Company	
	2017 £m	2016 £m	2017 £m	2016 £m
Cash and cash equivalents (note 15)	**248.7**	210.2	**–**	–
Borrowings – current (note 16)	**(10.4)**	(39.9)	**(10.2)**	(39.9)
Borrowings – non-current (note 16)	**(60.6)**	(30.1)	**(60.0)**	(30.0)
Net cash/(debt)	**177.7**	140.2	**(70.2)**	(69.9)

Group	Cash and cash equivalents £m	Borrowings – current £m	Borrowings – non-current £m	Total £m
Net cash/(debt) at 1 January 2016	146.7	(38.5)	–	108.2
Cash flows	63.6	–	(30.1)	33.5
Effect of foreign exchange rate changes	(0.1)	(1.4)	–	(1.5)
Net cash/(debt) at 31 December 2016	210.2	(39.9)	(30.1)	140.2
Net cash/(debt) at 1 January 2017	**210.2**	**(39.9)**	**(30.1)**	**140.2**
Cash flows	**38.5**	**29.8**	**(30.5)**	**37.8**
Effect of foreign exchange rate changes	**–**	**(0.3)**	**–**	**(0.3)**
Net cash/(debt) at 31 December 2017	**248.7**	**(10.4)**	**(60.6)**	**177.7**

Company	Cash and cash equivalents £m	Borrowings – current £m	Borrowings – non-current £m	Total £m
Net cash/(debt) at 1 January 2016	0.1	(38.5)	–	(38.4)
Cash flows	(0.1)	–	(30.0)	(30.1)
Effect of foreign exchange rate changes	–	(1.4)	–	(1.4)
Net cash/(debt) at 31 December 2016	–	(39.9)	(30.0)	(69.9)
Net cash/(debt) at 1 January 2017	**–**	**(39.9)**	**(30.0)**	**(69.9)**
Cash flows	**–**	**30.0**	**(30.0)**	**–**
Effect of foreign exchange rate changes	**–**	**(0.3)**	**–**	**(0.3)**
Net cash/(debt) at 31 December 2017	**–**	**(10.2)**	**(60.0)**	**(70.2)**

18 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. 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.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

18 Financial instruments – Fair values and risk management continued

a) Risk management continued

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 and bank facilities. 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 £96.9 million (2016: £69.1 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 2017, the Group had banking and bonding facilities, including a £131.0 million (2016: £125.0 million) Revolving Credit Facility and a £60.0 million (2016: £30.0 million) Term Loan, extending to 25 June 2022. The facilities, which were increased by £36.0 million and extended by one year during 2017, have financial covenants based on interest cover and leverage measured quarterly. The covenants are based on accounting standards already in force at the date of signing the facilities. The unsecured bonding facilities are set out below:

	Group and Company	
	2017 £m	2016 £m
Expiring between one and five years*	**320.0**	400.0
* Element of above facilities available for borrowings	**2.5**	2.5

At 31 December 2017, the utilisation of these bonding facilities amounted to £97.0 million (2016: £78.7 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 UK 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.

iv) Interest rate risk

The Group has cash balances in the UK and overseas and bank borrowings in the UK and Spain. The largest constituents are UK balances denominated in pounds sterling.

During the year ending 31 December 2017, the Group entered into interest rate swap arrangements that fixed the effective LIBOR interest rate on £60.0 million of borrowings up to June 2021 (2016: no interest rate hedging undertaken by the Group).

A 1% rise in interest rates would have increased the annual interest income on net cash balances by approximately £1.2 million (due to the interest rate swap noted above) (2016: £0.7 million).

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.

The Group's subsidiary, Alcaidesa Holding SA, a company based in Spain is denominated in euro. At the year-end, the net carrying value of the assets was £26.2 million (2016: £26.3 million). A 10% strengthening in the euro would have adversely impacted the results by £0.1 million (2016: £0.1 million).

The Group's investment in Alcaidesa Holding SA is hedged by euro currency sale contracts which mitigate the foreign currency risk arising from the subsidiary's net assets. The value of the forward sales contracts at 31 December 2017 was €28.0 million (2016: €30.5 million). The Group's investments in other subsidiaries are not hedged.

As a consequence, a 10% strengthening in the euro would have no impact on the statement of financial position (2016: £nil).

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.

Interest rate swaps are classified as cash flow hedges and stated at fair value based on a Level 2 valuation method using yield curves derived from prevailing market interest rates.

At 31 December 2017, the Group had foreign currency sale and purchase contracts designated as cash flow hedges of future transactions and interest rate swaps that fixed the effective LIBOR rate of £60.0 million of borrowings to June 2021. These are 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 (2016: none).

	2017				2016			
	Carrying amount £m	Contractual cash flows £m	Within one year £m	Between one and five years £m	Carrying amount £m	Contractual cash flows £m	Within one year £m	Between one and five years £m
Foreign exchange contracts:								
Purchases	**1.3**	**(17.5)**	**(8.3)**	**(9.2)**	2.8	(29.6)	(19.7)	(9.9)
Sales	**(0.1)**	**(3.2)**	**(0.6)**	**(2.6)**	(0.1)	11.8	8.6	3.2
	1.2	**(20.7)**	**(8.9)**	**(11.8)**	2.7	(17.8)	(11.1)	(6.7)
Interest rate swaps	**(0.2)**	**(1.8)**	**(0.5)**	**(1.3)**	–	–	–	–
	1.0	**(22.5)**	**(9.4)**	**(13.1)**	2.7	(17.8)	(11.1)	(6.7)

The expected impact on the income statement of the foreign exchange contracts is £nil and of the interest rate swaps is £0.5 million in 2018.

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.

i) Currency and maturity of financial assets

Financial assets not measured at fair value

	2017				2016			
	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	**241.9**	**241.9**	**–**	**–**	205.4	205.4	–	–
other	**6.8**	**6.8**	**–**	**–**	4.8	4.8	–	–
	248.7	**248.7**	**–**	**–**	210.2	210.2	–	–
Loans to joint ventures and associates:								
pounds sterling	**1.6**	**0.1**	**0.4**	**1.1**	1.7	0.1	0.4	1.2
Trade, other receivables and amounts owed by joint ventures and associates:								
pounds sterling	**131.5**	**126.6**	**4.9**	**–**	156.1	148.4	7.7	–
other	**1.2**	**1.2**	**–**	**–**	1.3	1.3	–	–
	132.7	**127.8**	**4.9**	**–**	157.4	149.7	7.7	–
Total financial assets not measured at fair value	**383.0**	**376.6**	**5.3**	**1.1**	369.3	360.0	8.1	1.2

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 £1.6 million (2016: £1.7 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.

18 Financial instruments – Fair values and risk management continued

c) Financial assets and liabilities continued

ii) Currency and maturity of financial liabilities

Financial liabilities not measured at fair value

	2017			2016		
	Total £m	Within one year £m	Between one and five years £m	Total £m	Within one year £m	Between one and five years £m
Term Loan - pounds sterling	**60.0**	**–**	**60.0**	30.0	–	30.0
Revolving Credit Facility:						
pounds sterling	**–**	**–**	**–**	30.0	30.0	–
euro	**10.2**	**10.2**	**–**	9.9	9.9	–
Other loans – euro	**0.8**	**0.2**	**0.6**	0.1	–	0.1
	71.0	**10.4**	**60.6**	70.0	39.9	30.1
Trade and other payables:						
pounds sterling	**194.9**	**194.3**	**0.6**	211.3	210.5	0.8
other	**3.0**	**3.0**	**–**	2.6	2.6	–
	197.9	**197.3**	**0.6**	213.9	213.1	0.8
Total financial liabilities not measured at fair value	**268.9**	**207.7**	**61.2**	283.9	253.0	30.9

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.

Financial liabilities measured at fair value

	2017			2016		
	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	**0.7**	**–**	**0.7**	1.8	1.6	0.2

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

	2017		2016	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other receivables (as above)	**127.8**	**4.9**	149.7	7.7
Amounts due from customers	**140.8**	**–**	125.2	–
Prepayments and accrued income	**19.2**	**–**	24.2	–
	287.8	**4.9**	299.1	7.7

	2017		2016	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other payables (as above)	**197.3**	**0.6**	213.1	0.8
Deferred consideration (as above)	**–**	**0.7**	1.6	0.2
Credit balances on long-term contracts	**5.8**	**–**	5.0	–
Accruals and deferred income	**199.4**	**–**	177.5	–
	402.5	**1.3**	397.2	1.0

iv) Effective interest rates of financial assets and liabilities

	2017	2016
Financial assets		
Cash and cash equivalents	0.0% to 0.4%	0.0% to 0.4%
Loans to joint ventures and associates	10.7% to 13.6%	10.0% to 11.5%

Financial liabilities

The Group has overdraft facilities, a Revolving Credit Facility (RCF), a Term Loan and other loans. The £60.0 million (2016: £30.0 million) Term Loan and £10.2 million (2016: £39.9 million) of the RCF was drawn at the year-end. Other loans totalled £0.8 million (2016: £0.1 million). These are unsecured and carry interest at floating rates at a margin over Base, LIBOR or EURIBOR. The effective LIBOR cost to the Group on £60.0 million of borrowings was fixed by the Group entering into interest rate swaps in 2017.

The Company's financial assets comprised cash at bank of £nil (2016: £nil) and trade and other receivables of £139.0 million (2016: £133.4 million) with £128.1 million (2016: £123.1 million) denominated in pounds sterling and £10.9 million (2016: £10.3 million) denominated in euros and all maturing within one year.

The Company's financial liabilities comprise trade and other payables of £28.5 million (2016: £27.2 million) denominated in pounds sterling, the £60.0 million (2016: £30.0 million) Term Loan denominated in pounds sterling and the £10.2 million RCF denominated in euro (2016: £39.9 million with £30.0 million denominated in pounds sterling and £9.9 million denominated in euro). The Term Loan matures between one and five years, all other liabilities mature within one year.

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
Deferred consideration	Discounted cash flows: The valuation models consider the present value of the contractual payments, discounted using a risk-adjusted discount rate.	Risk-adjusted discount rate (12.5%)	The estimated fair value would increase (decrease) if the risk-adjusted discount rate were lower (higher).
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. Interest rate swaps are measured by discounting the related cash flows using yield curves derived from prevailing market interest rates.	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.
Term Loan	Discounted cash flow.	Not applicable.

18 Financial instruments – Fair values and risk management continued

d) Measurement of fair value continued

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 2016	1.8
Addition charged to income statement (including unwind of discount)	2.0
Payments	(2.0)
At 31 December 2016	1.8
At 1 January 2017	**1.8**
Addition charged to income statement (including unwind of discount)	**1.3**
Payments	**(2.4)**
At 31 December 2017	**0.7**

There were no transfers out of Level 3 other than the payments made during the year.

Sensitivity analysis

For the fair value of the £0.7 million non-current deferred consideration, a change of the risk-adjusted discount rate by 10% would impact the profit or loss by less than £0.1 million. The amount payable is contractual and not dependent on performance.

19 Trade and other payables

	Group		Company	
	2017 £m	2016 £m	2017 £m	2016 £m
Current liabilities				
Trade payables	**161.9**	175.1	**–**	–
Other payables	**27.3**	30.8	**–**	–
Social security	**7.8**	7.1	**–**	–
Credit balances on long-term contracts	**5.8**	5.0	**–**	–
Accruals and deferred income	**199.4**	177.5	**0.6**	0.3
Deferred consideration	**–**	1.6	**–**	
Amounts owed to joint ventures and associates	**0.3**	0.1	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**27.9**	26.9
	402.5	397.2	**28.5**	27.2
Non-current liabilities				
Other payables	**0.6**	0.8	**–**	–
Deferred consideration	**0.7**	0.2	**–**	–
	1.3	1.0	**–**	–

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.

20 Provisions for other liabilities and charges

Group	Property £m	Other £m	Total £m
Current			
At 1 January 2016	1.1	0.9	2.0
Provided	–	0.2	0.2
Utilised	(0.4)	(0.4)	(0.8)
Released	(0.3)	–	(0.3)
At 31 December 2016	0.4	0.7	1.1
At 1 January 2017	**0.4**	**0.7**	**1.1**
Provided	**–**	**0.4**	**0.4**
Utilised	**(0.3)**	**(0.3)**	**(0.6)**
Reclassified from non-current	**0.3**	**0.1**	**0.4**
At 31 December 2017	**0.4**	**0.9**	**1.3**

	Property £m	Other £m	Total £m
Non-current			
At 1 January 2016	–	0.1	0.1
Provided	0.3	–	0.3
At 31 December 2016	0.3	0.1	0.4
At 1 January 2017	**0.3**	**0.1**	**0.4**
Reclassified to current	**(0.3)**	**(0.1)**	**(0.4)**
At 31 December 2017	**–**	**–**	**–**

Company	Funding obligations £m
Current	
At 1 January 2016	0.1
Utilised	(0.1)
At 31 December 2016	–
At 1 January 2017	**–**
Reclassified from non-current	**0.2**
Utilised	**(0.1)**
At 31 December 2017	**0.1**
Non-current	
At 1 January 2016	1.1
At 31 December 2016	1.1
At 1 January 2017	**1.1**
Reclassified to current	**(0.2)**
At 31 December 2017	**0.9**

Group

Property provisions relate to costs of vacant properties and will be utilised over the next year.

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

21 Employee benefits

(a) Pensions

A defined benefit pension scheme is operated in the UK and a number of defined contribution pension schemes are in place in the UK and overseas. Contributions are paid by subsidiary undertakings and, to the defined contribution schemes, by employees. The total pension charge in the income statement was £12.9 million comprising £11.1 million included in operating costs plus £1.8 million included in net finance expense (2016: £12.1 million, comprising £11.0 million in operating costs plus £1.1 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 2016 and this was updated to 31 December 2017 by a qualified independent actuary. At 31 December 2017, there were 2,829 retirees and 3,100 deferred members. The weighted average duration of the obligations is 17.3 years.

	2017 £m	2016 £m	2015 £m
Present value of defined benefit obligations	**(803.4)**	(827.5)	(687.4)
Fair value of scheme assets	**779.5**	754.0	650.7
Recognised liability for defined benefit obligations	**(23.9)**	(73.5)	(36.7)

Movements in present value of defined benefit obligations

	2017 £m	2016 £m
At 1 January	**827.5**	687.4
Interest cost	**21.9**	25.5
Remeasurements – demographic assumptions	**16.8**	–
Remeasurements – financial assumptions	**6.9**	153.0
Remeasurements – experience adjustments	**(34.5)**	(6.8)
Benefits paid	**(35.2)**	(31.6)
At 31 December	**803.4**	827.5

Movements in fair value of scheme assets

	2017 £m	2016 £m
At 1 January	**754.0**	650.7
Interest income	**20.1**	24.4
Remeasurements – return on assets	**28.4**	96.4
Contributions by employer	**12.5**	14.3
Administrative expenses	**(0.3)**	(0.2)
Benefits paid	**(35.2)**	(31.6)
At 31 December	**779.5**	754.0

Expense recognised in the income statement

	2017 £m	2016 £m
Administrative expenses paid by the pension scheme	**(0.3)**	(0.2)
Administrative expenses paid directly by the Group	**(1.9)**	(2.3)
Interest cost on the net liabilities of the defined benefit pension scheme	**(1.8)**	(1.1)
	(4.0)	(3.6)

Fair value of scheme assets	2017 £m	2016 £m
UK equities	**128.5**	116.2
Overseas equities	**104.2**	95.9
Multi-credit fund	**90.7**	87.1
Index linked gilts	**319.4**	311.0
PFI investments	**52.2**	51.6
Property	**22.1**	22.3
Absolute return fund	**52.8**	68.4
Cash	**9.6**	1.5
	779.5	754.0

All equities are quoted securities. The multi-credit fund invests in a portfolio of primarily floating rate debt of non-investment grade or unrated borrowers. The PFI investments is the portfolio of interests in 10 PFI investments transferred by the Group to The Costain Pension Scheme in 2010, 2012 and 2014. The absolute return fund targets a lower volatility return by investing primarily in long/short equity strategies.

The investment portfolio comprises 41% index linked gilts, which are targeted to hedge inflation risk, plus a portfolio of other assets targeted, as a whole, to generate a higher return over the long-term than the cost of the liabilities.

Quoted investments are valued at the prevailing bid, offer or middle market stock exchange or over-the-counter market prices. The loans in the multi-credit fund may be priced either using quotes from a pricing vendor (if available), a broker or at a level determined by the investment manager that is agreed with the fund. The index-linked gilts value is derived from executable bid and offer prices. The PFI investments are valued using a level 3 valuation method based on the future cash flows of the individual investments. The absolute return fund invests principally through the use of collective investment schemes as well as other entities or structures managed by pooled fund managers. Units in collective investment schemes are valued by reference to their most recently available price. The property investment is held within a limited partnership and is valued by the general partner in accordance with RICS valuation standards.

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)

	2017 %	2016 %	2015 %
Discount rate	**2.50**	2.70	3.80
Future pension increases	**2.90**	3.10	2.95
Inflation assumption	**3.10**	3.20	3.00

Weighted average life expectancy from age 65 as per mortality tables used to determine benefits at 31 December 2017 and 31 December 2016 is:

	2017		2016	
	Male (years)	Female (years)	Male (years)	Female (years)
Currently aged 65	**22.8**	**24.8**	22.2	24.7
Non-retirees currently aged 45	**24.5**	**26.7**	24.1	26.7

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	34.7	0.9
Decrease inflation, pension increases by 0.25%, decreases pension liability and reduces pension cost by	29.9	0.7
Increase life expectancy by one year, increases pension liability and increases pension cost by	15.0	0.4

21 Employee benefits continued

(a) Pensions continued

In accordance with the pension regulations, a triennial actuarial review of the Costain defined benefit pension scheme was carried out as at 31 March 2016. In February 2017, the valuation and an updated deficit recovery plan were agreed with the scheme Trustee resulting in cash contributions of £10.0 million for the 12 months to 31 March 2017 and then £9.6 million per annum (increasing annually with inflation) until the deficit is cleared, which would be in 2031 on the basis of the assumptions made in the valuation and agreed recovery plan.

In addition, as previously implemented, the Group will continue to make an additional contribution so that the total deficit contributions match the total dividend amount paid by the Company each year. Consequently, the total amount of contribution is anticipated to be at a similar level to that under the previous plan. Any additional payments in this regard would have the effect of reducing the recovery period in the agreed plan. The Group will also pay the expenses of administration in the next financial year.

Any surplus of deficit contributions to the Costain Pension Scheme would be recoverable by way of a refund, as the Group has the unconditional right to any surplus once all the obligations of the Scheme have been settled. Accordingly, the Group does not expect to have to make provision for these additional contributions arising from this agreement in future accounts.

Defined contribution schemes

Several defined contribution pensions are operated. The total expense relating to these plans was £8.9 million (2016: £8.5 million).

(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 2014 AGM that allows for conditional awards with a maximum face value of up to 100% of base salary to be awarded. Performance conditions, such as those based on earnings per share, are determined by the Remuneration Committee of the Board at the time of grant.

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 was satisfied by shares purchased by a trust on behalf of the Group, so did not dilute shareholder interests. The last grant under the DSBP was made in 2014 and vested on 31 March 2016.

Save As You Earn Scheme (SAYE)

The Company operates a SAYE scheme that is open to all eligible employees who pay a fixed amount from salary into a savings account each month and elect to save over three 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 tax, for share-based payment transactions with employees was £2.7 million (2016: £2.8 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 2016	2.2	0.5	0.8	3.7	246.9
Adjusted during the year	–	–	(0.1)	–	–
Forfeited during the year	(0.2)	–	–	(0.3)	273.5
Exercised during the year	(0.6)	(0.4)	–	(1.4)	209.9
Granted during the year	0.6	–	0.5	1.1	279.0
Outstanding at 31 December 2016	2.0	0.1	1.2	3.1	271.9
Outstanding at 1 January 2017	**2.0**	**0.1**	**1.2**	**3.1**	**271.9**
Forfeited during the year	**(0.8)**	**–**	**–**	**(0.3)**	**275.1**
Exercised during the year	**(0.1)**	**–**	**(0.3)**	**(0.9)**	**231.6**
Granted during the year	**–**	**–**	**–**	**1.1**	**357.4**
Outstanding at 31 December 2017	**1.1**	**0.1**	**0.9**	**3.0**	**315.5**
Exercisable at the end of the period	**–**	**–**	**–**	**0.1**	**234.8**

Share options outstanding at the end of the year had a weighted average remaining contractual life of 5.5 years (2016: 5.4 years).

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 £3.3 million (2016: £2.6 million). The prior year comparative has been revised to show the value of granted amounts in the year. Previously the value included AIP schemes notified in the year, but not granted. The assumptions used in valuing the grants were:

	2017	2016
Expected volatility	**20%**	20%
Expected life (years)	**2.7 – 5.0**	2.7 – 5.0
Risk-free interest rate	**1.9%**	1.5%
Expected dividend yield	**2.7%**	3.2%

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.

22 Share capital

	2017		2016	
	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	**104.2**	**52.1**	102.1	51.1
Issued in year (see below)	**1.3**	**0.7**	2.1	1.0
Shares in issue at end of year - ordinary shares of 50p each, fully paid	**105.5**	**52.8**	104.2	52.1

The Company's issued share capital comprised 105,553,323 ordinary shares of 50 pence each as at 31 December 2017.

On 19 May 2017, pursuant to the scrip dividend scheme, shareholders elected to receive 382,406 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 2016, and shareholders elected to receive a further 63,867 ordinary shares on 20 October 2017 in lieu of cash in respect of all or part of their interim dividend for the year ended 31 December 2017.

During 2017, the Company issued 103,134 shares on exercise of options granted under the 2013 3-year SAYE scheme.

During 2017, the Company issued 67,502 shares on exercise of options granted under the 2011 5-year SAYE scheme.

During 2017, the Company issued 702,223 shares on exercise of options granted under the 2014 3-year SAYE scheme.

All shares rank pari passu regarding entitlement to capital and dividends.

The share options outstanding at the year end are detailed in note 21. Details of the performance conditions and the options granted to executive directors are given in the Directors' Remuneration Report.

23 Contingent liabilities

Group

Group bank borrowing facilities and bank and surety bonding facilities are supported by cross-guarantees given by the Company and participating companies in the Group. There are contingent liabilities in respect of:

- performance bonds and other undertakings entered into in the ordinary course of business
- legal claims arising in the ordinary course of business and
- creditors of joint operations, which are less than the book value of their assets.

It is not anticipated that any material liabilities will arise from the contingent liabilities other than those provided for (note 20).

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 UK. At 31 December 2017, the potential liability was £23.9 million (2016: £73.5 million) on an IAS 19 basis and is included in these financial statements as disclosed in note 21.

24 Other financial commitments

Group

Operating lease commitments

Leases as lessee	2017 Land and buildings £m	2017 Other operating leases £m	2016 Land and buildings £m	2016 Other operating leases £m
Future aggregate minimum lease payments under non-cancellable leases:				
Within one year	**4.8**	**5.0**	4.3	4.6
Between one and five years	**13.4**	**5.6**	11.9	4.6
Later than five years	**2.9**	**–**	3.9	–
	21.1	**10.6**	20.1	9.2

Leases as lessor	Land and buildings 2017 £m	Land and buildings 2016 £m
Future aggregate minimum lease income under non-cancellable leases:		
Within one year	**0.1**	–
Between one and five years	**0.4**	–
	0.5	–

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 and computers under non-cancellable operating leases. None of the leases include contingent rents.

Company

The Company does not have any other financial commitments (2016: £nil).

25 Subsidiary undertakings, joint ventures, associates and joint operations

	Activity	Percentage of equity held	Registered office/principal place of business
Principal subsidiary undertakings			
Alcaidesa Holding SA	Golf Course and Marina Operations	100	(5)
Costain Ltd	Engineering, Construction and Maintenance	100	(1)
Costain Engineering & Construction Ltd	Holding and Service Company	100	(1)
Costain Integrated Services Ltd	Professional Services	100	(1)
Costain Integrated Technology Solutions Ltd	Technology Integration	100	(1)
Costain Oil, Gas & Process Ltd	Process Engineering	100	(1)
Costain Upstream Ltd	Engineering and Design Services	100	(2)
Richard Costain Ltd	Service Company	100	(1)

	Activity	Issued share capital £m	Percentage of equity held	Registered office/ principal place of business	Reporting date
Principal joint ventures					
ABC Electrification Ltd	Rail Electrification	–	33.3	(11)	31 March
4Delivery Ltd	Civil Engineering	–	40	(3)	31 March

The equity capital of the above are held by subsidiary undertakings with the exception of Richard Costain Ltd and Costain Engineering & Construction Ltd.

All undertakings operate mainly in the country of incorporation. See key to registered office/principal place of business at the bottom of this note.

All holdings are of ordinary shares except Richard Costain Ltd, where Costain Group PLC holds 100% of the ordinary and preference shares.

25 Subsidiary undertakings, joint ventures, associates and joint operations continued

	Activity	Percentage interest	Country of business
Major joint operations			
Alstom-Babcock-Costain Joint Venture – Edinburgh to Glasgow Rail Improvement Programme	Rail Engineering	33.3	UK
Alstom-Costain C644 Joint Venture – Traction power – Crossrail	Rail Engineering	32.5	UK
Alstom-Costain C650 Joint Venture – HV power supply – Crossrail	Rail Engineering	32.5	UK
A-one+ Integrated Highway Services – MAC 14	Engineering & Maintenance	33.3	UK
A-one+ Joint Venture – ASC area 12 – Highways England	Engineering & Maintenance	33.3	UK
A-one+ Joint Venture – ASC area 4 – Highways England	Engineering & Maintenance	33.3	UK
ATC Joint Venture – C610 – Crossrail	Rail Engineering	32.5	UK
Balfour Beatty-BmJV-Carillion-Costain Joint Venture – National Major Projects – Highways England	Civil Engineering	22	UK
CH2M-Costain Joint Venture – Area 14 M&R contract	Engineering & Maintenance	50	UK
Costain-CH2M UK – ESCC JV – East Sussex highway maintenance	Engineering & Maintenance	50	UK
Costain-Atkins-Black & Veatch Joint Venture – Thames Water AMP6	Engineering	70	UK
Costain-Carillion Joint Venture – M1 Widening and A5/M1 Link	Civil Engineering	50	UK
Costain-Galliford Try Joint Venture – M1 smart motorways	Civil Engineering	70	UK
Costain-Laing O'Rourke Joint Venture – Bond Street station	Civil Engineering	50	UK
Costain-MWH Joint Venture – Southern Water AMP6	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 C412 Joint Venture – Bond Street – Crossrail	Civil Engineering	50	UK
Costain-Skanska – HS2 Enabling works	Civil Engineering	50	UK
Costain-Skanska Joint Venture – A14 Cambridge to Huntingdon Improvement Scheme	Civil Engineering	50	UK
Costain-Skanska Joint Venture – NGT Tunnels, London	Civil Engineering	50	UK
Costain-Skanska Joint Venture – Paddington Station Bakerloo Line Link Project	Civil Engineering	50	UK
Costain-Vinci Construction Joint Venture – Shieldhall	Civil Engineering	50	UK
Costain-Vinci Joint Venture – M4 corridor around Newport	Civil Engineering	50	UK
CVB Joint Venture – Thames Tideway Tunnel East	Civil Engineering	40	UK
Educo UK Joint Venture – Bradford Schools	Building	50	UK
Galliford-Costain-Atkins Joint Venture – United Utilities	Engineering	42.5	UK
Skanska-Costain-Strabag S1 Joint Venture - HS2 Main Works	Civil Engineering	34	UK
Skanska-Costain-Strabag S2 Joint Venture - HS2 Main Works	Civil Engineering	34	UK
The ASP Batch Joint Venture – Severn Trent – Large capital schemes outside AMP6	Engineering	33.3	UK

In accordance with Section 409 of the Companies Act 2006 a full list of subsidiaries, associates, joint ventures and joint arrangements is required:

	Status	Percentage of equity held	Registered office/principal place of business
Other subsidiaries owned directly by Costain Group PLC			
Costain Civil Engineering Limited	Holding Company	100	(1)
Costain Investments Limited	Dormant	100	(13)
Costain USA Inc.	Holding Company	100	(6)
County & District Properties Limited	Trading	100	(1)
Renown Investments (Holdings) Limited	Trading	100	(1)
Lysander Services Limited	Trading	100	(1)
Other subsidiaries owned indirectly by Costain Group PLC			
AB Rhead & Associates Limited	Trading	100	(1)
Aguas De Alcaidesa SL	Trading	100	(5)
Alcaidesa Golf SL	Trading	100	(5)
Alcaidesa Servicios SA	Trading	100	(5)
Alway Associates (London) Limited	Dormant	100	(1)
Brunswick Infrastructure Services Limited	Trading	100	(1)
Calvert & Russell Limited	Trading	100	(1)
C-in-A Limited	Dormant	100	(1)
CLM Engineering (Overseas) Limited	Dormant	100	(1)
COGAP (Middle East) Limited	Holding Company	100	(1)
Construction Study Centre Limited	Trading	100	(1)
Costain Abu Dhabi Co WLL	Trading	49	(14)
Costain Alcaidesa Limited	Holding Company	100	(1)
Costain America Inc	Holding Company	100	(6)
Costain Building & Civil Engineering Ltd	Holding Company	100	(1)
Costain Construction (Botswana) (Pty) Ltd	Dormant	100	(7)
Costain Construction Limited	Dormant	100	(1)
Costain de Venezuela CA	Dormant	100	(23)
Costain Energy Solutions Limited	Trading	100	(1)
Costain Engineering & Construction (Overseas) Limited	Holding Company	100	(1)
Costain Engineering Services Inc	Dormant	100	(6)
Costain Holdings (Botswana) (Pty) Limited	Holding Company	100	(7)
Costain Holdings (Malaysia) Sdn Bhd	Dormant	100	(8)
Costain International Limited	Dormant	100	(1)
Costain (Malaysia) Sdn Bhd	Dormant	100	(8)
Costain Management Design Limited	Dormant	100	(1)
Costain Minerals Inc.	Dormant	100	(6)
Costain Mining Services Inc.	Dormant	100	(6)
Costain Oil, Gas & Process (Malaysia) Sdn Bhd	Dormant	100	(8)
Costain Oil, Gas & Process (Nigeria) Limited	Dormant	95	(24)
Costain Oil, Gas & Process (Overseas) Limited	Dormant	100	(1)
Costain Process Construction Limited	Dormant	100	(1)
EPC Offshore Limited	Dormant	100	(2)
International Commercial and Project Solutions Pty Limited	Trading	100	(19)
JBCC Rhead PTE Limited	Trading	100	(17)
L.R.R. Holdings Limited	Holding Company	100	(1)

25 Subsidiary undertakings, joint ventures, associates and joint operations continued

	Status	Percentage of equity held	Registered office/principal place of business
Promanex (Civils & Industrial Services) Limited	Dormant	100	(1)
Promanex (Construction & Maintenance Services) Limited	Dormant	100	(1)
Promanex Group Holdings Limited	Holding Company	100	(1)
Promanex Group Limited	Dormant	100	(1)
Promanex (Total FM & Environmental Services) Ltd	Trading	100	(1)
RG Bidco Limited	Trading	100	(1)
Rhead Group Holdings Ltd	Holding Company	100	(1)
Rhead Group Holdings (Australia) Pty Limited	Holding Company	100	(18)
Rhead Group Pty Limited	Trading / Disposed Nov 2017	100	(20)
Rhead Holdings Limited	Holding Company	100	(1)
Southview Holdings (Private) Limited	Trading	100	(25)
Southview Investments (Private) Limited	Trading	100	(25)
Sunland Mining Corporation (II)	Dormant	100	(6)
Westminster Plant Co. Limited	Dormant	100	(1)
Other joint ventures or associates owned indirectly by Costain Group PLC			
ACM Health Solutions Limited	Dormant	33.3	(4)
Brighton & Hove 4Delivery Ltd	Trading	49	(3)
Budimex & Costain SP ZO.O	Dormant	50	(22)
China Harbour-Costain Mexico S de RL de CV	Dormant	50	(21)
Gravitas Offshore Limited	Dormant	45	(9)
Integrated Bradford LEP FIN Co One Limited	Trading	40	(10)
Integrated Bradford LEP Limited	Trading	40	(10)
Integrated Bradford PSP Limited	Holding Company	50	(10)
Jalal Costain WLL	Dormant	49	(15)
L21 Lewisham PSP Limited	Holding Company	50	(12)
Lewisham Schools for the Future LEP Ltd	Trading	40	(12)
Nesma-Costain Process Co. Limited	Dormant	50	(16)

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. Dormant status means no or a very small number of transactions with activity winding down.

	Activity	Percentage interest	Country of business
Other joint operations, including completed			
ACTUS Joint Venture – Trawsfynydd nuclear power station active waste retrieval	Civil Engineering	25	UK
Amec-Costain-Jacobs Joint Venture – Magnox ILW Management Programme	Civil Engineering	33.3	UK
A-one+ Integrated Highway Services - MAC 7	Engineering & Maintenance	33.3	UK
A-one+ Integrated Highway Services – MAC 10	Engineering & Maintenance	25	UK
A-one+ Integrated Highway Services - MAC 12	Engineering & Maintenance	33.3	UK
Bachy Soletanche-Costain-Skanska Joint Venture – CTRL 240 – Stratford Box	Civil Engineering	33.3	UK
Black & Veatch-Costain Joint Venture – Margate & Broadstairs UWWTD Scheme – Southern Water	Civil Engineering	62	UK
Costain-Dalekovod Joint Venture – National Grid HV Overhead Line System	Engineering	60	UK
Costain-Hochtief Joint Venture – Reading station	Civil Engineering	50	UK
Costain-John Mowlem-Skanska Joint Venture – A2/M2 widening (Cobham to Jct.2)	Civil Engineering	30	UK
Costain-Lafarge Joint venture – East and South East Framework	Civil Engineering	50	UK
Costain-Lafarge Joint venture – Midlands Framework	Civil Engineering	50	UK
Costain-Laing O'Rourke Joint Venture – Farringdon station	Civil Engineering	50	UK
Costain-Laing O'Rourke Joint Venture – King's Cross Eastern Range Refurbishment	Civil Engineering	50	UK
Costain-Skanska C411 Joint Venture – Bond Street – Crossrail	Civil Engineering	50	UK
Costain-Skanska Joint Venture – A14 Ellington to Fen Ditton	Civil Engineering	50	UK
Costain-Skanska Joint Venture – A43 Silverstone	Civil Engineering	50	UK
Costain-Skanska Joint Venture – Crossrail Civils Framework Enabling Works	Civil Engineering	50	UK
Costain-Skanska Joint Venture – Kings College Hospital, London	Building	50	UK
Costain-Skanska Joint Venture – Lower Precinct Shopping Centre, Coventry	Building	50	UK
Costain-Skanska Joint Venture – The new Met Office	Building	50	UK
Costain-Taylor Woodrow Joint Venture – King's Cross re-development & Phase II Northern works	Civil Engineering	50	UK
Costain-VWS Joint Venture – Mersey Valley Processing Centre (Shell Green) Extension Project Stage 2	Engineering	50	UK
Lagan-Ferrovial-Costain - A8	Civil Engineering	45	UK
The e5 Joint Alliance Severn Trent Framework	Engineering	25	UK
TSIF-ILW Joint Venture – Trawsfynydd nuclear power station decommissioning	Civil Engineering	33.3	UK

25 Subsidiary undertakings, joint ventures, associates and joint operations continued

Key to registered office/principal place of business

(1)	Costain House, Vanwall Business Park, Maidenhead, Berkshire, SL6 4UB, England
(2)	Salvesen Tower, Blaikies Quay, Aberdeen, AB11 5PW, Scotland
(3)	210 Pentonville Road, London, N1 9JY, England
(4)	Carillion House, 84 Salop Street, Wolverhampton, West Midlands, WV3 0SR, England
(5)	Avda. Pablo Cerezo, s/n, Club de Golf Alcaidesa, 11360 – San Roque-Cádiz, Spain
(6)	The Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington, Delaware 19801 (New Castle County), USA
(7)	Plot 67978, Mokolwane House, First Floor, Fairgrounds Office Park, Gaborone, Botswana
(8)	Suite 16-10, Level 16, Wisma UOA II, No. 21 Jalan Pinang, 50450 Kuala Lumpur, Malaysia
(9)	Whitehill House, Windmill Hill Business Park, Whitehill Way, Swindon, SN5 6PE, England
(10)	The Sherard Building, Edmund Halley Road, Oxford, Oxfordshire, OX4 4DQ, England
(11)	8th Floor, The Place, High Holborn, London, WC1V 7AA, England
(12)	3 More London Riverside, London, SE1 2AQ, England
(13)	P.O.Box N-7768, Bank Lane, Nassau, Bahamas
(14)	Building 4F, Corniche Road, Ground floor, Office 1, Mussafah Industrial Area, 3069, Abu Dhabi, UAE
(15)	Flat 33, Building 232, Road 18, Block 321, Manama, Bahrain
(16)	P.O.Box 6967, 21452, Jeddah, Saudi Arabia
(17)	Peninsula Plaza #27-01, 111 North Bridge Road, 179098, Singapore
(18)	10-12 Laramie Road, Narre Warren South, City of Casey, Melbourne, Victoria 3805, Australia
(19)	BGC Centre, Mezzanine level, 28 The Esplanade, Perth, WA 6000, Australia
(20)	737 Burwood Road, Hawthorn Road, Melbourne, Victoria 3122/3123, Australia
(21)	Calle Delfines No. 268 – 2, Frac. Playa Ensenada, Ensenada, B.C., CP. 22880, Mexico
(22)	Marszałkowska 82, Warsaw, Mazowieckie, 00-517, Poland
(23)	Dormant company – Venezuela, no record of address
(24)	Dormant company – Nigeria, no record of address
(25)	10th Floor, Club Chambers Building, Corner Nelson Mandela Avenue / 3rd Street, Harare, Zimbabwe

26 Acquisitions

There were no acquistions during the year and there were no changes to the acquisition fair values of Costain Integrated Technology Solutions Limited (formerly Simulation Systems Limited) disclosed in the 2016 financial statements.

27 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

	2017			2016		
	Joint ventures and associates £m	Joint operations £m	Total £m	Joint ventures and associates £m	Joint operations £m	Total £m
Services of Group employees	**19.5**	**157.9**	**177.4**	32.6	133.9	166.5
Construction services and materials	**0.1**	**33.5**	**33.6**	0.2	28.4	28.6
	19.6	**191.4**	**211.0**	32.8	162.3	195.1

Balances with joint ventures and associates are disclosed in notes 14 and 19. Balances with joint operations are eliminated on consolidation.

The Costain Pension Scheme

Details of transactions between the Group and The Costain Pension Scheme are included in note 21.

Transactions with key management personnel

Disclosures related to the remuneration of key personnel as defined in IAS 24 'Related Party Disclosures' are given in note 6. Key management personnel, as defined under IAS 24 '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 772,449 ordinary shares in Costain Group PLC, which expressed as a percentage of the issued share capital is 0.73% (2016: 0.71%) 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, AIP, DSBP and SAYE plans, which are detailed in note 21.

The compensation of key management personnel, including the directors, is as follows:

	Group	
	2017 £m	2016 £m
Directors' emoluments	**3.0**	2.0
Executive officers' emoluments	**2.5**	2.3
Post-employment benefits	**0.2**	0.2
Share-based payments	**1.8**	1.6
	7.5	6.1

The above amounts are included in employee benefit expense (note 5).

Nigel Curry, director of Costain Limited and Costain Integrated Services Limited and Andrew Ferguson, director of Costain Integrated Services Limited are beneficiaries of a pension scheme that owns and leases a property to a Costain subsidiary under a lease dated 17 September 2012. The duration of the lease is 10 years with a break clause after five years. The rent is £0.2 million per annum. The lease was surrendered on 31 July 2017.

Louis Thompson, who until 5 July 2016 was a director of Simulation Systems Limited (now Costain Integrated Technology Solutions Limited), is a beneficiary of a pension scheme that owns and leases certain properties to a Costain subsidiary under three leases dated between 2007 and 2013. The lease terms are seven, 10 and 25 years and the 25-year lease has a break option period between 18 and 36 months following the acquisition by the Group. The aggregate rent is under £0.1 million per annum.

Company

The Company has no transactions with related parties other than the charge in relation to share-based payments (note 21) (2016: none).

FIVE-YEAR FINANCIAL SUMMARY

	2017 £m	2016 £m	2015 £m	2014 £m	2013 £m
Revenue and profit					
Revenue (Group and share of joint ventures and associates)	**1,728.9**	1,658.0	1,316.5	1,122.5	960.0
Less: Share of joint ventures and associates	**(44.9)**	(84.3)	(52.9)	(50.7)	(74.8)
Group revenue	**1,684.0**	1,573.7	1,263.6	1,071.8	885.2
Group operating profit before other items	**48.7**	41.1	33.2	28.7	27.4
Other items:					
Exceptional transaction costs	**–**	–	–	–	(3.7)
Amortisation of acquired intangible assets	**(3.2)**	(4.6)	(3.2)	(3.0)	(1.8)
Employment related and other deferred consideration	**(1.2)**	(1.6)	(0.4)	(2.2)	(2.8)
Group operating profit	**44.3**	34.9	29.6	23.5	19.1
Profit on sales of interests in joint ventures and associates	**–**	–	–	4.0	9.1
Share of results of joint ventures and associates	**0.3**	0.2	(0.1)	(1.3)	(11.3)
Profit from operations	**44.6**	35.1	29.5	26.2	16.9
Finance income	**0.4**	0.6	0.8	0.7	0.7
Finance expense	**(6.1)**	(4.8)	(4.3)	(4.3)	(4.7)
Net finance expense	**(5.7)**	(4.2)	(3.5)	(3.6)	(4.0)
Profit before tax	**38.9**	30.9	26.0	22.6	12.9
Taxation	**(6.3)**	(4.5)	(3.8)	(1.6)	(0.4)
Profit for the year attributable to equity holders of the parent	**32.6**	26.4	22.2	21.0	12.5
Earnings per share – basic*	**31.1p**	25.7p	21.8p	22.2p	17.6p
Earnings per share – diluted*	**30.6p**	25.0p	21.2p	21.7p	16.9p
Dividends per ordinary share					
Final	**9.25p**	8.40p	7.25p	6.25p	7.75p
Interim	**4.75p**	4.30p	3.75p	3.25p	3.75p
Summarised consolidated statement of financial position					
Intangible assets	**62.5**	65.9	52.3	31.0	33.0
Property, plant and equipment	**43.0**	42.2	37.3	10.0	7.9
Investments in equity accounted joint ventures and associates	**2.7**	2.6	2.6	27.5	32.1
Other non-current assets	**15.0**	22.6	18.8	41.0	31.8
Total non-current assets	**123.2**	133.3	111.0	109.5	104.8
Current assets	**537.9**	512.9	421.4	346.9	276.5
Total assets	**661.1**	646.2	532.4	456.4	381.3
Current liabilities	**421.3**	441.6	372.2	299.3	296.1
Retirement benefit obligations	**23.9**	73.5	36.7	41.7	37.2
Other non-current liabilities	**61.9**	31.5	2.9	4.6	4.7
Total liabilities	**507.1**	546.6	411.8	345.6	338.0
Equity attributable to equity holders of the parent	**154.0**	99.6	120.6	110.8	43.3

* The earnings per share figures for 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	1 March 2018
Annual report mailing	16 March 2018
Ex-dividend date for final dividend	12 April 2018
Final dividend record date	13 April 2018
Annual General Meeting	8 May 2018
Final dividend payment date[2]	18 May 2018
Half-year end	30 June 2018
Half-year results 2018	22 August 2018
Ex-dividend date for interim dividend	13 September 2018
Interim dividend record date	14 September 2018
Interim dividend payment date	19 October 2018
Financial year end	31 December 2018

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 8 May 2018

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 26 April 2018. 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 0371 384 2268* or +44 (0) 121 415 7173 if calling from outside the UK.

Analysis of shareholders

as at 1 March 2018

	Total number of holdings	Total number of shares	Percentage issued capital
Shareholdings 100,000 and more	118	93,137,231	88.20%
Shareholdings 50,000–99,999	47	3,387,081	3.21%
Shareholdings 25,000–49,999	56	2,082,098	1.97%
Shareholdings 5,000–24,999	339	3,410,943	3.23%
Shareholdings 1–4,999	8,349	3,575,494	3.39%
Totals	8,909	105,592,847	100.00%

Secretary

Tracey Wood

Registered Office

Costain House, Vanwall Business Park, Maidenhead, Berkshire SL6 4UB
Telephone 01628 842 444
costain.com
info@costain.com
Company Number 1393773

Registrar

Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA

Telephone 0371 384 2250* or +44 (0)121 415 7047 if calling from outside the UK.

* 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 of 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 0371 384 2250* (+44 (0) 121 415 7047 if calling from outside the UK) who will be pleased to help 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 'dividend tax confirmation' 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 'dividend tax confirmation' electronically. Instead of receiving the paper 'dividend tax confirmation', 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.

* Lines are open Monday to Friday 08.30am to 05.30pm, excluding UK bank holidays.

CONTACT US

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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

costain.com
costain.com/investors
costain.com/our-culture
costain.com/annual-report-2017
costain.com/news

costain.com/investors

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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