Engineering Tomorrow... today

Costain Group PLC
Annual Report 2013

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Find us online

Our Annual Report 2013 is available in both printed form and within the 'Investors' section of the Costain website at **www.costain.com/investors**. Effective communication with our shareholders is vital to our continued success and we would welcome feedback on either or both versions of this Annual Report – email us at **info@costain.com**

KPI

This icon has been used throughout the report and references our key performance indicators ('KPIs').

Throughout the Annual Report, we have used the following icons to direct you to further information either in the report or elsewhere.

Links to further information in this report.

Links to further information within our website.

The spirit of innovation...

Isambard Kingdom Brunel was the celebrated engineer of his era. His vision and pursuit of innovative engineering ideas revolutionised infrastructure in the nineteenth century. In the twenty-first century, Costain is driven by a similar passion to build a better world. We seek new ways to meet the complex challenges of today's infrastructure programmes; engineering solutions that will benefit the UK for generations to come.

Brunel had a fundamental impact on the world in which he lived and on the world in which we live today.

At Costain, we share the Brunel spirit by ***Engineering Tomorrow***.

How we create value

Our ***Engineering Tomorrow*** strategy is designed to meet national needs by upgrading and maintaining the UK's infrastructure and aiding economic recovery and growth. Value is created by our drive for innovation and we are committed to a constant quest for improvement. We are confident that our robust business model and our strategic focus will continue to deliver shareholder value in the years ahead.

Additional information concerning our ***Engineering Tomorrow*** strategy can be found at key locations in this report, specifically on pages 6, 8-9, 12-23, 28-33, 35, 40 and 42.

Costain Cares and Our Values

We care about all our stakeholders. Our set of values drives our behaviour and provides the basis for all our decisions. Everyone at Costain is committed to being:

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

Focusing on six strategic priorities

- **Operate safely, efficiently and responsibly**
- **Continue to enhance customer insight**
- **Grow by broadening and integrating our services**
- **Develop best-in-class team**
- **Create and deliver innovative sustainable solutions**
- **Working in collaboration**

More detailed information about our strategic priorities can be found on pages 13-19 of this report.

Our strategy for sustainable growth can be found on pages 11-23.

Our vision...
is to be one of the UK's top engineering solutions providers.
We must be the best for technical, innovative and sustainable solutions.

Behaviour...
we are committed to operating our business both sustainably and responsibly. We are focused on one simple but powerful message – 'Costain Cares'. This is not a slogan: it is an attitude of mind. It is integral to everything we do and a touchstone against which we can evaluate and measure our performance. Costain Cares about relationships, our environment and the future.

Operations...
we focus on intelligent solutions to meet national needs. As a Tier One engineering solutions provider, we provide front-end engineering consultancy, construction and ongoing care and maintenance services across market sectors. We have two core operating and reporting divisions within our business, Infrastructure and Natural Resources.

Infrastructure	Natural Resources
Rail	Water
Highways	Nuclear Process
Power	Waste
Airports	Oil & Gas

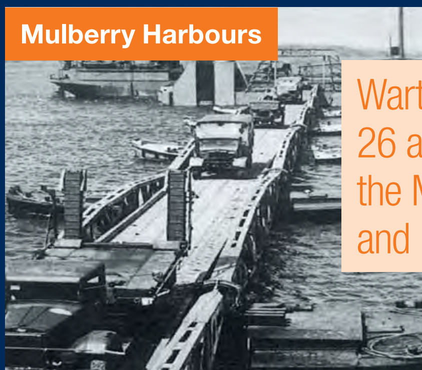
Services
Advisory and concept development
Specialist design
Programme management
Complex project delivery
Technology integration
Asset optimisation and support

Delivering value to all our stakeholders
Delivering a sustainable business through the development of a strong and profitable forward order book.

The history of Costain spans a period of nearly 150 years

Costain continues to be one of the UK's leading engineering solutions providers, working to improve people's lives by focusing on the issues you care about.

The Group was founded in Liverpool in 1865 by Richard Costain, aged 26, a jobbing builder from the Isle of Man.


Mulberry Harbours

Wartime work included 26 aerodromes, part of the Mulberry Harbours and munitions factories.


Festival of Britain

Costain built the Skylon and Dome of Discovery for the 1951 Festival of Britain.

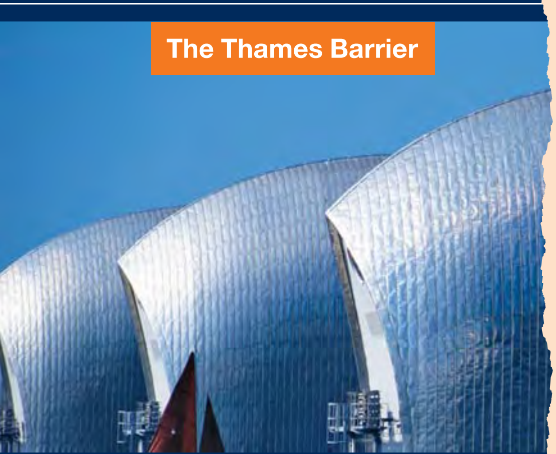
A list of 101 interesting facts about Costain can be found on its website: **www.costain.com/news**

Costain was the first UK contractor to win the Queen's Award for Export Achievement, in 1971.


London Bridge Station

Costain regularly announces key stakeholder information on the 'News' section of its website: **www.costain.com/news**

The Thames Barrier



Costain voted Top 100 company

4 December 2013

One of the UK's leading engineering solutions providers, Costain, was placed 55th (joint place with Virgin Trains) in Britain's 'Most Admired' league table, climbing up from last year's 61st position.

The table, comprising 247 top names including Rolls-Royce, Unilever, Marks & Spencer, Royal Dutch Shell, J Sainsbury and Coca-Cola Enterprises, was organised by *Management Today* magazine and sponsored by BSI.

The league table was compiled by asking Britain's largest public companies in 26 sectors to evaluate their peers.

Costain was a founder member of the Channel Tunnel joint venture.

The 1,377 metre Tsing Ma suspension bridge built in consortium in Hong Kong is the world's longest combined road and rail bridge.

Contract finalised with EDF for Hinkley Point Nuclear Power Station.

Costain awarded M6 – Heysham Link Road contract.

Costain awarded five-year framework contract for Network Rail.

Costain to refurbish Hammersmith Flyover.

Costain awarded a £400 million contract to redevelop London Bridge Station.

Costain JV awarded £900 million Network Rail contract.

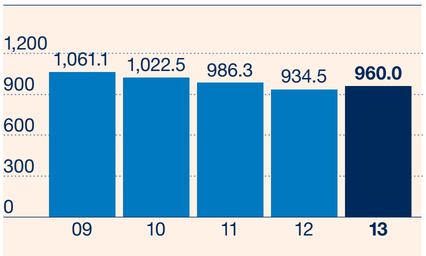
Costain appointed to Thames Water AMP6 programme.

2013 highlights

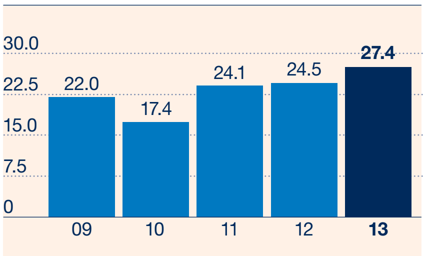
Strategy delivering results

Financial highlights

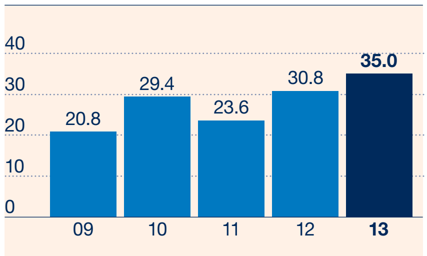
Revenue[2]
£m



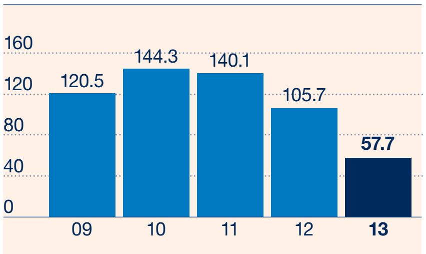
Underlying operating profit[1,3]
KPI
£m



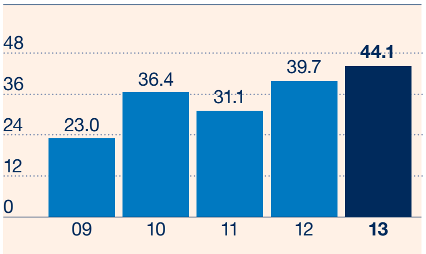
Adjusted profit from operations[1,4]
£m



Net cash balance
KPI
£m



Adjusted earnings per share[1,4]
Pence



Dividend per share
Pence

	2013	2012 (restated)[1]
Revenue[2]	**£960.0m**	£934.5m
Operating profit		
Underlying[3]	**£27.4m**	£24.5m
Profit before tax		
Adjusted[4]	**£31.0m**	£28.1m
Reported	**£12.9m**	£24.7m
Basic earnings per share		
Adjusted[4]	**44.1p**	39.7p
Reported	**18.8p**	35.4p
Net cash balance	**£57.7m**	£105.7m
Dividend per share	**11.5p**	10.75p

1 2012 restated for revised IAS 19 Employee benefits accounting standard.
2 Including share of joint ventures and associates.
3 Underlying operating profit before Other items (amortisation of acquired intangible assets and employment related and other deferred consideration and in 2013 £3.7 million one-off costs associated with the offer for May Gurney Integrated Services plc) and in 2012 excludes the £2.8 million one-off costs resulting from pension scheme liability actions.
4 Results stated before Other items (amortisation of acquired intangible assets and employment related and other deferred consideration and in 2013 £3.7 million one-off costs associated with the offer for May Gurney Integrated Services plc and non-cash impairment of £9.8 million on carrying value of assets in non-core Land Development activity in Spain).

KPI

This icon has been used throughout the report and references our key performance indicators ('KPIs').

The Finance Director's review can be found on pages 43-45.

The financial statements can be found on pages 86-132.

Highlights

- Underlying operating profit[3] up 12% to £27.4 million (2012: £24.5 million)
- Increase of 10% in adjusted profit before tax[4] to £31.0 million (2012: £28.1 million)
- Adjusted basic earnings per share[4] increased by 11% to 44.1 pence (2012: 39.7 pence)
- Forward order book up 25% to £3.0 billion (2012: £2.4 billion): over 90% of order book comprises repeat orders and over 90% lower risk cost-reimbursable forms of contract
- £57.7 million year-end net cash balance (2012: £105.7 million), reflecting the anticipated transition to lower risk cost-reimbursable contracts, reduced levels of advance payments and increasing support services revenues
- Acquisition of EPC Offshore Ltd, a specialist oil and gas project management services company, and launch of Costain Upstream, to provide services across the life-cycle of upstream offshore oil and gas assets
- Recommended increase in final dividend for the seventh successive year, taking the total for the year to 11.5 pence, a 7% increase on the prior year
- Proposed firm placing and placing and open offer to raise circa £75 million (before expenses) to take advantage of the growing number of opportunities available to accelerate the Group's development in the medium and long term

Andrew Wyllie, Chief Executive, reviews the Group's performance in more detail on pages 8-10.

Environmental and social highlights

- Costain achieved the highest ranking, Platinum Big Tick, in Business in the Community's ('BITC') annual benchmark of responsible business management, the Corporate Responsibility Index
- We were delighted to be named in the Climate Performance Leadership Index as one of the best performing companies in the Carbon Disclosure Project's annual FTSE 350 climate change report
- In September, Costain, in conjunction with BITC, hosted The Big Infrastructure Conversation at London's City Hall
- In December, Costain was recognised at the prestigious NEF (The Innovation Institute) Innovation Awards, receiving high commendations for the Most Innovative Business Process and Most Inspiring Business Leader categories

A more detailed review of the Group's Corporate Responsibility performance can be found on pages 34-42.

Chairman's statement

David Allvey
Chairman

Overview and strategic update

Costain has delivered another strong performance.

The Group has been transformed in recent years and is now recognised as one of the UK's leading engineering solutions providers. The Group is part of a select group of companies with the integrated consulting, project delivery and operational capability required to meet the needs of major customers in a rapidly developing multi-billion pound market.

We recognise the changing dynamics of the UK marketplace, in which major customers are seeking to build strategic relationships with fewer service providers involving larger, longer term contracts incorporating a broader range of services across the full life-cycle of an asset.

Through the successful implementation of our ***Engineering Tomorrow*** strategy, Costain now provides a range of integrated consulting, project delivery and operations and maintenance services to blue-chip customers in the UK's infrastructure, energy and water markets. The Group has a well-respected brand, excellent reputation and strong track record of performance.

The opportunities in our marketplaces are substantial as investment by major customers in transportation, energy and water resources is expected to grow significantly, and supplier consolidation is anticipated to continue. In this changing and competitive environment, it is essential that Costain is able to demonstrate that it has the scale, skills, experience and financial strength necessary to secure, and then deliver, a strong performance on these increasingly large and complex contracts.

The proposed under-written capital raising will enable Costain to capitalise on these opportunities by demonstrating the Group's financial capacity to support a greater number of longer, larger contracts, investing in innovation and technology, financing bid costs for projects, funding increased working capital requirements and, where opportunities arise, adding further expertise by acquisition, thereby accelerating the Group's development.

Performance

Revenue, including the Group's share of joint ventures and associates, for the year increased to £960.0 million (2012: £934.5 million), 30% of which was derived from support service related activities. Our focus on higher margin activities led to an increase of 12% in Group underlying operating profit of £27.4 million (2012: £24.5 million). Adjusted profit before tax increased by 10% to £31.0 million (2012: £28.1 million). Adjusted basic earnings per share were up 11% to 44.1 pence (2012: 39.7 pence).

The Group's net cash position at 31 December 2013 was £57.7 million (2012: £105.7 million). This reduction was expected given the Group's rapid transformation and strategic focus on major customers who utilise target cost, cost-reimbursable contracts. Over 90% of the order book now includes this lower risk form of contract, which is more suited to complex, long-term projects. The lower net cash position also reflects an increase in support service related activities, a reduction in advance payments and a delayed contract.

We were successful in securing a number of major new contract awards and extensions to existing contracts. Consequently, the order book was up 25% to £3.0 billion as at 31 December 2013, compared to the start of the year (2012: £2.4 billion).

Dividend

In light of another successful performance and our continuing confidence in the long-term prospects for the Group, the Board is recommending a 7% increase in the final dividend, the seventh successive year of increase. If approved, the 7.75 pence per share (2012: 7.25 pence) final dividend will be paid on 25 April 2014 to shareholders on the register as at the close of business on 14 March 2014. This would bring the total dividend for the full year to 11.5 pence per share (2012: 10.75 pence), an increase of 7% over the prior year.

Group pension scheme

The deficit on the Group's legacy Costain Pension Scheme ('CPS') at 31 December 2013 was £29.4 million net of deferred tax (2012: £40.0 million). The assumptions and sensitivities used in the valuation of the pension scheme are set out in the notes to the financial statements. In accordance with the requirement for a triennial review, another full actuarial valuation of the CPS is being carried out as at 31 March 2013.

The Board of Directors including their appointment date, skills and experience and external appointments can be found on pages 48-49.

Proposed capital raising

Costain has announced a proposed capital raising to enable the Group to take greater advantage of the opportunities in its chosen markets and thereby accelerate the Group's medium- and long-term growth prospects.

The Group proposes to raise approximately £70.3 million (net of expenses) by way of a firm placing and placing and open offer of, in aggregate, 33,382,068 new ordinary shares at an offer price of 225 pence per new ordinary share. 11,111,112 new ordinary shares will be issued through the firm placing and 22,270,956 new ordinary shares will be issued through the placing and open offer on the basis of 1 new ordinary share for every 3 existing ordinary shares.

The proceeds will be utilised:

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

The capital raising has been fully underwritten by Investec Bank plc and Liberum Capital Limited.

Please see the separate announcement made by Costain for further details of the terms and conditions of the proposed capital raising.

People

On 20 November 2013, we announced that Mr Samer Younis, a Non-Executive Director of Costain and the nominee of Mohammed Abdulmohsin Al-Kharafi & Sons Co. W.L.L. ('Kharafi'), had notified the Board of his resignation as a Director of the Company with effect from 30 November 2013. We would like to thank Samer for his contribution during his years of service.

We were pleased to welcome to the Board Mr Ahmed Aly Samy, a nominee of Kharafi, as a Non-Executive Director with effect from 30 November 2013. Mr Samy, the Deputy Director General Investment Affairs at Kharafi, is also a member of Costain's Nomination Committee.

We announced on 28 January 2014 that Alison Wood would join the Board as a Non-Executive Director with effect from 1 February 2014. Alison is currently a Non-Executive Director at Cobham plc and Senior Independent Director at e2v technologies plc and was formerly Non-Executive Director at BTG plc and Thus Group plc. Alison will succeed Mike Alexander as Chair of the Remuneration Committee when he retires, as previously announced, on 31 March 2014.

There were a number of operational management changes in the year and these are covered in the Chief Executive's review.

On behalf of the Board, I would like to place on record our recognition and appreciation of the excellent colleagues we have at Costain who continue to play a major role in our success.

Summary and outlook

Costain has delivered another strong performance in 2013, with a forward order book up 25% to £3.0 billion, and the Board is recommending an increase in the final dividend for the seventh successive year.

The Group has been transformed, and is now one of the UK's leading Tier One engineering solutions providers. Costain is established in a developing market of a limited number of providers who can deliver the innovative integrated consulting, project delivery and operations and maintenance services increasingly demanded by major customers.

The proposed capital raising alongside these good results provides us with the opportunity to accelerate our growth in the medium and long term in rapidly evolving markets, in which it is expected that over £400 billion will be spent in the next ten years.

David Allvey
Chairman

26 February 2014

Chief Executive's review

Andrew Wyllie
Chief Executive

This has been another year of significant progress in the transformation of Costain into a full engineering service provider for major customers who continue to invest billions of pounds addressing essential national needs.

The development of new skills and capabilities, broadening the scope of our activities, and the introduction of new technology has ensured that we were able to deliver a strong financial performance and secure a 25% increase in our order book to £3.0 billion, of which over 90% is repeat business. We have increased to over £750 million the revenue secured for 2014 (2012: over £700 million secured for 2013) and in excess of a further £2.2 billion of revenue secured for 2015 and beyond. In addition, the Group has maintained a strong preferred bidder position of over £400 million. It is encouraging to have started the new financial year with such good long-term revenue visibility.

Costain is now established as a leading Tier One UK engineering solutions provider.

Through the implementation of our ***Engineering Tomorrow*** strategy, we are focused on providing innovative and cost-effective solutions to customers who are increasingly seeking more strategic relationships through larger and longer-term contracts in order to meet their complex requirements.

This change in customer procurement approach, and associated supplier consolidation, along with the very substantial expenditure expected in the next few years is creating a dynamic marketplace which provides Costain with a tremendous opportunity to accelerate the development of the business.

Market trends and developments

The UK transport, energy and water markets are defined by significant and long-term planned expenditure programmes underpinned by committed regulated spend and essential capital investment. The future opportunities in these markets are substantial.

The UK Government, as set out in their recent National Infrastructure Plan, estimates that average annual infrastructure investment in the UK has increased to £45 billion per annum compared to an average of £41 billion per annum between 2005 and 2010. The National Infrastructure Plan has set out an overall investment of £224 billion to 2020 in an identified pipeline of projects in the UK.

Rail remains a priority area of investment for the UK Government, to stimulate economic growth, with a 14% increase in demand for rail travel estimated for the next five years. To address this demand, £38 billion has been allocated to national rail networks in areas including electrification, track and network upgrades. A further £43 billion has been allocated for High Speed 2.

In highways, the Chancellor promised in June 2013 the most extensive programme of road building in over 50 years. By 2020-21, the UK Government is expected to invest over £28 billion in enhancements and maintenance of national and local roads.

In energy, it is estimated £110 billion is to be invested by 2020 in new energy infrastructure to meet the forecast energy supply capacity gap; and £50 billion is expected to be spent to address the UK's nuclear waste legacy, whilst the ongoing capital investment in North Sea oil and gas is at its strongest for over 30 years (£13 billion forecast in 2013).

In water, there remains an ongoing need for asset performance improvements, increased water standards and a greater focus on the combination of capital and operating costs, with continued regulated investment planned. The 5 year AMP6 period commencing in April 2015, is expected to include an investment level similar to the £21 billion invested over 5 years during AMP5.

Alongside these planned levels of infrastructure investment, our major customers are consolidating their supply chains as they seek to derive business benefits by working in a more strategic and collaborative manner with a reduced number of preferred Tier One engineering solutions providers, like Costain, who have the ability to satisfy the full range of their service needs for increasingly complex and large-scale projects.

The complex nature of the customers' requirements also dictates that a target cost, cost-reimbursable form of contract is the most appropriate to be utilised. Consequently, over 90% of our order book is now comprised of this form of contract. Contracts of this form benefit from generally being lower-risk than lump sum contracts, but they do tend to be associated with higher bid costs and working capital requirements. The speed of the move to this form of contract is reflected in the cash flow movement in the year.

Scan this QR code to view the announcement interview with Andrew Wylie.

Additional information concerning our ***Engineering Tomorrow*** strategy can be found at key locations in this report, specifically pages 6, 8-9, 12-23, 28-33, 35, 40 and 42.

The provision of an increasing range of skills and services, along with our strong brand and reputation for excellent delivery, has enabled us to secure over £1.5 billion worth of large, integrated and complex projects and contract extensions during the course of the year, including:

- a contract with EDF to design and deliver the water cooling systems for the new Hinkley Point C nuclear power station;
- the electrification upgrade of the West Coast Mainline for Network Rail;
- the AMP6 programmes for Thames Water and Severn Trent;
- a number of contracts for Crossrail including the design, fit-out and commissioning of the railway systems;
- delivery of the Front End Engineering Design ('FEED') for Centrica's gas terminal at Barrow, following successful completion of the design and construction of the Easington terminal for the York field; and
- a highways framework contract with Transport for London including the Hammersmith Flyover strengthening project.

Engineering Tomorrow strategy

Our customers' endorsement of Costain as a Tier One provider and our market leading reputation is founded on our commitment to excellence in engineering. ***Engineering Tomorrow*** is the Costain commitment to identifying, developing and implementing innovative solutions to major national needs. It is this that enables us to win large and long-term, strategic contracts involving highly complex work across the full life-cycle of our major customers' assets.

We are increasing our investment in Research and Development, and we have initiatives in place to encourage and support entrepreneurial members of staff to develop their ideas into business opportunities. The 'Mario' asset management tool was one such idea, which is now being sold commercially to rail and highways customers as an addition to Costain's range of services. Other examples of new innovation and technology being driven across our entire service offering include: COpath, an asset intelligence resource which gathers data intelligence on the behaviour and movement of people within major assets such as railway stations; carbon capture and storage technology; Nuclear Waste Management Graphite Gasification; and GRAVITAS offshore, which carries out research on the design and construction of concrete gravity foundations for large offshore wind turbines.

The wide range of new technology within the business was showcased for customers at a successful innovation event held in September at the Darwin Centre in the Natural History Museum in London.

Broadening our capabilities through acquisition

On 1 August 2013, we were delighted to announce the acquisition of EPC Offshore, a specialist oil and gas project management services company, for an initial consideration of £10.6 million (including £1.0 million for excess cash). The acquisition is expected to be earnings enhancing to Costain in the first full year of acquisition.

Costain also announced the launch of Costain Upstream, to provide services across the life-cycle of upstream offshore oil and gas assets. Costain Upstream will combine the capabilities of ClerkMaxwell, the oil and gas engineering and support services provider, which has more than doubled in size since its acquisition in 2011, and EPC Offshore, to increase the scale of the Group's services in the growing, high-value North Sea upstream oil and gas market.

Operating results

The strong performance of the Group is reflected by a 12% increase in Group underlying operating profit to £27.4 million (2012: £24.5 million).

The Infrastructure division in particular has had a very successful year, with an increase in revenue, underlying operating profit and order book. This strong performance is a result of our previous focus on a number of opportunities in the infrastructure markets now delivering excellent operating returns for the Group.

During the year, the Natural Resources division has continued its transformation and the reduced profitability reflects lower revenues, additional costs to complete a small number of projects and restructuring and business development costs including the deployment of new skills and capabilities under a strengthened leadership team. The transformation is now complete and the division finished the year with an increased order book and a high level of tendering activity.

Significant developments in joint venture activities

During the period, Costain completed the sale of its minority shareholdings in three joint venture companies to Severn Trent PLC for a total consideration of £12.0 million. Severn Trent will therefore become 100% owner of the three companies, which provide services in the water sector. As a result of the transaction, Costain realised a profit of £9.1 million in 2013.

At the period end, the Group acquired the 27% interest from its partner Serco Group plc in their Managed Motorway Technology joint venture arrangement for a cash consideration of £2.4 million. The joint venture arrangement, in which Costain already held the remaining 73% interest, has a place on the Highways Agency framework to deliver new technology-led highways improvements.

Strategic report
Chief Executive's review
continued

The Group has reassessed the carrying value of the assets in its non-core Land Development activity in Spain, which is undertaken in a 50:50 joint venture with Santander Bank. As a consequence of continuing uncertainty regarding future market conditions in Spain, a non-cash impairment has been taken against the assets, the Group's share of which is £9.8 million, reducing Costain's total carrying value in the joint venture to £26.6 million.

Lapsed all-share merger with May Gurney Integrated Services plc ('May Gurney')

The Boards of Costain and May Gurney announced in March that they had reached agreement on the terms of a recommended all-share merger of Costain and May Gurney (the 'Proposed Merger').

Following an offer from another party in April, Costain announced that, having undertaken several months of detailed due diligence, it did not believe that it would be in the best interests of Costain shareholders for Costain to amend the terms of the Proposed Merger and that it would not be making a revised offer for May Gurney. Accordingly, the Proposed Merger lapsed in accordance with its terms.

The Group incurred transaction pre-tax costs of £3.7 million associated with the May Gurney proposal and these have been expensed in the results and treated as a one-off non-trading item.

Additional information concerning our Costain Cares strategy can be found on pages 34-42 and on our website: **www.costain.com/responsibility**

'Costain Cares'

Our customers place great emphasis on the 'good citizen' credentials of their supply-chain partners. Increasingly, customers insist that their Tier One providers share their corporate and social responsibility values, and failure to embrace this means non-qualification for tender lists. We passionately share these values because we believe that investment in corporate social responsibility capital is a vital investment in the Group's future success.

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

We received a further Platinum award from Business in the Community, recognising our proactive commitment to mitigating the environmental and social aspects of our operations.

Costain places the highest priority on the effective management of Safety, Health and Environment, and the Group's Accident Frequency Rate ('AFR') was 0.12, which continues to compare favourably with our major Tier One peer group. We also received 16 Gold Awards from RoSPA, four Gold Medals and two prestigious Orders of Distinction.

Costain improved its position in the annual assessment by *Management Today* magazine of Britain's Most Admired Companies, ranking 55th overall and improving to second place in the sector.

Teamwork

The strong results generated by Costain in 2013 were delivered by our outstanding multi-disciplined team of approximately 4,000. During the year, we increased once again our training and development programmes across the organisation so that we have the requisite skills and resources. There was a further increase in the number of apprentices across the Group.

During the period, Alex Vaughan was appointed Managing Director of the Natural Resources division, succeeding Mark Rogerson who left the Group to pursue other opportunities. Tim Bowen replaced Alex Vaughan as Corporate Development Director.

The Future

Costain has delivered another strong performance and demonstrated again that it has the right strategy to drive profitable growth by responding to the complex and fast-evolving requirements of its blue-chip customers.

Our established status as one of the UK's leading engineering solutions providers, our increased order book and our market-leading reputation for innovation means that we are confident of delivering further progress and being able to take advantage of significant opportunities in our chosen sectors.

The proposed capital raising will enable us to accelerate the rate at which we address these opportunities, and will thereby enhance the Group's medium- and long-term growth prospects, by demonstrating the Group's financial capacity to support a greater number of longer, larger contracts, investing in innovation and technology, financing bid costs for projects, funding increased working capital requirements and, where opportunities arise, adding further expertise by acquisition.

I look forward to reporting on further progress during the year.

Andrew Wyllie
Chief Executive

26 February 2014

Our business model

We are committed to growing our business in a controlled manner across all our target markets. We deliver this through our business model which enables us to deliver innovative engineering solutions for our clients and their customers.

Our strategy and business model are underpinned by strong leadership and robust processes across finance, risk management and operations, strong governance and very high standards of responsibility.

This approach delivers sustainable growth, allowing us to meet our business goal of delivering value to all our stakeholders.

Our vision...

is to be one of the UK's top engineering solutions providers.
We must be the best for technical, innovative and sustainable solutions.

Behaviour...

we are committed to operating our business both sustainably and responsibly. We are focused on one simple but powerful message – 'Costain Cares'. This is not a slogan: it is an attitude of mind. It is integral to everything we do and a touchstone against which we can evaluate and measure our performance. Costain Cares about relationships, our environment and the future.

Operations...

we focus on intelligent solutions to meet national needs. As a Tier One engineering solutions provider, we provide front-end engineering consultancy, construction and ongoing care and maintenance services across market sectors. We have two core operating and reporting divisions within our business, Infrastructure and Natural Resources.

Infrastructure

Rail
Highways
Power
Airports

Natural Resources

Water
Nuclear Process
Waste
Oil & Gas

Services

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

Delivering value to all our stakeholders

Delivering a sustainable business through the development of a strong and profitable forward order book.

The Costain difference

01 Creating value through our customer focused strategy

Our strategy...

Engineering Tomorrow...

is our strategic commitment to identifying, developing and implementing innovative and sustainable solutions to meet major national needs.

Additional information can be found online:
www.costain.com/engineering-tomorrow

02 Focusing on six strategic priorities

Our strategic focus is to enhance our growth and market position by providing innovative and sustainable solutions to increasingly complex and large-scale national needs. The Group has been transformed in recent times to meet our customers' continuously evolving requirements. Our *Engineering Tomorrow* strategy will ensure we remain competitive and continue to deliver shareholder value.

1: Operate safely, efficiently and responsibly

The Health and Safety of our people and everyone who is involved with Costain remains our highest priority. We demand that safety must be adhered to at all times to ensure that we operate in an environment which is free from harm.

We concentrate on solutions that deliver best value for customers. This requires an unrelenting focus on our customers' costs and our own operating procedures.

We believe that responsible business is integral to delivering greater value to our customers and all our stakeholders. Our commitment to delivering services responsibly and sustainably is vitally important to the Group. We are focused on building a long-term sustainable business that creates economic, environmental and social value.

2013 performance and KPIs

Accident Frequency Rate ('AFR') KPI
Target: To continually improve safety performance with a zero tolerance approach.

0.12

2013	2012	2011
0.12	0.09	0.11

Within the Company, there is both a corporate and an individual responsibility to ensure that operations are managed in a safe, healthy and environmentally controlled manner. The common measure in the construction sector for measuring safety performance is the AFR which measures the number of serious workplace accidents reportable under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 1995 per 100,000 hours worked. The Group's AFR increased in 2013 compared to 2012. We are continuing to work to reduce the AFR in line with our aspiration towards zero accidents.

CO_2 equivalent emissions KPI
Target: To reduce our measure emissions.

14,365 tonnes CO_2e

	Total	Scope 1	Scope 2	Emission intensity
CO_2 equivalent emissions (tonnes)	14,365	10,474	3,891	
CO_2 equivalent emissions (tonnes/ £million)				14.85

In accordance with the requirements of the Companies Act 2006 (Strategic and Directors' Report) Regulations 2013, the Group has adjusted its carbon reporting boundaries. Emissions under this regulation cover scope 1 and 2 emissions for all Costain Group activities, including overseas interests and joint ventures, in which the Company has a 50% or greater financial stake. In 2014, we will continue to expand our scope of reporting to ensure that we incorporate all scope 1 and 2 emissions where Costain has a financial interest.

Underlying operating profit KPI
Target: In line with business plan.

£27.4m

2013	2012	2011
£27.4m	£24.5m	£24.1m

The level of underlying operating profit is a key measure of performance for the Group. The measure represents the results of the operating elements of the Group's performance and excludes sales of assets and joint ventures. The Group's underlying operating profit in 2012 and 2013 increased as a result of the strong performance in the Group during each year. The increased profitability reflects the Group's continued focus on higher margin work.

The Costain difference

02 Focusing on six strategic priorities continued

1: Operate safely, efficiently and responsibly continued

Net cash balance
Target: Maintain a net cash balance at an appropriate level to suit the business requirements.

KPI

£57.7m

2013	2012	2011
£57.7m	£105.7m	£140.1m

The Group has a positive net cash balance and close monitoring and measurement of cash resources is carried out as part of the performance measurement process. The reduced positive position reflects a transition to over 90% of the order book being a lower risk, target-cost form of contract, an increase in support services activities and a delayed contract completion.

Health and Safety Awards
Our strong Health and Safety performance was recognised by the achievement of 35 RoSPA Awards, including two Orders of Distinction, one President's Award, four Gold Medals and 16 Gold Awards.

The Costain Way
The Costain Way is Costain Group's Business Assurance System, a risk-based, integrated management system that provides instructions and advice on how to promote best practice across the Group. The Costain Way updates and builds on the strength and success of its predecessor, Implementing Best Practice ('IBP'), providing a new innovative approach. It contains the required standards, guidance, best practices and standard forms for all the activities undertaken by everyone across the Costain Group – the Costain Way of working. The Costain Way is faster, easier to access, easier to search and is simplified to tell you what you must do and how to do it, with guidance and tools. This improvement will help manage and reduce risk and drive efficiencies across the business.

2014 focus

- Continue to reduce the Group AFR and the All Accident Frequency Rate ('AAFR') towards our goal of zero harm: AFR 0.08, AAFR 2.1
- Reduce measured carbon emissions intensity by 55% by 2020 (against 2009 baseline)
- Launch our 2020 Costain Cares (Corporate Responsibility) Strategy
- Reduce non-operating and operating costs

Risks

- Health and Safety
- Operational delivery
- Failure of IT system

Additional information relating to the principal risks and uncertainties can be found on pages 24 and 25.

2: Continue to enhance customer insight

The ability to understand the challenges facing our customers is crucial if we are to strengthen and evolve our relationships with them. Continuing to enhance our customer insight is one of our top priorities and it is by building strategic, long-term, collaborative partnerships that we are best positioned to deliver innovative solutions to these customers.

Additional value is delivered to both customers and end users by operating efficiently with a strong focus on speed and agility and an uncompromising attitude to safety. We recognise that talented, integrated and accountable project teams are fundamental to maximising the opportunities presented by unique customer insights.

2013 performance and KPIs

Repeat business KPI
Target: In line with business plan.

+90%

2013	2012	2011
+90%	+90%	+90%

The Group's strategy ***Engineering Tomorrow*** is focused on providing innovative and cost-effective solutions to customers who are increasingly seeking more strategic longer-term contracts in order to meet their complex requirements. Repeat business is, therefore, an essential measure for the business. With over 90% repeat business, Costain has maintained a strong pipeline of business development opportunities and we continue to demonstrate the quality of our customer insight and relationship.

Customer satisfaction

84%

2013	2012	2011
84%	84%	81%

Customer innovation evening
In September, the Darwin Centre at London's Natural History Museum was host venue for a Customer Innovations Evening, showcasing exciting products and developments that the Group has brought to fruition over the past year.

The audience consisted of over 60 customers and key stakeholders, who were able to talk to the Costain personnel behind the innovations, discovering the benefits of individual innovations and how they could improve the performance of their business.

2014 focus

- Continue to build strategic relationships with our customers, gaining deeper insight into their business challenges
- Continue to strengthen our thought leadership position by ensuring we become the influential 'voice of the industry' in terms of sustainable infrastructure development

Risks

- Economic conditions
- Winning new work
- Operational delivery

Additional information relating to the principal risks and uncertainties can be found on pages 24 and 25.

The Group's divisional performance can be found on pages 26 and 27.

The Costain difference

02 Focusing on six strategic priorities continued

3: Grow by broadening and integrating our services

We continue to deliver engineering services across the full asset life-cycle, from advisory and design to operations and maintenance.

In 2013, we continued to broaden and enhance our service offering. We have developed our value proposition across six core service lines in an increasingly integrated offering to customers: advisory and concept development, specialist design, programme management, complex project delivery, technology integration, asset optimisation and support.

2013 performance and KPIs

Order book
Target: To build a strong order book in line with strategy.

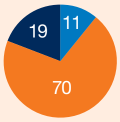
KPI

£3.0bn

2013	2012	2011
£3.0bn	£2.4bn	£2.5bn

The level of secured orders on which work is to be carried out is a key measure for achieving continued profitability and growth. The order book has increased compared to 2012 due to the Group securing over £1.5 billion of new contracts and extensions.

Revenue
Target: In line with business plan.



2013
- 11% Advisory and design
- 70% Programme delivery
- 19% Operations and maintenance

Costain delivers engineering solutions across our customers' full asset life-cycle, from advisory and design, programme delivery to operations and maintenance. The increasing range of skills and services across these activities has enabled the Group to continue to increase the revenue derived from this broader range of services.

Acquisition of EPC Offshore
In August, Costain acquired EPC Offshore, a specialist oil and gas project management services company. EPC Offshore, a field development and project management specialist providing client-side services to North Sea oil and gas companies, complements the acquisition of ClerkMaxwell in 2011. These acquisitions strengthen our strategy, broadening our range of capabilities in response to requirements of major customers, increasing the scale of the Group's services in the growing, high-value North Sea upstream oil and gas market.

2014 focus

- Increase revenue and order book across our six core service lines
- Organic growth and growth through acquisition

Risks

- Economic conditions
- Winning new work
- Operational delivery
- Acquisitions

Additional information relating to the principal risks and uncertainties can be found on pages 24 and 25.

4: Develop best-in-class team

Attracting, retaining and developing the best people for Costain is key to our success.

We continue to grow and enhance our capability in line with our customers' needs for the relevant skills for today and tomorrow. By investing in a diverse, knowledgeable and highly capable workforce, with transferable skills, we can be sure that we have a pipeline of talent throughout the business.

2013 performance and KPIs

Staff turnover KPI

Target: To provide initiatives and working conditions in order to retain key staff.

8.5%

2013	2012	2011
8.5%	7.4%	7.0%

The retention of staff is fundamental to delivering a quality service to customers. The Group undertakes a number of important initiatives to retain key staff, including actively facilitating their career development. Clear action plans are in place to address issues such as Health and Safety, reward, training and development and job satisfaction. The Group uses a 'voluntary leavers' turnover rate to monitor staff retention. In 2013, our staff turnover increased slightly to 8.5%, but it continues to compare favourably to the industry average.

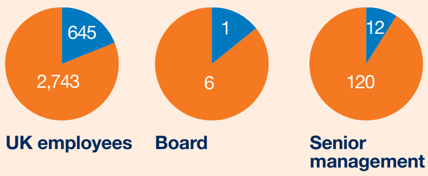
Diversity and inclusion KPI

Target: To value diversity and inclusion in the workforce.

19.0% female

7.2% BAME

2013	2012	2011
19.0% female	19.4% female	22.2% female
7.2% BAME	8.0% BAME	6.6% BAME



UK employees: 3,388, 645 are female
Board: one female out of seven
Senior management: 12 females out of 132
(Figures as at 31 December 2013)

Costain is an inclusive employer and promotes equality and inclusion from recruitment and selection, through training and development, to promotion, reward, recognition and retirement. The Group values the differences that a diverse workforce brings to the organisation. The Group has monitored the diversity profile of its employees, as a total population, over the last six years, which shows a fairly consistent profile of female and Black, Asian and Minority Ethnic ('BAME') employees. In 2013, there has been a slight decrease in the number of female employees to 19.0% and a decrease in BAME employees to 7.2% (employees who declared their ethnicity). In 2013, the Group has expanded reporting to include women in senior positions within the Company.

Investment in training and development

£3.0m

over 10,000 training days
2012: 7,988 training days

Big Infrastructure Conversation

In September Costain, in conjunction with Business in the Community, hosted the Big Infrastructure Conversation, at London's City Hall.

On the day, students, ambassadors, apprentices and trainees met business leaders and discussed their own apprenticeship experiences, the importance of inspirational work experience and skills.

For the industry leaders, there was also an opportunity to share best practice about how businesses can tackle youth unemployment and to listen to young people about their needs, hopes and ambitions for the future, particularly in relation to securing valuable career advice.

2014 focus

- Broaden graduate, apprentice and sponsorship pipelines to new disciplines
- Continue to develop transferrable skills across sectors
- Talent management
- Unconscious bias training

Risks

- People

Additional information relating to the principal risks and uncertainties can be found on pages 24 and 25.

The Costain difference

02 Focusing on six strategic priorities continued

5: Create and deliver innovative sustainable solutions

We are focused on creating intelligent, sustainable solutions that improve the performance of our customers' businesses. We invest significantly in research, innovation and emerging technology to provide customers with new services that reduce impact on the communities we serve. By aligning our pipeline of innovation to our customer challenge, we are able to work closely with them through every stage of development.

2013 performance and KPIs

Number of patents and patents pending

31 patents

2013	2012
31 patents (14 granted, 17 in application phase)	36 patents

The Group has realigned its patent portfolio to reflect the business' focus.

Innovation Awards

In December, Costain was recognised at the prestigious NEF (The Innovation Institute) Innovation Awards, receiving high commendations in the Most Innovative Business Process and Most Inspiring Business Leader categories.

The innovations included a science, technology, engineering and maths ('STEM') game app aimed at raising young people's awareness of the construction and engineering industry and the different career options available using a smartphone or tablet device, and COpath, an innovative passenger monitoring and measurement technology for use in the travel and transport industries.

Both innovations earned Costain a runner-up award from the judging panel, which included the award sponsors EMC, BASF: The Chemical Company, National Grid and EDF Energy.

2014 focus

- Enhance relationships with our partners to identify, develop and implement innovation through our current contracts and provide new services to our customers
- Identify funding and, through 'open innovation', transfer innovation from other sectors to create new business opportunities
- Use advanced technology to create insights about the performance of our customer asset
- Rethink contract delivery with our customers to deliver better outcomes

Risks

- People

Additional information relating to the principal risks and uncertainties can be found on pages 24 and 25.

Examples of Innovation can be found in the section titled ***Engineering Tomorrow...*** 'in action' on pages 6, 8-9, 12-23, 28-33, 35, 40 and 42.

6: Working in collaboration

Partnering and collaboration form a central part of our approach. Both are essential in delivering complex engineering and services. In a market where collaboration continues to deliver value, Costain focuses on developing strategic partnerships to support the development of broader services and technology.

2013 performance and KPIs

Supply chain performance KPI
Target: Average key supplier performance score of greater than 50%.

70%

2013	2012	2011
70%	69%	65%

The Group has a number of key suppliers and is reliant on their performance in carrying out its business. Consequently, an internal performance measurement tool is used to assess the performance of key suppliers on a regular basis against a number of indicators including Health and Safety, programme, commercial and quality performance. The result of the assessment is shown as a percentage score which allows comparison against previous scores and other suppliers. The assessment and results are then used as a basis for discussion with each strategic and preferred supplier of their performance and to put in place, where necessary, actions to improve performance or, if appropriate, reduce the amount of work performed by a supplier.

In 2013, the average key supplier performance score continued to improve. The number of suppliers achieving Costain Blue standard (80% or above) in a single quarterly review increased to 255 from 171 in 2012, a 49% increase.

+90%

of contracts are lower risk cost-reimbursable

Collaborative Business Relationships: BS11000
Costain has developed a best practice process in which relationships can be formed and developed between organisations of any size, for mutual additional benefit. The process is accredited to BS11000 (Collaborative Business Relationships) which is a procedural framework introduced in 2010 by the British Standards Institute.

Costain is a foundation member of the Institute of Collaborative Working.

2014 focus

- To be recognised as the UK's leading exponent of BS11000
- To deliver shared benefits through 'game-changing' relationships
- To increase our revenue from alliance/ framework contracts

Risks

- Economic conditions
- Operational delivery

Additional information relating to the principal risks and uncertainties can be found on pages 24 and 25.

Business model

continued

The Costain difference

03 Our market focus

The sectors in which the Costain Group is active have, in total, a targeted investment spend of more than £70 billion per annum for the immediate future. Below is a summary of activity in those Costain sectors:

Water

£11bn total

Potential	Addressable
£4.6 billion	£2.6 billion

The recent submission of water company business plans to OfWat for the sixth asset management cycle reflects a continued commitment to spend in the sector. The regulator's focus on total expenditure ('totex') provides the opportunity to grow into higher value services.

Airports

£3.2bn total

Potential
£1 billion

Aviation investment continues to be an area of intense public debate with the Airports Commission Interim report, published on 17 December 2013, supporting the need for further investment in developing capacity in the sector and suggesting that without this it will cost users and providers of airport infrastructure £18-£20 billion and the wider economy £30-£45 billion. Existing investment remains high to support the intensity of use on our existing infrastructure which sees Heathrow at capacity and London Gatwick expected to reach the same point by 2020.

The Airports Commission's shortlisted alternatives vary in cost from £13 billion to £112 billion. Despite these challenges, the UK has more seats available and serves more destinations on a daily basis than any other European country. The debate is no longer whether we need new runways and infrastructure, but when and where.

Highways

£6.3bn total

Potential	Addressable
£3.2 billion	£2 billion

In June 2013, the Chancellor promised the biggest programme of road building in over 50 years. The Government will invest over £28 billion in enhancements to and maintenance of national and local roads to: add extra lanes to the busiest motorways, identify and fund solutions to tackle some of the most notorious and longstanding road hotspots in the country, upgrade the national non-motorway network; repair the national and local road network; and transform the Highways Agency into a publicly-owned corporation.

Power

£3.9bn total

Potential	Addressable
£1.8 billion	£700 million

The UK's challenge is to secure a sustainable energy future whilst at the same time replacing power generation capacity and ageing infrastructure. For energy to be truly sustainable, solutions must ensure that they meet carbon reduction targets and minimise the impact of rising consumer prices. In 2012, private sector investment in energy rose to £11.6 billion, representing around 10% of the UK's capital investment, or equivalent to building 20 Olympic stadiums.[1] This level of investment is expected to continue and will include renewables, new technologies, smarter networks and demand-side controls. Around £110 billion of investment is anticipated by 2020.

[1] Source: Powering the UK – Investing in future growth, EY 2013.

Nuclear Process

£6bn total

Potential	Addressable
£2.8 billion	£1.5 billion

With all but one of the UK's current reactors retiring over the next ten years, there remains significant decommissioning opportunities from the £49.5 billion investment pledged by the Nuclear Decommissioning Authority for the clean-up of its sites. This goes hand-in-hand with the Government's aim to deliver 16GW of new nuclear capacity by 2030, presenting further opportunities for Costain's already mature and established position in the UK market.

Rail

£17.4bn total

Potential	Addressable
£9.5 billion	£5.4 billion

Rail investment in the UK continues to be robust as outlined in the National Infrastructure Plan 2013. This remains a priority area of investment for Government to stimulate economic growth, with a 14% increase in demand for rail travel estimated for the next five years. To address this, £38 billion has been allocated for national rail networks in areas including electrification, track and network upgrades and the proposed High Speed 2.

Oil & Gas

£27bn total

Potential	Addressable
£1.8 billion	£600 million

Sustained activity and growth in the UK market are set to continue. In 2020, we will still rely on oil and gas for 70% of our energy requirements as a nation. With an enhanced market need for asset maintenance and decommissioning, Costain also has opportunity to convert successes in Front End Engineering and Design ('FEED') activity into engineering, procurement and construction management contracts. The launch of Costain Upstream highlights the Group's commitment to capitalise on the substantial growth in the UK market, with a two-fold increase in the number of exploration wells expected in the next two years. Costain Upstream will leverage its already established market position to become a trusted supplier of choice across whole-life services.

Information concerning the Group's activities in these sectors are described on pages 26 and 27. Additional information together with examples of our work can be viewed on our website: **www.costain.com/engineering-tomorrow**

The Costain difference

04 Our business divisions

We have two core operating and reporting divisions within our business:

Infrastructure

The Infrastructure division delivers engineering solutions for principal infrastructure providers in:

Rail

A leading provider of multi-disciplinary projects for Network Rail, Crossrail and LUL. Currently delivering major projects principally focused on transportation hubs, most recently at London Bridge, Reading and Bond Street.

Highways

Delivering major programmes for the Highways Agency, Welsh Government and local authorities. Maintenance under the current MAC contracts and Early Contractor Involvement works.

Power

Focusing on thermal generation, new nuclear, offshore wind, transmission and distribution. Currently delivering major tunnelling works for National Grid.

Airports

Delivering programmes of work across airport assets at Heathrow, Gatwick and Manchester.

Additional information relating to the Infrastructure division can be found on page 26.

Natural Resources

The Natural Resources division delivers engineering solutions in:

Water

A leading provider of capital framework and maintenance framework programmes under the current AMP5 arrangements. Providing water services to commercial and industrial customers.

Nuclear Process

Major frameworks and capital schemes delivered across a number of the UK's strategic assets.

Waste

Delivering major waste schemes in the UK.

Oil & Gas

Developing and implementing solutions for the upstream and downstream oil and gas and chemical sectors in the UK and Middle East.

Additional information relating to the Natural Resources division can be found on pages 26-27.

Costain regularly announces key stakeholder information in the 'News' section of its website: **www.costain.com/news**

05 Our service lines

To reflect our value proposition and as we continue to broaden our services and enhance our product range, we have evolved our business architecture to meet the changing needs of our major blue-chip customers. We deliver integrated solutions across six service lines.

Advisory and concept development

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

Specialist design

Complex and niche engineering solutions.

Programme management

The operational and commercial management of programmes of complex inter-related projects.

Complex project delivery

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

Technology integration

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

Asset optimisation and support

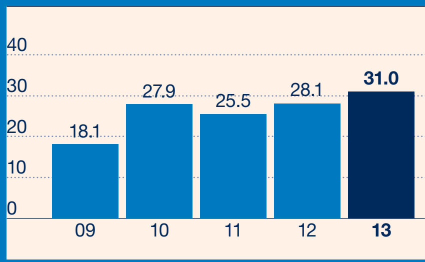
Long-term contracts to operate and maintain physical infrastructure assets.

06 Delivering shareholder value

Adjusted profit before tax £m

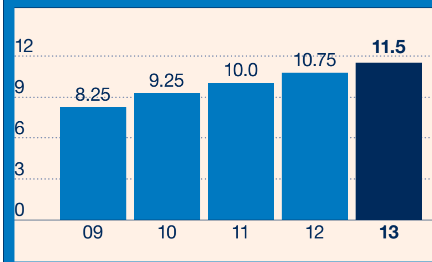
KPI

Target: In line with business plan.



Adjusted profit before tax is a key measure for the Group and incorporates interest, including the IAS 19 pension interest. The adjusted profit before tax in 2013 increased due to a strong underlying performance in the Group.

Dividend per share pence



Costain has delivered another strong performance in 2013 and our confidence in the Group's future is reflected in the Board's decision to increase the final dividend for the seventh consecutive year.

Together with our strong order book and increase in profits, we are continuing to deliver shareholder value.

Principal risks and uncertainties

Managing risk through our business

This section highlights the principal risks and uncertainties facing the Group.

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

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

Risk and Impact	Mitigation
Economic conditions • Change in Government policy on spending. • Loss of material contract. • Failure of customers/subcontractors/suppliers/joint venture partners.	The Group focuses on targeting and working with blue-chip customers whose spending plans are driven by national need, regulatory commitments or essential maintenance requirements. The Group also regularly monitors the pipeline of opportunities available and develops relationships with customers across a range of markets in both the private and public sectors. The Company seeks to ensure that it is not over-reliant on any one subcontractor, supplier or joint venture partner. In addition, the Company maintains a list of preferred subcontractors and suppliers which is reviewed regularly. The Company also undertakes financial monitoring of subcontractors and suppliers and endeavours to maintain a dialogue with them in order to identify any issue or cause for concern. The Company has in use an external audit system to ensure compliance by its preferred and strategic suppliers.
Winning new work • Working capital impact of moving away from fixed price contracts towards target cost. • Failure to estimate accurately risks, costs, contractual terms. • Competition and failure to win work.	Target cost contracts tend to have less advantageous cash flow characteristics but they benefit from generally being lower-risk than lump sum contracts. Costain has defined delegated authority levels for approving all tenders. All significant contracts are subject to review by the Investment Committee. To mitigate the cost risk, experienced and qualified staff are used to prepare bids, which are subject to internal review and approval before submission. During the life of the contract, regular project manager's report meetings and end forecast meetings take place to discuss safety, progress, quality, cost, financial performance, risk, etc. The Company's strategy of targeting blue-chip customers with committed long-term capital and operational spending plans will enable us to continue to pursue and win work less affected by the downturn. The Company's ongoing drive, both organically and by acquisition, to broaden its skills and services, along with its strong brand and excellent reputation for delivery, will also provide us with a competitive edge.

The overall effectiveness of the Group's risk management programme can be viewed in the Audit Committee report on pages 55-57.

Risk and Impact	Mitigation
Operational delivery • Cost overruns, time overruns, disallowed costs. • Design faults. • Procurement delay or failure. • Failure to obtain/renew insurance or refusal of claim by insurers.	Work on site is audited by in-house specialists and reports prepared so that corrective action, where required, can be taken. A senior executive is responsible for overall quality issues, the updating of best practice and ensuring compliance. The senior executive is also responsible for reviewing and updating the Company's procedures in line with the changing business.
Health and Safety • Major incident exposing an inadequate safety regime.	Costain has detailed Health and Safety policies in place. Regular Health and Safety visits by experienced professionals and on-site training take place to reduce the risk of human error. Any breaches in procedures are reported quickly and acted upon as appropriate. Employees are encouraged to take responsibility for safety in their work areas. A Health and Safety committee also meets monthly to develop a consistent approach and consider best practice.
People Failure to attract, develop and retain highly skilled management or personnel may limit the Group's ability to grow the business as anticipated.	The Company has in place a well-developed succession planning process which is regularly monitored. This process includes carrying out 'talent reviews' and encouraging ongoing development at all levels. The Company seeks to actively engage with employees through engagement surveys and its Employee Consultative Committee. Pay and conditions of employment are also regularly reviewed against the prevailing market and benchmarked against competitors to ensure that the Company remains competitive at all levels.
Pension liabilities The Group operates a defined benefit scheme which was closed to new members from 1 June 2005 and was closed to future accrual on 30 September 2009. The current deficit on the scheme is £37.2 million (before deferred tax). If the market value of the scheme's assets decline in relation to its assessed liabilities, the Group may be required to increase its cash contributions to cover funding shortfalls, which could have an adverse impact on the Group's operational results.	The valuation under IAS 19 for the scheme as at 31 December 2013 valued the scheme's assets at £592.5 million and liabilities of £629.7 million. An actuarial valuation of the scheme as at 31 March 2010 was concluded during 2010 and Costain agreed a deficit recovery plan with the Trustee. A full actuarial valuation is being carried out as at 31 March 2013. The value of the deficit recognised in the Group's balance sheet pursuant to IAS 19 is dependent on certain critical assumptions, including mortality rates, pension increases, investment returns and inflation and is likely to vary from year to year. The Company reviews the options regarding what actions Costain can take to mitigate its long-term risk and consults professional advisers as necessary.
Acquisitions Failure to integrate successfully an acquired business or recognise and mitigate new and related risks could have a damaging impact on the Group's future revenue and profits.	Full due diligence is carried out before any acquisition is made. Integration plans are put in place and managed by a dedicated team.
Failure of IT systems Failure of IT systems, inability to manage and/or to integrate IT systems, as well as the failure to store key documentation securely, could cause financial loss to the Group and expose the Company to breaches of legislation and fines.	A senior executive is responsible for the IT systems and has a suitably qualified team in support. Critical areas are subject to testing and include rapid recovery as well as sound data backup procedures. Online security training is provided for safe usage and storage of documentation.

Divisional performance

We continue to focus and prioritise our Group-wide resources, and our customer-aligned divisional structure, on identifying the most attractive new business opportunities across the sectors in which we operate.

Infrastructure

The Infrastructure division, which incorporates activities in the Highways, Rail, Power and Airports sectors, experienced another year of profit growth as customers invested in upgrading and renewing the UK's infrastructure assets.

Revenue was £560.6 million (2012: £494.9 million) whilst adjusted profit from operations rose over 30% to £31.4 million (2012: £23.5 million) as we delivered excellent performance across the division including the award of gain-share on a number of contracts. The order book for the division has grown to £1.9 billion (2012: £1.5 billion) and the level of tendering activity remains high, particularly in the highways, rail and power sectors.

In Highways, Costain is benefiting from the development of its innovative technology offering, developing and delivering complex solutions for the Welsh Government's All-Wales Technology framework and the Highways Agency. The Group continues to be a leading supplier to the Highways Agency, with a large portfolio of design, construction and maintenance projects for this customer. During the period, some major projects, such as the M1 J10-13 Managed Motorway and Walton Bridge across the Thames, were completed, whilst a new contract to deliver the A160/A180 Port of Immingham Improvement scheme in North Lincolnshire was secured. The Group's three Managing Agent Contracts ('MACs') all performed well with one of them, the five-year highway maintenance contract for the East Midlands, being awarded a two-year contract extension. During the year, the MAC10 contract came to the end of its term and was renewed with another party.

Costain was also awarded a place by Transport for London (a new customer for the Group) on its Early Contractor Involvement ('ECI') and Construction framework, worth approximately £200 million overall. The Group's first project within this framework, the Hammersmith Flyover strengthening project, is now well underway.

In Rail, the division experienced growth in both revenues and order book. Significant milestones were reached on the major London Bridge Station redevelopment contract, and works at Reading Station and on the complex Bond Street upgrade project continued to progress well. The Group continues to be a major partner to Crossrail, securing its eleventh contract with this customer during the year for Paddington New Yard.

The Group's investment in developing its programme management and rail engineering capabilities continues to yield benefits. During the year, three railway systems contracts for Crossrail were secured and these are progressing well, as is the delivery of the West Coast Main Line power upgrade contract for Network Rail. Costain is also involved in providing consultancy services for HS2.

In Power, the Group is now a major contract partner in the construction of the new Hinkley Point C nuclear power station in Somerset, providing the design and delivery of the water cooling systems. During the year, Costain was also awarded a place on UK Power Networks' £40 million power transmission framework contract. The Group also consolidated its position as a leading player in power station maintenance, with work being carried out for SSE, E.ON and Scottish Power. Good progress continued to be made on the London Cable Tunnels project for National Grid, as part of its investment to upgrade the power infrastructure in the South-East.

Costain continues to be active in the Airports sector, where there is growing pressure to increase the capacity of the UK's aviation infrastructure to accommodate economic growth. The Group is a Tier One supplier on the Heathrow Framework and at Manchester Airport.

Natural Resources

The Natural Resources division, encompassing the Water, Oil & Gas, Nuclear Process and Waste sectors, was established in November 2012, combining most of the Energy & Process and Environment Divisions and some support service activities previously in Infrastructure.

Customer spend in this market is underpinned by regulatory and legislative requirements and we expect this to grow over the medium and long-term to meet the energy and water needs of the UK's rapidly growing population.

Revenue (including share of joint ventures and associates) in the division for the year was £397.6 million (2012: £437.7 million), with adjusted profit from operations, including £9.1 million profit on sale of interest in associates, of £12.8 million (2012: £19.5 million including £10.5 million profit on sale of interest in joint venture). The reduction in revenue reflected the prioritisation of resources towards attractive opportunities for growth across the Group. Operating profits in this division declined in the period as a result of those lower revenues, additional costs to complete a small number of projects, and restructuring and business development costs including the deployment of new skills and capabilities under a strengthened leadership team. The division finished the year with a forward order book of £1.1 billion (2012: £0.9 billion).

In Oil & Gas, Costain announced during the year the launch of Costain Upstream, which combines the ClerkMaxwell and EPC Offshore businesses, the latter was acquired in August. Costain Upstream will provide engineering and advisory services in the upstream oil and gas market, where there are significant opportunities to secure work in this high-value, highly specialised area.

Elsewhere in the sector, the Group continued to deliver high complexity projects for blue-chip customers: the Easington contract for Centrica was completed, and significant progress was made on the Barrow Terminal Optimisation project for the same customer; the scheme is expected to be complete by 2015.

The Group is continuing to deliver support services for the Oil and Pipelines Agency ('OPA'), implementing a programme of upgrades and improvements in performance across OPA's network of jet fuel pipelines and storage facilities.

Work in Nuclear Process was dominated by the achievement of all major contractual milestones on two very significant projects. The Evaporator D construction project at Sellafield saw the successful delivery of the final module-920 in October, and the Fuel Element Debris ('FED') dissolution construction at Bradwell entered into the final construction and full-time commissioning phases. In addition, as one of two suppliers to the Magnox framework contract, additional facilities were delivered and continue to be maintained. It is expected that the sector's frameworks within the Nuclear Decommissioning Authority ('NDA') estate will continue to bring repeat-order business into the Group's overall portfolio.

In Water, 2013 saw significant bidding activity associated with the next five-year Asset Management Programme cycle ('AMP6') and Costain secured the sector's first AMP6 contract for Thames Water, whilst also retaining a place on the Severn Trent Water AMP6 programme. The Group has also prequalified for further AMP6 long-term contract opportunities.

Costain has continued the successful delivery of its AMP5 framework contracts with Northumbrian Water, Southern Water, United Utilities, Severn Trent and Welsh Water whilst also continuing to deliver large capital wastewater treatment schemes for Liverpool and Brighton & Hove, the latter of which won Major Project of the Year at the 2013 British Construction Industry Awards.

In Waste, the Group is completing the PFI contract for the Greater Manchester Waste Disposal Authority, which utilises a range of sophisticated waste management technologies. Of the 46 waste facilities under the contract, 36 have reached final acceptance, three are seeking to obtain final acceptance, six are currently in the post-completion (warranty) period and one remains to be completed. Design faults have been identified at four sites, including the site that remains to be completed, and remedial work and testing is ongoing in respect of that site. Costain is in discussions with relevant contract counterparties and the Group's insurers regarding the issues that have arisen and expects a successful outcome to discussions.

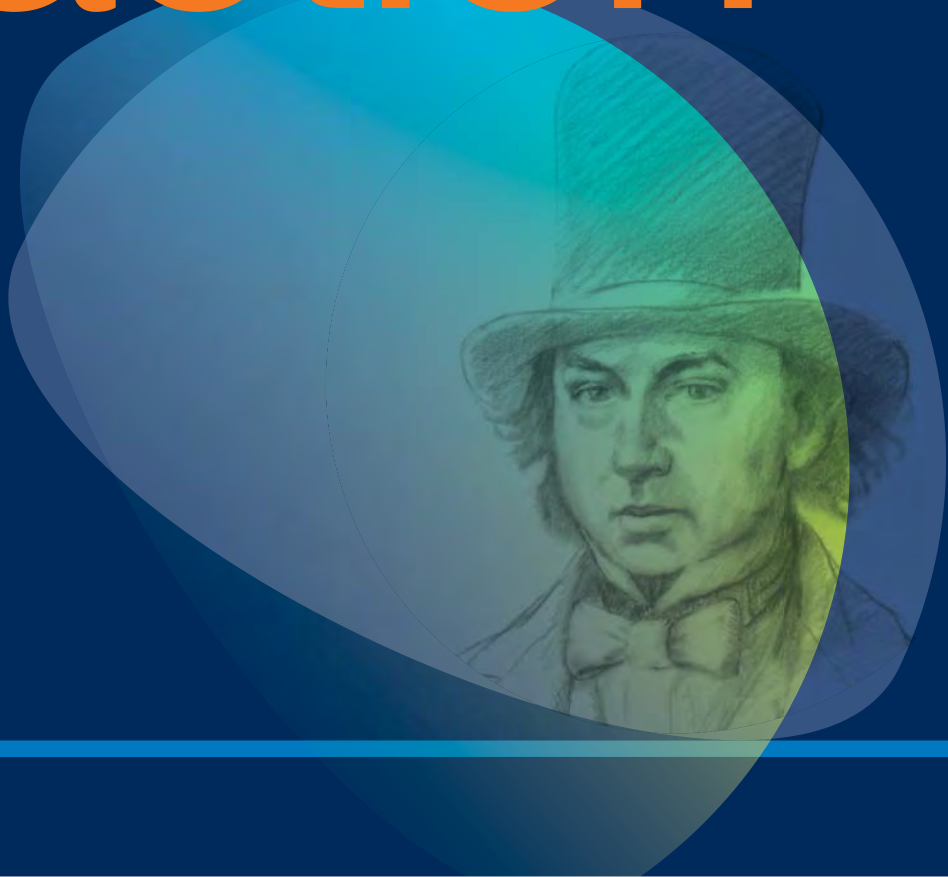
Land Development

Our non-core Land Development activity in Spain undertaken in a 50:50 joint venture with Santander Bank continued to be subject to challenging market conditions. The joint venture has a portfolio of in excess of 500 hectares of land in Southern Spain with varying levels of planning approval and, although the Spanish economy is showing some early signs of improvement, there remains considerable uncertainty as to when significant recovery will be achieved. As a consequence of continuing uncertainty regarding future market conditions, a non-cash impairment has been taken against the assets, the Group's share of which is £9.8 million, reducing Costain's total carrying value in the joint venture to £26.6 million.

As anticipated, no significant land sales were completed in the year, and revenue was £1.8 million (2012: £1.9 million) and the loss after tax was £2.1 million (2012: £2.3 million), excluding the exceptional asset writedown outlined in the previous paragraph.

Our activities have continued to focus on our leisure businesses of golf courses and our 624-berth yacht marina adjacent to Gibraltar, both of which have reported improving revenue streams, particularly in the marina where our new boat repair yard is in demand and is assisting in raising marina occupancy.

Engine
Tomorr
‘in action’



ering
ow...

Engineering Tomorrow is the Costain strategy aimed at identifying, developing and implementing innovative solutions to meet the UK's major national infrastructure needs.

Costain has implemented a number of schemes which will enhance the quality of project delivery, develop the skills and ideas of its people and provide cost-effective solutions, all in support of ***Engineering Tomorrow***. The strategy relies on sharing knowledge and applying best practice across the Costain Group.

Costain places high priority on innovation and this can be seen in the Company's technological and organisational initiatives, in addition to skills-based training and the determination to be more socially responsible, at all times, to the needs of Costain stakeholders.

The following pages provide examples of
Engineering Tomorrow... 'in action'

Engineering Tomorrow... 'in action'

Additional information about ***Engineering Tomorrow*** can be found online: **www.costain.com/engineering-tomorrow**

Engineering Tomorrow... 'in action'

A new approach to carbon capture

Carbon capture – reducing the amount of CO_2 pumped into the atmosphere – is vital to help control climate change.

Current carbon capture technology requires the installation of massive solvent scrubbing 'absorber' columns.

The visual impact of these is considerable – less so with coal-fired power stations, much of whose existing infrastructure is tall, but a major problem with 'low-rise' gas-fired stations.

Costain is collaborating with Edinburgh University on novel designs of absorber column with an emphasis on modularisation.

The project is looking at fundamental modelling such as the flow of gases and liquids. It is thought that alternative column designs will also involve shorter construction time, be easier to upgrade in the future, and possibly more cost-effective.

Results of the year-long project will be published by mid-2014.

Engineering Tomorrow... 'in action'

Tracking passenger flows through rail hubs

Problem: How to accurately measure passenger usage of a railway station where many travellers use it only to change trains and therefore never pass through the gatelines?

Answer: Costain has applied its COpath solution, provided in partnership with Path Intelligence, which uses sensors to detect signals emitted by mobile phones carried by passengers using the station. The sensors allocate an anonymised designation to each telephone and record its movements, creating a detailed picture of passenger flows.

Costain has pioneered COpath's first use in the UK rail sector. It allows station and airport operators to understand passenger movements and behaviours to, among other things, reduce congestion and increase non-fare revenues.

Its successful trial at one station has led to installation contracts for several more.

- Operate safely, efficiently and responsibly
- Continue to enhance customer insight
- Grow by broadening and integrating our services
- Develop best-in-class team
- Create and deliver innovative sustainable solutions
- Working in collaboration

Engineering Tomorrow... 'in action'

Smart motorways

Sometimes, innovation is about behaviours and not just new technology.

In 2009, Costain entered a partnership agreement to develop what are now known as 'smart motorways'.

This is a way of creating more capacity from the existing road network at a fraction of the cost of building new lanes. Motorists can use the hard shoulder as a permanent running lane or when instructed by signals on overhead gantries.

"The innovation that we can be the most proud of is working together," says Highways Programme Director Tony Scutt. "I've been in meetings where six contractors were sharing ideas for the benefit of everyone. Getting that behavioural change of collaboration is the real ground-breaking part of this contract."

This collaborative programme approach has led to the Department for Transport's 20% efficiency savings target against the Highways Agency's project estimates being exceeded.

Engineering Tomorrow… ‘in action’

Additional information about ***Engineering Tomorrow*** can be found online: **www.costain.com/engineering-tomorrow**

Engineering Tomorrow… ‘in action’

Managing Mobicloud to improve site efficiency

Mobicloud is a European Union-funded project to develop a ‘corporate app store’ – part of the EU’s Competitiveness and Innovation Framework Programme.

It is deployed in both Android and IOS tablets that are planned to connect to Costain’s corporate systems via a cloud-hosted platform; the Group believes it is one of the leaders in deploying the system in the construction industry.

Mobicloud’s first development with Costain is a site diary app that allows engineers to record details or events as they happen while out on site. This aids accuracy and saves time.

A joint effort with Sheffield University is underway to develop further apps to estimate volumes and to replace traditional paper-based survey books. The ultimate aim is to have a suite of apps bespoke to Costain.

Engineering Tomorrow… ‘in action’

Bridging the gap with a robot tug

Using miniature robot ‘tugs’ to help rig new cables between electricity pylons high across roads or railways is not new. But getting approval for their use in a fraction of the normal three to four years, is. And that’s what Costain anticipates in 2014.

The battery-powered, remotely-controlled tug system developed by Costain and subcontractor partner TLI is designed to eliminate the large, expensive scaffolding structures normally required before initial ropes and pulley blocks can be strung between pylons. Once in place, new cables can be hauled through the pulleys.

Getting the tug approved involves considerable methodology and effective planning to prove the tug’s safety.

Far faster than traditional methods of rigging new cables, Costain believes this could potentially save its client several hundred thousand pounds in 2014 alone.

- Operate safely, efficiently and responsibly
- Continue to enhance customer insight
- Grow by broadening and integrating our services
- Develop best-in-class team
- Create and deliver innovative sustainable solutions
- Working in collaboration

Engineering Tomorrow... 'in action'

BIM brings down barriers among project team

Getting designers and site personnel to talk the same language can be problematic. At the upgrade of London Bridge Station, Costain and Building Information Modelling ('BIM') are solving that problem.

BIM involves creating an intelligent, virtual 3D model of a facility. At London Bridge design consultants and specialist subcontractors are sharing highly-detailed 3D models. This enables collaborative reviews of progress.

Engineers concerned about measurements on a project document, for example, can now simply send a screenshot taken from the model to the designer asking for confirmation of its accuracy.

The team is also in the process of piloting an innovative mobile form-filling app solution that will allow site engineers to complete multiple forms electronically using iPads. This will reduce the need for paper forms on site.

Engineering Tomorrow... 'in action'

Cutting the cost of carbon capture

Costain's heritage of gas processing expertise is being directed towards a new avenue. Research is underway to remove CO_2 from a new generation of coal-fired power plants by processing the gas stream at low temperature to separate the CO_2 in liquid form.

This approach has been patented by Costain and holds out the promise of reducing the substantial costs currently associated with carbon capture, which is a major front in the battle to minimise climate change.

If less costly methods of removing CO_2 can be developed, the likelihood of implementation by public or private sector energy producers is increased.

If successful, the fruits of this research will be available in the 2020s.

Costain Cares

We are committed to delivering projects and services responsibly and sustainably. Ensuring that we meet our customers' and society's needs while managing the social, environmental and economic issues that impact our business either directly or through our supply chain. Through stakeholder engagement and by assessing our impacts and level of influence, we have identified key priorities that are material to our business. Costain Cares, our Corporate Responsibility strategy and vision to build a longer-term sustainable business that creates economic, environmental and social value, was launched in 2011. Costain Cares is based on three fundamental pillars:

Relationships

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

- provide a working environment where the health of our people is protected, their wellbeing is enhanced and everyone returns home safely at the end of the working day;
- support the local communities in which we operate, ensuring we leave a lasting legacy;
- attract, retain and develop the best people for the Costain Group;
- provide sustainable solutions and the highest standards of service for our customers; and
- operate a collaborative, responsible supply chain where our partners support us in delivering efficient, innovative, sustainable solutions.

Our Environment

We operate in the built environment, where we meet national needs for strategic investment in infrastructure. We compete in the economic environment, where we must deliver value for customers and shareholders. We have to deliver responsibly to the natural environment for the benefit of everyone. We will work with our customers and supply chain to, where possible:

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

The Future

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

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

A detailed review of our approach to Corporate Responsibility can be found on our website:
www.costain.com/responsibility

Costain Cares... 'in action'

Relationships

BeSafe

Health and Safety

The Health and Safety of our workforce remains our overriding priority. During 2013, we continued to focus on promoting a positive Health and Safety culture where everyone is supported to work safely and encouraged to take responsibility for keeping themselves and others free from harm in the workplace. We continued to develop our already robust Health and Safety systems in order to further improve our performance on our sites and in our offices.

Accidents and incidents

In January 2013, we received a Prohibition Notice in respect of insufficient cover over exposed pipelines across the traffic route on one of our sites. Following the issue of the notice, a comprehensive action plan was drawn up and agreed with the regulator to address the shortfalls identified.

Please see page 13 for details of the Group's Accident Frequency Rate.

We have developed and implemented a new toolkit for the investigation of serious accidents and incidents based on the Swiss Cheese model. The new methodology has not only significantly improved the identification of underlying and root causes of accidents/incidents, but has also enhanced the communication of lessons learnt across our business.

***Engineering Tomorrow...* 'in action'**

Additional examples of ***Engineering Tomorrow...*** 'in action' can be found on pages 28-33.

Leadership

We recognise the importance of visible and engaging Health and Safety leadership. Two successful Health and Safety Leadership Impact days were held across the business in May and October. Led by the two Managing Directors, the most senior personnel from across the business visited over 40 sites in order to engage with site personnel, reinforce Costain's Health and Safety message, and demonstrate commitment from the highest level.

Vulnerable road users

Following nationwide concern about the safety of cyclists and pedestrians on our streets, particularly in London, we introduced a number of measures in order to play our part in addressing this very serious issue. The measures include enhancements to the specification of vehicles rated greater than 3.5 tonnes, requirements with regard to registration with the Fleet Operators Registration Scheme and recommendations with regard to driver training. Adoption of these leading-edge standards aims to reduce the risk to vulnerable road users whilst also improving the safety standards of transport and construction vehicles, thereby contributing towards making our roads a safer place.

Health and wellbeing

BE HEALTHY

The health and wellbeing of our people is of vital importance to us. In order to improve the management of health and wellbeing at project level, a new key role of site Health Champion has been created. In addition, the site Health, Safety and Environmental Management Plan has been enhanced and now includes a specific Health section with the aim of ensuring that health issues are given the correct level of consideration in all relevant aspects of project management.

Corporate Responsibility
continued

Costain Cares

During 2013, we ran two Company-wide wellbeing campaigns. During the first quarter of the year, a pedometer challenge was initiated as a means of encouraging our workforce to become more active in a fun and sociable way. The second week-long campaign was during October and focused on how to maintain a healthy heart. Furthermore, our commitment to offering 'wellbeing' medicals to all staff continued.

In order to improve the competency of key members of our workforce, we ran a one-day bespoke Health course at venues across the country. The course, attended by our supervisors and health champions, provides guidance on how to manage the key health issues on our sites.

We continued to support the Public Health Responsibility Deal, a Department of Health initiative to improve public health and tackle health inequalities. In addition to honouring our public pledge with regard to staff medicals, our Group SHE Director became a member of the Construction Sub-committee, which developed and launched a collective pledge on behalf of the construction/civil engineering industry in October. A number of leading construction companies, including Costain, have signed up to this pledge, aimed at managing the causes of occupational disease and taking action to improve the health and wellbeing of their workforces.

Communities

We recognise that our work affects the communities in which we operate. How we manage our relationships and work with local communities and other stakeholders is vital. We are committed to developing and maintaining excellent relations with local communities.

Community engagement

Our projects develop and implement community engagement plans, which identify socio-economic issues specific to the local community and actions when Costain can work in partnership with the community to have a positive impact.

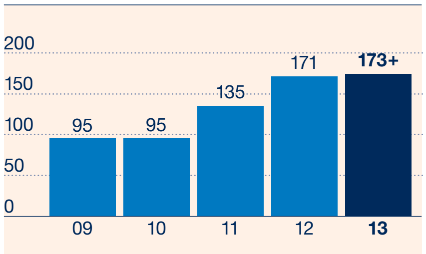
As an associate member of the Considerate Constructors Scheme, we are committed to the principles set out in the Considerate Constructors Code of Considerate Practice. In 2013, a number of our projects were recognised by the scheme. We received three Gold Awards, five Silver Awards, 10 Bronze Awards and two of our projects were runners-up in the Most Considerate Site Award. The awards recognise sites' excellent standards of consideration towards their neighbours, their workforce and the environment. Award winners are selected from the top performing 10% of sites registered under the Scheme.

Charitable giving and volunteering

Costain is pleased to be a patron of The Prince's Trust, the youth charity that helps change young lives, and a member of the Trust's Construction and Business Services Leadership Group. The Trust works with 13- to 30-year-olds who have struggled academically, have been in care, are long-term unemployed or have been in trouble with the law. In 2012 Costain, in collaboration with CITB-ConstructionSkills, the National Skills Academy for Construction and The Prince's Trust, secured Employee Ownership of Skills ('EOS') funding to provide 100 opportunities for young people to undertake the Trust's three-week 'Get into Construction' programme during 2013–2014. We are on target to deliver this commitment.

Proud to be a Patron of **The Prince's Trust**

Group charitable donations
£000



We continue to support various charities local to our operations and via the Costain Community Chest, where small donations are made by the Company to support employee charity involvement. In 2013, we donated over £173,500 to worthy causes.

Through our employee volunteering policy, we provide our employees with the opportunity to develop and share skills while making a valuable contribution to local communities.

Employment, education and skills

We work with a range of partners and organisations to offer employment and training opportunities in the communities where we operate.

In 2013, we became a 'Champion' business supporting a joint initiative between BITC and the Department for Work and Pensions, the 'Generation Talent' programme. The aim of the programme is to help businesses scale up the number of unemployed young people they recruit. It has a growing number of large UK employers (90+ so far) who have found that by making small changes to their recruitment process they can make more jobs available to talented unemployed young people.

Our people

We are focused on attracting, developing and retaining the best people and creating an environment where people can fulfil their true potential.

Building a diverse workplace

Costain is an inclusive employer and promotes equality and inclusion from recruitment and selection, through training and development, to promotion, reward, recognition and retirement. We are fully committed to the elimination of unlawful and unfair discrimination and we value the differences that a diverse workforce brings to the organisation. We support our supply chain and encourage its active commitment to our approach on equality and inclusion.

We have monitored our diversity profile for the last six years, which shows a fairly consistent profile of female and Black, Asian and Minority Ethnic ('BAME') employees.

Details of our diversity statistics can be found on page 17.

In 2012, Costain became a member of Business in the Community's Opportunity Now campaign to share ideas with other industries to improve the attraction and retention of women in the workplace. In 2013, we strengthened our commitment by becoming signatories to Opportunity Now's Project 28-40, a pioneering study into the experiences of women in the workplace. The focus of the study is to gain valuable insight and identify actions aimed at improving the attraction and retention of women. Our focus in 2014 is to deliver unconscious bias training and to continue to address the gender balance in the Group.

Developing our people

In June, we launched 'Find My Future', a series of career mapping tools designed to support both managers and employees with career development discussions. The tools include career inspiration and advice from leaders within Costain, a master schedule of current and planned job roles, career maps detailing possible career paths, and self-coaching tools to support employees to explore and discover many more opportunities beyond the traditional vertical promotion routes. We will continue to develop further career paths in preparation for our 2014 career development reviews.

During 2013, we promoted 316 employees and transferred over 400 employees into different sectors or disciplines within the business, creating new opportunities for individuals to broaden their experience, skills and capabilities.

We continued to invest in training and development for all our employees, delivering over 10,000 training days in 2013. We successfully led a consortium bid to secure EOS funding, enabling us to develop and deliver enhanced training to our supply chain. Our focus for 2014 is to refresh our suite of management, leadership and executive development programmes. We will be complementing our strong focus on project management development delivered through our Academy.

To ensure that we continue to develop and grow the Costain capability, we are active in attracting new talent to the business. We have continued to expand our award-winning graduate scheme which includes 11 diverse disciplines, from our traditional roots in civil engineering, quantity surveying, and chemical engineering, to English and business management. In 2014, we will broaden this further to encompass technology disciplines such as computer and data science. We increased our graduate intake to 61 in 2013, bringing our total cohort to 129. We have also significantly expanded our apprentice programmes. We recruited a further 31 apprentices in 2013 across 13 disciplines ranging from accountancy to track and signalling engineering and business administration. Since the relaunch of our apprentice programme in 2008, we have recruited 92 apprentices and have a current completion rate of 83%. In 2014, we will introduce higher apprenticeships and continue to broaden our schemes to cover project controls and BIM.

Please see page 41 for more information about our work developing skills for the future.

Costain Cares

Employee engagement and involvement
Engaging effectively with our people is crucial to the success of our business. The views of our employees are extremely important and we want our people to feel valued, listened to and rewarded. We maintain a strong communication network and employees are encouraged to discuss with management matters of interest and issues affecting the day-to-day operations of the Group. Employees are kept informed of the financial and economic factors affecting the Company's performance, and other matters of concern to them as employees, in various ways. These include regular updates from the Chief Executive and other senior managers, a Costain online news service, personal briefings and emails. Senior managers also visit sites and discuss with employees matters of current interest and concern to them and the business. Employees also have the opportunity to provide feedback and ask questions at the annual staff roadshows which take place around the country. Our established Employee Consultative Committee convenes three times a year and on an ad hoc basis throughout the year, to discuss matters impacting the business, in order that the views of employees can be taken into account in making decisions likely to affect their interests. The Company operates an employee share plan (the 'SAYE' scheme) which encourages and supports the ownership of shares in Costain and a further grant was made under this scheme during the course of 2013.

Following the acquisitions of ClerkMaxwell, Promanex and EPC Offshore and some significant TUPE movements in and out of the business during 2012 and 2013, we took the decision not to repeat our engagement survey in 2013 but to focus on developing a new survey in 2014. This will re-benchmark engagement data and develop and implement targeted improvement plans through our Employee Consultative Committee.

Reward and recognition
In February 2014, we hosted our Achieving Excellence Awards to recognise and celebrate the outstanding performance and contributions of our people and our supply chain.

Customers

Our aim is to provide sustainable, innovative solutions and the highest standards of service to our customers. We constantly strive to improve our performance and actively seek feedback from our customers. In 2013, we have been widely recognised for our sustainability performance from various external bodies, including:

Port Talbot, Harbour Way...
achieved a CEEQUAL (Civil Engineering Environmental Quality Assessment) Excellent Award and won the Best Conceptual Design category, in the 2013 Brownfield Briefing Awards, for the remediation works undertaken as part of the construction of the Harbour Way Scheme. The project was also highly commended in the Best Reuse of Material category.

Farringdon Station redevelopment
Following the project's 2012 CEEQUAL Excellent Award, it was awarded an Outstanding Achievement Award for Ecology and Biodiversity and was highly commended in the Historic Environment category. The project also won the Sustainable Excellence Award at the Network Rail Partnership Awards for its collaborative approach to delivering sustainable outcomes.

Welsh Water Coed Dolwyd Service water reservoir scheme...
won the Green Apple Wales National Gold Award, in recognition of the positive environmental impact and best practice work carried out on the site.

Paddington Station Crossrail...
was awarded the Green Line Award under the Crossrail Green Line Recognition Scheme, a unique and intelligent way for project teams to increase their environmental performance.

Supply Chain

We understand the economic, environmental and social impacts of our procurement activities and are committed to the responsible management of our supply chain. We ask our suppliers to share our values and standards and to support us in delivering efficient, innovative, sustainable solutions. In turn, we are committed to engaging and supporting our supply chain to ensure compliance, continual improvement and the achievement of mutual goals.

Supply chain engagement
We continue to prioritise supply chain engagement. In December, we hosted a supply chain engagement event, 'Engagement and Opportunities with Costain', in Newport, South Wales. The aim of the event was to increase supply chain diversity. Speakers included Dafydd Hughes, Head of the Construction Sector, Welsh Government and Alan Kay, Group Technical and Operations Director, Costain. In addition to this event, our projects hosted a number of local 'meet the buyer' events across the country.

In April 2014, we will host our fourth supply chain conference at Warwick University, which will be attended by senior representatives from our supply chain partners and senior management from Costain. The conference offers a chance for suppliers to hear about the future of working with Costain.

Costain regularly announces key stakeholder information on the 'News' section of its website: **www.costain.com/news**. Your opinions, views and questions about Costain matter to us. Please contact us via the home page of our website: **www.costain.com**

Sustainable procurement

Sustainable procurement for Costain means leading socially, environmentally and economically responsible procurement to deliver value and benefits to stakeholders. We have adopted the UK Government's Flexible Framework as the method through which we will develop our approach and measure our progress. In support of this commitment, we have updated our sustainable procurement policy and developed a guidance document, 'Delivering Sustainable Procurement', for our procurement staff and our current and future suppliers. In addition, to ensure our procurement teams approach sustainable procurement in a uniform manner, we have developed and piloted a sustainable procurement training module. The sustainable procurement module will be rolled out to all our commercial and procurement teams in 2014.

Save it

Our Environment

We continue to successfully manage our impact on the environment through implementation of our Environmental Management System, which is certified to ISO 14001:2004. We continue to focus on reducing the risk of any direct impact on the environment, and have widened our focus to assess and minimise the indirect impact of our activities.

Climate change

We remain committed to reducing our measured carbon emissions. In 2013, we published our first Climate Change Strategy, which clearly sets out our vision to be a leading provider of low-carbon solutions whilst also setting an exemplary standard of how the Company should manage and reduce its own greenhouse gas emissions and those of its customers. We have set ourselves the target of reducing carbon emissions intensity by 55% by 2020. The Climate Change Steering Group continued to co-ordinate Costain's approach to climate change and to demonstrate clear, visible leadership, to ensure that the Company is managing its impacts and maximising potential opportunities in providing low-carbon solutions to our customers.

In 2012, we achieved external accreditation of our carbon footprint to CEMARS ('Certified Emissions Measurement and Reduction Scheme') certification. The CEMARS standard includes independent verification of our emissions data and a yearly review to ensure we continue to deliver reductions in our emissions. We have successfully renewed this accreditation in 2013. Our method of reporting is in accordance and certified to ISO 14064-1. To date, we have achieved a 30.1% reduction in emission intensity against our 2009 baseline, demonstrating that we are on track to meet our 2020 target of a 55% reduction in emission intensity.

In addition to this footprint we also report in accordance with the requirements of the Companies Act 2006 (Strategic and Directors' Report) Regulations 2013. Please see page 13.

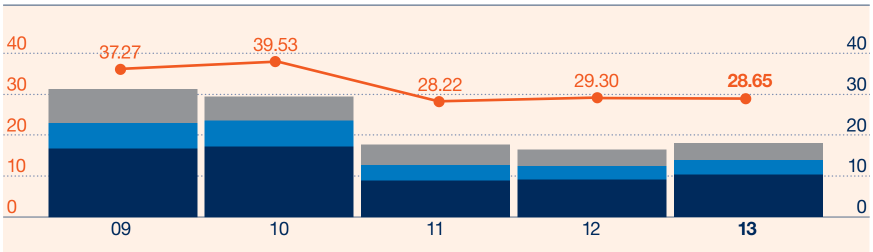
We also submit our data annually to the Carbon Disclosure Project ('CDP') – an independent, not-for-profit organisation that aims to increase transparency and promote climate change data as a factor in business, policy and investment decisions.

We were delighted to be named in the Climate Performance Leadership Index ('CPLI') as one of the best performing companies in the Carbon Disclosure Project's annual FTSE 350 climate change report. We achieved a score of 84A, highlighting the positive impact the company has made in measuring and driving down its greenhouse gas emissions. We are also the only FTSE SmallCap company to achieve band 'A' status in 2013, and only the second small-cap company to achieve an 'A' band rating since the ratings were introduced in 2009.

Resource management

We continue to drive down the amount of waste going to landfill, and we strive towards zero waste to landfill. In June, a Waste Reduction & Recycling campaign was implemented Company-wide to coincide with National Recycling Week, the aim to reduce the quantity of waste produced on our projects and in our offices and to ensure that recycling is maximised.

CO_2 equivalent emissions
tCO_2e per £m turnover/'000 tCO_2e



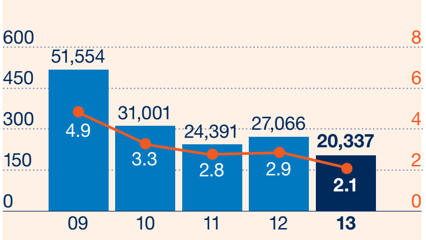
- Scope 3 – Other indirect emissions (employee business travel, emissions from water usage and waste disposed to landfill)
- Scope 2 – Indirect emissions arising from electricity consumption
- Scope 1 – Direct emissions arising from our operations (fuel combustion, Company-owned or leased vehicles)
- Emissions intensity (tCO_2e/£M)

Figures are reported in accordance with ISO14064-1:2006 and reflect UK operations within Costain's direct operational control.

Corporate Responsibility
continued

Costain Cares

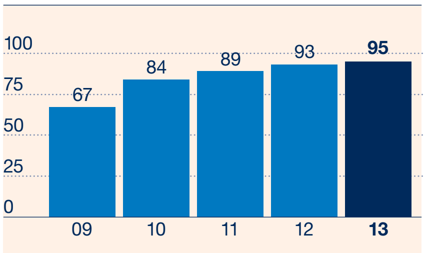
Construction waste removed from site
'000 tonnes of waste/tonnes per £100,000 turnover



■■ Tonnes of waste removed from site
■ Tonnes per £100,000 turnover

Figures are reported in accordance with WRAP Waste Measurement and Reporting Guidance. Turnover figures reflect operations reporting waste. 2009–2011 figures relate to UK operations excluding MAC joint ventures and 2011 acquisitions. 2012 figures reflect all operations but exclude our MAC 10 joint venture and Alcaidesa operations and the associated turnover.

Waste diverted from landfill
%



Figures are reported in accordance with WRAP Waste Measurement and Reporting Guidance. Turnover figures reflect operations reporting waste. 2009–2011 figures relate to UK operations excluding MAC joint ventures and 2011 acquisitions. 2012 figures reflect all operations but exclude our MAC 10 joint venture and Alcaidesa operations and the associated turnover.

We have successfully increased our total waste diverted from landfill to 95% compared to 93% in 2012 and 87% of construction waste diverted from landfill compared to 85% in 2012.

Protecting the environment
We are committed to minimising our impact on the environment ensuring, where possible, that our activities do not result in damage and that we reduce our overall environmental incidents year on year. We ensure that all environmental incidents are reported and investigated to capture lessons and prevent recurrence.

Engineering Tomorrow... 'in action'

Harbour Way, Port Talbot

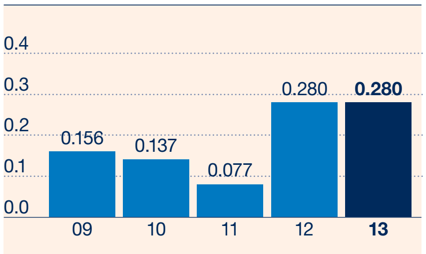
The Harbour Way dual carriageway links the M4 Junction 38 to Port Talbot and its docks. The route passes through an area of the Port Talbot Steel Works site which has an extensive historical legacy and is an area of land that was grossly contaminated from previous heavy industrial uses. Through the implementation of a remediation strategy and a material management plan, an estimated 23% saving in CO_2e was realised through techniques such as the remediation and reuse of previously contaminated soils, and sourcing fill materials locally.

Prior to construction over 1,800 reptiles were translocated to new receptor sites. Areas of grassland identified as suitable habitat for the Small Blue Butterfly (a UK Biodiversity Action Plan species) were also moved prior to construction and additional replacement habitat was provided along the scheme corridor. Over 15,200 new trees and shrubs were planted in the landscaping scheme and a Sustainable Urban Drainage System ('SUDS') was incorporated into the drainage design with planted swales and ponds to provide additional habitat and reduce flood risk.

The project's achievements were recognised by winning a CEEQUAL Excellent Award as well as Best Conceptual Design in the Brownfield Briefing Awards.

Additional examples of ***Engineering Tomorrow...*** 'in action' can be found on pages 28-33.

Environmental incident frequency rate
Number of environmental incidents per 1,000,000 man hours



Our reported environmental incidents and the associated environmental incident frequency rate ('EIFR') in 2013 remained at 0.28. We have, however, reduced the number of significant and minor incident compared to 2012. We recorded four significant incidents compared to seven in 2012 and 76 minor incidents compared to 78 in 2012.

No major incidents were reported in 2013 and no environmental prosecutions, cautions or notices were received. We have received no environmental prosecutions, cautions or formal notices since 2004.

Training
During 2012–2013, Costain took a lead role developing a CITB-accredited environmental training course, the Site Environmental Awareness Training Scheme, ('SEATS'), which was launched by Group SHE Director, Peter Fisher, in February. Costain is a registered training provider for SEATS and we intend to rollout SEATS as a mandatory requirement for all site supervisors and managers. During the year, we have trained a total of 143 Costain employees and 95 sub-contractors, and three courses have already been run as part of Costain's supply chain academy.

The Future

In 2013, we underlined our continued commitment to sustainable development by signing the Welsh Government's Sustainable Development Charter. Signing the Charter is a voluntary commitment to making sustainability central to business, promoting and delivering environmental, social and economic wellbeing through decisions and operations, and sharing the learning from that journey.

Developing skills for the future

We recognise the importance of engaging with schools, colleges and universities to ensure we attract young talent into our organisation, build a sustainable pipeline of talent for the future and support local communities where we operate. Through our Engineering Futures programme, we aim to raise the awareness and aspirations of young people to find out more about careers in engineering and related industries. We have over 100 ambassadors across the Group who volunteer their time to go into schools to inspire young people in Science, Technology, Engineering and Maths ('STEM') subjects. In addition, we offer inspirational work experience to young people, aiming to make their experience of the world of work more accessible and meaningful.

We have also joined forces with innovative careers website 'plotr' to encourage more young people to consider a career at Costain. 'Plotr' is an online careers service for 11- to 24-year-olds that is free for young people, parents and teachers to use. Founded in 2011, 'plotr' is a not-for-profit Community Interest Company that combines input from careers advisers, youth organisations, teachers, leading technology and social media companies and hundreds of young people to create an innovative and informative careers advice platform. Working with 'plotr' we have created the 'Costain Career World' to represent the sectors the Company operates in and included 11 job roles to demonstrate the various careers available within the Group. The jobs are a mix of entry-level and aspirational roles and the site offers advice about how you get started, what skills are needed, what qualifications are required and what salary might be expected. There are also short video clips of Costain employees talking about their role, how they got started, what their key skills are, what they love about their job and, as with all jobs, what the biggest challenges are.

The site is regularly updated with vacancies for work experience, apprenticeships and graduate training positions, as well as forthcoming employment events and seminars.

Supply chain academy

In 2012, we launched the Costain supply chain academy, an initiative that aims to support and develop small and medium-sized enterprises. To date, 45 suppliers have been through the academy, where representatives attend 19 learning modules covering business administration, commercial and financial best practice, insurance, Health and Safety, behavioural safety and quality. We are pleased with feedback received to date and are planning to support a further 30 suppliers through the academy in 2014.

Corporate Responsibility
continued

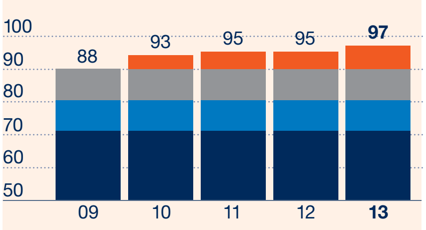
Costain Cares

Our performance
Costain achieved the highest ranking in BITC's annual benchmark of responsible business management, the Corporate Responsibility Index ('CR Index'). The CR Index is the UK's leading and most in-depth voluntary benchmark of Corporate Responsibility. It has been run by Business in the Community for over a decade to help companies: accurately measure and manage all aspects of their social and environmental performance; shape how they integrate and improve Corporate Responsibility throughout their business operations, and benchmark themselves against competitors.

A new banding in the Index for 2013, Platinum Big Tick, is designed to challenge leading companies with 'stretch questions' on topics such as their long-term planning and the unique contribution their business can make to create transformational change and a sustainable economy.

Achieving Platinum Big Tick status means that Costain can demonstrate that it is thinking about how global mega trends, such as population growth and resource scarcity, are affecting the future strategy of the business. The banding is an indication that it is making long-term investments to improve or launch new environmentally and socially sound products and services, and is embedding responsible values throughout the workforce.

Business in the Community Corporate Responsibility Index performance and band thresholds
%



Bronze ≥ 70.00%
Silver ≥ 79.76%
Gold ≥ 89.76%
Platinum ≥ 94.76%

In 2011, BITC renamed the CR Index 2010 as CR Index 2011 to reflect the year the results were published.

Engineering Tomorrow... 'in action'

The Big Infrastructure Conversation

In September Costain, in conjunction with Business in the Community, hosted The Big Infrastructure Conversation at London's City Hall. On the day students, ambassadors, apprentices and trainees met business leaders and discussed their own apprenticeship experiences, the importance of inspirational work experience and skills. For the industry leaders, there was also an opportunity to share best practice about how businesses can tackle youth unemployment and to listen to young people about their needs, hopes and ambitions for the future, particularly in relation to securing valuable career advice.

Additional examples of ***Engineering Tomorrow...*** 'in action' can be found on pages 28-33.

Costain Cares: our 2020 vision
In 2011, we launched our Corporate Responsibility strategy, Costain Cares, setting out our vision for 2014. This year, we will undertake a full review of our 2014 vision, report on our achievements and, in an aim to ensure continual improvement, launch our 2020 vision.

Additional information concerning our Costain Cares strategy can be found online: **www.costain.com/responsibility**

Finance Director's review

Tony Bickerstaff
Finance Director

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

The Group generated a 12% increase in underlying[1] operating profit to £27.4 million (2012[2]: £24.5 million) on Group revenue, including share of joint ventures and associates, of £960.0 million for the 12 months to 31 December 2013 (2012: £934.5 million). The increased profitability reflects the Group's continued focus on higher margin work.

Profit before tax, before other items[3], for the year ended 31 December 2013 increased to £31.0 million (2012[2]: £28.1 million). Basic earnings per share, before other items[3], amounted to 44.1 pence (2012[2]: 39.7 pence per share), reflecting increased profits and a tax timing benefit. Reported basic earnings per share were 18.8 pence (2012[2]: 35.4 pence).

1 Underlying operating profit is before Other items (amortisation of acquired intangible assets and employment related and other deferred consideration and in 2013 £3.7 million one-off costs associated with the offer for May Gurney Integrated Services plc) and in 2012 excludes the £2.8 million one-off costs resulting from pension scheme liability actions.
2 Restated for revised IAS 19 Employee benefits accounting standard.
3 Other items are the amortisation of acquired intangible assets of £1.8 million (2012: £1.7 million), employment related and other deferred consideration of £2.8 million (2012: £1.7 million) and in 2013 the £3.7 million one-off costs associated with the offer for May Gurney Integrated Services plc and the non-cash impairment of £9.8 million on carrying value of assets in non-core Land Development activity in Spain.

In 2013, the Group sold its minority shareholdings in three joint venture companies as part of the continued disposal of its PFI equity portfolio, for an aggregate consideration of £12.0 million. The Group realised a profit of £9.1 million as a result of the sale.

The Group has reassessed the carrying value of the assets in its non-core Land Development activity in Spain, and as a consequence of continuing uncertainty regarding future market conditions, a non-cash impairment has been taken against the assets, the Group's share of which is £9.8 million.

In 2012, the Group transferred two PFI investments into The Costain Pension Scheme ('CPS') at an agreed value of £20.3 million which resulted in a profit on the transfer of £10.5 million. In addition, during 2012 the Group implemented an Enhanced Transfer Value and Pension Increase Exchange offers to the members of the CPS which resulted in a one-off accounting cost of £2.8 million in the year.

During the year, the Group secured a number of new contracts and extensions and the Group's order book stood at £3.0 billion (31 December 2012: £2.4 billion).

As a result of the Group's ongoing strategic focus on major blue-chip customers who increasingly utilise a target cost based form of contract, our net cash position includes a lower level of advanced payments typically paid on lump sum contracts. Additionally, our increasing emphasis on support service related activities and changing industry cash flow trends, together with the cash flow implications of a delayed contract, accounted for the reduction in net cash to £57.7 million (December 2012: £105.7 million). We expect these trends will continue to be reflected in a lower average net operating cash position.

The results of the Group's operating divisions are considered in the Divisional performance section (pages 26 and 27) and are shown in the segmental analysis in the financial statements (pages 101 to 103).

Acquisitions

In August 2013, the Group acquired the 100% share capital of EPC Offshore Limited for an initial consideration of £10.6 million (including £1.0 million for excess cash). EPC Offshore Limited is a field development and project management specialist providing client-side services to North Sea oil and gas companies and enhances the Group's skills and capabilities in the North Sea upstream oil and gas market. Further consideration may be payable depending on the financial performance of the business in the financial years ending 31 December 2014, 2015 and 2016 and the retention of certain key employees in 2016. This performance consideration is subject to a minimum of £2.0 million and a maximum of £14.4 million.

At the period end, the Group acquired the 27% interest from its partner Serco Group plc in their Managed Motorway Technology joint venture arrangement for a cash consideration of £2.4 million. The joint venture agreement, in which Costain already held the remaining 73% interest, has a place on the Highways Agency framework to deliver new technology-led highways improvements.

In accordance with accounting standards, any deferred consideration for acquisitions that is related to employment is expensed in the income statement over the period of deferment. In 2013, employment related and other deferred consideration amounted to £2.8 million (2012: £1.7 million), the increase from the prior period is due to an increase in the expected performance of a previous acquisition, including a deferred consideration element not related to employment. This expense is shown

Finance Director's review

continued

separately in the income statement under 'other items' to aid the user of the financial statements in understanding the underlying performance of the Company.

Interest

Net finance expense amounted to £4.0 million (2012[2]: £2.7 million). The interest payable on bank overdrafts and other similar charges was £2.6 million (2012: £1.8 million) and the interest income from bank deposits and other loans and receivables amounted to £0.7 million (2012: £1.0 million). In addition, the net finance expense includes the interest cost on the net liabilities of the pension scheme of £2.1 million (2012[2]: £1.9 million).

Tax

The Group's effective rate of tax was 3.1% of the profit before tax (2012: 6.5%). The lower than normal rate of tax arose owing to tax relief on the sale of shareholdings in PFI assets, Research and Development tax relief claims, timing differences, not previously recognised as deferred tax assets, and the effect on the brought forward deferred tax balances of the reduced rate of corporation tax of 21% from 1 April 2014.

Dividend

The Board has recommended a final dividend for the year of 7.75 pence per share (2012: 7.25 pence per share) to bring the total for the year to 11.5 pence per share (2012: 10.75 pence per share), an increase of 7%.

Subject to finalisation of the 31 March 2013 actuarial review, as in previous years, the Group will make an additional cash contribution to the pension scheme equal to the amount of dividend paid to shareholders.

Shareholders' equity

Shareholders' equity increased in the year to £43.3 million (2012: £31.8 million). The profit for the year amounted to £12.5 million and other comprehensive income of £4.2 million. The movements are detailed in the consolidated statements of comprehensive income and expense and changes in equity in the financial statements.

On 27 February 2014, the Group announced a proposed £70.3 million (net of expenses) capital raising which, if approved at the extraordinary general meeting on 17 March 2014, will increase the level of shareholders equity significantly in 2014.

Pensions

As at 31 December 2013, the Group's pension scheme deficit in accordance with IAS 19, net of deferred tax, was £29.4 million (2012: £40.0 million). The scheme deficit position has reduced primarily as a result of the return on assets and Company contributions exceeding the increased liabilities arising from changes in the financial assumptions.

In February 2012, the Group announced two further actions being taken to manage the obligations in the CPS. The first of these was the transfer of the Group's interest in two PFI investments into the CPS at an agreed value of £20.3 million which was completed on 22 February 2012 and resulted in an accounting profit on the transfer of £10.5 million. The second action was the implementation of Enhanced Transfer Value ('ETV') and Pension Increase Exchange ('PIE') offers to the members of the CPS. The ETV and PIE exercises resulted in a reduction in the scheme liabilities and assets of approximately £35 million and in a one-off accounting cost of £2.8 million expensed in 2012.

A full actuarial valuation of the CPS was last performed by the Scheme Actuary as at 31 March 2010 and a recovery plan agreed with the Trustee of the Scheme. A full actuarial valuation is being carried out as at 31 March 2013.

Cash flow and borrowings

The Group has a positive net cash balance, which was £57.7 million as at 31 December 2013 (2012: £105.7 million) and included £26.6 million of borrowings (2012: £1.7 million) and cash held by jointly controlled operations of £25.6 million (2012: £29.6 million).

As set out in the consolidated cash flow statement and explained above, during the year, the Group had an operating cash outflow, together with outflows for payment of dividends and matching pension deficit contributions. The average month-end net cash balance during 2013 was £50.7 million (2012: £103.4 million).

Key risks and uncertainties

The principal risks and uncertainties of the business, and the factors which mitigate these risks, are set out on pages 24 and 25. The Board proactively monitors these risks and the Chairman's statement and the Chief Executive's review in these financial statements include consideration of uncertainties affecting the Group.

Contract bonding and banking facilities

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

Costain financial statements can be found on pages 86-132.

Treasury

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

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

Liquidity risk

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

Foreign currency exposure

Translation exposure: the results of the Group's overseas activities are translated into sterling at rates approximating to the foreign exchange rates ruling at the dates of the transactions. The balance sheets of overseas subsidiaries and investments are translated at foreign exchange rates ruling at the balance sheet date.

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

Interest rate risks and exposure

The Group enters into financial instruments, where necessary, for two main purposes: to finance its operations and, in its project finance investments, to manage interest rate risks arising from its operations and its sources of finance. 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. Within the investments in joint ventures and associates, interest rate movements will affect the value of any swaps that may be entered into and are classified as cash flow hedges and this will impact the Group's equity.

Going concern

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

Tony Bickerstaff
Finance Director

26 February 2014

Governance

This section explains our corporate governance and decision-making processes. We detail the committees and our accountability and audit procedures.

In this section

Additional information about our governance can be found online:
www.costain.com/responsibility

Chairman's statement on corporate governance

David Allvey
Chairman

"The Board is committed to achieving the highest standards of governance. This overview sets out our approach to effective leadership and best practice."

Dear Shareholder

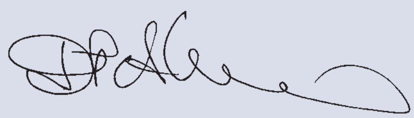
At Costain, we take corporate governance very seriously and are committed to robust corporate governance practices and accountability. The Board considers that the principles set out in the UK Corporate Governance Code are central to the effective management of the business and to maintaining the confidence of investors.

The Board is responsible for providing strong leadership to the Costain Group and effective leadership is realised through collaboration between the Board and the executive team. My role as Chairman is to ensure that we harness the experience and knowledge of the Directors and drive a culture of continual improvement in standards, decision-making, policies and accountability.

A key strength of our Board lies in its diversity across a range of measures, including skills, experience, gender and nationality. We further strengthened our Board with the appointments of Ahmed Samy and Alison Wood. Alison will become the Chair of the Remuneration Committee on 1 April 2014 when Mike Alexander will retire from the Board.

The Board has also continued to undertake wide-ranging discussions on key strategic issues, which included a number of Board workshops attended by members of the Executive Board and third-party advisers. Discussions were focused on developing our ***Engineering Tomorrow*** strategy included the ongoing consideration of potential acquisitions and investments. A business plan for 2014–2016 was approved in December 2013.

The Board is ultimately responsible for the success of Costain and we are committed to the highest standards of corporate governance to enable us to continue to achieve our vision of being one of the UK's leading engineering solutions providers.



David Allvey
Chairman

26 February 2014

Board of Directors

Experienced leadership

David P Allvey (68)
FCA, ATII [3]
Non-Executive Chairman

Appointment: November 2001

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

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

Former Director
Mr Samer Younis retired as a Non-Executive Director with effect from 30 November 2013.

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

Andrew Wyllie (51)
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, the Far East and the UK.

External appointments: Non-Executive Director of Scottish Water.

Anthony O Bickerstaff (49)
FCCA
Finance Director

Appointment: June 2006

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

James Morley (65)
BSc, FCA [1,2,3]
Senior Independent Director

Appointment: January 2008

Skills and experience: James Morley served as Chairman of the Audit Committee from January 2008 until the end of October 2012 and was appointed as the Senior Independent Director at the start of January 2013. He is a Chartered Accountant with some 27 years' experience as a board member of both listed and private companies. Previous roles include Chief Operating Officer of Primary Group Ltd (2006–2007), 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 Bankers' Investment Trust plc (1994–2008), Non-Executive Director of WS Atkins plc (2001–2009), Non-Executive Director of Trade Indemnity Group plc (1991–1996) and Non-Executive Chairman of Acumus Ltd (2011–2012).

External appointments: Non-Executive Director of The Innovation Group plc, Clarkson plc, Speedy Hire plc, and BMS Associates Ltd.

The responsibilities of the Directors have been set out on page 81.

Jane A Lodge (58)
FCA, BSc [1,2,3]
Independent Non-Executive Director

Appointment: August 2012

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

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

Alison J Wood (50)
MBA, BA [1,2,3]
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 will be appointed as Chair of the Remuneration Committee from the beginning of April 2014. Alison is the former Global Director of Strategy and Corporate Development at National Grid plc (2008–2013). Before that, Alison spent nearly 20 years in a number of strategy and leadership roles at BAE Systems plc including Group Strategic Development Director. Alison has also held Non-Executive Director positions with BTG plc (2004–2008) and Thus Group plc (2007–2008).

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

Michael R Alexander (66)
BSc, MSc, FIChem.E, FIET, FIGM, CEng, CSci [1,2,3]
Independent Non-Executive Director

Appointment: July 2007

Mike Alexander will be retiring from the Board with effect from 31 March 2014.

Skills and experience: Mike Alexander, Chairman of the Remuneration Committee, has extensive experience of the energy market. Previous roles include Chief Executive of British Energy plc (2003–2005), Managing Director of British Gas Trading, Chief Operating Officer and Executive Director of Centrica plc (1994–2003), Non-Executive Chairman of Goldfish Bank Ltd (2002–2003), Chairman of TGE Marine AG (2007–2010), Chairman of the Association of Train Operators (2008–2009), Non-Executive Director of the Energy Saving Trust Ltd (1994–2001) and Deputy Chairman and Senior Independent Director of Russian Platinum PLC (2011-2013).

External appointments: Independent Non-Executive Director of Payments Council Ltd.; Executive Director of Lexican Ltd and Lexican Associates Ltd., member of the European Advisory Board for Landis & Gyr, Special Adviser at EGS Energy Ltd and Senior Independent Director and Chairman of the Remuneration Committee of Seplat Petroleum Development Company Limited.

Tracey Wood (44)
LLB
Legal Director and Company Secretary

Appointment: June 2011

Skills and experience: Tracey Wood joined the Company in February 2006. She has a construction and corporate law background and was formerly a partner at Hammonds. She has had a number of senior roles in the Company and was appointed Legal Director and Company Secretary in June 2011. She also has responsibility for human resources across the Group.

Ahmed Samy (58)
BCom/Accounting [3]
Non-Executive Director

Appointment: November 2013

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

External appointment: Board Member of Credit Bank of Albania.

Group Executive Board

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

Andrew Wyllie
Chief Executive

Tony Bickerstaff
Finance Director

Tim Bowen
Corporate Development Director

Patrick Bruce
Group Commercial Director

Martin Hunter
Group Financial Controller

Darren James
Managing Director – Infrastructure

Alan Kay
Group Technical and Operations Director

Alex Vaughan
Managing Director – Natural Resources

Tracey Wood
Legal Director and Company Secretary

Corporate Governance statement

Principles statement

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

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

Statement of compliance

The version of the Corporate Governance Code applicable to the current reporting period is the June 2010 and September 2012 UK Corporate Governance Code (the 'Code'). Throughout the year the Company complied with the provisions of the Code, except for provision B.2.3 of the Code, which requires Non-Executive Directors to be appointed for a specific term because the Company's two major shareholders are entitled to appoint a Non-Executive Director for so long as they each hold 7% of the then issued ordinary share capital of the Company, as detailed on page 52 of this Corporate Governance report.

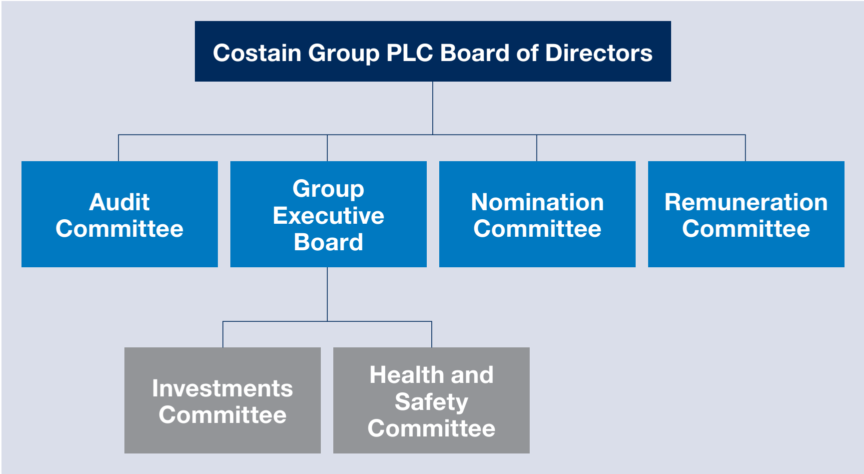
The Audit Committee report on pages 55 to 57, the Nomination report on page 58 and the Directors' Remuneration report on pages 59 to 76 are also incorporated into this Report by reference.

Role of the Board

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

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

2 A copy of the schedule is available on the Company's website at **www.costain.com**



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

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

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

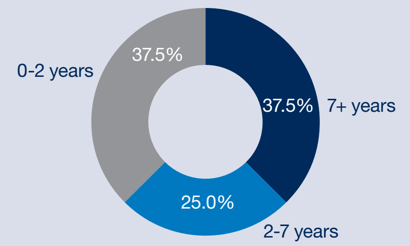
The Group Executive Board is accountable for running the business and delivering the Group strategy. It consists of the Executive Directors and other senior managers, is chaired by Andrew Wyllie (Chief Executive) and works with the support of a number of operational committees and functions.

Board composition

As at the date of this Report, the Board comprised the Chairman, two Executive Directors and four independent Non-Executive Directors and one nominee Non-Executive Director. The nominee Non-Executive Director is nominated by one of our major shareholders, Mohammed Abdulmohsin Al-Kharafi & Sons Co. W.L.L. The membership of the Board and biographical details of all the Directors can be found on pages 48 to 49.

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

Length of Service Non-Executive Directors
as at 31 December 2013



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

The Directors' attendance record at the scheduled Board meetings and Board Committee meetings for the year ended 31 December 2013 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 also arranged to deal with matters between the scheduled meetings as appropriate.

Board independence

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

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

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

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

	Board Maximum 7	Audit Committee Maximum 4	Remuneration Committee Maximum 6	Nomination Committee Maximum 1
Executive Directors				
Andrew Wyllie	7/7	4***	3***	1***
Tony Bickerstaff	7/7	4***	1***	1***
Non-executive Directors				
David Allvey	7/7	4***	5***	1/1
James Morley	7/7	4/4	6/6	1/1
Mike Alexander	7/7	3/4	6/6	1/1
Jane Lodge	7/7	4/4	6/6	1/1
Samer Younis*	3/6	n/a	n/a	0/1
Ahmed Samy**	1/1	n/a	n/a	n/a

* Resigned on 30 November 2013.
** Appointed on 30 November 2013.
*** Not a member of the Committee – attendance at meeting by invitation.

Appointments to the Board and retirement of Directors

Ahmed Samy was appointed to the Board in November 2013 and replaced Samer Younis as the nominee Non-Executive Director nominated by one of our major shareholders, Mohammed Abdulmohsin Al-Kharafi & Sons Co. W.L.L. Alison Wood was appointed to the Board on 1 February 2014 and will replace Mike Alexander as Chair of the Remuneration Committee upon his retirement from the Board on 31 March 2014.

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

In accordance with the Company's Articles of Association and provision B.7.1 of the Code, David Allvey, James Morley, Ahmed Samy and Alison Wood will offer themselves for re-election at the next Annual General Meeting. Having due regard to the results of the independently facilitated review of the Board's performance conducted towards the end of 2011 and to periodic internal evaluations, the Board confirms that it is of the opinion that each of the Directors standing for re-election continues to make an effective and valuable contribution to the Board and should therefore be re-elected at the forthcoming Annual General Meeting.

Corporate Governance statement

continued

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

Effectiveness

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

The last externally facilitated Board and Committee review was conducted towards the end of 2011 by SCT Consultants Ltd (who, having no other connection with the Company, were considered to be independent). The next independently facilitated review is expected to commence in 2014 in accordance with provision B.6.2 of the Code, notwithstanding that this requirement is waived in respect of smaller companies, such as the Company, which are members of the FTSE SmallCap Index.

The last internally facilitated evaluation of the Board and its Committees was concluded in March 2013. This was facilitated internally by the then Joint Company Secretary, under the direction of the Chairman. The process involved each of the Directors completing a high level questionnaire and a comprehensive discussion between the Chairman and each of the Board members. Separately, the Senior Independent Director met with the Non-Executive Directors without the Chairman being present.

Board induction and training

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

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

Operation of the Board

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

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

Director's conflicts of interest

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

Corporate Responsibility ('CR')

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

Shareholder communication and engagement

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

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.

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

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

The Board regards the Annual General Meeting as an important opportunity to communicate directly with shareholders. Board members, including the Chairs of the Remuneration, Nomination and Audit Committees, attended the 2013 meeting and propose attending the 2014 meeting where they will be available to answer questions.

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

Risk management and internal control

Risk management

The Company has various procedures for identifying and managing risk, including a pre-qualification and pre-tender review for obtaining approval to bid for a project from the Investments Committee and a specific project risk management procedure which involves a continuous review of risks and opportunities by the project manager and commercial manager of the project following contract award. For the duration of a contract, the risks and opportunities are updated on a monthly basis and the top five risks and opportunities reviewed by Group senior management.

The Company has also established a corporate risk and opportunity register, which is monitored and updated regularly, as well as sector business risk registers. The Board and Audit Committee receive reports on the Company's main corporate risks and opportunities. As recommended by the Code, the Board has determined the nature and extent of the significant risks it is willing to take in achieving its strategic objectives.

The risk management strategy is regularly reviewed and the Group's risks and opportunities compared against those of other blue-chip companies. The Group reviews any changes in moving into new markets, such as its recent move into technology contracts, and attempts to identify any emerging risks and possible effects on the business. Internal Audit provides independent assurance that risks inherent to the Company's business processes are reasonably controlled and assists management in assessing those risks and how effectively they are managed by internal controls. Internal Audit also promotes best practice in risk management processes to ensure delivery of corporate objectives.

In 2013, Internal Audit conducted project and departmental reviews to appraise and report on the effectiveness of the risk management processes. All reviews carried out were subject to appropriate follow-up action to provide assurance that accepted recommendations have been implemented effectively. The overall assessment is that there is a strong risk management culture within the Group which is continuing to develop.

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

The Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group, which has been in place for the year under review and up to the date of approval of the Annual Report. This process extends not only to projects undertaken solely by subsidiaries of the Group but also to projects undertaken in joint arrangements and by joint ventures and associates. This process is reviewed by the Audit Committee on behalf of the Board and accords with the Financial Reporting Council's ('FRC') guidance on internal control.

Internal controls

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

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

Corporate Governance statement
continued

In 2013, the Company considerably strengthened and updated its internal controls with the introduction of a common platform, which houses all its governances, controls, policies and procedures for all activities within our business, called 'The Costain Way' and also updated its HR information system with a new module called MyHR, which captures all HR matters.

The Audit Committee has reviewed the effectiveness of the system of internal controls. The review covered all controls, including financial, operational and compliance controls and risk management.

Operational controls

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

The Company has developed an operational management system ('the Costain Way') that has been externally certified by BSi as compliant to ISO 9001, ISO 14001, OHSAS 18001, ISO 22301, ISO 27001 and BS 11000 and which is designed to support management in providing safety, quality, environmental, business continuity, information security collaborative management processes across the entire business. The objective of The Costain Way is to provide assurance that:

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

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

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

Financial controls

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

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

Compliance

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

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

Audit Committee report

Operation of the Audit Committee ('the Committee')

The Committee is comprised exclusively of independent Non-Executive Directors. The members of the Committee and details of their attendance at Audit Committee meetings are given on page 51. Biographies are shown on pages 48 and 49.

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

The meetings of the Committee are normally also attended by the Chairman, the Chief Executive, the Finance Director, the External Auditor, the Head of Internal Audit and the Group Financial Controller. The Audit Committee regularly meets privately with the External Auditor and Head of Internal Audit. The Company Secretary is the Secretary to the Committee.

Terms of reference

The Committee's terms of reference are available from the Company Secretary and are published on the Company's website at **www.costain.com**

Role of the Audit Committee

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

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

Principal activities during the year

In 2013, the principal activities of the Committee and the manner in which it discharged its responsibilities were as follows:

Financial statements

The Committee reviewed the Group's draft financial statements, preliminary and interim results and reports from the External Auditor, KPMG Audit Plc, on the outcome of its reviews and audits in 2013.

Significant accounting matters

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

(1) Key contract judgments

As more fully explained in Note 2, on pages 99 to 100 the majority of the Group's activities are undertaken via long-term contracts and these contracts are accounted for in accordance with IAS 11, which requires estimates to be made for contract costs and revenues. These costs and revenues may be affected by a number of uncertainties that depend on the outcome of future events and may need to be revised as events unfold and uncertainties are resolved.

Management bases its judgments of costs and revenues and its assessment of the expected outcome of each long-term contractual obligation on detailed contract valuations and forecast of the costs to complete. During the year, the Committee critically examined these judgments and was content with the position adopted.

(2) Pension

The Group's defined benefit scheme requires significant judgments in relation to the assumptions for inflation, future pension increases, investment returns and member longevity that underpin the valuation. Each year, in selecting the appropriate assumptions, the Committee takes written advice from an independent qualified actuary. The assumptions and sensitivities are set out in Note 20 on pages 124 to 125.

(3) The carrying value of goodwill and intangible assets

As set out in Note 11 on pages 108 to 109, the goodwill and acquired intangible balances within the Group relate principally to the acquisition of businesses including EPC Offshore, ClerkMaxwell and Promanex. During the year ended 31 December 2013, the Committee critically reviewed the analysis performed by management on goodwill and intangibles and agreed with the amortisation charge in respect of intangibles and that no impairment to goodwill was necessary.

Audit Committee report

continued

(4) Alcaidesa Holding SA
The Committee has reviewed the net realisable value of each of the land holdings in Spain held by the Group's 50/50 joint venture. The Committee addressed this issue by considering the report from management on the review carried out of the net realisable value of each of the land holdings in Spain and of the carrying value of the marina assets, and the golf courses including the use of external valuations. The Committee agreed that as a consequence of continuing uncertainty regarding future market conditions in Spain, a non-cash impairment should be taken against the assets of the joint venture, the Group's share of which is £9.8 million, reducing the Company's total carrying value in the joint venture to £26.6 million.

(5) Future IFRS and UK GAAP developments
During the year, the Committee received a management report from the External Auditor regarding future accounting developments likely to affect the presentation of the Group's financial statements.

Independence of the External Auditor

The Company's External Auditor is KPMG Audit Plc.

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

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

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

In 2013, the External Auditor performed non-audit services in respect of potential acquisitions and the provision of tax services. The External Auditor also provided services in reporting on working capital in connection with the lapsed all share merger with May Gurney and the proposed capital raising. The External Auditor was selected as the most cost-effective and efficient supplier to undertake these services based on their thorough understanding of the Group and their particular expertise. In the financial year, the Company spent £1.7 million (2012: £0.4 million) with the External Auditor in respect of non-audit fees.

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

The Senior Statutory Auditor (who has signed the Audit Report on behalf of KPMG on page 84) is Mr Andrew Marshall who was appointed as the lead audit partner at the beginning of the year. He replaces Mr Stephen Bligh who had been the Company's Audit Director since 2010 and who has retired from KPMG.

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

Audit quality and approach to audit tender

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

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

The Committee has not therefore considered it necessary to require the audit to be put out to tender. The Committee continues to be satisfied with the work of the External Auditor and that it continues to remain objective and independent.

KPMG Audit Plc has informed the Company that it wishes to formally change the entity which conducts the Company's audit from KPMG Audit Plc to KPMG LLP. KPMG Audit Plc has indicated therefore that it will not stand for reappointment at the Company's 2014 AGM. However, KPMG LLP will seek election at this meeting. The Committee decided to recommend to the Board that KPMG LLP be appointed as External Auditor to the Company at the AGM. The Committee also recommends the Board seek authority for the Directors to fix the External Auditors' remuneration.

The Committee recognises the new requirement in the Code that the External Audit contract be put out to tender at least every ten years, notwithstanding that this requirement is waived in respect of smaller companies, such as the Company, which are members of the FTSE SmallCap Index.

Risk management and internal controls

Details of the Group's internal controls and risk management are more fully set out on pages 53 to 54 of the Corporate Governance statement.

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

Internal audit

The Group has an internally resourced internal audit function reporting directly to the Committee. The Committee has received reports on its findings and programme of reviews at each of its meetings during the course of the year. During the year, the Committee undertook an internal assessment of the effectiveness and independence of the internal audit function.

Accountability

The Board is required to present a fair, balanced and understandable assessment of the Company's financial position and prospects. The responsibilities of the Directors and External Auditor are set out on pages 81 to 84. As set out in the Director's Report, the Directors consider the Company's business is a going concern.

Jane Lodge
Chair of the Audit Committee

26 February 2014

Nomination Committee report

Operation of the Nomination Committee ('the 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 51. Biographies are shown on pages 48 to 49.

Role of the Committee

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

The Committee directs the Board effectiveness reviews and also reviews management training and succession planning arrangements in respect of senior management. The Company Secretary is the Secretary of the Committee.

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

With effect from 1 February 2014, Alison Wood was appointed as a Non-Executive Director and will become Chair of the Remuneration Committee with effect from 1 April 2014 upon the retirement from the Board of Mike Alexander. The Committee instructed Odgers Berndtson (who do not have any other connection with the Company) to identify appropriate external candidates, and subsequent to meetings with shortlisted candidates, the Committee identified Alison Wood as a suitable successor and recommended to the Board her appointment. Alison brings considerable experience to her role and enhances the skill-set of the Board as a whole.

Main activities during the year

In 2013, the Committee discharged its responsibilities by performing the following activities:

- reviewing the results of the internal review of Board effectiveness which concluded in March 2013;
- reviewing recruitment of Non-Executive Directors;
- receiving notifications from Directors of situations, such as proposed external appointments, in which a potential conflict of interest may arise;
- 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; and
- reviewing succession planning in respect of the Company's senior management.

Directors' remuneration report

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This report, approved by the Board, has been prepared in accordance with the provisions of the Companies Act 2006 and Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. It also meets the requirements of the UK Listing Authority's Listing Rules and the Disclosure and Transparency Rules. It is unaudited unless otherwise stated. In this report we describe how the principles of good governance relating to Directors' remuneration, as set out in the UK Corporate Governance Code (the 'Code'), are applied in practice. The Remuneration Committee (the 'Committee') confirms that throughout the financial year the Company has complied with these governance rules and best practice provisions.

Chairman's Summary Statement

Dear Shareholder

I am pleased to take this opportunity to set out Costain's remuneration strategy and the way it has been implemented during the past year.

In accordance with the new regulations governing the disclosure and approval of directors' remuneration, our remuneration report has been split into two parts:

- our Policy on Directors' remuneration, which sets out our future remuneration policy; it will be the subject of a binding shareholder vote at the forthcoming AGM;
- the Annual Report on remuneration, which describes how the policy was implemented in 2013 and will be implemented in 2014; it will be the subject of an advisory shareholder vote.

During the year, the Committee reviewed the remuneration policy for Executive Directors, to ensure our structures were fit for purpose in advance of seeking shareholders' approval for a policy that it is hoped will endure for the coming three years. We concluded that the current structure is fit for purpose, but that we should make several changes that would simplify the structure and tilt the balance of Executives' incentives towards the long-term.

We decided to combine the annual bonus and the Deferred Share Bonus Plan ('DSBP') into a single annual incentive plan ('AIP') with an element of deferral into shares. We are proposing to simplify the share-based Long-Term Incentive Plan ('LTIP') structure for Executive Directors by taking away the two-tier approach to performance targets; we also introduced an additional two years' deferral on half of the LTIP for Executive Directors. Whilst holding constant the overall level of incentive pay, we moved the balance to the longer term.

These proposals were discussed with major shareholders in late 2013 and the final design took into account feedback received. The resulting new Policy will be subject to a vote at the forthcoming AGM in May as will the new and revised incentive plans that are required to give effect to these changes.

I do hope that you will feel able to support both the resolutions to approve the level of remuneration paid during 2013 and the Committee's forward looking remuneration policy, at this year's Annual General Meeting. The Committee believes that the remuneration policy will continue to retain and motivate our senior team, while fostering alignment with the Company's strategic objectives and the drive for long-term growth for our shareholders. We believe that the remuneration of Executives during 2013 reflects our successes to date in the delivery of that strategy.

Yours sincerely

Michael Alexander
Chairman of the Remuneration Committee

26 February 2014

Directors' remuneration report
continued

Policy report

This report sets out the Company's policy on the remuneration of its Directors and will be put to a binding shareholder vote at the AGM in 2014 and the policy will take formal effect from that date.

The Committee also determines the remuneration policy for the Company Secretary and such other members of the executive management team as it is designated by the Board, with the aim of attracting, motivating and retaining executives of the appropriate calibre and expertise, so that the Company is managed successfully for the benefit of its stakeholders. The framework has been designed as an integral part of the Company's overall business strategy. For the avoidance of doubt, although the policy for employees below the Board follows similar principles and structure to that for the executive directors, the remuneration policy set out below governs the policy for the Board only.

Future Remuneration Policy for Executive Directors, to apply from the date of the 2014 AGM, is set out below.

Element: Salary

Purpose and link to strategy
- To attract and retain high-calibre individuals.
- Reflects skills, experience over time.
- Provides an appropriate level of basic fixed income whilst avoiding excessive risk arising from over reliance on variable income.

Operation
- Generally reviewed annually (with any change effective 1 April) but exceptionally at other times of the year.
- Set with reference to individual performance, experience and responsibilities.
- Reflects the market rate for the individual and their role, determined with reference to remuneration levels in companies of similar size and complexity, taking into account pay levels within the Company in general.
- Higher increases may be appropriate where an individual is promoted, changes role or where an individual is appointed on a below market salary with the expectation that his salary will increase with experience and performance.

Maximum opportunity
- Salaries to apply for the year from 1 April 2014 are:
  – Chief Executive: £437,228
  – Finance Director: £289,664
- There is no maximum salary value.

Element: Annual Incentive Plan ('AIP')

Purpose and link to strategy
- 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.

Operation
- The Committee considers and approves the measures and targets at the start of each year and ensures they are aligned with business strategy and are sufficiently stretching.
- Financial metrics will comprise at least three-quarters of AIP opportunity, of which at least half will be a measure of Group profit.
- In addition to these financial metrics, the AIP includes Health and Safety targets and personal objectives.
- In setting financial parameters, the Committee takes into account the Company's internal budgets and, where applicable investors' expectations. The targets applying to financial measures are based on a sliding scale.
- Two-thirds paid in cash.
- Not pensionable.
- Deferral into shares of one-third of earned AIP; this vests on the second anniversary of grant (subject to continued employment and not being under notice of termination, either given or received, on the date of vesting).
- Shares provided under the AIP are typically purchased by a trust on behalf of the Group so as to not lead to any dilution of shareholder interest.
- Awards may be subject to clawback if the Committee becomes aware of a material misstatement to the audited accounts, an error in calculation of targets resulting in an overpayment, gross misconduct or criminal behaviour on the part of a participant.

Maximum opportunity
- Maximum: 150% of salary.
- There is no minimum opportunity.

Element: Long-Term Incentive Plan ('LTIP')

Purpose and link to strategy
- Aligned to main strategic objectives of delivering sustainable profit growth which in turn should deliver enhanced returns.

Operation
- Annual grant of performance shares, half of which vest after three years subject to continued service and performance targets, and half of which vest after five years (the final two years being subject only to continued service).
- LTIP performance will be measured over three years.
- The performance condition consists of a measure of EPS over a three-year period, starting with the year of grant.
- Awards may be subject to clawback if the Committee becomes aware of a material misstatement to the audited accounts, an error in calculation of targets resulting in an overpayment, gross misconduct or criminal behaviour on the part of a participant.

Maximum opportunity
- LTIP awards with a face value of not more than 100% of salary.
- Amount that is paid for achievement of threshold performance: 15% of the maximum.

Element: SAYE Scheme

Purpose and link to strategy
- Offered to all UK employees, to facilitate share ownership and provide further alignment with shareholders.

Operation
- Periodic grants which normally vest after three or five years subject to continued service.

Maximum opportunity
- Executive Directors are eligible to participate in the SAYE Scheme on the same terms as other employees.

Element: Pension

Purpose and link to strategy
- To aid retention and remain competitive in the market place.

Operation
- Annual pension allowance.
- Paid as a cash contribution to the Defined Contribution pension scheme and/or a cash supplement.

Maximum opportunity
- Allowance up to 22% of base salary.

Element: Other benefits

Purpose and link to strategy
- To aid retention and be competitive in the market place.
- Healthcare benefits in order to minimise business disruption.

Operation
- Company car and fuel (or car allowance).
- Medical insurance.
- Life assurance.

Maximum opportunity
- N/A.

Element: Share ownership guidelines

Purpose and link to strategy
- Further alignment of interests between Costain Board and shareholders.

Operation
- Executive Directors are required to build and maintain a shareholding worth not less than 100% of base salary through the retention of vested share awards or through open market purchases.

Maximum opportunity
- N/A.

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

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

Directors' remuneration report

continued

Incentive plan discretions

The Committee will operate the AIP and LTIP according to their respective rules, the policy set out above and in accordance with the Listing Rules and HMRC rules where relevant. A copy of the Plan rules is available on request from the Company Secretary. The Committee, consistent with market practice, retains discretion over a number of areas relating to the operation and administration of these plans. These include (but are not limited to) the following:

- who participates in the plans;
- the timing of grant of award and/or payment;
- the size of an award and/or a payment;
- the choice of (and adjustment of) performance measures and targets for each incentive plan in accordance with the policy set out above and the rules of each plan;
- discretion relating to the measurement of performance in the event of a change of control or reconstruction;
- determination of a good leaver (in addition to any specified categories) for incentive plan purposes based on the rules of each plan and the appropriate treatment chosen; and
- adjustments required in certain circumstances (e.g. rights issues, corporate restructuring, on a change of control and special dividends).

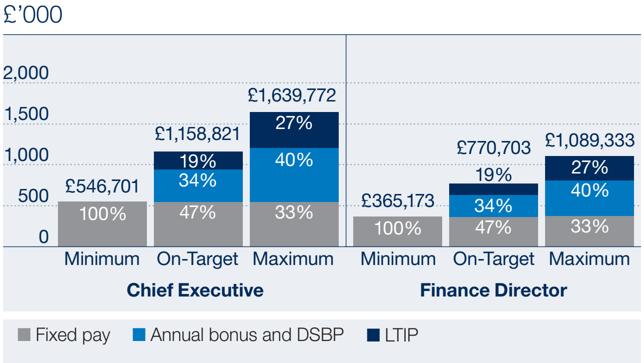
Any use of the above discretions would, where relevant, be explained in the Annual Report on Remuneration and may, as appropriate, be the subject of consultation with the Company's major shareholders.

Legacy arrangements

For the avoidance of doubt, in approving the Policy report, authority is given to the Company to honour any commitments entered into with current or former Directors that have been disclosed previously to shareholders. It is also part of this policy that we will honour payments or awards crystallising after the effective date of this policy but arising from commitments entered into prior to the effective date of the new policy, or at a time when the relevant individual was not a Director of the Company. The Company will also have the authority to meet any claims against the Company arising as a result of a Director's termination.

Illustration of application of Remuneration Policy

We estimate that the level of remuneration received by each of the two Executive Directors for the first full year under the Remuneration Policy set out above will be:



The chart above illustrates how the total pay opportunities for the Executive Directors vary under three performance scenarios: Minimum, On-Target and Maximum.

Assumptions:

- Minimum – fixed pay only, including salary effective 1 April 2014, 22% pension allowances and benefits as paid in FY2013.
- On-Target – fixed pay, plus 60% of the maximum payout under the AIP (and mandatory deferred element), and 50% LTIP vesting.
- Maximum – fixed pay, plus 100% of the maximum payout under the AIP and (and mandatory deferred element), and 100% LTIP vesting.

Service agreements and loss of office

The Executive Directors have service contracts that can be terminated by either party on the giving of 12 months' notice. There is no entitlement to the payment of a predetermined amount on termination of employment in any circumstances. There are no liquidated damages provisions for compensation on termination within the Executive Directors' service agreements. The Executive Directors' service agreements do contain provisions for payment in lieu of notice, but these are at the Company's sole discretion.

The Company seeks to avoid any payment for failure. The circumstances of the termination (taking into account the individual's performance) and an individual's duty and opportunity to mitigate losses are taken into account in every case. Our policy is to stop or reduce compensatory payments to former Executive Directors to the extent that they receive remuneration from other employment during the compensation period and that any such payments would be paid monthly in arrears.

Under the rules of the new AIP (deferral element), the legacy DSBP and the LTIP, outstanding awards may vest if a participant leaves the Group for certain specified reasons.

It is the Committee's intention that any future service contracts will be made in accordance with the policy stated above.

The conditions covering loss of office payments are as set out in the individual Plan rules for the deferred element of the AIP, the legacy DBSP and the LTIP. The Committee will operate within these parameters when determining remuneration in the event of the loss of office.

Executive Directors	Date of contract	Expiry date	Termination payment	Remuneration entitlements	Compensation on termination following a change of control
Andrew Wyllie Tony Bickerstaff	25 April 2005 3 March 2006	Terminable on 12 months' notice	Base salary plus benefits (including pension), paid monthly and subject to mitigation	No other specific entitlements are contained within our contracts. The rules of the Company's share plans provides for partial vesting if Executive Directors leave for a specified reason; performance targets would be used to determine any amount paid	No additional provisions

Recruitment remuneration

Salaries for new hires will be set to reflect their skills and experience, the Company's intended pay positioning and the market rate for the role. If it is considered appropriate to appoint a new Director on a below market salary (for example, to allow them to gain experience in the role) their salary may be increased to a market level by way of a series of above inflation increases over two to three years.

The remuneration package for a new Executive Director would be set in accordance with the terms of the Company's approved remuneration policy in force at the time of appointment. In addition, the Committee may offer additional cash and/or share-based elements (on a one-time basis or ongoing) when it considers these to be in the best interests of the Company (and therefore shareholders). Any such payments would be based solely on remuneration lost when leaving the former employer and would reflect the delivery mechanism, time horizons and performance requirement attaching to that remuneration.

In the case of an internal appointment, any variable pay element awarded in respect of the prior role may be allowed to pay out according to its terms on grant, adjusted as relevant to take into account the appointment. In addition, any other ongoing remuneration obligations existing prior to appointment may continue, provided that they are put to shareholders for approval at the first AGM following their appointment.

The Committee may also agree that the Company will compensate Executives, both internal and external, for certain relocation expenses as appropriate.

Non-Executive Directors will be recruited subject to the terms set out within the stated policy on page 64.

External directorships

The Company encourages Executive Directors to take up Non-Executive appointments, with the prior consent of the Company, in the belief that such appointments broaden their skills and the contribution which they can make to the Company's performance. Generally, no more than one such appointment may be undertaken. There must be no conflict of interest and the time devoted to the external appointment must be reasonable in relation to the individual's commitment to the Company. Fees paid for external appointments may be retained by the individual concerned.

Directors' remuneration report

continued

Chairman and other Non-Executive Directors

The Non-Executive Directors have letters of appointment. The appointment of an independent Non-Executive Director can be terminated by reasonable notice on either side. David Allvey, Michael Alexander, James Morley, Jane Lodge and Alison Wood are not entitled to compensation for loss of office.

The nominee Non-Executive Directors (as indicated in the Corporate Governance statement on page 50), hold office for as long as the shareholder nominating them holds a specific percentage of the issued share capital. The nominee Non-Executive Directors are required to stand for re-election in the usual way and are not entitled to compensation for loss of office. Currently, only one of the two shareholders entitled to appoint a Non-Executive Director has appointed a nominee to sit on the Board.

The dates of each Non-Executive Director's original appointment are as follows:

Non-Executive Director	Date of original appointment	Expiry of current term[1]
David Allvey	01.11.2001	Close of 2014 AGM
Michael Alexander	25.07.2007	Close of 2014 AGM[2]
Jane Lodge	01.08.2012	Close of 2016 AGM
James Morley	09.01.2008	Close of 2014 AGM
Ahmed Samy	30.11.2013	Close of 2014 AGM
Alison Wood	01.02.2014	Close of 2014 AGM

1 Subject to re-election at the AGM following their appointment, subsequent re-election at intervals of no more than three years and re-election at each AGM if having served on the Board for more than nine years, in accordance with the UK Corporate Governance Code and the Company's Articles of Association.

2 Michael Alexander will, however, be retiring prior to that date, on 31 March 2014.

Remuneration Policy for Chairman and Non-Executive Directors

Element: Fees

Purpose and link to strategy

- Attract and retain high performing individuals.

Operation

- Remuneration for Non-Executive Directors, other than the Chairman, is determined by the Board, following consultation between the Chairman and the Chief Executive. The Chairman's fee is determined by the Board following consultation between the Committee and the Chief Executive. Fees are reviewed annually and any increase is effective from 1 April.
- Remuneration for Non-Executive Directors, other than the Chairman, comprises a basic annual fee for acting as Non-Executive Director of the Company and additional fees for the Senior Independent Director, and chairmanship of the Audit and Remuneration Committees.

Maximum opportunity

- N/A.

Element: Share ownership guidelines

Purpose and link to strategy

- Alignment of interests between Costain Board and shareholders.

Operation

- Non-Executive Directors are required to build and maintain a shareholding worth not less than 100% of their annual fee.

Maximum opportunity

- N/A.

Consideration of employee views

Although the Committee does not formally consult employees on executive remuneration, it considers the general basic salary increase as well as pay and conditions for the broader employee population when determining the annual salary increases for the Executive Directors.

Consideration of shareholder views

The Committee considers shareholder feedback received in relation to the AGM each year at a meeting following the AGM. This feedback, plus any additional feedback received during any meetings from time to time, is then considered as part of the Company's annual review of remuneration policy.

When there are material issues relating to executive remuneration or proposed changes in policy, we engage actively with major shareholders to ensure we understand the range of their views. When significant changes are made within the policy, the Committee Chairman will inform shareholders of these.

Details of votes cast for and against the resolution to approve last year's remuneration report and any matters discussed with shareholders during the year are set out in the Annual Report on Remuneration.

Annual Report on Remuneration

Governance

Operation of Committee

The Remuneration Committee is comprised exclusively of independent Non-Executive Directors. The members of the Committee and details of their attendance at the Remuneration Committee meetings are given on page 51. Biographies are shown on pages 48 and 49.

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

Terms of reference

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

Remuneration Committee activity

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

Date	Key agenda items
7 February 2013	Approved the 2012 annual cash bonuses subject to final audit of the 2012 Accounts
	Reviewed the senior executives' salaries
	Approved the Deferred Share Bonus Plan ('DSBP') performance targets for the 2013 base year
	Reviewed the Chairman's and Non-Executives' fees
	Reviewed the annual salary adjustment for the wider workforce
	Reviewed the Directors' remuneration report
15 March 2013	Considered the impact of a potential acquisition on the Company's incentive plans (including bonus payments)
3 April 2013	Approved the vesting of the 2010 LTIP
	Granted awards under the DSBP for the 2012 base year
7 May 2013	Granted awards under the 2013 LTIP
	Approved notification to participants in respect of the DSBP 2013 base year
30 September 2013	Approved amendments to the HMRC approved plans to reflect changes under the Finance Act 2013
	Reviewed a market update on remuneration packages (prepared by New Bridge Street)
10 December 2013	Considered the introduction of a new 2014 LTIP (subject to shareholder approval)
	Reviewed the proposed 2014 LTIP performance targets
	Considered the introduction of a new annual incentive plan comprising a new 2014 Share Deferral Plan replacing the existing DSBP and the current annual cash bonus plan (subject to shareholder approval)
	Reviewed the proposed 2014 annual incentive plan performance measures
	Approved the list of LTIP and annual incentive plan participants
	Approved the 2014 annual salary review

Directors' remuneration report

continued

Advice provided to the Committee

Advice was sought where appropriate from other sources. During the course of the year, the Chief Executive, the Finance Director, the Group's Chairman, the Group HR Director, and 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 New Bridge Street (a trading name of Aon Hewitt Limited).

New Bridge Street is a founder signatory to the Remuneration Consulting Group's Code of Conduct. Neither New Bridge Street nor any other part of Aon Hewitt provided other services to the Company during the year and, having no other connection with the Company, New Bridge Street is considered to be independent. Following a tender process in 2012 by the Committee, New Bridge Street was re-appointed to act as the Company's remuneration consultants. 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. New Bridge Street received fees of £165,937 for the year ended 31 December 2013.

Voting on the Remuneration Report at the AGM in 2013

Last year's remuneration report was approved by shareholders with a 96.9% (2012: 96.86%) vote in favour (including discretionary votes).

Implementation of Policy in the year to 31 December 2013

Single Total Figure of Remuneration for each Director.

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

	2013						2012					
	Salary & Fees £	Taxable Benefits £	Pension* £	Annual Incentive** £	LTIP*** £	Total £	Salary & Fees £	Taxable Benefits £	Pension* £	Annual Incentive** £	LTIP £	Total
Executive Directors												
A Wyllie	**423,963**	**13,283**	**93,272**	**482,017**	**238,704**	**1,251,239**	414,120	13,394	91,106	345,413	225,304	1,089,337
A O Bickerstaff	**280,876**	**11,783**	**61,793**	**333,467**	**158,140**	**846,059**	274,354	11,894	60,358	226,079	149,263	721,948
Chairman												
D P Allvey	**131,928**	**–**	**–**	**–**	**–**	**131,928**	128,875	–	–	–	–	128,875
Non-Executive Directors												
M R Alexander	**48,839**	**–**	**–**	**–**	**–**	**48,839**	47,705	–	–	–	–	47,705
J A Lodge[1]	**51,437**	**–**	**–**	**–**	**–**	**51,437**	18,870	–	–	–	–	18,870
J Morley[2]	**48,839**	**–**	**–**	**–**	**–**	**48,839**	48,797	–	–	–	–	48,797
A Samy[3]	**3,572**	**–**	**–**	**–**	**–**	**3,572**	–	–	–	–	–	–
A J Wood[4]	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
S G Younis[5] (former Director)	**39,032**	**–**	**–**	**–**	**–**	**39,032**	41,615	–	–	–	–	41,615
Other former directors[6]	**–**	**–**	**–**	**–**	**–**	**–**	47,705	–	–	–	–	47,705

* Pension contributions in excess of £47,500 paid as a cash supplement.
** The Annual Incentive includes payments under the legacy annual bonus scheme and legacy DSBP.
*** The value of the LTIP for 2013 is subject to the Committee's determination (see Additional Notes below).
1 appointed as a Non-Executive Director w.e.f. 1 August 2012 and as Chair of the Audit committee w.e.f. 31 October 2012 (succeeding J Morley).
2 appointed Senior Independent Director w.e.f. 31 October 2012.
3 appointed as a Non-Executive Director w.e.f. 30 November 2013.
4 appointed as a Non-Executive Director w.e.f. 1 February 2014 and as Chair of the Remuneration Committee w.e.f. 1 April 2014.
5 retired as a Non-Executive Director w.e.f. 30 November 2013.
6 J M Bryant retired as a Non-Executive Director w.e.f. 31 December 2012.

Additional Notes to the Single Total Figure of Remuneration

Taxable benefits provided to Executive Directors

The main benefits available to the Executive Directors during 2013 (and their approximate values) were a car allowance of £12,000 (Andrew Wyllie) and £10,500 (Tony Bickerstaff) and private medical insurance for both of £1,283. This package of benefits was unchanged from 2012.

Determination of 2013 Annual bonus – Cash

Annual bonus payments were determined with reference to performance over the financial year ending 31 December 2013, against a maximum opportunity of 100% of salary. The performance measures and targets are set out below:

Metric	Actual performance	Maximum percentage of Bonus	Performance as a percentage of Bonus	Adjusted performance as a percentage of Bonus
EBITA†	£35.0m	50%	50%	42%
Group Overhead	*	10%	7%	7%
Health and Safety	AFR not achieved, Scored Inspections achieved	10%	5%	5%
Order Book Contract Profit	*	5%	2%	2%
Total Order Book	*	5%	5%	5%
Cash Balance	*	5%	0%	0%
Cash Conversion	*	5%	0%	0%
Personal Performance	N/A	10%	10%	10%
Total	N/A	100%	79%	71%

* The Committee has determined that those particular performance measures remain commercially sensitive and, as such, has chosen not to disclose them.
† As adjusted by the Committee.

In determining the bonus outcome for the Executive Directors, the Remuneration Committee took into account that the performance against the principal financial measure (EBITA), calculated in accordance with the scheme rules, would include the profit recognised on the disposal during 2013 of our share of a joint venture with Severn Trent, which amounts to £9.1 million. Whilst the Committee took the view that the management team had performed commendably both in the stewardship of this asset prior to sale and in the negotiation of its eventual disposal, we took the view that this profit should not count fully towards the target for the 2013 bonus. We therefore reviewed the bonus outcome both including and excluding the effect of this disposal and determined that the bonus payable should be at the mid-point of these two results. The adjusted result in the right-hand column shows this adjusted amount which will form the basis for payment.

Determination of 2013 DSBP (Grant to be made in 2014)

The level of DSBP grants to be made in 2014 is determined with reference to performance over the financial year ending 31 December 2013, their value being included in the 2013 Annual Incentive in the Single Total Figure Table shown on page 66 and is subject to the Committee's determination that the performance conditions have been met, against a maximum of 50% of salary. The performance measures and targets are set out below:

Group EBITA for 2013	Percentage of Relevant Maximum Award
£22.6 million or less	0%
Between £22.6 million and £25.1 million	Between 0% and 60% on a straight line basis
£25.1 million	60%
Between £25.1 million and £28.9 million	Between 60% and 100% on a straight line basis
£28.9 million or more	100%

Metric	Performance target	Actual performance*	Actual percentage of DSBP*	Adjusted performance as a percentage of DSBP
EBITA†	see table above	£35.0m	100%	84%

* Subject to the Committee's official determination that the performance conditions have been met.
† As adjusted by the Committee.

Directors' remuneration report

continued

The measure for the DSBP is also EBITA, which is the principal measure for the annual bonus and therefore subject to the same considerations as set out above. The Committee followed the same process for determining the result of the DSBP as for the annual bonus.

Determination of 2012 DSBP (grant made in 2013)

The 2012 DSBP award (granted 13 April 2013) was based on performance for the year ended 31 December 2012. In the previous Directors' remuneration report details of the grant were not included in the emoluments table as the award of shares had not been determined at that time. The report indicated, however, that an award of shares equivalent to 62% of the maximum opportunity of 50% of salary would be made. We have therefore included details of the 2012 DSBP award (granted April 2013) below.

The DSBP grants made in 2013 are included in the 2012 AIP in the Single Total Figure Table shown on page 66.
The performance measures and targets are set out below:

Group EBITA for 2012	Percentage of Relevant Maximum Award
£21.2 million or less	0%
Between £21.2 million and £23.5 million	Between 0% and 60% on a straight line basis
£23.5 million	60%
Between £23.5 million and £28.2 million	Between 60% and 100% on a straight line basis
£28.2 million or more	100%

Metric	Performance target	Actual percentage of DSBP
EBITA	See table above	62%

The EBITA for the year ended 31 December 2012 was £23.7 million and accordingly 62% of the maximum DSBP award opportunity vested as confirmed by the Committee.

The grants made under the DSBP during 2013, based on performance for the year ending 31 December 2012, are set out below:

Executive	Number of shares	Face value
Andrew Wyllie	36,401[1] 10,771 (£29,997)[2] 10,771[3]	£129,010
Tony Bickerstaff	20,394[1] 10,771 (£29,997)[2] 10,771[3]	£85,469

1 Number of ordinary shares under the Deferred Award.
2 Maximum number and value or shares under the Combined Deferred Award.
3 Number of shares under the Option.

The DSBP includes a mechanism to allow the Company to deliver a combined arrangement at no additional cost to the Company by delivering to participants a combination of HM Revenue & Customs ('HMRC') tax-approved market value share options (with an exercise price determined at the time of grant) over a fixed number of shares, together with non tax-approved Combined Deferred Awards with a nil exercise price over a fixed value of shares. The tax-approved and non tax-approved options/awards are linked, in terms of value and exercise, and mirror the same commercial terms as the Deferred Awards.

Long-Term Incentive Plan

The LTIP award granted on 12 April 2011 was based on performance to the year ended 31 December 2013 and is due to vest in March 2014, subject to the Committee's determination that the performance conditions have been met. The 2010 LTIP award (granted 14 April 2010) was based on performance for the year ended 31 December 2012 and vested in March 2013 but as the previous Directors' remuneration report, although indicating that the EPS target had been 100% met, did not confirm that the award had vested (as the Committee had not at that stage convened to officially determine the extent to which the performance condition had been met), these awards have also been included below.

14 April 2010 award (included in 2012 Long-Term Incentives figure in Single Figure Table on page 66).
There was a single EPS performance condition relating to this award:

EPS for the financial year ended 31 December 2012	Vesting level
Below 21.0 pence	0%
21.0 pence	15%
Between 21.0 pence and 27.5 pence	15% – 100% pro rata
27.5 pence or more	100%

EPS for the financial year ended 31 December 2012 approved by the Remuneration Committee was 37.1 pence. Therefore, the awards granted on 14 April 2010 vested in full in 2013, as shown in the table below:

	Number of shares at grant	Number of shares vested	Number of shares to lapse	Sub-total	Dividends on shares to vest	Total	Value[1]
Andrew Wyllie	81,632	81,632	–	81,632	–	81,632	£225,304
Tony Bickerstaff	54,081	54,081	–	54,081	–	54,081	£149,263

1 Valued using the share price on the date of vesting being £2.76.

12 April 2011 award (included in 2013 Long-Term Incentives figure in Single Figure Table on page 66).
This award had two EPS-based performance conditions:

Aggregate EPS for the financial years ended 31 December 2011, 2012 and 2013	Vesting level (for 50% of the award)
Below 102.3 pence	0%
102.3 pence	15%
Between 102.3 pence and 112.6 pence	15% – 100% pro rata
112.6 pence or more	100%

EPS for the financial year ended 31 December 2013	Vesting level (for 50% of the award)
Below 47.0 pence	0%
Between 47.0 pence and 56.0 pence	0% – 100% pro rata
56.0 pence or more	100%

EPS for the financial year ended 31 December 2013 calculated on an adjusted basis approved by the Remuneration Committee was 46.9 pence and aggregate EPS for the financial years ended 31 December 2011, 2012 and 2013 (calculated on the same basis) was 118.7 pence. As a result, 100% of the element relating to aggregate EPS is due to vest (50% of the maximum award), and 0% of the element relating to 2013 EPS is due to vest (50% of the maximum award). Therefore, 50% of the awards granted on 12 April 2011 are due to vest in 2014* and are shown in the table below:

	Number of shares at grant	Number of shares due to vest*	Number of shares to lapse	Dividends on shares to vest	Total	Estimated value[1]
Andrew Wyllie	169,294	84,647	84,647	–	84,647	£238,704
Tony Bickerstaff	112,157	56,078	56,079	–	56,079	£158,140

* Subject to the Committee's official determination that the performance conditions have been met and to any other adjustment.
1 Valued based on the average share price over the final three months of the financial year ended 31 December 2013, being £2.82.

Grants Made During the Year

2013 DSBP Grants

The grants under the 2013 DSBP are set out on page 68.

2013 LTIP Grants

The grants made under the LTIP during 2013 which are due to vest in May 2016, based on performance from 1 January 2013 to 31 December 2015, are as follows:

	Number of shares	Face value[1]	End of performance period	Performance Condition	Threshold vesting	Weighting (% of award)	Performance measure
Andrew Wyllie	163,293	£424,562	31 December 2015	(2)	50% EPS	50% Operating Profit	(2)
Tony Bickerstaff	108,691	£282,597	31 December 2015	(2)	50% EPS	50% Operating Profit	(2)

1 Valued using the share price on the day prior to the date of grant (07 May 2013), being 260p per share.

(2) Performance conditions relating to the grants made under the LTIP during 2013 are as follows:

Aggregate EPS targets over the 2013-2015 financial years	Percentage of vesting of that portion of an option/award made over Ordinary Shares worth up to and including 50% of salary
Below 88.7 pence	0%
88.7 pence	15%
100 pence or more	100%
Between 88.7 pence and 100 pence	Between 15% and 100% vesting on a straight-line basis

Operating profit for the 2015 financial year	Percentage of vesting of that portion of an option/award made over Ordinary Shares worth in excess of 50% of salary
£35 million or below	0%
£42 million	50%
£50 million or more	100%
Between £42 million and £50 million	Between 50% and 100% on a straight-line basis

Irrespective of the extent to which the operating profit performance condition shall be achieved, no part of this portion of an option/award will vest unless the following EPS underpins have been achieved:

- EPS for the 2015 financial year must be at least 37.3 pence; and
- aggregate EPS over three financial years ending with the 2015 financial year must equal 100 pence or more.

If these two EPS underpins have been met, the portion of the option/award subject to the operating profit performance condition will vest in accordance with the above table.

Pensions

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 Tony Bickerstaff were £1,950 (2012: £1,904) and £1,292 (2012: £1,262) 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.

All-employee Share Plans

The Company granted options under the 2012 SAYE Scheme to the Executive Directors during 2013, details of which are shown on page 75.

Non-Executive Directors

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 Committee. The annual fees set with effect from 1 April 2013 are as follows:

2013 Fees	Basic Fee	Senior Independent Director	Audit Committee Chairman	Remuneration Committee Chairman
Fees	£42,865	£6,273	£8,887	£6,273

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.

	2013	2012	% change
Chief Executive			
– salary	**£423,963**	£414,120	2.4 %
– benefits	**£13,283**	£13,394	-0.8%
– bonus/AIP[1]	**£345,412**	£528,360	-34.6%
Average per employee			
– salary[2]	**£39,616**	£37,885	4.6%
– benefits[3]	**£4,679**	£4,217	11.0%
– bonus/AIP[4]	**£3,239**	£2,768	17.0%

1 Bonus/AIP figures for the Chief Executive are calculated on the basis of the combined cash bonus and DSBP actually paid in 2012 and 2013 (for the performance years 2011 and 2012).
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 is 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/AIP figures for 2014 for the whole company are not available, hence for employees, the comparator figure is the total bonus payments made to monthly paid employees in 2012 and 2013 averaged per head.

Relative importance of spend on pay

The table below illustrates the change in expenditure by the Company on remuneration paid to all the employees of the Group and distributions to shareholders from the financial year ending 31 December 2012 to the financial year ending 31 December 2013.

	2013 £million	2012 £million	% change
Overall expenditure on pay	**151.4**	153.7	-1.5%
Dividend	**7.2**	6.7	7%

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

Directors' remuneration report

continued

Statement of implementation of policy for 2014

Salary

For 2014, the Committee approved a 2.5% increase for Executive Directors, effective 1 April 2014. A 2.5% salary increase budget was also applied across the Company in 2014. The results of the salary review are set out in the table below:

	Salary 2013	Salary 2014	% change
Andrew Wyllie	**£426,564**	£437,228	2.5%
Tony Bickerstaff	**£282,599**	£289,664	2.5%

Annual Incentive Plan

During 2013, the Committee decided to simplify the structure of the annual bonus plan by combining the annual cash bonus and the Deferred Share Bonus Plan into one Annual Incentive Plan ('AIP'). The proposed operation of the deferred element of the new AIP will be subject to the approval of the Company's Shareholders at the 2014 AGM. The combined maximum bonus opportunity for the Chief Executive and the Finance Director for the year ended 31 December 2014 will remain unchanged from 2013 at 150% of base salary, with one-third of earned bonus deferred into shares for a further two years (i.e. maintaining the same level of deferral as under the operation of the DSBP).

Executive Directors and other senior management are eligible for annual bonuses to encourage improved performance, with targets established by the Committee to align rewards with the Company strategy. The targets are set at the beginning of the year by the Committee and are reviewed with appropriate input from the Audit Committee at the end of the year.

The performance measures for the 2014 AIP are as follows:

Metric	Maximum percentage of AIP
EBITA	66.7%
Group Overhead	6.7%
Health and Safety	6.7%
Order Book Contract Profit	3.3%
Total Order Book	3.3%
Cash Balance	3.3%
Cash Conversion	3.3%
Personal Performance	6.7%

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

Long-Term Incentive Plan

In December 2013, the Committee determined that the LTIP should be amended from the current tiered structure to a single award, subject to the approval of the Company's Shareholders at the 2014 AGM. It is proposed that the grant level is to remain at 100% of salary. The Committee also decided that, subject to achievement of the performance conditions set out below, half of the award that vests should be subject to deferral for a further two years (i.e. to the fifth anniversary of grant). This will ensure long-term alignment of Executive Directors with shareholder interests. It is proposed that the targets for the 2014 LTIP awards will be as follows:

EPS condition

Sum of the EPS for the financial years ending 31 December 2014, 2015 and 2016	Vesting level for awards
Below 113.2 pence	0%
113.2 pence	15%
126.7 pence or more	100%
Between 113.2 pence and 126.7 pence	Between 15% and 100% vesting on a straight line basis

The Committee has the discretionary power to vary these EPS targets. It is anticipated that the 2014 LTIP awards will take place immediately following the 2014 AGM, subject to Shareholder approval of the new LTIP.

The Committee believes that EPS is the most appropriate metric to use under the LTIP, as growth in EPS is one of the key drivers of the Company's share price. As with previous LTIP awards, EPS for the awards that are due to be made in 2014 is to be calculated on an adjusted basis.

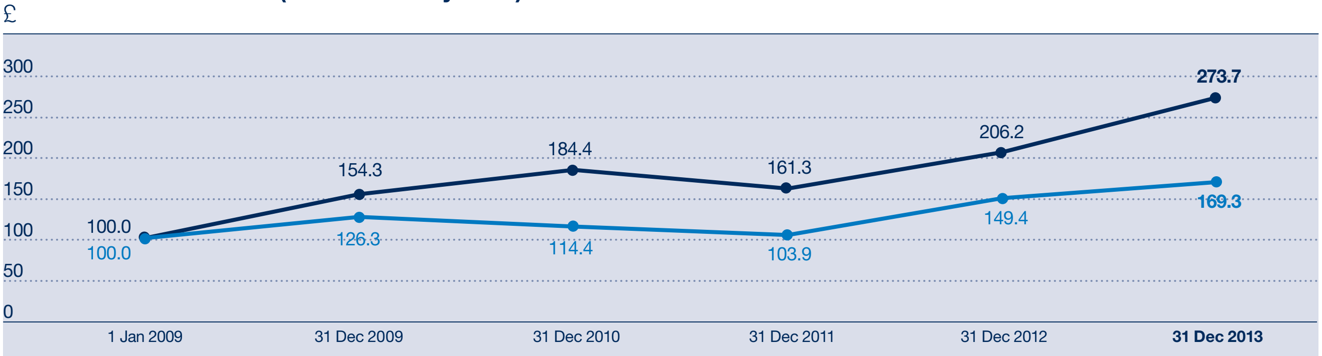
A clawback provision is incorporated in the new AIP and the LTIP (and the legacy DSBP) with regard to any material misstatement to audited accounts, an error in calculation of targets resulting in an overpayment, gross misconduct or criminal behaviour on the part of a participant.

Other information

Performance graph

The graph below shows the value, by 31 December 2013, for £100 invested in Costain Group PLC on 1 January 2009 compared with the value of £100 invested in the FTSE SmallCap Index. The Committee believes that the SmallCap Index is an appropriate Index to use as it is the Index in which the Company is a constituent and comprises companies of a more similar size to Costain than the FTSE All-Share.

Total shareholder return (from 1 January 2009)



■ Costain Group PLC ■ FTSE SmallCap Index
Source: Thomson Reuters

Directors' remuneration report
continued

Change in Chief Executive's Remuneration

	Year ending 31 December				
	2013	2012	2011	2010	2009
Total Remuneration	**£1,251,239**	£1,089,337	£1,228,332	£1,603,014	£887,814
AIP (%)	**75%**	55%	86%	94%	84%
LTIP vesting (%)	**100%**	100%	100%	96%	0%

External directorships

Andrew Wyllie was appointed a Non-Executive Director of Scottish Water on 7 April 2009 and in respect of the appointment for the year ended 31 December 2013, he was paid £19,872 (2012: £19,872). He has retained these fees in accordance with the policy set out in the Policy Report.

Share awards under the legacy DSBP

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

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

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

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

Executive	Date granted	Balance at 1 January 2013	Granted during year	Share price at date of grant	Vested during year	Market price at date of vesting	Market price at date of exercise	Amount realised on exercise (excluding deduction of tax)	Balance at 31 December 2013	Actual/expected vesting date
Andrew Wyllie	12.04.11	82,644[1]	–	241p	82,644[2]	£2.89	£2.89	£247,415	–	April 2013
	04.04.12	78,258[1]	–	232p	–	–	–	–	78,258	April 2014-2022
	03.04.13	–	36,401[1]	272p	–	–	–	–	36,401	April 2015-2013
			10,771 (£29,997)[3]						10,771 (£29,997)	
			10,771[4]						10,771	
Tony Bickerstaff	12.04.11	54,752[1]	–	241p	54,752[2]	£2.89	£2.79	£158,240	–	August 2013
	04.04.12	51,846[1]	–	232p	–	–	–	–	51,846	April 2014-2022
	03.04.13	–	20,394[1]	272p	–	–	–	–	20,394	April 2015-2023
			10,771 (£29,997)[3]						10,771 (£29,997)	
			10,771[4]						10,771	

1 Number of shares under the Deferred Award.
2 In addition, Andrew Wyllie and Tony Bickerstaff received 2,967 and 1,965 dividend shares respectively upon vesting.
3 Maximum number and value of shares under the Combined Deferred Award.
4 Number of shares under the Option.

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

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

Share awards under the LTIP

Executive	Date granted	Balance at 1 January 2013	Granted during year	Share price at date of grant	Vested during year	Market price at date of vesting	Market price at date of exercise	Lapsed during year	Amount realised on exercise (excluding deduction of tax)	Balance at 31 December 2013	Actual/ expected vesting date
Andrew Wyllie	14.04.10[1]	81,632	–	245p	81,632	£2.76	£2.75	–	£224,488	–	March 2013
	12.04.11[2]	169,294	–	241p	–	–	–	–	–	169,294	March 2014
	09.05.12[3]	207,044	–	205p	–	–	–	–	–	207,044	May 2015
	07.05.13[4]	–	163,293	260p	–	–	–	–	–	163,293	May 2016
Tony Bickerstaff	14.04.10[1]	54,081	–	245p	54,081	£2.76	£2.75	–	148,732	–	March 2013
	12.04.11[2]	112,157	–	241p	–	–	–	–	–	112,157	March 2014
	09.05.12[3]	137,167	–	205p	–	–	–	–	–	137,167	May 2015
	07.05.13[4]	–	108,691	260p	–	–	–	–	–	108,691	May 2016

1 EPS for the financial year ended 31 December 2012 of 21.0 pence (15% vests) to EPS of 27.5 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The EPS target was 100% met.

2 50% of the award is subject to an aggregate EPS for the financial years ended 31 December 2011, 2012 and 2013 of 102.3 pence (15% vests) to EPS of 112.6 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The remaining 50% of the award will be based on an EPS for the financial year ended 31 December 2013 of 47 pence (0% vests) to EPS of 56 pence (100% vests) on a sliding scale between 0% and 100% pro-rata to the actual EPS achieved. (EPS targets rounded as appropriate). Subject to the Committee's confirmation, 50% of the target has been met.

3 50% of the award (Tier 1) is subject to an aggregate EPS target for the financial years ended 31 December 2012, 2013 and 2014 of 90 pence (15% vests) to EPS of 100 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The remaining 50% of the award (Tier 2) is based on operating profit for the financial year ending 31 December 2014 of £37 million (50% vests) to £44.4 million (100% vests) on a sliding scale between £29.6 million and £44.4 million pro-rata to the operating profit actually achieved. In addition, no element of the Tier 2 award will vest unless the EPS (before pension interest) for the financial year ended 31 December 2014 is at least 35.5 pence and Tier 1 has vested in full.

4 50% of the award (Tier 1) is subject to an aggregate EPS target for the financial years ended 31 December 2013, 2014 and 2015 of 88.7 pence (15% vests) to EPS of 100 pence (100% vests) on a sliding scale between 15% and 100% pro-rata to the EPS actually achieved. The remaining 50% of the award (Tier 2) is based on operating profit for the financial year ending 31 December 2014 of £42 million (50% vests) to £50 million (100% vests) on a sliding scale between £35 million and £50 million pro-rata to the operating profit actually achieved. In addition, no element of the Tier 2 award will vest unless the EPS (before pension interest) for the financial year ended 31 December 2015 is at least 37.3 pence and Tier 1 has vested in full.

The LTIP awards, which are expressed as options, are subject to an exercise price of £1. At 31 December 2013, the derived mid-market price of the ordinary shares in the Company, as advised by the Company's brokers, was 277 pence. The range of the share price of the ordinary shares during 2013 was 248 pence to 306 pence.

Save As You Earn scheme awards

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

Executive	Date granted	Balance at 1 January 2013	Granted during year	Exercise price	Exercised during year	Market price at date of exercise	Lapsed during year	Amount realised on vesting	Balance at 31 December 2013	Exercisable from/to
Andrew Wyllie	11.10.11	1,633	–	205p	–	–	–	–	1,633	Nov 2014-May 2015
	30.09.13	–	1,572	222p	–	–	–	–	1,572	Nov 2016-May 2017
Tony Bickerstaff	11.10.11	1,633	–	205p	–	–	–	–	1,633	Nov 2014-May 2015
	30.09.13	–	1,572	222p	–	–	–	–	1,572	Nov 2016-May 2017

Directors' remuneration report
continued

Directors' shareholdings
Details of the directors' share interests as at 31 December 2013 and at the date of this report are as follows:

Executive	Beneficially owned	Outstanding DBSP awards	Outstanding LTIP awards	Outstanding SAYE awards	% shareholding requirement (% of salary/ fee)	% actual shareholding (% of salary/ fee)
Andrew Wyllie	289,089	125,430	539,631	3,205	100%	153.99%
Tony Bickerstaff	145,860	83,011	358,015	3,205	100%	111.83%
David Allvey	5,250	–	–	–	100%	7.56%
Michael Alexander	19,101	–	–	–	100%	73.00%
Jane Lodge[1]	2,500	–	–	–	100%	13.09%
James Morley	27,000	–	–	–	100%	115.26%
Ahmed Samy	0	–	–	–	100%	0%

[1] Held by a connected person.

As set out in the Policy Report, Executive Directors are required to build and maintain a shareholding worth not less than 100% of base salary through the retention of vested share awards or through open market purchases. As at 31 December 2013, both the Executive Directors met the shareholding requirement.

On behalf of the Board

Michael R Alexander
Chairman of the Remuneration Committee

26 February 2014

Directors' report

The Directors submit to the members their Report and Accounts of the Company for the year ended 31 December 2013.

The Governance report on pages 46 to 84 and the Corporate Responsibility report on pages 34 to 42 (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 in the Strategic report.

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

Profit and dividends
The profit after tax for the financial year ending 31 December 2013 amounted to £12.5 million (2012: £23.1 million). An interim dividend of 3.75 pence per share (2012: 3.50 pence) amounting to £2.5 million (2012: £2.3 million) was paid on 25 October 2013. A final dividend at the rate of 7.75 pence per share (2012: 7.25 pence) amounting to £5.2 million (2012: £4.7 million) will also be recommended to Shareholders at the General Meeting to be held on 17 March 2014. If approved, the dividend will be paid on 25 April 2014 to shareholders registered at close of business on 14 March 2014.

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

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

Going concern
The Directors believe, after due and careful enquiry, that the Group has sufficient resources for its present requirements and, therefore, consider it appropriate to adopt the going concern basis in preparing the 2013 financial statements as discussed on page 45 of the Finance Director's review and Note 2 to the financial statements.

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

The issued share capital of the Company as at 31 December 2013 was £33,396,470.5, consisting of 66,792,941 ordinary shares of 50 pence each.

Further details of the share capital of the Company can be found in Note 21 on page 127.

The awards granted in April 2010 under the 2002 Long-Term Incentive Plan (the '2002 LTIP') matured as at 31 December 2012 resulting in the vesting of awards in March 2013 over 605,533 ordinary shares of 50 pence each with an exercise price of £1 per exercise. Further details with regard to the vesting of these LTIP awards can be found in the Directors' remuneration report on page 69.

Directors' report

continued

At the 2013 Annual General Meeting, shareholders approved the renewal of the scrip dividend scheme which authorises the Directors to offer and allot ordinary shares in lieu of cash dividends to those shareholders who elect to participate in the scrip dividend. In May 2013, 93,558 ordinary shares of 50 pence each were allotted to shareholders in respect of the final dividend for 2012, and 67,150 ordinary shares of 50 pence each were allotted to shareholders in October 2013 in respect of the interim dividend for 2013. Further information on the scrip dividend scheme is set out on page 134. 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 Listing Rules of the Financial Services Authority whereby certain employees of the Company require the approval of the Company to deal in the Company's ordinary shares.

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

Major shareholders

As at 25 February 2014, the Company had been notified, including under the Disclosure and Transparency Rules issued by the Financial Services Authority ('DTR5'), of the following voting interests in its ordinary share capital:

UEM Builders Berhad(i)	13,810,850	20.68%
Mohammed Abdulmohsin Al-Kharafi & Sons Co. W.L.L.(i)	13,789,490	20.65%

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

Rights and obligations attaching to shares

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

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

The Directors may only issue and buy back shares if authorised to do so by the Articles of Association or the shareholders in general meeting. At the Company's Annual General Meeting held on 8 May 2013, shareholders granted an authority to the Directors to allot ordinary shares up to an aggregate nominal amount of £10.92 million. As this authority is due to expire on 8 May 2014, shareholders' approval will be sought to renew the Directors' authority to allot ordinary shares at the 2014 Annual General Meeting, up to an aggregate nominal amount of £16,699,156. As at 31 December 2013, the only shares that had been allotted were in order to satisfy awards under employee share schemes and the scrip dividends. The Directors did not request authority to buy back any of the Company's shares at the last Annual General Meeting in 2013 and they do not propose to do so at this year's Annual General Meeting.

Securities carrying special rights

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

Restrictions on voting

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

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

Rights under the employee share schemes

ACS HR Solutions Share Plan Services (Guernsey) Limited, as Trustee of the Costain Group Employee Trust, holds 0.58% of the issued share capital of the Company as at 31 December 2013 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 and Save As You Earn Scheme (in respect of 'good leavers' who leave the employment of the Company before their contract matures). The Trustee does not exercise any right to vote or to receive a dividend in respect of this shareholding.

Powers of the Directors

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

Amendment of Articles of Association

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

Political Donations

No political donations were made during the year ended 31 December 2013 (2012: none). The Company has a policy of not making donations to political organisations.

Directors and Directors' interests

Brief biographies of the present members of the Board are given on pages 48 to 49.

In accordance with Article 78 of the Company's Articles of Association and provision B.7.1 of the Code, David Allvey, James Morley, Ahmed Samy and Alison Wood will offer themselves for re-election at the 2014 Annual General Meeting. David Allvey, having been in office for a continuous period in excess of nine years, is required to stand for re-election on an annual basis. James Morley, having served on the Board at the time of the two preceding Annual General Meetings without retiring, is required to stand for re-election at the 2014 Annual General Meeting. Ahmed Samy and Alison Wood, having been appointed as Directors of the Company since the last Annual General Meeting, are required to stand for re-election at the 2014 Annual General Meeting. David Allvey, James Morley, Ahmed Samy and Alison Wood have letters of appointment with the Company, details of which are set out in the Directors' remuneration report.

With regard to the re-election of David Allvey, James Morley, Ahmed Samy and Alison Wood, the Board is of the opinion that they each continue to perform effectively and demonstrate commitment of time for Board and committee meetings and other respective duties.

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 2013, are contained in the Directors' remuneration report, which appears on pages 59 to 76.

Independent Auditors

KPMG Audit Plc has notified the Company that they are not seeking reappointment. It is proposed that KPMG LLP are appointed as auditors of the Company and they will hold office from the conclusion of the AGM in May 2014 until the conclusion of the next general meeting at which the accounts are laid before the Company. See page 55 of the Audit Committee Report and the Notice of Meeting for further details.

Significant agreements – change of control

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

Research and development

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

Greenhouse gas emissions

The Strategic report on page 13 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 Directors.

Directors' report

continued

Appointment and replacement of Directors

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

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

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

Employee Information

The average number of employees within the Company and Group is shown in Note 5 to the Financial Statements on page 105.

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, look 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.

Full details of actions taken to introduce, maintain or develop arrangements aimed at employees are described in the Corporate Responsibility report on pages 37 to 38.

Essential contracts or other arrangements

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

Disclosure of information to Auditors

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

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

By Order of the Board

T. Wood

Tracey Wood
Company Secretary

Directors' responsibilities statement

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

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

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

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

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

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

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

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

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

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

- the Group accounts, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and result 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 Group taken as a whole, together with a description of the principal risks and uncertainties that it faces.

On behalf of the Board

David Allvey
Chairman

Andrew Wyllie
Chief Executive

Independent Auditor's report

to the members of Costain Group PLC

Opinions and conclusions arising from our audit

1 Our opinion on the financial statements is unmodified

We have audited the financial statements of Costain Group PLC for the year ended 31 December 2013 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated and Company Statement of Financial Position, the Consolidated and Company Statement of Changes in Equity, the Consolidated and Company Cash Flow Statement and related notes. In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2013 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

2 Our assessment of risks of material misstatement

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

Contract accounting estimates

Refer to page 55 (Audit Committee Report), page 93 (accounting policy).

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

- inspecting the selected contracts for key clauses, identifying relevant contractual mechanisms such as pain/gain shares, design bonuses, liquidated damages and success fees and assessing whether these key clauses have been appropriately reflected in the amounts recognised in the financial statements;
- assessing whether the amounts recognised in the financial statements resulting from the estimates and assumptions made represent a balanced view of the risks and opportunities pertinent to each contract position;
- considering whether provisions against contracts sufficiently reflect the level of risk, and challenging the Group's judgement in this area with reference to our own assessments.; and
- considering the adequacy of the group's disclosures in respect of contract accounting and the key risks relating to these amounts.

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

Refer to page 55 (Audit Committee Report), page 93 (accounting policy) and pages 111-112 (financial disclosures)

- *The Risk:* Alcaidesa Holding SA (equity accounted joint venture with a carrying value of £27 million in the accounts) operates in the Spanish real estate market and holds as its principal non-current assets, a marina and two golf courses and, as its principal current asset, land held for development. The Group performs a yearly review for impairment of the non-current assets and of the net realisable value of the development land to determine if these assets are being recorded at an appropriate level and that the additional write down recognised in the current year was appropriate. Due to the current depressed state of the Spanish economy and the property market in particular the valuation of these assets represents a significant risk in the Group balance sheet.
- *Our response:* The non-current assets (namely golf courses and a marina) have been valued by the company using discounted cash flow projection models. In respect of these assets our procedures included, among others, testing these models to establish whether they were appropriately designed and operating correctly. With respect to the key inputs and assumptions driving the outputs of the models, we utilised a member of the audit team with specialist valuation skills to compare that data with our historical experience, our knowledge of the relevant market and market forecasts for growth and inflation. Our audit procedures in respect of the land held for development in the Alcaidesa portfolio included, among others, inspecting copies of the external valuations for that land and performing procedures to evaluate whether the valuation firms that produced the reports were suitably qualified. We utilised a member of the team with specialist valuation skills to test the underlying assumptions by comparing them to market evidence and our knowledge of the sites. We also considered the adequacy of the group's disclosures in respect of the joint venture.

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

The materiality for the financial statements as a whole was set at £1.7 million. This has been determined with reference to a benchmark of group profit before taxation which we consider to be one of the principal considerations for members of the company in assessing the financial performance of the group. Materiality represents 13% of group profit before tax and 5.4% of group profit before other items as disclosed on the face of the consolidated income statement.

We agreed with the audit committee to report to it all corrected and uncorrected misstatements we identified through our audit with a value in excess of £85,000, in addition to other audit misstatements below that threshold that we believe warranted reporting on qualitative grounds.

Audits for group reporting purposes were performed by component auditors at the key reporting component in Spain and by the group audit team in the UK. These procedures covered 99% of total group revenue; 99% of group profit before other items and taxation and 99% of total group assets. The segment disclosures in Note 3 set out the individual significance of a specific countries.

The audit undertaken for group reporting purposes in Spain was performed to a materiality level set by the group audit team at £850,000.

Detailed audit instructions were sent to the auditors in Spain. These instructions covered the significant audit areas that should be covered by the audit (which included the relevant risks of material misstatement detailed above) and set out the information required to be reported back to the group audit team. The group audit team also attended the final audit meeting in Spain.

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

In our opinion:

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

Independent Auditor's report
continued

5 We have nothing to report in respect of the matters on which we are required to report by exception
Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

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

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

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

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

Under the Listing Rules we are required to review:

- the directors' statement, set out on page 77, in relation to going concern;
- the part of the Corporate Governance statement on page 50 relating to the company's compliance with the nine provisions of the 2010 UK Corporate Governance Code specified for our review.

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

Scope of report and responsibilities
As explained more fully in the Directors' responsibilities statement set out on page 81, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at **www.frc.org.uk/auditscopeukprivate**. This report is made solely to the Company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at **www.kpmg.com/uk/auditscopeukco2013a**, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

Andrew Marshall
(Senior Statutory Auditor)

for and on behalf of KPMG Audit Plc,
Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

26 February 2014

Financial statements

This section contains the detailed financial statements and other information that our stakeholders find useful, including the financial calendar and shareholder services.

In this section

The Chairman's statement can be found on page 6.
The Chief Executive's review can be found on page 8.
The Finance Director's review can be found on page 43.

Consolidated income statement

Year ended 31 December

	Notes	2013 Before other items £m	2013 Other items £m	2013 Total £m	2012 (restated) Before other items £m	2012 (restated) Other items £m	2012 (restated) Total £m
Continuing operations							
Revenue	3	**960.0**	**–**	**960.0**	934.5	–	934.5
Less: Share of revenue of joint ventures and associates	13	**(74.8)**	**–**	**(74.8)**	(86.1)	–	(86.1)
Group revenue		**885.2**	**–**	**885.2**	848.4	–	848.4
Cost of sales		**(826.7)**	**–**	**(826.7)**	(794.2)	–	(794.2)
Gross profit		**58.5**	**–**	**58.5**	54.2	–	54.2
Administrative expenses		**(31.1)**	**–**	**(31.1)**	(29.7)	–	(29.7)
Pension liability management		**–**	**–**	**–**	(2.8)	–	(2.8)
Exceptional transaction costs	4	**–**	**(3.7)**	**(3.7)**	–	–	–
Amortisation of acquired intangible assets		**–**	**(1.8)**	**(1.8)**	–	(1.7)	(1.7)
Employment related and other deferred consideration		**–**	**(2.8)**	**(2.8)**	–	(1.7)	(1.7)
Group operating profit		**27.4**	**(8.3)**	**19.1**	21.7	(3.4)	18.3
Profit on sales of interests in joint ventures and associates	4	**9.1**	**–**	**9.1**	10.5	–	10.5
Share of results of joint ventures and associates	13	**(1.5)**	**(9.8)**	**(11.3)**	(1.4)	–	(1.4)
Profit from operations	3	**35.0**	**(18.1)**	**16.9**	30.8	(3.4)	27.4
Finance income	7	**0.7**	**–**	**0.7**	1.0	–	1.0
Finance expense	7	**(4.7)**	**–**	**(4.7)**	(3.7)	–	(3.7)
Net finance expense		**(4.0)**	**–**	**(4.0)**	(2.7)	–	(2.7)
Profit before tax	3/4	**31.0**	**(18.1)**	**12.9**	28.1	(3.4)	24.7
Income tax	8	**(1.8)**	**1.4**	**(0.4)**	(2.2)	0.6	(1.6)
Profit for the year attributable to equity holders of the parent		**29.2**	**(16.7)**	**12.5**	25.9	(2.8)	23.1
Earnings per share							
Basic	9	**44.1p**	**(25.3)p**	**18.8p**	39.7p	(4.3)p	35.4p
Diluted	9	**42.4p**	**(24.3)p**	**18.1p**	38.3p	(4.1)p	34.2p

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

	2013 £m	2012 (restated) £m
Profit for the year	**12.5**	23.1
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of foreign operations	**(0.2)**	(1.1)
Cash flow hedges		
Group:		
Effective portion of changes in fair value during year	**(0.1)**	–
Net changes in fair value transferred to the income statement	**0.2**	0.1
Joint ventures and associates:		
Effective portion of changes in fair value (net of tax) during year	**(0.2)**	(0.4)
Net changes in fair value (net of tax) transferred to the income statement	**1.2**	4.0
Total items that may be reclassified subsequently to profit or loss	**0.9**	2.6
Items that will not be reclassified to profit or loss:		
Remeasurement of defined benefit liability	**8.6**	(23.0)
Tax recognised on remeasurement of defined benefit liability	**(5.3)**	2.4
Total items that will not be reclassified to profit or loss	**3.3**	(20.6)
Other comprehensive income/(expense) for the year	**4.2**	(18.0)
Total comprehensive income for the year attributable to equity holders of the parent	**16.7**	5.1

Consolidated statement of financial position

As at 31 December

	Notes	2013 £m	2012 £m
Assets			
Non-current assets			
Intangible assets	11	**33.0**	18.7
Property, plant and equipment	12	**7.9**	9.1
Investments in equity accounted joint ventures	13	**27.1**	36.1
Investments in equity accounted associates	13	**0.2**	1.6
Loans to equity accounted associates	13	**4.8**	2.7
Other	14	**22.0**	17.5
Deferred tax	8	**9.8**	17.4
Total non-current assets		**104.8**	103.1
Current assets			
Inventories		**1.6**	1.7
Trade and other receivables	14	**190.6**	181.5
Cash and cash equivalents	15	**84.3**	107.4
Total current assets		**276.5**	290.6
Total assets		**381.3**	393.7
Equity			
Share capital	21	**33.4**	32.8
Share premium		**4.7**	3.7
Foreign currency translation reserve		**4.8**	5.0
Hedging reserve		**(0.1)**	(1.2)
Retained earnings		**0.5**	(8.5)
Total equity attributable to equity holders of the parent		**43.3**	31.8
Liabilities			
Non-current liabilities			
Retirement benefit obligations	20	**37.2**	51.9
Other payables	18	**4.3**	5.0
Provisions for other liabilities and charges	19	**0.4**	1.9
Total non-current liabilities		**41.9**	58.8
Current liabilities			
Trade and other payables	18	**266.1**	297.6
Income tax liabilities	8	**1.6**	1.7
Bank overdrafts	15	**1.6**	1.7
Interest bearing loans and borrowings	16	**25.0**	–
Provisions for other liabilities and charges	19	**1.8**	2.1
Total current liabilities		**296.1**	303.1
Total liabilities		**338.0**	361.9
Total equity and liabilities		**381.3**	393.7

The financial statements were approved by the Board of Directors on 26 February 2014 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	2013 £m	2012 £m
Assets			
Non-current assets			
Investments in subsidiaries	13	**97.9**	95.2
Total non-current assets		**97.9**	95.2
Current assets			
Trade and other receivables	14	**51.3**	39.9
Cash and cash equivalents	15	**–**	30.0
Total current assets		**51.3**	69.9
Total assets		**149.2**	165.1
Equity			
Share capital	21	**33.4**	32.8
Share premium		**4.7**	3.7
Other reserves		**12.0**	9.3
Retained earnings		**21.9**	32.1
Total equity attributable to equity holders of the parent		**72.0**	77.9
Liabilities			
Non-current liabilities			
Provisions for other liabilities and charges	19	**1.3**	1.3
Total non-current liabilities		**1.3**	1.3
Current liabilities			
Trade and other payables	18	**49.3**	84.0
Income tax liabilities	8	**1.5**	1.7
Interest bearing loans and borrowings	16	**25.0**	–
Provisions for other liabilities and charges	19	**0.1**	0.2
Total current liabilities		**75.9**	85.9
Total liabilities		**77.2**	87.2
Total equity and liabilities		**149.2**	165.1

The financial statements were approved by the Board of Directors on 26 February 2014 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 2012	32.4	3.3	6.1	(4.9)	(6.1)	30.8
Profit for the year	–	–	–	–	23.1	23.1
Other comprehensive income/(expense)	–	–	(1.1)	3.7	(20.6)	(18.0)
Issue of ordinary shares under employee share option plans	0.3	–	–	–	(0.3)	–
Equity-settled share-based payments	–	–	–	–	2.1	2.1
Dividends paid	0.1	0.4	–	–	(6.7)	(6.2)
At 31 December 2012	32.8	3.7	5.0	(1.2)	(8.5)	31.8
At 1 January 2013	**32.8**	**3.7**	**5.0**	**(1.2)**	**(8.5)**	**31.8**
Profit for the year	**–**	**–**	**–**	**–**	**12.5**	**12.5**
Other comprehensive income/(expense)	**–**	**–**	**(0.2)**	**1.1**	**3.3**	**4.2**
Issue of ordinary shares under employee share option plans	**0.5**	**0.6**	**–**	**–**	**(0.3)**	**0.8**
Shares purchased to satisfy employee share schemes	**–**	**–**	**–**	**–**	**(1.5)**	**(1.5)**
Equity-settled share-based payments	**–**	**–**	**–**	**–**	**2.2**	**2.2**
Dividends paid	**0.1**	**0.4**	**–**	**–**	**(7.2)**	**(6.7)**
At 31 December 2013	**33.4**	**4.7**	**4.8**	**(0.1)**	**0.5**	**43.3**

Company statement of changes in equity

	Share capital £m	Share premium £m	Other reserve £m	Retained earnings £m	Total equity £m
At 1 January 2012	32.4	3.3	6.4	38.1	80.2
Comprehensive income	–	–	–	1.0	1.0
Issue of ordinary shares under employee share option plans	0.3	–	–	(0.3)	–
Equity-settled share-based payments granted to employees of subsidiaries	–	–	2.9	–	2.9
Dividends paid	0.1	0.4	–	(6.7)	(6.2)
At 31 December 2012	32.8	3.7	9.3	32.1	77.9
At 1 January 2013	**32.8**	**3.7**	**9.3**	**32.1**	**77.9**
Comprehensive expense	**–**	**–**	**–**	**(2.7)**	**(2.7)**
Issue of ordinary shares under employee share option plans	**0.5**	**0.6**	**–**	**(0.3)**	**0.8**
Equity-settled share-based payments granted to employees of subsidiaries	**–**	**–**	**2.7**	**–**	**2.7**
Dividends paid	**0.1**	**0.4**	**–**	**(7.2)**	**(6.7)**
At 31 December 2013	**33.4**	**4.7**	**12.0**	**21.9**	**72.0**

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

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

Group

Translation reserve

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

Hedging reserve

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

Company

Other reserve

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

Consolidated cash flow statement

Year ended 31 December

	Notes	2013 £m	2012 £m
Cash flows from operating activities			
Profit for the year		**12.5**	23.1
Adjustments for:			
Share of results of joint ventures and associates	13	**11.3**	1.4
Finance income	7	**(0.7)**	(1.0)
Finance expense	7	**4.7**	3.7
Income tax	8	**0.4**	1.6
Profit on sales of interests in joint ventures and associates	4	**(9.1)**	(10.5)
Depreciation of property, plant and equipment	4	**2.4**	2.3
Amortisation of intangible assets	4	**2.3**	1.8
Employment related and other deferred consideration		**2.8**	1.7
Shares purchased to satisfy employee share schemes		**(1.5)**	–
Share-based payments expense	5	**2.7**	2.9
Cash from operations before changes in working capital and provisions		**27.8**	27.0
Decrease in inventories		**0.1**	0.6
(Increase)/decrease in receivables		**(12.2)**	4.1
Decrease in payables		**(40.7)**	(48.1)
Movement in provisions and employee benefits		**(7.9)**	(5.9)
Cash used by operations		**(32.9)**	(22.3)
Interest received		**0.6**	1.0
Interest paid		**(2.9)**	(1.8)
Income tax paid		**(0.3)**	–
Net cash used by operating activities		**(35.5)**	(23.1)
Cash flows from/(used by) investing activities			
Dividends received from joint ventures and associates	13	**1.3**	0.6
Additions to property, plant and equipment	12	**(1.3)**	(0.8)
Additions to intangible assets	11	**(1.2)**	(0.1)
Proceeds of disposal of property, plant and equipment		**0.2**	0.6
Additions to loans to joint ventures and associates	13	**(2.2)**	(5.4)
Additions to cost of investments	13	**(2.7)**	–
Proceeds of sale of interests in associates		**11.7**	–
Acquisition related deferred consideration		**(3.0)**	–
Acquisition of subsidiary (net of acquired cash and cash equivalents and overdrafts)	25	**(9.4)**	–
Net cash used by investing activities		**(6.6)**	(5.1)
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		**0.8**	–
Ordinary dividends paid		**(6.7)**	(6.2)
Drawdown of revolving credit facility	16	**25.0**	–
Net cash from/(used by) financing activities		**19.1**	(6.2)
Net decrease in cash, cash equivalents and overdrafts		**(23.0)**	(34.4)
Cash, cash equivalents and overdrafts at beginning of the year	15	**105.7**	140.1
Cash, cash equivalents and overdrafts at end of the year	15	**82.7**	105.7

Company cash flow statement

Year ended 31 December

	Notes	2013 £m	2012 £m
Cash flows from operating activities			
(Loss)/profit for the year		**(2.7)**	1.0
Adjustments for:			
Finance income		**(0.7)**	(2.2)
Finance expense		**0.3**	0.3
Income tax		**(1.1)**	(0.1)
Loss on sale of investment		**–**	0.7
Cash used by operations before changes in working capital and provisions		**(4.2)**	(0.3)
Increase in receivables		**(9.9)**	(3.5)
Decrease in payables		**(32.2)**	(23.4)
Movement in provisions		**(0.1)**	(0.3)
Cash used by operations		**(46.4)**	(27.5)
Interest received		**–**	0.6
Interest paid		**(2.8)**	(0.3)
Income tax received		**0.1**	0.1
Net cash used by operating activities		**(49.1)**	(27.1)
Cash flows from investing activities			
Dividends received		**–**	1.6
Net cash from investing activities		**–**	1.6
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		**0.8**	–
Ordinary dividends paid		**(6.7)**	(6.2)
Drawdown of revolving credit facility	16	**25.0**	–
Net cash from/(used by) financing activities		**19.1**	(6.2)
Net decrease in cash and cash equivalents		**(30.0)**	(31.7)
Cash and cash equivalents at beginning of the year	15	**30.0**	61.7
Cash and cash equivalents at end of the year	15	**–**	30.0

Notes to the financial statements

1 General information

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

The consolidated financial statements of the Company for the year ended 31 December 2013 comprise the Group and the Group's interests in associates, jointly controlled entities and jointly controlled 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 26 February 2014.

2 Summary of significant accounting policies

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

Basis of preparation

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

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

Going concern

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

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

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

Accounting policies

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

The following standards and interpretations are effective for the year ended 31 December 2013:

- IAS 19 (revised 2011) 'Employee Benefits'
- Amendments to IAS 1 'Presentation of Items of Other Comprehensive Income'
- Amendments to IFRS 7 'Financial Instruments: Disclosures' – 'Offsetting Financial Assets and Financial Liabilities'
- IFRS 13 'Fair Value Measurement'

Notes to the financial statements
continued

2 Summary of significant accounting policies continued

Accounting policies continued

The revision to IAS 19 requires the financing cost of a defined benefit scheme to be calculated on the net surplus or deficit. The 2012 figures have been restated for consistency with 2013 and this has reduced the previously reported operating profit by £0.6 million, increased pension interest expense by £0.8 million and reduced the tax charge by £0.3 million with a corresponding increase in other comprehensive income. Earnings per share has reduced by 1.7 pence. There is no impact on the pension deficit or cash.

The amendment to IAS 1 requires an entity to present the items of other comprehensive income that may be recycled to profit or loss in the future separately from those that would never be recycled to profit or loss. The presentation has been amended to satisfy this requirement.

The amendment to IFRS 7 changes the disclosure requirements in respect of financial instruments that are set-off in accordance with guidance in IAS 32. This has not had an impact on these financial statements.

Fair value measurement

IFRS 13 'Fair Value Measurement' establishes a single framework for measuring fair value and making disclosures about fair value measurements when such measures are required or permitted by other IFRSs. It unifies the definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. an exit price). It replaces and expands the disclosure requirements about fair value measurements in other IFRSs, including IFRS 7. As a result, the Group has included additional disclosures in this regard (see Note 17).

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

- Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

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

In accordance with the transitional provisions of IFRS 13, the Group has applied the new fair value measurement guidance prospectively and has not provided any comparative information for new dislcosures. Notwithstanding the above, the change had no significant impact on the measurement of the Group's assets and liabilities. A limited number of assets and liabilities required Level 2 or Level 3 valuations, see Note 17(e)(i), but have not resulted in a change to their carrying values.

Basis of consolidation

(a) The Group's financial statements include the financial statements of the Company and subsidiaries controlled by the Company. Control exists where the Company or one of its subsidiaries has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. 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. If the share of losses equals the investment, no further losses are recognised, except to the extent that there are amounts receivable that may not be recoverable or further commitments to provide funding.

(c) Jointly controlled entities are those joint ventures where control is shared with another entity, established by contractual agreement. Jointly controlled entities are accounted for using the equity method from the date that the jointly controlled entity commences until the date that joint control of the entity ceases. If the share of losses equals the investment in the entity, no further losses are recognised, except to the extent that there are amounts receivable that may not be recoverable or further commitments to provide funding.

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

2 Summary of significant accounting policies continued

Basis of consolidation continued

(e) Jointly controlled operations are those joint ventures over which joint control exists, established by contractual agreement, which are not legal entities. Where a jointly controlled operation exists, then the Group entity involved records the assets it controls, the liabilities and expenses it incurs and its share of income. Such jointly controlled operations are reported in the consolidated financial statements on the same basis. Transactions between Group companies and jointly controlled 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, jointly controlled entities and jointly controlled operations are eliminated to the extent of the interest in the entity or operation. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Currency translation

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

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

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

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable, net of value added tax and includes the share of revenue of jointly controlled operations. 96% of the Group's revenue arises from long-term contracts.

(a) Long-term contracts

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

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

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

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

(b) Other revenue

Revenue from other services contracts is recognised when the service is provided.

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

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

Income statement presentation – Other items

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

2 Summary of significant accounting policies
continued

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

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

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

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

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

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

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

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

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

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

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

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

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

2 Summary of significant accounting policies continued

Impairment of non-financial assets

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

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

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

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

Provisions

A provision is recognised in the statement of financial position when there is a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

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

Taxation

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

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

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

Deferred tax liabilities are recognised for temporary differences arising on investments in subsidiaries and interests in joint ventures, 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.

2 Summary of significant accounting policies continued

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

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

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

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

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

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

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

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

Adminstration 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 available-for-sale financial assets and loans and receivables. The classification depends on the nature and purpose of the financial assets 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.

Effective interest method
The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

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

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

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

2 Summary of significant accounting policies continued

(a) Financial assets continued

Cash and cash equivalents

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

Investments

Investments are recognised and derecognised on the trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned.

Investments are measured initially at fair value plus transaction costs.

(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. The fair value of interest rate and RPI swaps is the estimated amount that would be received or paid to terminate the swap at the statement of financial position date. Valuations for forward exchange contracts and interest rate and RPI swaps are determined using valuation techniques supported by reference to market values for similar transactions.

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

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

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

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

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

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

Significant areas of judgment and estimation

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

Notes to the financial statements
continued

2 Summary of significant accounting policies continued

Significant areas of judgment and estimation continued

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

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

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

Alcaidesa Holding SA, one of the Group's joint ventures, operates in the Spanish real estate market and holds land and property within its current and non-current assets. The company has also developed and operates a marina under a long-term concession agreement and has developed and operates two golf courses. At 31 December 2013, a review of the net realisable value of each of its land holdings has been undertaken using external professional valuers. A review of the carrying value of the marina and golf course assets has been undertaken using a discounted cash flow model. As a consequence of those reviews, write downs in the value of Alcaidesa's assets of £9.8m (Costain's share) have been reflected in these financial statements.

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

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

IFRSs not applied

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

- IAS 27 (Revised) 'Separate Financial Statements' will be effective from 2014. This is not expected to have an impact on the financial statements.
- IAS 28 (Revised) 'Investments in Associates and Joint Ventures' will be effective from 2014. This is not expected to have an impact on the financial statements.
- Amendment to IAS 32 'Financial Instruments: Presentation' – Offsetting Financial Assets and Financial Liabilities' – this amendment clarifies the application of offsetting criteria in financial statements. This is not expected to have a significant impact on the financial statements. It will be effective for 2014.
- IFRS 10 'Consolidated Financial Statements' – this now provides a single model establishing principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. This is not expected to have a significant impact on the consolidated financial statements. It will be effective for 2014, being adopted as a 'suite of standards' (with IFRS 11 and 12 and the revisions to IAS 27/28).
- IFRS 11 'Joint Arrangements' – this could result in changes to the classification of certain jointly controlled operations where the Group accounts for its share of the individual assets or liabilities to being equity accounted as associates or joint ventures. Currently, it will not affect the Group's profit for the period or net assets. It will be effective for 2014, being adopted as a 'suite of standards' (with IFRS 10 and 12 and the revisions to IAS 27/28).
- IFRS 12 'Disclosure of Interests in Other Entities' – requires the disclosure of information that enables users of financial statements to evaluate the nature of, and risk associated with, its interests in other entities and the effects of those interests on its financial position, financial performance and cash flows. This is not expected to have a significant impact on the financial statements. It will be effective for 2014, being adopted as a 'suite of standards' (with IFRS 10 and 11 and the revisions to IAS 27/28).
- Transition guidance: Amendments to IFRS 10, IFRS 11 and IFRS 12 – amendments to simplify the transition to these standards.

The following IFRSs have not been endorsed, but may be applicable in the future:

- IFRS 9 'Financial Instruments' – classification of financial assets for measurement purposes. This is not expected to have a significant impact on the financial statements. There is no current EU adoption date.

3 Operating segments

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

In November 2012, the Group announced the formation of the new Natural Resources operating division, encompassing Water, Hydrocarbons and Chemicals, Nuclear Process and Waste sectors. The division combined most of the existing Energy & Process and Environment divisions with some support service activities previously in Infrastructure. The new divisional structure enables the Group to align itself more closely with its customers' evolving requirements and to combine further its front end process engineering, project delivery and operations capability into an integrated service for customers. Results for the year ended 31 December 2012 have been restated for consistency with 2013.

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

Intersegment sales and transfers are not material.

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

Notes to the financial statements
continued

3 Operating segments continued

	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Expenditure on non-current assets					
Property, plant and equipment	**1.2**	**0.1**	**–**	**–**	**1.3**
Intangible assets	**0.7**	**2.9**	**–**	**–**	**3.6**
Loans to joint ventures and associates	**2.2**	**–**	**–**	**–**	**2.2**
Segment liabilities					
Reportable segment liabilities	**109.7**	**155.4**	**–**	**7.5**	**272.6**
Unallocated liabilities:					
Retirement benefit obligations					**37.2**
Overdrafts					**1.6**
Borrowings					**25.0**
Income tax					**1.6**
Total liabilities					**338.0**

2012 (restated)	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Segment revenue					
External revenue	353.5	494.9	–	–	848.4
Share of revenue of joint ventures and associates	84.2	–	1.9	–	86.1
Total segment revenue	437.7	494.9	1.9	–	934.5
Segment profit/(loss)					
Operating profit/(loss)	8.1	23.5	–	(7.1)	24.5
Pension liability management	–	–	–	(2.8)	(2.8)
Profit on sale of interest in joint venture	10.5	–	–	–	10.5
Share of results of joint ventures and associates	0.9	–	(2.3)	–	(1.4)
Profit/(loss) from operations before other items	19.5	23.5	(2.3)	(9.9)	30.8
Other items:					
Amortisation of acquired intangible assets	(0.8)	(0.9)	–	–	(1.7)
Employment related deferred consideration	(1.2)	(0.5)	–	–	(1.7)
Profit/(loss) from operations	17.5	22.1	(2.3)	(9.9)	27.4
Net finance expense					(2.7)
Profit before tax					24.7
Segment profit/(loss) is stated after charging the following:					
Depreciation	2.0	0.3	–	–	2.3
Amortisation (including acquired intangible assets)	0.2	1.6	–	–	1.8
Segment assets					
Reportable segment assets	107.7	125.2	36.0	–	268.9
Unallocated assets:					
Deferred tax					17.4
Cash and cash equivalents					107.4
Total assets					393.7

3 Operating segments continued

	Natural Resources £m	Infrastructure £m	Land Development £m	Central costs £m	Total £m
Expenditure on non-current assets					
Property, plant and equipment	0.3	0.5	–	–	0.8
Intangible assets	0.2	–	–	–	0.2
Loans to joint ventures and associates	2.2	–	3.2	–	5.4
Segment liabilities					
Reportable segment liabilities	148.7	146.7	–	11.2	306.6
Unallocated liabilities:					
Retirement benefit obligations					51.9
Overdrafts					1.7
Income tax					1.7
Total liabilities					361.9

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.

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

2012	External revenue £m	Share of revenue of JVs and assoc's £m	Total segment revenue £m	Non-current assets £m
United Kingdom	826.0	84.2	910.2	49.7
Spain	–	1.9	1.9	36.0
Rest of the World	22.4	–	22.4	–
	848.4	86.1	934.5	85.7

Customers accounting for more than 10% of revenue

Two customers (2012: one) in the Infrastructure segment accounted for revenue of £289.6 million (2012: £116.0 million).

Notes to the financial statements

continued

4 Other operating expenses and income

	2013 £m	2012 £m
Profit before tax is stated after charging:		
Amortisation of intangible assets (Note 11)	**2.3**	1.8
Depreciation of property, plant and equipment (Note 12)	**2.4**	2.3
Exceptional transaction costs	**3.7**	–
Hire of plant and machinery	**27.6**	26.8
Rent of land and buildings	**5.2**	4.0
and after crediting:		
Profit on sales of interests in joint ventures and associates	**9.1**	10.5
Income from sub-leases of land and buildings	**0.7**	1.1

Costs of £3.7 million associated with the lasped all share merger with May Gurney Integrated Services plc have been shown as exceptional transaction costs within Other items.

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

In February 2012, the Group transferred two PFI investments, Integrated Bradford Holdco Two Limited and Lewisham Schools for the Future Holdings 2 Limited, to The Costain Pension Scheme for £20.3 million. The transfer amount was included as a contribution received by the Scheme. As a result of the transfer, £4.0 million of fair value adjustments on the PFI financial assets relating to cash flow hedges were recycled through the income statement within the profit of £10.5 million.

Auditors' remuneration

	2013 £m	2012 £m
Fees payable to the Group's auditor for the audit of the annual financial statements	**0.1**	0.1
Fees payable to the Group's auditor and its associates in respect of:		
– Audit of financial statements of subsidiaries of the Company	**0.3**	0.3
– Other tax advisory services	**0.1**	0.1
– Transaction related services not covered above	**1.6**	0.3
	2.1	0.8

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	2013 £m	2012 £m
Wages and salaries	**151.4**	153.7
Social security costs	**16.2**	16.1
Pension costs (Note 20)	**7.1**	8.1
Share-based payments expense (Note 20)	**2.7**	2.9
	177.4	180.8

Average number of persons employed	2013 Number	2012 Number
Natural Resources	**1,397**	2,132
Infrastructure	**2,201**	2,129
Central	**22**	22
	3,620	4,283

Of the above employees 292 were employed overseas (2012: 1,012).

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, 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 2013 and 2012 are detailed below.

	2013 £m	2012 £m
Remuneration	**1.6**	1.4
Post-employment benefits	**0.1**	0.1
Gains made on the exercise of share-based plans	**0.7**	0.6
	2.4	2.1

7 Net finance expense

	2013 £m	2012 (restated) £m
Interest income from bank deposits	**0.1**	0.3
Interest income on loans to related parties	**0.6**	0.7
Finance income	**0.7**	1.0
Interest payable on bank overdrafts, interest bearing loans, borrowings and other similar charges	**(2.6)**	(1.8)
Interest cost on the net liabilities of the defined benefit pension scheme (Note 20)	**(2.1)**	(1.9)
Finance expense	**(4.7)**	(3.7)
Net finance expense	**(4.0)**	(2.7)

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

Notes to the financial statements

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8 Income tax

	2013 £m	2012 (restated) £m
On profit for the year		
United Kingdom corporation tax at 23.25% (2012: 24.5%) – Adjustment in respect of prior years	**0.1**	0.1
Current tax credit for the year	**0.1**	0.1
Deferred tax charge for current year	**(1.4)**	(1.9)
Adjustment in respect of prior years	**0.9**	0.2
Deferred tax charge for the year	**(0.5)**	(1.7)
Income tax expense in the consolidated income statement	**(0.4)**	(1.6)

	2013 £m	2012 (restated) £m
Tax reconciliation		
Profit before tax	**12.9**	24.7
Income tax at 23.25% (2012: 24.5%)	**(3.0)**	(6.1)
Share of results of joint ventures and associates at 23.25% (2012: 24.5%)	**(2.6)**	(0.3)
Disallowed provisions and expenses	**(0.1)**	(0.2)
Non-taxable gains and profits relieved by capital losses	**2.2**	2.6
Utilisation of previously unrecognised temporary differences	**0.7**	1.5
Rate adjustments relating to deferred taxation and overseas profits and losses	**1.4**	0.6
Adjustments in respect of prior years, mainly research and development tax relief claims	**1.0**	0.3
Income tax expense in the consolidated income statement	**(0.4)**	(1.6)
Effective rate of tax	**3.1%**	6.5%

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

The current tax liabilities of £1.6 million (2012: £1.7 million) for the Group and £1.5 million (2012: £1.7 million) for the Company represent the amount of income taxes in respect of all outstanding periods.

Accumulated tax losses carried forward, mainly in the United Kingdom, were £5.3 million (2012: £5.3 million).

Deferred tax asset recognised at 21.0% (2012: 23.0%)	2013 £m	2012 £m
Accelerated capital allowances	**1.6**	1.7
Short-term temporary differences	**–**	3.5
Retirement benefit obligations	**7.9**	11.9
Tax losses	**0.3**	0.3
Deferred tax asset	**9.8**	17.4

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

8 Income tax continued

Analysis of deferred tax movements	2013 £m	2012 £m
At 1 January	**17.4**	17.4
Deferred tax relating to business combinations		
Transfer in respect of acquired intangible assets	**(1.3)**	–
Deferred tax in consolidated income statement		
Accelerated capital allowances	**(0.4)**	(0.2)
Short-term temporary differences	**(1.2)**	2.2
Trading tax losses	**–**	(0.1)
Retirement benefit obligations	**1.1**	(3.6)
	(0.5)	(1.7)
Deferred tax in other comprehensive income and expense statement		
Retirement benefit obligations	**(5.3)**	2.4
Deferred tax recognised directly in the consolidated changes in equity statement		
Short-term temporary differences	**(0.5)**	(0.7)
At 31 December	**9.8**	17.4

Factors that may affect future tax charges

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

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

	Group		Company	
	2013 £m	2012 £m	**2013 £m**	2012 £m
Accelerated capital allowances	**3.3**	3.0	**–**	–
Short-term temporary differences	**22.0**	21.3	**–**	–
Trading tax losses	**3.8**	3.9	**–**	–
Temporary differences	**29.1**	28.2	**–**	–
In addition to the above temporary differences, the following deferred gross tax assets are available.				
Management expenses and charges incurred by parent Company	**56.9**	56.9	**56.9**	56.9
Capital losses	**275.0**	275.0	**241.0**	241.0

The current year tax effect at 23.25% of using the above short-term temporary differences and trading tax losses was £0.7 million (2012: £1.5 million) as detailed 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.

A further reduction to reflect the proposed tax rate of 20.0% from 1 April 2015 would reduce the deferred tax asset by £0.5 million.

Notes to the financial statements
continued

9 Earnings per share

The calculation of earnings per share is based on profit of £12.5 million (2012: £23.1 million (restated)) and the number of shares set out below.

	2013 Number (millions)	2012 Number (millions)
Weighted average number of ordinary shares in issue for basic earnings per share calculation	**66.3**	65.3
Dilutive potential ordinary shares arising from employee share schemes	**2.6**	2.3
Weighted average number of ordinary shares in issue for diluted earnings per share calculation	**68.9**	67.6

At 31 December 2013, all options were included in the diluted weighted average number of ordinary shares calculation (2012: all).

10 Dividends

	Dividend per share pence	2013 £m	2012 £m
Final dividend for the year ended 31 December 2011	6.75	**–**	4.4
Interim dividend for the year ended 31 December 2012	3.50	**–**	2.3
Final dividend for the year ended 31 December 2012	7.25	**4.7**	–
Interim dividend for the year ended 31 December 2013	3.75	**2.5**	–
Amount recognised as distributions to equity holders in the year		**7.2**	6.7
Dividends settled in shares		**(0.5)**	(0.5)
Dividends settled in cash		**6.7**	6.2

A final dividend in respect of the year ended 31 December 2013 of 7.75p per share, amounting to a dividend of £5.2 million, is to be proposed at the Annual General Meeting. If approved, the dividend is expected to be paid on 25 April 2014 to shareholders registered at the close of business on 14 March 2014 and a scrip dividend alternative will be offered. These financial statements do not reflect the final dividend payable.

11 Intangible assets

Group	Goodwill £m	Customer relationships £m	Other acquired intangibles £m	Software & development £m	Total £m
Cost					
At 1 January 2012	15.2	4.1	1.7	5.1	26.1
Additions	–	–	–	0.2	0.2
At 31 December 2012	15.2	4.1	1.7	5.3	26.3
At 1 January 2013	**15.2**	**4.1**	**1.7**	**5.3**	**26.3**
Acquired through business combinations	**7.1**	**4.5**	**1.4**	**–**	**13.0**
Additions	**–**	**–**	**2.4**	**1.2**	**3.6**
At 31 December 2013	**22.3**	**8.6**	**5.5**	**6.5**	**42.9**
Amortisation					
At 1 January 2012	–	0.7	0.2	4.9	5.8
Provided in year	–	1.5	0.2	0.1	1.8
At 31 December 2012	–	2.2	0.4	5.0	7.6
At 1 January 2013	**–**	**2.2**	**0.4**	**5.0**	**7.6**
Provided in year	**–**	**0.4**	**1.4**	**0.5**	**2.3**
At 31 December 2013	**–**	**2.6**	**1.8**	**5.5**	**9.9**
Net book value					
At 31 December 2013	**22.3**	**6.0**	**3.7**	**1.0**	**33.0**
At 31 December 2012	15.2	1.9	1.3	0.3	18.7
At 1 January 2012	15.2	3.4	1.5	0.2	20.3

11 Intangible assets continued

In December 2013, the Group acquired the 27% interest from its partner Serco Group plc in their Managed Motorway Technology joint venture arrangement for a cash consideration of £2.4 million. The joint venture arrangement, in which Costain already held the remaining 73% interest, has a place on the Highways Agency framework to deliver new technology-led highways improvements.

The net book value of other acquired intangible assets comprises £3.6 million (2012: £0.8 million) relating to order book, £Nil (2012: £0.5 million) relating to brand value and £0.1 million (2012: £Nil) relating to manpower.

Goodwill has been allocated to the applicable cash generating units identified within the Infrastructure (£5.5 million) and Natural Resources (£16.8 million) reporting segments.

As described in Note 2, the Group reviews the value of goodwill and in the absence of any identified impairment risks, tests are based on internal value in use calculations of the cash generating unit ('CGU'). The key assumptions for these calculations are: discount rates, growth rates and expected changes to revenue and direct costs during the period.

Discount rates have been estimated based on pre-tax rates that reflect current market assessments of the Group's weighted average cost of capital and the risks specific to the CGU. The rate used to discount the forecast cash flows for the CGU in Infrastructure was 10.5% and for the CGU in Natural Resources was 12.5%.

The Group prepares cash flow forecasts derived from the most recent financial forecasts for the following two years and extrapolates those cash flows based on the following internal assessments of the annual growth rates attributable to the CGUs:

Growth rates	Infrastructure %	Natural Resources %
Years 3-4	2.5	2.5
Year 5	1.5	2.5
Long-term average	1.5	1.5

As at 31 December 2013, based on these internal valuations, the recoverable value of goodwill exceeded the carrying amounts by a comfortable amount.

Notes to the financial statements
continued

12 Property, plant and equipment

Group	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 January 2012	0.9	23.2	24.1
Additions	–	0.8	0.8
Disposals	–	(1.7)	(1.7)
At 31 December 2012	0.9	22.3	23.2
At 1 January 2013	**0.9**	**22.3**	**23.2**
Additions	**–**	**1.3**	**1.3**
Disposals	**–**	**(1.3)**	**(1.3)**
Acquired through business combinations	**–**	**0.1**	**0.1**
At 31 December 2013	**0.9**	**22.4**	**23.3**
Depreciation			
At 1 January 2012	0.6	12.1	12.7
Provided in year	–	2.3	2.3
Disposals	–	(0.9)	(0.9)
At 31 December 2012	0.6	13.5	14.1
At 1 January 2013	**0.6**	**13.5**	**14.1**
Provided in year	**–**	**2.4**	**2.4**
Disposals	**–**	**(1.1)**	**(1.1)**
At 31 December 2013	**0.6**	**14.8**	**15.4**

Net book value			
At 31 December 2013	**0.3**	**7.6**	**7.9**
At 31 December 2012	0.3	8.8	9.1
At 1 January 2012	0.3	11.1	11.4

13 Investments and loans in subsidiaries, equity accounted joint ventures and associates

Group	Investments Joint ventures £m	Investments Associates £m	Loans Joint ventures £m	Loans Associates £m	Total £m
Cost or fair value					
At 1 January 2012	38.1	0.2	13.7	11.3	63.3
Currency realignment	(0.8)	–	(0.5)	–	(1.3)
Additions	–	–	3.2	2.2	5.4
Disposal	–	–	–	(9.9)	(9.9)
Transfer*	17.6	–	(16.4)	–	1.2
At 31 December 2012	54.9	0.2	–	3.6	58.7
At 1 January 2013	**54.9**	**0.2**	**–**	**3.6**	**58.7**
Currency realignment	**(0.3)**	**–**	**–**	**–**	**(0.3)**
Additions	**2.7**	**–**	**–**	**2.2**	**4.9**
Disposal	**–**	**(0.1)**	**–**	**(1.0)**	**(1.1)**
At 31 December 2013	**57.3**	**0.1**	**–**	**4.8**	**62.2**
Share of post-acquisition reserves					
At 1 January 2012	(16.7)	(3.7)			(20.4)
Currency realignment	0.2	(0.1)			0.1
Dividends	–	(0.6)			(0.6)
(Loss)/profit for the year	(2.3)	0.9			(1.4)
Cash flow hedges – change in fair value	–	(0.4)			(0.4)
Cash flow hedges – disposals	–	4.0			4.0
At 31 December 2012	(18.8)	0.1			(18.7)
At 1 January 2013	**(18.8)**	**0.1**			**(18.7)**
Currency realignment	**0.1**	**–**			**0.1**
Disposals	**–**	**0.1**			**0.1**
Dividends	**–**	**(1.3)**			**(1.3)**
(Loss)/profit for the year	**(11.5)**	**0.2**			**(11.3)**
Cash flow hedges – change in fair value	**–**	**(0.2)**			**(0.2)**
Cash flow hedges – disposals	**–**	**1.2**			**1.2**
At 31 December 2013	**(30.2)**	**0.1**			**(30.1)**
Reclassifications					
At 1 January 2012	–	4.9	–	(4.9)	–
Arising in the year	–	(3.6)	–	4.0	0.4
At 31 December 2012	–	1.3	–	(0.9)	0.4
At 1 January 2013	**–**	**1.3**	**–**	**(0.9)**	**0.4**
Arising in the year	**–**	**(1.3)**	**–**	**0.9**	**(0.4)**
At 31 December 2013	**–**	**–**	**–**	**–**	**–**

Net book value					
At 31 December 2013	**27.1**	**0.2**	**–**	**4.8**	**32.1**
At 31 December 2012	36.1	1.6	–	2.7	40.4
At 1 January 2012	21.4	1.4	13.7	6.4	42.9

* During 2012, the loan to Alcaidesa Holding SA, including outstanding interest, was converted into equity.

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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

	2013				2012			
	Alcaidesa Holding SA £m	**Other joint ventures £m**	**Associates £m**	**Total £m**	Alcaidesa Holding SA £m	Other joint ventures £m	Associates £m	Total £m
Revenue	**1.8**	**43.1**	**29.9**	**74.8**	1.9	52.9	31.3	86.1
(Loss)/profit before tax	**(11.9)**	**0.4**	**0.3**	**(11.2)**	(2.3)	–	1.3	(1.0)
Income tax	**–**	**–**	**(0.1)**	**(0.1)**	–	–	(0.4)	(0.4)
(Loss)/profit for the year	**(11.9)**	**0.4**	**0.2**	**(11.3)**	(2.3)	–	0.9	(1.4)
Non-current assets	**18.4**	**–**	**0.8**	**19.2**	20.0	–	0.9	20.9
Current assets	**19.6**	**18.3**	**41.2**	**79.1**	29.5	15.3	58.9	103.7
Current liabilities	**(2.6)**	**(17.8)**	**(15.9)**	**(36.3)**	(3.4)	(15.2)	(10.3)	(28.9)
Non-current liabilities	**(8.8)**	**–**	**(25.9)**	**(34.7)**	(10.1)	–	(47.9)	(58.0)
Investments in joint ventures and associates	**26.6**	**0.5**	**0.2**	**27.3**	36.0	0.1	1.6	37.7
Financial commitments	**–**	**–**	**–**	**–**	–	–	2.3	2.3
Capital commitments	**–**	**–**	**–**	**–**	–	–	2.2	2.2

During 2013, the Group has re-assessed the carrying value of the assets in its non-core Land Development activity in Spain, which is undertaken in a 50:50 joint venture with Santander Bank. As a consequence of continuing uncertainty regarding future market conditions in Spain, a non-cash impairment has been taken against the assets, the Group's share of which is £9.8 million, reducing Costain's total carrying value in the joint venture to £26.6 million.

Net interest payable by joint ventures and associates in 2013 was £1.0 million (2012: £1.7 million payable). The applicable interest rates are income of 0.2% to 6.5% per annum (2012: 0.2% to 6.1%) and expense of 1.7% to 11.5% per annum (2012: 5.4% to 11.5%).

The financial commitments related to associates involved in PFI schemes and the capital commitments to ongoing construction works. All figures are the Group's share.

Analysis of the total revenue, income, assets and liabilities of joint ventures and associates

	2013				2012			
	Alcaidesa Holding SA £m	**Other joint ventures £m**	**Associates £m**	**Total £m**	Alcaidesa Holding SA £m	Other joint ventures £m	Associates £m	Total £m
Revenue	**3.7**	**105.1**	**93.6**	**202.4**	3.7	126.3	99.1	229.1
(Loss)/profit before tax	**(23.7)**	**0.8**	**0.7**	**(22.2)**	(4.6)	0.1	5.7	1.2
Income tax	**–**	**–**	**(1.0)**	**(1.0)**	–	–	(1.8)	(1.8)
(Loss)/profit for the year	**(23.7)**	**0.8**	**(0.3)**	**(23.2)**	(4.6)	0.1	3.9	(0.6)
Non-current assets	**36.8**	**–**	**2.1**	**38.9**	38.7	–	2.3	41.0
Current assets	**39.3**	**43.1**	**103.1**	**185.5**	59.6	34.9	178.5	273.0
Current liabilities	**(5.3)**	**(41.9)**	**(39.6)**	**(86.8)**	(6.8)	(34.6)	(32.2)	(73.6)
Non-current liabilities	**(17.6)**	**–**	**(64.8)**	**(82.4)**	(20.2)	–	(142.7)	(162.9)
Equity	**53.2**	**1.2**	**0.8**	**55.2**	71.3	0.3	5.9	77.5

Details of the principal subsidiary undertakings, joint ventures, jointly controlled operations and associates are shown in Note 24.

13 Investments and loans in subsidiaries, equity accounted joint ventures and associates continued

Company	
Investments in subsidiaries	£m
Cost	
At 1 January 2012	394.1
Additions	2.9
Disposal	(32.6)
At 31 December 2012	364.4
At 1 January 2013	**364.4**
Additions	**2.7**
At 31 December 2013	**367.1**
Amounts written off	
At 1 January 2012	(272.7)
Provided	3.5
At 31 December 2012	(269.2)
At 1 January 2013	**(269.2)**
At 31 December 2013	**(269.2)**

Net book value	
At 31 December 2013	**97.9**
At 31 December 2012	95.2
At 1 January 2012	121.4

Additions relate to the increase in the cost of investments in subsidiaries by the equivalent amount of the equity settled share-based payment charge in relation to employees of subsidiaries included in the income statement.

Details of the principal subsidiaries in which the Company has an interest are set out in Note 24.

14 Trade and other receivables

	Group		Company	
	2013 £m	2012 £m	**2013 £m**	2012 £m
Amounts included in current assets				
Trade receivables	**87.4**	73.0	**–**	–
Other receivables	**5.3**	12.8	**–**	–
Amounts due from customers for contract work	**80.3**	79.0	**–**	–
Prepayments and accrued income	**15.2**	15.9	**1.0**	0.9
Amounts owed by joint ventures and associates	**2.4**	0.8	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**50.3**	39.0
	190.6	181.5	**51.3**	39.9
Amounts included in non-current assets				
Other	**22.0**	17.5	**–**	–

At 31 December 2013, amounts due from customers for contract work falling due within one year include retentions of £20.6 million (2012: £22.8 million) relating to long-term contracts in progress. Other receivables falling due after more than one year include retentions of £21.5 million (2012: £17.0 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.

14 Trade and other receivables continued

The average credit period within trade receivables on amounts billed for construction work and on sales of goods is 33 days (2012: 33 days). The analysis of the due dates of the trade receivables was £76.1 million (2012: £65.3 million) due within 30 days, £8.8 million (2012: £4.6 million) due between 30 and 60 days and £2.5 million (2012: £3.1 million) due after 60 days.

These balances include receivables, with a carrying amount of £5.0 million (2012: £6.8 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 £2.8 million (2012: £3.0 million) overdue by less than 30 days, £0.5 million (2012: £0.9 million) overdue by between 30 and 60 days and £1.7 million (2012: £2.9 million) overdue by more than 60 days.

The provision for impairment of trade and other receivables is £6.9 million (2012: £6.7 million).

The aggregate amount of costs incurred plus recognised profits, less recognised losses, for all contracts in progress at the statement of financial position date was £2,782.6 million (2012: £2,753.2 million). Progress billings and advances received from customers under open construction contracts amounted to £2,728.8 million (2012: £2,707.8 million). Advances for which work has not started, and billings in excess of costs incurred and recognised profits are included in credit balances on long-term contract (Note 18).

15 Cash and cash equivalents

Cash and cash equivalents are analysed below, and include the Group's share of cash held by jointly controlled operations of £25.6 million (2012: £29.6 million).

	Group		Company	
	2013 £m	2012 £m	**2013 £m**	2012 £m
Cash and cash equivalents	**84.3**	107.4	**–**	30.0
Bank overdrafts	**(1.6)**	(1.7)	**–**	–
Cash, cash equivalents and overdrafts in the cash flow statement	**82.7**	105.7	**–**	30.0

16 Interest bearing loans and borrowings

	Group		Company	
	2013 £m	2012 £m	**2013 £m**	2012 £m
Revolving Credit Facility	**25.0**	–	**25.0**	–

The Group's borrowings facilities are described in Note 17.

17 Financial instruments – Fair values and risk management

a) Risk management

The Group's centralised treasury function manages financial risk, principally arising from liquidity and funding risks and movements in foreign currency rates, interest rates and inflation rates, in accordance with policies agreed by the directors.

The Group does not enter into speculative transactions.

The Company does not have any forward foreign currency contracts or other derivatives.

i) Capital Management

The Group's objectives when managing capital are to safeguard its ability to continue as a going concern and to provide resources to grow the business, in order to provide returns for shareholders and other stakeholders. The current capital base of the Group is driven by equity capital from shareholders and retained earnings. The Board of directors ('Board') continues to explore options 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.

17 Financial instruments – Fair values and risk management continued

a) Risk management continued

ii) Liquidity and funding risk

Ultimate responsibility for liquidity and funding risk rests with the Board, which has put in place a monitoring and reporting framework to manage funding requirements.

Liquidity risk is managed by monitoring actual and forecast short and medium term cash flows and the maturity profile of financial assets and liabilities and by maintaining adequate cash reserves. The nature and timing of the contract cash flows causes the cash balances to vary over the month with the balance usually highest at the month end.

The average month end net cash balance during the year was £50.7 million (2012: £103.4 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 2013, the Group has banking and bonding facilities, including a £95 million Revolving Credit Facility, extending to 30 June 2017. The facilities were renegotiated and the term extended during the year. The facilities have financial covenants based on profit, interest cover and leverage measured quarterly.

Unsecured bonding facilities

	Group and Company	
	2013 £m	2012 £m
Expiring between two and five years*	**400.0**	420.0
* Element of above facilities available for borrowings	**2.5**	2.5

At 31 December 2013, the utilisation of these bonding facilities amounted to £157.1 million (2012: £144.4 million).

iii) Credit risk

The Group uses an external credit scoring system to assess a potential customer's credit quality and will enter into a contract only if that assessment is satisfactory. Deposits in the United Kingdom are placed with the bank facility providers or, in jointly controlled 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 counter-parties 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 counter-party 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 United Kingdom and Overseas and bank borrowings Overseas. The largest constituents are United Kingdom balances denominated in Pounds sterling. A 1% rise in interest rates would have increased the annual interest income on net cash balances by £0.5 million (2012: £1.0 million).

No interest rate hedging is currently undertaken by the Group.

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17 Financial instruments – Fair values and risk management continued

a) Risk management continued

v) Foreign currency risk

Transactional currency exposures arise from sales or purchases by operating companies in currencies other than their functional currency. The current strategy is to hedge both committed and forecast foreign currency exposures, where applicable, and where the transaction timing and amount can be determined reliably and no natural hedge exists. The Group only enters into forward contracts when a contractual commitment exists in respect of the foreign currency transaction and the Group's policy is to negotiate the terms of the hedge derivative to match the terms of the hedged item to maximise hedge effectiveness.

Investments in joint ventures includes the Group's investment in Alcaidesa Holding SA, a company based in Spain and denominated in Euro. At the year-end, the net carrying value of the equity investment was £26.6 million (2012: £36.0 million). A 10% strengthening in the Euro would have favourably impacted the statement of financial position favourably by £3.0 million (2012: £4.0 million). A 10% strengthening in the Euro would have adversely impacted the results by £1.3 million (2012: £0.3 million).

In addition, a 10% strengthening in the UAE Dirham would have adversely impacted the results by £0.2 million (2012: £0.4 million) and at 31 December 2013, the net monetary assets denominated in currencies other than the functional currency of the operation involved were Euro denominated net monetary assets of £0.1 million (2012: £Nil) in members of the Group with sterling as their functional currency.

b) Cash flow hedges

Foreign currency contracts are measured using quoted forward exchange rates and yield curves derived from quoted interest rates matching maturities of the contracts.

At 31 December 2013, the Group had foreign currency contracts (seven purchase contracts (2012: 22) and five sale contracts (2012: four)) designated as hedges of future transactions.

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. These amounts were recognised as fair value derivatives. The terms of the foreign currency contracts match the terms of the commitments. There were no ineffective hedges at the year-end (2012: Nil).

The foreign currency sale and purchase contracts outstanding at 31 December 2013 are summarised below. The carrying value represents the fair value of the contract; the contractual cash flows represent the sterling commitments.

Foreign exchange contracts

	2013				2012			
	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
Purchases	**–**	**(1.8)**	**(1.8)**	**–**	(0.3)	(7.6)	(7.6)	–
Sales	**(0.1)**	**1.4**	**–**	**1.4**	0.1	2.6	2.6	–
	(0.1)	**(0.4)**	**(1.8)**	**1.4**	(0.2)	(5.0)	(5.0)	–

The expected impact on the income statement of the foreign exchange contracts is a loss of £Nil in 2014.

c) Maturity of PFI swaps

Interest rate swaps are measured at the present value of the future cash flows estimated and discounted based on the applicable yield curves derived from quoted interest rates.

At 31 December 2013, the Group had no interest rate swaps outstanding. At 31 December 2012, PFI project companies, in which the Group had an interest and recorded as investments in associates, had entered into the following swaps to hedge the interest rate risk of bank loans. These swaps are classified as cash flow hedges and stated at fair value based on a Level 2 valuation method. The fair value will reverse over the life of the swaps. There were no ineffective hedges at the end of 2012.

17 Financial instruments – Fair values and risk management continued

c) Maturity of PFI swaps continued

	2013				2012			
	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
Interest rate swaps	–	–	–	–	1.3	0.1	0.4	0.8
Less tax	–	–	–	–	(0.3)	–	(0.1)	(0.2)
	–	–	–	–	1.0	0.1	0.3	0.6

These amounts (net of tax) were recognised as fair value derivatives within the value of the investment.

d) 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

	2013				2012			
	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	83.8	83.8	–	–	106.1	106.1	–	–
UAE Dirham	0.2	0.2	–	–	1.1	1.1	–	–
Other	0.3	0.3	–	–	0.2	0.2	–	–
	84.3	84.3	–	–	107.4	107.4	–	–
Loans to joint ventures and associates:								
Pounds sterling	4.8	0.2	0.9	3.7	2.7	0.1	0.5	2.1
	4.8	0.2	0.9	3.7	2.7	0.1	0.5	2.1
Trade, other receivables and amounts owed by joint ventures and associates:								
Pounds sterling	114.9	92.9	22.0	–	101.8	84.3	17.5	–
Other	2.2	2.2	–	–	2.3	2.3	–	–
	117.1	95.1	22.0	–	104.1	86.6	17.5	–
Total financial assets not measured at fair value	206.2	179.6	22.9	3.7	214.2	194.1	18.0	2.1

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 £4.8 million (2012: £2.7 million), but not by a material amount.

Financial assets measured at fair value

At 31 December 2013, the Group does not have any financial assets measured at fair value. At 31 December 2012, the Group had interest rate swaps (see (c) above), which were included within the valuation of investments in associates.

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17 Financial instruments – Fair values and risk management continued

d) Financial assets and liabilities continued

ii) Currency and maturity of financial liabilities

Financial liabilities not measured at fair value

	2013			2012		
	Total £m	Within one year £m	Between one and five years £m	Total £m	Within one year £m	Between one and five years £m
Bank overdrafts – UAE Dirham	**1.6**	**1.6**	**–**	1.7	1.7	–
Revolving Credit Facility – Pounds sterling	**25.0**	**25.0**	**–**	–	–	–
Trade and other payables:						
Pounds sterling	**112.1**	**111.0**	**1.1**	139.0	135.3	3.7
UAE Dirham	**0.4**	**0.4**	**–**	5.2	5.2	–
	112.5	**111.4**	**1.1**	144.2	140.5	3.7
Total financial liabilities not measured at fair value	**139.1**	**138.0**	**1.1**	145.9	142.2	3.7

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. Valuing the Revolving Credit Facility under a Level 2 valuation method gives the same value as the carrying value.

Financial liabilities measured at fair value

	2013			2012		
	Total £m	Within one year £m	Between one and five years £m	Total £m	Within one year £m	Between one and five years £m
Deferred consideration – Pounds sterling	**6.9**	**3.7**	**3.2**	3.8	2.5	1.3
Total financial liabilities measured at fair value	**6.9**	**3.7**	**3.2**	3.8	2.5	1.3

The deferred consideration is valued at a Level 3 valuation method. The fair value is the same as the carrying value. See (e) 'Measurement of fair value' below.

iii) Reconciliation of trade and other receivables and trade and other payables to the statement of financial position

	2013		2012	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other receivables (as above)	**95.1**	**22.0**	86.6	17.5
Amounts due from customers	**80.3**	**–**	79.0	–
Prepayments and accrued income	**15.2**	**–**	15.9	–
	190.6	**22.0**	181.5	17.5

	2013		2012	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other payables (as above)	**111.4**	**1.1**	140.5	3.7
Deferred consideration (as above)	**3.7**	**3.2**	2.5	1.3
Credit balances on long-term contracts	**6.0**	**–**	7.6	–
Accruals and deferred income	**145.0**	**–**	147.0	–
	266.1	**4.3**	297.6	5.0

17 Financial instruments – Fair values and risk management continued

d) Financial assets and liabilities continued

iv) Effective interest rates of financial assets and liabilities

	2013	2012
Financial assets		
Cash and cash equivalents	**0.0% to 0.5%**	0.0% to 1.2%
Loans to joint ventures and associates	**10.0% to 11.5%**	10.0% to 11.5%

Financial liabilities

The Group has overdraft facilities and a Revolving Credit Facility. These are unsecured and carry interest at floating rates, at a margin over LIBOR, or in the case of the overdraft in Abu Dhabi at a margin over EIBOR.

The Company's financial assets comprised cash at bank of £Nil (2012: £30.0 million) and trade and other receivables of £50.3 million (2012: £39.0 million) denominated in Pounds sterling and maturing within one year.

The Company's financial liabilities comprised the Revolving Credit Facility of £25.0 million (2012: £Nil) and trade and other payables of £49.3 million (2012: £84.0 million) denominated in Pounds sterling and maturing within one year.

e) Measurement of fair value

i) 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.

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 expected payment based on 2013 EBITDA and forecast EBITDA for the next two years, discounted using a risk-adjusted discount rate.	Forecast annual revenue growth rate (2013: 25 – 35%) Forecast EBITDA margin (2013: 15 – 20%) Risk-adjusted discount rates (12.7 – 12.9%)	The estimated fair value would increase (decrease) if: the annual revenue growth rate were higher (lower); the EBITDA margin were higher (lower); or the risk-adjusted discount rate were lower (higher). Generally, a change in the annual revenue growth rate is accompanied by a directionally similar change in EBITDA.
Cash flow hedges and interest rate (PFI) swaps	Market comparison technique: The fair values are based on broker quotes. Similar contracts are traded in an active market and quotes reflect the actual transactions in similar instruments.	Not applicable.	Not applicable.

17 Financial instruments – Fair values and risk management continued

e) Measurement of fair value continued

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.

ii) Transfers between level 1 and 2

There are no financial instruments whose value could be determined under Level 1, hence no transfers between level 1 and Level 2.

iii) Level 3 fair values

The following table shows a reconciliation from the opening to closing balances for Level 3 fair values:

	Deferred consideration £m
At 1 January 2013	**3.8**
Assumed within a business combination	**3.2**
Addition charged to income statement	**2.8**
Payments	**(2.9)**
At 31 December 2013	**6.9**

iv) Transfers out of Level 3

There were no transfers out of Level 3 other than the payments made during 2013.

v) Sensitivity analysis

For the fair value of non-current deferred consideration, reasonably possible changes at the reporting date to one of the significant unobservable inputs, holding other inputs constant, would have effects to profit and loss as set out in the table below. The fair value of current deferred consideration will not change.

Non-current deferred consideration

	Profit/(loss)	
	Increase £m	Decrease £m
31 December 2013		
Annual revenue growth rate (0.5% movement)	(0.1)	0.1
EBITDA margin (0.5% movement)	(0.1)	0.1
Risk-adjusted discount rate (2.0% movement)	0.1	(0.1)

18 Trade and other payables

	Group		Company	
	2013 £m	2012 £m	**2013 £m**	2012 £m
Current liabilities				
Trade payables	**90.5**	105.1	**–**	–
Other payables	**10.9**	21.5	**–**	–
Social security	**5.3**	5.5	**–**	–
Credit balances on long-term contracts	**6.0**	7.6	**–**	–
Accruals and deferred income	**145.0**	148.3	**–**	–
Deferred consideration	**3.7**	1.2	**–**	–
Amounts owed to joint ventures and associates	**4.7**	8.4	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**49.3**	84.0
	266.1	297.6	**49.3**	84.0
Non-current liabilities				
Other payables	**1.1**	3.7	**–**	–
Deferred consideration	**3.2**	1.3	**–**	–
	4.3	5.0	**–**	–

At 31 December 2013, credit balances on long-term contracts included no advance payments from customers (2012: £Nil).

Accruals and deferred income include subcontract liabilities (not yet payable), subcontract retentions and other accruals and deferred income.

The directors consider that the carrying amount of trade payables, other payables, social security and amounts owed to joint ventures and associates approximates to their fair value.

Financial risk management policies are in place that seek to ensure that all payables are paid within their credit timeframes.

19 Provisions for other liabilities and charges

Group	Property £m	Other £m	Total £m
Current			
At 1 January 2012	1.0	1.1	2.1
Provided	0.7	0.5	1.2
Utilised	(0.4)	–	(0.4)
Released	(0.3)	(0.5)	(0.8)
At 31 December 2012	1.0	1.1	2.1
At 1 January 2013	**1.0**	**1.1**	**2.1**
Provided	**0.1**	**0.4**	**0.5**
Utilised	**(0.4)**	**–**	**(0.4)**
Released	**(0.1)**	**(0.3)**	**(0.4)**
At 31 December 2013	**0.6**	**1.2**	**1.8**

Notes to the financial statements

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19 Provisions for other liabilities and charges continued

	Property £m	Other £m	Total £m
Non-current			
At 1 January 2012	0.2	2.1	2.3
Provided	–	0.3	0.3
Transfer	(0.1)	(0.6)	(0.7)
At 31 December 2012	0.1	1.8	1.9
At 1 January 2013	**0.1**	**1.8**	**1.9**
Provided	**–**	**0.3**	**0.3**
Utilised	**(0.1)**	**(1.7)**	**(1.8)**
At 31 December 2013	**–**	**0.4**	**0.4**

Company	Funding obligations £m	Other £m	Total £m
Current			
At 1 January 2012	0.2	0.3	0.5
Utilised	–	(0.3)	(0.3)
At 31 December 2012	0.2	–	0.2
At 1 January 2013	**0.2**	**–**	**0.2**
Utilised	**(0.1)**	**–**	**(0.1)**
At 31 December 2013	**0.1**	**–**	**0.1**
Non-current			
At 1 January 2012	1.3	–	1.3
At 31 December 2012	1.3	–	1.3
At 1 January 2013	**1.3**	**–**	**1.3**
At 31 December 2013	**1.3**	**–**	**1.3**

Group

Property provisions relate to costs of vacant properties and will be utilised over the next three years.

Other provisions, mainly comprise a provision for staff benefits payable to the staff of an Overseas subsidiary company, which will be utilised over the next two years and insurance claims, 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.

20 Employee benefits

(a) Pensions

A defined benefit pension scheme is operated in the United Kingdom and a number of defined contribution pension schemes are in place in the United Kingdom and Overseas. Contributions are paid by subsidiary undertakings and employees. The total pension charge in the income statement was £9.2 million comprising £7.1 million included in operating costs plus £2.1 million included in net finance expense (2012: £10.6 million, comprising £8.7 million in operating costs plus £1.9 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 is being carried out as at 31 March 2013 and this was updated to 31 December 2013 by a qualified independent actuary.

	2013 £m	2012 £m	2011 £m
Present value of defined benefit obligations	**(629.7)**	(610.7)	(600.8)
Fair value of scheme assets	**592.5**	558.8	547.9
Recognised liability for defined benefit obligations	**(37.2)**	(51.9)	(52.9)

Movements in present value of defined benefit obligations

	2013 £m	2012 £m
At 1 January	**610.7**	600.8
Interest cost	**26.2**	27.4
Amendments (Pension Increase Exchange 'PIE')	**–**	(1.7)
Plan Settlements (Enhanced Transfer Value 'ETV')	**–**	(29.3)
Remeasurements	**21.6**	40.7
Benefits paid	**(28.8)**	(27.2)
At 31 December	**629.7**	610.7

Movements in fair value of scheme assets

	2013 £m	2012 (restated) £m
At 1 January	**558.8**	547.9
Interest income	**24.1**	25.5
Remeasurements	**30.2**	17.6
Contributions by employer	**8.2**	27.8
Plan Settlements (ETV)	**–**	(32.8)
Benefits paid	**(28.8)**	(27.2)
At 31 December	**592.5**	558.8

Contributions by the employer in 2012 included the transfer of two PFI investments, Integrated Bradford Holdco Two Limited and Lewisham Schools for the Future Holdings 2 Limited, at an agreed of £20.3 million (Note 4).

Notes to the financial statements

continued

20 Employee benefits continued

(a) Pensions continued

Expense recognised in the income statement

	2013 £m	2012 (restated) £m
Pension liability management (ETV and PIE, including costs of £0.9 million)	–	(2.8)
Administrative expenses	(1.1)	(0.6)
Interest cost on the net liabilities of the defined benefit pension scheme	(2.1)	(1.9)
	(3.2)	(5.3)

History of the scheme for the last five years

	2013	2012	2011	2010	2009
Experience adjustments on scheme liabilities (£m)	(8.9)	–	–	18.5	–
	1%	–	–	3%	–
Change in assumptions on scheme liabilities (£m)	(12.7)	(40.7)	(40.7)	(27.0)	(113.7)
	2%	7%	3%	5%	20%
Experience adjustments on scheme assets (£m)	30.2	17.6	16.2	33.1	46.3
	5%	3%	1%	6%	10%
Total gain/(loss) (£m)	8.6	(23.1)	(24.5)	24.6	(67.4)

The cumulative amount of actuarial gains and losses recognised in other comprehensive income and expense since 1 January 2004, the transition date to IFRS, is a loss of £74.7 million (2012: £83.3 million). Figures for 2012 have been restated in accordance with IAS 19 (revised) for comparison with 2013.

Fair value of scheme assets and the return on scheme assets

	2013 £m	2012 £m
Equities	175.6	184.2
Multi-credit (2012: High yield bonds)	65.7	46.2
Government bonds	212.4	195.8
Infrastructure and property	64.8	63.8
Absolute return funds and cash	74.0	68.8
	592.5	558.8

The infrastructure holding is the portfolio of eight PFI investments transferred by the Group to The Costain Pension Scheme in 2010 and 2012.

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)

	2013 %	2012 %	2011 %
Discount rate	4.60	4.40	4.80
Future pension increases	3.20	2.85	2.90
Inflation assumption	3.30	2.95	3.00

20 Employee benefits continued

(a) Pensions continued

Weighted average life expectancy from age 65 as per mortality tables used to determine benefits at 31 December 2013 and 31 December 2012 is:

	2013		2012	
	Male (years)	**Female (years)**	Male (years)	Female (years)
Currently aged 65	**22.0**	**24.5**	21.7	23.8
Non-retirees	**23.8**	**26.4**	24.5	25.6

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	23.7	1.0
Decrease inflation, pension increases by 0.25%, decreases pension liability and reduces pension cost by	20.6	0.9
Increase life expectancy by one year, increases pension liability and increases pension cost by	17.6	0.8

Subject to finalisation of the acturial valuation as at 31 March 2013, the Group expects to make contributions of up to £6.0 million, plus an element of dividend matching and the expenses of administration to its deferred benefit scheme in the next financial year.

Defined contribution schemes

Several defined contribution pensions are operated. The total expense relating to these plans was £6.0 million (2012: £5.3 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 2012 AGM that allows for conditional awards with a maximum face value of up to 100% of base salary with a performance condition based on earnings per share.

Deferred Share Bonus Plan ('DSBP')

Executive directors and other senior management are eligible to participate in the Company's Deferred Share Bonus Plan which promotes greater alignment with shareholders through an award of deferred shares. The DSBP allows for conditional awards with a face value of up to 50% of base salary with a performance condition based on EBIT (Earnings before interest and tax). The deferred bonus award 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. Consequently, the DSBP 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.

Save As You Earn Plans ('SAYE')

The Company operates a number of SAYE plans that are open to all employees who pay a fixed amount from salary into a savings account each month and may elect to save over [three or five] years. At the end of the savings period, employees have six months in which to exercise their options (after which the options expire) using the funds saved. If employees decide not to exercise their options, they may withdraw the funds saved. Exercise of options is subject to continued employment within the Group (except where permitted by the rules of the scheme).

Share-based payment expense

The amounts recognised in the income statement, before income tax, for share-based payment transactions with employees was £2.7 million (2012: £2.9 million); the entire charge relates to subsidiaries.

20 Employee benefits continued

(b) Share-based payments continued

Options outstanding at the end of the year

The outstanding LTIPs (exercise price £1 per individual grant) 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. Outstanding awards granted prior to 2010 have been restated for the 1 to 10 share consolidation in 2010.

	LTIP	DSBP	SAYE	
	Number (m)	Number (m)	Number (m)	Weighted average exercise price (p)
Outstanding at 1 January 2012	2.0	1.4	1.9	199.0
Adjusted during the year	–	0.2	–	–
Forfeited during the year	–	–	(0.4)	231.4
Exercised during the year	(0.6)	–	–	–
Granted during the year	0.8	0.6	–	–
Outstanding at 31 December 2012	2.2	2.2	1.5	199.0
Adjusted during the year	**–**	**(0.2)**	**–**	**–**
Forfeited during the year	**–**	**–**	**(0.1)**	**186.7**
Exercised during the year	**(0.6)**	**(0.9)**	**(0.6)**	**195.8**
Granted during the year	**0.7**	**0.3**	**1.2**	**222.0**
Outstanding at 31 December 2013	**2.3**	**1.4**	**2.0**	**207.6**
Exercisable at the end of the period	**0.7**	**0.7**	**–**	**–**

Share options outstanding at the end of the year had a weighted average remaining contractual life of 5.8 years (2012: 6.4 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 £2.8 million (2012: £2.7 million). The assumptions used in valuing the grants were:

	2013	2012
Expected volatility	**20%**	20%
Expected life (years)	**2.7 – 5.0**	2.7 – 5.0
Risk-free interest rate	**3.5%**	2.1%
Expected dividend yield	**4%**	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.

21 Share capital

	2013		2012	
	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	**65.5**	**32.8**	64.7	32.4
Issued in year (see below)	**1.3**	**0.6**	0.8	0.4
Shares in issue at end of year – Ordinary shares of 50p each, fully paid	**66.8**	**33.4**	65.5	32.8

The Company's issued share capital comprised 66,792,941 ordinary shares of 50 pence each.

On 3 April 2013, the Company issued 605,533 shares in respect of the exercise of options granted under the 2010 LTIP.

The Company announced on 24 May 2013 that shareholders had, pursuant to the Scrip Dividend Scheme, elected to receive 93,558 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 2012, and shareholders elected to receive a further 67,150 ordinary shares on 25 October 2013 in lieu of cash in respect of all or part of their interim dividend for the year ended 31 December 2013.

During the year, the Company issued 482,394 shares on exercise of options granted under the 2008 5-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 20. Details of the performance conditions and the options granted to executive directors are given in the Directors' remuneration report.

22 Contingent liabilities

	Group		Company	
	2013 £m	**2012 £m**	2013 £m	2012 £m
Under guarantees of bank overdrafts to subsidiary companies	**–**	**–**	1.6	1.7

Group
There are contingent liabilities in respect of:

- creditors of jointly controlled operations, which are less than the book value of their assets;
- performance bonds and other undertakings entered into in the ordinary course of business; and
- legal claims arising in the ordinary course of business.

It is not anticipated that any material liabilities will arise from the contingent liabilities other than those provided for (Note 19).

Company
The Company has guaranteed the obligations of the subsidiary companies that are participating employers of The Costain Pension Scheme, the defined benefit pension scheme in the United Kingdom. At 31 December 2013, the potential liability was £37.2 million (2012: £51.9 million) on an IAS 19 basis and is included in these financial statements as disclosed in Note 20.

Notes to the financial statements

continued

23 Other financial commitments

Group

Operating lease commitments

Leases as lessee	2013 Land and buildings £m	2013 Other operating leases £m	2012 Land and buildings £m	2012 Other operating leases £m
Future aggregate minimum lease payments under non-cancellable leases:				
Within one year	**3.5**	**3.4**	4.3	3.6
Between one and five years	**8.9**	**3.4**	7.1	3.4
Later than five years	**7.0**	**–**	7.5	–
	19.4	**6.8**	18.9	7.0

Leases as lessor	Land and buildings 2013 £m	Land and buildings 201 £m
Future aggregate minimum lease income under non-cancellable leases:		
Within one year	**0.3**	0.6
Between one and five years	**0.3**	0.5
	0.6	1.1

The Group has various offices under non-cancellable operating lease agreements. The leases have various terms, escalation clauses and renewal rights. The Group also leases vehicles under non-cancellable operating leases. None of the leases include contingent rents.

Company

The Company does not have any other financial commitments (2012: £Nil).

24 Principal subsidiary undertakings, jointly controlled entities, associates and jointly controlled operations

	Activity	Percentage of equity held	Country of incorporation
Subsidiary undertakings			
ClerkMaxwell Ltd	Engineering and Design Services	100	UK
Costain Ltd	Engineering, Construction and Maintenance	100	UK
Costain Abu Dhabi Co WLL	Process Engineering	49	UAE
Costain Building & Civil Engineering Ltd	Engineering and Construction	100	UK
Costain Engineering & Construction Ltd	Holding and Service Company	100	UK
Costain Oil, Gas & Process Ltd	Process Engineering	100	UK
EPC Offshore Ltd	Project Management Services	100	UK
Promanex (Civils & Industrial Services) Ltd	Support Services	100	UK
Promanex (Construction & Maintenance Services) Ltd	Support Services	100	UK
Promanex (Total FM & Environmental Services) Ltd	Support Services	100	UK
Richard Costain Ltd	Service Company	100	UK

24 Principal subsidiary undertakings, jointly controlled entities, associates and jointly controlled operations continued

	Activity	Issued share capital £m	Percentage of equity held	Country of incorporation	Reporting date
Jointly controlled entities					
Alcaidesa Holding SA	Land Development	11.3	50	Spain	31 December
Brighton & Hove 4Delivery Ltd	Civil Engineering	–	49	UK	31 March
4Delivery Ltd	Civil Engineering	–	40	UK	31 March
Associates					
Integrated Bradford LEP Ltd	Construction and Operation of Schools	–	40	UK	31 December
Lewisham Schools for the Future LEP Ltd	Construction and Operation of Schools	0.1	40	UK	31 March
Lewisham Schools for the Future SPV 3 Ltd	Construction and Operation of Schools	–	40	UK	31 March
Lewisham Schools for the Future SPV 4 Ltd	Construction and Operation of Schools	–	40	UK	31 March

The equity capital of the above are held by subsidiary undertakings with the exception of Richard Costain Limited and Costain Engineering & Construction Ltd.

Costain Abu Dhabi Co WLL has been treated as a subsidiary undertaking due to Costain having power to influence and control the composition of the board of directors and the beneficial right to all the net income.

All undertakings operate mainly in the country of incorporation.

All holdings are of ordinary shares except Richard Costain Ltd, where Costain Group PLC holds 100% of the ordinary and preference shares.

A full list of Group companies will be included in the Company's annual return.

	Activity	Percentage of equity held	Country of incorporation
Major jointly controlled operations			
A-one+ Integrated Highway Services – MAC 7	Engineering & Maintenance	33	UK
A-one+ Integrated Highway Services – MAC 12	Engineering & Maintenance	33	UK
A-one+ Integrated Highway Services – MAC 14	Engineering & Maintenance	33	UK
ATC Joint Venture C610 – Crossrail	Engineering	33	UK
Costain-Carillion Joint Venture – M1 Widening and A5/M1 Link	Civil Engineering	50	UK
Costain-Hochtief Joint Venture – Reading station	Civil Engineering	50	UK
Costain-Laing O'Rourke Joint Venture – Bond Street station	Civil Engineering	50	UK
Costain-Laing O'Rourke Joint Venture – Farringdon station	Civil Engineering	50	UK
Costain-Skanska C405 Joint Venture – Paddington – Crossrail	Civil Engineering	50	UK
Costain-Skanska C411 Joint Venture – Bond Street – Crossrail	Civil Engineering	50	UK
Costain-Skanska C412 Joint Venture – Bond Street – Crossrail	Civil Engineering	50	UK
Educo UK Joint Venture – Bradford Schools	Construction	50	UK
Galliford-Costain-Atkins Joint Venture – United Utilities	Civil Engineering	42	UK
Lagan-Ferrovial-Costain-A8	Civil Engineering	45	UK
The e5 Joint Venture Severn Trent Framework	Civil Engineering	25	UK

Notes to the financial statements

continued

25 Acquisitions

On 1 August 2013, the Group purchased the share capital of EPC Offshore Limited ('EPC'). The business, which is based in the United Kingdom, provides project management services to the upstream oil and gas sector.

The initial consideration was £10.6 million. Further payments, based on an 8 times multiple of EBITDA, may also be payable after the completion of the results for the years to December 2014, 2015 and 2016. The percentage payable in respect of the results for the year increases each year.

The total estimated value of these future payments is £8.9 million. Part of the payment estimated at £3.2 million is based only on the financial performance in years 2014 and 2015. This has been included in the cost of acquisition (see below) and accounted as a financial liability based on a Level 3 valuation method. The balance of the payments, estimated at £5.7 million, is dependent on continued future service and, in accordance with IFRS 3, will be expensed to the income statement. The payments are dependent on the future performance and financial results and the £3.2 million provided as part of the cost of acquisition could range between £2.0 million and £4.0 million.

The Group believes the acquisition will broaden its capabilities in the upstream oil and gas market.

The contributions to revenue and operating profit before amortisation of acquired intangibles and employment related consideration within the Group's results of this acquisition was revenue £4.5 million, operating profit £0.4 million, including integration costs.

The proforma figures as required by IFRS 3, assuming that the acquisition had been part of the Group throughout the year, were revenue £11.5 million and operating profit before amortisation of acquired intangibles of £1.5 million.

The acquisition had the following effect on the Group's assets and liabilities:

	Total £m
Cash	10.6
Contingent consideration	3.2
Consideration	**13.8**
Acquired intangible assets – Customer relationships	4.5
Acquired intangible assets – Other	1.4
Property, plant and equipment	0.1
Cash	1.2
Other current assets	2.4
Other current liabilities	(1.6)
Deferred tax	(1.3)
Fair value of assets acquired and liabilities recognised	**6.7**
Goodwill arising on acquisitions	**7.1**

Based on the provisional assessment of the recognised values of assets and liabilities, the goodwill arising on the acquisition is expected to be £7.1 million.

Costs of £0.6 million were incurred by the Group in relation to the acquisition and have been expensed in administrative expenses within the income statement.

There were no acquisitions in 2012.

26 Related party transactions

Group

A related party relationship exists with its major shareholders, subsidiaries, joint ventures and associates, jointly controlled operations, The Costain Pension Scheme and with its directors and executive officers.

Sales of goods and services

	2013			2012		
	Joint ventures and associates £m	**Jointly controlled operations £m**	**Total £m**	Joint ventures and associates £m	Jointly controlled operations £m	Total £m
Services of Group employees	**13.8**	**70.6**	**84.4**	20.6	61.9	82.5
Construction services and materials	**11.7**	**16.6**	**28.3**	41.0	3.2	44.2
	25.5	**87.2**	**112.7**	61.6	65.1	126.7

There were no sales of goods and services to major shareholders during the year (2012: £Nil).

An amount due from a major shareholder has been fully provided against since 2006. It relates to work carried out under a subcontract. Discussions among all the parties continue but recovery is uncertain.

Balances with joint ventures and associates are disclosed in Notes 14 and 18. Balances with jointly controlled operations are eliminated on consolidation.

Major shareholders

Mohammed Abdulmohsin Al-Kharafi & Sons Co W.L.L. and York Place Limited are regarded as related parties of the Company.

The Costain Pension Scheme

Details of transactions between the Group and The Costain Pension Scheme are included in Note 20 and, in respect of the transfer of two PFI investments in 2012, also Note 4.

Transactions with key management personnel

The directors of the Company and their immediate relatives control 488,468 ordinary shares in Costain Group PLC, which expressed as a percentage of the issued share capital is 0.73% (2012: 0.58%) of the voting shares of the Company.

In addition to their salaries, in respect of the Executive Directors and executive officers, the Group provides non-cash benefits and contributes to defined contribution pension plans. Executive Directors and executive officers also participate in the Group's LTIP, DSBP and SAYE plans, which are detailed in Note 20.

The compensation of key management personnel, including the directors, is as follows:

	Group	
	2013 £m	2012 £m
Directors' emoluments	**1.6**	1.4
Executive officers' emoluments	**2.0**	2.1
Post-employment benefits	**0.3**	0.3
Termination benefits	**–**	0.2
Share-based payments	**1.1**	1.1
	5.0	5.1

The above amounts are included in employee benefit expense (Note 5).

Company

The Company has no transactions with related parties other than the charge in relation to share-based payments (Note 20) (2012: none).

Financial statements

Five-year financial summary

	2013 £m	2012 (restated) £m	2011 £m	2010 £m	2009 £m
Revenue and profit					
Revenue (Group and share of joint ventures and associates)	**960.0**	934.5	986.3	1,022.5	1,061.1
Less: Share of joint ventures and associates	**(74.8)**	(86.1)	(117.8)	(98.0)	(67.7)
Group revenue	**885.2**	848.4	868.5	924.5	993.4
Group operating profit before other items	**27.4**	21.7	24.1	17.4	22.0
Other items:					
Exceptional transaction costs	**(3.7)**	–	–	–	–
Amortisation of acquired intangible assets	**(1.8)**	(1.7)	(0.9)	–	–
Employment related deferred consideration	**(2.8)**	(1.7)	(0.7)	–	–
Group operating profit	**19.1**	18.3	22.5	17.4	22.0
Profit on sales of investments	**–**	–	0.5	–	–
Profit on sales of interests in joint ventures and associates	**9.1**	10.5	0.3	11.2	2.0
Profit on sale of land and property	**–**	–	–	1.3	–
Share of results of joint ventures and associates	**(11.3)**	(1.4)	(1.3)	(0.5)	(3.2)
Profit from operations	**16.9**	27.4	22.0	29.4	20.8
Finance income	**0.7**	1.0	34.1	30.7	26.0
Finance expense	**(4.7)**	(3.7)	(32.2)	(32.2)	(28.7)
Net finance (expense)/income	**(4.0)**	(2.7)	1.9	(1.5)	(2.7)
Profit before tax	**12.9**	24.7	23.9	27.9	18.1
Income tax	**(0.4)**	(1.6)	(5.2)	(4.8)	(3.5)
Profit for the year attributable to equity holders of the parent	**12.5**	23.1	18.7	23.1	14.6
Earnings per share – basic*	**18.8p**	35.4p	29.2p	36.4p	23.0p
Earnings per share – diluted*	**18.1p**	34.2p	28.2p	35.4p	22.6p
Dividends per ordinary share					
Final*	**7.75p**	7.25p	6.75p	6.25p	5.5p
Interim*	**3.75p**	3.50p	3.25p	3.0p	2.75p
Summarised consolidated statement of financial position					
Intangible assets	**33.0**	18.7	20.3	0.1	1.0
Property, plant and equipment	**7.9**	9.1	11.4	9.7	11.5
Investments in equity accounted joint ventures and associates	**32.1**	40.4	42.9	37.4	44.1
Other non-current assets	**31.8**	34.9	33.8	39.8	47.3
Total non-current assets	**104.8**	103.1	108.4	87.0	103.9
Current assets	**276.5**	290.6	332.0	309.3	325.1
Total assets	**381.3**	393.7	440.4	396.3	429.0
Current liabilities	**296.1**	303.1	348.3	311.4	320.5
Retirement benefit obligations	**37.2**	51.9	52.9	39.6	104.7
Other non-current liabilities	**4.7**	6.9	8.4	7.7	7.6
Total liabilities	**338.0**	361.9	409.6	358.7	432.8
Equity attributable to equity holders of the parent	**43.3**	31.8	30.8	37.6	(3.8)

The figures for 2012 are restated for IAS 19 (revised).

* The figures for 2009 have been restated for the 1 for 10 share consolidation in 2010.

Other information

Financial calendar and other shareholder information

Financial calendar[1]

Full-year results	27 February 2014
Ex-dividend date for final dividend	12 March 2014
Final dividend record date	14 March 2014
Annual Report mailing	21 March 2014
Final dividend payment date[2]	25 April 2014
Interim Management Statement	7 May 2014
Annual General Meeting	7 May 2014
Half-year end	30 June 2014
Half-year results 2014	21 August 2014
Ex-dividend date for interim dividend	17 September 2014
Interim dividend record date	19 September 2014
Interim dividend payment date	24 October 2014
Interim Management Statement	06 November 2014
Financial year-end	31 December 2014

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 a general meeting to be held on 17 March 2014.

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 2 April 2014. Copies of the mandate form and the scrip dividend brochure can be downloaded from the Company's website at **www.costain.com** or obtained from Equiniti by telephoning 0871 384 2268* or +44 121 415 7173 if calling from outside the United Kingdom.

Analysis of shareholders

as at 26 February 2014

	Accounts	Shares	%
Institutions, companies, individuals and nominees:			
Shareholdings 100,000 and more	62	55,603,155	83.22
Shareholdings 50,000-99,999	34	2,445,356	3.66
Shareholdings 25,000-49,999	53	1,900,683	2.84
Shareholdings 5,000-24,999	321	3,251,402	4.87
Shareholdings 1-4,999	10,671	3,612,272	5.41
Totals	11,141	66,812,868	100.00

Secretary

Tracey Wood

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Registrar

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Shareholder information

For enquiries regarding your shareholding, please contact the Registrar, Equiniti (details above). You can also view up-to-date information about your holdings by visiting the shareholder website at **www.shareview.co.uk** (see page 135 for further details). Please ensure that you advise Equiniti promptly of a change of name or address.

* Calls to 0871 numbers cost 8p per minute plus network extras. Lines are open Monday to Friday 8.30am to 5.30pm, excluding UK bank holidays.

Dividend mandate

Shareholders can arrange to have their dividends paid directly into their bank or building society account, by completing a bank mandate form. The advantages to using this service are:

- the payment is more secure as you can avoid the risk of cheques getting lost in the post;
- it avoids the hassle of paying in a cheque; and
- there is no risk of lost, stolen or out-of-date cheques.

A mandate form can be obtained from the Company's website, or by contacting Equiniti on 0871 384 2250* (+44 121 415 7047 if calling from outside the United Kingdom) who will be pleased to assist you and can also be obtained via the shareholder website at **www.shareview.co.uk** (see below for further details). Alternatively, you will find one attached to the tax voucher of your last dividend payment. Overseas shareholders can arrange for their dividends to be paid in their local currency and more information can be obtained from **www.shareview.com/overseas**

Shareview service

The Shareview service from our Registrar, Equiniti, gives shareholders:

- direct access to data held on their behalf on the share register including recent share movements and dividend details; and
- the ability to change their address or dividend payment instructions online.

To sign up for Shareview you need the 'shareholder reference' printed on your proxy form or dividend stationery. There is no charge to register.

When you register with the site, you can register your preferred format (post or email) for shareholder communications. If you select email as your mailing preference, you will be notified of various shareholder communications, such as annual results, by email instead of post.

If you have your dividends paid straight to your bank account, and you have selected email as your mailing preference, you can also collect your tax voucher electronically. Instead of receiving the paper tax voucher, you will be notified by email with details of how to download your electronic version. Visit the website at **www.shareview.co.uk** for more details. Details of software and equipment requirements are given on the website.

Unsolicited mail

The Company is legally obliged to make its share register available to the general public. Consequently, some shareholders may receive unsolicited mail, including correspondence from unauthorised investment firms. Shareholders who wish to limit the amount of unsolicited mail they receive can contact:

The Mailing Preference Service
Freepost 29
LON20771
London W1E OZT

Further guidance on this issue can also be found on the Company's website at **www.costain.com**

ShareGift

The Orr Macintosh Foundation (ShareGift) operates a charity share donation scheme for shareholders with small parcels of shares whose value makes it uneconomic to sell them. Details of the scheme are available on the ShareGift website at **www.sharegift.org**. Equiniti can provide stock transfer forms on request. Donating shares to charity in this way gives rise neither to a gain nor a loss for Capital Gains Tax purposes. This service is completely free of charge.

Additional shareholder information including detailed share price, Directors' holdings, dividends, share price chart, significant shareholders together with regulatory news, our investment case and AGM details can be found on our website: **www.costain.com/investors/investor-home**

Contact us

For shareholder information, please contact:

Tracey Wood
Legal Director and Company Secretary
info@costain.com

For corporate responsibility, please contact:

Catherine Warbrick
Corporate Responsibility Director
info@costain.com

For corporate communications, please contact:

Graham Read
Communications Director
info@costain.com

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. A feedback response box has been provided on the Annual Report microsite to enable you to comment.

Useful links

www.costain.com
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www.costain.com/responsibility
www.costain.com/annual-report-2013
www.costain.com/engineering-tomorrow
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Costain photographers: Ian Routledge pages 6, 8, 43, 47, 48, 49 (Costain Board Directors); Ed Tyler pages 49, 136 (Jane Lodge, Graham Read); and Mike Doherty pages 49, 136 (Tracey Wood, Catherine Warbrick).

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This Annual Report is available at: **www.costain.com**

Visit www.costain.com

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