



# Solutions

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*Engineering solutions to meet national needs*

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# New solutions for new challenges

Costain, through insight and innovation, delivers solutions to meet national infrastructure challenges.

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At Costain, we are continually seeking new and better ways to deliver sustainable solutions for our nation's complex infrastructure needs.

Solutions start with insight, the ability to understand fully customer needs and to establish optimum outcomes.

Where insight provides vision, innovation drives execution. We have the capacity to look at old problems in new ways and apply new ideas, new technologies, new standards and new procedures.

Our graphic represents the driving force of inspiration. It encapsulates our drive for innovative solutions.

New solutions for new challenges.

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## Our vision

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

## Who we are

Costain is an international engineering and construction group with a reputation for technical excellence founded on more than 140 years of experience. The Costain name has been at the forefront of many world-famous projects including the Thames Barrier and the Channel Tunnel.

## What we do

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 including water, waste, power, rail, hydrocarbons and chemicals, highways and nuclear process.

## How we operate

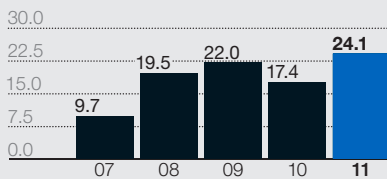
We are committed to operating our business both sustainably and responsibly. We are focused on one simple but powerful message – Costain Cares. This is not a slogan, it's an attitude of mind. It is integral to everything we do and a touchstone against which we can evaluate and measure our performance.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

## How we create value

Our ambition is to double profits over the medium term. We will do this by focusing on the needs of our major blue-chip customers. Our 'Choosing Costain' 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 change and improvement. We are confident that our robust business model and our strategic focus will continue to deliver shareholder value in the years ahead.

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## Adjusted group operating profit<sup>2</sup> £m



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## Directors' Report > Business review

This section provides greater focus on our strategy and our sustainable investment proposition. We explain how our strategy is underpinned by our commitment to Corporate Responsibility, how our business is organised and how it has developed over the year, and we provide details of our financial performance. We also review our strategic objectives, principal risks and key performance indicators.

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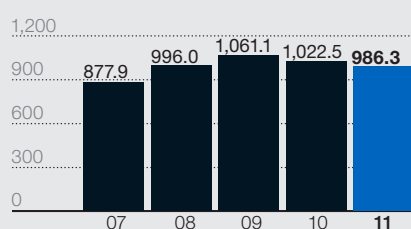
# 2011 highlights

## Strategy delivering results

### Financial highlights

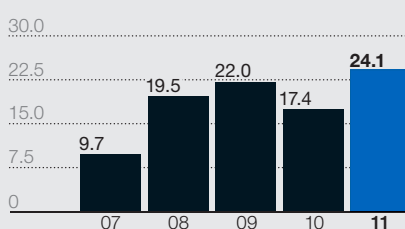
#### Revenue<sup>1</sup>

£m



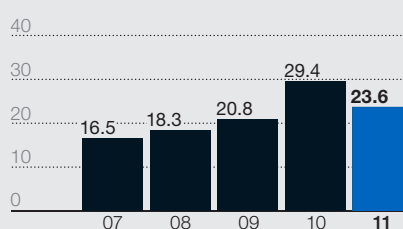
#### Adjusted group operating profit<sup>2</sup>

£m



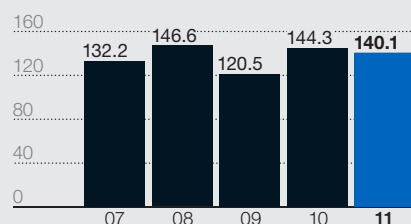
#### Adjusted profit from operations<sup>2,3</sup>

£m



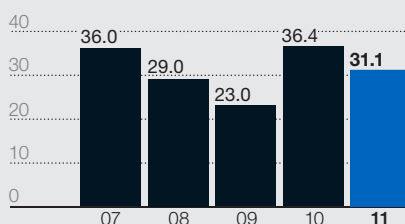
#### Net cash balance

£m



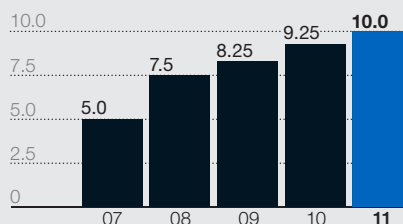
#### Adjusted earnings per share<sup>2,3,4</sup>

Pence



#### Dividends per ordinary share<sup>4</sup>

Pence



Year ended 31 December	2011	2010
<b>Revenue<sup>1</sup></b>	<b>£986.3m</b>	£1,022.5m
<b>Group operating profit</b>		
– Adjusted <sup>2</sup>	<b>£24.1m</b>	£17.4m
– Reported	<b>£22.5m</b>	£17.4m
<b>Profit from operations</b>		
– Adjusted <sup>2</sup>	<b>£23.6m</b>	£29.4m <sup>3</sup>
– Reported	<b>£22.0m</b>	£29.4m <sup>3</sup>
<b>Profit before tax</b>		
– Adjusted <sup>2</sup>	<b>£25.5m</b>	£27.9m <sup>3</sup>
– Reported	<b>£23.9m</b>	£27.9m <sup>3</sup>
<b>Basic earnings per share</b>		
– Adjusted <sup>2</sup>	<b>31.1p</b>	36.4p <sup>3</sup>
– Reported	<b>29.2p</b>	36.4p <sup>3</sup>
<b>Net cash</b>		
Year-end cash balance	<b>£140.1m</b>	£144.3m
Average month-end cash balance	<b>£130.4m</b>	£116.0m
<b>Dividend per share</b>	<b>10.00p</b>	9.25p

#### Notes

<sup>1</sup> Including share of joint ventures and associates.

<sup>2</sup> 2011 Results stated before amortisation of acquired intangible assets and employment related acquisition consideration.

<sup>3</sup> 2010 Results include profit of £11.2 million arising from the transfer of PFI assets into Group pension scheme.

<sup>4</sup> The figures for 2007 to 2009 have been restated for the 1 to 10 share consolidation.

**Find out more:****Chairman's statement**  
on pages 06 and 07**Chief Executive's Q&A and review**  
on pages 08 to 13**Business model**  
on pages 14 to 19**Group Finance Director's review**  
on pages 42 to 45**Board of Directors**  
on pages 46 and 47**Operational highlights**

- > Increase of 38% in adjusted Group operating profit<sup>2</sup> to £24.1 million.

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- > Year-end order book increased to £2.5 billion, in excess of 90% from repeat orders (2010: £2.4 billion).

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- > £140 million year-end net cash balance, no significant debt.

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- > Banking and bonding facilities increased to £465 million and extended to September 2015.

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- > Two successful acquisitions completed in 2011, broadening the range of services provided by the Group.

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- > Support services activities now represent 25% of work secured for 2012.

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- > Recommended 8% increase in dividend for the year: fifth successive year of increase.

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- > On course to achieve our ambition to double profits in the medium-term.

## £400m

### Costain awarded Network Rail £400m London Bridge station contract

The redevelopment of London Bridge station is a key part of the Thameslink Programme, which aims to increase significantly the total frequency of trains through the station per hour. Work is due to commence in full in 2013 and is scheduled for completion in 2018. Costain will ensure that the station remains fully operational at all times to minimise disruption to passengers.

## £150m

### Highways contract

Costain was awarded a contract worth £150 million by the Welsh Government to construct the A465 Heads of the Valleys road in South Wales.

In partnership with Atkins, Halcrow and RPS Group, Costain will design and construct an 8km section between Brynmawr and Gilwern. The project will present significant engineering and environmental challenges as the road passes through a number of Sites of Special Scientific Interest including the Clydach Gorge within the Brecon Beacons National Park.

**Promanex**

In August 2011, Costain announced that it had acquired Promanex, an industrial support services business providing facilities management, installation, repair and maintenance and general asset management in a number of high-growth, specialist markets such as power, petrochemicals and nuclear.

Mark Dixon, Managing Director of Promanex, said: "We are delighted to be joining Costain. Costain rightly has an outstanding reputation for applying technological expertise and innovation to add value to customers. Allied with Promanex's proven capabilities and market leading position in our core sectors, we will make a formidable team."

"Costain has an exciting future and we are very much looking forward to being a part of it."

**Promanex**  
a Costain Group Company

**ClerkMaxwell**

Costain acquired ClerkMaxwell, an Aberdeen-based front-end engineering and operations support services provider delivering front-end engineering and operations support services to blue-chip customers in the upstream oil and gas sector including Chevron, BG Group, TAQA, GDF SUEZ, Talisman Energy and ConocoPhillips.

ClerkMaxwell's full breadth of services includes feasibility and conceptual engineering, front-end engineering, detailed engineering, and operations support for projects in the upstream oil and gas sector including topsides, subsea and pipelines.

This acquisition provides Costain with a full hydrocarbons value chain capability from upstream oil and gas, gas processing, LNG and gas storage through to downstream. It also provides both companies with access to a larger and broader customer base.

  
A Costain Group Company





# 2011 highlights continued

## Focused on our responsibilities

### Environmental and social highlights



The Costain led Seeing is Believing visit at St Joseph's RC Primary School.

**In April 2011, Andrew Wyllie, Chief Executive, and David Allvey, Chairman, hosted an event on behalf of HRH The Prince of Wales' Seeing is Believing programme.**

The Prince's Seeing is Believing programme aims to inspire and engage business leaders on responsibility issues. Through unique visits into the heart of UK communities, the programme offers a way to challenge business leaders' perceptions on responsibility issues within their individual businesses, through their supply chains and across industries. The event saw senior business leaders visit Crest Boys' Academy, in Neasden, and St Joseph's RC Primary School, in Willesden, to see how programmes, such as STEMNET and Mosaic, are being implemented in order to bridge the growing skills gap in the UK.

The event then moved on to the National Grid Tunnelling Project, in Willesden, for an insight into what Costain is doing to help bridge the skills gap, and to meet apprentices, trainee engineers, construction ambassadors and graduates to gain an understanding of the challenges facing young people looking to forge a career in a technical industry and the importance of apprenticeships.



# 44%

Reducing the total waste we generate by 44% and diverting 89% from landfill.

**Costain became a patron of The Prince's Trust, a youth charity that helps change young lives.**

"The Prince's Trust and the young people we support are indebted to leaders of the UK's construction and business services sectors, including Costain Group PLC, which, through their support, contribute to an improvement in the skills and employment potential of hundreds of young people."

Martina Milburn, Chief Executive, The Prince's Trust.



### CEEQUAL awards

In 2011, we received the CEEQUAL ('Civil Engineering Environmental Quality Assessment and Award Scheme') 'Outstanding Achievement' Award in the community relations category for the Castleford Footbridge project and an 'Excellent' Award for the Church Village Bypass project.

# 95%

## Costain achieved a score of 95% in the BITC Corporate Responsibility Index.

Costain achieved a score of 95%, a Platinum banding, in the BITC Corporate Responsibility ('CR') Index 2011. The Index helps companies to integrate and improve CR throughout their operations by providing a systematic approach to managing, measuring and reporting on business impacts in society and on the environment.

"I congratulate Costain on achieving Platinum in the 2011 BITC Corporate Responsibility Index. It is a challenging time, but the results of this year's Index demonstrate that companies are still focused on transforming their businesses in order to have a positive impact on society. All the companies who participated this year are at different stages in their responsible business journey, but they are all taking these issues seriously and are prepared to lead by example."

Stephen Howard, Chief Executive, Business in the Community.



## Costain – selected by the Energy Technologies Institute

Costain was selected by the Energy Technologies Institute ('ETI') to lead the development of the next generation in carbon capture technology. The project will see a carbon capture pilot plant capable of capturing 95% of CO<sub>2</sub> emissions designed, built, operated and tested by the middle of 2015.

## Gold Green Apple Environment Award

The Costain joint venture working on the redevelopment of Farringdon station in central London, received a prestigious Gold Green Apple Environment Award for its sustainable approach to building and construction. The Green Apple Awards recognise environmental best practice and the business reasons behind employing environmental initiatives in order to safeguard the environment.

The project won by demonstrating how sustainable development can have both an environmental and economic benefit. For example, the team diverted 100% of the demolition waste from landfill which saved £365,000 in landfill tax, while reusing the rubble from the demolition removed the need for approximately 850 lorry movements which saved 30 tonnes of CO<sub>2</sub> emissions and approximately £70,000 on the cost of additional materials. For the new ticket hall, instead of using what would have amounted to 500 tonnes of steel, the team used an eco-reinforced alternative that was 95% recycled and responsibly sourced.

# 40

## RoSPA Awards

Our strong Health & Safety performance was recognised by the achievement of many Health & Safety Awards. We received 40 RoSPA Awards, comprising 2 Orders of Distinction, 6 Gold Medals, 22 Gold Awards and 10 Silver Awards.

# 35%

## Reduced our measured carbon emissions by 35% in 2011, a 46% reduction in the last four years.

## The Company awarded two Big Tick Awards

Costain received recognition in Business in the Community's Awards for Excellence 2011. The Company was awarded two Big Tick Awards in the 'Skills in the Workplace' and 'Building Stronger Communities' categories. The skills award acknowledged the work Costain has put into developing talent throughout the organisation at all levels – from basic literacy classes for local trainees to continuing development of the skills of Executive Board members.

The community award recognised the efforts the Company made while building the Church Village Bypass in South Wales. Substantial numbers of local unemployed people were taken on to the project workforce and considerable efforts were made to maximise expenditure within the local community and small businesses.



Brian Greaves, Community Relations Manager, receiving BITC's Big Tick Award 'Building Stronger Communities' for the Church Village Bypass project.



# Chairman's statement

## We are transforming Costain into a broad-based Tier One engineering solutions provider..

### Costain delivered another strong performance in 2011, in line with the Board's expectations.

It is particularly pleasing to report a substantial increase in operating profit and an increase in our order book, the result of a deliberate and ongoing focus on those UK market sectors where there is, and will continue to be, significant private and public investment to meet critical national needs.

The year also saw Costain pursuing its twin strategic objectives of growing by acquisition, as well as organically, and broadening its range of services to include a greater proportion of support service activities as we continued to build on our position as a leading Tier One engineering solutions provider.

Revenue, including the Group's share of joint ventures and associates, for the year was £986.3 million (2010: £1,022.5 million). Our focus is on higher margin work and consequently, Group operating profit, before other items, was £24.1 million (2010: £17.4 million), an increase of 38%. Profit before tax and other items was £25.5 million (2010: £27.9 million), with the prior year having benefited from

a profit of £11.2 million realised on the transfer of the Group's interest in a portfolio of six PFI investments into The Costain Pension Scheme.

#### Strategic delivery

Costain secured a number of major, nationally strategic contracts during the year. A highlight was the award of the five-year £400 million contract by Network Rail for the redevelopment of London Bridge station, notable not just for the scale and scope of the contract, but also that it was awarded in recognition of Costain's proven ability to manage such complex projects on its own.

As a result, the Group's year-end order book increased to £2.5 billion, including over £650 million of work already secured for 2012. In excess of 90% of our order book is from repeat orders and support services activities now represent 25% of the work secured for 2012. Further contract awards and extensions since the year-end has increased the level of revenue secured for 2012 to over £750 million.

Whilst the continuing uncertain macro-economic environment is impacting the UK market as a whole with total volumes reduced, procurement periods extended and a variation of activity levels across regions, our strategy of targeting customers with committed long-term capital and operational spending plans has enabled us to pursue and win work less affected by the downturn. Moreover, we believe that our target customers will

continue to commit substantial expenditure over the medium to long-term, providing Costain with significant opportunity to grow.

To achieve that growth, we must also continue to diversify and broaden the range of services we offer. Our 'Choosing Costain' strategy was developed and is being implemented in line with major structural market changes as our customers increasingly seek suppliers who can offer both an innovative cost-effective approach and provide a broad, end-to-end service across the life-cycle of an asset. The ongoing drive, both organically and by acquisition, to broaden our services across engineering consultancy, construction, and operations and maintenance will remain a key priority in 2012.

Potential acquisitions must meet a range of strict criteria, including strategic rationale and shareholder value enhancement. During the year, we were pleased to announce the acquisitions of ClerkMaxwell, a front-end engineering and operations support services provider operating in the upstream oil and gas sector, and Promanex, an industrial support services business providing facilities management, installation, repair and maintenance and general asset management. Both companies have been successfully integrated, are operating in line with our expectations, and provide Costain with a broader range of services to offer its customers.





**David Allvey** Chairman

With a £140 million net cash balance and no significant debt and with banking and bonding facilities increased to £465 million, and extended to September 2015, the Group is in a very strong position to deliver on its strategy.

#### **Dividend**

Reflecting another successful year and our continuing confidence in the long-term prospects for the Group, the Board is recommending an 8% increase in the final dividend, the fifth successive year of increase. If the 6.75 pence per share (2010: 6.25 pence) final dividend is approved at the forthcoming Annual General Meeting, then it will be paid on 25 May 2012 to shareholders on the register as at the close of business on 20 April 2012. This would bring the total for the full year to 10.0 pence per share (2010: 9.25 pence), an increase of 8% over the prior year.

#### **Staff**

The year would not have been a success, nor would we be as confident for the future, without the people we have at Costain. On behalf of the whole Board, I would like to express our gratitude to all our colleagues and place on record our recognition and appreciation of their commitment to the business.

#### **Group pension scheme**

At the year-end, the Group's pension scheme deficit in accordance with IAS 19, net of deferred tax, was £39.7 million (2010: £28.9 million),

the increase is primarily as a result of a reduction in the discount rate, based on corporate bond yields, used to calculate the liabilities. We have in place a deficit recovery plan based on the latest actuarial position as at 31 March 2010, agreed with the Pension Scheme Trustee and expected to eliminate the deficit over a period of less than ten years.

Since the year-end, the Group has made a further transfer of two PFI investments into the scheme at an agreed value of £20.3 million. Furthermore, the Group has instigated a liability risk management exercise and is in the process of issuing Enhanced Transfer Value and Pension Increase Exchange offers to the members of The Costain Pension Scheme. Together, the above actions are estimated to reduce the pension deficit by approximately £16 million, with an associated potential reduction in annual deficit contributions, following the next triennial actuarial valuation of The Costain Pension Scheme which is due as at 31 March 2013. Full details of these measures are contained in the Group Finance Director's review.

#### **Summary and outlook**

Costain delivered another strong performance in 2011, with operating profit up substantially and an increased order book.

The Group has been successful in targeting those blue-chip customers who are spending billions of pounds

per annum on essential capital projects and ongoing maintenance of essential, nationally strategic assets. This provides a major opportunity to grow the business further.

We are transforming Costain into a broad-based Tier One engineering solutions provider, aligned with structural market changes. Winning projects such as the complex £400 million London Bridge redevelopment is testimony to that. Meanwhile, our strong cash position, robust balance sheet and increased banking and bonding facilities provide us with the resources to grow the business by acquisition as well as organically.

Our confidence in Costain's future, and in achieving our ambition of doubling profit over the medium term, is reflected in the Board's recommendation to increase the final dividend for the fifth successive year.

**David Allvey**  
Chairman

7 March 2012

# CEO interview

## Q&A with Andrew Wyllie

### Q The Company is focused on Meeting National Needs... what does that mean?

A "Successful companies measure their value by their relevance to the external world. At Costain, we have identified the clear national priorities which are fundamental to ensuring the UK has a competitive future and an infrastructure which can support commerce and community alike. Whether it is solving transport congestion, avoiding an energy crisis, reducing the waste problem or supporting education, enterprise and employment, these are issues critical to generating economic growth and ensuring the nation's future.

"Costain has the technical skills, experience and commitment to play a significant role in providing solutions to meet these national needs. In recent years the Company has been at the forefront of developments in a number of areas including transport, nuclear decommissioning, water supply and developing skills needed for the future and we will continue to be so. Our customers have long-term investment programmes underpinned by strategic needs, regulatory commitments or essential maintenance requirements and they need high-quality service providers such as Costain."

### Q Costain describes itself as an engineering solutions provider... but is that not a description which many companies could employ?

A "No it is not. We only focus on major blue-chip customers, and they are looking to work with fewer number of Tier One service providers, through

longer-term, larger contracts incorporating a broader range of services across the life-cycle of their assets. To be an engineering solutions provider to these customers, it is essential that you are able to demonstrate that you have the necessary scale, experience and financial strength to be able to deliver a broad range of services through consulting, construction and operations and maintenance."

### Q Costain states that it is 'Transforming'... but what is the evidence to support that in the last 12 months?

A "Costain is being transformed as we develop and grow our capability, both organically and by targeted acquisition. In 2011, we acquired two companies with precisely that aim in mind.

"In May 2011, we announced the acquisition of Aberdeen-based front-end engineering and operations

support services provider ClerkMaxwell. This enabled Costain to offer customers full hydrocarbon value chain capability from upstream oil and gas, gas processing, LNG and gas storage, right through to downstream activities. ClerkMaxwell's customer list includes such names as TOTAL, Chevron and ConocoPhillips and the acquisition was another important step for Costain into a vital market. Then in August 2011, we acquired Promanex, an industrial support services business which strengthened Costain's presence in key growth target markets particularly in power, nuclear process, hydrocarbons and chemicals and water.

"Over a quarter of our income secured for 2012 now comes from support service activity as we align our services with our customers' requirements. Costain is now delivering the largest waste PFI project in Europe, the largest nuclear decommissioning project in the UK, and is the leading service provider to the Highways Agency."

**"Over a quarter of our income secured for 2012 now comes from support service activity as we align our services with our customers' requirements."**

**Q** What makes Costain different from its competitors?

**A** “Our people, and our culture. We have some of the best people in the industry, and I am very proud of them. The evidence of their performance and achievements is reflected in the 90% repeat orders we receive from our customers. It is that premier level of performance coupled with the Company’s values and heritage which makes Costain unique. Our customers know that a Costain person possesses high levels of skill, integrity and commitment. It is precisely that combination which makes the Costain service special.”

# 90%

## Repeat orders from our customers

**Q** As CEO you have taken on responsibility for the Costain heritage and you also make continual reference to ‘Transforming Costain’... are the two compatible?

**A** “Absolutely. The Costain reputation has been built on a long history of innovation, leadership and constantly adapting to changing requirements. Around the globe, people have witnessed Costain teams adapting to and overcoming difficult conditions and providing exactly what clients required. In the current age, we are continuing that philosophy by adapting and growing the Costain capability to meet the needs we all face now. As long as we continue to quickly drive innovation into our products, and enhance our service at a price point that customers are willing to pay, then we will continue to grow.”

# “The Costain reputation has been built on a long history of innovation, leadership and constantly adapting to changing requirements.”

**Q** Costain provides a service to customers but in your six-year tenure as CEO how has that ‘service’ changed?

**A** “Over that time we have focused entirely on meeting the needs of the sophisticated major customers who have larger investment programmes. We have dispensed with one-off contracting relationships. We have moved away from customers and business opportunities where we cannot establish a competitive advantage. As a result of that focus we have lots of opportunities to grow the business. We have moved away from international construction activities where the risk was not commensurate with the return. Our customer base now includes some of the best known names in industry all with long-term specific needs. We have a wider skills base than before and we are capable of competing at new levels because we now have a stronger, more comprehensive service involving front-end engineering consultancy, construction and ongoing care and maintenance.”

# “We have a wider skills base than before and we are capable of competing at new levels because we now have a stronger, more comprehensive service...”

**Q** Do you expect the major changes in Costain in the next five years to be internally driven or externally driven?

**A** “Both. Our growth aspirations will be achieved through a combination of organic growth and by suitable acquisitions in line with strategy. This will allow us to accelerate the development of the Group, and is how we will broaden and improve the quality of earnings stream. Ultimately, it is the customers who place the orders, and therefore decide our destiny. With over 90% repeat orders in an increased order book, we have a good platform to take the business forward successfully over the next five years.”



# Chief Executive's review

## Andrew Wyllie outlines the successful transformation of the business and gives the reasons behind a strong performance in 2011.

**Costain has delivered another strong performance. An increase of 38% in operating profit, an increase in the size of the order book and an increase in the recommended final dividend are testimony to the success of our strategy and its implementation.**

The UK faces unprecedented challenges, including the impact of a rapidly growing population, climate change, and the need to ensure a secure, sustainable and balanced portfolio of energy sources. An ageing and increasingly obsolete infrastructure means that there is a clear and recognised national need for strategic investment.

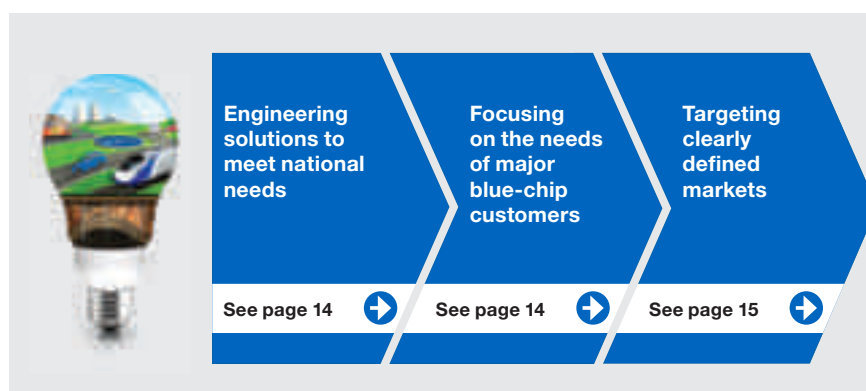
Alongside this imperative is the reality of the global macro-economic environment and the impact it is having on the prioritisation of spending plans.

We have, therefore, maintained a focus on targeting and working with blue-chip customers in sectors whose spending activity is underpinned by strategic national needs, regulatory commitments or essential maintenance requirements. Our target customers are spending billions of pounds per annum on capital, operations and maintenance contracts. In its 2011 Autumn Statement, the UK Government identified an increase in infrastructure investment, and has recently announced the go-ahead for the second high-speed rail link. Notwithstanding this welcome increase in commitment from the public sector, by far the majority of future spending is expected to continue to come from the private sector.

The Board continues to believe that, over the next decade, such expenditure will be primarily in the critical areas of transport, energy, water and waste, where national needs are being addressed. These areas provide a strong and sustainable pipeline of future investment to ensure energy security, the provision of a sustainable water supply, and creating key transport infrastructure capable of supporting vital economic growth.

We are continuing to transform the Group through the implementation of our 'Choosing Costain' strategy and are reinforcing our position as one of the UK's top Tier One engineering solutions providers, with well-established positions in sectors such as highways, water and rail.

### Our business model







**Andrew Wyllie** Chief Executive Officer

We are developing the skills, capabilities and service offering necessary to meet the changing needs of our major customers. They are increasingly expecting Tier One suppliers to provide broad and bespoke solutions to their specific requirements by delivering an innovative service across engineering consultancy, construction and operations and maintenance, through larger and longer-term bundled contracts.

These skills enable us to engineer solutions to meet some of the country's most complex and pressing national needs. For example, Costain is delivering the largest waste PFI project in Europe, the largest nuclear decommissioning project in the UK and is the leading service provider to the Highways Agency.

In addition to the organic development of those skills within Costain, for the first time in over 20 years, Costain augmented the implementation of its strategy through the acquisition of two businesses, ClerkMaxwell, an upstream oil and gas consultancy, and Promanex, an industrial support services business. Both businesses have been integrated successfully and are performing well and in line with our expectations.

ClerkMaxwell provides Costain with a full hydrocarbons value chain capability from upstream oil and gas, gas processing, LNG and gas storage through to downstream, and provides the Group with access to a larger and broader customer base in the oil & gas sector.

Promanex's customer base includes such blue-chip companies as ConocoPhillips, EDF, E.ON, Magnox, RWE, Scottish and Southern Energy, Siemens and TOTAL, a number of which are existing Costain customers.

Consequently, the services we can offer to our customers, and the composition of our earnings, are being transformed as we broaden the business through the implementation of our strategy. Currently, 25% of our 2012 order book now comes from support services activities and we expect this to continue to grow.

Core to our transformation and our value proposition to customers is our 'Costain Cares' initiative which places responsible, effective and collaborative stakeholder relationships at the core of everything that we do.



# Chief Executive's review continued

This ranges from taking a unique and innovative approach to finding solutions for each individual customer requirement, to wider initiatives such as our school leavers' apprentice scheme or our participation in an ex-offenders' programme. As well as having a beneficial effect on our corporate culture, these factors differentiate us from our peer group, are an increasingly important factor in our stakeholders' selection processes, and have directly contributed to the award of our largest contracts this year.

## Increased order book providing long-term earnings visibility

Costain's strategy is to focus on securing longer term and higher margin contracts from major blue-chip customers. Whilst this approach has led to a decrease in revenue in 2011, our operating profit and quality of earnings have improved significantly.

During the year, we secured new contracts and extensions to existing contracts of some £1.1 billion and as a consequence, the Group finished the year with an increased forward order book of £2.5 billion (2010: £2.4 billion), providing good earnings visibility. The order book included in excess of £650 million of work secured for 2012 (December 2010: circa £800 million secured for 2011), and over £1.8 billion of revenue secured for 2013 and beyond. In addition, we again ended the year with preferred bidder positions on contracts with an aggregate value in excess of £400 million. Further contract awards and extensions since the year-end have increased the level of revenue secured for 2012 to over £750 million. These include a £60 million three-year maintenance contract for a new customer in the energy sector, a contract we were able to secure as a consequence of the skills acquired following the purchase of Promanex.

We are delighted that major customers continue to reappoint Costain for their investment plans with the result that repeat orders now account for in excess of 90% of the order book. We were also pleased to secure a number of new customers during the year with the potential for increasing the scope and scale of work we do for them.

The focus on key customers, and the provision of value-adding solutions to complex challenges, has ensured that Costain has maintained a strong pipeline of business development opportunities. During the year, we increased our business development and bidding activity to capitalise on these opportunities, resulting in an increase in the order book.

## Progress in Operations

The Group has three core divisions: **Environment, Infrastructure and Energy & Process.**

The **Environment** division focuses on the water and waste markets as well as the specific requirements of a number of long-term customers. Customer spend in this market is underpinned by regulatory and legislative requirements and is expected to grow over the medium and long-term.

Revenue (including share of joint ventures and associates) in the division for the year was £375.4 million (2010: £489.8 million), with profit from operations of £17.5 million (2010: £17.2 million including profit of £11.2 million from the transfer of six PFI investments into The Costain Pension Scheme). Underlying operating profits increased very significantly, reflecting strong project delivery performance and the successful close-out of a number of legacy issues well within our allowances. The reduction in revenue in this division was fully anticipated and is a consequence of the strategic decision to withdraw from lower margin activities, as well as a slower than anticipated start to the AMP 5 programme of work.

The division finished the year with a forward order book of £0.8 billion (2010: £1.2 billion), the reduction reflecting the completion of a number of historic contracts in the year. With our established positions in water and waste, and the continued broadening of our services portfolio, we look forward with confidence to continued progress in this division.

The **Infrastructure** division, which incorporates activities in the highways, rail and airports sectors, saw a year of significantly increased investment in business development in order to take advantage of a strong pipeline of opportunities.

Revenue (including share of joint ventures and associates) in the division for the year increased to £466.0 million (2010: £395.3 million) although adjusted profit from operations decreased to £10.2 million (2010: £12.2 million). This short term decrease reflects the costs associated with the higher level of bidding activity, which has resulted in a 36% increase in the order book to £1.5 billion (2010: £1.1 billion), as well as the costs of the Promanex acquisition and additional costs for the completion of a project.

The **Energy & Process** division undertakes work in the hydrocarbons and chemicals, nuclear process and power sectors.

Revenue (including share of joint ventures and associates) in the division for the year increased to £143.4 million (2010: £136.6 million) with adjusted profit from operations of £4.7 million (2010: £8.2 million). Profits were impacted by increased investment in business development, the costs to complete the ClerkMaxwell acquisition and the additional costs required to complete a project in Abu Dhabi. The division's year-end order book has increased to £215 million (2010: £127 million) and we see a number of exciting opportunities for further growth in this division.

Our non-core **Land Development** activity in Spain, which is a joint venture with a subsidiary of Santander Bank, continued to be subject to very difficult market conditions. Revenue was £1.5 million (2010: £0.8 million) and the loss after tax was £2.0 million (2010 £1.8 million). As anticipated, no land sales were completed in the year and land development activity has been scaled back until the market improves and maximum shareholder value can be secured for the assets. Our activities during the year have been focused on our leisure businesses of golf courses and our 600-berth yacht marina adjacent to Gibraltar.

Further detail on each operating division is contained within the Business review.

#### **Enhancing our Safety, Health and Environmental performance**

Costain places the highest priority on the effective management of Safety, Health and Environment.

Further progress was made in the year and we again recorded an improved Group Accident Frequency Rate ('AFR') reducing from 0.15 to a new record low of 0.11, which continues to compare favourably with our major Tier One peer group.

We received 22 RoSPA Gold safety Awards and two prestigious Orders of Distinction recognising 15 consecutive annual Gold Awards.

A significant achievement was an external accreditation by the Cambridge Centre for Behavioural Studies for our in-house Costain Behavioural Safety initiative. We are the first company in the UK to achieve this accreditation and it is a unique differentiator for our industry.

However, despite our continuous vigilance and focus on our safety performance, there was a fatal accident involving an employee of a subcontractor on the Newbury Parkway project. Also, four Costain employees were killed in a fire in an accommodation facility

in Abu Dhabi. The cause of the fire, which was in a facility not owned or operated by Costain, is still being investigated by the authorities.

Everyone in Costain extends their deepest sympathies to the families of those involved.

We received our first Platinum award following an external assessment by Business in the Community, recognising our proactive commitment to mitigating the environmental and social impacts of our operations.

#### **Developing our team**

A strong business is one that employs and retains good and motivated people.

During the year, we increased our training and development programmes across the organisation to ensure that we continue to have the requisite skills and resources. There was a 30% increase in the number of training days which, through improved efficiency, were delivered at a lower total cost than in 2010.

There was also an increase in the number of apprentices across the Group and the introduction of a new graduate development programme.

Tracey Wood became Group Company Secretary on 1 June 2011, following the retirement of Clive Franks after 30 years of service with Costain. Tracey continues to be responsible for HR and legal matters on the Executive Board, whilst Fiona Ware has been promoted to Group HR Director reporting to Tracey.

#### **Summary**

Costain has delivered another strong performance.

The implementation of our 'Choosing Costain' strategy continues to transform the Group, as we develop or acquire the skills and capabilities to reinforce our position as one of the UK's leading Tier One engineering solutions providers.

Looking ahead, whilst mindful of economic conditions, we see significant opportunity for the continued successful implementation of our strategy which, in turn, will lead to the delivery of the Board's ambition of doubling profit over the medium-term.

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



**Andrew Wyllie**  
Chief Executive

7 March 2012

# Business model

Creating value through our customer focused strategy.



Engineering solutions to meet national needs

## Focusing on the needs of major blue-chip customers

### Intelligent solutions

Today's environment requires businesses to innovate at a faster rate than ever before. Our response to this trend and to the need to provide the right product or service to our customers has led to our focus on developing intelligent solutions.

### Cost competitiveness

In a challenging global economy, businesses continue to come under pressure to drive down costs. We concentrate not just on solutions that deliver the best value for customers but also on how we deliver those solutions. This requires an unrelenting focus on our customers' costs and our own operating procedures.

### Scale and capability

Customers value their key relationships but also require a strong breadth of capability and financial stability in this uncertain environment. In response, building on our strong balance sheet and robust order book, we will continue to expand our offer across the full life of an asset – from conception through construction to operation and maintenance.

### Tier One engineering solutions provider

Whatever their core role – providing a safe, reliable and efficient railway; managing, maintaining and improving the nation's roads; developing environmentally, sustainable power or cost efficient water services – customers seek out organisations that have a detailed understanding of their business and an ability to manage, co-ordinate and deliver the solutions required to support their ambitions.

### Sustainability

Our role is to work with our customers to provide solutions that meet national needs. Our commitment to delivering these services responsibly and sustainably is paramount. We believe that sustainability is central to delivering greater value to our customers and all other stakeholders.



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## Our market focus

Why these markets are attractive to Costain

**Targeting £billions worth of committed spend** (based on estimated annual industry spend)

### Water

**£11bn**

Water resources are already under pressure as a result of both climate change and population growth. The resulting impact suggests reduced water availability with a greater supply/demand gap. DEFRA's latest predictions show that even with a good Climate Change scenario the areas in water deficit will more than double over the next 20 years.

### Waste

**£8bn**

As the UK works to reduce waste, the market continues to show significant growth, principally as a result of the UK Government's objective to become a 'zero waste' economy. This typically favours prevention, reuse and recycling, rather than landfills and incineration. It is predicted that the waste management market will increase by 22% in terms of value over the next five years.

### Highways

**£8bn**

Increasing population and migration towards urban hubs has resulted in greater pressure on our road network. It is predicted that total vehicle traffic will grow by 25% by 2025 and 43% by 2035 (both compared to 2003) with average delays set to increase by over 50%, driving a significant demand for more efficient use of the assets through effective maintenance and technology.

### Rail

**£17bn**

As the population continues to grow, rail has become a vital form of transport to move within and between increasingly congested cities. As Network Rail and TfL continue to plan for a significant growth in passenger usages, TfL predicts a 30% growth in passengers by 2031 and is spending £1.5 billion annually on London Underground and currently £875 million on Crossrail. High-Speed 2 offers a £32.7 billion opportunity until 2026, whilst Network Rail and the Train Operating Companies continue to invest significant sums in the development of the national rail network.

### Nuclear process

**£4bn**

The Nuclear Decommissioning Authority has committed to a lifetime investment of £49.5 billion for the decommissioning and clean-up of civil nuclear sites around the UK.

Government remains committed to safely dealing with the legacy from the post-war nuclear research programme and subsequent first generation of nuclear power stations. Volume growth of nuclear fuel demand in the global markets continues to drive fuel cycle investment plans and, in defence, the Government has confirmed its commitment to replacement of the UK's deterrent.

### Power

**£10bn**

The key challenges facing the UK today are to ensure that future electricity supply is secure, low-carbon and affordable. Security of supply is threatened as approximately a quarter (20 GW) of existing power generation capacity will soon shut down. To provide clean energy, investment is required in new nuclear, renewable and carbon capture. Whilst we continue to maintain existing infrastructure, extending its life and, where feasible, converting it to a more sustainable fuel source. This will help to enable the transition of the UK to a low-carbon economy and meet the 15% renewable energy target by 2020. DECC forecasts that approximately £75 billion of investment could be needed in new electricity generation capacity by 2020.

### Hydrocarbons and Chemicals

**£20bn**

The upstream oil and gas sector is set to maintain significant activity in the North Sea and the Middle East, with investment of up to £140 billion over the next decade. This is underpinned by the soaring demand from China and other developing markets, dwindling oil reserves, increased unrest in the Middle East and increased pressure from oil speculators. Driving enhanced oil recovery techniques are increasingly being deployed to improve hydrocarbon recovery. Currently, the UK recovers only around 40% of the hydrocarbons from existing reservoirs and so increasing this by even a small amount would be hugely beneficial – around £12 billion for every additional 1% of recovery.

# Business model continued

Creating value through our customer focused strategy.

## Our strategy to value creation

## Strategic priorities and progress in 2011

### Our 'Choosing Costain' strategy

The evolution of our 'Choosing Costain' strategy implemented last year sees us focus on providing intelligent solutions to meet national needs. Building upon our core strengths delivering complex construction projects whilst developing our existing capabilities in Consultancy and Care (Operations and Maintenance). This approach positions Costain as a Tier One engineering solutions provider in our priority target markets, of water, waste, highways, rail, nuclear process, power, hydrocarbons and chemicals.

Costain's ambition – To double profits in the medium-term

#### Meeting National Needs

A focus on customers whose major spending plans are aligned with projects which are essential to improving national competitiveness.

##### Progress

- Order book: grown £100 million to £2.5 billion.
- In 2011, we focused on the following areas: Crossrail and Thameslink, highway technology and major congestion schemes, nuclear process and new nuclear, water capital schemes, offshore oil and gas and offshore wind.

#### Providing intelligent solutions

By providing innovative solutions, we are able to help our customers solve the problems they face.

##### Progress

- 34 patents (20 technology areas).
- £6 million deployed to support research and development.
- £5 million directed Government investment.
- Award of the ETI Carbon Capture Pilot project.

#### Broadening our offer

Providing customers with the capability across their assets to conceive, develop, construct, maintain and operate.

##### Progress

- In 2011, we focused on developing consultancy and care opportunities such as:
  - the front-end design for GASCO's nitrogen rejection units
  - support services at TOTAL's Lindsey oil refinery.

#### Sustaining our customer focus

It is of strong strategic importance to develop close partnerships with our customers. As our capability broadens, our customer relationships deepen and become more productive. Sustaining our customer focus remains at the heart of our business and strategy.

#### Progress

- Our customer retention rate remains high with over 90% of our current order book being delivered for existing customers.
- Significant market shares in water, highways and rail.

#### Identifying the right acquisitions

To leverage our growth opportunities in our chosen markets and improve the profitability of our business, we will continue to pursue selective acquisitions that are consistent with the implementation of our strategy.

#### Progress

- In 2011, the successful acquisition and integration of Promanex and ClerkMaxwell is delivering enhanced growth across the Group.

#### Operating responsibly

By contributing to the sustainable development of the UK's infrastructure, it is important that we approach our business in a responsible way. Corporate Responsibility sits in the mainstream of our business and we want to take full account of the social, environmental and ethical impact of our business on our customers, our employees and the communities we serve.

#### Progress

- We continue to measure our performance using third-party assessment through Business in the Community's ('BITC's') Corporate Responsibility Index. In June 2011, the Group was delighted to be awarded Platinum status in the Index, and was placed top in the construction and materials sector.

#### Engaging supply chain partners

Delivering efficient, innovative and sustainable solutions through early engagement and integration.

#### Progress

- Average supplier performance score of 65%.
- 130 suppliers accredited by Achilles.

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## Our business divisions and architecture

### Our business divisions

#### ► Environment

The Environment division delivers engineering solutions in water and waste, whilst also delivering legacy projects in education and retail.

#### Water

A leading provider of Capital Framework and Maintenance Framework Programmes under the current AMP 5 arrangements.

#### Waste

Delivering major waste schemes across the UK, the sector provides integrated and complete support services.

#### Education

Ongoing projects in Bradford and Lewisham, under the Building Schools for the Future programme.

#### Retail

Completion of legacy schemes.

#### ► Infrastructure

The Infrastructure division delivers engineering solutions for principal infrastructure providers.

#### Rail

A leading provider of multidisciplinary projects, currently delivering major projects principally focused on transportation hubs most recently at Farringdon, Reading and Paddington.

#### Highways

Delivering major programmes for the Highways Agency, maintenance under the current MAC contracts and Early Contractor Involvement works.

#### Airports

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

#### ► Energy & Process

The Energy & Process division provides consultancy, engineering, project delivery and asset support services across power, nuclear process and hydrocarbons and chemicals.

#### Nuclear process

Major frameworks delivered across key strategic assets.

#### Power

Focusing on thermal generation, new nuclear, offshore wind, transmission, distribution and biomass.

#### Hydrocarbons and chemicals

Developing and implementing solutions for upstream and midstream oil and gas and chemical sectors in the UK and Abu Dhabi.

[Find out more on pages 28 to 30](#)

### Our business architecture

#### ► Consultancy

##### Technology

Developing leading engineering solutions to customers' needs through the appropriate use of service and technology. To provide efficient and effective advice to customers' challenges.

##### Front-end solutions

Building on the extensive capability across our business. Costain is often employed at pre-development phase and development phase of project solutions.

##### Consultancy

We provide our customers with engineering consultancy, advice and support across the asset lifecycle.

##### Programme management

Delivering investment with certainty.

#### ► Construction

##### Delivery of assets

Delivering operational excellence in complex construction projects. Our experience of delivering major schemes on time, to budget and to a high level of quality remains a core capability. We continue to drive efficient delivery of these projects focusing on our people, our process and our partners.

#### ► Care

##### Operation and management of assets

Operating assets to drive efficient and effective utilisation. Minimising whole-life cost and maximising value.

##### Industrial services

The acquisition of Promanex, during 2011, delivers operations and maintenance activity across the power, water and nuclear sectors.

##### Outsourcing

Supporting customers' needs to focus on their core business, partnering with and developing these to a successful conclusion.

##### Maintenance

Delivering maintenance of major assets.

##### Support services

Working with our customers to deliver services to improve standards and achieve better value.

# Business model continued

Creating value through our customer focused strategy.

## Operating effectively and responsibly

To achieve our vision 'to be one of the UK's top engineering solutions providers', we must be the best for technical, innovative expertise and sustainable solutions.

We are committed to operating our business responsibly and sustainably, ensuring that we meet our customers' and society's needs while managing the social, environmental and economic impacts of our business.

Our primary focus is to both understand and meet the needs of stakeholders. In every relationship and facet of operation, we are focused on one simple but powerful message – Costain Cares.

Costain Cares is not a slogan. It is an attitude of mind. It is a commitment to exemplary behaviour and a touchstone against which we can all evaluate and measure our performance.

We have listened to the views of customers, communities, colleagues, supply chain partners and shareholders. This process has highlighted the issues that matter. It has allowed us to assess what we are doing well and identify where we need to focus for the future. We have used this feedback to set ambitious goals against which we can be held to account. Costain Cares is based on relationships, our environment and the future.

### Relationships

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

#### We will:

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

[Find out more on pages 31 to 34](#)

### Our Environment

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

#### We will:

- Work with our customers and supply chain to protect and, where possible, enhance the natural environment by:
  - Reducing our impact on climate change
  - Conserving natural resources through effective waste management, minimising water consumption and sustainably sourcing materials
  - Protecting the environment.

[Find out more on pages 35 and 36](#)

### The Future

We have a key role to play in helping the UK economy flourish. 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 for tomorrow's challenges
- Work with our customers and supply chain to develop skills to respond to future needs within our sector
- Contribute to economic growth by supporting our supply chain, including small and medium-sized enterprises.

[Find out more on page 37](#)

## Costain values

C	O	S	T	A	I	N
Customer Focused	Open and Honest	Safe and Environmentally Aware	Team Players	Accountable	Improving Continuously and therefore the...	Natural Choice



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## Investing in...

### Funding

Providing innovative funding solutions to support the delivery of priority infrastructure projects.

### Acquisitions

A focus on strategic acquisitions to support the 'Choosing Costain' strategy in our chosen markets.

Find out more on pages 08 and 10 to 13

### Business development

A greater level of targeted investment in business development and work-winning, specifically in new areas to deliver our growth.

### Research and development

Delivering intelligent solutions through the effective deployment of direct investment, research funding and customer led innovation.

### People

Retain, recruit and develop the best people and in doing so support 'Our Ambition'.

Find out more on pages 31 to 34

### Strong financial position

A strong balance sheet, a good long-term order book and banking and bonding facilities provide a springboard to deliver 'Our Ambition'.

Find out more on pages 42 to 45

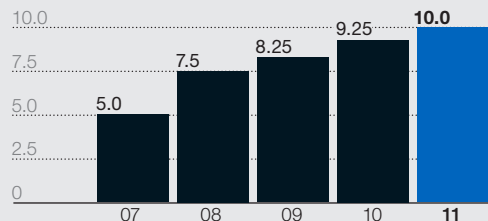
## Delivering shareholder value

**Our ultimate goal is to deliver maximum value to our shareholders.**

**As a mark of our confidence in our future prospects, the Board is recommending the payment of a final year dividend for the year of 6.75 pence per share.**

**That will bring the total dividend for 2011 to 10.0 pence per share which is an increase of 8% on 2010.**

**Dividends per ordinary share<sup>1</sup>**  
Pence



<sup>1</sup> The figures for 2007 to 2009 have been restated for the 1 to 10 share consolidation.

**Engineering solutions to meet national needs**

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## Sector focus

# Engineering solutions – Keeping people moving

### The need

#### Increase capacity

The UK's rail network is seeing the highest level of usage in peacetime since the 1920s, according to the Association of Train Operating Companies.

Recent figures show that, since privatisation was completed, passenger numbers have increased by 69% to more than 1.35 billion passenger journeys a year and demand is expected to double in the next 25 years. That means investment in the UK's rail infrastructure is vital to keep pace with demand, support the country's economic growth and to ensure passenger satisfaction, punctuality and safety.

The backbone of the national rail network was largely completed by 1851, while the first underground railway opened in London in 1863. While we can still marvel at the ingenuity, and in many cases the beauty, of Victorian construction and engineering, the rail infrastructure as it stands today isn't able to support the volume of people that depend on it.

Without attention and urgent action, the performance of this infrastructure will deteriorate and the UK risks falling behind its trading partners in Europe and the rest of the world. A country's infrastructure can influence business decisions on whether or not to locate in the UK.

The Government's strategy for the country's rail is a mixture of getting more from existing railway infrastructure through upgrades and to increase capacity on inter-urban routes.

The Government has pledged to improve the railway network, including bringing forward bridge renewals, increase electrification, continually improve safety, enhance access and capacity at stations and reduce disruption to the rail network.

Costain's Rail Sector has a strong track record in addressing these needs and is well positioned to deliver world class infrastructure, using innovative technology, design and engineering solutions.

### The solution

#### Innovative technology, design and construction

Much of Costain's recent work in the rail sector has been focused around London. This is because of the large number of major transport hubs located in the capital and their connectivity with other cities in the UK.

Costain is working with its customers to increase capacity by upgrading existing stations and developing new infrastructure such as Crossrail, the biggest rail project in Europe, which will significantly increase the capacity of the rail network into and across London and relieve congestion and overcrowding on the existing rail and underground networks.

Costain, in joint venture, is currently redeveloping London Underground's ('LU') Bond Street station as part of LU's Tube Upgrade Programme. More than 155,000 passengers use Bond Street tube station every day and that figure is expected to rise to over 225,000 with the arrival of Crossrail in 2018.

Costain is using Building Information Modelling ('BIM') technology and systems at Bond Street to overcome potential problems associated with working on a site in close proximity to a large transport network and major utilities.

BIM allows engineers to generate and manage a large amount of data by checking for structural, architectural and building services clashes within existing



structures. It also analyses geometry, spatial relationships and geographic information, which can save time and money not only in the design stage but also as the project progresses.

LU now specifies the use of BIM on all complex projects in order to mitigate risk during the design and construction of major assets in a live working railway environment.

The expanded tube station will include an interchange with Crossrail, the 118km high-frequency rail route that will run from Maidenhead and Heathrow in the west, through new twin-bore 21km tunnels under central London, before forking at Stepney Green for Shenfield near Brentwood, and Abbey Wood in southeast London.



In September, Costain, in joint venture, handed over the first of five tunnel portals at Royal Oak while continuing to work on another tunnel portal at Pudding Mill Lane near Stratford. The portals will act as an entry point for the tunnel boring machines that are constructing the Crossrail tunnels.

Meanwhile, in July, Costain was appointed by Crossrail, in joint venture, to redevelop Paddington station and maximise the station's space while preserving, as Costain did at St Pancras International, the historic features of the mainline station. The new station will take the form of a 260m long, 25m wide and 23m deep underground box.

More recently, Costain was appointed to carry out detailed design and deliver a redeveloped London Bridge station for Network Rail and it recently completed a major milestone in the delivery of the Farringdon station redevelopment, in constructing longer platforms that allow 12-car trains to use the station.

Scheduled for completion in 2018, the London Bridge project will see through-station passenger capacity rise to 90 million people a year from 55 million. At Farringdon, the redevelopment includes a new train shed roof, refurbishing the original London Underground entrance, a new ticket hall serving both Thameslink and Crossrail passengers, replacement of the highway bridge to the front of the station, the installation of new power supplies and plant rooms, three new escape staircases and the installation of five new lifts to allow step-free access from platforms to street level.

Outside London, Reading is one of the UK's busiest stations, handling around 17 million passengers annually, serving the Great Western Main Line for express trains to South Wales and the West Country, as well as being the terminus for a network of local routes throughout Berkshire, Oxfordshire and Hampshire.

Here, Costain, in joint venture, recently handed over a new Platform 4 to Network Rail, while a new temporary Platform 10 was built in the middle of existing running lines, with tracks diverted around it.

**“Building on the success of delivering major rail infrastructure projects like St Pancras International, Costain’s multidisciplinary capabilities are increasingly being used not only to deliver demanding programmes of works but also to provide innovative solutions more effectively in order to bring greater benefits to customers and passengers alike.”**

**Darren James**, Managing Director, Costain's Infrastructure division.

## Sector focus continued

# Engineering solutions – The road to safety

### The need

#### Reduce congestion

A safe, reliable and well maintained infrastructure network is vital for the future prosperity of the country. The efficient movement of goods and people, supported by a balanced, dynamic and low-carbon-economy is essential if the nation wants to compete on the world stage.

A well-functioning road network promotes growth by reducing business costs, improving access to markets, increasing labour mobility and attracting inward investment. Highways act as major arteries which open up new opportunities for leisure and travel and the development of urban and suburban areas.

The Strategic Road Network ('SRN'), managed by the Highways Agency, carries nearly a third of all traffic and two-thirds of all freight traffic, despite making up only 3% of the total road network.

Investing in that infrastructure is key to the Government's economic strategy. In its National Infrastructure Plan ('NIP') released in November 2011, the Government set out its long-term strategy to keep the country moving.

This included improving the capacity, performance and resilience of the nation's roads, railways and international gateways; improve integration between different modes of transport; support the move to a low-carbon economy and improve connectivity and capacity between main urban areas.

The Department for Transport forecasts congestion across the English road network to increase from 2003 levels by 27% by 2025 and by 54% by 2035. While traffic is expected to shift to less congested roads, it is expected that congestion will ultimately increase over time.

The economic cost of not alleviating congestion on the road network could be considerable, but the costs are significantly outweighed by the financial benefits if the problem is tackled. The Eddington Transport Study, published in 2006, estimates that with a 5% reduction in travel time for all business and freight travel on the roads, a cost saving of £2.5 billion, or 0.2% of GDP, could be generated.

While the Government is investing £1 billion to tackle areas of congestion and improve the national road network, the NIP also sets out extensive recommendations to reduce the cost of infrastructure delivery and realise cost savings while still providing better value for money for taxpayers, road users and the wider economy.

In this new economic and commercial environment, customers like the Highways Agency are now more discerning in how they procure services from contractors and suppliers. That means companies working with the Highways Agency and other major customers need to work smarter to improve service delivery and drive out cost and waste in order to maintain the quality of service.

### The solution

#### Capacity enhancements

Costain's 'Meeting National Needs' focus is geared towards helping its customers meet society's needs by addressing the growing demand for infrastructure services, extracting greater value from existing infrastructure and being more efficient in how those services are delivered.

In line with this, Costain has increasingly employed lean engineering, which involves cutting waste and applying innovative tailor-made solutions to project specific problems. The aim is to deliver the same or better product while using few resources, which can save time and money.

An example of this is the M53 Bidston Moss Viaduct Refurbishment Scheme on the Wirral. The 730m long, 37-span steel box-girder structure was built in 1969 and had slowly deteriorated with time. Weight restrictions had to be imposed and heavy goods vehicles were precluded from crossing it, which disrupted goods going to market.

Costain strengthened the structure and returned it to full capacity using lean engineering and found £2.8 million in cost savings on the £90 million project.

"Customers are under increasing pressure to find savings on their capital projects and this has significantly influenced how they procure work. We employed lean engineering principles on the M53 Bidston Moss strengthening project which realised





significant cost savings for the customer,” said Darren James, Managing Director of Costain’s Infrastructure division.

Costain, in joint venture, is involved in four Managing Agent Contracts, or MACs, on behalf of the Highways Agency, including Area 7 in the East Midlands and Areas 10, 12 and 14 which cover the majority of the north of England. A MAC combines roles that were previously undertaken by separate Managing Agents and Term Maintenance Contractors, with an emphasis on innovation to deliver a value-added service.

That means designing a service more closely aligned to the customer’s needs and rigorously reviewing how that service is delivered.



Costain is also involved in a number of Managed Motorways Schemes on behalf of the Highways Agency. This comprises a ‘tool box’ of measures to manage road capacity, traffic demand and incidents in order to increase the efficiency of road use and reliability of journey times. Some of the measures include hard shoulder running, which uses the hard shoulder along more congested sections of the highway when traffic demand exceeds the capacity of normal running lanes.

Costain maintains around one-third of the SRN of motorways and major A-roads in England, on behalf of the Highways Agency and often in joint operation with other contractors, and is also involved in a number of major highway schemes on behalf of local authorities in England and Wales.

Costain helped to deliver £15 million worth of cost savings in the Early Contractor Involvement phase of the Port Talbot Peripheral Distributor Road (‘PDR’) Stage 2 project for Neath Port Talbot County Borough Council, through

managing innovative client specific solutions which ensured the project went ahead and continued to receive funding from the Welsh Assembly.

The Port Talbot PDR will be an important catalyst for the regeneration and economic development of the industrial area of Port Talbot by providing direct access to the M4 motorway and dock area. The three-mile link road will also remove local traffic from the M4 and reduce congestion in a restricted corridor.

The savings also delivered improved cost benefit assessment results for the scheme, which helped inform the award of a European Convergence grant of £59 million for the scheme.

Costain’s ‘Meeting National Needs’ focus is helping, within the new economic and commercial environment, to address the country’s highways infrastructure requirements, and working with the customer using innovative solutions to arrive at the best possible outcome.

**“We’re delighted with the results which represent an excellent example of working together to find client-specific solutions.”**

**Rhys Griffith**, Project Manager for Port Talbot PDR scheme.

## Sector focus continued

# Engineering solutions – To combat global warming

### The need

#### Reduce CO<sub>2</sub> emissions

The UK faces three long-term challenges to meet its energy requirements: to ensure secure, clean and affordable energy as it becomes even more dependent on imported fossil fuels, secondly, to tackle climate change by reducing CO<sub>2</sub> emissions and thirdly, to keep prices for electricity at a level affordable for both domestic and industrial consumers.

Global warming and climate change are international issues which potentially threaten the basic elements of life on the planet, including access to water, food production, health and the use of land and the environment.

The International Energy Agency forecasts global energy demand to rise by 53% by 2030, with energy related greenhouse gas emissions expected to rise by 55%. Based on current trends, global emissions of CO<sub>2</sub> are set to reach double that of 2007 levels before 2050.

Therefore, the gap in which to reform the global economy to a low-carbon footing is shrinking.

Accordingly, it is therefore imperative that the risk of using fossil fuels is managed and new technologies are harnessed to try and reduce the impact of carbon emissions.

In 2008, the Government brought in the Climate Change Act which created a new legal framework for the UK achieving, through domestic and international action, at least a 34% reduction in emissions by 2020 and an 80% reduction by 2050, against 1990 levels. These targets are underpinned by five-year carbon budgets which place binding limits on aggregate CO<sub>2</sub> emissions.

In order to reach these targets, a major component of the Government's strategy is to provide more support and promote the use of low-carbon technologies.

### A solution

#### Carbon Capture and Storage ('CCS') technology

Costain Energy & Process was selected in July by the Energy Technologies Institute ('ETI'), a public private partnership between six global industrial companies – BP, Caterpillar, EDF, E.ON, Rolls-Royce and Shell – and the UK Government, to help develop the next generation of carbon capture technology.

While key elements of the CCS technology have been proven to work, this hasn't been achieved on a commercial basis. The challenge then is to develop the next generation of carbon capture technology which not only increases the carbon capture rate but also improves capital costs and power generation efficiencies in comparison to conventional capture schemes.



CCS is an emerging combination of technologies that enables the capture of CO<sub>2</sub> generated from fossil fuel combustion or other industrial processes. The captured CO<sub>2</sub> is then transported via pipes and injected into long-term storage sites such as abandoned gas and oil fields and deep saline aquifers.

Costain, working in conjunction with Edinburgh University and Imperial College London, is undertaking the first phase of the project, which is the front-end engineering design, valued at £3.5 million. The new plant design will allow the capture of 95% of CO<sub>2</sub> from gases within a power station.

Thereafter, Costain will design, build, operate and test the new £20 million carbon capture pilot plant by the middle of 2015.

The Government is fully supportive and committed to harnessing the potential of CCS as a means of reaching its targets and it is looking at ways of reducing the costs of CCS technology so that it is cost-competitive in the 2020s.

Analysis from the IEA suggests that CCS technology will play a vital role in worldwide, cost-effective efforts to limit global warming. The use of CCS technology would allow electricity

to be generated based on burning coal and gas, and it can also be deployed alongside low-carbon sources such as nuclear and offshore wind farms.

Costain is playing a significant role in developing new technology that will help address a national need to develop clean energy, reduce emissions of CO<sub>2</sub> and help the UK meet its climate change targets.



“The causes and threat of climate change are global and the UK is at the forefront in trying to establish the next generation in carbon capture technology that will significantly reduce the risk of further damage to the environment and make CCS technology viable for generations to come.

“Innovation is central to what we do as a Group and, in line with our strategy of Meeting National Needs, we have the opportunity to help significantly reduce the amount of CO<sub>2</sub> that is produced by coal fired power stations. Demonstration of this project is key to building user group confidence in the capture technology.”

**Charles Sweeney**, Managing Director, Costain’s Energy & Process division.

# Performing responsibly is integral to our success and sustainability.

This is the fourth year we have combined our Financial and Corporate Responsibility ('CR') reporting, demonstrating that responsible business is core to our Company. Our aim is to deliver a totally integrated approach to our reporting.



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**Our operational reporting framework**

**Environment**

The Environment division comprises Costain's operations in the water, waste, education and retail sectors.

**Infrastructure**

Costain's Infrastructure division includes our operations in the highways, rail and airports sectors.

**Energy & Process**

The Energy & Process division includes our operations in nuclear, power and hydrocarbons and chemicals sectors.

**Land Development**

This division is responsible for the Alcaidesa land and marina development activity in Southern Spain, a 50% joint venture with a subsidiary of Santander Bank.

**Our CR reporting framework**

**Relationships**

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

**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.

**The Future**

We have a key role to play in helping the UK economy flourish. The benefits of investment in infrastructure today will be felt for many years to come.

# Performing responsibly

## Divisional performance – Environment

Costain has a well-established position in the UK water market. The Company has secured AMP 5 frameworks with Southern Water, United Utilities, Welsh Water, Severn Trent and Northumbrian Water. In addition to these long-term asset management contracts, Costain has continued successfully to design, secure and deliver major complex capital works infrastructure for the water industry. During the year, construction progressed well on the large Brighton and Hove waste water treatment works for Southern Water and the project will shortly move into the commissioning phase. On this and other projects, we see the potential to extend the scope of our work into long-term care and maintenance of the asset – reflecting the strategic broadening of our service offering.

The UK waste market continues to offer significant long-term growth opportunities for Costain. In 2011, we continued to make progress on our delivery of the Greater Manchester Waste Scheme, Europe's largest waste PFI project, for the Greater Manchester Waste Disposal Authority ('GMWDA'), where we are now in the commissioning phase of this complex scheme.

Costain has a strong capability in the waste sector and, this year, further strengthened its sector management team in order to broaden the service offering across the full life-cycle of consultancy, construction and maintenance of assets.

During the course of the year, the Group restructured its geotechnical services activity into a broader Environmental Services consultancy which secured a place on the Environment Agency's National Site Investigation Framework ('NSIF'). The consultancy has also added a number of innovative services, such as aerial photography and 3D laser scanning, which enable us to offer a more attractive portfolio of services to our customers.

In 2011, we substantially closed out our portfolio of schools in the final phase of the Bradford Building Schools for the Future ('BSF') programme. In our Local Education Partnership with Lewisham, also under the BSF programme, we continue to deliver a programme of new schools which will continue through 2012. During the year, we successfully handed over the first phase of the Newbury Parkway shopping centre development with the remainder scheduled for completion in 2012.



Greater Manchester's Recycling and Waste Management Contract

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## Divisional performance – Infrastructure

Our Rail sector enjoyed an outstanding performance with the award of several significant, long-term contracts. Investment in the UK's railway infrastructure is expected to grow with £40 billion of spend committed over the next five years. Costain is now a significant player in this market. Proof of this was the award by Network Rail of the prestigious £400 million Thameslink London Bridge station redevelopment contract. Costain will carry out this project from design to delivery, and results directly from the broadening of our service offering across the full life-cycle of consulting, construction and care.

We are making excellent progress on our contract to redevelop Reading station for Network Rail and the Bond Street station upgrade for London Underground. We successfully completed the Royal Oak Portal and Pudding Mill Lane Portal contracts for Crossrail (part of Europe's largest infrastructure programme) and have, subsequently, been awarded significant further Crossrail contracts for Bond Street and Paddington stations.

With significant Government investment expected over the medium and long-term in order to improve the UK's travel infrastructure, we continue to see exciting opportunities for growth in this market.

Our Highways sector saw a consistently strong performance throughout the year in which Costain reinforced its market leading position in Highways Maintenance. The Managing Agent Contracts ('MAC') service we are providing to the Highways Agency includes the operation and maintenance of a network in excess of one million lane miles, the largest of its kind in the sector. We also completed the strengthening of the M53 Bidston Moss Viaduct three months early and ahead of budget and we are making excellent progress on the construction of the first of the Highways Agency Managed Motorway Programme Schemes: the M1 Junction 10 to 13.

We have an industry leading portfolio of Early Contractor Involvement Schemes with contracts for the Highways Agency, Welsh Government, Northern Ireland Road Service and Lancashire County Council.

We were awarded the prestigious A465 Heads of the Valleys contract for the Welsh Government, and completed the A40 Penblewyn to Slebech Park Scheme ahead of time and budget. We also made good progress on Walton Bridge, the first bridge to be built over the Thames in over 20 years, for Surrey County Council, and on the Harbour Way for Neath Port Talbot County Borough Council.

In power infrastructure, our London Power Tunnel Project for National Grid, a 33km long tunnel that will help secure the power supply to the capital, has made good progress during the year.

The Riverside Resource Recovery Facility ('RRRF') Energy from Waste facility at Belvedere is now operational. There is some outstanding work to complete and negotiations regarding the final account are ongoing.

In our airports sector, during the year we were awarded and delivered the rehabilitation of Runway 1 as part of our framework agreement with the Manchester Airport Group. For Gatwick Airport, we successfully completed the Security Improvement on its Central Search facility. For BAA at Heathrow, we have continued to deliver services through our existing framework and were awarded capital contracts on the airfield and within Terminal 3.



M1 Junction 10-13 scheme



# Performing responsibly continued

## Divisional performance – Energy & Process

In hydrocarbons and chemicals, we were awarded by Centrica the engineering, procurement and construction management of a major development at one of its key gas terminals. The E.ON Holford underground gas storage project was successfully completed and handed over. Our capabilities in the upstream oil and gas sector were greatly boosted by the acquisition of ClerkMaxwell, an engineering consultancy based in Aberdeen, which is performing well and providing significantly enhanced opportunities to win new work in this high-growth area.

In nuclear process, we made further good progress in our various projects across the UK. Work continues on the Evaporator D contract at Sellafield, the UK's largest nuclear decommissioning

project, with the delivery of the first two modules to site. 'Evap D' will play a vital role in the future of Sellafield's operations. This highly complex project is being designed, fabricated and constructed to exacting specifications. In addition, the design of the Bradwell Fuel Element Debris Dissolution facilities (part of a multi-faceted ten-year framework contract) is well advanced.

In power, we were selected by the Energy Technologies Institute to lead the development of a technology to significantly reduce the amount of CO<sub>2</sub> produced by coal fired power stations. This will be a critical factor in the UK's ability to meet its climate change targets, and is a further demonstration of our ability to design and develop innovative solutions which add value for our customers.

## Land Development

Economic conditions in Spain remain very challenging, with a depressed real estate market and weak demand for development land and, consequently, we have scaled back land development activity until conditions improve. Our activities during the year have been focused on our leisure businesses of golf courses and our 600 berth yacht marina adjacent to Gibraltar. The marina continues to report increasing revenue and we expect that this will be further enhanced this year following the opening in January 2012 of a substantial dry dock and repair yard facility with 75-tonne travel lift capability.



Holford underground gas storage project



Our ongoing drive towards zero accidents and incidents resulted in the achievement of an Accident Frequency Rate of 0.11 in 2011...

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**Costain Cares – Relationships**

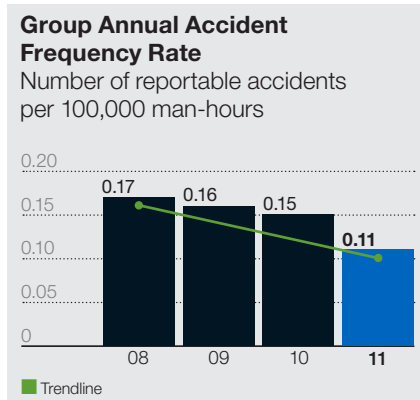
**We encourage open, honest, respectful communication. We believe in strong, long-lasting relationships that are mutually beneficial.**

**Health & Safety: Providing a safe working environment free from harm**

The Health & Safety of our workforce is of paramount importance. We are committed to providing a safe working environment, where the health and wellbeing of our people is both protected and actively promoted.

Our ongoing drive towards zero accidents and incidents resulted in the achievement of an Accident Frequency Rate ('AFR') of 0.11 in 2011, which represents a reduction of 27% over the previous year and a 35% reduction in the last four years.

Costain Group has not received any fines or prosecutions in the last four years.



**0.11**  
Group AFR, a 35% reduction in the last four years.

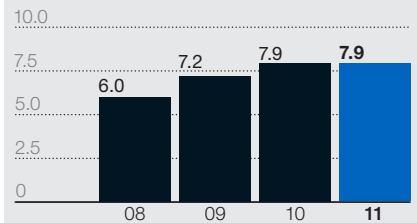
However, despite our continuous vigilance and focus on our safety performance, there was a fatal accident involving an employee of a subcontractor on the Newbury Parkway project. Also, four Costain employees were killed in a fire in an accommodation facility in Abu Dhabi. The cause of the fire, which was in a facility not owned or operated by Costain, is still being investigated by the authorities. Everyone in Costain extends their deepest sympathies to the families of those involved.

Our commitment to our people and stakeholders is demonstrated by our management of Health & Safety and our continual drive towards zero accidents and incidents. We focus this drive on the following three areas: compliance, competence and culture.

**Compliance**

We continue to monitor performance on our sites and compliance with our systems by means of our internal auditing and inspection regime. Over the last four years, we have achieved consistently high standards of Safety, Health and Environmental ('SHE') performance across all our projects. We strive continually to improve our performance, raise our standards and are dedicated to promoting best practice across our business and industry.

**Group average score in monthly SHE scored inspection**



**7.9**

**Group average SHE performance score.**

**Competence**

A safe site is one where all workers are confident and qualified to carry out the tasks to which they are assigned. For this reason, we insist on a fully competent workforce and provide ongoing training and development for both our own employees and those of our supply chain partners. Our competence card compliance policy outlines our requirement for all employees and subcontractors to be able to demonstrate appropriate competence in Health & Safety management, supervisory and technical skills.

We recognise that the role of front line supervisors ('FLS') is a key factor in improving Health & Safety performance and, during 2011, an enhanced protocol which mandates the assessment of all FLS on our sites was developed and implemented. All FLS (including those working for our subcontractors) must meet Costain's minimum standards in terms of competency levels, behaviour and attitude.

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# Performing responsibly continued

## Costain Cares – Relationships continued

It is critical that our senior management demonstrate positive leadership with regard to Health & Safety issues as this has a direct impact on our culture and the creation of a safe and healthy working environment. To that end, we ran a total of 11 Health & Safety leadership courses, based on the Institute of Directors' ('IoD') policy for Health & Safety leadership, which were attended by the 127 most senior members of our staff.

Following the overwhelming success of our leadership courses for our directors and senior managers, we will be targeting Health & Safety training for our middle management with the introduction of a bespoke training course aimed at this level of personnel.

### Culture

We promote a culture where our managers lead by example and our people demonstrate personal leadership in Health & Safety. Our values of teamwork and accountability actively encourage our workforce to engage and interact with their colleagues, customers and supply chain partners alike so that we learn from one another, explore different ways and methods of working and promote best practice and innovation.

We continued to promote behavioural safety training for our workforce and have nominated champions amongst our own staff who are now competent to deliver the training. Our training system, Costain Behavioural Safety ('CBS'), utilises the principles of Applied Behavioural Science and focuses on the leadership behaviours of our people, as well as designing and implementing Project Specific Implementation Plans that address the specific needs and issues of the Project.

In December 2011, Costain received international third-party accreditation from the Cambridge Centre for Behavioural Studies ('CCBS'), Massachusetts USA, for its CBS Programme, making it the first company in the UK to have a third-party accredited Behavioural Safety Programme.

### Providing a healthy working environment for all our people

The health and wellbeing of our staff and all other personnel engaged in work for us on our sites and in our offices remains a priority. In 2011, we continued to offer wellbeing medicals to our staff and enhanced our mandatory medical regime for safety critical workers. In addition, we ran two themed health campaigns across our business to educate our workforce and assist them to make informed choices regarding their lifestyle.

The first campaign focused on the dangers and effects of drugs and alcohol, not only on the workers themselves, but also their colleagues, families and friends and it highlighted the potential implications for their lifestyle.

The theme of our second campaign was selected following an analysis of medicals undertaken in 2010, which revealed the main health issues affecting our workforce. It focused on promoting the benefits of a healthy lifestyle, with particular emphasis on the prevention of strokes, heart attacks and obesity.

We will continue to promote the health and wellbeing of our people who we consider to be our most valuable resource. Our existing medical regime will continue as will our drive to raise awareness of health issues and develop innovative ways of promoting the wellbeing of our workforce.

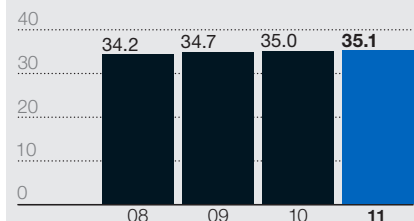
### Communities: Supporting the local communities in which we operate, ensuring we leave a lasting legacy

We recognise that the nature of our work can affect the communities in which we operate. How we manage our relationships and work together with these communities and other stakeholders is very important to us. We are committed to developing and maintaining excellent relations within local communities.

As an associate member of the Considerate Constructors Scheme, we are committed to minimising the impact our operations have on the community. We continue to receive consistently high scores on all our projects, achieving an average score, in 2011, of 35.1 out of 40 (the average score of all sites registered with the scheme is approximately 31). In addition, our performance was also recognised by the receipt of 20 Awards from the Considerate Constructors Scheme, including runner up for the prestigious 'Most Considerate Site' Award for our M25 Bell Common Tunnel refurbishment project.

### Considerate Constructors Scheme performance

Group average score



# 35.1

Average score in the Considerate Constructors Scheme.

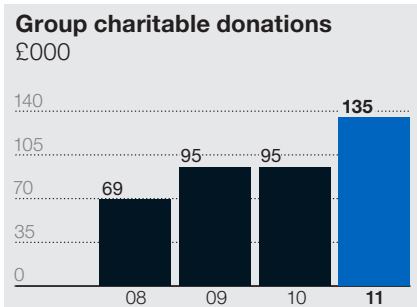
We are extremely proud of our graduate programme which has won external accolades and is accredited by seven professional institutions.

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**£135,424**

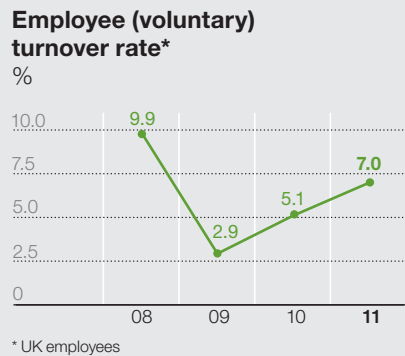
Donated to charitable causes in 2011.

We continue to support various charities both corporately and through local donations given by our project teams. In 2011, we donated £135,424 to worthy causes.

Through our employee volunteering policy, we provide our employees with the opportunity to develop and share skills while making a visible and sustainable difference to local communities. In 2011, we saw an increase in the number of days our employees volunteered and we have set a target to increase this contribution by 10% in 2012.

**Our People: Attracting, retaining and developing the best people for the Costain Group**

Following the successful acquisitions of ClerkMaxwell and Promanex, Costain Group now employs circa 3,600 people in the UK and a further 1,400 people in the Middle East. We continue to have a relatively stable work force, with 46% of staff having been with us for over five years and our staff turnover at a modest 7.0%. We filled 144 vacancies last year, 52% of these through internal placements, ensuring a good mix of employee career progression and bringing fresh talent into the organisation.

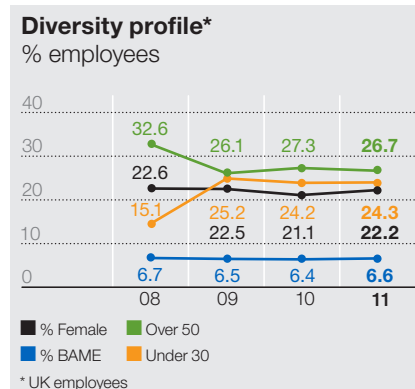


**7.0%**

Employee (voluntary) turnover rate.

**Building a diverse workforce**

We recognise the value in a diverse workforce. We ensure that all people activities continue to be inclusive and that we provide fair access and participation in training, promotions, reward and recognition. We have monitored our diversity profile over the last six years, which indicates a fairly consistent profile of female and Black, Asian and Minority Ethnic ('BAME') employees, at 22.2% and 6.6% respectively, which compares favourably to the industry average.



**22.2%**

Of our people are female, 6.6% are BAME.

**Developing talent**

We are extremely proud of our graduate programme which has won external accolades and is accredited by seven professional institutions. This year saw the introduction of our graduate 'boot camp' aimed at consolidating our graduate training into a more efficient and effective delivery model. We are also successfully rebuilding a strong apprentice programme, with 31 apprentices currently on level 3 frameworks and we plan to increase both the numbers and types of apprentices in 2012. In conjunction with our early talent pipeline, we are continuing to encourage ongoing development with our 'Earn while you Learn' scheme and have provided further study to 442 employees in a wide variety of subjects and qualifications ranging from NVQs through to MBAs. We have a focused internal talent programme, which caters for the provision of leadership development for our rising stars through to a Board successor programme which includes gaining IoD professional status.

**Engaging with our employees**

This year, we ran a full employee engagement survey and received valuable feedback from our workforce. Overall engagement was up 2%, which is pleasing in such challenging times. We are fully committed to improving this further with the implementation of a number of key actions in the areas of performance management, career development and communication. We introduced 'honest conversations' training for our line managers to improve their handling of performance reviews. We are improving our employee transfer process to ensure we can maximise career development opportunities across the whole Group and we have revamped the constitution of our Employee Consultative Committee to ensure it is a more effective and engaging two-way discussion forum.

# Performing responsibly continued

## Costain Cares – Relationships continued

### Reward and recognition

In February 2012, we hosted our Achieving Excellence Awards which recognise the outstanding performance and contributions of individuals. The Awards attracted a record number of nominations, 1,545 in total.

### Customers: Providing sustainable solutions and the highest standards of service for our customers

Our customers' needs are at the core of our business. 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. We undertake regular customer satisfaction surveys, where we ask our customers to rate our performance against core values such as safety, health and environment, quality, delivery, subcontract management, and relationships. Over the past five years, we have received consistently high scores and, in 2011, achieved an average score of 81%.



# 81%

We continue to achieve consistently high customer satisfaction scores.



In February 2012, we hosted our Achieving Excellence Awards.

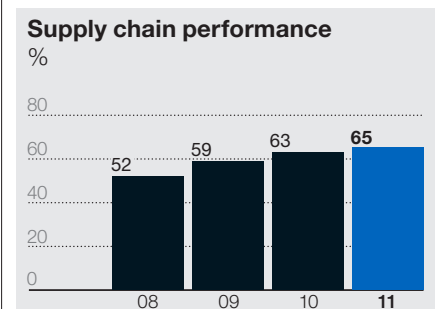
### Supply chain: Operating a collaborative, responsible supply chain where our partners support us in delivering efficient, innovative and sustainable solutions

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

In 2010, we introduced our Responsible Procurement Policy, which outlined our ongoing commitment to the responsible management of our supply chain. In 2011, to ensure we adopted consistent and improving standards within our supply chain, the Group commenced the rollout of an industry recognised accreditation scheme, delivered by a reputable outsource provider, Achilles. To date, 59% of our preferred and strategic supply chain partners have registered with Achilles and we have set a target to increase this in 2012.

Throughout 2011, our relationship managers and supply chain sponsors have continued to develop and enhance

relationships with our supply chain partners by holding regular business to business meetings and encouraging openness and transparency. We undertake regular performance reviews with our supply chain partners, discussing performance in areas such as supervision, competency, communication and teamwork, cost, quality and innovation, and health, safety and environment. In 2011, we achieved an average score across the Group of 65% with the notable success that 68 suppliers achieved over 80%. The objective is to ensure all key suppliers have a performance of greater than 50%. We also actively encourage 360-degree feedback based on the criteria outlined in the performance reviews. This feedback is used to determine what either party can improve or change to enable mutual goals to be achieved.



# 25%

Increase in supply chain performance in the last four years.

During 2011, we worked with several customer groups to pursue practical solutions that address the economic, social and environmental challenges presented by procuring from a global market. Ensuring our supply chain complies with legislation, recognised standards and are competent is a task the Group, in line with our customer base, is committed to delivering.



We successfully met our 2011 target, increasing the percentage of waste diverted from landfill to 89%.

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**Costain Cares – Our Environment**

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

We will work with our customers and supply chain to protect and where possible enhance the natural environment by:

**Climate change: reducing our impact on climate change**

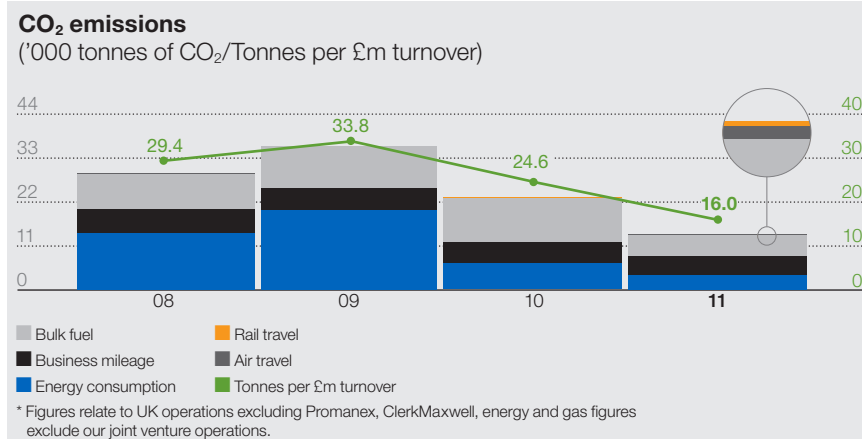
We remain committed to reducing our measured carbon emissions by 50% by 2020, compared to our 2008 baseline. We are pleased to report that, in 2011, we achieved a 35% reduction compared to 2010.

We continue to improve the way we measure our carbon emissions to ensure our results are as accurate as possible. Under the Carbon Reduction Commitment Energy Efficiency Scheme, we were required

to report our energy usage and associated carbon emission figures to the Environment Agency.

In 2012, we hope to further reduce our emissions and improve our position on the Carbon Reduction Commitment league table. We will work with our customers, delivering low-carbon solutions to help them meet their reduction aims and objectives. Sharing this knowledge and our successes both internally and within the industry as a whole is also vital.

**35%**  
Reduction in measured emissions, compared to 2010.



**Conserving natural resources: through effective waste management, minimising water consumption and sustainably sourcing materials**

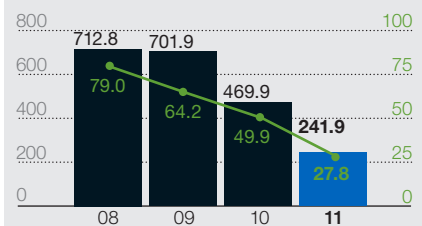
We constantly look for ways to conserve resources and use them more efficiently through good design, reducing and recycling waste, conserving water and using of sustainable materials.

**Waste management**

We continue to focus on waste management and the reduction of waste produced from all our activities. We successfully met our 2011 target, increasing the percentage of waste diverted from landfill to 89%. We are also pleased to report a reduction in tonnes of waste produced as a result of our activities. This has been achieved by careful planning of operations and giving due consideration to eliminating, reducing or reusing all potential waste wherever possible.

**Waste removed from site**

(’000 tonnes of waste/Tonnes per £100,000 turnover)



\* Figures relate to UK operations, excluding Promanex, ClerkMaxwell and our MAC joint ventures.

**44%**  
Reduction in waste removed from site per £100,000 turnover, compared to 2010.

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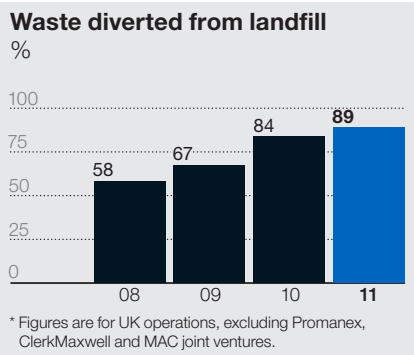
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# Performing responsibly continued

## Costain Cares – Our Environment continued



**89%**  
Waste diverted from landfill.

Reducing our waste and the associated environmental impact is important to us and our customers alike and we will strive to ensure our performance improves year on year. We will continue to work with our customers and supply chain to identify solutions to eliminate waste via early planning and design and to increase opportunities for waste to be diverted from landfill. In 2012, we will target a further increase in the percentage of waste diverted from landfill and reduction in total waste produced compared to turnover.

**Water management**

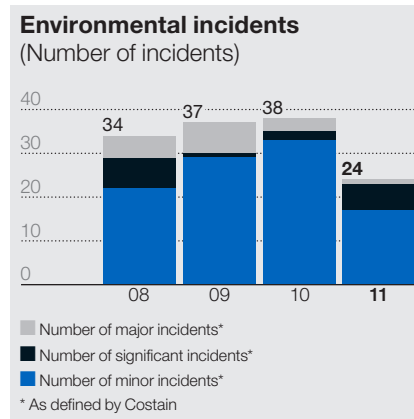
Obtaining a greater understanding of water usage as a result of our activities is a key driver, in 2012 which will help us to target areas for reduction with greater efficiency. We will also assist and provide solutions to our customers to enable them to reduce their water consumption.

**Sustainably sourcing materials**

Working with our supply chain, we aim to target high impact materials and seek alternative, more sustainable materials with a lower environmental impact. We want to ensure we learn and share best practices with our supply chain.

**Protecting the environment**

We are committed to minimising our impact on the environment and reducing our environmental incidents year on year. We actively encourage the reporting of all environmental incidents to ensure that lessons learnt are shared across the business to prevent recurrence. In 2011, we saw a 36.8% reduction in reported environmental incidents compared with 2010.

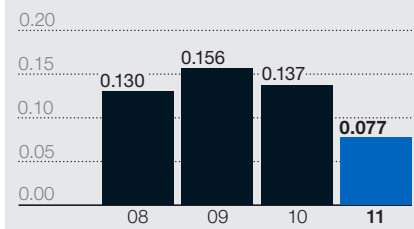


**37%**  
Reduction in reported environmental incidents over the year.

In 2011, we reviewed our definition of environmental incidents to simplify our reporting procedure and ensure that, where possible, it is aligned to that of our customers and the regulator. We have developed an Environmental Incident Frequency Rate ('EIFR') that enables us to track our impact compared to the volume of our activities and is normalised against working hours.

**Environmental Incident Frequency Rate**

(Number of environmental incidents per 100,000 man hours)



**44%**  
Reduction in EIFR in the last year.

Pollution prevention and the associated impacts will continue to be a focus area in 2012. It is important to educate all our stakeholders to ensure they are aware of potential environmental risk and how to prevent incidents occurring in the first place. We are working with Construction Skills and other members of the UK Construction Confederation to establish a standard for environmental training within the construction industry with a view to running externally accredited environmental awareness courses.

In 2011, we developed our Costain Cares vision for 2014, setting ambitious goals and targets...

**Find out more:**

**2011 highlights**  
on pages 02 to 05

**Divisional performance**  
on pages 28 to 30

**Costain Cares**  
on pages 31 to 37

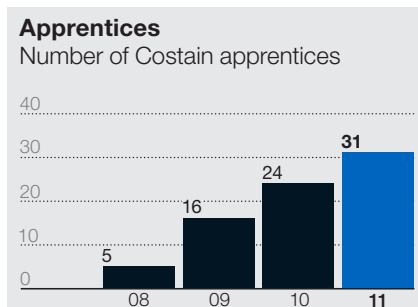
**Costain Cares – The Future**

**We have a key role to play in helping the UK economy flourish. The benefits of investment in infrastructure today will be felt for many years to come.**

**Developing Skills for the Future**

We recognise the importance of engaging with schools, colleges and universities to ensure we can attract the best young talent into our organisation and build a pipeline for the future. In 2011, we refreshed our 'Building Awareness' programme, which focuses on raising awareness of the types of careers available and skills required to join the engineering industry. Our construction and STEMNET ambassadors continue to visit schools, colleges and universities to engage with young people directly and, in 2011, we offered inspirational work experience to 95 individuals. We have set a target to increase the number of work experience placements we offer across the Group in 2012.

We are also successfully rebuilding a strong apprentice programme, with 31 apprentices currently on level 3 frameworks and we plan to increase both the numbers and types of apprentices in 2012.



**31**  
Apprentices on our apprenticeship programme.

Through our patronage of The Prince's Trust and programmes with London Probation Service supporting ex-offenders, we continue to support young people who are not in employment, education or training ('NEET').

**Innovation**

Innovation underpins our strategy and will contribute to our growth, productivity and competitiveness. We are committed to providing intelligent solutions to our customers that will help them achieve their ambitions and aspirations.

**Contribute to economic growth through supporting our supply chain including small and medium size enterprises**

With the UK's SMEs (small and medium sized enterprises) providing 60% of private sector jobs and accounting for half of all private sector turnover they are crucial to economic growth (figures taken from the CBI website). In recognition and support of this, we are committed to ensuring our supply chain is accessible to a diverse supplier base, including SMEs, and that we support SMEs within our supply chain, empowering them to achieve their potential.

**Costain Cares: Our vision for 2014**

In 2011, we developed our Costain Cares vision for 2014, setting ambitious goals and targets against which we will measure our performance and drive continual improvement. For more information and to download a copy of our Costain Cares vision, please visit our website at [www.costain.com](http://www.costain.com).



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# Principal risks

## Strategic and Financial Risk

### Risk and Impact

### Mitigation

#### Economic outlook

Uncertain outlook for the UK and global economy, including the extent of any changes to government and international regulation, taxation and interest rates, may impact the Group's ability to win work and deliver forecast returns. The uncertain economic outlook also affects our customers' ability and confidence to place orders, potentially impacting the Group's level of opportunities.

The Group 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 Group has set out a clear strategy to target customers whose spending plans are driven by national need, regulatory commitments or essential maintenance requirements.

#### Change of Government Policy on spending

Certain of the Group's operations are dependent on government policy with regard to improving public infrastructure and services. Any reduction in government investment and funding would be likely to affect the Group's future revenues and profitability adversely.

Key factors that may affect the Group strategy are kept under regular review by senior management and action taken where potential future workload shortfalls are identified.

The UK Government identified in its 2011 Autumn Statement an increase in infrastructure investment which will assist the Group in its aim to meet national needs.

#### Competition

The failure by the Group to compete effectively, resulting in a failure to win work in a competitive market, could reduce the Group's revenue, profitability and cash flow.

The Company's strategy of targeting 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 services across engineering consultancy, construction and operations and maintenance and to provide innovative cost-effective solutions will also provide it with a competitive edge.

#### 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 £39.7 million net of 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 2011 valued the scheme's assets at £547.9 million and liabilities of £600.8 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. The next actuarial valuation is due on 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 advisors, as necessary.

#### Acquisitions

Failure to integrate successfully an acquired business.

Full due diligence is carried out before any acquisition is made. Integration plans are put in place and managed by a dedicated team.



# Operational Risk

Risk and Impact	Mitigation
<p><b>Operational delivery</b>                      Failure to follow Best Practice: Projects are not delivered to time, cost, quality or appropriate health and safety and environmental standards and therefore do not meet customers' expectations. Failure to follow Company Standards, Policies, Procedures and Guidelines could adversely affect the Group's reputation and/or expose the Group to financial liabilities and adversely affect the operational, financial and share price performance.</p>	<p>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.</p> <p>Work on site is audited by in-house specialists and reports prepared so that corrective action can be taken.</p> <p>Regular Health &amp; Safety visits 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.</p>
<p><b>Loss of IT systems</b>                      Failure of IT systems and failure to manage and/or integrate IT systems could cause financial loss to the Group and expose the Company to breaches of legislation and fines.</p>	<p>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.</p>
<p><b>Subcontractor/supply chain and customer failure</b>                      If a subcontractor or supplier of goods or services fails financially or is responsible for late or inadequate delivery or below quality work it could damage the Group's reputation and/or cause it to suffer financial losses. If a customer fails financially, the Group could suffer financial losses.</p>	<p>The Company seeks to ensure that it is not over-reliant on any one subcontractor or supplier. 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 issues or cause for concern.</p> <p>The Company focuses on targeting and working with blue-chip customers in sectors whose spending activity is underpinned by strategic national need, regulatory commitments or essential maintenance requirements.</p>
<p><b>People</b>                      Failure to attract, develop and retain highly skilled management or personnel may limit the Group's ability to grow the business as anticipated.</p>	<p>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.</p> <p>Pay and conditions of employment are also regularly reviewed against the prevailing market and benchmarked against competitors to ensure that the Company remains competitive for all levels.</p>

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# Key performance indicators

The Group uses a range of performance indicators across its business units. These start with a formal three-year business plan that sets out clear strategic targets and objectives and which forms the basis of the budget for the following financial year.

The Board considers that the following Non-financial and Financial key performance indicators are the most effective measures for monitoring its objectives:

Non-financial				
KPI	Target	2011	2010	2009
<b>Accident Frequency Rate ('AFR')</b>	<b>To continually improve safety performance with a zero tolerance approach</b>	0.11	0.15	0.16
<p>Safety is the number one priority. Within the Company there is both a corporate and 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, occupational diseases and specified dangerous occurrences</p>		<p>reportable under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 1995 per 100,000 of hours worked. The further improvement achieved in 2011 reflects the continued attention given to all areas of safety and represents upper-quartile safety performance in the construction sector.</p>		
<b>Staff turnover</b>	<b>To provide initiatives and working conditions in order to retain key staff</b>	7.0%	5.1%	2.9%
<p>The retention of staff is fundamental in delivering a quality service to customers. The Group undertakes a number of important initiatives to retain key staff, including closely managing their career development. Clear action plans are in place to address items such as customer satisfaction,</p>		<p>health and safety, reward, training and development and job satisfaction. The Group uses a 'voluntary leavers' turnover rate to monitor staff retention. In 2011, staff retention was very strong compared to long-term industry norms.</p>		
<b>Supply chain performance</b>	<b>Average key supplier performance score of greater than 50%</b>	65%	63%	59%
<p>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 &amp; 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 means</p>		<p>to discuss with each supplier their performance and to put in place actions to improve performance or, if appropriate, reduce the amount of work performed using that supplier. In 2011, the average key supplier performance score continued to improve. The objective is to ensure that all key suppliers have a performance of at least 50%. The Group has also implemented an external accreditation system called Achilles (Building Confidence) for its strategic and preferred supply chain members.</p>		

## Financial

KPI	Target	2011	2010	2009
<b>Adjusted operating profit</b>	<b>In line with business plan</b>	<b>£24.1m</b>	<b>£17.4m</b>	<b>£22.0m</b>

The level of adjusted operating profit (before acquisition related other items) 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 sale of assets and joint ventures. The Group's operating profit in 2011 increased

as a result of the strong performance in the Group during the year. The operating profit in 2010 reduced in comparison to 2009 as a result of additional share based payment costs and a lower level of project completion bonuses.

<b>Adjusted profit from operations</b>	<b>In line with business plan</b>	<b>£23.6m</b>	<b>£29.4m</b>	<b>£20.8m</b>
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The level of adjusted profit from operations (before acquisition related other items) is a key measure of performance across all areas and divisions of the Group. The profit from operations for each segment of the business is reported in detail in the Business review section of the Annual Report. The Group's

profit from operations in 2011 decreased compared to 2010 due to the significant profit of £11.2 million from the transfer of assets into The Costain Pension Scheme in 2010. Excluding this item, the profit from operations has increased on a like-for-like basis from £18.2 million to £23.6 million.

<b>Adjusted profit before tax</b>	<b>In line with business plan</b>	<b>£25.5m</b>	<b>£27.9m</b>	<b>£18.1m</b>
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Adjusted profit before tax is a key measure for the Group and incorporates the interest from cash deposits held and the IAS 19 pension interest. The reported profit before tax in 2010

included the significant profit of £11.2 million from the transfer of assets into The Costain Pension Scheme.

<b>Order book</b>	<b>To build a strong order book in line with strategy</b>	<b>£2.5bn</b>	<b>£2.4bn</b>	<b>£2.6bn</b>
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The level of secured orders on which work is to be carried out is a key measure for achieving continued profitability and growth. At the end of 2011, the order book for the Group has

increased from the level at the start of the year, reflecting good contract awards during the year.

<b>Net cash balance</b>	<b>Maintain a net cash balance at an appropriate level to suit the business requirements</b>	<b>£140.1m</b>	<b>£144.3m</b>	<b>£120.5m</b>
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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 reduction in the 2011 year-end cash balance compared to 2010 is due to expenditure in the year on two acquisitions.

The operating cash position, excluding the acquisitions made, increased in the year. The average month-end cash balance for the Group during 2011 was £130.4 million compared to £116.0 million in 2010.

# Group Finance Director's review

## Focused on growth and delivering shareholder value

**Costain further strengthened its financial position during the year. Our stakeholders require us to be able to demonstrate a strong financial covenant, given our strategic focus on major customers and their increasingly large and longer-term contracts.**

Operating profit, before other items, for the year increased by 38% to £24.1 million (2010: £17.4 million).

Profit from operations, before other items, for the year was £23.6 million (2010: £29.4 million).

The other items referred to above relate to the two acquisitions completed during the year and are the amortisation of acquired intangible assets of £0.9 million (2010: £Nil) and employment related acquisition consideration of £0.7 million (2010: £Nil).

Profit before tax for the year ended 31 December 2011 was £23.9 million (2010: £27.9 million) on revenue (including the Group's share of joint ventures and associates) of £986.3 million (2010: £1,022.5 million).

Basic earnings per share amounted to 29.2 pence (2010: 36.4 pence per share).

In 2010, a profit of £11.2 million was realised on the transfer of the Group's interest in a portfolio of six PFI investments into The Costain Pension Scheme at an agreed valuation of £22.0 million.

The order book increased during the year to £2.5 billion (2010: £2.4 billion), as the Group secured a number of new contracts and extensions including the London Bridge station redevelopment for Network Rail, AMP 5 contracts for Northumbrian Water and Severn Trent, Evap D at Sellafield, Centrica Easington gas plant upgrade, A465 road upgrade for the Welsh Government and the Paddington and Bond Street Crossrail redevelopment projects.

### Acquisitions

In line with our strategy to expand the services offered to customers, the Group made two acquisitions during 2011.

In April, the Group purchased ClerkMaxwell, an Aberdeen based upstream oil and gas engineering company. Initial cash consideration was £3.2 million. Deferred cash consideration payments, based on a percentage of the notional future value of ClerkMaxwell on the basis of an 8.0 times multiple of EBITDA ('Notional Future Value'), may also be payable shortly after completion of the financial years ending 31 December 2012, 2013 and 2014. The total percentage of Notional Future Value payable over the three years ending 31 December 2014 is 49% and an element is linked to continued employment.





**Tony Bickerstaff** Group Finance Director

In August, Costain acquired Promanex, an industrial support services business providing facilities management, installation, repair and maintenance and general asset management in a number of high-growth markets such as power, petrochemicals and nuclear. The consideration for the acquisition, together with management retention payments, was £16.2 million. In addition, the business was acquired with normalised net debt of £2.4 million.

#### Interest

Net finance income amounted to £1.9 million (2010: £1.5 million expense).

Net interest income from bank deposits and other loans and receivables amounted to £0.1 million (2010: £0.1 million). In addition, the net finance income included the difference between the expected return on the pension scheme's assets of £32.3 million (2010: £29.7 million) and the interest cost on the present value of the pension scheme's liabilities of £30.5 million (2010: £31.3 million) being a net income of £1.8 million (2010: £1.6 million expense).

In accordance with IAS 19, the pension scheme deficit position was reassessed as at 31 December 2011. As a consequence of the accounting reassessment, the net pension interest is expected to be an interest expense in 2012 due to the change in the market conditions.

#### Tax

The Group's effective rate of tax was 21.8% of profit before tax (2010: 17.2% which included an element of tax relief on the PFI asset transfer into The Costain Pension Scheme). There were benefits during the year arising from Research & Development tax relief claims, pension contributions incurred in 2010 but tax deductible in 2011 and a decrease in brought forward temporary timing differences, being the utilisation of capital allowances, taxed provisions and tax losses.

#### Dividend

The Board has recommended a final dividend for the year of 6.75 pence per share (2010: 6.25 pence per share) to bring the total for the year to 10.0 pence per share (2010: 9.25 pence per share), an increase of 8%.

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 reduced in the year to £30.8 million (2010: £37.6 million). The profit for the year amounted to £18.7 million and other comprehensive expense to £22.6 million. The movements are detailed in the consolidated statements of comprehensive income and expense and changes in equity in the financial statements. The most significant element was the increase in the Group's pension scheme deficit.

#### Pensions

As at 31 December 2011, the Group's pension scheme deficit in accordance with IAS 19, net of deferred tax, was £39.7 million (2010: £28.9 million). The scheme deficit position has increased primarily as a result of a reduction in the discount rate, based on corporate bond yields, used to calculate the liabilities.

A full actuarial valuation of The Costain Pension Scheme ('CPS') was performed by the Scheme Actuary as at 31 March 2010 and a recovery plan that is expected to eliminate the deficit over a period of less than ten years was agreed with the Trustee of the Scheme. This agreement, which incorporates the £22.0 million transfer of the PFI investments, resulted in a corresponding reduction in the Group's future annual cash contributions into the scheme over a thirty-nine month period which started with effect from 1 January 2011.

# Group Finance Director's review continued

The agreement also incorporates the ongoing commitment to match dividend payments with an equivalent cash contribution to the Scheme.

The Group's defined benefit pension scheme was closed to future accrual from 30 September 2009. Costain now operates only a defined contribution scheme for all employees from that date.

Since the year-end, the Board has agreed with the Trustee of the CPS to transfer the Group's interest in a portfolio of two PFI investments into the CPS, at an agreed valuation of £20.3 million, which represents an effective discount rate of circa 7%. As a result of the transaction, the accounting profit realised on the transfer of the assets is £10.2 million in 2012.

Furthermore, the Group has instigated a liability risk management exercise. The Group is in the process of issuing Enhanced Transfer Value and Pension Increase Exchange offers to the members of the CPS. These initiatives, which potentially include every member of the CPS, will offer each individual greater choice and flexibility regarding their pension entitlement, and will also reduce the overall pension liabilities and risk remaining within the scheme. The level of liability reduction will depend on the take-up of the offer by members and financial conditions at the point the entire exercise completes (expected to be May 2012). At this stage, it is estimated that the initiatives could reduce the Scheme liabilities by approximately £50 million, and could incur a one-off accounting cost, estimated at £6 million, to be expensed in 2012.

Together, the above actions are estimated to reduce the pension deficit by approximately £16 million, with an associated potential reduction in annual deficit contributions, following the next triennial actuarial valuation of the CPS which is due as at 31 March 2013.

## Cash Flow and Borrowings

The Group has a strong positive net cash balance, which was £140.1 million as at 31 December 2011 (2010: £144.3 million) and included £1.6 million of borrowings (2010: £1.7 million) and cash held by jointly controlled operations of £33.6 million (2010: £33.8 million).

As set out in the consolidated cash flow statement, during the year, the Group had strong operating cash flow offset by investment in acquisitions and payment of dividends and matching pension deficit contributions. The average month-end cash balance during 2011 was £130.4 million (2010: £116.0 million).

The cash position is affected by monthly and contract specific cycles and in order to accommodate these cyclical flows, the Group seeks to maintain a base cash balance.

## Key Risks and Uncertainties

The principal risks and uncertainties of the business, and the factors which mitigate these risks, are set out in the Group's Annual Report and include the economic outlook, change of government policy on spending, competition, pension liabilities, operational delivery, loss of IT systems, supply chain and customer failure and people retention. The Board continuously assesses and monitors these risks and the Chairman's statement, Chief Executive's review and business and operations review in these financial statements include consideration of uncertainties affecting the Group.

## Accounting policies and significant areas of judgment and estimation

A summary of the significant accounting policies of the Group is set out in the Notes to the financial statements.

There has been no significant change to the accounting policies in the year and there is no material effect on the financial statements of new accounting standards adopted in the period.

The Notes to the financial statements also include the significant areas of judgment and estimation used in preparation of the financial statements.

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

## 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 2011, the Group renegotiated its contract bonding and banking facilities with its relationship banks and surety companies. The facilities were increased to £465 million and extended to a maturity date of 30 September 2015.

The Group has a strong positive net cash balance, which was £140.1 million as at 31 December 2011...

### Find out more:

**2011 highlights**  
on pages 02 to 05

**Chairman's statement**  
on pages 06 and 07

**Chief Executive's review**  
on pages 10 to 13

#### 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.

#### 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 and retained profits. 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 transactional currency exposure arising from subsidiaries' commercial activities overseas and, 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 holds financial instruments for two main purposes: to finance its operations and, currently only within its PFI investments, to manage the 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. With the Group's cash balances and low level of borrowings, 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. Within the investments in joint ventures and associates, interest rate movements will affect the value of swaps classified as cash flow hedges and this will impact the Group's equity.



**Tony Bickerstaff**  
Group Finance Director

7 March 2012

# Board of Directors

## Experienced leadership



**David Allvey (67)**  
**FCA, ATII**<sup>3</sup>  
 Non-Executive Chairman

**Appointment:** November 2001

**Skills and experience:** David 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, previous roles include Group Finance Director for BAT Industries plc, Barclays Bank plc and Chief Operating Officer for Zurich Financial Services, member of the UK Accounting Standards Board, member of the International Accounting Standards Insurance Group, Non-Executive Director of Thomas Cook plc (2007 to 2012), Senior Non-Executive Director of Intertek Group plc (2002 to 2011) and Senior Non-Executive Director of William Hill plc (2002 to 2011).

**External appointments:** Chairman of Arena Coventry Ltd, Senior Independent Director of Friends Provident Group plc.



**Andrew Wyllie (49)**  
**FREng, BSc, MBA, FICE, CEng**  
 Chief Executive

**Appointment:** September 2005

**Skills and experience:** Formerly Managing Director of Taylor Woodrow Construction Ltd (2001 to 2005) and a member of the Taylor Woodrow plc Executive Committee. Andrew joined Taylor Woodrow in 1984 and worked on major contracts in Africa, the Middle East, the Far East and the UK.

**External appointments:**  
 Non-Executive Director of Scottish Water.



**John Bryant (68)**  
**MA (Cantab), FREng, FIM, CEng, DSc (Hon)**<sup>1 2 3</sup>  
 Senior Independent Director

**Appointment:** February 2002

**Skills and experience:** John was appointed as Senior Independent Director in January 2008. Previous roles include Chief Executive of Corus Group plc (1999 to 2000), Chief Executive of British Steel plc (1999), Executive Director of British Steel plc (1995 to 1999) and Non-Executive Director of Bank of Wales plc (1996 to 2001).

**External appointments:**  
 Non-Executive Director, Welsh Water plc and Glas Cymru Limited both since 2001, Chairman of Actoris Group Ltd.



**Tony Bickerstaff (47)**  
**FCCA**  
 Group Finance Director

**Appointment:** June 2006

**Skills and experience:** Formerly Finance Director of Taylor Woodrow Construction Ltd (2001 to 2006). Tony joined Taylor Woodrow in 1982 and undertook a number of senior roles both in the UK and overseas including Divisional Operations Director prior to becoming Finance Director in 2001.

### Find out more:

#### Corporate Governance statement

on pages 50 to 57

#### Other statutory information

on pages 58 to 62

#### Directors' remuneration report

on pages 63 to 70

#### Directors' responsibilities statement

on page 71





**James Morley (63)**  
**BSc, FCA**<sup>1 2 3</sup>  
 Independent Non-Executive Director

**Appointment:** January 2008

**Skills and experience:** James became Chairman of the Audit Committee upon his appointment in January 2008. He is a Chartered Accountant with some 27 years' experience as a board member of both listed and private companies. Previous roles include Chief Operating Officer of Primary Group Ltd (2006 to 2007), Group Finance Director of Cox Insurance Holdings plc (2002 to 2005), Group Finance Director of Arjo Wiggins Appleton plc (1999 to 2001), Group Executive Director Finance of Guardian Royal Exchange plc (1990 to 1999), Deputy Chief Executive and Finance Director of Avis Europe plc (1976-1989), Non-Executive Director of the Bankers' Investment Trust plc (1994 to 2008), Non-Executive Director of WS Atkins plc (2001-2009) and Non-Executive Director of Trade Indemnity Group plc (1991-1996).

**External appointments:**

Non-Executive Director of The Innovation Group plc, Clarkson plc, Speedy Hire plc and BMS Associates Ltd and Non-Executive Chairman of Acumus Ltd.

**Notes**

<sup>1</sup> Member of Remuneration Committee

<sup>2</sup> Member of Audit Committee

<sup>3</sup> Member of Nomination Committee



**Michael Alexander (64)**  
**BSc, MSc, FIChem.E,**  
**FIET, FIGM, CEng, CSci**<sup>1 2 3</sup>  
 Independent Non-Executive Director

**Appointment:** July 2007

**Skills and experience:** Mike 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) and Non-Executive Director of the Energy Savings Trust Ltd (1994-2001).

**External appointments:** Independent Non-Executive Director of the UK Payments Council; Executive Director of Lexican Ltd, member of the European Advisory Board for Landis & Gyr, Senior Advisor at EGS Energy Ltd, Deputy Chairman and Senior Independent Director of Russian Platinum Ltd.



**Samer G. Younis (50)**  
**BSc, Commander of the**  
**Knights – Italian Solidarity Star**<sup>3</sup>  
 Non-Executive Director

**Appointment:** June 2009

**Skills and experience:** Samer was appointed as a Non-Executive Director in June 2009 and is Vice Chairman and Managing Director of Kharafi National Group; Board Member of ABJ Engineering and Contracting Co KSCC (Kuwait), Utilities Development Company (Kuwait), Kuwait Jordanian Holding Company (Jordan), SSH Consultants (Kuwait), Global Clearing House Systems (Kuwait), Emirates Utilities Company Holding (UAE) and Heavy Engineering Industries & Shipbuilding Co (HEISCO) (Kuwait); and a Trustee of the Arab Forum for Environment and Development.

**Tracey Wood (42)**  
**LLB**  
 Legal Director and  
 Company Secretary

**Appointment:** June 2011

**Skills and experience:** Tracey joined the Company in February 2006. She has a construction and commercial law background and was formerly a partner at Hammonds. She has responsibility for legal, secretariat and human resources.

## 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 other members of the Executive Board are:

**Tony Bickerstaff**  
 Group Finance Director

**Patrick Bruce**  
 Group Commercial Director

**Alistair Handford**  
 Director Group Investments

**Martin Hunter**  
 Group Financial Controller

**Darren James**  
 Managing Director – Infrastructure

**Alan Kay**  
 Managing Director – Environment

**Charles Sweeney**  
 Managing Director – Energy & Process

**Alex Vaughan**  
 Corporate Development Director

**Tracey Wood**  
 Legal Director and Company Secretary

# Corporate Governance

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

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**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

**We believe that great companies are built on the foundation of trust. By providing open and transparent information, together with strong compliance with both the spirit and letter of the law, trust is earned by managing the business in a responsible and sustainable way.**

At Costain, we are committed to robust governance practices and accountability. As we mentioned in our 2010 Annual Report, this year, we are complying with the new disclosure requirements as set out in the UK Corporate Governance Code 2010. These principles are considered to be central to the effective management of the business and to maintaining the confidence of the investors.

During the year, the Board has made considerable progress on a number of different issues, which are detailed within the Governance report. We have also taken part in an externally facilitated independent Board evaluation.

Our Board is responsible for providing strong leadership for the Costain Group. Effective leadership is realised through collaboration between the Board and the Executive team and 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.

Governance goes well beyond the boardroom. At Costain, we operate with diligence and discipline across the whole business and believe it is important to assess continually how we do things. Encouraging dialogue with stakeholders helps to guide and shape our approach to governance and risk management.

We continually monitor the composition of the Board to ensure we have the right level of skills and expertise. The Directors have a strong understanding of our business and sector and bring valuable insight and experience to the table.

Our Board is ultimately responsible for the success of Costain and we are committed to the highest standards of corporate governance that will enable us to achieve our vision of becoming one of the UK's top engineering solutions provider.

**David Allvey**  
Chairman

# Corporate Governance statement

**The Board of Directors of Costain Group PLC is committed to achieving the highest standards of Corporate Governance and to managing operations in accordance with the principles set out in the UK Corporate Governance Code (the 'Code')<sup>1</sup> adopted by the Financial Reporting Council in June 2010 to which the Company is subject.**

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

## Responsibilities

**The Board has adopted a schedule of matters specifically reserved to the Board for its approval.<sup>2</sup>**

The principal matters reserved to the Board include:

Reviewing the environmental and health and safety performance of the Group.

Setting Group strategy.

Approving the annual operating and capital expenditure budgets and material changes to them.

Reviewing performance in light of the Group strategy, objectives, business plans and budgets and ensuring that any necessary corrective action is taken.

Supervising the Group's operations and financial performance.

Approving major acquisitions and divestments.

Reviewing the Group's systems of financial control and risk management.

Ensuring that appropriate management development and succession plans are in place.

Approving appointments to the Board and Executive Board and the appointment of the Company Secretary.

Approving policies relating to Executive Directors' remuneration and the severance of Executive Directors' service agreements.

Ensuring that a satisfactory dialogue takes place with shareholders.

<sup>1</sup> A copy of the Code is publicly available at [www.frc.org.uk](http://www.frc.org.uk).

<sup>2</sup> A copy of the schedule is available on the Company's website at [www.costain.com](http://www.costain.com).



## Achievements of 2011

**What has the Board done during the year?**  
 Set out below is a summary of the key matters undertaken by the Board in 2011:

<b>Strategic discussions and investment</b>	The Board devoted increased time to deeper and broader discussions on key strategic issues and took part in a number of Board workshops focused on strategy over a three-year cycle. These workshops were attended by members of the Executive Board. The Board has also facilitated more opportunities for informal Board discussions on strategic issues. The Board has engaged in some significant strategic developments during the year, including the acquisitions of ClerkMaxwell and Promanex.
<b>Monitoring risk</b>	The Board has assessed the effectiveness of the Group's reporting controls and ensured that the Group's risk profile reflects the Company's strategic objectives.
<b>Visits</b>	The Board attended senior leadership team gatherings and visited a number of sites across the country to ensure directors maintain an understanding of the operational issues that affect the Group.
<b>Training</b>	The Audit Committee discussed the Company's response to the Bribery Act 2010 and all Board members undertook training in this area. The Board has also overseen the updating of the Company's Ethical Business Conduct Policy, PLC Board and Committee Procedures Policy and Share Dealing Code.
<b>Evaluation</b>	The Board took part in an externally facilitated independent Board evaluation. Further details of the external evaluation can be found on page 53.
<b>Corporate Responsibility ('CR')</b>	The Board developed a more strategic approach to CR with the launch of 'Costain Cares'. The Company now has a dedicated CR Director and monitors progress on a regular basis.

## Board and Committees

### The role of the Board

The Group 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.

### Who is on the Board?

The Board currently comprises two executive directors and five non-executive directors of whom one is the Chairman, three are independent non-executive directors (one being the Senior Independent Director) and one is a nominee non-executive director. The nominee non-executive director is nominated by our major shareholder, Mohammed Abdulmohsin Al-Kharafi & Sons WLL.

A list of the individual directors and their biographies are set out on pages 46 to 47. 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 chart on page 52.

The Board recognises the importance of greater diversity (not just gender specific) in the boardroom and throughout the business. 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.

Overview

Business review

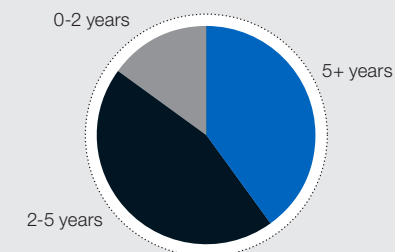
Corporate Governance

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# Corporate Governance statement continued

## Length of service: Non-executive directors as at 31 December 2011



## 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, notwithstanding that in the case of Mr Bryant, the Senior Independent Director, he has served on the Board for more than nine years.

By the date of the 2012 Annual General Meeting, Mr Bryant, the Senior Independent Director, will have served on the Board for ten years and, as a result, his continued independence has been the subject of particular scrutiny. The Nomination Committee has given detailed consideration to Mr Bryant's independence. Mr Bryant continues to demonstrate excellent stewardship as Senior Independent Director. As a result of his length of service and commitment, he provides an in-depth knowledge of the Group that is invaluable to the Board. Accordingly, the Board takes the view that Mr Bryant has retained independence of character and judgment and this has not diminished over the period of his tenure.

The Nomination Committee continues to review succession on a regular basis and is currently working with an external search consultant with a view to possible new appointment(s) in the future.

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 appropriate 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 being a member of the FTSE SmallCap index.

## Conflicts

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 interests and has adopted appropriate processes to manage and, if appropriate, approve any such conflict.

## Appointments to the Board and retirement of directors

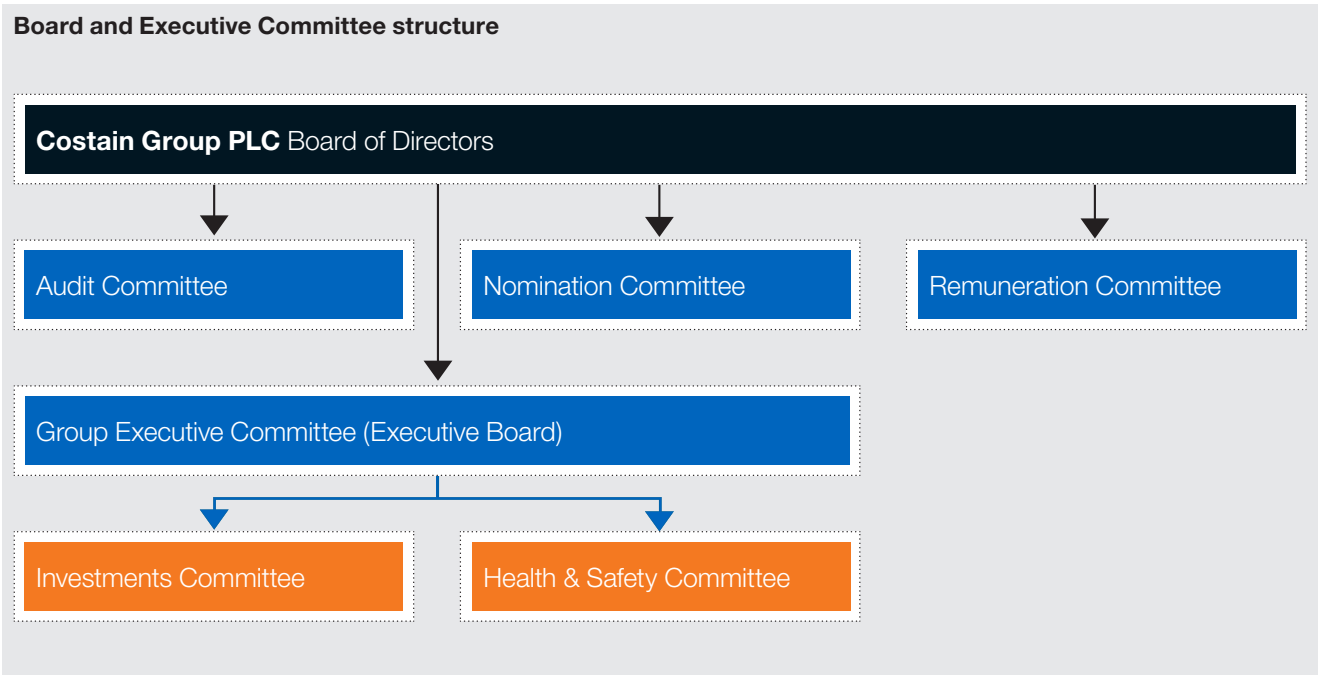
The membership of the Board and biographical details of the executive and non-executive directors are given on pages 46 to 47.

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, Mr Allvey, Mr Bryant and Mr Wyllie will retire by rotation at the next Annual General Meeting and offer themselves for re-election.

The Chairman and independent 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 WLL and the other major shareholder York Place Limited, a subsidiary of UEM Builders Berhad, are each entitled to appoint a non-executive director for so long as those shareholders each hold 7% of the aggregate nominal value of the then issued ordinary share capital of the Company. York Place Limited 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 and be subject to re-election.



**How often does the Board meet?**

The Board holds scheduled meetings throughout the year and meets on an ad hoc basis both physically and by telephone conference as required. During 2011, the Board met formally on eight occasions. Details of the attendance at Board meetings in 2011 are given in the table below:

Board meetings		
Director	A	B
D P Allvey	8	8
A Wyllie	8	8
A O Bickerstaff	8	8
J M Bryant	8	8
M R Alexander	8	8
J Morley	8	8
S G Younis	8	4

- A Maximum number of meetings the director could have attended
- B Number of meetings the director actually attended

Mr S G Younis attended four out of the eight scheduled Board meetings throughout the year due to other work commitments. Mr S G Younis regularly attended board meetings held on an ad hoc basis.

**How do we make sure our Board is effective?**

The Board has established a formal process for the evaluation of the performance of the Board and its principal committees. In 2011, in accordance with best practice, the Board commissioned an independently facilitated Board and Committee review. The review was conducted by SCT Consultants Ltd and each director completed a questionnaire and was interviewed individually on a confidential basis. The review forms part of the regular evaluation and development work conducted by the Board to ensure it continues to improve its overall effectiveness and built on the previous evaluation conducted by SCT Consultants in 2009. The outputs of this external Board and Committee evaluation have begun to inform the Board's action planning for 2012-2013.

During the year, Mr Allvey met with the non-executive directors without the executive directors being present and, as part of the process to appraise Mr Allvey's performance, the Senior Independent Director met with the non-executive directors without the Chairman being present.

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 offsite visits are considered essential to ensure that directors have a thorough understanding of the business operations and issues that affect the Group.

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# Corporate Governance statement continued

In order to discharge their duties, the directors are provided with full and timely access to papers prior to Board meetings and the directors are free to seek any further information they consider necessary. In addition, between Board meetings, non-executive directors have access to the Chief Executive, Group Finance Director and Company Secretary in order to progress the Company's business. The non-executive directors also receive a weekly report from the Chief Executive, monthly management accounts, certain 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 advisors as and when required at the expense of the Group.

The Group's organisation and 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 on page 53. The Board has established committees which are responsible for audit, remuneration, and succession. Each committee plays a vital role in helping the Board ensure 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 membership of each of the Board committees is detailed as follows.

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

## Audit Committee

Audit Committee Members		
Director	A	B
<b>J Morley</b> (Committee Chair)	5	5
<b>J M Bryant</b>	5	5
<b>M R Alexander</b>	5	4

**A** Maximum number of meetings the director could have attended

**B** Number of meetings the director actually attended

Details of the attendance at Audit Committee meetings in 2011 are given in the table above. The Committee's terms of reference are available from the Company Secretary and are published on the Company's website. The meetings of the Committee are normally also attended by the Chairman, the Chief Executive, the Group Finance Director, the external auditors, the Head of Internal Audit and the Group Financial Controller. The Audit Committee regularly meets privately with the external auditors and Head of Internal Audit. The Company Secretary is the Secretary to the Audit Committee.

The Company considered that it had in Mr Morley, as Chairman of the Audit Committee, an appropriate person possessing what the Smith Report describes as recent and relevant experience. Mr Morley, a chartered accountant, was Finance Director, Avis Europe PLC (1976 to 1989), Group Executive Director, Finance, Guardian Royal Exchange Plc (1990 to 1999), Group Finance Director, Arjo Wiggins Appleton Plc (1999 to 2001) and Group Finance Director, Cox Insurance Holdings Plc (2002 to 2005).

## Role of the Audit Committee

In accordance with its terms of reference, the Audit Committee is responsible for:

- monitoring the integrity of the Group's financial statements and any formal announcement relating to the Group's performance;
- monitoring the effectiveness of the external audit process and making recommendations to the Board in relation to the appointment, re-appointment and remuneration of the external auditors;
- ensuring that an appropriate relationship between the Group and the external auditors 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 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.

## Main activities during the year

In 2011, the Audit Committee discharged its responsibilities by performing the following activities:

- reviewing the Group's draft financial statements and interim results prior to Board approval and reviewing the external auditors' detailed reports thereon;
- reviewing the appropriateness of the Group's accounting policies;



- reviewing and setting the Group's non-audit and audit fees;
- reviewing the external auditors' plan for the audit of the Group's financial statements;
- reviewing and monitoring the external auditors' independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements;
- reviewing the internal audit function's work programme, internal audit reports and quarterly reports on its work during the year;
- reviewing the Group's system of internal controls and its effectiveness, reporting to the Board on the results of the review and receiving regular updates on key risk areas of financial control;
- monitoring the process for formally identifying, evaluating and managing any significant risks and opportunities within the business;
- reviewing and monitoring the development of the Group's commercial and financial IT systems;
- supporting the implementation of an anti-bribery policy and training following the introduction of the Bribery Act 2010; and
- undertaking an internal review of the effectiveness of internal audit and our external auditors.

**Non-audit services**

The Audit Committee monitors the non-audit services being provided to the Group by its external auditors, and has developed a formal policy on the provision of non-audit services by the external auditors to check this does not impair their independence or objectivity, and that the Group maintains a sufficient choice of appropriately qualified audit firms. The policy sets out four key principles that underpin the provision of non-audit services by the external auditors: The auditors should not audit their 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.

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

In 2011, KPMG performed a high level of non-audit services in respect of completed and aborted acquisitions and providing tax services. KPMG were 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. The Audit Committee approved the provision of these services in advance and were satisfied that the non-audit services have not impacted on KPMG's objectivity and independence.

**Nomination Committee**

Nomination Committee Members		
Director	A	B
<b>D P Allvey</b> (Committee Chair)	2	2
<b>J M Bryant</b>	2	2
<b>J Morley</b>	2	2
<b>M R Alexander</b>	2	2
<b>S G Younis</b>	2	0

**A** Maximum number of meetings the director could have attended  
**B** Number of meetings the director actually attended

Details of the attendance at Nomination Committee meetings in 2011 are given in the table above. The Committee's terms of reference are available from the Company Secretary and are published on the Company's website.

**Role of the Nomination Committee**

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

**Main activities during the year**

In 2011, the Nomination Committee discharged its responsibilities by performing the following activities:

- directing the external review of Board effectiveness;
- receiving notifications from directors of situations, such as proposed external appointments, in which a potential conflict of interest may arise;
- approving the directors who will offer themselves for re-election at the 2012 Annual General Meeting in accordance with the Articles of Association following detailed consideration of the Board's policy on independence in respect of those directors; and
- reviewing succession planning in respect of the Company's senior management.

**Remuneration Committee**

Remuneration Committee Members		
Director	A	B
<b>M R Alexander</b> (Committee Chair)	7	7
<b>J M Bryant</b>	7	7
<b>J Morley</b>	7	6

**A** Maximum number of meetings the director could have attended  
**B** Number of meetings the director actually attended

Details of the attendance at Remuneration Committee meetings in 2011 are given in the table above. The Committee's terms of reference are available from the Company Secretary and are published on the Company's website.



# Corporate Governance statement continued

## Role of the Remuneration Committee

The role and operation of the Remuneration Committee is set out in the Director's remuneration report on pages 63 to 70.

## Relationship with institutional investors and private investors

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. 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 Mr Bryant, 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, on the views of institutional investors on a non-attributed basis. As a matter of routine, the Board reviews at each meeting a report 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 Chairmen of the Remuneration, Nomination and Audit Committees attended the 2011 meeting and propose attending the forthcoming meeting and 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.

## Internal controls and risk management

### Review of 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 misstatement or loss.

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

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 Turnbull guidance.

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.

### Risk management

The Company has various procedures for identifying and managing risk, including a prequalification and pre-tender review for obtaining approval to bid for a project from the Executive Investments Committee and a specific project risk management procedure which involves a continuous review of risks by the project manager and commercial manager of the project following contract award.

The Company has established a Corporate Risk Register, as well as, sector business Risk Registers, which are monitored and updated regularly. 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 strategic objectives.

For the duration of a contract, the Risk/Opportunity Registers are updated on a monthly basis and the top five risks and opportunities reviewed by Group senior management. Internal Audit conducts site reviews and circulates reports with further follow-up actions and inspections.

The risk management strategy is regularly reviewed and the Group's risks and opportunities compared against those of blue-chip companies. 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 2011, 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, which revisits areas previously subject to audit and provides assurance that accepted recommendations have been implemented effectively. The overall assessment is that a strong risk management culture is continuing to develop within the Group.

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

### **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 operational management systems that are accredited to ISO 9001:2000 which are designed to support management in providing safe construction processes of the highest quality. Implementation and compliance with the management system is monitored and audited by Internal Audit. In order to maintain the Company's accreditation, external audits of the management systems are undertaken twice yearly by the British Standards Institution.

Each Project Manager 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 at 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 & 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 produces a monthly rolling forecast update for the current year which is compared with the annual budget. Each operation'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. The Group Treasurer and Group Taxation Manager 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 of the Company's business dealings. This statement is regularly reviewed and updated as appropriate to ensure compliance with any change in legislation, for example, the Bribery Act 2010. 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.

The Chairman of the Audit Committee reports the outcome of the Audit Committee meetings to the Board and all Board members receive the minutes of all Audit Committee meetings.

# Other statutory information

## The directors submit to the members their Report and Accounts of the Company for the year ended 31 December 2011.

The Directors' Report of the Company for the year ended 31 December 2011 is set out on pages 06 to 72. The Business review (pages 06 to 47), Principal Risks (pages 38 and 39), Key Performance Indicators (page 40 and 41), Group Finance Director's review (pages 42 to 45), Board of Directors section (pages 46 and 47), Corporate Governance statement (pages 50 to 57), Other statutory information (pages 58 to 62) and Directors' remuneration report (pages 63 to 70) are incorporated by reference into this Directors' Report, together with the other sections of the Report and Accounts referred to in the Directors' Report.

### Activities

The principal activities of the Group are Consultancy, Engineering, Construction and Operations and Maintenance. The Group also has a share in a Land Development and Marina Joint Venture in Southern Spain. The progress and prospects of the Group's businesses and the main factors which could affect the future development and performance of the Group are set out in the Business review (pages 06 to 47).

### Fixed assets

The Board is of the opinion that the aggregate market value of the Group's land and buildings is in excess of book value but that this difference is not significant in relation to the affairs of the Group as a whole.

### Profit and dividends

The profit after tax for the financial year ending 31 December 2011 amounted to £18.7 million (2010: £23.1 million). An interim dividend of 3.25 pence per share (2010: 3.00 pence) amounting to £2.2 million (2010: £1.9 million) was paid on 28 October 2011. The directors recommend a payment of a final dividend at the rate of 6.75 pence per share (2010: 6.25 pence) amounting to £4.4 million (2010: £4.0 million). If approved, the dividend will be paid on 25 May 2012 to shareholders registered at close of business on 20 April 2012.

### 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 2011 financial statements as discussed on page 45 of the Group Finance Director's Review and Note 2 of the financial statements.

### Forward looking statements

This Annual Report contains forward looking statements. These forward looking statements are not guarantees of future performance. Rather, they are based on current views and assumptions and involve known and unknown risks, uncertainties and other factors that may cause actual results to differ from any future results or developments expressed or implied from the forward looking statements. Each forward looking statement speaks only as of its particular date.

### Directors and directors' interests

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

In accordance with Article 78 of the Company's Articles of Association and the Code, Mr Allvey, Mr Bryant and Mr Wyllie, being eligible, will offer themselves for re-election at the Annual General Meeting. Mr Allvey and Mr Bryant having been in office for a continuous period in excess of nine years are required to stand for re-election on an annual basis. Mr Allvey and Mr Bryant have letters of appointment with the Company and Mr Wyllie has a service contract with the Company, details of which are set out in the Directors' remuneration report.

With regard to the re-election of Mr Allvey, Mr Bryant and Mr Wyllie, 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 2011, are contained in the Directors' remuneration report, which appears on pages 63 to 70.

### Related party transactions

Details of transactions with related parties undertaken by the Group during the year are disclosed in Note 25 to the financial statements on page 116.

### Incorporation and constitution

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

Costain Group PLC's Articles of Association are available on the Company's website at [www.costain.com](http://www.costain.com).

### 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 2011 was £32,353,462, consisting of 64,706,925 ordinary shares of 50 pence each.

Details of the share capital of the Company can be found in Note 20 on page 112.

The 2008 three-year savings contract in the Company's 2008 Save As You Earn Plan matured in July 2011. As at 31 December 2011, a total of 765,096 shares were allotted to participants who exercised their options to receive shares under the scheme at an option price of £1.96.

The 2007 and 2008 Long-Term Incentive Plans ('LTIP') matured as at 31 December 2010 resulting in the vesting of awards in April 2011 over 351,847 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.

The Company has obtained shareholder approval to offer a 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 2011, 59,673 ordinary shares of 50 pence each were allotted to shareholders in respect of the final dividend for 2010, and 43,377 ordinary shares of 50 pence each were allotted to shareholders in October 2011 in respect of the interim dividend for 2011. Further information on the scrip dividend option is set out on page 118. Details about joining the scrip dividend scheme can also be found on the website [www.costain.com](http://www.costain.com).

#### Major shareholders

As at 5 March 2012, the Company had been notified, in accordance with the Disclosure and Transparency Rules issued by the Financial Services Authority, of the following voting interests in its ordinary share capital:

York Place Limited*	13,810,850	21.34%
Mohammed Abdulmohsin Al-Kharafi & Sons WLL	13,789,490	21.31%
Henderson Global Investors Limited	3,390,310	5.24%
Legal & General Group PLC	2,594,479	4.01%

\* UEM Builders Berhad owns 100% of York Place Limited.

The above holdings are all indirect, being held by nominees on behalf of the beneficial owners.

#### 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.

#### Rights and obligations attaching to shares

Subject to the Companies Act 2006, any resolution passed by the Company under the Companies Act 2006 and other shareholders' rights, shares may be issued with such rights and restrictions as the Company may, by ordinary resolution, decide, or (if there is no such resolution or so far as it does not make specific provision) as the Board may decide. 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 2008, shareholders granted an authority to the directors to allot ordinary shares up to an aggregate nominal amount of £10.47 million, such authority to apply until 7 May 2013. As at 31 December 2011, the only shares that had been allotted were in order to satisfy awards under employee share schemes and the 2010 and 2011 scrip dividends. The directors did not request authority to allot or to buy back any of the Company's shares at the last Annual General Meeting in 2011 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.

#### Corporate Responsibility

The section on Performing responsibly is on pages 26 to 37.

#### Employee involvement

The Company maintains a strong communication network and employees are encouraged to discuss with management matters of interest and issues affecting 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 films and 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 road shows which take place around the country.

The Company also organised a staff engagement survey in 2011, allowing the Company to understand how employees feel about Costain. In December 2011, the Company also launched '[ask.costain.com](http://ask.costain.com)', enabling employees to get involved in two-way communication with the Company.

# Other statutory information continued

The Company has an established Employee Consultative Committee which convenes biannually 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.

Share schemes are an established part of our reward package, encouraging and supporting employee share ownership; in particular, employees currently participate in the Company's Save As You Earn Scheme plan.

## Diversity and Inclusion

The Company is an inclusive employer and promotes equality and inclusion from recruitment and selection, through training and development, and promotion to 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. It is Company policy that people with disabilities should have full and fair consideration for all vacancies. Wherever possible, we endeavour to interview those people with disabilities who fulfill the minimum criteria, and to retain employees in the workforce if they become disabled during employment and to provide specialist training where appropriate. We support our supply chain and encourage their active commitment to our approach on equality and inclusion.

Our customers are looking to us to provide local employment and skills, and to facilitate inclusion on our projects. We continue to work with the UK Contractors Group to deliver an Equality and Diversity Action plan across Costain and to apply local solutions to diversity issues on projects. We assist our customers in their employment and skills agenda by delivering an Apprentice Development Programme and through establishing National Skills Academies.

## Policy and practice on payment of suppliers

As a result of the nature of the Group's business, the contractual relationships with suppliers of goods and services and with subcontractors vary according to circumstances and type of supplier or subcontractor. It is the Group's policy to enter into an appropriate form of contractual agreement on payment terms when agreeing the terms of each transaction and to pay according to those terms. The Group does not follow any particular code or practice for the payment of creditors. In practice, the Group makes every effort to pay accordingly when it can be confirmed that the supplier has provided the goods or services in accordance with the relevant terms of the contract. The amount for trade creditors of the major subsidiary trading companies represents 46 (2010: 43) days of average daily purchases. The Company has no trade creditors (2010: None).

## 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.

## 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.

## Research and development

The Group is involved in research and development in all sectors in which it operates but specifically in highways, rail, airports, nuclear, hydrocarbons and chemicals, waste and water. The Group's engineers and technical staff in these named sectors develop and deliver technical advances, processes and innovations in an effort to achieve practical, integrated solutions that incorporate the most advanced technologies, while taking account of the broader regulatory perspective and seek to resolve all scientific and technological uncertainties. In undertaking certain elements of this research and development work, the Group is supported by arrangements with certain British universities.

## Donations

Charitable donations of £135,424 (2010: £94,565) were made by the Group during the year, principally to industry related charities serving the communities in which the Group operates.

No political donations were made during the year ended 31 December 2011 (2010: None). The Company has a policy of not making donations to political organisations.



### Disclosure of information to auditors

The directors who held office at the date of approval of this report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's external auditors are unaware; and each director has taken all the steps that he ought to have taken as a director to make himself 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.

### Auditors

KPMG Audit Plc has expressed its willingness to continue in office as independent auditor of the Company and a resolution to reappoint will be proposed at the forthcoming Annual General Meeting.

### Directors' Indemnity

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

### Directors' responsibilities

The directors' responsibilities for the financial statements contained within this Annual Report and the directors' confirmations required under DTR 4.1.12 are set out on page 71.

### Voting Rights

Every member and every duly appointed proxy present at a general meeting or class meeting has, upon a show of hands, one vote and every member present in person or by proxy has, upon a poll, one vote for every share held by him. In the case of joint holders of a share, the vote of the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders and, for this purpose, seniority shall be determined by the order in which the names stand in the register in respect of the joint holding.

### 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 if any call or other sum then payable by him 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.

### 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.

### Variation of rights

Subject to the Companies Act 2006, rights attached to any class of shares may be varied with the written consent of the holders of not less than three-fourths in nominal value of the issued shares of that class (calculated excluding any shares held as treasury shares), or with the sanction of a special resolution passed at a separate general meeting of the holders of those shares. At every such separate general meeting (except an adjourned meeting), the quorum shall be one or more persons holding or representing by proxy not less than one-third in nominal value of the issued shares of the class (calculated excluding any shares held as treasury shares). The rights conferred upon the holders of any shares shall not, unless otherwise expressly provided in the rights attaching to those shares, be deemed to be varied by the creation or issue of further shares ranking *pari passu* with them.

### 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.

### 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 the Company but is encouraged to do so by the introduction of new 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.

# Other statutory information continued

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 for reappointment by the members.

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

## 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, whether relating to the management of the business of the Company or not. 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.

## Rights under the employee share schemes

ACS HR Solutions Share Plan Services (Guernsey) Limited (formerly Excellerate HRO Share Plan Services (Guernsey) Limited), as Trustee of the Costain Group Employee Trust, holds 0.35% of the issued share capital of the Company as at 31 December 2011 on trust for the benefit of 'good leavers' from the Company who are members of any Save As You Earn Plan and leave the employment of the Company before the scheme matures. The Trustee does not exercise any right to vote or to receive a dividend in respect of this shareholding.

## Annual General Meeting ('AGM')

The AGM of the Company will be held in The More Suite, 2nd Floor, Dexter House, No 2 Royal Mint Court, Tower Hill, London EC3N 4QN on Wednesday 9 May 2012 at 11.00 a.m.

The Notice of Annual General Meeting will be sent in paper form to all shareholders. It will also be available on the Company's website – [www.costain.com](http://www.costain.com). This 2011 Annual Report will be available on the Company's website. You may recall that the Company now provides this information in electronic form unless you have elected to receive the documents in paper form. For those who elected for paper form, this 2011 Annual Report will accompany the Notice of Annual General Meeting.

Mr James Morley, the Chairman of the Audit Committee and Mr Mike Alexander, the Chairman of the Remuneration Committee will be available at the Annual General Meeting.

By Order of the Board



**Tracey Wood**  
Company Secretary

7 March 2012

# Directors' remuneration report

## This report, approved by the Board, has been prepared in accordance with the requirements of the UKLA listing rules, the Companies Act 2006, the UK Corporate Governance Code and best practice guidelines.

A resolution to approve the Directors' remuneration report will be proposed at the AGM.

### Remuneration Committee

The Remuneration Committee (the Committee) is comprised exclusively of independent non-executive directors. The members of the Committee are Michael Alexander (Chairman), John Bryant and James Morley.

In 2011, the Committee met seven times and details of the attendance at those meetings are as follows:

Director	A	B
<b>M R Alexander</b> (Chair)	7	7
<b>J M Bryant</b>	7	7
<b>J Morley</b>	7	6

**A** Maximum number of meetings the director could have attended

**B** Number of meetings the director actually attended

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 Aon Hewitt Limited (operating through the brand New Bridge Street). This advice related to developing its remuneration policy, particularly in relation to (i) the production of bespoke benchmarking data in respect of the remuneration of executive directors and senior management and (ii) the design of the proposed new Long-Term Incentive Plan and SAYE Plan for which shareholder approval is to be sought at the forthcoming AGM (further details of which are set out below).

Neither Aon Hewitt Limited, nor any other part of the Aon Corporation Group, provided other services to the Company during the year.

In addition, advice was sought where appropriate from other sources, namely the Chief Executive, Group Finance Director, the Company's Chairman and the HR & Legal Director. The Company Secretary acts as secretary to the Committee. The Committee may invite any of the executive directors to attend all or part of its meetings. Individuals are not present when their own remuneration is being discussed.

The Committee's terms of reference are available on the Company's website at [www.costain.com](http://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
15 February 2011	<ul style="list-style-type: none"> <li>Approved 2010 Annual Cash Bonuses subject to final audit of accounts</li> <li>Reviewed salary of the senior executives</li> <li>Reviewed the 2011 Annual Cash Bonus targets</li> <li>Approved the Deferred Share Bonus Plan ('DSBP') performance target for 2011 base year</li> <li>Reviewed the Chairman's fee</li> <li>Reviewed the Directors' remuneration report</li> </ul>
2 March 2011	<ul style="list-style-type: none"> <li>Reviewed the Long-Term Incentive Plan ('LTIP') performance targets for the 2011 awards</li> <li>Approved 2011 Annual Cash Bonus targets</li> </ul>
8 March 2011	<ul style="list-style-type: none"> <li>Approved the vesting of the 2007 and 2008 LTIP and the vesting and release of the 2007 and 2008 Phantom LTIP</li> <li>Approved the LTIP performance targets for the 2011 awards</li> </ul>
12 April 2011	<ul style="list-style-type: none"> <li>Granted awards under the 2011 LTIP</li> <li>Granted awards under the DSBP for 2010 base year</li> <li>Approved the notification of participants for the DSBP 2011 base year</li> </ul>
4 October 2011	<ul style="list-style-type: none"> <li>Reviewed LTIP term sheet for introduction of new LTIP</li> <li>Approved the introduction of clawback</li> <li>Approved the share ownership guidelines</li> <li>Approved the new SAYE design</li> </ul>
11 October 2011	<ul style="list-style-type: none"> <li>Approved grants made under the 2011 Save As You Earn ('SAYE') scheme</li> </ul>
13 December 2011	<ul style="list-style-type: none"> <li>Final approval of new LTIP design</li> <li>Reviewed LTIP performance targets for 2012 awards</li> <li>Considered on behalf of the Board outline salary proposals across the Company for 2012</li> <li>Reviewed the current remuneration arrangements to ensure that they do not encourage undue risk</li> </ul>

### Remuneration policy

The Committee determines the remuneration policy for executive directors, the Chairman and other senior management 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.

Overview

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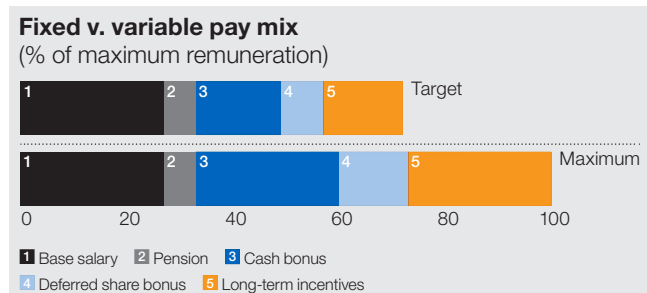
# Directors' remuneration report continued

Each year, the Committee reviews the remuneration policy, taking into account both the external market (including environment, social and corporate governance issues) and the Company's strategic objectives over the short and the medium term. The framework has been designed as an integral part of the Company's overall business strategy.

The remuneration package is based on the following principles:

Principle	How achieved	Rationale
To provide competitive and appropriate total remuneration	Target levels of remuneration are independently benchmarked against comparable companies primarily in the UK-based construction sector and of other companies of a similar size	To attract and retain executives of the appropriate calibre and expertise
Reward both short and long-term performance	Ensure an appropriate balance between short and long-term through mixture of incentive programmes	Focuses executives on the long-term strategy of the Company and so motivates executives to make decisions that lead to the creation of long-term value, while avoiding any incentive for undue risk taking
Link remuneration practices to strategy of the Company	Regularly review performance metrics used in short and long-term incentive programmes and the use of cash and equity	

The chart below illustrates the average mix between the fixed and variable (performance-related) elements of remuneration of the executive directors at target and maximum performance. Target performance assumes target payouts of cash and DSBP and an expected value of LTIP awards. Maximum performance assumes all bonuses and long-term incentive awards vest in full. It demonstrates the weighting of the package towards variable pay, particularly at maximum performance. The Committee considers the mix between fixed and variable pay to be appropriate. During the year, the Committee reviewed the executive remuneration arrangements from a risk perspective and concluded that they do not encourage undue risk and that the arrangements, as a whole, provide an appropriate balance.



## External directorships

The Company encourages executive directors to take up external 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.

Mr 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 2011 he was paid £19,872 (2010: £19,872). He has retained these fees in accordance with the above policy.

## Remuneration arrangements for executive board directors

Remuneration packages for executive directors and other members of senior management consist of the following elements:

- Base salary;
- Benefits;
- Pension;
- Annual cash bonus;
- Deferred share bonus; and
- Long-term incentives.

Details of each of the above elements follow, but the following table summarises the packages of the two executive directors for 2012:

Component	Andrew Wyllie Chief Executive	Tony Bickerstaff Group Finance Director
Base salary from 1 April 2012	£416,160	£275,706
Maximum Annual Cash Bonus (% of salary)	100%	100%
Maximum DSBP (% of salary)	50%	50%
Maximum 2012 LTIP award* (% of salary)	100%	100%
Pension arrangement	Pension allowance – 22% of salary	
Benefits	Company car or car allowance, fuel, medical insurance and life assurance	

\* Assuming shareholder approval is obtained for the 2012 LTIP at the forthcoming AGM.

### Base salary

Base salaries for the executive directors are reviewed annually by the Committee and take effect from 1 April. The Committee also gives guidance to the Chief Executive as to the matters being taken into account in the salary review of other senior management and all other employees of the Group. The Company's policy is to target broadly the median position in light of remuneration generally within the Company and other companies in the UK-based construction sector. Salaries are set with reference to individual performance, experience and responsibilities.

For 2012, the Committee approved a 2% increase for executive directors, resulting in the base salaries being payable as set out in the above table. A 2% salary increase budget was also applied across the Company in 2012.

### Other Benefits

The non-salary benefits for executive directors comprise:

- Company car or car allowance;
- Fuel;
- Medical insurance; and
- Life assurance.

### 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 Messrs Wyllie and Bickerstaff were £1,867 (2010: £1,811) and £1,237 (2010: £1,190) 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.

### Annual cash bonus

Executive directors and other senior management are eligible for annual cash 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. For the year ended 31 December 2011, the Chief Executive and Group Finance Director each had a maximum bonus opportunity of 100% of base salary.

For the year ended 31 December 2011, 90% of the executive directors' annual bonus metrics were set as measurable key financial targets. These metrics included Group earnings before interest and tax, Group overhead costs, cash flow, order book and health and safety targets. The remaining 10% was linked to personal goals relating to building and developing the Executive team and the talent pool within the organisation.

The total bonus payment for the executive directors for the year ended 31 December 2011 was 85% of salary of which 75% related to measurable financial targets and 10% related to personal goals.

For the year ended 31 December 2012, the maximum annual cash bonus potential for the Chief Executive and the Group Finance Director remains unchanged, with the same basic approach to target-setting (i.e. 90% relating to key financial targets, 10% relating to personal goals).

### Deferred Share Bonus Plan

Executive directors and other senior management are eligible to participate in the Company's DSBP which promotes greater alignment with shareholders through the award of deferred shares. Under the DSBP, any bonus earned is deferred in shares which vest 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 to satisfy the deferred bonuses are purchased by a trust on behalf of the Group and so do not lead to any dilution of shareholder interest.

For the year ended 31 December 2011, both executive directors had a maximum DSBP opportunity of 50% of base salary. The performance measure was EBIT, as described in the table below:

Group EBIT for 2011	Percentage of Relevant Maximum Award
£19.47 million or less	0%
Between £19.47 million and £20.5 million	Between 0% and 60% on a straight-line basis
£20.5 million	60%
Between £20.5 million and £22.55 million	Between 60% and 100% on a straight-line basis
£22.55 million or more	100%

The EBIT for the year ended 31 December 2011 was £22.0 million and so the measure has been met as to 89%. The number of shares to which a participant in the DSBP will be entitled will be calculated on the basis of the monetary value of the deferred bonus divided by the middle market quotation of a share at the date of the deferred award. The grant of the deferred bonus award will be made in the six weeks following the preliminary announcement of the results for the financial year ended 31 December 2011.

For the year ended 31 December 2012, the maximum DSBP for the executive directors remains unchanged. The Committee will disclose on a retrospective basis the EBITA measure (defined as underlying earnings before interest, tax, amortisation of acquired intangible assets and employment related acquisition consideration but excluding any PFI transfer into the pension and risk management costs) for 2012 in next year's report.



# Directors' remuneration report continued

The DSBP includes a mechanism to allow the Company to deliver the DSBP awards in a tax-efficient manner at no additional cost to the Company by delivering to participants a combination of HM Revenue & Customs ('HMRC') tax-approved market value share options over a fixed number of shares and non-tax approved share options with a nil exercise price over a fixed value of shares. The tax approved and non-tax approved options are linked, in terms of value and on exercise and mirror the same commercial terms as a DSBP award. An advantage of this combined arrangement is that it allows for greater tax efficiencies for both the participant and the Company.

For 2012 onwards, the Committee will introduce a clawback provision incorporated into the annual cash bonus and the DSPB 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.

## Long-Term Incentive Plans

The current LTIP was approved by shareholders at the 2002 AGM which means that the current plan reaches the end of its ten-year life in 2012. During 2011, the Committee reviewed proposals for a new plan and will seek shareholder approval for a new 2012 LTIP at the AGM in 2012. Full details of the 2012 LTIP (which has been designed to reflect many of the core features of the current LTIP) are set out in the Notice of AGM.

The current LTIP allows for conditional awards to a participant with a maximum face value of up to 100% of base salary at the date of grant of the award.

The EPS targets for the 2011 awards are:

Sum of the EPS for the financial years ending 31 December 2011, 2012 and 2013*	Vesting level for awards up to 50% of salary
102p	15%
113p	100%
Between 102p and 113p	Pro-rata between 15% and 100%
EPS for the financial year ending 31 December 2013	Vesting level for awards from 50% to 100% of salary
47p	0%
56p	100%
Between 47p and 56p	Pro-rata between 0% and 100%

\* EPS targets rounded as appropriate.

The Committee believes that EPS is the most appropriate metric to use in the LTIP, as growth in EPS is one of the key drivers of the Company's share price together with operating profit. As reported last year, for awards made in 2011 EPS should be calculated before pension interest (itself calculated under IAS 19).

The performance conditions that are intended to apply to the first awards to be made under the 2012 LTIP are described in the Notice of AGM.

The Remuneration Committee is committed to the concept of creating a genuine alignment of interests between investors and the Costain Board. The Committee therefore welcomed the significant increases in Mr Wyllie and Mr Bickerstaff's shareholdings during 2011 and has further aligned the interests of executives and investors by introducing a share ownership guideline under which executive directors will be encouraged to build up and maintain a shareholding worth not less than 100% of base salary. Executives and other senior managers will be encouraged to retain up to 50% of the net number of shares received under any 2012 LTIP or future DSBP award until this guideline is satisfied. Furthermore, to ensure a true alignment of interests across the entire Board, a similar share ownership guideline has been introduced for non-executive directors who will be encouraged to build up and maintain a shareholding of not less than 100% of their annual fee.

## All employee share plans

The Company's existing SAYE Plan was approved by shareholders at the 2002 AGM. Again, this means that it will expire in 2012. Consequently, shareholder approval will be sought for the establishment of a new 2012 SAYE Plan (which will be of standard design) at the forthcoming AGM.

Under the current Plan, the Company granted options on 11 October 2011 at an option price of 205p per share to participants in the 3 year saving scheme, and 182p per share to participants in the 5-year saving scheme. Details of the grants made under the Plan are shown in Note 19 to the financial statements on page 111.

## Service agreements and letters of appointment

The executive directors have service contracts that can be terminated by either party on the giving of 12 months' notice. There is no provision for payment of predetermined compensation in case of wrongful termination by the Group and the duty to mitigate loss applies.

Mr Wyllie's service agreement is dated 25 April 2005 and Mr Bickerstaff's 3 March 2006.

## Chairman and other non-executive directors

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 and recommended to 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 Committee. Following a review in 2012, it was decided to increase the basic annual fees and the additional fees, reflecting the increased time commitment expected of non-executive directors and the expertise that they bring to the Company. The fees are:

Year	Annual fee	Senior Independent Director	Audit Committee Chairman	Remuneration Committee Chairman
2012	£41,820	£6,120	£8,670	£6,120
2011	£41,000	£6,000	£8,500	£6,000

During 2011, the Chairman was paid fees of £127,000. He does not receive any additional fees for committee memberships. For 2012, he will receive a fee of £129,500.

The independent non-executive directors have letters of appointment. The appointment of an independent non-executive director can be terminated by reasonable notice on either side. Messrs Allvey, Alexander, Bryant and Morley are not entitled to compensation for loss of office.

The nominee non-executive directors (as indicated in the Corporate Governance Statement on page 52), 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 major shareholders has appointed a nominee to sit on the Board.

The dates of each non-executive directors' original appointment are as follows:

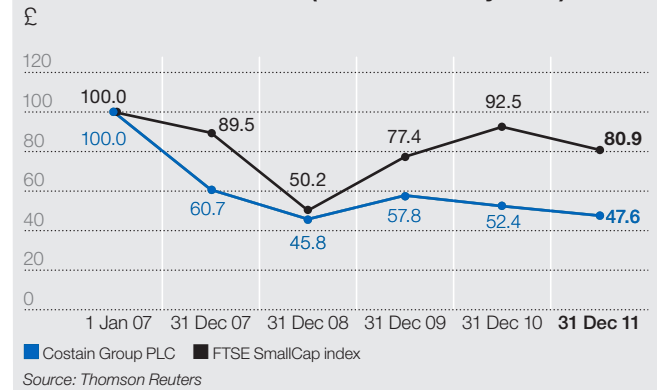
Non-executive director	Date of appointment	Expiry of current term*
David P Allvey	01.11.2001	Close of the 2012 AGM
John M Bryant	01.02.2002	Close of the 2012 AGM
Michael R Alexander	25.07.2007	Close of the 2014 AGM
James Morley	09.01.2008	Close of the 2014 AGM
Samer G Younis	23.06.2009	22.06.2012

\* Subject to election at the AGM following their appointment and subsequent re-election at intervals of no more than three years in accordance with the Company's Articles of Association.

### Performance graph

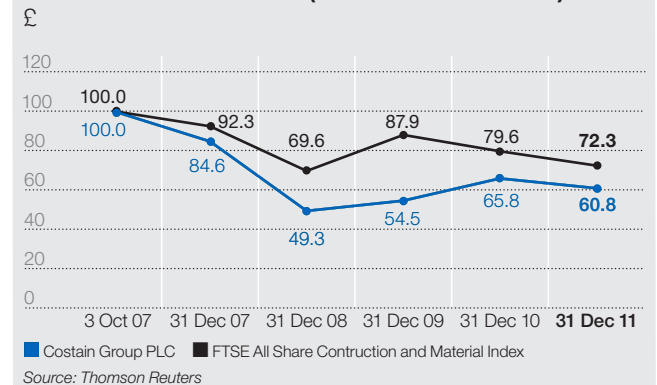
The graph below shows the value, by 31 December 2011, for £100 invested in Costain Group PLC on 1 January 2007 compared with the value of £100 invested in the FTSE SmallCap Index. While the FTSE All-Share Index has been used for this purpose in previous reports, the Committee now believes that the SmallCap Index is a more 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 2007)



The additional graph below shows the value, by 31 December 2011, for £100 invested in Costain Group PLC on 3 October 2007 (i.e. the date following the EGM at which the 3 for 4 rights issue was approved by shareholders) compared with £100 invested in the FTSE All-Share Construction and Materials Index.

#### Total shareholder return (From 3 October 2007)



The text and table that follow comprise the auditable part of the Directors' remuneration report, being the information required by the UKLA listing rules 9.8.6 and 9.8.8.

# Directors' remuneration report continued

## Directors' emoluments

The following sections have been audited by KPMG Audit Plc.

The aggregate directors' remuneration for the year ended 31 December 2011 was £1,584,800 (2010: £1,525,230).

	Salary/Fee £	Bonus £	Benefits £	2011 Total £	2010 Total £	2011 Pension* £	2010 Pension £
<b>Executive directors</b>							
A Wyllie	406,000	346,800	13,510	<b>766,310</b>	767,215	<b>89,320</b>	86,625
A O Bickerstaff	268,975	229,755	12,010	<b>510,740</b>	461,515	<b>59,175</b>	56,925
<b>Non-executive directors</b>							
D P Allvey	125,250			<b>125,250</b>	120,000		–
J M Bryant	46,500			<b>46,500</b>	45,000		–
M R Alexander	46,500			<b>46,500</b>	45,000		–
J Morley	49,000			<b>49,000</b>	47,500		–
S G Younis	40,500			<b>40,500</b>	39,000		–
Former directors	–			–	–		–
<b>Total</b>	<b>982,725</b>	<b>576,555</b>	<b>25,520</b>	<b>1,584,800</b>	<b>1,525,230</b>	<b>148,495</b>	<b>143,550</b>

\* Pension contributions in excess of £50,000 paid as a cash supplement.

## Directors' share interests

### (i) Beneficial holdings

	At 1 January 2011 Number of ordinary shares	At 31 December 2011 Number of ordinary shares
A Wyllie	28,217	142,016
A O Bickerstaff	12,000	79,833
D P Allvey	5,250	5,250
J M Bryant*	9,627	15,028
M R Alexander	9,263	17,533
J Morley	5,000	23,000
S G Younis	–	–

\* All shares held by spouse through a nominee account.

There was a significant increase in shareholding in 2011 and as noted above in 2012 share ownership guidelines have also been introduced.

### (ii) Deferred Share Bonus Plan awards

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

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

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

	Date granted	At 1 Jan 2011	Granted during the year	Lapsed during the year	Exercisable during the year	At 31 Dec 2011	Exercise price	Exercisable from
A Wyllie	19.04.10	25,800 <sup>1</sup>	–	–	–	25,800	–	April 2012-2020
	19.04.10	12,377	–	–	–	12,377	£2.42p	April 2012-2020
		(£29,999.91) <sup>2</sup>				(£29,999.91)		
	19.04.10	12,377 <sup>3</sup>	–	–	–	12,377	–	April 2012-2020
	12.04.11	–	82,644 <sup>1</sup>	–	–	82,644 <sup>1</sup>	–	April 2013-2021
A O Bickerstaff	19.04.10	12,180 <sup>1</sup>	–	–	–	12,180	–	April 2012-2020
	19.04.10	12,377	–	–	–	12,377	£2.42p	April 2012-2020
		(£29,999.91) <sup>2</sup>				(£29,999.91)		
	19.04.10	12,377 <sup>3</sup>	–	–	–	12,377	–	April 2012-2020
	12.04.11	–	54,752 <sup>1</sup>	–	–	54,752 <sup>1</sup>	–	April 2013-2021

<sup>1</sup> Number of shares under the Deferred Award.

<sup>2</sup> Maximum number and value of shares under the Combined Deferred Award.

<sup>3</sup> 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 exercisable until the tenth anniversary of the date of grant.

### (iii) Long-Term Incentive Plan awards

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

	Date granted	At 1 Jan 2011	Granted during the year	Lapsed during the year	Vested during the year	At 31 Dec 2011	Exercisable from
A Wyllie	18.04.07 <sup>1</sup>	77,599	–	–	68,287	–	March 2011
	21.04.08 <sup>2</sup>	154,639	–	–	154,639	–	March 2011
	07.04.09 <sup>3</sup>	82,417	–	–	–	82,417	March 2012
	14.04.10 <sup>4</sup>	81,632	–	–	–	81,632	March 2013
	12.04.11 <sup>5</sup>	–	169,294	–	–	169,294	March 2014
A O Bickerstaff	18.04.07 <sup>1</sup>	43,410	–	–	38,200	–	March 2011
	21.04.08 <sup>2</sup>	90,721	–	–	90,721	–	March 2011
	07.04.09 <sup>3</sup>	52,747	–	–	–	52,747	March 2012
	14.04.10 <sup>4</sup>	54,081	–	–	–	54,081	March 2013
	12.04.11 <sup>5</sup>	–	112,157	–	–	112,157	March 2014

<sup>1</sup> EPS for the financial year ended 31 December 2010 of 32.7p (25% vests) to EPS of 37.1p (100% vests) on a sliding scale between 25% and 100% pro rata to the EPS actually achieved. The EPS target was 88% met.

<sup>2</sup> EPS for the financial year ended 31 December 2010 of 30.9p (25% vests) to EPS of 34.3p (100% vests) on a sliding scale between 25% and 100% pro rata to the EPS actually achieved. The EPS target was 100% met.

<sup>3</sup> EPS for the financial year ended 31 December 2011 of 21.0p (15% vests) to EPS of 27.5p (100% vests) on a sliding scale between 15% and 100% pro rata to the EPS actually achieved.

<sup>4</sup> EPS for the financial year ended 31 December 2012 of 21.0p (15% vests) to EPS of 27.5p (100% vests) on a sliding scale between 15% and 100% pro rata to the EPS actually achieved.

<sup>5</sup> 50% of the award is subject to an aggregate EPS for the financial years ended 31 December 2011, 2012 and 2013 of 102p (15% vests) to EPS of 113p (100% vests) on a sliding scale between 15% and 100% pro rata to the EPS actually received. The remaining 50% of the award will be based on an EPS for the financial year ended 31 December 2013 of 47p (0% vests) to EPS of 56p (100% vests) on a sliding scale between 0% and 100% pro rata to the actual EPS achieved. (EPS targets rounded as appropriate).

# Directors' remuneration report continued

## Notes

- (a) The awards, which are expressed as options, are subject to an exercise price of £1.
- (b) The average closing middle market price of ordinary shares of 50p each in the Company for the dealing day immediately preceding the date of grant for the 2009 award was 227p, for the 2010 award 245p and for the 2011 award 241p.
- (c) The total number of ordinary shares of 50p each still outstanding and subject to the 2009 award is 620,262 (2010: 678,295), the 2010 award 606,550 (2010: 678,602) and the 2011 award 761,402.
- (d) At 31 December 2011, the derived mid-market price of the ordinary shares in the Company, as advised by the Company's brokers, was 222.5p. The range of the share price of the ordinary shares during 2011 was 180p to 265p.

### (iv) Save As You Earn share options

	Date granted	At 1 Jan 2011	Granted during the year	Lapsed during the year	Exercisable during the year	At 31 Dec 2011	At exercised price	Exercisable from
A Wyllie	23.05.08	4,795	–	–	4,795	–	196.0p	Jul-Dec 2011
	11.10.11	–	1,633	–	–	1,633	205.0p	Nov 2014-May 2015
A O Bickerstaff	23.05.08	4,795	–	–	4,795	–	196.0p	Jul-Dec 2011
	11.10.11	–	1,633	–	–	1,633	205.0p	Nov 2014-May 2015

On behalf of the Board



**Michael R Alexander**

Chairman of the Remuneration Committee

7 March 2012



# Directors' responsibilities statement

## The directors are responsible for preparing the Annual Report and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare the Group and parent company financial statements for each financial year. Under that law, they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis.

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 parent company and of their profit or loss for that period.

In preparing each of the Group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent companies' transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

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

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

We confirm that to the best of our knowledge:

- the financial statements for the year ended 31 December 2011, prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Directors' Report, the Business review, the Principal risks and Key Performance Indicators and the Group Finance Director's review sections of this report include a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

On behalf of the Board



**David Allvey**  
Chairman



**Andrew Wyllie**  
Chief Executive

7 March 2012

# Independent Auditors' report to the members of Costain Group PLC

We have audited the financial statements of the Costain Group PLC for the year ended 31 December 2011 which comprise the Group Income Statement, the Group and Parent Company Statement of Comprehensive Income, the Group and Parent Company Statement of Financial Position, the Group and Parent Company Statements of Changes in Equity, the Group and Parent Company Cash Flow Statements and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

## Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's ('APB's') Ethical Standards for Auditors.

## Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at [www.frc.org.uk/apb/scope/private.cfm](http://www.frc.org.uk/apb/scope/private.cfm).

## Opinion on financial statements

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 2011 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with 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.

## Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- information given in the Corporate Governance statement with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.

## Matters on which we are required to report by exception

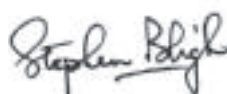
We have nothing to report in respect of the following:

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 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; or
- a Corporate Governance statement has not been prepared by the Company.

Under the Listing Rules we are required to review:

- the directors' statement, set out in the Directors' Report, in relation to going concern; and
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on director's remuneration.



## Stephen Bligh

Senior Statutory Auditor

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

7 March 2012

# Financial statements

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

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# Consolidated income statement

Year ended 31 December

	Notes	2011			2010
		Before other items £m	Other items £m	Total £m	Total £m
<b>Continuing operations</b>					
Revenue	3	<b>986.3</b>	–	<b>986.3</b>	1,022.5
Less: Share of revenue of joint ventures and associates	13	<b>(117.8)</b>	–	<b>(117.8)</b>	(98.0)
<b>Group revenue</b>		<b>868.5</b>	–	<b>868.5</b>	924.5
Cost of sales		<b>(818.8)</b>	–	<b>(818.8)</b>	(883.9)
Gross profit		<b>49.7</b>	–	<b>49.7</b>	40.6
Administrative expenses		<b>(25.6)</b>	–	<b>(25.6)</b>	(23.2)
Amortisation of acquired intangible assets		–	<b>(0.9)</b>	<b>(0.9)</b>	–
Employment related deferred consideration		–	<b>(0.7)</b>	<b>(0.7)</b>	–
<b>Group operating profit</b>		<b>24.1</b>	<b>(1.6)</b>	<b>22.5</b>	17.4
Profit on sale of non-consolidated subsidiary	4	<b>0.5</b>	–	<b>0.5</b>	–
Profit on sales of interests in joint ventures and associates	4	<b>0.3</b>	–	<b>0.3</b>	11.2
Profit on sale of land and property		–	–	–	1.3
Share of results of joint ventures and associates	13	<b>(1.3)</b>	–	<b>(1.3)</b>	(0.5)
<b>Profit from operations</b>	3	<b>23.6</b>	<b>(1.6)</b>	<b>22.0</b>	29.4
Finance income	7	<b>34.1</b>	–	<b>34.1</b>	30.7
Finance expense	7	<b>(32.2)</b>	–	<b>(32.2)</b>	(32.2)
Net finance income/(expense)		<b>1.9</b>	–	<b>1.9</b>	(1.5)
<b>Profit before tax</b>	3/4	<b>25.5</b>	<b>(1.6)</b>	<b>23.9</b>	27.9
Income tax	8	<b>(5.6)</b>	<b>0.4</b>	<b>(5.2)</b>	(4.8)
<b>Profit for the year attributable to equity holders of the parent</b>		<b>19.9</b>	<b>(1.2)</b>	<b>18.7</b>	23.1
<b>Earnings per share</b>					
Basic	9	<b>31.1p</b>	<b>(1.9)p</b>	<b>29.2p</b>	36.4p
Diluted	9	<b>30.0p</b>	<b>(1.8)p</b>	<b>28.2p</b>	35.4p

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

	2011 £m	2010 £m
<b>Profit for the year</b>	<b>18.7</b>	23.1
Exchange differences on translation of foreign operations	(0.8)	(1.1)
Cash flow hedges		
Group:		
Effective portion of changes in fair value during year	(0.1)	0.3
Net changes in fair value transferred to the income statement	0.2	(0.3)
Joint ventures and associates:		
Effective portion of changes in fair value (net of tax) during year	(2.8)	(1.3)
Net changes in fair value (net of tax) transferred to the income statement	-	8.1
Actuarial (losses)/gains on defined benefit pension scheme	(22.1)	24.6
Tax recognised on actuarial losses/(gains) recognised directly in equity	3.0	(8.1)
<b>Other comprehensive (expense)/income for the year</b>	<b>(22.6)</b>	22.2
<b>Total comprehensive (expense)/income for the year attributable to equity holders of the parent</b>	<b>(3.9)</b>	45.3

## Company statement of comprehensive income and expense

The Company does not have any comprehensive income or expense, other than a loss for the year of £2.5 million (2010: profit of £7.5 million).

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# Consolidated statement of financial position

As at 31 December

	Notes	2011 £m	2010 £m
<b>Assets</b>			
<b>Non-current assets</b>			
Intangible assets	11	20.3	0.1
Property, plant and equipment	12	11.4	9.7
Investments in equity accounted joint ventures	13	21.4	24.5
Investments in equity accounted associates	13	1.4	1.5
Loans to equity accounted joint ventures	13	13.7	10.8
Loans to equity accounted associates	13	6.4	0.6
Other	14	16.4	18.9
Deferred tax	8	17.4	20.9
<b>Total non-current assets</b>		<b>108.4</b>	<b>87.0</b>
<b>Current assets</b>			
Inventories		2.3	1.3
Trade and other receivables	14	188.0	162.0
Cash and cash equivalents	15	141.7	146.0
<b>Total current assets</b>		<b>332.0</b>	<b>309.3</b>
<b>Total assets</b>		<b>440.4</b>	<b>396.3</b>
<b>Equity</b>			
Share capital	20	32.4	31.7
Share premium		3.3	2.0
Foreign currency translation reserve		6.1	6.8
Hedging reserve		(4.9)	(2.2)
Retained earnings		(6.1)	(0.7)
<b>Total equity attributable to equity holders of the parent</b>		<b>30.8</b>	<b>37.6</b>
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Retirement benefit obligations	19	52.9	39.6
Other payables	17	6.1	5.2
Provisions for other liabilities and charges	18	2.3	2.5
<b>Total non-current liabilities</b>		<b>61.3</b>	<b>47.3</b>
<b>Current liabilities</b>			
Trade and other payables	17	342.9	304.8
Income tax liabilities	8	1.7	1.7
Bank overdrafts	15	1.6	1.7
Provisions for other liabilities and charges	18	2.1	3.2
<b>Total current liabilities</b>		<b>348.3</b>	<b>311.4</b>
<b>Total liabilities</b>		<b>409.6</b>	<b>358.7</b>
<b>Total equity and liabilities</b>		<b>440.4</b>	<b>396.3</b>

The financial statements were approved by the Board of Directors on 7 March 2012 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	2011 £m	2010 £m
<b>Assets</b>			
<b>Non-current assets</b>			
Investments in subsidiaries	13	121.4	123.0
<b>Total non-current assets</b>		<b>121.4</b>	123.0
<b>Current assets</b>			
Trade and other receivables	14	8.1	5.8
Cash and cash equivalents	15	61.7	77.6
<b>Total current assets</b>		<b>69.8</b>	83.4
<b>Total assets</b>		<b>191.2</b>	206.4
<b>Equity</b>			
Share capital	20	32.4	31.7
Share premium		3.3	2.0
Other reserves		6.4	4.5
Retained earnings		38.1	46.9
<b>Total equity attributable to equity holders of the parent</b>		<b>80.2</b>	85.1
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Provisions for other liabilities and charges	18	1.3	1.4
<b>Total non-current liabilities</b>		<b>1.3</b>	1.4
<b>Current liabilities</b>			
Trade and other payables	17	107.5	117.9
Income tax liabilities	8	1.7	1.7
Provisions for other liabilities and charges	18	0.5	0.3
<b>Total current liabilities</b>		<b>109.7</b>	119.9
<b>Total liabilities</b>		<b>111.0</b>	121.3
<b>Total equity and liabilities</b>		<b>191.2</b>	206.4

The financial statements were approved by the Board of Directors on 7 March 2012 and were signed on its behalf by:

**A Wyllie**  
Director

**A O Bickerstaff**  
Director

Registered number: 1393773

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# 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 2010	31.7	1.9	7.0	(9.0)	(35.4)	(3.8)
Profit for the year	–	–	–	–	23.1	23.1
Other comprehensive income/(expense)	–	–	(1.1)	6.8	16.5	22.2
Transfer between reserves	–	–	0.9	–	(0.9)	–
Equity-settled share-based payments	–	–	–	–	1.5	1.5
Dividends paid	–	0.1	–	–	(5.5)	(5.4)
At 31 December 2010	31.7	2.0	6.8	(2.2)	(0.7)	37.6
At 1 January 2011	<b>31.7</b>	<b>2.0</b>	<b>6.8</b>	<b>(2.2)</b>	<b>(0.7)</b>	<b>37.6</b>
Profit for the year	–	–	–	–	18.7	18.7
Other comprehensive expense	–	–	(0.8)	(2.7)	(19.1)	(22.6)
Transfer between reserves	–	–	0.1	–	(0.1)	–
Issue of ordinary shares under employee share option plans	0.6	1.1	–	–	(0.2)	1.5
Equity-settled share-based payments	–	–	–	–	1.4	1.4
Dividends paid	0.1	0.2	–	–	(6.1)	(5.8)
<b>At 31 December 2011</b>	<b>32.4</b>	<b>3.3</b>	<b>6.1</b>	<b>(4.9)</b>	<b>(6.1)</b>	<b>30.8</b>

# Company statement of changes in equity

	Share capital £m	Share premium £m	Other reserve £m	Retained earnings £m	Total equity £m
At 1 January 2010	31.7	1.9	2.3	44.9	80.8
Comprehensive income	–	–	–	7.5	7.5
Equity-settled share-based payments granted to employees of subsidiaries	–	–	2.2	–	2.2
Dividends paid	–	0.1	–	(5.5)	(5.4)
At 31 December 2010	31.7	2.0	4.5	46.9	85.1
At 1 January 2011	<b>31.7</b>	<b>2.0</b>	<b>4.5</b>	<b>46.9</b>	<b>85.1</b>
Comprehensive expense	–	–	–	(2.5)	(2.5)
Issue of ordinary shares under employee share option plans	0.6	1.1	–	(0.2)	1.5
Equity-settled share-based payments granted to employees of subsidiaries	–	–	1.9	–	1.9
Dividends paid	0.1	0.2	–	(6.1)	(5.8)
<b>At 31 December 2011</b>	<b>32.4</b>	<b>3.3</b>	<b>6.4</b>	<b>38.1</b>	<b>80.2</b>

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	2011 £m	2010 £m
<b>Cash flows from operating activities</b>			
<b>Profit for the year</b>		<b>18.7</b>	23.1
Adjustments for:			
Share of results of joint ventures and associates	13	1.3	0.5
Finance income	7	(34.1)	(30.7)
Finance expense	7	32.2	32.2
Income tax	8	5.2	4.8
Profit on sales of interests in joint ventures and associates	4	(0.3)	(11.2)
Profit on sale of non-consolidated subsidiary	4	(0.5)	-
Profit on sale of plant and equipment		-	(1.2)
Profit on sale of land and property		-	(1.3)
Depreciation of property, plant and equipment	4	1.9	1.7
Amortisation of intangible assets	4	0.9	0.9
Employment related deferred consideration		0.7	-
Share-based payments expense	5	1.9	4.5
<b>Cash from operations before changes in working capital and provisions</b>		<b>27.9</b>	23.3
(Increase)/decrease in inventories		(1.0)	1.1
(Increase)/decrease in receivables		(10.1)	37.2
Increase/(decrease) in payables		25.0	(10.2)
Movement in provisions and employee benefits		(7.1)	(20.0)
<b>Cash from operations</b>		<b>34.7</b>	31.4
Interest received		1.8	1.0
Interest paid		(1.7)	(0.9)
Income tax received		-	0.2
<b>Net cash from operating activities</b>		<b>34.8</b>	31.7
<b>Cash flows from/(used by) investing activities</b>			
Dividends received from joint ventures and associates	13	1.4	0.1
Additions to property, plant and equipment	12	(2.9)	(1.1)
Additions to intangible assets	11	(0.1)	-
Proceeds of disposal of property, plant and equipment		0.2	3.8
Additions to loans to joint ventures and associates	13	(13.5)	(5.9)
Loan repayments by joint ventures and associates	13	0.4	0.5
Proceeds from sale of interest in joint venture		0.3	-
Proceeds from sale of subsidiary		0.5	-
Acquisitions of subsidiaries (net of acquired cash and cash equivalents and overdrafts)		(21.1)	-
<b>Net cash used by investing activities</b>		<b>(34.8)</b>	(2.6)
<b>Cash flows from/(used by) financing activities</b>			
Issue of ordinary share capital		1.5	-
Ordinary dividends paid		(5.8)	(5.4)
<b>Net cash used by financing activities</b>		<b>(4.3)</b>	(5.4)
<b>Net (decrease)/increase in cash, cash equivalents and overdrafts</b>		<b>(4.3)</b>	23.7
Cash, cash equivalents and overdrafts at beginning of the year	15	144.3	120.5
Effect of foreign exchange rate changes		0.1	0.1
<b>Cash, cash equivalents and overdrafts at end of the year</b>	15	<b>140.1</b>	144.3

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# Company cash flow statement

Year ended 31 December

	Notes	2011 £m	2010 £m
<b>Cash flows from operating activities</b>			
<b>(Loss)/profit for the year</b>		<b>(2.5)</b>	7.5
Adjustments for:			
Finance income		<b>(2.3)</b>	(3.7)
Finance expense		<b>0.4</b>	0.3
Income tax		<b>(0.6)</b>	(1.2)
Amount written off/(back) against investments		<b>3.5</b>	(6.3)
<b>Cash used by operations before changes in working capital and provisions</b>		<b>(1.5)</b>	(3.4)
Increase in receivables		<b>(2.3)</b>	(4.2)
(Decrease)/increase in payables		<b>(10.4)</b>	60.3
Movement in provisions		<b>0.1</b>	(0.2)
<b>Cash (used by)/from operations</b>		<b>(14.1)</b>	52.5
Interest received		<b>0.3</b>	0.2
Interest paid		<b>(0.4)</b>	(0.3)
Income tax received		<b>0.6</b>	0.8
<b>Net cash (used by)/from operating activities</b>		<b>(13.6)</b>	53.2
<b>Cash flows from investing activities</b>			
Dividends received		<b>2.0</b>	3.5
<b>Net cash from investing activities</b>		<b>2.0</b>	3.5
<b>Cash flows from/(used by) financing activities</b>			
Issue of ordinary share capital		<b>1.5</b>	–
Ordinary dividends paid		<b>(5.8)</b>	(5.4)
<b>Net cash used by financing activities</b>		<b>(4.3)</b>	(5.4)
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(15.9)</b>	51.3
Cash and cash equivalents at beginning of the year	15	<b>77.6</b>	26.3
<b>Cash and cash equivalents at end of the year</b>	15	<b>61.7</b>	77.6



# 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 2011 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 7 March 2012.

## 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 as required by IFRS.

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 16.

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. As part of its contracting operations, it is sometimes 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, including a profit-based one, which 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.

Following the acquisitions of ClerkMaxwell Ltd and Promanex Group Holdings Ltd, IFRS 3 'Business combinations' is applicable for the first time.

The following standards and interpretations are effective for the year ended 31 December 2011 but are not material to the Group:

- Amendments to IFRS 1 'First-time Adoption of International Financial Reporting Standards'
- Amendments to IFRS 2 'Share-based payment'
- Amendments to IAS 32 'Financial Instruments: presentation'
- IFRIC 15 'Agreements for the Construction of Real Estate'
- IFRIC 19 'Extinguishing financial liabilities with equity instruments'

# Notes to the financial statements continued

## 2 Summary of significant accounting policies

continued

### 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 is negative, due to losses incurred, then an amount equal to 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. Transfers of any excess losses are shown within reclassifications in Note 13.
- (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, including goodwill and fair value adjustments, 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. Most of the Group's revenue arises from construction contracts.

### (a) Construction contracts

Revenue arises from increases in valuations on contracts. Where the outcome of a construction 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, except where this would not be representative of the stage of completion.

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

## 2 Summary of significant accounting policies

continued

### Revenue recognition continued

#### (a) Construction contracts continued

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 construction 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.

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 the sale of goods is recognised when the significant risks and rewards of ownership of the goods 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.

Revenue from services is recognised when the service is provided.

Revenue in respect of property development sales is recognised on the transfer to the buyer of the significant risks and rewards of ownership. This is typically achieved when the legal title is transferred. If at the time that the sale reaches legal completion there remains infrastructure works to complete, the nature and extent of the Group's continuing involvement is assessed to determine whether it is appropriate to recognise revenue. Where the conditions for revenue recognition are met, an appropriate amount is recognised. Amounts deferred in respect of infrastructure works are only recognised when such works are substantially complete.

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.

#### 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

Costs classified as relating to research and development activities are expensed as incurred.

#### Goodwill and other intangible assets

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

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

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

Amortisation begins when an asset is acquired or, in the case of computer software, available for use and is calculated on a straight-line basis to allocate the cost of the assets over their estimated useful lives.

#### 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.

# Notes to the financial statements continued

## 2 Summary of significant accounting policies

continued

### Investments – Company

Company investments in subsidiaries are carried at cost less impairment losses less any pre-acquisition dividends received.

### PFI investments

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

### Impairment of non-financial assets

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

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

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

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

### Provisions

A provision is recognised in the statement of financial position when there is a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

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

### Taxation

The tax expense represents the sum of United Kingdom corporation tax and Overseas tax currently payable and Deferred tax.

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

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

Deferred tax liabilities are recognised for temporary differences arising on investments in subsidiaries and interests in joint 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.



## 2 Summary of significant accounting policies

continued

### Taxation continued

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

### Leases

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

### Financial guarantee contracts

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

### Share capital

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

### Dividends

Dividends are recognised as distributions in the period in which they are declared. Dividends proposed but not declared are not recognised but are disclosed in 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 19. 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.

Any increase in the present value of the liabilities of the defined benefit pension scheme arising from employee service is charged to profit from operations in the period. The expected return on the scheme's assets and the increase during the period in the present value of the scheme's liabilities arising from the passage of time are included in finance income and finance expense respectively. Actuarial gains and losses 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.



# Notes to the financial statements continued

## 2 Summary of significant accounting policies

continued

### Financial assets and liabilities continued

#### (a) Financial assets continued

##### *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 individual receivables are provided against when management deem the amounts are not collectible.

##### *Cash and cash equivalents*

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

##### *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, except financial assets classified as at fair value through profit or loss, which are measured initially at fair value.

#### (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 in order 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; and
- 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.

## 2 Summary of significant accounting policies

continued

### Significant areas of judgment and estimation

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

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

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 19.

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 require 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. At 31 December 2011, a review of the net realisable value of each of its land holdings was undertaken, including the use of external valuations, and provisions, if considered necessary, 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.

### IFRSs not applied

The following Adopted IFRS has been endorsed but is not mandatory and has not been applied by the Group in these financial statements. Adoption is not expected to have a material effect on the financial statements.

- IFRS 7 'Amendments to Financial instruments': Disclosures – transfers of financial assets (mandatory for years commencing on or after 1 July 2011).

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.
- IAS 19 'Employee benefits' – this amendment will require the financing cost of a defined benefit scheme to be calculated on the net surplus or deficit. It will increase the net pension interest expense. It should be effective for 2013.
- IFRS 11 'Joint arrangements' – this may result in changes to the classification of certain jointly controlled operations where the Group accounts for its share of the individual assets and liabilities, to being equity accounted as associates or joint ventures. It will not affect the Group's profit for the period or net assets. It should be effective for 2013.

# Notes to the financial statements continued

## 3 Operating segments

Segment information is based on four business segments: Environment, Infrastructure, Energy & Process and Land Development operations in Spain. The segments are strategic business units with separate management reporting to a segment managing director and have different core customers or different services. This information is provided to the Chief Executive who is the chief operating decision maker. The segments are discussed in the Business review section of these financial statements.

The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies. The Group evaluates segment performance on the basis of profit or loss from operations before interest and income tax expense. 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.

2011	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
<b>Segment revenue</b>						
External revenue	281.8	448.5	138.2	-	-	868.5
Share of revenue of joint ventures and associates	93.6	17.5	5.2	1.5	-	117.8
<b>Total segment revenue</b>	<b>375.4</b>	<b>466.0</b>	<b>143.4</b>	<b>1.5</b>	<b>-</b>	<b>986.3</b>
<b>Segment profit/(loss)</b>						
Operating profit/(loss)	16.1	10.2	4.6	-	(6.8)	24.1
Profit on sale of non-consolidated subsidiary	0.5	-	-	-	-	0.5
Profit on sale of interests in joint venture	0.3	-	-	-	-	0.3
Share of results of joint ventures and associates	0.6	-	0.1	(2.0)	-	(1.3)
<b>Profit/(loss) from operations before other items</b>	<b>17.5</b>	<b>10.2</b>	<b>4.7</b>	<b>(2.0)</b>	<b>(6.8)</b>	<b>23.6</b>
Other items						
Amortisation of acquired intangible assets	-	(0.7)	(0.2)	-	-	(0.9)
Employment related deferred consideration	-	(0.3)	(0.4)	-	-	(0.7)
<b>Profit/(loss) from operations</b>	<b>17.5</b>	<b>9.2</b>	<b>4.1</b>	<b>(2.0)</b>	<b>(6.8)</b>	<b>22.0</b>
Net finance income						1.9
<b>Profit before tax</b>						<b>23.9</b>
Segment profit/(loss) is stated after charging the following:						
Depreciation	0.1	1.3	0.5	-	-	1.9
Amortisation (including acquired intangible assets)	-	0.7	0.2	-	-	0.9

### 3 Operating segments continued

Segment assets	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
Reportable segment assets	77.8	122.3	45.1	35.9	0.2	281.3
Unallocated assets:						
Deferred tax						17.4
Cash and cash equivalents						141.7
<b>Total assets</b>						<b>440.4</b>

Expenditure on non-current assets	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
Property, plant and equipment	–	3.4	0.4	–	–	3.8
Intangible assets	–	16.6	4.5	–	–	21.1
Loans to joint ventures and associates	10.3	–	–	3.2	–	13.5

Segment liabilities	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
Reportable segment liabilities	138.4	165.0	49.7	0.1	0.2	353.4
Unallocated liabilities:						
Retirement benefit obligations						52.9
Overdrafts						1.6
Income tax						1.7
<b>Total liabilities</b>						<b>409.6</b>

2010	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
<b>Segment revenue</b>						
External revenue	422.3	371.0	131.2	–	–	924.5
Share of revenue of joint ventures and associates	67.5	24.3	5.4	0.8	–	98.0
<b>Total segment revenue</b>	489.8	395.3	136.6	0.8	–	1,022.5

Segment profit/(loss)	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
Operating profit/(loss)	3.6	12.2	8.0	–	(6.4)	17.4
Profit on sales of joint ventures and associates	11.2	–	–	–	–	11.2
Profit on sale of land and property	1.3	–	–	–	–	1.3
Share of results of joint ventures and associates	1.1	–	0.2	(1.8)	–	(0.5)
<b>Profit/(loss) from operations</b>	17.2	12.2	8.2	(1.8)	(6.4)	29.4
Net finance expense						(1.5)
<b>Profit before tax</b>						<b>27.9</b>

Segment profit/(loss) is stated after charging the following:

Depreciation	–	1.3	0.4	–	–	1.7
Amortisation	0.4	0.4	0.1	–	–	0.9

# Notes to the financial statements continued

## 3 Operating segments continued

<b>Segment assets</b>	Environment £m	Infrastructure £m	Energy & Process £m	Land Development £m	Central costs £m	Total £m
Reportable segment assets	66.7	78.7	48.6	35.2	0.2	229.4
Unallocated assets:						
Deferred tax						20.9
Cash and cash equivalents						146.0
<b>Total assets</b>						<b>396.3</b>
<b>Expenditure on non-current assets</b>						
Property, plant and equipment	–	0.8	0.3	–	–	1.1
Loans to joint ventures and associates	3.5	–	–	2.4	–	5.9
<b>Segment liabilities</b>						
Reportable segment liabilities	156.5	112.1	46.6	–	0.5	315.7
Unallocated liabilities:						
Retirement benefit obligations						39.6
Overdrafts and loans						1.7
Income tax						1.7
<b>Total liabilities</b>						<b>358.7</b>

## 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.

	Revenue		Non-current assets	
	2011 £m	2010 £m	2011 £m	2010 £m
United Kingdom	<b>957.9</b>	1,000.8	<b>68.8</b>	48.8
Spain	<b>1.5</b>	0.8	<b>37.3</b>	35.0
Rest of the World	<b>26.9</b>	20.9	<b>2.3</b>	3.2
	<b>986.3</b>	1,022.5	<b>108.4</b>	87.0

## Customers accounting for more than 10% of revenue

One customer (2010: one) in the Infrastructure segment accounted for revenue of £155.4 million (2010: £126.9 million). In 2010, one customer in the Environment segment accounted for revenue of £163.2 million.



#### 4 Other operating expenses and income

	2011 £m	2010 £m
Profit before tax is stated after charging:		
Amortisation of intangible assets (Note 11)	0.9	0.9
Depreciation of property, plant and equipment (Note 12)	1.9	1.7
Hire of plant and machinery	23.1	28.6
Rent of land and buildings	3.2	2.9
and after crediting:		
Profit on sale of non-consolidated subsidiary	0.5	–
Profit on sales of interests in joint ventures and associates	0.3	11.2
Income from rent of land and buildings	1.4	1.6

In April 2011, the Group sold its interest in its Zimbabwe based contracting business, Ceezed Construction (Private) Limited, for net proceeds of £0.5 million.

In October 2011, the Group disposed of its interest in the assets of China Harbour-Costain Mexico S de RL de CV for net proceeds of £0.3 million.

The £11.2 million profit on sale of interests in joint ventures and associates in 2010 related to the transfer of a portfolio of six PFI investments to The Costain Pension Scheme for £22.0 million. As a result of this transfer, £8.1 million of fair value adjustments on the PFI financial assets relating to cash flow hedges was recycled through the income statement.

<b>Auditors' remuneration</b>	2011 £m	2010 £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 for other services		
– Audit of the Company's subsidiaries, pursuant to legislation	0.4	0.4
– Other services relating to taxation and acquisitions advice (2010: Taxation and pensions advice)	0.7	0.3
	<b>1.2</b>	<b>0.8</b>

Amounts paid to the Company's auditors and their 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 to be disclosed on a consolidated basis.

# Notes to the financial statements continued

## 5 Employee benefit expense

Group	2011 £m	2010 £m
Wages and salaries	139.9	130.9
Social security costs	14.9	13.2
Pension costs (Note 19)	5.3	6.5
Share-based payments expense (Note 19)	1.9	4.5
	<b>162.0</b>	155.1

Average number of persons employed	2011 Number	2010 Number
Environment	1,128	1,639
Infrastructure	1,615	1,263
Energy & Process	1,394	1,424
Central	22	23
	<b>4,159</b>	4,349

### 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.

## 7 Net finance income/(expense)

	2011 £m	2010 £m
Interest income from bank deposits	0.4	0.4
Interest income on loans to related parties	1.4	0.6
Expected return on defined benefit pension scheme assets (Note 19)	32.3	29.7
Finance income	<b>34.1</b>	30.7
Interest payable on bank overdrafts and other similar charges	(1.7)	(0.9)
Interest cost on the present value of the defined benefit obligations (Note 19)	(30.5)	(31.3)
Finance expense	<b>(32.2)</b>	(32.2)
Net finance income/(expense)	<b>1.9</b>	(1.5)

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

## 8 Income tax

	2011 £m	2010 £m
<b>On profit for the year</b>		
United Kingdom corporation tax at 26.5% (2010: 28.0%) – Adjustment in respect of prior years	0.1	0.2
Current tax credit for the year	0.1	0.2
Deferred tax charge for current year	(5.9)	(5.0)
Adjustment in respect of prior years	0.6	–
Deferred tax charge for the year	(5.3)	(5.0)
<b>Income tax expense in the consolidated income statement</b>	<b>(5.2)</b>	<b>(4.8)</b>
	2011 £m	2010 £m
<b>Tax reconciliation</b>		
Profit before tax	23.9	27.9
Income tax at 26.5% (2010: 28.0%)	(6.3)	(7.8)
Share of results of joint ventures and associates at 26.5% (2010: 28.0%)	(0.3)	(0.1)
Disallowed provisions and expenses	(0.3)	(0.9)
Non-taxable gains and profits relieved by capital losses	0.3	3.5
Utilisation of previously unrecognised temporary differences	0.3	0.8
Rate adjustments relating to deferred taxation and overseas profits and losses	0.4	(0.5)
Adjustments in respect of prior years	0.7	0.2
<b>Income tax expense in the consolidated income statement</b>	<b>(5.2)</b>	<b>(4.8)</b>
<b>Effective rate of tax</b>	<b>21.8%</b>	<b>17.2%</b>

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# Notes to the financial statements continued

## 8 Income tax continued

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 £1.7 million (2010: £1.7 million) for the Group and Company represent the amount of income taxes in respect of all outstanding periods.

Accumulated tax losses carried forward, mainly in the United Kingdom, were £5.8 million (2010: £6.0 million).

	2011 £m	2010 £m
<b>Deferred tax asset recognised at 25.0%</b> (2010: 27.0%)		
Accelerated capital allowances	1.9	2.2
Short-term temporary differences	1.8	8.0
Retirement benefit obligations	13.2	10.7
Tax losses	0.5	–
<b>Deferred tax asset</b>	<b>17.4</b>	<b>20.9</b>

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

	2011 £m	2010 £m
<b>Analysis of deferred tax movements</b>		
At 1 January	20.9	34.6
<b>Deferred tax relating to business combinations</b>		
Transfer in respect of business combinations	0.8	–
Transfer in respect of acquired intangible assets	(1.5)	–
	(0.7)	–
<b>Deferred tax in consolidated income statement</b>		
Accelerated capital allowances	(0.4)	(0.3)
Short-term temporary differences	(4.2)	5.8
Tax losses	(0.2)	–
Retirement benefit obligations	(0.5)	(10.5)
	(5.3)	(5.0)
<b>Deferred tax in other comprehensive income and expense statement</b>		
Retirement benefit obligations	3.0	(8.1)
<b>Deferred tax recognised directly in the consolidated changes in equity statement</b>		
Short-term temporary differences	(0.5)	(0.6)
<b>At 31 December</b>	<b>17.4</b>	<b>20.9</b>

## 8 Income tax continued

### 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.

#### Deferred tax asset not recognised at 25.0% (2010: 27.0%)

	Group		Company	
	2011 £m	2010 £m	2011 £m	2010 £m
Accelerated capital allowances	0.7	0.8	–	–
Short-term temporary differences	5.7	4.0	–	–
Trading tax losses	0.7	1.6	–	–
Management expenses and charges incurred by parent Company	14.2	15.4	14.2	15.4
Temporary differences	21.3	21.8	14.2	15.4
In addition to the above temporary differences, the following deferred tax assets are available.				
Surplus Advance Corporation Tax	9.7	9.7	–	–
Capital losses	68.9	74.4	60.3	67.3

The current year tax effect, at 26.5%, of using the above short-term temporary differences and trading tax losses was £0.3 million (2010: £0.8 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 23.0% from 1 April 2014 would reduce the deferred tax asset by £1.4 million.

## 9 Earnings per share

The calculation of earnings per share is based on profit of £18.7 million (2010: £23.1 million) and the number of shares set out below.

	2011 Number (millions)	2010 Number (millions)
Weighted average number of ordinary shares in issue for basic earnings per share calculation	64.1	63.5
Dilutive potential ordinary shares arising from employee share schemes	2.2	1.7
Weighted average number of ordinary shares in issue for diluted earnings per share calculation	66.3	65.2

At 31 December 2011, all options were included in the diluted weighted average number of ordinary shares calculation (2010: all).

## 10 Dividends

	Dividend per share pence	2011 £m	2010 £m
Final dividend for the year ended 31 December 2009	5.5	–	3.6
Interim dividend for the year ended 31 December 2010	3.0	–	1.9
Final dividend for the year ended 31 December 2010	6.25	3.9	–
Interim dividend for the year ended 31 December 2011	3.25	2.2	–
Amount recognised as distributions to equity holders in the year		6.1	5.5
Dividends settled in shares		(0.3)	(0.1)
Dividends settled in cash		5.8	5.4

A final dividend in respect of the year ended 31 December 2011 of 6.75p per share, amounting to a dividend of £4.4 million, is to be proposed at the Annual General Meeting. If approved, the dividend is expected to be paid on 25 May 2012 to shareholders registered at the close of business on 20 April 2012 and a scrip dividend alternative will be offered. These financial statements do not reflect the final dividend payable.



# Notes to the financial statements continued

## 11 Intangible assets

Group	Goodwill £m	Customer relationships £m	Other acquired intangibles £m	Software & development £m	Total £m
<b>Cost</b>					
At 1 January 2010	–	–	–	5.0	5.0
Additions	–	–	–	–	–
At 31 December 2010	–	–	–	5.0	5.0
At 1 January 2011	–	–	–	<b>5.0</b>	<b>5.0</b>
Acquired through business combinations	<b>15.2</b>	<b>4.1</b>	<b>1.7</b>	–	<b>21.0</b>
Other additions	–	–	–	<b>0.1</b>	<b>0.1</b>
<b>At 31 December 2011</b>	<b>15.2</b>	<b>4.1</b>	<b>1.7</b>	<b>5.1</b>	<b>26.1</b>
<b>Amortisation</b>					
At 1 January 2010	–	–	–	4.0	4.0
Provided in year	–	–	–	0.9	0.9
At 31 December 2010	–	–	–	4.9	4.9
At 1 January 2011	–	–	–	<b>4.9</b>	<b>4.9</b>
Provided in year	–	<b>0.7</b>	<b>0.2</b>	–	<b>0.9</b>
<b>At 31 December 2011</b>	–	<b>0.7</b>	<b>0.2</b>	<b>4.9</b>	<b>5.8</b>
<b>Net book value</b>					
<b>At 31 December 2011</b>	<b>15.2</b>	<b>3.4</b>	<b>1.5</b>	<b>0.2</b>	<b>20.3</b>
At 31 December 2010	–	–	–	0.1	0.1
At 1 January 2010	–	–	–	1.0	1.0

The net book value of other acquired intangible assets comprises £0.9 million relating to order book and £0.6 million relating to brand value (2010: £Nil).

Goodwill has been allocated to the applicable cash generating units identified within the Infrastructure and Energy & Process 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 14% and for the CGU in Energy & Process was 16%.

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 acquired businesses:

Growth rates	Infrastructure %	Energy & Process %
Year 3	5	40
Years 4-5	2.5	2.5
Long-term average	1.5	1.5

As at 31 December 2011, based on these internal valuations, the recoverable value of goodwill exceeded the carrying amounts.

## 12 Property, plant and equipment

Group	Land and buildings £m	Plant and equipment £m	Total £m
<b>Cost</b>			
At 1 January 2010	2.0	21.4	23.4
Currency realignment	–	0.1	0.1
Additions	–	1.1	1.1
Disposals	(1.1)	(2.5)	(3.6)
At 31 December 2010	0.9	20.1	21.0
At 1 January 2011	<b>0.9</b>	<b>20.1</b>	<b>21.0</b>
Additions	–	<b>2.9</b>	<b>2.9</b>
Disposals	<b>(0.2)</b>	<b>(0.5)</b>	<b>(0.7)</b>
Acquired through business combinations	<b>0.2</b>	<b>0.7</b>	<b>0.9</b>
<b>At 31 December 2011</b>	<b>0.9</b>	<b>23.2</b>	<b>24.1</b>
<b>Depreciation</b>			
At 1 January 2010	0.4	11.5	11.9
Provided in year	0.3	1.4	1.7
Disposals	(0.1)	(2.2)	(2.3)
At 31 December 2010	0.6	10.7	11.3
At 1 January 2011	<b>0.6</b>	<b>10.7</b>	<b>11.3</b>
Provided in year	<b>0.1</b>	<b>1.8</b>	<b>1.9</b>
Disposals	<b>(0.1)</b>	<b>(0.4)</b>	<b>(0.5)</b>
<b>At 31 December 2011</b>	<b>0.6</b>	<b>12.1</b>	<b>12.7</b>
<b>Net book value</b>			
<b>At 31 December 2011</b>	<b>0.3</b>	<b>11.1</b>	<b>11.4</b>
At 31 December 2010	0.3	9.4	9.7
At 1 January 2010	1.6	9.9	11.5

## 13 Investments and loans in subsidiaries, equity accounted joint ventures and associates

Group	Investments		Loans		Total £m
	Joint ventures £m	Associates £m	Joint ventures £m	Associates £m	
<b>Cost or fair value</b>					
At 1 January 2010	27.3	0.6	23.9	8.9	60.7
Currency realignment	(0.6)	–	(0.4)	–	(1.0)
Additions	–	–	5.9	–	5.9
Repayments	–	–	(0.5)	–	(0.5)
Reclassifications	14.5	(0.4)	(14.5)	(1.8)	(2.2)
Disposals	(2.4)	–	(3.6)	(5.6)	(11.6)
At 31 December 2010	38.8	0.2	10.8	1.5	51.3
At 1 January 2011	<b>38.8</b>	<b>0.2</b>	<b>10.8</b>	<b>1.5</b>	<b>51.3</b>
Currency realignment	<b>(0.7)</b>	–	<b>(0.3)</b>	<b>(0.1)</b>	<b>(1.1)</b>
Additions	–	–	<b>3.2</b>	<b>10.3</b>	<b>13.5</b>
Repayments	–	–	–	<b>(0.4)</b>	<b>(0.4)</b>
<b>At 31 December 2011</b>	<b>38.1</b>	<b>0.2</b>	<b>13.7</b>	<b>11.3</b>	<b>63.3</b>

# Notes to the financial statements continued

## 13 Investments and loans in subsidiaries, equity accounted joint ventures and associates continued

Group	Investments		Loans		Total £m
	Joint ventures £m	Associates £m	Joint ventures £m	Associates £m	
<b>Share of post-acquisition reserves</b>					
At 1 January 2010	(18.4)	(5.5)	–	–	(23.9)
Currency realignment	(0.2)	–	–	–	(0.2)
Disposals	2.1	(0.3)	–	–	1.8
Reclassifications	–	1.0	–	–	1.0
Dividends	–	(0.1)	–	–	(0.1)
(Loss)/profit for the year	(1.4)	0.9	–	–	(0.5)
Cash flow hedges – change in fair value	–	(1.3)	–	–	(1.3)
Cash flow hedges – disposals	3.6	4.5	–	–	8.1
At 31 December 2010	(14.3)	(0.8)	–	–	(15.1)
At 1 January 2011	<b>(14.3)</b>	<b>(0.8)</b>	–	–	<b>(15.1)</b>
Currency realignment	<b>0.2</b>	–	–	–	<b>0.2</b>
Dividends	<b>(0.8)</b>	<b>(0.6)</b>	–	–	<b>(1.4)</b>
(Loss)/profit for the year	<b>(1.8)</b>	<b>0.5</b>	–	–	<b>(1.3)</b>
Cash flow hedges – change in fair value	–	<b>(2.8)</b>	–	–	<b>(2.8)</b>
<b>At 31 December 2011</b>	<b>(16.7)</b>	<b>(3.7)</b>	–	–	<b>(20.4)</b>
<b>Amounts written off</b>					
At 1 January 2010	–	(0.2)	–	(0.2)	(0.4)
Reclassifications	–	0.2	–	0.2	0.4
<b>At 31 December 2010 and 2011</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
<b>Reclassifications</b>					
At 1 January 2010	18.3	6.7	(11.1)	(6.2)	7.7
Arising in the year	(18.3)	(4.6)	11.1	5.3	(6.5)
At 31 December 2010	–	2.1	–	(0.9)	1.2
At 1 January 2011	–	<b>2.1</b>	–	<b>(0.9)</b>	<b>1.2</b>
Arising in the year	–	<b>2.8</b>	–	<b>(4.0)</b>	<b>(1.2)</b>
<b>At 31 December 2011</b>	<b>–</b>	<b>4.9</b>	<b>–</b>	<b>(4.9)</b>	<b>–</b>
<b>Net book value</b>					
<b>At 31 December 2011</b>	<b>21.4</b>	<b>1.4</b>	<b>13.7</b>	<b>6.4</b>	<b>42.9</b>
At 31 December 2010	24.5	1.5	10.8	0.6	37.4
At 1 January 2010	27.2	1.6	12.8	2.5	44.1

### 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

	2011				2010			
	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	1.5	80.4	35.9	117.8	0.8	81.1	16.1	98.0
(Loss)/profit before tax	(2.0)	0.2	0.8	(1.0)	(2.5)	0.5	1.4	(0.6)
Income tax	–	–	(0.3)	(0.3)	0.7	(0.1)	(0.5)	0.1
(Loss)/profit for the year	(2.0)	0.2	0.5	(1.3)	(1.8)	0.4	0.9	(0.5)
Non-current assets	20.9	–	1.0	21.9	23.6	–	54.5	78.1
Current assets	31.2	30.3	113.6	175.1	32.7	21.4	18.9	73.0
Current liabilities	(5.3)	(30.2)	(11.3)	(46.8)	(15.5)	(20.7)	(6.9)	(43.1)
Non-current liabilities	(25.5)	–	(101.9)	(127.4)	(17.0)	–	(65.0)	(82.0)
Investments in joint ventures and associates	21.3	0.1	1.4	22.8	23.8	0.7	1.5	26.0
Financial commitments	–	–	3.6	3.6	–	–	14.8	14.8
Capital commitments	–	–	13.4	13.4	–	–	48.2	48.2

Net interest payable by joint ventures and associates in 2011 was £2.5 million (2010: £0.9 million payable). The applicable interest rates are income of 0.2% to 0.4% per annum (2010: 0% to 0.3%) and expense of 5.4% to 11.5% per annum (2010: 1.3% to 11.5%).

The financial commitments relate to associates involved in PFI schemes and the capital commitments relate 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

	2011				2010			
	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	3.0	176.3	119.4	298.7	1.6	175.7	57.3	234.6
(Loss)/profit before tax	(4.1)	0.4	3.5	(0.2)	(5.0)	0.7	4.0	(0.3)
Income tax	–	(0.1)	(0.9)	(1.0)	1.4	(0.2)	(1.6)	(0.4)
(Loss)/profit for the year	(4.1)	0.3	2.6	(1.2)	(3.6)	0.5	2.4	(0.7)
Non-current assets	42.0	–	2.4	44.4	43.4	–	203.5	246.9
Current assets	62.4	69.2	369.3	500.9	65.5	51.3	56.7	173.5
Current liabilities	(10.5)	(68.9)	(38.5)	(117.9)	(31.1)	(49.7)	(25.5)	(106.3)
Non-current liabilities	(50.9)	–	(328.1)	(379.0)	(29.2)	–	(230.1)	(259.3)
Equity	43.0	0.3	5.1	48.4	48.6	1.6	4.6	54.8

Details of the principal subsidiary undertakings, joint ventures, jointly controlled operations and associates are shown in Note 23.

# Notes to the financial statements continued

## 13 Investments and loans in subsidiaries, equity accounted joint ventures and associates continued

### Company

Investments in subsidiaries	£m
<b>Cost</b>	
At 1 January 2010	390.0
Additions	2.2
At 31 December 2010	392.2
At 1 January 2011	<b>392.2</b>
Additions	<b>1.9</b>
<b>At 31 December 2011</b>	<b>394.1</b>
<b>Amounts written off</b>	
At 1 January 2010	(275.5)
Released	6.3
At 31 December 2010	(269.2)
At 1 January 2011	<b>(269.2)</b>
Provided	<b>(3.5)</b>
<b>At 31 December 2011</b>	<b>(272.7)</b>
<b>Net book value</b>	
<b>At 31 December 2011</b>	<b>121.4</b>
At 31 December 2010	123.0
At 1 January 2010	114.5

Additions relate to the increase in the cost of investments in subsidiaries by the equivalent amount of the equity settled share-based payment charge in relation to employees of subsidiaries included in the income statement. The amount written off in the year is a provision against the carrying value of Costain Alcaidesa Ltd.

Details of the principal subsidiaries in which the Company has an interest are set out in Note 23.

## 14 Trade and other receivables

	Group		Company	
	2011 £m	2010 £m	2011 £m	2010 £m
<b>Amounts included in current assets</b>				
Trade receivables	<b>84.8</b>	54.9	-	-
Other receivables	<b>15.2</b>	6.9	-	-
Amounts due from customers for contract work	<b>74.3</b>	93.1	-	-
Prepayments and accrued income	<b>13.2</b>	6.7	<b>0.9</b>	0.2
Amounts owed by joint ventures and associates	<b>0.5</b>	0.4	-	-
Amounts owed by subsidiary undertakings	-	-	<b>7.2</b>	5.6
	<b>188.0</b>	162.0	<b>8.1</b>	5.8
<b>Amounts included in non-current assets</b>				
Other	<b>16.4</b>	18.9	-	-

At 31 December 2011, amounts due from customers for contract work falling due within one year and other receivables falling due after more than one year included retentions of £21.0 million (2010: £28.8 million) relating to construction contracts in progress.

The directors consider that the carrying amount of trade, other receivables and amounts owed by joint ventures and associates approximates to their fair value. Based on prior experience, the directors believe that the trade receivables are recoverable and, other than as disclosed in Note 25, there is no allowance for bad or doubtful debts (2010: £Nil).



## 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 31 days (2010: 30 days). The analysis of the due dates of the trade receivables was £61.5 million (2010: £39.3 million) due within 30 days, £19.6 million (2010: £14.1 million) due between 30 and 60 days and £3.7 million (2010: £1.5 million) due after 60 days.

Included in the trade receivables balance are debtors, with a carrying amount of £6.1 million (2010: £2.2 million), which are past due at the reporting date 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 aggregate amount of costs incurred plus recognised profits, less recognised losses, for all contracts in progress at the statement of financial position date was £2,789.6 million (2010: £3,132.5 million). Progress billings and advances received from customers under open construction contracts amounted to £2,757.9 million (2010: £3,070.5 million). Advances for which work has not started, and billings in excess of costs incurred and recognised profits are included in credit balances on long-term contracts (Note 17).

## 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 £33.6 million (2010: £33.8 million).

	Group		Company	
	2011 £m	2010 £m	2011 £m	2010 £m
Cash and cash equivalents	141.7	146.0	61.7	77.6
Bank overdrafts	(1.6)	(1.7)	-	-
<b>Cash, cash equivalents and overdrafts in the cash flow statement</b>	<b>140.1</b>	<b>144.3</b>	<b>61.7</b>	<b>77.6</b>

## 16 Financial instruments and risk management

The Group's centralised treasury function manages financial risk, principally arising from movements in foreign currency rates, interest rates and inflation rates and liquidity and funding risks, in accordance with policies agreed by the directors. To manage these risks, forward foreign currency sale and purchase contracts are used in respect of foreign currency requirements and interest rate and RPI swaps are used for PFI investments.

The Group does not enter into speculative transactions.

The Company does not have any forward foreign currency contracts or other derivatives.

### 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 Group has no long-term debt and 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 Business review 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.

The Group increased its banking and bonding facilities during the year and these now include a £45 million Revolving Credit Facility. It also extended the term of the facilities to 30 September 2015 and revised the covenant structure. The new facilities have financial covenants based on profit, interest cover and leverage measured quarterly. There were no other changes in the Board's approach to capital management during the year.

### 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 cash balance during the year was £130.4 million (2010: £116.0 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. Therefore, it has facilities in place to provide these bonds and it monitors the usage and regularly updates the forecast usage of these facilities.

# Notes to the financial statements continued

## 16 Financial instruments and risk management continued

### Unsecured bonding facilities available

	Group and Company	
	2011 £m	2010 £m
Expiring between two and five years*	420.0	345.0
* Element of above facilities available for borrowings	2.5	5.0

#### 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 do 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.

#### 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 net interest income on cash balances by £1.3 million (2010: £1.2 million).

The only interest rate hedging currently undertaken by the Group is within PFI investments, where interest rate derivatives have been used as a means of hedging interest rate risk. The policy is to fix the interest cost on variable rate financing on specific projects by taking out floating to fixed interest rate swaps; these swaps are designated to the underlying debt obligations and are expected to be effective for cash flow hedge accounting purposes.

#### 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. Forward contracts are only entered into when a contractual commitment exists in respect of the foreign currency transaction and it is the policy to negotiate the terms of the hedge derivatives to match the terms of the hedged item to maximise hedge effectiveness.

At 31 December 2011, the net monetary assets denominated in currencies other than the functional currency of the operation involved were US Dollar denominated net assets of £0.1 million (2010: £0.2 million) and Euro denominated net monetary assets of £16.5 million (2010: £10.9 million) in members of the Group with sterling as their functional currency.

A 10% strengthening in the US Dollar would have impacted the results favourably by £0.1 million (2010: £Nil). A 10% strengthening in the Euro would have adversely impacted the results by £0.2 million (2010: adversely impacted by £0.2 million). A 10% strengthening in the UAE Dirham would have adversely impacted the results by £0.2 million (2010: £0.3 million).

## 16 Financial instruments and risk management continued

### Cash flow hedges

The Group uses foreign currency contracts and interest rate swaps. Foreign currency contracts are measured using quoted forward exchange rates and yield curves derived from quoted interest rates matching maturities of the contracts. 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 2011, the Group had foreign currency contracts (26 purchase contracts (2010: 67) and 11 sale contracts (2010: 33)) designated as hedges of committed future purchases. The Group held no other foreign currency sale contracts (2010: Nil).

Forward currency contracts, which 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 (2010: Nil).

Foreign currency sale and purchase contracts outstanding at 31 December 2011 are summarised below. The carrying value represents the fair value of the contract; the contractual cash flows represent the sterling commitments.

### Foreign exchange contracts

	2011				2010			
	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	(0.5)	(10.7)	(6.4)	(4.3)	(0.8)	(47.0)	(40.3)	(6.7)
Sales	0.2	4.5	2.2	2.3	0.4	17.5	13.1	4.4
	(0.3)	(6.2)	(4.2)	(2.0)	(0.4)	(29.5)	(27.2)	(2.3)

The expected impact on the income statement of the foreign exchange contracts is: 2012 loss £0.2 million, 2013 loss £0.1 million.

At 31 December 2011, PFI project companies in which the Group has an interest and records 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 year-end (2010: Nil).

### Maturity of PFI swaps

	2011				2010			
	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	6.0	0.3	1.2	4.5	2.8	0.2	0.6	2.0
Less tax	(1.5)	(0.1)	(0.3)	(1.1)	(1.1)	(0.1)	(0.3)	(0.7)
	4.5	0.2	0.9	3.4	1.7	0.1	0.3	1.3

These amounts (net of tax) were recognised as fair value derivatives within the value of the investment or, if a future commitment exists, within provisions.

# Notes to the financial statements continued

## 16 Financial instruments and risk management continued

### Financial liabilities and assets

#### Currency and maturity of financial assets

	2011				2010			
	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	135.9	135.9	–	–	142.3	142.3	–	–
UAE Dirham	2.6	2.6	–	–	3.2	3.2	–	–
US Dollar	0.3	0.3	–	–	0.2	0.2	–	–
Euro	2.8	2.8	–	–	0.1	0.1	–	–
Other	0.1	0.1	–	–	0.2	0.2	–	–
	<b>141.7</b>	<b>141.7</b>	<b>–</b>	<b>–</b>	<b>146.0</b>	<b>146.0</b>	<b>–</b>	<b>–</b>
Loans to joint ventures and associates:								
Pounds sterling	6.4	0.6	2.4	3.4	0.6	0.2	0.4	–
Euro	13.7	–	13.7	–	10.8	–	10.8	–
	<b>20.1</b>	<b>0.6</b>	<b>16.1</b>	<b>3.4</b>	<b>11.4</b>	<b>0.2</b>	<b>11.2</b>	<b>–</b>
Trade, other receivables and amounts owed by joint ventures and associates:								
Pounds sterling	113.7	97.3	16.4	–	80.3	61.4	18.9	–
Other	3.2	3.2	–	–	0.8	0.8	–	–
	<b>116.9</b>	<b>100.5</b>	<b>16.4</b>	<b>–</b>	<b>81.1</b>	<b>62.2</b>	<b>18.9</b>	<b>–</b>
<b>Total financial assets</b>	<b>278.7</b>	<b>242.8</b>	<b>32.5</b>	<b>3.4</b>	<b>238.5</b>	<b>208.4</b>	<b>30.1</b>	<b>–</b>

#### Currency and maturity of financial liabilities

	2011			2010		
	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 overdraft – UAE Dirham	1.6	1.6	–	1.7	1.7	–
Trade and other payables:						
Pounds sterling	148.4	142.3	6.1	134.4	129.2	5.2
Other	6.4	6.4	–	5.5	5.5	–
	<b>154.8</b>	<b>148.7</b>	<b>6.1</b>	<b>139.9</b>	<b>134.7</b>	<b>5.2</b>
<b>Total financial liabilities</b>	<b>156.4</b>	<b>150.3</b>	<b>6.1</b>	<b>141.6</b>	<b>136.4</b>	<b>5.2</b>

The bank overdrafts are at a floating rate and are unsecured.

**16 Financial instruments and risk management** continued**Currency and maturity of financial liabilities** continued

Reconciliation of trade and other receivables and trade and other payables to the balance sheet.

	2011		2010	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other receivables (as above)	100.5	16.4	62.2	18.9
Amounts due from customers	74.3	–	93.1	–
Prepayments and accrued income	13.2	–	6.7	–
	<b>188.0</b>	<b>16.4</b>	162.0	18.9

	2011		2010	
	Current £m	Non-current £m	Current £m	Non-current £m
Trade and other payables (as above)	148.7	6.1	134.7	5.2
Credit balances on long-term contracts	22.3	–	21.2	–
Accruals and deferred income	171.9	–	148.9	–
	<b>342.9</b>	<b>6.1</b>	304.8	5.2

**Effective interest rates of financial assets and liabilities**

	2011	2010
<b>Financial assets</b>		
Cash and cash equivalents	0.0% to 1.3%	0.0% to 0.5%
Loans to joint ventures and associates	10.0% to 11.5%	10.0% to 11.5%
<b>Financial liabilities</b>		
Bank overdrafts	5.5%	5.0%

The Company's financial assets comprised cash at bank of £61.7 million (2010: £77.6 million) denominated in Pounds sterling and maturing within one year.

There are no significant differences between the carrying values of the Group's and Company's financial assets and liabilities and their fair values except the fair values of loans carrying interest rates above 10% may be higher than their carrying values of £6.4 million (2010: £0.6 million).

**17 Trade and other payables**

	Group		Company	
	2011 £m	2010 £m	2011 £m	2010 £m
<b>Current liabilities</b>				
Trade payables	108.1	107.6	–	–
Other payables	23.3	19.3	–	–
Social security	4.6	3.9	–	–
Credit balances on long-term contracts	22.3	21.2	–	–
Accruals and deferred income	171.9	148.9	0.6	0.1
Amounts owed to joint ventures and associates	12.7	3.9	–	–
Amounts owed to subsidiary undertakings	–	–	106.9	117.8
	<b>342.9</b>	304.8	<b>107.5</b>	117.9
<b>Non-current liabilities</b>				
Other payables	6.1	5.2	–	–



# Notes to the financial statements continued

## 17 Trade and other payables continued

At 31 December 2011, credit balances on long-term contracts included advance payments from customers of £13.1 million (2010: £10.7 million).

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.

## 18 Provisions for other liabilities and charges

Group	Engineering & Construction £m	Void space £m	PFI investments £m	Other £m	Total £m
<b>Current</b>					
At 1 January 2010	0.2	0.7	3.4	0.9	5.2
Provided	–	0.1	0.6	0.5	1.2
Utilised	–	(0.1)	–	(0.3)	(0.4)
Disposals	–	–	(3.4)	–	(3.4)
Transfer	–	–	0.6	–	0.6
At 31 December 2010	0.2	0.7	1.2	1.1	3.2
At 1 January 2011	<b>0.2</b>	<b>0.7</b>	<b>1.2</b>	<b>1.1</b>	<b>3.2</b>
Provided	<b>0.1</b>	<b>0.2</b>	–	<b>0.3</b>	<b>0.6</b>
Utilised	–	<b>(0.1)</b>	–	–	<b>(0.1)</b>
Released	–	–	–	<b>(0.6)</b>	<b>(0.6)</b>
Transfer	–	<b>0.2</b>	<b>(1.2)</b>	–	<b>(1.0)</b>
<b>At 31 December 2011</b>	<b>0.3</b>	<b>1.0</b>	–	<b>0.8</b>	<b>2.1</b>
<b>Non-current</b>					
At 1 January 2010	–	0.5	0.6	2.0	3.1
Currency alignment	–	–	–	0.1	0.1
Provided	–	0.1	–	0.1	0.2
Utilised	–	(0.2)	–	(0.1)	(0.3)
Transfer	–	–	(0.6)	–	(0.6)
At 31 December 2010	–	0.4	–	2.1	2.5
At 1 January 2011	–	<b>0.4</b>	–	<b>2.1</b>	<b>2.5</b>
Provided	–	–	–	–	–
Utilised	–	–	–	–	–
Transfer	–	<b>(0.2)</b>	–	–	<b>(0.2)</b>
<b>At 31 December 2011</b>	–	<b>0.2</b>	–	<b>2.1</b>	<b>2.3</b>

**18 Provisions for other liabilities and charges** continued

<b>Company</b>	Funding obligations £m	Other £m	Total £m
<b>Current</b>			
At 1 January 2010	0.1	0.3	0.4
Released	–	(0.2)	(0.2)
Transfer	0.1	–	0.1
At 31 December 2010	0.2	0.1	0.3
At 1 January 2011	<b>0.2</b>	<b>0.1</b>	<b>0.3</b>
Provided	–	<b>0.2</b>	<b>0.2</b>
Utilised	<b>(0.1)</b>	–	<b>(0.1)</b>
Transfer	<b>0.1</b>	–	<b>0.1</b>
<b>At 31 December 2011</b>	<b>0.2</b>	<b>0.3</b>	<b>0.5</b>
<b>Non-current</b>			
At 1 January 2010	1.5	–	1.5
Transfer	(0.1)	–	(0.1)
At 31 December 2010	1.4	–	1.4
At 1 January 2011	<b>1.4</b>	–	<b>1.4</b>
Transfer	<b>(0.1)</b>	–	<b>(0.1)</b>
<b>At 31 December 2011</b>	<b>1.3</b>	–	<b>1.3</b>

**Group**

Void space provisions relate to costs of vacant properties and will be utilised over the next three years.

PFI investment provisions relate investments where the carrying value of the investment is negative and an obligation exists to provide further funding. The provisions are expected to reverse when the obligation to provide funding is satisfied, expected to be within one year.

Other provisions, mainly comprise remedial costs and litigation provisions, most of which will be utilised over the next year and a provision for staff benefits payable to the staff of an Overseas subsidiary company, which will be utilised over the next five years.

**Company**

Provisions in the Company relate to funding obligations to a non-trading Overseas subsidiary, which eliminates on consolidation and a void space provision that is expected to be used within one year.

**19 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 £3.5 million comprising £5.3 million included in operating costs less £1.8 million included in net finance income (2010: £8.1 million, comprising £6.5 million in operating costs and £1.6 million in net finance expense).

The Company does not operate a pension scheme.

# Notes to the financial statements continued

## 19 Employee benefits continued

### (a) Pensions continued

#### Defined benefit scheme

The defined benefit scheme was closed to new members on 31 May 2005 and from 1 April 2006 future benefits were calculated on a Career Average Revalued Earnings basis. The scheme was closed to future accrual of benefits to members on 30 September 2009. A full actuarial valuation of the scheme was carried out at 31 March 2010 and was updated to 31 December 2011 by a qualified independent actuary.

	2011 £m	2010 £m	2009 £m
Present value of defined benefit obligations	<b>(600.8)</b>	(576.7)	(560.5)
Fair value of scheme assets	<b>547.9</b>	537.1	455.8
<b>Recognised liability for defined benefit obligations</b>	<b>(52.9)</b>	(39.6)	(104.7)

#### Movements in present value of defined benefit obligations

	2011 £m	2010 £m
At 1 January	<b>576.7</b>	560.5
Past service cost	–	1.2
Interest cost	<b>30.5</b>	31.3
Actuarial losses	<b>18.2</b>	8.5
Benefits paid	<b>(24.6)</b>	(24.8)
<b>At 31 December</b>	<b>600.8</b>	576.7

#### Movements in fair value of scheme assets

	2011 £m	2010 £m
At 1 January	<b>537.1</b>	455.8
Expected return on scheme assets	<b>32.3</b>	29.7
Actuarial (losses)/gains	<b>(3.9)</b>	33.1
Contributions by employer	<b>7.0</b>	43.3
Benefits paid	<b>(24.6)</b>	(24.8)
<b>At 31 December</b>	<b>547.9</b>	537.1

#### (Income)/expense recognised in the income statement

	2011 £m	2010 £m
Past service cost	–	1.2
Interest cost on defined benefit obligations (Note 7)	<b>30.5</b>	31.3
Expected return on scheme assets (Note 7)	<b>(32.3)</b>	(29.7)
<b>Total</b>	<b>(1.8)</b>	2.8

**19 Employee benefits** continued**(a) Pensions** continued**Income statement classification of (income)/expense**

	2011 £m	2010 £m
Cost of sales	-	1.0
Administrative expenses	-	0.2
Finance income	(32.3)	(29.7)
Finance expense	30.5	31.3
<b>Total</b>	<b>(1.8)</b>	<b>2.8</b>

**History of the scheme for the last five years**

	2011	2010	2009	2008	2007
Experience adjustments					
Experience gain/(loss) on scheme liabilities (£m)	-	18.5	-	-	6.5
	-	3%	-	-	1%
Change in assumptions on scheme liabilities (£m)	(18.2)	(27.0)	(113.7)	94.6	9.4
	3%	5%	20%	19%	2%
Experience adjustments on scheme assets (£m)	(3.9)	33.1	46.3	(105.1)	(4.2)
	1%	6%	10%	27%	1%
Total (loss)/gain (£m)	(22.1)	24.6	(67.4)	(10.5)	11.7

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 £60.2 million (2010: £38.2 million).

**Fair value of scheme assets and the return on scheme assets**

	2011 £m	2010 £m
Equities	173.9	207.9
High yield bonds	52.8	54.0
Government bonds	223.4	131.2
Corporate bonds	-	53.0
Infrastructure and property	43.7	36.0
Absolute return funds and cash	54.1	55.0
	547.9	537.1

The infrastructure holding is the portfolio of six PFI investments transferred by the Group to The Costain Pension Scheme in 2010.

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)**

	2011 %	2010 %	2009 %
Discount rate	4.80	5.40	5.70
Expected rate of return on scheme assets	4.95	6.11	6.51
Future pension increases	2.90	3.40	3.50
Inflation assumption	3.00	3.40	3.50

The expected rate of return on scheme assets is determined by reference to relevant indices. The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the scheme's investment portfolio.

# Notes to the financial statements continued

## 19 Employee benefits continued

### (a) Pensions continued

The switch from RPI to CPI relates only to Guaranteed Minimum Pensions (GMPs) accrued between 6 April 1988 and 5 April 1997. Under the rules of the scheme, these GMP amounts are increased in the course of payment in line with statutory requirements (which now provide for increases in line with CPI rather than RPI). Benefits in excess of the GMP continue to be increased in line with RPI in accordance with the provisions of the rules. The impact on the liability of allowing for 3% CPI rather than 3% RPI on the post 1988 GMP is around £4.5 million.

Weighted average life expectancy from age 65 as per mortality tables used to determine benefits at 31 December 2011 and 31 December 2010 is:

	2011		2010	
	Male (years)	Female (years)	Male (years)	Female (years)
Currently aged 65	21.5	23.7	21.4	23.6
Non-retirees	24.4	25.6	24.2	25.5

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 increases pension cost by	28.0	0.1
Decrease inflation, pension increases by 0.25%, decreases pension liability and reduces pension cost by	25.1	1.2
Increase life expectancy by one year, increases pension liability and increases pension cost by	15.5	0.7

The Group expects to contribute an amount equal to dividends paid to shareholders and the expenses of administration to its defined benefit scheme in the next financial year.

### Defined contribution schemes

Several defined contribution pensions are operated. The total expense relating to these plans was £5.3 million (2010: £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')

The Long-term Incentive Plan was approved by shareholders at the 2002 AGM. The LTIP allows for conditional awards with a maximum face value of up to 100% of base salary with a performance condition based on EPS.

#### 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 will vest on the second anniversary of the date of grant. The shares to satisfy the deferred bonus will be purchased by a trust on behalf of the Group and so 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 which are open to all employees. Employees 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 using the funds saved. If employees decide not to exercise their options, they may withdraw the funds saved; the options expire six months after maturity. Exercise of options is subject to continued employment within the Group (except where permitted by the rules of the scheme).



**19 Employee benefits** continued**(b) Share-based payments** continued*Share based payment expense*

The amounts recognised in the income statement, before income tax, for share-based payment transactions with employees was £1.9 million (2010: £4.5 million); the entire charge relates to subsidiaries.

*Options outstanding at the end of the year*

Outstanding awards granted prior to 2010 have been restated for the 1 to 10 share consolidation in 2010 and the rights issue in 2007.

The following LTIPs arrange for the grant of shares to Executive Directors and senior management at an exercise price of £1 per individual grant. The DSBPs arrange for the Nil-cost option grant of shares to Executive Directors and senior management. The weighted average exercise price of the outstanding SAYE schemes is shown below.

	LTIP	DSBP	SAYE	
	Number (m)	Number (m)	Number (m)	Weighted average exercise price (p)
Outstanding at 1 January 2010	2.4	0.5	2.4	227.0
Adjusted during the year	–	(0.1)	–	–
Forfeited during the year	(0.2)	(0.1)	(0.4)	249.0
Granted during the year	0.7	0.9	–	–
Outstanding at 31 December 2010	2.9	1.2	2.0	223.4
Adjusted during the year	–	(0.2)	–	–
Forfeited during the year	(0.2)	(0.2)	(0.3)	308.8
Exercised during the year	(1.5)	–	(0.8)	196.0
Granted during the year	0.8	0.6	1.0	186.5
<b>Outstanding at 31 December 2011</b>	<b>2.0</b>	<b>1.4</b>	<b>1.9</b>	<b>199.0</b>
<b>Exercisable at the end of the period</b>	<b>–</b>	<b>–</b>	<b>0.2</b>	<b>196.0</b>

Share options outstanding at the end of the year had a weighted average remaining contractual life of 3.6 years (2010: 3 years).

*Fair value of options granted during the year*

The fair value of options granted are calculated using the Black-Scholes option pricing model. The aggregate fair value of options granted during the year was £3.2 million (2010: £2.7 million). The assumptions used in valuing the grants were:

	2011	2010
Expected volatility	<b>20%</b>	20%
Expected life (years)	<b>2.7 – 5.0</b>	2.7
Risk-free interest rate	<b>3.6%</b>	4.2%
Expected dividend yield	<b>2%</b>	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 managements best estimate having regard to the effect of non-transferability, exercise restrictions and behavioural considerations.

# Notes to the financial statements continued

## 20 Share capital

	2011		2010	
	Number (millions)	Nominal value (£m)	Number (millions)	Nominal value (£m)
<b>Authorised share capital</b>				
Ordinary shares of 50p each	101.5	50.7	101.5	50.7
Shares in issue at beginning of year – Ordinary shares of 50p each, fully paid	63.5	31.7	63.4	31.7
Issued in year (see below)	1.2	0.7	0.1	–
Shares in issue at end of year – Ordinary shares of 50p each, fully paid	64.7	32.4	63.5	31.7

The Company's issued share capital comprised 64,706,925 ordinary shares of 50 pence each.

On 5 April 2011, the Company issued 351,847 shares following the exercise of options granted under the 2007 and 2008 LTIPs.

The Company announced on 18 May 2011 that shareholders had, pursuant to the Scrip Dividend Scheme, elected to receive 59,673 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 2010, and a further 43,377 ordinary shares on 26 October 2011 in lieu of cash in respect of all or part of their interim dividend for the year ended 31 December 2011.

During the year, the Company issued 765,096 shares on exercise of options granted under the 2008 3-year SAYE scheme.

All shares rank pari passu regarding entitlement to capital and dividends.

The share options outstanding at the year-end are detailed in Note 19. Details of the performance conditions and the options granted to executive directors are given in the Directors' remuneration report.

## 21 Contingent liabilities

	Group		Company	
	2011 (£m)	2010 (£m)	2011 (£m)	2010 (£m)
Under guarantees of bank overdrafts to subsidiary companies	–	–	1.6	1.7

### Group

Certain subsidiary undertakings have entered into cross-guarantees for overdraft facilities made available to the Group. At 31 December 2011, these liabilities amounted to £Nil (2010: £Nil).

There are also 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;
- 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 18).

### 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 2011, the potential liability was £52.9 million (2010: £39.6 million) as disclosed in Note 19.

## 22 Other financial commitments

### Group

#### Operating lease commitments

	2011		2010	
	Land and buildings £m	Other operating leases £m	Land and buildings £m	Other operating leases £m
<b>Leases as lessee</b>				
Future aggregate minimum lease payments under non-cancellable leases expiring:				
No later than one year	4.8	2.8	4.4	2.4
Between one and five years	9.5	4.3	10.9	2.7
Later than five years	8.3	–	9.6	–
	<b>22.6</b>	<b>7.1</b>	24.9	5.1

	Land and buildings	
	2011 £m	2010 £m
<b>Leases as lessor</b>		
Future aggregate minimum lease income under non-cancellable leases expiring:		
No later than one year	0.9	1.2
Between one and five years	1.0	1.7
	<b>1.9</b>	2.9

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.

#### Company

The Company does not have any other financial commitments (2010: £Nil).

## 23 Principal subsidiary undertakings, jointly controlled entities, associates and jointly controlled operations

	Activity	Percentage of equity held	Country of incorporation
<b>Subsidiary undertakings</b>			
ClerkMaxwell Ltd	Engineering and Support Services	100	UK
Costain Abu Dhabi Co WLL	Process Engineering	49	UAE
Costain Ltd	Engineering, Construction and Maintenance	100	UK
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
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

# Notes to the financial statements continued

## 23 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
<b>Jointly controlled entities</b>					
Alcaidesa Holding SA	Land Development	10.8	50	Spain	31 Dec
Brighton & Hove 4Delivery Ltd	Civil Engineering	–	49	UK	31 Mar
Costain Petrofac Ltd	Process Engineering	–	50	UK	31 Dec
4Delivery Ltd	Civil Engineering	–	40	UK	31 Mar
<b>Associates</b>					
Coast to Coast Holdings Ltd	Asset Management	0.5	20	UK	31 Mar
C2C Services Ltd	Asset Management	–	20	UK	31 Mar
Integrated Bradford LEP Ltd	Construction and Operation of Schools	–	40	UK	31 Dec
Integrated Bradford SPV Two Ltd	Construction and Operation of Schools	0.1	40	UK	31 Dec
Lewisham Schools for the Future LEP Ltd	Construction and Operation of Schools	0.1	40	UK	31 Mar
Lewisham Schools for the Future SPV 2 Ltd	Construction and Operation of Schools	–	40	UK	31 Mar

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.

All undertakings operate mainly in the country of incorporation, with the exception of Costain Building & Civil Engineering Ltd, which operates outside the United Kingdom.

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
<b>Major jointly controlled operations</b>			
A-one+ Integrated Highway Services – MAC 7	Engineering & Maintenance	33	UK
A-one+ Integrated Highway Services – MAC 10	Engineering & Maintenance	25	UK
A-one+ Integrated Highway Services – MAC 12	Engineering & Maintenance	33	UK
A-one+ Integrated Highway Services – MAC 14	Engineering & Maintenance	33	UK
Costain-Carillion Joint Venture – M1 Widening and A5/M1 Link	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-Hochtief Joint Venture – Reading 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 – Pudding Mill Lane – Crossrail	Civil Engineering	50	UK
Costain-Skanska – Royal Oak – 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
Lafarge Costain Joint Venture	Civil Engineering	50	UK

## 24 Acquisitions

On 6 April 2011, the Group purchased 75% of the share capital of ClerkMaxwell Limited ('ClerkMaxwell') and entered into a call option to acquire the remaining 25% between 26 April and 31 May 2011, which the Group exercised. The business, which is based in the UK, provides front-end engineering and support services to the upstream oil and gas sector.

The initial consideration, including the cost of exercising the call option was £3.2 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 2012, 2013 and 2014. The specified percentage to be used in this calculation increases each year.

The total estimated value of these future payments is £6.1 million. Part of the payment estimated at £1.3 million is based only on the financial performance in years 2011, 2012 and 2013. This has been included in the cost of acquisition (below) and as a financial liability based on a Level 3 valuation method. The balance of the payments, estimated at £4.8 million, are dependent on continued future service and, in accordance with IFRS 3, will be expensed to the income statement (2011 expense £0.4 million). The payments are dependent on the future performance and financial results and the £1.3 million provided as part of the cost of acquisition could range between £0.5 million and £2.1 million.

On 20 August 2011, the Group purchased the entire share capital of Promanex Group Holdings Limited ('Promanex') for a consideration of £14.6 million, including the repayment of loans provided by the principal shareholder. A management retention payment of £1.6 million was agreed, this is normally payable on the second anniversary following completion and is being charged to the income statement. Promanex provides a range of services across the UK and Ireland in management, operation, maintenance and repair of customers' sites and plant assets; water services; civils and industrial services and mechanical and electrical services.

The Group believes the acquisitions will broaden the Group's capabilities in ongoing care and maintenance and strengthens the Group's presence in key growth target markets, particularly power, nuclear process, hydrocarbons and chemicals and water, where significant investment is needed to meet national needs.

The contributions to revenue and operating profit before amortisation of acquired intangibles and employment related consideration within the Group's results of these acquisitions were ClerkMaxwell: revenue £5.2 million, operating profit £0.4 million and Promanex revenue £23.5 million, operating profit £0.9 million.

The proforma figures as required by IFRS 3, assuming that the acquisitions had been part of the Group throughout the year, were revenue £65.7 million and operating profit before amortisation of acquired intangibles and employment related consideration £2.0 million.

The acquisitions had the following effect on the Group's assets and liabilities:

	ClerkMaxwell £m	Promanex £m	Total £m
Cash	3.2	14.6	17.8
Contingent consideration	1.3	-	1.3
<b>Consideration</b>	<b>4.5</b>	<b>14.6</b>	<b>19.1</b>
Acquired intangible assets – Customer relationships	0.2	3.9	4.1
Acquired intangible assets – Other	0.4	1.3	1.7
Property, plant and equipment	0.1	0.8	0.9
Cash	0.2	-	0.2
Other current assets	0.8	12.6	13.4
Bank overdraft	-	(3.5)	(3.5)
Other current liabilities	(0.7)	(10.9)	(11.6)
Deferred tax	(0.2)	(0.6)	(0.8)
Non-current liabilities	(0.1)	(0.4)	(0.5)
<b>Fair value of assets acquired and liabilities recognised</b>	<b>0.7</b>	<b>3.2</b>	<b>3.9</b>
<b>Goodwill arising on acquisitions</b>	<b>3.8</b>	<b>11.4</b>	<b>15.2</b>

Based on the provisional assessment of the recognised values of assets and liabilities, the goodwill arising on the acquisitions is expected to be £15.2 million.

The costs incurred by the Group in relation to the acquisitions were £1.3 million and have been expensed in administrative expenses within the income statement.



# Notes to the financial statements continued

## 25 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

	2011			2010		
	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	23.9	59.6	83.5	35.1	45.8	80.9
Construction services and materials	46.7	2.9	49.6	50.3	–	50.3
	70.6	62.5	133.1	85.4	45.8	131.2

There were no sales of goods and services to major shareholders during year (2010: Nil).

The amount due from a major shareholder of £6.7 million 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 17. Balances with jointly controlled operations are eliminated on consolidation.

### Major shareholders

Mohammed Abdulmohsin Al-Kharafi & Sons WLL 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 19.

### Transactions with key management personnel

The Directors of the Company and their immediate relatives control 282,660 ordinary shares in Costain Group PLC, which expressed as a percentage of the issued share capital is 0.4% (2010: 0.1%) 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 officers also participate in the Group's LTIP, DSBP and SAYE plans, which are detailed in Note 19.

The compensation of key management personnel, including the directors, is as follows:

	Group	
	2011 £m	2010 £m
Directors' emoluments	1.6	1.7
Executive officers' emoluments	2.1	2.9
Post retirement benefits	0.4	0.4
Share-based payments	0.9	2.3
	5.0	7.3

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 19) (2010: none).

## 26 Post balance sheet events

Since the year-end, the Group made a further transfer of two PFI investments into The Costain Pension Scheme at an agreed value of £20.3 million, generating a net profit from the transaction of £10.2 million for the year ended 31 December 2012.

# Five-year financial summary

	2011 £m	2010 £m	2009 £m	2008 £m	2007 £m
<b>Revenue and profit</b>					
Revenue (Group and share of joint ventures and associates)	986.3	1,022.5	1,061.1	996.0	877.9
Less: Share of joint ventures and associates	(117.8)	(98.0)	(67.7)	(93.4)	(130.3)
<b>Group revenue</b>	<b>868.5</b>	924.5	993.4	902.6	747.6
<b>Group operating profit before other items</b>	<b>24.1</b>	17.4	22.0	19.5	9.7
Other items:					
Amortisation of acquired intangible assets	(0.9)	–	–	–	–
Employment related deferred consideration	(0.7)	–	–	–	–
<b>Group operating profit</b>	<b>22.5</b>	17.4	22.0	19.5	9.7
Profit on sales of investments	0.5	–	–	–	2.7
Profit on sales of interests in joint ventures and associates	0.3	11.2	2.0	2.7	3.2
Profit on sale of land and property	–	1.3	–	–	–
Share of results of joint ventures and associates	(1.3)	(0.5)	(3.2)	(3.9)	0.9
<b>Profit from operations</b>	<b>22.0</b>	29.4	20.8	18.3	16.5
Finance income	34.1	30.7	26.0	34.8	29.6
Finance expense	(32.2)	(32.2)	(28.7)	(30.0)	(26.3)
<b>Net finance income/(expense)</b>	<b>1.9</b>	(1.5)	(2.7)	4.8	3.3
Profit before tax	23.9	27.9	18.1	23.1	19.8
Income tax	(5.2)	(4.8)	(3.5)	(4.9)	(3.8)
<b>Profit for the year attributable to equity holders of the parent</b>	<b>18.7</b>	23.1	14.6	18.2	16.0
Earnings per share – basic*	29.2	36.4p	23.0p	29.0p	36.0p
Earnings per share – diluted*	28.2	35.4p	22.6p	29.0p	35.0p
<b>Dividends per ordinary share</b>					
Final*	6.75p	6.25p	5.5p	5.0p	5.0p
Interim*	3.25p	3.0p	2.75p	2.5p	–
<b>Summarised consolidated statement of financial position</b>					
Intangible assets	20.3	0.1	1.0	1.8	2.7
Property, plant and equipment	11.4	9.7	11.5	7.7	3.5
Investments in equity accounted joint ventures and associates	42.9	37.4	44.1	42.7	40.1
Other non-current assets	33.8	39.8	47.3	24.9	27.9
Total non-current assets	108.4	87.0	103.9	77.1	74.2
Current assets	332.0	309.3	325.1	329.2	285.7
<b>Total assets</b>	<b>440.4</b>	396.3	429.0	406.3	359.9
Current liabilities	348.3	311.4	320.5	312.1	273.2
Retirement benefit obligations	52.9	39.6	104.7	50.2	50.6
Other non-current liabilities	8.4	7.7	7.6	10.4	8.7
<b>Total liabilities</b>	<b>409.6</b>	358.7	432.8	372.7	332.5
<b>Equity attributable to equity holders of the parent</b>	<b>30.8</b>	37.6	(3.8)	33.6	27.4

\* The figures for 2007 to 2009 have been restated for the 1 for 10 share consolidation.

# Financial calendar and other shareholder information

Financial calendar*	
Full year results	7 March 2012
Annual Report mailing	30 March 2012
Ex-dividend date for final dividend	18 April 2012
Final dividend record date	20 April 2012
Interim Management Statement	9 May 2012
Annual General Meeting	9 May 2012
Final dividend payment (subject to shareholder approval)	25 May 2012
Half-year end	30 June 2012
Half-year results 2012	23 August 2012
Interim Management Statement	October 2012
Financial year-end	31 December 2012

\* The financial calendar may be updated from time to time throughout the year. Please refer to our website [www.costain.com](http://www.costain.com) for up-to-date details.

## 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 3 May 2012. Copies of the mandate form and the scrip dividend brochure can be downloaded from the Company's website [www.costain.com](http://www.costain.com) or obtained from Equiniti by telephoning 0871 384 2268\*\* or +44 121 415 7173 if calling from outside of the United Kingdom.

## Analysis of Shareholders

	Accounts	Shares	%
Institutions, companies, individuals and nominees:			
Shareholdings 100,000 and more	64	54,531,359	84.27
Shareholdings 50,000-99,999	37	2,612,960	4.04
Shareholdings 25,000-49,999	34	1,178,194	1.82
Shareholdings 5,000-24,999	289	2,893,026	4.47
Shareholdings 1-4,999	11,112	3,491,386	5.40
	<b>11,536</b>	<b>64,706,925</b>	<b>100</b>

## Secretary

Tracey Wood

## Registered Office

Costain House, Vanwall Business Park, Maidenhead, Berkshire SL6 4UB

Telephone 01628 842444

[www.costain.com](http://www.costain.com)

info@costain.com

Company Number 1393773

## Registrar

Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA

Telephone 0871 384 2250\*\* or +44 121 415 7047 if calling from outside of the United Kingdom.

## Shareholder information

The Company's Registrar is Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA. For enquiries regarding your shareholding, please telephone 0871 384 2250\*\* or +44 121 415 7047 if calling from outside of the United Kingdom. You can also view up to date information about your holdings by visiting the shareholder website at [www.shareview.co.uk](http://www.shareview.co.uk). Please ensure that you advise Equiniti promptly of a change of name or address.

## 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 than having a cheque sent by 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 our website, by contacting Equiniti, or 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](http://www.shareview.com/overseas). If your dividend is not currently paid directly into your bank or building society account and you would like to benefit from this service, please contact Equiniti on 0871 384 2250\*\* or +44 121 415 7047 if calling from outside of the United Kingdom who will be pleased to assist. By receiving your dividends in this way, you can avoid the risk of cheques getting lost in the post.

\*\* Calls to 0871 numbers cost 8p per minute from a BT Landline. Other telephone providers' costs may vary. Lines are open Monday to Friday 8.30 a.m. to 5.30 p.m., excluding bank holidays.

### 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 e-mail) for shareholder communications. If you select 'e-mail' as your mailing preference, you will be sent shareholder communications such as annual results by e-mail instead of post.

If you have your dividends paid straight to your bank account, and you have selected 'e-mail' as your mailing preference, you can also collect your tax voucher electronically. Instead of receiving the paper tax voucher, you will be notified by e-mail with details of how to download your electronic version. Visit the website at [www.shareview.co.uk](http://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 0ZT

### 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 [www.sharegift.org](http://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.

# 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.

### Website links:

- [www.costain.com](http://www.costain.com)
- [www.costain.com/investors](http://www.costain.com/investors)
- [www.costain.com/responsibility](http://www.costain.com/responsibility)
- [www.costain.com/annual-report-2011](http://www.costain.com/annual-report-2011)
- [www.costain.com/news](http://www.costain.com/news)





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Designed and produced by The College [www.the-college.com](http://www.the-college.com)

**Costain photographers:** Mike Doherty, page 1 and 34 (Achieving Excellence Awards), page 11 (Andrew Wyllie), page 47 and 120 (Tracey Wood) and page 120 (Catherine Warbrick and Graham Read); Alastair Fyfe, page 4 (Costain's Seeing is Believing visit at St Joseph's RC Primary School); Huw John, page 5 (BITC's Awards for Excellence 2011); Ian Routledge, pages 7, 43, 46, 47 and 49 (Costain Board Directors); Phil Starling, page 23 (Courtesy of Highways Agency East Midlands Regional Control Centre) and Gustavo Ferrari, Pro Light Studio, page 47 (Samer G. Younis).

**Additional photography:** [www.aerial-images.co.uk](http://www.aerial-images.co.uk), page 28 (Greater Manchester's Recycling and Waste Management Contract); Darren Ruane, page 29 (M1 Junction 10-13 scheme); Webb Aviation, page 30 (Holford underground gas storage project); Artist impression courtesy of Network Rail, pages 1 and 21 (London Bridge station).

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This Annual Report is available at: [www.costain.com](http://www.costain.com)






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Visit [www.costain.com](http://www.costain.com)

Costain Group PLC  
Costain House  
Vanwall Business Park  
Maidenhead  
Berkshire  
SL6 4UB

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