

Shaping Change

Costain Group PLC

Annual Report 2001

25 JUN 2002



16 Report of the directors

The directors submit their report, together with the audited accounts for the year ended 31 December 2001.

Activities

The progress and prospects of the Group's businesses are reviewed on pages 8 to 10.

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.

Directors and directors' interests

Present members of the Board are shown on pages 14 and 15.

Mr David George Jefferies was appointed as a non-executive director and Chairman of the Company on 6 June 2001. Mr Stuart John Doughty was appointed as Chief Executive of the Company on 1 July 2001. Mr Charles Joseph McCole was appointed as Finance Director of the Company on 25 March 2002.

Mr David Philip Alvey was appointed as a non-executive director of the Company on 1 November 2001 and Mr John Martin Bryant was appointed as a non-executive director on 1 February 2002.

Mr Michael E Beckett, who had been appointed as Chairman of the Company on 16 February 2001, resigned as a non-executive director and Chairman on 25 May 2001. Mr John A Armit resigned as Chief Executive on 30 June 2001. Mr Miles W Roberts resigned as Finance Director on 31 December 2001. Mr Peter L Burton, a non-executive director, resigned on 1 November 2001.

Dato' Dr Ramli bin Mohamad resigned as a non-executive director and Deputy Chairman of the Company on 11 December 2001. Mr Abdul Wahid Omar, a nominee of Daedalus Projects Limited, replaced Dato' Dr Ramli bin Mohamad as a non-executive director on 21 January 2002 and was appointed Deputy Chairman on 22 March 2002.

Mr Jefferies, Mr Doughty, Mr McCole, Mr Alvey, Mr Bryant and Mr Omar have been appointed by the Board during the period since the last Annual General Meeting. The Company's Articles of Association require that they retire and, being eligible, offer themselves for re-election. In accordance with the Company's Articles of Association, Mr Basil K Vasilios retires by rotation. Mr Doughty has a service agreement but no other retiring director has a service agreement with the Company.

Details of directors' emoluments and interests in shares in the Company are contained in the Report of the Directors' Remuneration which appears later in this Report on pages 19 to 23.

Related party transactions

Details of transactions with related parties undertaken by the Group during the year

are disclosed in Note 27 to the accounts on page 46.

Dividends

No dividends were paid or recommended.

Substantial interests in shares

At 22 March 2002, the Company had been notified of the following interests in its shares:

Daedalus Projects Limited*	125,354,541	37.18%
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Mohammed Abdulmohsin Al-Kharafi & Sons WLL	79,168,523	23.48%
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Raymond International WLL	38,243,750	11.34%
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The Royal Bank of Scotland Group PLC	12,470,273	3.69%
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Lloyds TSB Bank PLC	10,674,075	3.16%
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*Intria Berhad owns 93% of Daedalus Projects Limited.

Corporate Governance

The Company is committed to the principles of corporate governance contained in the Combined Code which is appended to the Listing Rules of the Financial Services Authority (the "Combined Code") and for which the Board is accountable to shareholders. This Statement of Corporate Governance, together with the Report on Directors' Remuneration, explains how the Company has applied the principles set out in Section 1 of the Combined Code.

The Board and Committees

The Board currently comprises two executive directors and nine non-executive directors of whom four are independent non-executive directors. The remaining five non-executive directors are nominated by major shareholders, namely Daedalus Projects Limited, Mohammed Abdulmohsin Al-Kharafi & Sons WLL and Raymond International WLL. The composition of the Board does not, therefore, comply with provision A3.2 of the Combined Code which requires the majority of non-executive directors to be independent of management and free from any business or other relationship with the Company. The right of these three major shareholders to nominate non-executive directors means that, to comply with provision A3.2 of the Combined Code, a number of additional independent non-executive directors would have to be appointed.

By virtue of the fact that the shareholders are entitled to appoint nominee non-executive directors for so long as they hold 7% of the aggregate nominal value of the then issued ordinary share capital of the Company means that the Company does not completely comply with provision A6.1 of the Combined Code. The appointment of four independent non-executive directors has brought the Company much closer to compliance with provision A6.1 of the Combined Code. The independent non-

executive directors' appointments are for an initial period of three years at the expiry of which time their appointments are to be reviewed by the Nomination Committee to determine whether their appointment continues. The Company's Articles of Association requires 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, thus complying with provision A6.2 of the Combined Code.

Brief biographies of the executive and non-executive directors appear on pages 14 and 15. The biographies demonstrate that the non-executive directors have a range of business and financial experience that is important and relevant to the management of the Company.

In the year ended 31 December 2001, the Board met on ten occasions. The Board has adopted a schedule of matters specifically reserved to itself for decision. The principal matters reserved to the Board concern strategic, financial, operational, compliance and risk management issues. The schedule of matters reserved to the Board is reviewed periodically. Mr Burton was the lead independent director until his resignation on 1 November 2001. No replacement appointment has been made since that date and so the Company does not comply with that element of provision A2.1 of the Combined Code. All directors have access to the advice and services of the Company Secretary and a procedure also exists whereby any director, wishing to do so in furtherance of his duties, may take independent professional advice at the Company's expense. In the year ended 31 December 2001, no director sought independent professional advice.

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, Finance Director and Company Secretary in order to progress the Company's business.

All newly appointed directors are provided with a booklet covering the responsibilities and duties of directors of a public company and with additional relevant materials produced by the Company's legal advisers, Slaughter and May. In accordance with the recommendations of provision A1.6 of the Combined Code, arrangements will be made to hold in-house training seminars for the executive and non-executive directors.

The principal Board Committees are the Remuneration Committee, the Audit Committee and the Nomination Committee. The members of the Remuneration Committee during 2001 were Mr Lana, Mrs Rogers, Mr Ballard and briefly Mr Beckett under the chairmanship of

Mr Peter Burton. On 17 July 2001, Mr Jefferies was appointed a member of the Remuneration Committee and on 16 January 2002, Chairman. On 22 March 2002, Mr Bryant was appointed a member and Chairman of the Remuneration Committee and, at the same time, the other members of the Committee were confirmed as Mr Jefferies, Mr Ballard and Mr Shehata. The Remuneration Committee has established written terms of reference, which were reviewed and re-issued on 29 August 2001 and it met on three occasions in 2001. The Chief Executive is normally in attendance at Remuneration Committee meetings but is always excluded when his own performance and remuneration are under review. The Board's Report on Directors' Remuneration appears later in this Report on pages 19 to 23.

The members of the Audit Committee during 2001 were Mr Lana and Mr Shehata under the chairmanship of Mr Burton until 17 July 2001. Mr Beckett was briefly a member of the Audit Committee. On 17 July 2001, Mr Jefferies was appointed a member and Chairman of the Audit Committee. On 11 December 2001, Mr Allvey was appointed a member and Chairman of the Audit Committee. On 22 March 2002, the members of the Audit Committee were confirmed as Mr Allvey, Chairman, Mr Jefferies, Mr Lana and Mrs Rogers. The Audit Committee has established written terms of reference which were reviewed and re-issued on 29 August 2001 and it met on four occasions in 2001. The executive directors, the external auditors, the internal auditors and Group Financial Controller attend all meetings but provision is also made for discrete meetings between the Audit Committee and the external auditors.

Although the Remuneration Committee and the Audit Committee only comprise of non-executive directors, the requirements of provision B2.2 and D3.1 of the Combined Code are not strictly complied with. In the case of the Remuneration Committee, not all members are independent non-executive directors and, in the case of the Audit Committee, the majority of members are not independent non-executive directors. This arises from the current composition of the Board.

The Nomination Committee comprises the Chairman of the Company and all non-executive directors. The Chairman of the Company is the Chairman of the Committee. The Nomination Committee has established written terms of reference which were reviewed and re-issued on 29 August 2001. This committee meets as required to select and propose to the Board suitable candidates for appointment as executive and non-executive directors. In 2001, the role of the Nomination Committee was undertaken by the Board and by a sub-committee of the Board consisting of the Chairman, Chief Executive, Mrs Rogers and Mr Ballard.

Relationship with institutional investors and private investors

The Chief Executive has been designated as the principal spokesperson with institutional investors, press and other interested parties.

The Company has three key shareholders who control the beneficial interest in 72% of the issued share capital of the Company and, also, appoint nominees to sit on the Board of the Company. However, apart from these three large shareholders, the Company has approximately 15,000 other shareholders and the Board recognises that not all of the Company's private investors have regular access to market information. All shareholders are sent copies of Annual and Interim Reports and, where appropriate, circulars and prospectuses and are given notice to enable them to attend the Company's Annual General Meeting. Shareholders whose shares are held by nominees may receive copies of such communications upon request. The Company has an internet web-site on which it publishes its in-house magazine, "Blueprint", press releases and other information concerning the Company's business and upon which it publishes its annual and interim results.

In accordance with provision C2.1 of the Combined Code, the Company will announce the votes cast by proxy at the forthcoming Annual General Meeting. The Company complied with this obligation in respect of the Annual General Meeting in 2001.

The Company will comply with the Combined Code by giving 20 working days' notice of the Annual General Meeting. The Company complied with this obligation in respect of the notice for the Annual General Meeting in 2001.

Review of internal controls

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

The Board maintains full control over strategic, financial, operational and compliance issues. Within the overall objectives set by the Board, the management of the Group is delegated to the Chief Executive who is assisted by other members of the Executive Board. The Chief Executive has full authority to act subject to the matters reserved to the Board and to the requirements of Group Policies.

Following publication of guidance for directors on internal control "Internal Control: Guidance for Directors on the Combined Code" (the Turnbull guidance), 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

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and up to the date of approval of the Annual Report and Accounts. This process is reviewed by the Board and accords with the Turnbull guidance.

The Board have reviewed the effectiveness of the system of internal controls as described below. The review covers all controls, including financial, operational and compliance controls and risk management. In particular:

Risk management

A detailed business risk review was undertaken in 2000 and identified and evaluated the significant project risks affecting the business. At the direction of the Board, existing procedures were reviewed and, where necessary, new procedures were developed to manage risk. This included a specific project risk management procedure which was published in April 2000 and among other things requires a Tender Project Risk Register and a Commercial Risk Review of the contract to be prepared in respect of each contract bid. This identifies key risks, the probability of those risks occurring, their impact if they do occur and the actions necessary to manage those risks to an acceptable level. The risks are divided into four broad categories namely: safety, technical, operational and environmental and are reviewed by the project manager and commercial manager of the project on a continuing basis following award.

The commercial and contractual risks identified as part of the Tender Project Risk Register are monitored by the commercial director and commercial managers within the operations. It is also the responsibility of the commercial director and commercial managers to ensure that the risks accepted are fully understood and in conjunction with operations to ensure the risks are properly managed. The commercial director regularly reports on commercial and contractual issues to both the Board and the Executive Board.

Management reviews the role of insurance in managing risks across the Group and bring any important issues to the attention of the Board.

Operational

Controls and procedures are detailed in Group Policy Statements, procedure manuals and other written instructions. A major review of the Group Policy Statements is being undertaken in 2002. The procedure manuals are regularly reviewed. The procedures and "lessons learnt" are progressively being published on the Costain Intranet.

The Company has developed in the United Kingdom, operational management systems which are registered to BSI 9002/1994 and which are designed to set out an operating framework that ensures a systematic approach to management to provide safe construction processes of the highest quality. The implementation and compliance with the management system is monitored and audited on a continual basis by a team

of internal quality assurance auditors. External audits of the management systems are undertaken by the British Standards Institution in order to maintain the Company's accreditation.

All projects operate in a controlled framework of health, safety and environmental systems. Execution of and compliance with these systems is monitored by the project management and audited by health, safety and environmental advisers. Further detail on health, safety and environmental matters is given on page 24.

The Board and Executive Board receive reports at each meeting on health, safety and environmental performance and on significant operational matters. The responsibility for ensuring compliance with the Company's procedures lies with the Executive Board.

Financial

There is a comprehensive annual budgeting system for each business within the Group. The annual budget is discussed by the Executive Board and reviewed by the Chief Executive and Finance Director prior to submission to the Board for approval. An updated forecast is produced quarterly and compared with the annual budget and where appropriate the previous quarterly forecast.

Monthly performance of each operation is reviewed by senior management and subsequently reported against forecast to the Executive Board and the Board. Reports cover profit and loss and cash flow with an accompanying narrative on significant issues underlying the financial reports.

The Treasury and Tax Managers report to the Finance Director who reports to the Audit Committee from time to time on any issues of significance to the Group.

Compliance

The Group Policies contain a statement on business conduct, which emphasises the legal, ethical and moral standards that have to be employed in all the Company's business dealings. The Company expects the highest standards from all its employees.

Litigation and other legal matters are controlled by the Company Secretary and Group Legal Adviser. A legal report would be submitted to the Board in the event that a critical legal issue arose and, subject to that, a review of all litigation with a value of above £10,000 is submitted to, and reviewed by, the Board annually. Significant changes in laws and regulations are drawn to the attention of the appropriate staff and training is given where necessary.

The processes used by the Audit Committee on behalf of the Board to review the effectiveness of the system of internal controls include the following:

- a review of the external and internal audit work plans;
- consideration of reports from management, internal and external audit on the system of internal controls and any material control weaknesses;

- discussion with management of the actions taken on problem areas identified by Board members or in management reports or in the internal/external audit reports;
- a review of the self-certification returns on risks and internal controls from the various operating divisions of the Group.

The process of self-certification and hierarchical reporting which is in place provides for a documented and auditable trail of accountability. These procedures are relevant across Group operations and provide assurance to senior management and, finally, to the Board. Internal audit also provide a degree of assurance as to the operation and validity of the system of internal controls.

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

Report on Directors' Remuneration

Remuneration policy

The Board has a Remuneration Committee that decides the remuneration policy which is to apply to executive directors and gives guidance as to the remuneration packages of other senior executives. Details of the members of the committee are given on pages 14 and 15. Mr Bryant is the Chairman of the Remuneration Committee. The remuneration policy is intended to attract, retain and motivate executive directors and senior executives of the appropriate calibre and experience. The Remuneration Committee is, however, aware that it should avoid paying more than is appropriate or necessary. Accordingly, the Group carries out each year, for the benefit of the Remuneration Committee, an exercise to benchmark remuneration packages and their constituent elements with those of comparable organisations, primarily within the UK-based contracting sector, to ensure that the remuneration packages within the Group bear reasonable comparison with those of other groups. This comparison exercise is only one element; the Remuneration Committee also takes into account personal performance. The Remuneration Committee is also entitled to access independent advice from external consultants on individual remuneration packages or the Company's remuneration practices in general. The Remuneration Committee did not take any independent advice during the financial year ended 31 December 2001.

The main components of executive directors' and senior executives' remuneration packages comprise basic salary, which forms the major element of remuneration, an annual bonus which is dependent on the achievement of short-term objectives approved by the Remuneration Committee, long-term incentive arrangements, membership of a pension scheme (which includes life cover of four times salary for death in service), a

company car (and in certain cases the provision of a fuel benefit) and the provision of health insurance or a contribution to the provision of health insurance.

Since the advent of the Combined Code, the Remuneration Committee has given due consideration to the provisions of B1.1 to B1.6, and to Schedule A of the Combined Code in formulating the remuneration policy of the Group, and has noted and taken account of the requirements of provision B1.7 to B1.10 with regard to service contracts and compensation. The Company does substantially comply with provisions B2.1 to B2.6 of the Combined Code with regard to the establishment and procedures of the Remuneration Committee, save that as already noted, the Company does not comply with provision B2.2 of the Combined Code in connection with the membership of the Remuneration Committee. The Remuneration Committee has also taken into account provisions B3.1 to B3.4 and the provisions in Schedule B of the Combined Code in the preparation of this report.

There have been no material changes to the remuneration policies of the Company during the year but changes are now planned and details are given later in this report.

Salary – Salary is a major element of the remuneration package. The Remuneration Committee reviews the salaries of the executive directors annually and, at the same time, gives guidance to the Chief Executive as to the matters to be taken into account in the salary review of other senior executives of the Group. Information obtained from the comparison exercise referred to above provides certain guidance as to market conditions. The salary review reflects market conditions and personal performance. The salary review is undertaken in February/March of each year after a review of the performance of the individual. A salary increase, if awarded, is effective from 1 April in each year.

Annual bonus – An annual bonus scheme is a further component of the remuneration package for executive directors and senior executives. Annual bonuses up to a maximum of between 20% and 40% of basic salary have been payable if performance targets are met. These performance targets currently relate to profit, both at Group and Divisional level, cash and overhead management and, in certain circumstances, items specific to the individual and, in addition, bonuses include a discretionary element. The targets for the annual bonus are reviewed and approved annually by the Remuneration Committee. For the period of 1 July 2001 to 31 December 2001, Mr Doughty was entitled to earn a bonus of £50,000. For the payment of £30,000 of that bonus, the Remuneration Committee has to be satisfied that certain performance criteria have been met. The balance of £20,000 is in the absolute discretion of the Remuneration Committee.

There is no requirement for any bonus earned to be taken as shares. Bonus payments are not pensionable.

The Remuneration Committee has agreed for 2002 to increase the maximum annual bonus to 50% of basic salary to bring the Company into line with other companies within the sector.

Long-term incentive arrangements – There are two long-term incentive arrangements. First, the Executive Share Option Scheme and secondly the Performance Share Scheme, brief details of which are given below:

a. Executive Share Option Scheme

A Revenue-approved arrangement in which executive directors and other senior management have participated was established in 1984 and was continued through a second scheme put in place in 1994. This is in most respects similar to the earlier scheme, save that no options may be exercised unless specific performance criteria have been achieved. There are options outstanding under the earlier scheme (none in favour of executive directors). The new scheme also allows for options to be granted outside the Revenue-approved arrangement.

Under the first Scheme, options over the Company's ordinary shares may be granted each year to executive directors and other senior management and, when granted within the Revenue-approved arrangement of the Scheme, the options over shares are limited to an aggregate limit of £30,000. The scheme rules do not permit options to be granted with an exercise price at a discount to the market value of the shares at the date of grant. The options are only exercisable following the attainment of a performance condition or conditions measured over a continuous period of at least three years, commencing no earlier than the financial year immediately preceding the date of grant. Options may not be exercised before the third anniversary of the date of grant and lapse if not exercised by the tenth anniversary of the date of grant.

As mentioned above, the second Scheme also allows for options to be granted outside the Revenue-approved arrangement. The Rules of this element of the Scheme are identical to the Revenue-approved arrangement, save that options may be granted over shares with an aggregate limit of four times the earnings of the employee to whom the grant is made. When an employee exercises an option, the Board may, at its discretion, pay to such employee a cash sum equal to the amount by which the value of the ordinary shares, in respect of which the notice of exercise was given, exceeds the total amount payable on any exercise by the employee, instead of allotting or procuring the transfer of ordinary shares to that employee.

Mr Armit the previous Chief Executive was, on 26 January 1998, granted options over

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774,648 ordinary shares of 10p each in the Company which had a total market value of £220,000 calculated in accordance with the Rules of the Scheme on the basis of a derived mid-market price at the date of grant of 28.4p per share. These options were exercisable at an exercise price of 40p per share, subject to the Rules of the Scheme, between 25 January 2001 and 25 January 2008, and subject to the achievement of the performance criteria applicable over the three financial years to 31 December 2000. The Remuneration Committee had determined that the performance criteria had been met. The options lapsed as they were not exercised on or before 31 December 2001, following Mr Armit's resignation from the Company on 30 June 2001.

At 31 December 2001, the derived mid-market price of the ordinary shares of the Company, as advised by the Company's Brokers was 13.25p. The range of the share price of the ordinary shares during 2001 was 9.50p to 16.50p.

b. Performance Share Scheme

This was introduced in 1993 and provides a means of awarding executive directors and other senior management shares in the Company provided that specific performance criteria have been met.

Under the terms of the Scheme, options over the Company's ordinary shares may be granted to executive directors and other senior management. There are various limitations on the grant of options, including a prohibition on a grant of an option to an employee unless a period of not less than 22 months has elapsed since the date of the previous grant of an option under the Scheme and a prohibition on a grant of an option if this would result in an employee holding options under the Scheme where the market value of the shares at the date of grant exceeded in aggregate four times the employee's salary, exclusive of bonuses and the value of other benefits. The Scheme also prohibits the grant of an option to an employee within three years of his retirement. The scheme does not permit options to be granted with an exercise price at a discount to the market value of the shares at the date of grant.

The options are only exercisable on the attainment of performance criteria measured over a continuous period of three financial years beginning with the financial year in which the grant of the option is first made. The option cannot be exercised until one month following the date of publication of the audited consolidated accounts of the Company for the last financial year of the three-year performance period. The shares to satisfy any exercise of an option would be transferred from the Costain Group Employee Trust and so options granted under this scheme do not dilute shareholders' equity as they have been bought on the market.

Options have been granted under this Scheme but none are outstanding at present.

Review of Long-Term Incentive Arrangements and Employee Share Options

The Remuneration Committee is currently reviewing long term incentive arrangements for senior executives and share incentive arrangements for employees. The Committee is proposing to introduce new long term share incentive arrangements that will further align the interests of directors and senior executives with those of shareholders; link the incentives provided with the Board's objectives for future growth; reward strong performance and do so in line with market practices and trends taking account of best practice as regards directors' and employees' remuneration; and ensure that all the Company's employees are increasingly focused on performance.

The Company proposes putting forward at the Annual General Meeting for the approval of shareholders a new long-term incentive plan for directors and senior executives and a new share plan for employees. Shares in the Company will be issued pursuant to the new plans within the institutional limits. Details of the current proposals for long-term incentive plans (the LTIP) are included in the report on long-term incentive arrangements below.

Long-Term Incentive Arrangements

Proposed Long-Term Incentive Plan

It is proposed that the LTIP will be established at the Annual General Meeting and awards made from 2002. Under the LTIP, it is envisaged that awards will be made initially to the executive directors and other members of the Executive Board. Awards may be made on an annual basis and will be conditional on meeting profit-related performance targets linked to the Company's business plan.

The award will be taken in the form of shares. Although awarded on entry, the vesting of the award will be conditional on the attainment of the additional performance target focused on shareholder return over a continuous period of three financial years beginning with the financial year in which the award is made. This performance measurement will be designed to achieve sustained performance by satisfying performance targets over the three-year period. The Company is determining the most appropriate performance requirements for the plan given the objective of the alignment of shareholders' interests and the business plan. In line with best practice the LTIP is likely to offer an incentive for executive directors and senior management to retain and so build up shareholdings.

All Employee Share Plan

The Company is also proposing to introduce an all employee share plan in which employees including the executive directors, will participate. The plan will be an Inland Revenue approved Save As You Earn (SAYE) plan. Under this plan, participants will enter into savings contracts and be granted options with three, five and or seven year terms. Monthly contributions will be capped at £250 or such lower figure as may be determined. Options may be granted at a discount of no more than 20% to the market value of the shares subject to option at grant. In line with common practice, these SAYE options will not be subject to performance conditions. The SAYE plan will, however, require an ongoing commitment from participants, while offering the prospect of gains in line with growth in the Company's share price.

Grants of awards under the employee plan will be at an appropriate level, taking into account market practice and in accordance with the dilution limits of the ABI and NAPF.

Contracts of service — In general, the service agreements with executive directors and other senior executives provide for termination by the Group on either one or two years' notice. No executive director has a notice period over one year. The Committee considers that such notice periods are reasonable and fair in the interests of the Group and the individuals concerned, having regard to prevailing practice amongst public companies both in the industry in which the Group operates and elsewhere.

The Remuneration Committee considers it unlikely that any executive director or senior executive would in the future be engaged with a notice period greater than one year. There is no provision for payment of pre-determined compensation in case of wrongful termination by the Group. The Remuneration Committee also believes that a robust line should be taken on reducing compensation to reflect departing directors' obligations to mitigate loss.

Outside appointments — In principle, the Company encourages executive directors to take outside 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. However, not more than one such appointment may be undertaken except in special circumstances. There must be no conflict of interest, and the time to be devoted to the outside appointment must be reasonable in relation to the individual's commitments to the Company. Fees paid for outside appointments may be retained by the individual concerned. The Board has agreed that Mr Doughty can hold more than one outside non-executive appointment.

Pension arrangements — Senior executives (with the exception of Mr Doughty) participate in an executive section of the Group's main approved UK pension scheme. This section provides enhanced benefits in respect of accrual rate and spouse pension and earlier retirement ages (e.g. 60 for executive directors and some members of senior management). In addition

to a maximum pension of two-thirds of final salary, the scheme provides a lump sum death in service benefit of four times basic salary and pensions for dependants of members. Some members of senior management participate on a non-contributory basis. Future membership of the executive section of the Group's Pension Scheme will be on a contributory basis.

In the case of the previous Chief Executive, Mr Armit, the Company contributed to a personal pension arrangement. In the case of Mr Doughty, the Company makes no contribution to his personal pension arrangements. Life assurance cover of four times basic salary is provided through the UK approved pension scheme in respect of earnings up to the Inland Revenue limit (£95,400 per annum with effect from 6 April 2001) and through the Costain Funded Unapproved Retirement and Death Benefit Scheme in respect of the excess. The annual premium payable in respect of life assurance for Mr Armit for the period ending 30 June 2001 was £1,105 (2000: £2,067). The premium payable in respect of life assurance for Mr Doughty is £1,520 and for Mr Roberts is £103 (2000: Nil).

Non-executive directors — Fees for non-executive directors are determined by the Board as a whole. Non-executive directors do not receive any remuneration or benefits in addition to their fees and do not participate in any of the Group's pension or incentive schemes.

Directors' remuneration

The aggregate directors' remuneration for the year ended 31 December 2001 was £960,300, as set out in the following table:

	Salary/Fee	Bonus	Benefits	Other	2001 Total	2000 Total
	£	£	£	£	£	£
Executive Directors						
S J Doughty ¹	120,000	-	6,520	-	126,520	-
J A Armit ²	111,461	43,177	9,029	300,000 ¹⁰	463,667	352,227
M W Roberts ³	129,999	20,040	12,310	-	162,349	77,884
Non-Executive Directors						
D G Jefferies ⁴	25,000	-	-	-	25,000	-
D P Alvey ⁵	4,166	-	-	-	4,166	-
F W Ballard ⁶	18,435	-	-	-	18,435	-
A Y Lana	17,500	-	-	-	17,500	13,933
Mrs L A W Rogers ⁸	17,185	-	-	-	17,185	-
S Y Shehata	17,500	-	-	-	17,500	17,500
B K Vasilicou	17,500	-	-	-	17,500	17,500
M E Beckett ⁷	8,051	-	-	40,000 ¹⁰	48,051	-
Dato' Dr Ramli bin Mohamad ⁸	14,583	-	-	-	14,583	4,510
P L Burton ⁹	13,264	-	-	14,580 ¹⁰	27,844	18,696
Former Directors	-	-	-	-	-	188,563
TOTAL	514,644	63,217	27,859	354,580	960,300	690,813

Notes:

1. appointed as Chief Executive on 1 July 2001.
2. resigned on 30 June 2001.
3. resigned on 31 December 2001.
4. appointed as Chairman on 6 June 2001.

5. appointed on 1 November 2001.
6. appointed on 9 January 2001.
7. appointed on 16 February 2001 and resigned on 25 May 2001.

8. resigned on 11 December 2001.
9. resigned on 1 November 2001.
10. compensation for loss of office.

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Directors' remuneration — continued
Performance-related bonus payments of £43,177 and £20,040 were made to Mr Armit and Mr Roberts respectively (2000: Mr Armit £129,133).

"Benefits" comprise primarily of the provision of a company car, fuel and subsidised medical insurance and the amounts stated exclude the pension and life assurance costs identified separately under "Pension arrangements". The amounts stated also exclude the cost of disability insurance which is provided by the Group to all staff employees under a general policy with no separately-identifiable cost in respect of individual beneficiaries, save in the case of Messrs Armit, Roberts and Doughty where the premium payable in respect of permanent health insurance for Mr Armit was £1,732 (2000: £1,712) and the premium payable in respect of permanent health insurances for Mr Roberts and Mr Doughty were £1,082 and £255 respectively. The cover in respect of Mr Doughty was only effected on 30 November 2001.

No payments were made to or benefits received by executive directors during the year under any long-term incentive schemes.

Provision for compensation payments relating to three former directors (following external legal advice taken by the Remuneration Committee in the case of Mr J A Armit as to the level) upon termination of their employment amounted to £354,580 (2000: £62,500).

Payments made to a third party in respect of director's services amounted to £27,844 (2000: £18,696). This figure is included within the Directors' emoluments.

No payment was made to any alternate director.

The emoluments of the highest-paid director were £463,667 (2000: £352,227). Both figures exclude attributed pension contributions.

Directors' pensions

Pension benefits earned by directors (defined benefit schemes):

	Increase in accrued pension during the year £pa	Transfer value of increase £	Accumulated total accrued pension £pa
M W Roberts	3,349	22,151	5,035 (2000: £1,658)

Notes to defined pension benefits

(1) The increase in accrued pension during the year excludes any increase for inflation.

(2) The transfer value has been calculated on the basis of actuarial advice in accordance with Actuaries Guidance Notes GN11 and GN27. The value quoted

includes the cost of providing life assurance cover.

(3) The pension entitlement shown is that which would be paid annually on retirement based on service to the end of the year.

(4) Members of the scheme have the option to pay additional voluntary contributions; neither the contributions nor the resulting benefits are included in the table.

Pension contributions paid on behalf of directors (money purchase scheme):

	Contribution £
J A Armit	14,658 (2000: £28,860)

Notes to money purchase benefits

The contribution excludes the cost of providing life assurance cover and any contribution made by the director.

The Group makes no provision for, and no contribution in respect of, pension arrangements for Mr Doughty or for the non-executive directors.

The Costain Funded Unapproved Retirement and Death Benefit Scheme was established in 1997 to provide pension

benefits for senior executives subject to the Inland Revenue limit (£95,400 per annum with effect from 6 April 2001) on earnings eligible for treatment as pensionable earnings under approved pension schemes.

Prior to the establishment of the scheme, pension entitlements on earnings in excess

of the limit were provided by way of an unfunded reserve. The unfunded liability is being externally funded through the unapproved scheme over a five-year period commencing from 1998 and the current position is:

	£
Unfunded reserve at 31 December 2000	96,883
Payment to unapproved scheme	(34,234)
Interest on balance carried forward	5,638
Unfunded reserve at 31 December 2001	68,287

Directors' interests

Directors' interests recorded by the Company in accordance with the requirements of the Companies Act 1985 are as follows:

		At 1.1.01	At 31.12.01
D G Jefferies	a	100,000*	100,000
S J Doughty		—*	—
S Y Shehata		—	—
B K Vasiliou		—	—
A Y Lana		—	—
Mrs L A W Rogers		—*	—
F W Ballard		—*	—
D P Alvey		—*	—
M E Beckett		—*	—†
Dato' Dr Ramli bin Mohamad		—	—†
J A Armit	a	60,000	60,000†
M W Roberts		—	—†
P L Burton		—	—†

* at subsequent date of appointment

† at date of resignation

a Costain Group PLC shares of 10p each

Mr F W Ballard and Mr D P Alvey have purchased 30,372 and 30,000 Ordinary Shares respectively since 31 December 2001.

All interests are beneficial. Particulars of directors' options are contained in the register of directors' interests.

The basis on which executive directors participate in long-term incentive schemes is decided by the Remuneration Committee, except for the Costain Share Savings Scheme which is open to all relevant UK employees. Non-executive directors do not participate in any of these schemes.

Options which were granted to Mr Armit under the Costain Executive Share Option Scheme during 1998 have lapsed.

No options were exercised by directors during the year.

Details of all outstanding options are set out in Note 20 to the accounts on page 42.

24 Report of the directors — continued

Employment Policies

Costain Group companies adopt employment practices best suited to their operations and in compliance with the requirements of the territories in which they work. Personnel policies are designed to provide equal opportunities to all. In particular, the employment of those who become disabled is continued wherever possible and opportunities are provided for the recruitment, training and career development of disabled people.

Health, Safety and the Environment

It is of paramount importance to both the Board and the Executive Board that:

- (i) health risks or accidents to employees, subcontractors, members of the public and others who may come into contact with the Group's activities are avoided; and
- (ii) the Group meets all applicable government guidelines or regulations and industry codes of practice on the environment and in so doing seeks to reduce environmental disturbance in all the Group's activities.

In order to achieve these objectives, regular reports on health, safety and the environment are submitted to and considered by the Board. The Executive Board considers health, safety and environmental performance at each monthly meeting. In addition, there is a Committee which is chaired by the Chief Executive and which is responsible, among other things, for overseeing the preparation, updating and dissemination of the Group's health, safety and environmental policies, monitoring health, safety and environmental performance, ensuring that appropriate training is undertaken by employees and the employees of subcontractors and taking the appropriate initiatives to deliver steady improvement in the health, safety and environmental performance of the Group.

Mr Doughty, the Chief Executive is the Board member responsible for Health & Safety.

The Group is committed to continuous improvement in health, safety and environmental performance. The steps taken to ensure continuous improvement include:

- the completion of the implementation of the Nattrass Report which was commenced during 2000. Mr Stuart Nattrass, formerly HM Chief Inspector of Construction with the Health & Safety Executive, has continued to advise on the health & safety management system of Costain Limited in his role as consultant. He is also a member of the Executive HSE Committee chaired by Mr Doughty, the Chief Executive.
- the setting of a number of targets for 2001 as a result of which the following were achieved:
 - a reduction of 17% on the Accident Frequency Rate for 2000 plus a reduction of 16% on Major Injuries rate for the preceding year.

- all the Operations Directors participated in cross boundary Health & Safety audits during the year. In total, eleven full health & safety audits were carried out. These audits were additional to those carried out by the Regional Safety Advisors who in the main achieved their target of two audits per site during the year.
- an environmental audit scheme was developed company wide and a minimum of two audits were carried out in each region.
- a system of company inductions was introduced and commenced in October 2001.
- on the training front, all project related staff received a minimum of one day's relevant HSE Training during the year and the target for 12 non-safety staff to pass the NEBOSH General Certificate was achieved. Furthermore, all Costain HSE training courses were aligned to a recognised certification scheme, mainly to the Institution of Occupational Safety & Health.
- ISO 14001 accreditation (the International Environmental Standard) was achieved for the whole of Costain Ltd and Costain Oil, Gas & Process Limited.

During 2001, Costain Limited was subject to three prosecutions for breaches of Section 3 (1) of the Health and Safety at Work etc Act 1974. The first prosecution was in connection with a fatal accident which occurred on 7 October 1999 at the Llynfi CSO site. Costain Limited pleaded guilty and was fined £200,000 with costs. The second prosecution related to an incident which occurred at Huddersfield Narrow Canal on 12 January 2001. Costain Limited pleaded guilty and was fined £12,000 with costs. The third prosecution related to an incident which occurred at M5 Avonmouth on 8 September 1999 when four subcontractors' operatives tragically fell from a temporary gantry that had become partially detached from the underside of the bridge. Costain Limited and their co-defendant, Yarn Road Limited (formerly Kvaerner Cleveland Bridge Limited), were jointly fined £500,000 plus costs.

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. It is the Group's policy to enter into an appropriate form of contractual agreement on payment terms and to pay accordingly 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 51 (2000: 51) days of average daily purchases. The Company has no trade creditors.

Donations

Group charitable donations of £631 were made during the year. No political donations were made.

Auditors

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

Annual General Meeting

The Annual General Meeting of the Company will be held at One Great George Street, Westminster, London, SW1P 3AA on Friday, 24 May 2002 at 11:00 am. The following resolutions will be proposed as Special Business:

a. An ordinary resolution will be proposed to renew the directors' authority to allot relevant securities within the meaning of Section 80 of the Companies Act 1985. The current authority lapses on 24 May 2006 but this authority is normally renewed at each Annual General Meeting so that the authority under the resolution (resolution no. 5 in the Notice of Meeting) will replace the existing authority and will lapse on 23 May 2007. The authority is limited to shares of a nominal value of £11 million which equates to 110 million ordinary shares of 10p each being approximately 33% of the current issued ordinary share capital.

b. Resolution 6 in the Notice of Meeting is a special resolution for the renewal of the directors' authority (i) to make a rights issue and (ii) to issue a limited number of shares for cash without first offering them to shareholders pro-rata to their holdings. In the latter case the authority is limited to shares of a nominal value of £1.6 million which equates to 16 million ordinary shares of 10p each which is approximately 5% of the currently issued ordinary share capital. The authority contained in the resolution expires at the earlier of next year's Annual General Meeting and 23 August 2003.

c. Resolution 7 in the Notice of Meeting is an ordinary resolution seeking approval for a long-term incentive plan (the "LTIP") which is more particularly described in a letter to members from the Chairman of the Remuneration Committee dated the 19 April 2002 and which accompanies the Annual Report. A copy of the draft rules of the plan will be available for inspection at the registered office of the Company and at the offices of KPMG, 8 Salisbury Square, London, EC4Y 8BB during normal business hours on any weekday (Saturdays and Public Holidays excepted) from the date of despatch of the circular up to and including the date of the Annual General Meeting and at the place of the Annual General Meeting for at least fifteen minutes prior to and during the Annual General Meeting.

d. Resolution 8 in the Notice of Meeting is an ordinary resolution seeking approval of the Company's 2002 Save As You Earn Plan (the "SAYE Plan") which is more particularly described in a letter to members from the Chairman of the Remuneration Committee dated 19 April 2002 and which accompanies the Annual Report. A copy of the draft rules of the plan will be available for inspection at the registered office of the Company and at the offices of KPMG, 8 Salisbury Square, London, EC4Y 8BB during normal business hours on any weekday (Saturdays and Public Holidays excepted) from the date of the despatch of the circular up to and including the date of the Annual General Meeting and at the place of the Annual General Meeting for at least fifteen minutes prior to and during the Annual General Meeting.

The directors have no current intention of exercising either authority contained in Resolution 5 or 6 in the Notice of Meeting save, in the case of the authority contained in Resolution 6, to the extent that it is necessary to satisfy the LTIP or the SAYE Plan referred to in Resolutions 7 and 8 in the Notice of Meeting.

Mr David Alvey the Chairman of the Audit Committee and Mr John Bryant the Chairman of the Remuneration Committee will be available at the Annual General Meeting.

By Order of the Board
Clive L. Franks
 Secretary

26 March 2002

26 Directors' responsibilities in respect of the preparation of financial statements

The directors are obliged, under company law, to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

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

In addition, the directors are responsible for maintaining proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 1985. The directors also have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

For the purposes of the above statement, the term "Company" shall be taken to include the Company and the Group.

27 Independent auditors' report to the members of Costain Group PLC

Costain Group PLC Annual Report 2001
Independent auditors' report to the members of Costain Group PLC

We have audited the financial statements on pages 28 to 46. We have also examined the amounts disclosed relating to the emoluments, shares options, long-term incentive scheme interests and directors' pension entitlements which form part of the Report on Directors' Remuneration on pages 19 to 23.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report. As described on page 26 this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding directors' remuneration and transactions with the Group is not disclosed.

We review whether the statement on pages 16 to 23 reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control covers all risks and controls or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error, in forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2001 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc
KPMG Audit Plc
Chartered Accountants
Registered Auditor
London
26 March 2002

28 Consolidated profit and loss account

Year ended 31 December

	Notes	2001 Continuing £m	2000 Continuing £m
Turnover	2		
Group undertakings and Group share of joint ventures		462.9	386.3
Less: Group share of joint ventures turnover		(5.8)	(5.1)
Group turnover		457.1	381.2
Cost of sales		(440.7)	(368.2)
Gross profit		16.4	13.0
Administration expenses		(16.1)	(15.8)
Operating profit/(loss) from Group undertakings		0.3	(2.8)
Share of joint ventures operating results		1.9	1.3
Operating profit/(loss) – Group and share of joint ventures		2.2	(1.5)
Profit on sale of fixed assets		–	1.9
Profit on ordinary activities before interest		2.2	0.4
Net interest receivable/(payable) and similar income/(charges)			
Group undertakings	4	2.5	2.2
Joint ventures		(0.5)	(0.3)
Other finance income – Group undertakings	5	4.5	4.2
Profit on ordinary activities before taxation	2, 3	8.7	6.5
Taxation	8	(0.5)	(1.4)
Profit on ordinary activities after taxation		8.2	5.1
Equity minority interests		0.1	–
Profit for the financial year	21	8.3	5.1
Earnings per share – basic and diluted	10	2.5p	1.5p

During the year and the previous year, no businesses were acquired and therefore all continuing results arise from existing operations.

The notes on pages 33 to 46 form part of these accounts.

29 Consolidated cash flow statement

Year ended 31 December

	£m	2001 £m	£m	2000 £m
Net cash inflow from operating activities		19.4		9.0
Returns on investments and servicing of finance				
Interest received	2.8		3.1	
Interest paid	(0.3)		(0.9)	
Net cash inflow from returns on investments and servicing of finance		2.5		2.2
Taxation				
Overseas tax paid		(0.2)		(0.6)
Capital expenditure and financial investment				
Purchases of tangible fixed assets	(0.8)		(0.4)	
Sales of tangible fixed assets	1.0		3.5	
Funding of investments	-		(1.4)	
Loans to joint ventures	(0.4)		(0.7)	
Repayment of loans to joint ventures	3.1		-	
Net cash inflow from capital expenditure and financial investment		2.9		1.0
Net cash inflow before financing		24.6		11.6
Financing				
Loan repayments	(2.9)		(3.1)	
Net cash outflow from financing		(2.9)		(3.1)
Increase in cash in the year		21.7		8.5

Costain Group PLC Annual Report 2001
 Consolidated cash flow statement

Reconciliation of net cash flow to movement in net cash

	2001 £m	2000 £m
Increase in cash in the year	21.7	8.5
Cash outflow from reduction in loan financing	2.9	3.1
	24.6	11.6
Currency realignment	0.5	0.8
Movement in net cash	25.1	12.4
Net cash at 1 January	42.7	30.3
Net cash at 31 December	67.8	42.7

The notes on pages 33 to 46 form part of these accounts and the notes to the cash flow statement are shown in note 25.

30 Consolidated balance sheet

As at 31 December

	Notes	2001 £m	2000 £m
Fixed assets			
Tangible assets	11	2.8	4.2
Investments	12	1.1	1.1
Investments in joint ventures	12		
Share of gross assets		48.6	45.4
Share of gross liabilities		(40.9)	(39.0)
		11.6	11.7
Current assets			
Stocks		1.1	1.6
Debtors	13	95.6	96.2
Cash at bank, monies on deposit and in hand	14	69.1	51.7
		165.8	149.5
Creditors: amounts falling due within one year			
Bank loans and overdrafts	15	(1.3)	(9.0)
Other creditors	17	(166.3)	(143.0)
		(167.6)	(152.0)
Net current assets/(liabilities)			
Due within one year		(7.3)	(7.1)
Due after one year	13	5.5	4.6
		(1.8)	(2.5)
Total assets less current liabilities			
		9.8	9.2
Creditors: amounts falling due after more than one year			
Other creditors	17	(0.5)	(0.5)
Provisions for liabilities and charges			
	18	(14.5)	(17.5)
Net liabilities excluding pension asset			
		(5.2)	(8.8)
Pension asset	19	9.5	34.6
Net assets including pension asset			
		4.3	25.8
Share capital and reserves			
Called up ordinary share capital	20	33.7	33.7
Share premium account	21	119.3	119.3
Profit and loss account	21	(148.9)	(127.6)
Equity shareholders' funds			
	22	4.1	25.4
Equity minority interests			
		0.2	0.4
		4.3	25.8

The accounts were approved by the Board of directors on 26 March 2002 and were signed on its behalf by:

D G Jefferies Director

S J Doughty Director

The notes on pages 33 to 46 form part of these accounts.

31 Company balance sheet

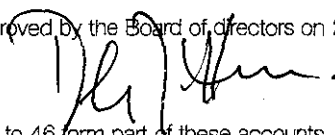
As at 31 December

	Notes	2001 £m	2000 £m
Fixed assets			
Investments	12	115.9	115.9
Current assets			
Debtors	13	6.1	3.3
Cash at bank, monies on deposit and in hand		19.1	1.3
		25.2	4.6
Creditors: amounts falling due within one year			
Other creditors	17	(111.0)	(89.6)
Net current liabilities		(85.8)	(85.0)
Total assets less current liabilities		30.1	30.9
Provisions for liabilities and charges	18	(3.3)	(4.0)
Net assets		26.8	26.9
Share capital and reserves			
Called up ordinary share capital	20	33.7	33.7
Share premium account	21	119.3	119.3
Profit and loss account	21	(126.2)	(126.1)
Equity shareholders' funds	22	26.8	26.9

The accounts were approved by the Board of directors on 26 March 2002 and were signed on its behalf by:

D G Jefferies Director
S J Doughty Director

The notes on pages 33 to 46 form part of these accounts.




32 Statement of total consolidated recognised gains and losses

Year ended 31 December

	Notes	2001 £m	2000 £m
Profit for the financial year from Group undertakings		6.9	4.1
Profit for the financial year from joint ventures		1.4	1.0
		8.3	5.1
Currency translation differences		(1.9)	(0.9)
Actuarial loss recognised in the pension scheme	19	(39.5)	(10.7)
Deferred tax arising thereon		11.8	3.2
Total recognised losses relating to the year	22	(21.3)	(3.3)

Historical cost profit is not materially different from reported profit.

33 Notes to the accounts

1 Accounting policies

BASIS OF ACCOUNTING

The accounts are prepared in accordance with applicable United Kingdom accounting standards under the historical cost convention. The following principal accounting policies have been applied consistently in dealing with items that are considered material in relation to the Group's accounts.

BASIS OF CONSOLIDATION

- a) The Group accounts include the accounts of Costain Group PLC and its subsidiary undertakings as at 31 December 2001. Details of the principal subsidiary undertakings, joint ventures and joint arrangements are shown in note 26.
- b) Investments in joint ventures are accounted for under the gross equity method.
- c) Interests in joint arrangements are accounted for by recognising the Group's share of assets and liabilities, profits, losses and cash flows measured in accordance with the terms of each arrangement.
- d) Goodwill represents the excess of the purchase consideration over the fair value of attributable net assets at the date of acquisition. Goodwill arising on acquisitions before 1 January 1998, when FRS 10, 'Goodwill and intangible assets' was adopted, was charged immediately against reserves. There have been no acquisitions since 1 January 1998.
- e) The balance sheets of overseas subsidiary undertakings and interests in overseas joint ventures are expressed in sterling at the rates of exchange ruling at 31 December. Profits and losses of overseas subsidiary undertakings and joint ventures are expressed in sterling at average rates of exchange. Exchange differences arising on translation of opening shareholders' funds less related foreign currency borrowings which finance overseas equity investments are recorded as a movement on reserves.

TURNOVER

Turnover represents the amounts receivable for goods and services provided, the value of work carried out during the year on long-term contracts, house sales, trading and investment property sales completed and rental income. Turnover includes the Group's share of turnover of joint arrangement contracts.

FOREIGN CURRENCY TRANSACTIONS

Monetary assets and liabilities in overseas currencies are translated into sterling at year-end exchange rates. Exchange differences on such items and on transactions completed in the ordinary course of business are dealt with in profit on ordinary activities.

HEDGING

The Group protects the sterling value of overseas income, where appropriate, by means of forward sales contracts. Profits or losses arising from these arrangements are accounted for in the period in which the contracts are due to mature. Accordingly, no account is taken of unrealised profits or losses arising on such forward contracts.

DEPRECIATION

Except for land, the cost or valuation of tangible fixed assets less any residual value is depreciated over the expected life on a straight line basis. Buildings are depreciated at a rate of 2% (or the life of the lease if that is less than 50 years). Plant and equipment is generally depreciated over the shorter of the remaining economic life of the plant and 12 years. The depreciation rates for the principal assets of the Group vary from 8% to 20% per annum.

Additional write-downs are made if, in the opinion of the directors, there has been a permanent diminution in the value of a class of asset, which is assessed by reference to the anticipated cash flows to be generated by those assets over their remaining useful lives.

INTEREST AND FINANCE CHARGES

Interest and finance charges are written off to the profit and loss account as incurred.

TAXATION

Deferred tax has been recognised as a liability or asset if transactions have occurred at the balance sheet date that give rise to an obligation to pay more tax in future, or a right to pay less tax in future. An asset is not recognised to the extent that the transfer of economic benefit in future is uncertain. Deferred tax assets and liabilities recognised have not been discounted.

No provision is made to cover any further liability to taxation that would arise in respect of the distribution of profits retained by overseas subsidiary undertakings and joint ventures.

LEASED ASSETS

Assets held under finance leases are included under tangible fixed assets at their capital value and depreciated over their useful lives. Lease payments consist of capital and interest elements and the interest element is charged to the profit and loss account. The annual rentals in respect of operating leases are charged to the profit and loss account.

STOCKS

Stocks comprise raw materials and are stated at the lower of cost and net realisable value.

LONG-TERM CONTRACTS

Amounts recoverable on long-term contracts represents the excess of the value of work carried out over cumulative payments on account. Long-term contracts are valued at cost plus attributable profit earned to date, less provision for foreseeable losses.

34 Notes to the accounts — continued

PENSIONS

The Group operates a pension scheme providing benefits based on final pensionable salary. 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 increase in the present value of the liabilities of the Group's defined benefit pension schemes expected to arise from employee service in the period is charged to the operating profit. The expected return on the schemes assets and the increase during the period in the present value of the schemes liabilities arising from the passage of time are included in the other finance income. Actuarial gains and losses are recognised in the statement of total recognised gains and losses.

2 Business and geographical segment information

Business segment information

In the opinion of the directors, the administering of the engineering and construction projects is the only material class of business.

Geographical segment information by origin

	Turnover		Profit/(loss)		Net assets/(liabilities)	
	2001 £m	2000 £m	2001 £m	2000 £m	2001 £m	2000 £m
Continuing operations						
Group undertakings						
United Kingdom	415.6	327.1	(2.2)	(5.1)	(68.8)	(31.2)
Rest of the world	41.5	54.1	2.5	2.3	(2.4)	7.9
Turnover, operating profit/(loss) and net liabilities of Group undertakings	457.1	381.2	0.3	(2.8)	(71.2)	(23.3)
Joint ventures						
United Kingdom	-	-	-	-	1.6	2.3
Rest of the world	5.8	5.1	1.9	1.3	6.1	4.1
	462.9	386.3	2.2	(1.5)	(63.5)	(16.9)
Profit on sale of fixed assets						
United Kingdom			-	-		
Rest of the world			-	1.9		
Net interest receivable/(payable) and similar income/(charges)			2.0	1.9		
Other finance income			4.5	4.2		
Net cash					67.8	42.7
Profit on ordinary activities before taxation and net assets			8.7	6.5	4.3	25.8

Turnover by destination is not materially different to turnover by origin.

3 Profit on ordinary activities before taxation

	2001 £m	2000 £m
Profit on ordinary activities before taxation is stated after charging:		
Staff costs (note 6)	62.0	58.3
Remuneration of directors (note 7)	1.0	0.7
Depreciation on assets owned by Group (note 11)	0.8	0.9
Hire of plant and machinery	10.6	11.5
Rent of land and buildings	4.0	4.3
Auditors' remuneration – audit services – Group	0.3	0.3
– audit services – Company	–	–
– other fees paid to the auditors and their associates	0.1	0.1
and after crediting:		
Net income from rents of land and buildings	1.4	1.2
Rental receivable from hire of plant and machinery	1.1	1.1

4 Net interest receivable/(payable) and similar income/(charges) of Group undertakings

	2001 £m	2000 £m
Interest payable on bank loans and overdrafts	(0.3)	(0.9)
Interest receivable	2.8	3.1
	2.5	2.2

5 Other finance income of Group undertakings

	2001 £m	2000 £m
Expected return on pension scheme assets	22.6	22.6
Interest on pension scheme liabilities	(18.1)	(18.4)
Net return	4.5	4.2

6 Staff costs

	2001 £m	2000 £m
Wages and salaries	53.2	50.4
Social security costs	4.4	3.8
Pension costs (note 19)	4.4	4.1
	62.0	58.3

The average number of persons employed by the Group during the year was:

	2001 Number	2000 Number
United Kingdom	1,473	1,440
Rest of the world	1,804	2,171
	3,277	3,611

7 Emoluments of directors

Details of directors' emoluments and share options are included on pages 21 to 23 in the Report of the Directors.

36 Notes to the accounts — continued

8 Taxation

	2001 £m	2000 £m
On profit for the year:		
United Kingdom corporation tax at 30%	-	-
Overseas taxation	(0.2)	(0.3)
Adjustments in respect of prior years	-	0.3
	(0.2)	-
Deferred taxation	(0.3)	(1.2)
Adjustments in respect of prior years	-	(0.2)
	(0.5)	(1.4)

	2001 £m	2000 £m
Tax reconciliation:		
Profit on ordinary activities before taxation	8.7	6.5
Tax at 30%	(2.6)	(2.0)
Rate adjustments relating to overseas profits	0.1	0.5
Sundry disallowed expenses and profits relieved by capital losses	(0.2)	0.7
Unrelieved overseas taxation	-	(0.3)
Timing differences relating to the pension asset	1.1	1.0
Other timing differences	1.6	(0.1)
Exchange differences	(0.2)	(0.1)
Adjustments in respect of prior years	-	0.3
Tax charge for current year	(0.2)	-

Accumulated tax losses carried forward, mainly in the United Kingdom, are estimated at £15.5m (2000: £10.6m).

The elements of deferred taxation are as follows:

	2001 £m	2000 £m
Accelerated capital allowances	(1.8)	(1.2)
Other timing differences	(0.9)	(0.7)
Deferred tax asset (note 13)	(2.7)	(1.9)
Deferred tax liability on pension asset (note 19)	4.0	14.8
	1.3	12.9

The movements in the deferred taxation balance were as follows:

	£m
Provision at beginning of year	12.9
Amount charged to profit and loss account	0.3
Amount credited to the statement of recognised gains and losses	(11.8)
Exchange differences	(0.1)
Provision at end of year	1.3

There are other deferred tax assets that have not been recognised on the basis that their future economic benefit is uncertain.

9 Profit attributable to Costain Group PLC

The loss dealt with in the accounts of Costain Group PLC is £0.1m (2000: £2.2m profit). A separate profit and loss account for Costain Group PLC has not been presented as permitted by Section 230 of the Companies Act 1985.

10 Earnings per share

The calculation of earnings per share is based on earnings of £8.3m (2000: £5.1m) and 337,136,350 ordinary shares being the weighted average number of ordinary shares in issue during the year.

Diluted earnings per share are the same as basic earnings per share.

11 Tangible assets – Group

	Freehold £m	Land and buildings		Plant and equipment Owned £m	Total £m
		Leasehold Over 50 years £m	Leasehold 50 years and under £m		
Cost					
At 1 January 2001	1.2	0.3	4.0	15.5	21.0
Currency realignment	(0.1)	–	0.1	(1.0)	(1.0)
Additions	–	–	0.1	0.7	0.8
Disposals	–	–	–	(5.7)	(5.7)
At 31 December 2001	1.1	0.3	4.2	9.5	15.1
Depreciation					
At 1 January 2001	0.1	0.1	3.8	12.8	16.8
Currency realignment	–	–	0.1	(0.7)	(0.6)
Provided in year	–	–	0.1	0.7	0.8
Disposals	–	–	–	(4.7)	(4.7)
At 31 December 2001	0.1	0.1	4.0	8.1	12.3
Net book value					
At 31 December 2001	1.0	0.2	0.2	1.4	2.8
At 31 December 2000	1.1	0.2	0.2	2.7	4.2

Freehold land and buildings includes land of £0.7m (2000: £0.7m) on which no depreciation has been charged.

38 Notes to the accounts — continued

12 Investments – Group

	Joint ventures £m	Loans to joint ventures £m	Other investments £m	Other loans £m	Total £m
Cost					
At 1 January 2001	26.3	5.5	0.9	1.1	33.8
Currency realignment	(0.6)	(0.1)	–	–	(0.7)
Additions	–	0.4	–	–	0.4
Repayments	–	(3.1)	–	–	(3.1)
Disposals	(0.1)	(0.4)	(0.4)	–	(0.9)
At 31 December 2001	25.6	2.3	0.5	1.1	29.5

Share of post-acquisition reserves

At 1 January 2001	(20.7)				(20.7)
Currency realignment	0.3				0.3
Profit for the year	1.4				1.4
Eliminated on disposal	0.5				0.5
At 31 December 2001	(18.5)				(18.5)

Amounts written off

At 1 January 2001	(4.4)	(0.3)	(0.9)	–	(5.6)
Currency realignment	0.1	–	–	–	0.1
Released in the year	2.9	–	–	–	2.9
Disposals	–	–	0.4	–	0.4
At 31 December 2001	(1.4)	(0.3)	(0.5)	–	(2.2)

Net book value

At 31 December 2001	5.7	2.0	–	1.1	8.8
At 31 December 2000	1.2	5.2	–	1.1	7.5

Investments – Company

	Subsidiary undertakings £m	Other investments £m	Total £m
Cost			
At 1 January 2001	387.6	0.4	388.0
Disposals	–	(0.4)	(0.4)
At 31 December 2001	387.6	–	387.6
Amounts written off			
At 1 January 2001	(271.7)	(0.4)	(272.1)
Disposals	–	0.4	0.4
At 31 December 2001	(271.7)	–	(271.7)
Net book value			
At 31 December 2001	115.9	–	115.9
At 31 December 2000	115.9	–	115.9

Details of the principal subsidiary undertakings and joint ventures are shown in note 26.

13 Debtors

	Group		Company	
	2001 £m	2000 £m	2001 £m	2000 £m
Amounts falling due within one year:				
Trade debtors	58.2	39.3	-	-
Other debtors	6.6	12.5	-	-
Amounts recoverable on long-term contracts	23.2	35.9	-	-
Prepayments and accrued income	2.0	3.9	-	0.2
Amounts owed by joint ventures	0.1	-	-	-
Amounts owed by subsidiary undertakings	-	-	5.5	1.9
Taxation	-	-	0.6	1.2
	90.1	91.6	6.1	3.3
Amounts falling due after more than one year:				
Other debtors	2.8	2.7	-	-
Deferred tax asset (note 8)	2.7	1.9	-	-
	5.5	4.6	-	-
	95.6	96.2	6.1	3.3

14 Cash at bank, monies on deposit and in hand – Group

Cash at bank, monies on deposit and in hand is analysed in note 16 and includes the Group's share of cash held by joint arrangements of £38.0m (2000: £30.1m). There are restrictions on these funds being transferred from the relevant joint arrangement.

15 Bank loans and overdrafts – Group

	2001 £m	2000 £m
Amounts falling due within one year:		
Overdrafts	1.3	6.0
Bank loans	-	3.0
Total borrowings	1.3	9.0

In 2000, bank loans of £3.0m were secured on the assets of Costain America Inc.

40 Notes to the accounts — continued

16 Financial instruments

An explanation of the Board's objectives, policies and strategies for holding and issuing financial instruments is set out in the financial review on page 13.

Short-term debtors and creditors, as defined in FRS 13, 'Derivatives and other financial instruments: disclosures', have been omitted from all of the financial instruments disclosures, save for those relating to currency risk.

a) Liquidity

The maturity of all financial liabilities is shown in note 15.

b) Undrawn committed borrowings facilities

Undrawn borrowing facilities are available to the Group as set out below. The conditions precedent to the availability of these facilities were all satisfied at the balance sheet date.

	2001 £m	2000 £m
Expiring in one year or less	3.0	10.4

c) Interest rate risk

The Group's financial liabilities were all at floating rate and denominated in the following currencies:

	2001 £m	2000 £m
US dollars	-	3.0
Sterling	1.0	5.4
Other	0.3	0.6
	1.3	9.0

The interest rate on sterling denominated borrowings is based on Base rate.

The Group's financial assets which comprised cash at bank, monies on deposit and in hand were denominated in the following currencies:

	2001 £m	2000 £m
Sterling	61.6	30.0
UAE Dirhams	2.2	3.4
Hong Kong Dollars	2.9	16.3
Zimbabwe Dollars	0.4	0.9
US Dollars	0.4	0.2
Other	1.6	0.9
	69.1	51.7

d) Currency risk

At 31 December 2001, the net monetary assets denominated in currencies other than the functional currency of the operation involved were Hong Kong dollar denominated net assets of £2.3m and US dollar denominated assets of £2.5m in the books of sterling companies. Forward currency sale contracts of US Dollars totalling £2.9m were in place at the year end as protection against currency fluctuations. At 31 December 2001, the unrealised profit on the forward contracts was £0.1m.

e) Fair value

The fair value of financial assets and financial liabilities is the same as the book value.

17 Other creditors

	Group		Company	
	2001 £m	2000 £m	2001 £m	2000 £m
Amounts falling due within one year:				
Trade creditors	63.5	49.0	-	-
Other creditors	8.8	10.8	0.5	-
Social security	2.9	1.1	-	-
Credit balances on long-term contracts	21.4	27.0	-	-
Accruals and deferred income	67.6	53.1	0.3	0.5
Amounts owed to subsidiary undertakings	-	-	108.4	87.3
Taxation	2.1	2.0	1.8	1.8
	166.3	143.0	111.0	89.6
Amounts falling due after more than one year:				
Accruals and deferred income	0.5	0.5	-	-
	0.5	0.5	-	-

18 Provisions for liabilities and charges – Group

	At beginning of year £m	Provided £m	Utilised £m	At end of year £m
Engineering & Construction provisions	13.4	3.4	(5.6)	11.2
US Mining – reclamation and other provisions	0.3	-	(0.1)	0.2
Void space	2.4	-	(0.6)	1.8
Other provisions ^a	1.4	-	(0.1)	1.3
	17.5	3.4	(6.4)	14.5

E & C provisions are in respect of liabilities incurred on long-term contracts most of which are estimated to be paid over the next two years.

US Mining provisions are mainly in respect of remedial costs, most of which are expected to be paid over the next year.

Void space provisions relate to costs of vacant properties. The provisions will be utilised over the next five years.

Other provisions comprise remedial costs and litigation provisions that are expected to be utilised over the next year.

Provisions for liabilities and charges – Company

	At beginning of year £m	Provided £m	Released £m	At end of year £m
Provisions against losses of subsidiary companies	3.2	1.1	(1.8)	2.5
Other provisions	0.8	-	-	0.8
	4.0	1.1	(1.8)	3.3

19 Pensions

The Group operates a number of pension schemes principally of the defined benefit type in the United Kingdom and overseas, under which contributions are paid by Group undertakings and employees. The pension cost charge of the United Kingdom pension schemes amounted to £4.4m (2000: £4.0m).

A full actuarial valuation of the United Kingdom scheme was carried out at 31 March 2001 and was updated to 31 December 2001 by a qualified independent actuary. The major assumptions used by the actuary were (in nominal terms):

	31.12.2001	31.12.2000	31.12.1999
Rate of increase in pensionable salaries	4.0%	4.0%	4.4%
Rate of increase in pensions in payment	2.5%	2.5%	2.9%
Discount rate	6.0%	5.9%	6.2%
Inflation assumption	2.5%	2.5%	2.9%

42 Notes to the accounts — continued

19 Pensions – continued

The assets in the scheme and the expected rate of return (net of administrative expenses) were:

	31.12.2001	31.12.2001 £m	31.12.2000	31.12.2000 £m	31.12.1999	31.12.1999 £m
Equities	7.2%	206.4	7.4%	231.5	7.2%	240.2
Bonds	4.9%	123.8	4.6%	128.7	4.9%	117.2
Total market value of assets		330.2		360.2		357.4
Actuarial value of liability		(316.7)		(310.8)		(300.7)
Surplus in the scheme		13.5		49.4		56.7
Related deferred tax liability		(4.0)		(14.8)		(17.0)
Net pension asset		9.5		34.6		39.7

Movement in surplus during the year

	2001 £m	2000 £m
Surplus in scheme at beginning of year	49.4	56.7
Movement in year (current service cost)	(4.3)	(4.0)
Contributions	3.4	3.2
Net return on assets	4.5	4.2
Actuarial loss	(39.5)	(10.7)
Surplus in scheme at end of year	13.5	49.4

The estimated actuarial valuation at 31 December 2001 showed a surplus of £13.5 million. The full actuarial valuation as at 31 March 2001 stated that the employer contribution rate could remain at 9.6% of pensionable salaries until the completion of the next full actuarial valuation to be carried out as at 31 March 2003, subject to actuarial review during this period. Employer contributions were paid at this rate in 2001.

20 Share capital of Costain Group PLC

	2001 and 2000	
	Authorised	issued and fully paid
	£	£
Ordinary shares of 10p each	55,000,000	33,713,635

On 26 January 1998, Mr Armitt was granted options over 774,648 Ordinary shares under the Costain Executive Share Option Scheme. The options lapsed as they were not exercised on or before 31 December 2001, following Mr Armitt's resignation from the Company on 30 June 2001. At 31 December 2001, options over a total of 15,000 shares (2000: 789,648 shares) were outstanding as follows:

Date of grant	Exercise price per share	Number of shares
13 April 1994	£3.57	15,000

The options granted on 13 April 1994 are exercisable up to 12 April 2004.

During the year, no options were granted under The Costain Group Performance Share Scheme. At 31 December 2001, no options (2000: Nil) were outstanding.

During the year no options were granted under the Costain Share Saving Scheme. At 31 December 2001, options over a total of 389,836 shares (2000: 628,596 shares) were outstanding as follows:

Date of grant	Exercise price per share	Number of shares
22 November 1996	£0.38	389,836

These options are exercisable up to 1 July 2002.

21 Reserves – Group

	Share premium account £m	Profit and loss £m
At 1 January 2001	119.3	(127.6)
Net exchange differences	–	(1.9)
Profit for the financial year	–	8.3
Actuarial loss recognised	–	(39.5)
Deferred tax	–	11.8
At 31 December 2001	119.3	(148.9)

The closing balance on the profit and loss includes £9.5m (2000: £34.6m), stated after deferred taxation of £4.0m (2000: £14.8m) in respect of pension scheme assets of the Group pension fund.

At 31 December 2001, the cumulative goodwill written off on acquisitions prior to 1 January 1998 amounted to £3.3m (2000: £3.3m).

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

Reserves – Company

	Share premium account £m	Profit and loss £m
At 1 January 2001	119.3	(126.1)
Loss for the year	–	(0.1)
At 31 December 2001	119.3	(126.2)

22 Reconciliations of movements in shareholders' funds

	Group		Company	
	2001 £m	2000 £m	2001 £m	2000 £m
Profit/(loss) for the financial year	8.3	5.1	(0.1)	2.2
Other recognised losses in the year	(29.6)	(8.4)	–	–
Net (reduction)/increase in shareholders' funds	(21.3)	(3.3)	(0.1)	2.2
Opening shareholders' funds	25.4	28.7	26.9	24.7
Closing shareholders' funds	4.1	25.4	26.8	26.9

23 Contingent liabilities

	Group		Company	
	2001 £m	2000 £m	2001 £m	2000 £m
Under guarantees of bank overdrafts, mortgages and loans:				
To subsidiary undertakings	–	–	0.2	3.5
To joint ventures	0.2	1.7	0.2	1.7

Certain subsidiary undertakings have entered into cross-guarantees for loans and overdraft facilities made available to the Group and certain joint ventures. At 31 December 2001, these liabilities amounted to £0.2m (2000: £4.6m) and are included or disclosed in these accounts.

The shares of Alcaidesa Holding SA held by Costain Alcaidesa Limited have been pledged as security for certain loans to Alcaidesa Holding SA.

There are also contingent liabilities in respect of:

- creditors of joint arrangements which are less than the book value of their assets;
- performance bonds and other undertakings entered into in the ordinary course of business.

44 Notes to the accounts — continued

24 Other financial commitments – Group

	2001		2000	
	Land and buildings £m	Other operating leases £m	Land and buildings £m	Other operating leases £m
Annual commitments under non-cancellable operating leases expiring:				
– within one year	–	0.8	–	0.4
– between one and two years	–	0.9	–	0.8
– between two and five years	0.5	0.7	0.1	0.6
– after five years	2.6	–	3.0	–
	3.1	2.4	3.1	1.8

25 Notes to the cash flow statement

Reconciliation of operating profit/(loss) to net cash inflow from operating activities

	2001 £m	2000 £m
Operating profit/(loss)	2.2	(1.5)
Depreciation	0.8	0.9
Amounts written back to investments	(2.9)	(0.7)
Joint ventures	(1.9)	(1.3)
Decrease/(increase) in stocks	0.8	(0.1)
Decrease in debtors	3.0	10.7
Increase/(decrease) in creditors	20.4	(3.6)
(Decrease)/increase in provisions	(3.0)	4.6
Net cash inflow from operating activities	19.4	9.0

Analysis of changes in net cash

	At 1 January 2001 £m	Currency realignment £m	Cashflow £m	At 31 December 2001 £m
Cash (note 14)	51.7	0.4	17.0	69.1
Overdrafts	(6.0)	–	4.7	(1.3)
	45.7	0.4	21.7	67.8
Bank loans due within one year	(3.0)	0.1	2.9	–
Net cash	42.7	0.5	24.6	67.8

26 Principal subsidiary undertakings, joint ventures and joint arrangements

	Activity	Percentage of equity held	Country of incorporation
Subsidiary undertakings			
Costain Abu Dhabi Co WLL	Process & Civil Engineering & Construction	49+*	UAE
Costain (Africa) Ltd	Holding & Property Company	100+	Zimbabwe
Costain America Inc	Holding Company	100+	USA
Costain Building & Civil Engineering Ltd	Civil Engineering & Construction	100+	
Costain Ltd	Civil Engineering & Construction	100+	
Costain Construction Ltd	Construction	100+	
Costain Dubai LLC	Civil Engineering & Construction	49+*	UAE
Costain Engineering & Construction Ltd	Holding Company	100	
Costain International Ltd	Civil Engineering & Construction	100+	
Costain (Malaysia) Sdn Bhd	Civil Engineering & Construction	100+	Malaysia
Costain Oil, Gas & Process Ltd	Process Engineering	100+	
Costain Oil, Gas & Process (Overseas) Ltd	Process Engineering	100+	
Costain USA Inc	Holding Company	100	USA
County & District Properties Ltd	Commercial Property	100	
Costain Zimbabwe (Pvt) Ltd	Civil Engineering & Construction	100+	Zimbabwe
Richard Costain Ltd	Service Company	100	
Yahya Costain LLC	Civil Engineering & Construction	49+*	Oman
	Activity	issued share capital £m	Percentage of equity held Country of incorporation
Joint ventures			
Alcaidesa Holding SA	Residential Property	18.7	50+ Spain
Jalal Costain WLL	Civil Engineering & Construction	0.1	49+ Bahrain
HpC King's College Hospital (Holdings) Ltd	Construction & Operation of Hospital	0.2	33+ UK

+ Equity capital held by subsidiary undertakings.

* Treated as subsidiary undertakings due to Costain having dominant influence and control of the composition of the Board of Directors.

All undertakings are incorporated in Great Britain, except where otherwise stated, and operate mainly in the country of incorporation with the exception of Costain Building & Civil Engineering Ltd and Costain Ltd which operate inside and outside of the UK and Costain International Ltd and Costain Oil, Gas & Process (Overseas) Ltd which operate in various countries outside the UK. All holdings are of ordinary shares except Richard Costain Ltd where Costain Group PLC holds 100 per cent of the ordinary and preference shares. A full list of Group companies will be included in the Company's annual return.

46 Notes to the accounts — continued

26 Principal subsidiary undertakings, joint ventures and joint arrangements – continued

	Activity	Percentage of equity held	Country of incorporation
Major joint arrangements			
Anglo Japanese Contractors Joint Venture	Civil Engineering	33	Hong Kong
Balfour Beatty-Costain Joint Venture – Cardiff Bay Barrage	Civil Engineering	35	UK
Balfour Beatty-Costain Joint Venture – Portsmouth	Civil Engineering	50	UK
Black & Veatch-Costain Joint Venture – Southern Water	Asset Management	50	UK
Costain-Bachy-O'Rourke Joint Venture – CTRL 105	Civil Engineering	33	UK
Costain-China Harbour Joint Venture	Civil Engineering	50	Hong Kong
Costain-Norwest Holst Joint Venture – Hungerford Bridge	Civil Engineering	50	UK
Costain Oil, Gas & Process Ltd and UK Construction Ltd Joint Venture – Seal Reception Facilities, Bacton	Process Engineering	50	UK
Costain-Skanska Joint Venture – A43 Dualling	Civil Engineering	50	UK
Costain-Skanska Joint Venture – Coventry Shopping Centre	Construction	50	UK
Costain-Skanska Joint Venture – Great Western Hotel	Construction	50	UK
Costain-Skanska Joint Venture – King's College Hospital	Construction	50	UK
Costain-Skanska Joint Venture – Met Office	Construction	50	UK
Costain-Skanska Joint Venture – Northgate House	Construction	50	UK
Costain-Skanska Joint Venture – Uxbridge Shopping Centre	Construction	50	UK
Costain-Skanska-Bachy Joint Venture – CTRL 240	Civil Engineering	33	UK
Costain-Skanska-Mowlem Joint Venture – A2/M2	Civil Engineering	30	UK
Costain-Taylor Woodrow Joint Venture – Jubilee Line	Civil Engineering	50	UK
Costain-Taylor Woodrow Joint Venture – King's Cross	Civil Engineering	50	UK
Hochtief-Costain Joint Venture – Winchester House	Construction	50	UK
Mitsui-Costain Joint Venture	Civil Engineering	50	Hong Kong
Nishimatsu-Costain-China Harbour Joint Venture	Civil Engineering	33	Hong Kong
Nishimatsu-Costain Joint Venture	Civil Engineering	50	Hong Kong

27 Related party transactions

The Group's related party transactions, as defined by FRS 8, and the nature of the relationships and the amounts involved are summarised below:

	Major shareholders £m	Joint ventures £m	Joint arrangements £m	Total £m
Sales of goods and services to related parties:				
Staff	–	–	14.8	14.8
Management services	–	–	0.8	0.8
Construction services and materials	–	–	1.6	1.6
Administrative services	–	–	2.4	2.4
	–	–	19.6	19.6

Balances with related parties at 31 December 2001

Amounts due to related parties

Amounts due from related parties

Balances with joint ventures are disclosed elsewhere in these accounts. Balances with joint arrangements are eliminated on consolidation.

Major shareholders

Mohammed Abdulmohsin Al-Kharafi & Sons WLL, Raymond International WLL and Intria Berhad, are regarded as related parties of Costain Group PLC.

47 Five year financial summary

Costain Group PLC Annual Report 2001
Five year financial summary

Turnover and profit

	2001 £m	2000 £m	1999 £m	1998 £m	1997 £m
Turnover					
Continuing operations	457.1	381.2	373.1	381.9	559.9
Discontinued operations	-	-	-	-	11.5
	457.1	381.2	373.1	381.9	571.4
Operating profit/(loss):					
Continuing operations	0.3	(2.8)	2.1	(2.7)	(3.8)
Discontinued operations	-	-	-	0.8	(2.2)
	0.3	(2.8)	2.1	(1.9)	(6.0)
Share of joint ventures	1.9	1.3	(0.9)	(0.5)	(1.6)
Net interest receivable/(payable) and other similar income/(charges)	2.0	1.9	0.8	2.5	(1.5)
Other finance income	4.5	4.2	3.2	-	-
Profit on disposals of discontinued operations	-	-	-	-	1.1
Profit on disposals of fixed assets	-	1.9	1.2	0.4	0.6
Profit/(loss) on ordinary activities before taxation	8.7	6.5	6.4	0.5	(7.4)
Profit/(loss) attributable to Costain Group PLC	8.3	5.1	4.9	0.1	(8.0)
Ordinary dividends	-	-	-	-	-
Amount retained/(deficit) for the year	8.3	5.1	4.9	0.1	(8.0)
Earnings/(loss) per share	2.5p	1.5p	1.5p	0.0p	(3.5)p
Summarised balance sheets					
Tangible assets	2.8	4.2	6.3	7.4	8.3
Investments	8.8	7.5	4.1	4.0	2.5
	11.6	11.7	10.4	11.4	10.8
Pension prepayment	-	-	-	39.5	43.0
Other net current (liabilities)/assets	(1.8)	(2.5)	(7.8)	(4.9)	12.3
Total assets less current liabilities	9.8	9.2	2.6	46.0	66.1
Long-term liabilities	(15.0)	(18.0)	(13.2)	(27.1)	(46.4)
	(5.2)	(8.8)	(10.6)	18.9	19.7
Pension asset	9.5	34.6	39.7	-	-
Net assets including pension asset	4.3	25.8	29.1	18.9	19.7
Equity shareholders' funds	4.1	25.4	28.7	18.5	19.1
Minority interests	0.2	0.4	0.4	0.4	0.6
	4.3	25.8	29.1	18.9	19.7

The figures for 1999 to 2001 comply with FRS 17.

48 Notice of annual general meeting

Notice is hereby given that the Annual General Meeting of the members will be held at One Great George Street, Westminster, London SW1P 3AA on Friday, 24 May 2002 at 11.00 a.m. for the following purposes:

Ordinary Business

1. To receive and adopt the directors' report and the audited accounts for the year ended 31 December 2001.
2. To elect the following directors who offer themselves for re-election: a - Mr David George Jefferies; b - Mr Stuart John Doughty; c - Mr Charles Joseph McCole; d - Mr David Philip Allvey; e - Mr Abdul Wahid bin Omar; f - Mr John Martin Bryant; g - Mr Basil Kim Vasiliou. Mr Vasiliou retires by rotation under Article 81 of the Articles of Association and Mr Jefferies, Mr Doughty, Mr McCole, Mr Allvey, Mr Omar and Mr Bryant retire under Article 77, having been appointed since the last Annual General Meeting. Each re-election will be proposed and voted on as a separate resolution.
3. To re-appoint KPMG Audit Plc auditors of the Company.
4. To authorise the directors to determine the remuneration of the Auditors.

Special Business

To consider and, if thought fit, to pass the following resolutions proposed as follows:

5. As an ordinary resolution:

THAT, in substitution for all subsisting authorities, the directors be and they are hereby generally and unconditionally authorised to exercise all the powers of the Company to allot relevant securities (within the meaning of Section 80 of the Companies Act 1985) up to an aggregate nominal amount of £11m provided that this authority shall expire on 23 May 2007 save that the Company may before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the directors may allot relevant securities in pursuance of such offer or agreement as if the authority confirmed hereby had not expired.

6. As a special resolution:

THAT, pursuant to the authority conferred on them by resolution number 5, the directors be and are hereby empowered pursuant to Section 95 of the Companies Act 1985 to allot equity securities for cash (within the meaning of Section 94 of the said Act) as if sub-section (1) of Section 89 of the said Act did not apply to any such allotment provided that this power shall be limited:

- (a) to the allotment of equity securities pursuant to Article 119 (A) and/or in connection with a rights issue in favour of the shareholders where the equity securities respectively attributable to the interests of all such shareholders are proportionate (as nearly as may be) to the respective numbers of shares held by them subject to such exclusions or

other arrangements as the directors may think fit in connection with fractional entitlements or legal or practical problems arising in connection with the laws of, or requirements of, any recognised regulatory body or stock exchange in any territory; and

- (b) to the allotment (otherwise than pursuant to sub-paragraph (a) above) of equity securities up to an aggregate nominal value of £1.6m

and shall expire 15 months following the passing of this resolution or, if earlier, at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and the directors may allot equity securities in pursuance of such offer or agreement as if the power conferred hereby had not expired.

7. THAT

- (a) the Costain Group PLC Long Term Incentive Plan (the Plan), a summary of which is set out in Part I of the Appendix to the letter from the Chairman of the Remuneration Committee to shareholders dated 19 April 2002, be and is hereby approved and the directors be and they are hereby authorised to do all acts and things necessary to establish and carry it into effect; and

- (b) the directors be and they are hereby authorised to vote and be counted in the quorum on any matter connected with the Plan (except that no director may vote or be counted in the quorum in respect of his own participation) and any prohibition on voting contained in the articles of association of the company be and is hereby relaxed accordingly.

8. THAT

- (a) the Costain Group PLC 2002 Save As You Earn Plan (the Plan), a summary of which is set out in Part II of the Appendix to the letter from the Chairman of the Remuneration Committee to shareholders dated 19 April 2002, be and is hereby approved and the directors be and they are hereby authorised to do all acts and things necessary to establish and carry it into effect; and

- (b) the directors be and they are hereby authorised to vote and be counted in the quorum on any matter connected with the Plan (except that no director may vote or be counted in the quorum in respect of his own participation) and any prohibition on voting contained in the articles of association of the company be and is hereby relaxed accordingly.

By Order of the Board
Clive L Franks
Secretary
19 April 2002

Notes:

1. A member entitled to attend and vote at the meeting may appoint one or more proxies to attend and, on a poll, to vote on his behalf. A proxy need not be a member of the Company. Appointment of a proxy will not preclude a member from attending and voting in person if he so wishes.
2. To be effective, a proxy and the authority (if any) under which it is signed or a notarially certified or office copy of such authority must be deposited with the Company's registrars, Lloyds TSB Bank Registrars, The Causeway, Worthing, West Sussex BN99 6DB no later than 11 am on Wednesday 22 May 2002. A proxy may be delivered by facsimile to the Company's registrars, Lloyds TSB Registrars, (facsimile number 01903 702341) provided that:
 - (a) the facsimile is actually received (whether or not it appears to the sender to have been received) by the Company's registrars no later than 11 am on Wednesday 22 May, 2002.
 - (b) the Chairman or the Secretary or any other person authorised by the Board for the purpose determines in his sole discretion (such determination to be conclusive) that such facsimile has been transmitted in an acceptable manner including a determination that such facsimile is complete and is in a clear and legible form; and
 - (c) the original instrument appointing the proxy and the authority (if any) under which it is executed or a notarially certified or office copy of such authority must be delivered to the Company's registrars, Lloyds TSB Registrars, The Causeway, Worthing, West Sussex, BN99 6DB no later than 10 am on Friday 24 May 2002.
3. The Company pursuant to Regulation 41 of the Uncertified Securities Regulations 2001, specifies that only those shareholders registered in the register of members of the company at 6.00 pm on Wednesday 22 May 2002 shall be entitled to attend or vote at the meeting in respect of the number of shares registered in their name at that time. Changes to entries on the relevant register of securities after 6.00 pm on Wednesday 22 May 2002 shall be disregarded in determining the rights of any person to attend or vote at the meeting.

50 Financial calendar

Half year results – Announced 31 August 2001
Full year results – Announced 27 March 2002
Report & Accounts – Sent to shareholders 19 April 2002
Annual General Meeting – To be held 24 May 2002

Analysis of Shareholders

Shares	Continuing Accounts	(millions)	%
Institutions, companies and nominees:			
Shareholdings 100,000 and over	78	304.5	90.3
Shareholdings 50,000 – 99,999	45	2.9	0.9
Shareholdings 25,000 – 49,999	46	1.6	0.5
Shareholdings 5,000 – 24,999	136	1.6	0.5
Shareholdings 1 – 4,999	359	0.4	0.1
Individuals	14,496	26.1	7.7
	15,160	337.1	100.0

Secretary and Registered Office

Secretary

Clive L Franks

Registered Office

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Maidenhead
Berkshire
SL6 1LN
Telephone 01628 842444
www.costain.com
info@costain.com
Company Number 1393773

Registrar and Transfer Office

Lloyds TSB Registrars
The Causeway
Worthing
West Sussex
BN99 6DA
Telephone 0870 6003970

Costain Group PLC

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