Report and Accounts

The Capita Group Plc

31 December 2005

THE CAPITA GROUP PLC
Registered number 2081330

COMPANY INFORMATION

DIRECTORS
R Aldridge OBE
G M Hurst
P Doyle
Martina King
P Cawdron
E Walters
P R M Pindar

SECRETARY
G M Hurst

AUDITORS
Ernst & Young LLP
1 More London Place
London SE1 2AF

BANKERS
Barclays Bank PLC
154 Lombard Street
London EC3V 9EX

SOLICITORS
Herbert Smith
Exchange House
Primrose Street
London EC2A 2HS

REGISTERED OFFICE
61-71 Victoria Street
London SW1H 0XA

Directors' report

The Directors present their report and the audited Group accounts for the year ended 31 December 2005.

Group activities
The Capita Group Plc and its subsidiaries (the Group) is a leading UK provider of professional support services and business process outsourcing solutions to organisations across the public and private sectors. The Group's 8 chosen markets are local government, central government, education, health, transport, life & pensions, insurance and other private sector (including financial services).

On behalf of its clients, the Group aims to improve service quality, reduce their costs of delivery and enable them to transform the way that they deliver services to their customers. The services that the Group provides are essential to the smooth running and success of its clients' operations. The Group designs, successfully implements and manages tailored service solutions, ranging across administration, information technology, financial, human resources, property and customer service functions. The Group maintains market leading positions due to its ability to draw on its wide base of professional services, detailed market knowledge and extensive business process transformation and change management skills.

The Group's principal activities are managed through five divisions comprising business services, commercial services, corporate services, professional services and integrated services, with two support divisions (being major sales and marketing and central support services).

Profits and dividends
The Group profit before taxation and discontinued operations, amounted to £153.1m (2004: £142.1m). The Directors recommend a final dividend of 4.9p per share (2004: 3.6p per share) to be paid on 5 May 2006 to ordinary shareholders on the register on 7 April 2006. This gives a total dividend for the year of 7.0p per share (2004: 5.35p per share).

Share repurchase
The company renewed its authority to repurchase up to 10% of its own issued share capital at the Annual General Meeting in April 2005 and during the year acquired 13,236,000 (2004: 8,925,000) ordinary shares of 2p each (see note 26) of which 8,236,000 (2004: 8,625,000) were added to those already held as treasury shares, the remainder were cancelled. To date there are 16,861,000 shares held in treasury which are available to satisfy any potential future share issues.

Directors
The Directors of the company currently in office are listed on the preceding page. Gordon Hurst and Eric Walters retire by rotation and, being eligible, offer themselves for re-election. Robert Alcock retired as a Non-Executive Director on 24 February 2005. Martina King was appointed on 1 January 2005. None of the Directors of the company had a material interest in any contract with the company or its subsidiary undertakings other than their contracts of employment and no Director has a service contract exceeding one year.

Directors' interests
The interests (all beneficial) of the Directors in the ordinary shares of the company were as follows:

	31 December 2005 or date of appointment if later Ordinary shares of 2p	31 December 2004 or date of appointment if later Ordinary shares of 2p
Rod Aldridge	**15,764,000**	17,794,000
Paul Pindar	**2,450,000**	3,050,000
Paddy Doyle	**26,664**	25,000
Gordon Hurst	**28,221**	28,221
Peter Cawdron	**24,000**	24,000
Eric Walters	**45,000**	45,000
Martina King (appointed 1 January 2005)	**–**	–

The Directors have no interests in the share capital of any other Group undertaking.

The interests of the Directors under the share option schemes, the Long Term Incentive Plan and the Long Term Indexed Share Appreciation Scheme of the company are shown in the Directors' remuneration report.

Since the year end, Paddy Doyle has acquired 65 ordinary shares of the company through the Capita Share Ownership Plan.

Substantial shareholders
On 22 February 2006 the company had notifications that the following were interested in 3% or more of the company's ordinary share capital:

	Number of shares	Percentage
FMR Corp and Fidelity International Ltd	97,732,752	14.99%
Lloyds TSB Group plc	33,479,685	5.04%

Statement of Directors' responsibilities in respect of the accounts and auditors
Company law requires the Directors to prepare accounts for each financial year that give a true and fair view of the state of affairs of the company and of the Group and of the profit or loss of the Group for that period. In preparing those accounts, the Directors are required to:

- select suitable accounting policies and then apply them consistently
- make judgments and estimates that are reasonable and prudent
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the Group will continue in business
- to the best of each Director's knowledge and belief, there is no information relevant to the preparation of their report of which the company's auditors are unaware
- each Director has taken all steps that a Director might reasonably be expected to have taken to be aware of all relevant audit information and to establish that the company's auditors are aware of that information.

The Directors confirm that the accounts comply with the above requirements.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Going concern
After making enquiries, the Group Board of Directors has a reasonable expectation that the Group and its Group holding company (The Capita Group Plc) have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.

Disabled persons
It is the Group's policy to give full consideration to suitable applications for employment of disabled persons. Disabled employees are eligible to participate in all career development opportunities available to staff. Opportunities also exist for employees of the Group who become disabled to continue in their employment or to be retrained for other positions in the Group.

Employee involvement
The Group is committed to involving all employees in the performance and development of the Group. Its approach to staff development offers continual challenges in the job, learning opportunities and personal development. Capita supports staff through a comprehensive range of key business and management skills courses and an annual management development programme.

The Group encourages all its employees to participate fully in the business through open dialogue. Employees receive news of the Group through *Recap*, the Group's newsletter, frequent email notices, internal notice board statements and *Capita Online*, a regular communication reviewing the performance of the Group from the perspective of the Directors. These communication initiatives enable staff to share information within and between business units and staff are encouraged to contribute news, views and feedback. The Group maintains a strong communications network and employees are encouraged, through our open door policy, to discuss with management matters of interest to the employee and subjects affecting day-to-day operations of the Group.

The Group grants share options to senior employees, on a discretionary basis, in order to reward their long term commitment to the Group. The granting of all share options is subject to the approval of the Remuneration Committee. The share option schemes have been a key factor in attracting, retaining and motivating senior employees across the Group.

The Capita Sharesave Scheme, an employee Save As You Earn Scheme, and the Capita Share Ownership Plan, a share incentive plan, are both firmly established and are designed to promote employee share ownership and to give employees the opportunity to participate in the future success of the Group.

The Group has continued to provide the Capita PC Purchase Scheme, a tax-free benefit, which provides employees with the opportunity to have a personal, high quality home computer at a discounted rate and has established a range of other staff discounts on products and services.

In keeping with its belief that staff are the Group's most valuable asset, the Group runs an annual staff awards scheme, celebrating the core values that embody the organisation and rewarding employees for *service excellence, effective teamwork, service to the community* and innovation.

International Financial Reporting Standards
The European Union issued a regulation in 2002 requiring all listed companies to adopt International Financial Reporting Standards in their consolidated accounts by 2005. The Group is a first time adopter for the year ended 31 December 2005. Further narrative disclosure is included in notes 1 and 34 to the accounts on pages 17 and 48.

Payment of suppliers
The company aims to pay suppliers in accordance with the suppliers' contract terms. The company had an average of 44 days' purchases *(2004: 44 days' purchases)* outstanding in trade creditors.

Charitable and political donations
During the year charitable donations amounted to £0.4m (2004: £0.3m). No political contributions were made.

Financial instruments
The Group's financial instruments primarily comprise bonds, unsecured loan notes, finance leases and overdrafts. The principal purpose of these is to raise funds for the Group's operations. In addition, various other financial instruments such as trade creditors and trade debtors arise directly from its operations. From time to time, the Group also enters into derivative transactions, primarily interest rate swaps and currency swaps, the purpose of which is to manage interest risk and currency risk.

The main financial risks to which the Group has exposure are interest rate risk, liquidity risk and foreign currency risk. The Group borrows in desired currencies at fixed and floating rates of interest and makes use of interest rate swaps to generate the desired interest profile and to manage its exposure to interest rate fluctuations. In respect of liquidity risk, the Group aims to maintain a balance between continuity of funding and flexibility through the use of bonds, unsecured loan notes, finance leases and overdrafts. The Group faces a small exposure to foreign currency risk as it has only limited investments in overseas operations (in the Republic of Ireland, India, Malaysia, Dubai, Korea and the Philippines) which are *affected by foreign exchange movements. Consequently, as the Group is* not exposed to significant foreign currency risk and does not intend to significantly increase its overseas operations, it currently does not hedge this exposure.

Qualifying third party indemnity provisions for the benefit of Directors
Under the Companies (Audit, Investigations and Community Enterprise) Act 2004 (which amends the Companies Act 1985), companies are under an obligation to disclose any indemnities which are in force in favour of their directors. The current Articles of Association of the company contain *an indemnity in favour of the Directors of the company which indemnifies* them in respect of certain liabilities and costs that they might incur in the execution of their duties as Directors. Copies of the relevant extract from the Articles of Association are available for inspection at the registered office of the company during normal business hours on any weekday and will be available at the venue of the AGM from 15 minutes before the meeting until it ends.

Auditors
In accordance with section 384 of the Companies Act 1985, a resolution to *re-appoint Ernst & Young LLP as the external auditors will be put to the* forthcoming Annual General Meeting.

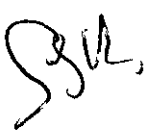
The company is committed to ensuring appropriate independence in its relationship with external auditors and the key safeguards are:

- the Group Risk Manager monitors the independence of the auditor as part of the Group's assessment of auditor effectiveness and reports to the Audit Committee
- the Audit Committee routinely benchmarks the level of the external audit *fee against other comparable companies both within and without its* sector, to ensure ongoing objectivity in the audit process
- the Group Finance Director monitors the level and nature of non-audit fees accruing to the external auditor, and specific assignments are discussed in advance with the external auditor and flagged for the approval by the Audit Committee as appropriate. The Audit Committee reviews, in aggregate, non-audit fees of this nature on an annual basis and considers implications for the objectivity and independence of the relationship with the external auditor.

Ensuring conflicts of interest are avoided is a fundamental criterion in the selection of any third party auditor for assignments with which the Group is involved. Such conflicts may arise across public or private sector customers and key supplier relationships, for example, and are a key determinant in the award process for external audit assignments.

By order of the Board

Gordon Hurst
Company Secretary
22 February 2006



Corporate governance

The Group is committed to high standards of corporate governance, for which the Group Board is accountable.

Further explanation of how the Combined Code on Corporate Governance has been applied is set out below and, in connection with Directors' remuneration, in the Directors' remuneration report. The Group has complied throughout the year with the provisions of the Combined Code.

Board responsibilities and effectiveness

The Group Board is collectively responsible to shareholders for setting the direction of the business and monitoring the Group's ongoing affairs. It is also responsible for ensuring an effective internal control environment that identifies and manages appropriately the risks associated with the business.

The Group Board demonstrates its commitment to the strategic direction and control of the Group by scheduling a series of meetings in the year. It can meet as necessary outside of this schedule to consider any urgent matters that may arise. It sets the strategic objectives of the Group, ensuring sufficient financial and human resources are in place to meet those aims. The Group Board sets the Group's values and standards and ensures that its obligations to customers, employees, the community, and other key stakeholders are understood and met. The Group Board has a formal schedule of matters specifically reserved to it for decision including the Group's business strategy, annual budget, annual and interim financial results, dividends and major corporate activities. The Group Board also considers regular reports from the Executive Chairman, Chief Executive, Group Finance Director and Group Operations Director. The Group Board is provided with complete, timely and relevant information to ensure that informed judgments are made in pursuit of the Group's objectives.

It also reviews the performance of management in meeting business objectives, plans the succession of key executives, and determines appropriate remuneration levels through the Remuneration Committee, a committee of the Group Board. The operational management of the Group is delegated to the Executive Management Board which meets monthly.

The Non-Executive Directors have a particular responsibility to challenge constructively and independently the business development plans that are proposed by executive management and monitor the performance of the management teams in the delivery of agreed business objectives and targets. The Executive Chairman encourages and engages in an open dialogue with Non-Executive Directors in particular, who are at liberty to meet with him as a group or individually as they feel fit, without the presence of Executive Directors.

A new Non-Executive Director, Martina King was appointed to the Group Board with effect from 1 January 2005. Robert Alcock retired from the Group Board on 24 February 2005.

Directors' and officers' liability insurance is maintained.

Board composition

The Directors acknowledge the need to segregate the responsibility for operating the Group Board from the management of the underlying business. Consequently, the roles of Executive Chairman (Rod Aldridge) and Chief Executive (Paul Pindar) are separated. The Group Board additionally comprised, throughout 2005, two further Executive Directors, and three Non-Executive Directors. Peter Cawdron is the Senior Independent Non-Executive Director and is available, as necessary, to lead meetings of the Non-Executive Directors without the Executive Directors and/or the Chairman being present and meet with shareholders to understand their concerns.

During 2005 the Group Board met nine times, excluding ad hoc meetings solely to deal with procedural matters, at which all Directors were present, except for apologies from Eric Walters on two occasions, Rod Aldridge on two occasions and Paul Pindar and Paddy Doyle on one occasion each. Any Director's non-attendance at Board Meetings or meetings of the Audit, Remuneration or Nomination Committees was due to illness or an absence previously agreed with the Chairman of the Board, the Chief Executive or the Chairman of the relevant committee.

Board balance and independence

The executive element of the Board is balanced by a strong independent group of Non-Executive Directors, such that no individual or small group of individuals can dominate the Board's decision making. The Group's Non-Executive Directors, Peter Cawdron, Eric Walters and Martina King are regarded as independent and free from any business or other relationship that could materially interfere with their judgment.

Director induction and professional development

Martina King received a comprehensive induction programme on joining the Board involving appropriate documentation, meetings and visits to Capita businesses with other Directors, attendance at Divisional Board meetings and discussions with advisers and senior management from across the Group.

All Group Board members have access to independent advice on any matters relating to their responsibilities as Directors and as members of the various Committees of the Group Board, at the Group's expense. The Company Secretary is available to all Directors and he is responsible for ensuring that all Group Board procedures are complied with.

During the year, the Directors received appropriate ongoing briefings and information, including updates on governance and regulatory issues, to enable them to perform their roles. They also attended external courses where appropriate.

Board performance evaluation

At the January 2006 Board meeting, the Group Board reviewed the report from the first board performance evaluation process carried out last year and updated the action plan in order to address any further outstanding suggestions for improvements. The various Committees repeated the self-assessment exercise carried out last year in order to assess whether their terms of reference had been satisfactorily fulfilled and how their processes and methods could be improved. The performance of individual Executive Directors is appraised annually by the Chief Executive, to whom they report. The performance of the Chairman is reviewed by the Non-Executive Directors, led by Peter Cawdron, taking into account the views of the Executive Directors. The performance review of the Chief Executive is conducted by the Chairman, taking into account the views of other Directors. Non-Executive Directors' performance is reviewed by the Chairman, taking into account the views of other Directors.

Re-appointment
All Directors are subject to election at the first Annual General Meeting after their appointment and to re-election at intervals of no more than three years in accordance with the Combined Code.

The Executive Chairman has, following the evaluation process described above, considered the performance of Gordon Hurst and Eric Walters who are subject to re-election at the 2006 Annual General Meeting and is satisfied that they continue to be effective and demonstrate a clear commitment to the role. A particularly rigorous review, taking into account the need for progressive refreshing of the Board, was carried out in respect of Eric Walters who will have served a 6 year term in October 2006.

Nomination Committee
The Nomination Committee comprised Peter Cawdron (Chairman), Eric Walters and Martina King throughout the year. Robert Alcock was a member until his retirement on 24 February 2005. The Committee reports to the Group Board and its duty is to seek suitably skilled and experienced candidates to be Non-Executive Directors and ensures plans are in place for orderly succession for appointments to the Board. The terms of reference of the Nomination Committee are displayed in the 'investor centre' at www.capita.co.uk.

The Committee met once during the year and all members were in attendance.

During 2004, the Committee instructed external search consultants to provide advice and support in relation to the appointment of an appropriate Non-Executive Director to fill the vacancy created on the retirement of Robert Alcock. A detailed role specification was drawn up, informed by the Executive Chairman's and the Committee's assessment of the mix of skills, knowledge and experience of the continuing Directors and the requirements of the Board. Interviews were conducted with a range of potential candidates by the external search consultants, members of the Committee and other Directors. As a result of this process, the Committee recommended to the Board, and the Board agreed, that Martina King be appointed to the Board as a Non-Executive Director with effect from January 2005. The anticipated time commitment for her role has been discussed and agreed and she has confirmed that she can and will make sufficient time available to carry out her responsibilities.

Remuneration Committee
Details of the Remuneration Committee and its activities are given in the Directors' remuneration report on page 6. Its terms of reference are displayed in the 'investor centre' section at www.capita.co.uk.

Audit Committee
The Audit Committee comprised the Non-Executive Directors throughout the year and was chaired by Robert Alcock until he retired on 24 February 2005 when Peter Cawdron assumed the chairmanship. Mr Cawdron has significant and recent relevant financial experience. Audit Committee meetings are also attended, by invitation, by the Executive Chairman, Chief Executive, Group Finance Director, Head of Risk Management and by representatives of the external auditors. The Audit Committee met 3 times during the year and all members attended all meetings. It is intended that the Committee will meet 4 times per annum in future. The Committee has written terms of reference that outline its authority and duties. These are displayed in the 'investor centre' section at www.capita.co.uk. The terms of reference were updated and approved by the Group Board at its meeting in November 2005.

At their meetings the Committee reviewed a wide range of financial reporting and related matters including the half-year and annual accounts prior to their submission to the Group Board. The Committee focused in particular on critical accounting policies and practices adopted by the Group and any significant areas of judgment that materially impact reported results. It also monitored the internal controls that are operated by management to ensure the integrity of information reported to shareholders. The Committee provides a forum for reporting by the Group's external auditors, and it advised the Group Board on the appointment, independence and objectivity of the external auditors and on their remuneration both for statutory audit and non-audit work. It also discussed the nature, scope and timing of the statutory audit with the external auditors. The Audit Committee annually performs an independent assessment of the suitability and performance of the external auditors in making its recommendation to the Group Board for their re-appointment.

The Committee reviewed the appropriateness of the annual internal audit programme for the Group, to ensure that the business risk management and internal audit functions are adequately sponsored and resourced. It also monitors the resourcing levels and performance of the Group's FSA compliance function.

At the meeting to review the 2005 Annual Report & Accounts, the Committee considered the level of non-audit services being provided by the Group's external auditors in order to satisfy itself that the objectivity and independence of the external auditors is safeguarded. An updated policy for use of the auditors for non-audit services was approved at this meeting. Details of audit and non-audit fees are given in note 6 on page 25.

The lead audit partner is rotated on a 5 year basis and consequently a new lead partner will take over following the publication of this Annual Report.

Dialogue with institutional shareholders
The Group Board encourages and seeks to build up a mutual understanding of objectives between the Group and its institutional shareholders. As part of this process, the Executive Chairman, Chief Executive, Group Finance Director and Group Operations Director make regular presentations to institutional shareholders and meet with shareholders to discuss any issues of concern and to obtain feedback. Members of the Group Board have met with institutional shareholders during the year to consider Corporate Governance issues. All the Non-Executive Directors are available to meet with shareholders to understand their views more fully. The Executive Chairman is personally available to the significant shareholders in the Group to address any concerns and discuss any issues.

The Corporate Communications team has effective day-to-day responsibility for managing communications with institutional shareholders and private shareholders and always acts in close consultation with the Board. Each year shareholders receive the Annual Report & Accounts. During the year the shareholders can receive up-to-date information through the 'investor centre section' of the company's website. This provides share price information, RNS Announcements, copies of presentations to analysts and answers to frequently asked questions. A telephone helpline is available on 0870 162 3100 which provides a contact point directly to the Group's registrars.

All members of the Group Board, including Non-Executive Directors, receive a report on any significant discussions with shareholders and the feedback that follows the half yearly presentations to investment analysts and shareholders is also circulated. All brokers' reports and analysts' briefings are circulated to Directors.

The Group Board encourages shareholders to attend its Annual General Meeting. Directors, including the chairmen of the various committees, are present to answer any questions from shareholders. The Group uses the Annual General Meeting to communicate with private investors and encourages their participation.

Internal control
The Group Board is responsible for the Group's system of internal control and for regularly reviewing its effectiveness. Procedures have been designed for, inter alia, the safeguarding of assets against unauthorised use or disposition, maintaining proper accounting records and the reliability of financial information used within the business or for publication. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material errors, losses or fraud.

There is an ongoing process of identifying, evaluating and managing the significant risks faced by the Group, which has been in place throughout the year under review and up to the date of approval of the Annual Report & Accounts. This process is regularly reviewed by the Group Board.

The Group's key internal control procedures include the following:

- the Executive Management Board has responsibility to set, communicate and monitor the application of policies, procedures and standards in areas including operations; finance; legal, commercial and regulatory compliance; human resources and health and safety; information security and property management and corporate social responsibility and the environment
- authority to operate the individual businesses comprising the Divisions that make up the Group is delegated to their respective Managing Directors within limits set by the Executive Management Board under powers delegated by the Group Board. The appointment of executives to the most senior positions within the Group, other than Group Board appointments, requires the approval of the Executive Management Board. It establishes key operational, functional and financial reporting standards for application across the whole Group. These are supplemented by operating standards set by local management teams, as required for the type of business and geographical location of each subsidiary and business unit
- comprehensive annual financial plans are prepared at the individual business unit level and summarised at the Divisional and Group level. Financial plans are reviewed and approved by both the Executive Management Board and the Group Board. Capital expenditure is subject to rigorous budgetary control beyond specified levels and detailed written proposals have to be submitted to the Group Board. Expenditure on acquisitions is the subject of appropriate consideration, review and approval by the Group Board
- results are monitored routinely by means of comprehensive management accounts and actual progress against plan is challenged directly by executive members of the Group Board on a Group-wide basis at the business unit level each month
- a framework is in place to identify, assess and mitigate the major business risks, including credit, liquidity, operations, reputation, regulatory and fraud. The framework also includes specific provision for risk-based due diligence in respect of business acquisitions and new customer contracts. Exposure to business risks is monitored as an integral part of the monthly challenge to business results discussed above, and by the Group Audit Committee
- the risk framework is supplemented in certain of the Group's businesses, including all financial services-related business streams, by a number of formally constituted management boards, which in turn are underpinned by dedicated risk committees. These provide an appropriate means to routinely monitor the risk profile of these businesses, including regulatory risks, and for proposed mitigating actions to be challenged and tracked
- the risk management framework is monitored and developed as required by the Group Risk and Business Assurance function, in conjunction with the Group Compliance function, to ensure that it remains appropriate to business requirements and consistent with best practice
- the Group Risk and Business Assurance function reports to the Group Finance Director and independently to the Group Audit Committee. In addition to independently facilitating the Group's risk management framework, it delivers a risk-based internal audit programme, to provide assurance on the effectiveness of the internal control structures operating across the business. The annual audit programme is focused on areas of greatest risk to the Group as determined by the group risk framework, and the independent view of those risks taken by the Group Risk and Business Assurance function
- in addition, regulatory risks and compliance matters are overseen by the Group Compliance function reporting through the Group Operations Director and independently to the Group Audit Committee. The Group Compliance Director and his team, in conjunction with dedicated Compliance teams within the relevant businesses, independently monitor regulatory compliance by way of risk-based work programmes and support operations in identifying and mitigating regulatory risks as an integral part of the Group's risk framework
- both the Group Compliance function and the Group Risk and Business Assurance function routinely apprise the Group's senior management and the Group Audit Committee of their work programmes and findings.

The Group Board keeps under review the effectiveness of this system of internal control. The key mechanisms used by the Group Board to achieve this include regular reports from the Executive Management Board; periodic updates from the Audit Committee based on its review of risk management, business assurance and compliance reports by the relevant Group functions; discussions with and reports from the external auditors and other advisers and periodic reports from relevant Regulators. In addition, the Divisional Executive Directors and Divisional Finance Directors provide annual confirmation that the Divisions' internal controls and systems are designed:

- to provide accurate financial information
- to adequately safeguard, verify and maintain accountability of the Group's assets
- to ensure that provision is made for all amounts known to be irrecoverable at the balance sheet date
- to ensure that accruals are accurately stated and, to the extent that they are known, all potential liabilities have been notified.

At several of its meetings during the year, the Group Board considered the means by which it monitors the effectiveness of internal controls and concluded that it was satisfied with the process and its compliance with the Internal Control Guidance for Directors on the Combined Code issued by the Institute of Chartered Accountants in England and Wales.

Social and environmental responsibility
Details of how we manage our social and environmental responsibilities can be found in the full Annual Report on pages 34 to 37.

Directors' remuneration report

As required by Section 234B of the Companies Act 1985, the Directors present the Report on Directors' Remuneration for the year ended 31 December 2005. In accordance with the requirements the report provides the disclosure in 2 parts: information that is not subject to audit and information that is subject to audit.

Information that is not subject to audit
The Capita Group Remuneration Committee (the Committee) is a sub-committee of the Group Board with terms of reference agreed with the Group Board. The purpose is to determine the terms of employment and the remuneration of the Executive Directors. The terms of reference of the Committee are available on Capita's website and on request.

The Committee was made up during the year of the following independent Non-Executive Directors: Peter Cawdron, Eric Walters and Robert Alcock until his resignation on 24 February 2005. Peter Cawdron was replaced as Chairman by Eric Walters during the year. Martina King was appointed a member of the Committee with effect from 1 January 2005. The Committee met twice during the year and all members attended each meeting.

The Committee consults the Executive Chairman about proposals for remuneration of the Executive Directors and other senior executives, except when issues relating to his own remuneration are discussed. In 2004, KPMG LLP (UK) (KPMG) was appointed as advisers by the Committee to provide independent advice on executive remuneration and the structure of share schemes, and they acted in this capacity throughout 2005.

KPMG has provided tax advisory services to subsidiaries of the company during the year under review. No other person or entity has provided material assistance to the Committee during the year.

The company has complied with the provisions set out in Section B of the Combined Code as relating to Directors' remuneration annexed to the Listing Rules of the Financial Services Authority.

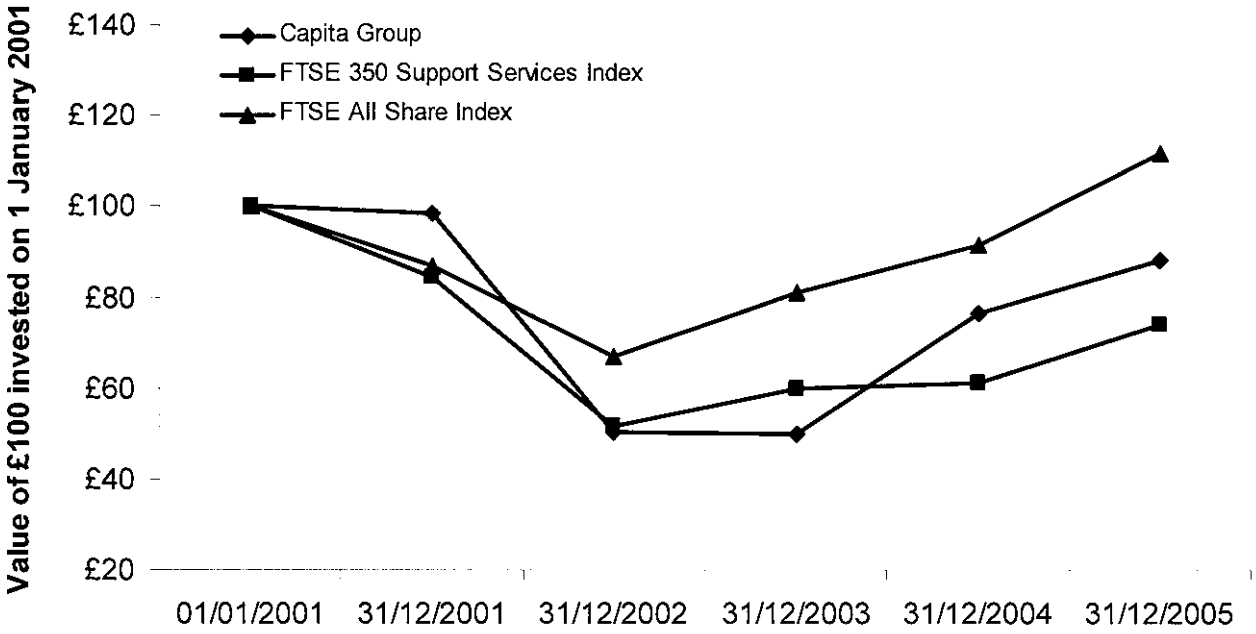
Directors' remuneration
a) Overall policy
The Committee's overall policy is to provide a remuneration structure with a strong performance-related element which it feels is justified by the nature of the Group's activities, its growth and profit record and its developing characteristics.

The overall package is weighted towards share based incentives which the Committee strongly believes links the interests of the Executive Directors with those of shareholders in respect of shareholder value. The Committee is satisfied that the remuneration policy is appropriate, particularly with regard to total executive remuneration and Group performance. The Committee plans to continue to pursue this approach in its future remuneration policy. Consistent with this principle approximately half of an executive's target total remuneration is performance-linked and weighted to the long term. *This percentage would increase in the case of a performance above target.*

The remuneration package for the Executive Directors consists of salary, annual bonus, long term incentives, pension and other benefits.

The chart below compares the value of an investment of £100 in the company's shares with an investment of the same amount in the FTSE All Share Index and the FTSE 350 Support Services Index over the five years starting 1 January 2001 and ending 31 December 2005 assuming that all dividend income is re-invested. The Committee is of the opinion that this comparison provides a clear picture of the performance of the Group relative to both a wide range of companies in the United Kingdom and also a specific group of companies within the same sector.

Comparison of total shareholder returns
Capita vs FTSE All Share Index and FTSE 350 Support Services Index
Value of investment of £100 on 1 January 2001



A £100 investment in Capita shares on 1 January 2001 would be worth £88.28 at 31 December 2005 compared to £111.58 for an investment in the FTSE All Share Index and £73.83 for an investment in the FTSE 350 Support Services Index.

b) Basic salary and benefits

The Committee regularly commissions independent reviews of the salaries and benefits of the Executive Directors. The policy adopted by the Committee requires that salaries and benefits be below those provided to comparable roles to enable the provision of a higher performance-related element.

This low basic salary policy allows the Directors to provide a lead in terms of keeping fixed remuneration costs low across the Group as a whole and is reflective of the Group's remuneration policy in general. The continued success of the Group has enabled it to provide the benefits of a highly geared reward structure which delivers a competitive total remuneration package.

c) Annual Bonus Scheme

The value of the annual bonus is determined at the start of each financial year and payments triggered at a predetermined Group profit before tax target. The Committee takes the view that this performance condition is relevant, challenging and designed to drive business enhancement.

For the 2004 financial year, the maximum annual bonus potential for Executive Directors was 100% of basic salary. In 2004 the Group exceeded its target profit before tax which resulted in annual bonuses being paid out in 2005 at 55% of base salary.

In conjunction with the introduction of the Deferred Annual Bonus Plan (details are shown below), the Committee increased the maximum annual bonus potential for the 2005 financial year to 140% of salary. Half of the annual bonus entitlement will be paid in cash and the remainder will be compulsorily deferred on a gross-basis into Capita shares (Deferred Shares). This reflects the Committee's policy of providing a significant proportion of performance-related remuneration whilst maintaining low basic salaries.

d) Deferred Annual Bonus Plan

The Deferred Annual Bonus Plan (DAB) was approved and adopted at the AGM on 28 April 2005. The DAB will comprise Deferred Shares, which are linked to the Annual Bonus Scheme, and Matching Shares. The Committee believes that this plan will focus participants on delivering strong year-on-year annual performance, which will in turn drive long term shareholder value creation. Executive Directors and Divisional Executive Directors will be eligible to participate in the DAB. The first awards under the DAB will be made in 2006, in respect of the 2005 financial year. No further awards will be made to participants under any other long term incentive plan.

The Deferred Annual Bonus Plan will operate as follows:

The value of Deferred Shares will be determined by the entitlement under the Annual Bonus Scheme: half of the bonus entitlement will be paid in cash and the remainder will be compulsorily deferred on a gross-basis into Deferred Shares. The Deferred Shares will be held for a period of 3 years from the date of award during which they will not be forfeitable, except in the case of dismissal for gross misconduct.

A conditional award of Matching Shares will be made at the same time as the award of Deferred Shares. Participants will be eligible to receive up to 1.5 Matching Shares for every Deferred Share. Matching Shares will vest after the 3 year holding period to the extent to which performance has been met.

The Committee has decided that the performance condition that will apply to the Matching Shares is earnings per share (EPS) growth against the UK Retail Price Index (RPI). 33.3% of the Matching Shares will vest if growth in the company's EPS is equal to RPI growth plus 6% per annum, rising on a straight-line basis to 100% vesting if growth in the company's EPS is equal to or greater than growth in the RPI plus 16% per annum. The Committee believes that long term EPS growth is the most appropriate performance condition for Capita as it is a key indicator of shareholder value creation.

The performance condition attached to the awards made under the bonus scheme may be amended by the Committee from time to time, subject to the new performance condition being no less demanding than the original condition.

e) Long Term Indexed Share Appreciation Scheme (LTISAS)
The scheme was only open to the Executive Directors and the Divisional Executive Directors. Under the LTISAS, participants were provided with 2 equal tranches of 600,000 options. The criteria are the same for each of these issues and therefore both tranches have performance periods that end on 31 December 2006. The exercise price of the options increases in line with the FTSE All Share Index from the date of grant to 25 November 2007. This feature ensures that participants only gain if the share price out-performs such index. The final option price at which the awards can be exercised cannot be below the market value of the share at the date of grant. The options will only be exercisable subject to the growth in the company's EPS over the performance period.

Options will become exercisable if, over the performance period, the growth in the company's EPS exceeds certain targets as follows: 25% of the options shall vest if growth in the company's EPS exceeds RPI growth by 8% per annum, rising on a straight-line basis to 100% vesting if growth in the company's EPS exceeds growth in the RPI by 12% per annum.

The last award under the LTISAS was made in November 2004 and no further awards will be made under this plan.

f) Long Term Incentive Plan (LTIP)
Awards under the LTIP were structured either as Restricted Share Awards or Indexed Performance Share Appreciation Rights.

Restricted share awards
Restricted Share Awards were designed to deliver shares to participants 3 years after the date of award. They would have been released if the company was ranked at or above the median in a comparator group selected from the support services sector. 5% of the awards would have been released at the 49th percentile, 50 percent at the 40th percentile and 100 percent at the 25th percentile or above. If the company's TSR had been below the median at the end of the performance period, the Restricted Share Awards would have lapsed. In addition, no shares would have been released if the growth in the company's EPS had not exceeded the growth in RPI over the 3 year performance period.

Indexed performance share appreciation rights (IPSARs)
Only one award of IPSARs was made to participants under the LTIP and participation was limited to the Executive Directors. Such appreciation rights were designed like share options except that the exercise price to be paid by the participants increased pro rata to the FTSE All Share Index.

IPSARs became exercisable five years after the awards were granted, subject to the company's TSR ranking relative to the comparator group of companies. If the company's TSR had been at the upper quartile level, 40 percent of the IPSARs would have vested. For 100 percent of the awards to have vested the company's TSR had to be at the 10th percentile or better within the comparator group. If the company's TSR ranking had been below the upper quartile, the IPSARs would have lapsed. In addition no IPSARs would have been exercisable if growth in the company's EPS had not exceeded the growth in RPI over the five year performance period.

Restricted Share Awards and awards of IPSARs vested in full in May 2001 and May 2003 respectively. No further awards have been made under the LTIP.

g) Share option schemes
The Group has 2 share option schemes. The 1997 Executive Share Option Scheme is a discretionary scheme for senior managers, in which the Executive Directors and Divisional Executive Directors no longer participate and the Capita Sharesave Scheme which is open to all Capita's employees.

Options granted under the 1997 Scheme currently become exercisable if the growth in the company's EPS exceeds growth in RPI by 8% over the 3 year period from the date of grant. Subject to shareholder approval at the 2006 AGM, the 1997 Scheme, due to expire early in 2007, will be renewed for a period of 10 years until 25 April 2016. Full details of the proposal, including some amendments to the Scheme rules, are given in the explanatory notes in the Notice of AGM.

h) Non-Executive Directors
Non-Executive Directors' fees are reviewed annually and determined by the Executive Directors.

i) Service contracts

The service contracts for Group Board Executive Directors are for an indefinite period and provide for a 1 year notice period. They do not include provisions for pre-determined compensation on termination that exceed 1 year's salary and benefits.

All Directors are appointed for an indefinite period but are subject to re-election at the Annual General Meeting every 3 years.

Details of the contracts are set out below:

Executive Directors	Date of contract	Notice period
Rod Aldridge	11.04.1989	12 Months
Paul Pindar	11.04.1989	12 Months
Paddy Doyle	10.01.1996	12 Months
Gordon Hurst	02.01.1990	12 Months

Non-Executive Directors	Date of appointment	Date of resignation
Peter Cawdron	01.09.1997	–
Eric Walters	31.10.2000	–
Martina King	01.01.2005	–
Robert Alcock	03.11.1993	24.02.2005

Information subject to audit

a) Directors' remuneration

The remuneration of the Directors, excluding Restricted Share Awards and gains made on the exercise of options, is made up as follows:

	2005 £000s	2004 £000s
Basic salaries	**1,063**	1,040
Benefits	**99**	58
Annual bonus	**1,609**	601
Pension contributions to the Group's defined contribution scheme	**154**	150
Fees	**90**	86
Total	**3,015**	1,935

Details of Group Board Directors' remuneration are as follows:

	Salary and fees £	Benefits £	Performance related bonus*** £	Total 2005 £	Total 2004 £	Pension 2005** £	Pension 2004** £
Rod Aldridge	342,150	33,996	479,010	855,156	531,703	16,558	15,601
Paul Pindar	321,300	27,509	449,820	798,629	500,591	15,690	14,751
Paddy Doyle	204,253	20,511	357,210	581,974	346,198	69,789	69,008
Gordon Hurst	195,000	16,696	323,400	535,096	320,223	51,783	50,577
Peter Cawdron*	30,000	–	–	30,000	30,000	–	–
Eric Walters*	30,000	–	–	30,000	30,000	–	–
Martina King*	30,000	–	–	30,000	–	–	–
Robert Alcock*	–	–	–	–	26,000	–	–

*Non-Executive Directors.

**Pension contributions to the Group's defined contribution scheme. In addition, by way of salary sacrifice, the base salaries of Gordon Hurst and Paddy Doyle have been reduced by £36,000 and £50,897 respectively and paid into separate defined contribution schemes.

***The sum disclosed above represents the value of the performance-related bonus and not the cash amount paid out, only 50% will be paid in cash the remainder will be settled through the issue of Deferred Shares as explained in d) on page 7.

The benefits of Paddy Doyle, the highest paid Director (including share exercises in the year), and Gordon Hurst are in respect of car allowance and private health insurance. The benefits of Rod Aldridge and Paul Pindar are in respect of private health insurance and the provision of a company car.

b) Share option schemes

Options were granted under the 1997 Scheme and consist of Inland Revenue Approved and Unapproved share options. Options become exercisable if the growth in the company's EPS exceeds the growth in the RPI by 8% over the 3 year period from the date of grant. Since May 2002, the Directors became ineligible for further awards under this scheme.

The Directors' interests in the 1997 Scheme are listed below:

	Exercise price (£)	At 1 January 2005	Granted in the year	Exercised in the year	At 31 December 2005	Exercisable between*
Rod Aldridge	0.71	**225,000**	–	–	**225,000**	25.02.2002 to 25.02.2007
	4.49	**200,000**	–	–	**200,000**	28.06.2004 to 28.06.2008
	4.36	**100,000**	–	–	**100,000**	22.05.2005 to 22.08.2009
Paul Pindar	0.71	**225,000**	–	–	**225,000**	25.02.2002 to 25.02.2007
	4.49	**200,000**	–	–	**200,000**	28.06.2004 to 28.06.2008
	4.36	**100,000**	–	–	**100,000**	22.05.2005 to 22.08.2009
Paddy Doyle	4.49	**200,000**	–	–	**200,000**	28.06.2004 to 28.06.2008
	4.36	**100,000**	–	–	**100,000**	22.05.2005 to 22.08.2009
Gordon Hurst	4.49	**200,000**	–	–	**200,000**	28.06.2004 to 28.06.2008
	4.36	**100,000**	–	–	**100,000**	22.05.2005 to 22.08.2009

*subject to performance

In 2005 the aggregate gain on the exercise of share options by Directors was £nil (2004: £2,753,000).

The market value of one of the company's shares at 31 December 2005 was 416.75p, and the high and low values for the year were 421.00p and 345.25p respectively.

Interests in Capita Sharesave Scheme

	Exercise price (£)	At 1 January 2005	Granted in the year	Exercised in the year	At 31 December 2005	Exercisable between
Paddy Doyle	1.88	**4,906**	–	–	**4,906**	31.10.2006 to 30.04.2007
Paul Pindar	1.88	**4,906**	–	–	**4,906**	31.10.2006 to 30.04.2007
Gordon Hurst	1.88	**8,430**	–	–	**8,430**	31.10.2008 to 30.04.2009
Eric Walters*	3.90	**4,326**	–	–	**4,326**	31.10.2006 to 30.04.2007
Robert Alcock*	1.88	**4,906**	–	–	**4,906**	31.10.2006 to 30.04.2007

* Non-Executive Directors

The exercise prices quoted above are set at 80% of the market price at the date of grant. The options are exercisable in the period given above after having completed a 3 or 5 year savings period. There are no performance criteria to be satisfied under this scheme.

c) Shares awarded under the Long Term Indexed Share Appreciation Scheme

	At 1 January 2005	Date of award	Price at date of grant (£)	Option granted	At 31 December 2005	Exercisable between
Rod Aldridge	600,000	25.11.2002	2.16	–	**600,000**	25.11.2007 to 25.11.2012
	600,000	25.11.2004	3.51	–	**600,000**	25.11.2007 to 25.11.2012
Paul Pindar	600,000	25.11.2002	2.16	–	**600,000**	25.11.2007 to 25.11.2012
	600,000	25.11.2004	3.51	–	**600,000**	25.11.2007 to 25.11.2012
Paddy Doyle	600,000	25.11.2002	2.16	–	**600,000**	25.11.2007 to 25.11.2012
	600,000	25.11.2004	3.51	–	**600,000**	25.11.2007 to 25.11.2012
Gordon Hurst	600,000	25.11.2002	2.16	–	**600,000**	25.11.2007 to 25.11.2012
	600,000	25.11.2004	3.51	–	**600,000**	25.11.2007 to 25.11.2012

The grant price for each tranche was calculated based on the average of the closing share price over the month prior to the date of grant. The exercise price of the options increases in line with the FTSE All Share Index, measured from the date of grant to 25 November 2007.

Options will become exercisable, if over the performance period, the growth in the company's EPS exceeds certain targets as follows: 25% of the options shall vest if growth in the company's EPS exceeds RPI growth by 8% per annum, rising on a straight-line basis to 100% vesting if growth in the company's EPS exceeds growth in the RPI by 12% per annum.

At 31 December 2005 the market price of a Capita share was 416.75p and the FTSE All Share Index stood at 2847 (25 November 2002 – 1980 and 25 November 2004 – 2367).

d) Shares awarded under the Long Term Investment Plan

Restricted Share Awards

Restricted Share Awards were designed to deliver shares to participants 3 years after the date of award subject to the company's TSR ranking relative to a comparator group of companies and the growth in the company's EPS exceeding the growth in RPI over the 3 year performance period, as discussed on page 8.

The performance requirements were met in full on 4 May 2001.

Rod Aldridge has not exercised his right of transfer in respect of these shares and therefore has an entitlement to 279,069 shares. Had he exercised his right to transfer on the 5 May 2001 when the shares vested, the share price would have been 509p and the gain would have been £1,420,461.

IPSARs

	Number of shares at 1 January 2005	Vesting date	Exercised in year	Number of shares at 31 December 2005	Latest exercise date
Rod Aldridge	1,200,000	05.05.2003	–	1,200,000	05.05.2008
Paul Pindar	1,200,000	05.05.2003	–	1,200,000	05.05.2008
Paddy Doyle	300,000	05.05.2003	300,000	–	05.05.2008
Gordon Hurst	300,000	05.05.2003	300,000	–	05.05.2008

IPSARs became exercisable 5 years after the awards were granted, subject to the company's TSR ranking relative to a comparator group of companies and the growth in the company's EPS exceeding the growth in RPI over the 5 year performance period. The performance requirements in respect of the IPSARs were met in full on 4 May 2003 and the IPSARs are exercisable at a price of 169p per share.

Paddy Doyle and Gordon Hurst exercised the IPSARs, as shown above, on 28 February 2005 when the market price was 381.2p. The aggregate gain on the exercise of IPSARs during the year was £1,267,510 (2004: £1,085,000).

e) Pensions

Pension contributions are made into the Group's defined contribution scheme. The company makes contributions at a rate of 5% of basic salary. Gordon Hurst and Paddy Doyle made additional contributions, by way of salary sacrifice in the year, to a separate executive defined contribution scheme.

f) Compensation for past directors

No compensation has been paid to former directors of the Group.

The report has been approved by the Group Board and has been signed on behalf of the Board by:

Rodney M Aldridge OBE
Executive Chairman
22 February 2006

Eric Walters
Chairman Remuneration Committee
22 February 2006

Consolidated income statement

Consolidated income statement
for the year ended 31 December 2005

	Notes	2005 Before impairment, amortisation and share based payment £m	2005 Impairment, amortisation and share based payment £m	2005 Total £m	2004 Before impairment, amortisation and share based payment £m	2004 Discontinued operations impairment, amortisation and share based payment £m	2004 Total £m
Continuing operations:							
Revenue	3	**1,435.5**	–	**1,435.5**	1,282.2	–	1,282.2
Cost of sales		**1,054.6**	–	**1,054.6**	955.6	–	955.6
Gross profit		**380.9**	–	**380.9**	326.6	–	326.6
Administrative expenses	4	**190.2**	24.1	**214.3**	166.1	6.5	172.6
Operating profit	6	190.7	(24.1)	**166.6**	160.5	(6.5)	154.0
Finance revenue	8	**0.4**	–	**0.4**	0.2	–	0.2
Finance costs	9	**(13.9)**	–	**(13.9)**	(12.1)	–	(12.1)
Profit before tax		177.2	(24.1)	**153.1**	148.6	(6.5)	142.1
Income tax expense	10	**(49.1)**	3.3	**(45.8)**	(41.8)	2.4	(39.4)
Profit for the year from continuing operations		128.1	(20.8)	**107.3**	106.8	(4.1)	102.7
Discontinued operations:							
Loss on discontinued operations	11	–	–	–	–	(2.2)	(2.2)
Profit for the year		128.1	(20.8)	**107.3**	106.8	(6.3)	100.5
Attributable to:							
Equity holders of the parent		**128.3**	(20.8)	**107.5**	107.0	(6.3)	100.7
Minority interest		**(0.2)**	–	**(0.2)**	(0.2)	–	(0.2)
		128.1	(20.8)	**107.3**	106.8	(6.3)	100.5
Earnings per share	12						
– basic		**19.44p**	**(3.16)p**	**16.28p**	16.08p	(0.95)p	15.13p
– diluted		**19.16p**	**(3.11)p**	**16.05p**	15.94p	(0.94)p	15.00p
– basic (excluding discontinued operations)		**19.44p**	**(3.16)p**	**16.28p**	16.08p	(0.62)p	15.46p
– diluted (excluding discontinued operations)		**19.16p**	**(3.11)p**	**16.05p**	15.94p	(0.61)p	15.33p

Consolidated statement of recognised income and expense

Consolidated statement of recognised income and expense
for the year ended 31 December 2005

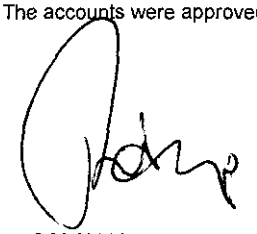
	2005 £m	2004 £m
Actuarial loss on defined benefit pension schemes	(3.7)	(19.7)
Exchange differences on translation of foreign operations	0.2	0.1
Tax on items taken directly to equity	3.7	8.3
Net income/(expense) recognised directly in equity	0.2	(11.3)
Profit for the year	107.3	100.5
Total income and expense for the period	107.5	89.2
Attributable to:		
Equity holders of the parent	107.7	89.4
Minority interest	(0.2)	(0.2)
	107.5	89.2
Effects of changes in accounting policy:		
Net gain on interest rate swap on first time adoption of IAS 39	1.4	
Net loss on currency swap on first time adoption of IAS 39	(3.1)	
Net gain on bonds on first time adoption of IAS 39	1.7	
	–	

Consolidated balance sheet

Consolidated balance sheet
at 31 December 2005

	Notes	2005 £m	2004 £m
Non-current assets			
Property, plant and equipment	14	**150.1**	129.1
Intangible assets	15	**588.7**	500.2
Financial assets	17	**13.8**	0.2
Trade and other receivables	19	**5.8**	6.1
Deferred taxation	10	**25.1**	32.6
		783.5	668.2
Current assets			
Trade and other receivables	19	**343.8**	260.3
Total assets		**1,127.3**	928.5
Current liabilities			
Trade and other payables	20	**378.0**	308.9
Financial liabilities	22	**49.9**	33.0
Provisions	24	**1.3**	2.1
Income tax payable		**32.5**	28.4
		461.7	372.4
Non-current liabilities			
Trade and other payables	20	**1.3**	3.1
Financial liabilities	22	**221.7**	145.2
Provisions	24	**2.0**	3.4
Employee benefits	32	**43.0**	44.1
		268.0	195.8
Total liabilities		**729.7**	568.2
Net assets		**397.6**	360.3
Capital and reserves			
Issued capital	26	**13.4**	13.4
Share premium	28	**258.1**	248.1
Treasury shares	26	**(0.4)**	(0.2)
Capital redemption reserve	28	**0.2**	0.1
Foreign currency translation	28	**0.3**	0.1
Retained earnings	28	**125.8**	98.4
Equity shareholders' funds		**397.4**	359.9
Minority interest	28	**0.2**	0.4
Total equity		**397.6**	360.3

The accounts were approved by the Group Board on 22 February 2006 and signed on its behalf by:



R M Aldridge

G M Hurst

Consolidated cash flow statement

Consolidated cash flow statement
for the year ended 31 December 2005

	Notes	2005 £m	2004 £m
Cash flows from operating activities			
Operating profit on continuing activities before interest and taxation		166.6	154.0
Operating loss on discontinued activities		–	(0.3)
Depreciation	14	31.7	27.9
Amortisation of other intangible assets (treated as depreciation)	15	4.9	2.9
Amortisation of intangible assets created on acquisition	15	4.5	1.8
Impairment of goodwill	16	12.0	–
Loss on sale of available-for-sale financial assets		–	0.1
Share based payment expense	27	7.6	4.7
Pension charge	32	12.0	13.1
Pension contributions	32	(16.6)	(16.5)
Loss on sale of property, plant and equipment		0.5	–
Movement in provisions		(2.4)	0.7
Increase in debtors		(19.4)	(12.5)
Increase in creditors		30.8	24.1
Cash generated from operations		232.2	200.0
Exceptional additional pension contribution		–	(50.0)
Income tax paid		(38.2)	(36.0)
Interest paid		(13.9)	(11.9)
Interest received		0.4	0.2
Net cash generated from operating activities		180.5	102.3
Net cash used in investing activities			
Purchase of property, plant and equipment	14	(49.7)	(46.2)
Proceeds from sale of property, plant and equipment		0.4	3.3
Purchase of intangible fixed assets	15	(4.0)	(8.0)
Acquisition of subsidiary undertakings and businesses		(101.9)	(56.4)
Cash acquired with subsidiary undertakings		2.7	3.8
Proceeds on disposal of subsidiary undertakings	11	–	3.1
Purchase of trade investments in insurance captives	17	(12.0)	–
Proceeds on sale of available-for-sale financial assets		–	4.9
		(164.5)	(95.5)
Net cash used in financing activities			
Issue of ordinary share capital	26	9.9	5.5
Share buybacks	26	(49.6)	(27.5)
Share transaction costs	26	(0.3)	(0.2)
Dividends	13	(38.0)	(29.6)
Capital element of finance lease rental payments	29	(0.2)	(0.3)
Asset based securitised financing		1.4	–
Repayment of loans notes and long term loans	29	(7.3)	(11.5)
Proceeds on issue of bond		75.0	–
Bond issue costs		(0.1)	–
		(9.2)	(63.6)
Net decrease in cash and cash equivalents		6.8	(56.8)
Cash and cash equivalents at the beginning of the period		(26.1)	30.7
Cash and cash equivalents at 31 December		(19.3)	(26.1)
Cash and cash equivalents comprise:			
Overdraft	22	(19.3)	(26.1)
Total		(19.3)	(26.1)

Notes to the consolidated financial statements

for the year ended 31 December 2005

1 Corporate information

The consolidated financial statements of The Capita Group Plc for the year ended 31 December 2005 were authorised for issue in accordance with a resolution of the Directors on 22 February 2006. The Capita Group Plc is a public limited company incorporated in England and Wales whose shares are publicly traded.

The principal activities of the Group are listed on page 63.

2 Summary of significant accounting policies

(a) Statement of compliance and first-time adoption of International Financial Reporting Standards

The consolidated financial statements of The Capita Group Plc and all of its subsidiaries (the Group) have been prepared in accordance with International Financial Reporting Standards (IFRS). These consolidated financial statements are the first annual financial statements which the Group has prepared in accordance with IFRS and consequently the Group has complied with IFRS 1 First-time adoption of International Financial Reporting Standards. The parent company continues to apply UK GAAP in the preparation of its individual financial statements and these are contained on pages 55 to 62.

The Group's date of transition to IFRS is 1 January 2004 and comparative information in the financial statements is restated to reflect the Group's adoption of IFRS except where otherwise required or permitted by IFRS 1. IFRS 1 requires an entity to comply with each IFRS effective at the reporting date for its first financial statements prepared under IFRS. As a general rule, IFRS 1 requires such standards to be applied retrospectively. However, the standard allows several optional exemptions from full retrospective application. The Group has elected to take advantage of the following exemptions:

- The Group has adopted IFRS 3 'Business Combinations' to the extent that it applies to acquisitions post 1 January 2004. Acquisitions before that date are recorded as under previous accounting rules as the Group has taken advantage of the exemption allowed in IFRS 1 regarding business combinations recognised before the date of transition to IFRS. All goodwill and intangibles will be tested for impairment, as required by IAS 36 'Impairment of Assets'; goodwill on an annual basis and intangibles when there is an indicator of impairment. In addition, the Group has taken advantage of the exemption allowed in IFRS 1 not to apply IAS 21 'The Effects of Changes in Foreign Exchange Rates' retrospectively to fair value adjustments and goodwill arising in business combinations that occurred before the date of transition to IFRS.
- The Group has also elected to take advantage of the exemption which allows cumulative actuarial gains or losses on defined benefit pension schemes at the date of transition to IFRS to be recognised immediately.
- The Group has elected to take advantage of the exemption allowed in IFRS 1 regarding cumulative translation differences. Accordingly, the cumulative translation differences for all foreign operations are deemed to be nil at the date of transition to IFRS.
- The Group has elected to apply the exemptions in IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' allowing the application of these standards from 1 January 2005 only.
- The Group has elected to take advantage of the exemptions allowed in IFRS 1 regarding IFRS 2 'Share-based payments'. The Group has applied the exemptions for share based payments granted on or before 7 November 2002. This means that only equity instruments granted after 7 November 2002 that vest after the effective date of IFRS 2 on 1 January 2005 needed to be valued.

The reconciliations required by IFRS 1 are set out in note 34. Specifically, these are the reconciliations of the Group's balance sheets, as prepared under UK GAAP, to those prepared in accordance with IFRS as at 1 January 2004 (the opening balance sheet as at the date of transition to IFRS) and 31 December 2004 as well as the reconciliation of the Group's profit and loss account prepared under UK GAAP to that prepared in accordance with IFRS for the year to 31 December 2004.

These financial statements have been prepared in accordance with IFRS as adopted for use in the European Union and as applied in accordance with the provisions of the Companies Act 1985.

(b) Basis of preparation

The consolidated financial statements have been prepared under IFRS where certain financial instruments, separately identifiable intangibles acquired on business combinations and the pension assets and liabilities have been measured at fair value. The carrying value of recognised assets and liabilities that are hedged are adjusted to record changes in the fair values attributable to the risks that are being hedged. The consolidated financial statements are presented in pounds sterling and all values are rounded to the nearest tenth of a million (£m) except when otherwise indicated.

(c) Basis of consolidation

The consolidated financial statements comprise the financial statements of The Capita Group Plc and its subsidiaries as at 31 December each year. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies, but in accordance with UK GAAP. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. Where there is a loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which The Capita Group Plc has control.

(d) Inventories

Inventories are stated at the lower of cost and net realisable value.

Costs are those incurred in bringing inventories to their present location and condition. Costs include any direct materials, where applicable, and labour together with a proportion of operating overheads based on normal operating capacity but excluding borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

For service contracts see accounting policy on page 18.

2 Summary of significant accounting policies (continued)

(e) Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Other than in respect of service contracts, described below, revenue represents fee income recognised in respect of services provided during the period (stated net of value added tax).

Revenue is earned within the United Kingdom, Europe, Dubai, India and South-east Asia.

(f) Service contracts

(i) **Brownfield outsourcing contracts** – Brownfield contracts are where there is a transfer of an existing operation to the Group. For brownfield contracts all costs incurred prior to service commencement are expensed as incurred and revenue represents fee income in respect of services provided.

(ii) **Greenfield outsourcing contracts** – A greenfield contract is one in which an entirely new service is being established for a customer. For these contracts no profit is recognised until service delivery commences and is being invoiced. Upon commencement, revenue represents fees invoiced in respect of services provided. Direct incremental costs incurred on the contract prior to service commencement and reimbursable during the contract, excluding any overheads, are included in debtors and amortised over the life of the contract. On some contracts, non-refundable payments are received, prior to full service commencement, on the achievement of agreed contract delivery milestones. These are recognised as revenue when earned.

(iii) **Property consultancy contracts** – Revenue represents the sales value of work done in the year, including fees invoiced and estimates in respect of amounts to be invoiced after the year-end. Profits are recognised on long term contracts where the final outcome can be assessed with reasonable certainty. In calculating this the percentage of completion method is used based on the proportion of costs incurred to the total estimated cost. Cost includes direct staff costs and outlays. Full provision is made for all known or anticipated losses on each contract immediately such losses are forecast.

Gross amounts due from customers are stated at the proportion of the anticipated net sales value earned to date less amounts billed on account. To the extent that fees paid on account exceed the value of work performed, they are included in creditors as gross amounts due to customers.

(g) Foreign currency translation

The functional and presentation currency of The Capita Group Plc and its United Kingdom subsidiaries is the pound sterling (£). Transactions in foreign currencies are initially recorded in the functional currency by applying the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement. with the exception of differences on foreign currency borrowings that provide a hedge against a net investment in a foreign operation. These are taken directly to equity until the disposal of the net investment, at which time they are recognised in the consolidated income statement.

Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction. Non-monetary items measured at fair value in a foreign currency shall be translated using the exchange rates at the date when the fair value was determined.

The functional currencies of overseas operations include the euro, Indian rupee, Malaysian ringgit, South Korean won and the Philippine peso. As at the reporting date, the assets and liabilities of the overseas operations are retranslated into the presentation currency of The Capita Group Plc at the rate of exchange ruling at the balance sheet date and its income statement is translated at the weighted average exchange rate for the year. The exchange differences arising on the retranslation are taken directly to a separate component of equity. On disposal of a foreign operation, the deferred cumulative amount recognised in equity relating to that particular foreign operation shall be recognised in the income statement.

The Group has elected not to record cumulative translation differences arising prior to the transition date as permitted by IFRS 1. In utilising this exemption, all cumulative translation differences are deemed to be zero as at 1 January 2004 and all subsequent disposals shall exclude any translation differences arising prior to the date of transition.

(h) Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

Freehold buildings and long leasehold property	– over 50 years
Leasehold improvements	– period of the lease
Plant and equipment	– 3-10 years

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognised in the income statement in the administrative expenses line item.

An item of property, plant and equipment is de-recognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year in which the item is de-recognised.

(i) Borrowing costs

Borrowing costs are currently recognised as an expense when incurred in accordance with the benchmark accounting treatment under IAS 23.

2 Summary of significant accounting policies (continued)

(j) Goodwill

Goodwill recognised under UK GAAP prior to the date of transition to IFRS is stated at net book value as at this date. This goodwill had been amortised on a straight-line basis, over its useful economic life (ranging from five to 20 years). This was changed on transition to IFRS. Goodwill recognised subsequent to 1 January 2004 is, on acquisition, initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually, or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill arising on acquisitions prior to 31 December 1997 remains set off directly against reserves even if the related investment becomes impaired or the business is disposed of.

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units expected to benefit from the combination's synergies. Impairment is determined by assessing the recoverable amount of the cash-generating unit, to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in these circumstances is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

(k) Intangible assets

Intangible assets acquired separately are capitalised at cost and those identified in a business acquisition are capitalised at fair value as at the date of acquisition. Following initial recognition, the carrying amount of an intangible asset is its cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. There are no indefinite-lived assets in 2004 or 2005. Amortisation is charged on assets with finite lives, this expense is taken to the income statement through the administrative expenses line item.

There are no intangible assets that have been created within the business and should such expenditure be incurred in the future it will be charged against profits in the year in which the expenditure is incurred.

Intangible assets with finite lives are only tested for impairment, either individually or at the cash-generating unit level, where there is an indicator of impairment. Intangible assets with indefinite lives are tested annually for impairment.

Gains or losses arising from de-recognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is de-recognised.

Intangible assets identified and recognised since transition to IFRS are treated as follows:

- Brands are amortised evenly over their useful economic lives of 5 and 10 years
- Software and licences are amortised over their useful economic lives of 5 years
- Contracts and committed sales are amortised over their useful economic lives of between 1.5 and 10 years
- Customer lists and relationships are amortised over their economic lives of between 4 and 10 years
- Other intangibles are amortised over their useful economic lives of 2.5 years

(l) Recoverable amount of non-current assets

At each reporting date, the Group assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. Recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets.

(m) Investments

All investments are initially recorded at fair value of the consideration given including acquisition charges associated with the investment. Subsequently they are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable. Trade investments are recognised at fair value.

(n) Trade and other receivables

Trade receivables are recognised and carried at original invoice amount less an allowance for any uncollectable amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

(o) Cash and cash equivalents

Cash and short term deposits in the balance sheet comprise cash at bank and in hand and short term deposits with an original maturity of 3 months or less.

For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(p) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at the fair value of the consideration received net of issue costs associated with the borrowing.

After initial recognition loans and borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs and any discount or premium on settlement.

Gains and losses are recognised in the income statement when the liabilities are de-recognised, as well as through the amortisation process.

2 Summary of significant accounting policies (continued)

(q) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when recovery is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost.

(r) Surplus properties

The Group provides, on a discounted basis, for the future rent expense and related cost of leasehold property (net of estimated sub-lease income) where the space is vacant or currently not planned to be used for ongoing operations.

(s) Pre-contract costs

Pre-contract award bidding costs are expensed as incurred.

(t) Pension schemes

The Group maintains a number of contracted-out defined contribution schemes and contributions are charged to the income statement in the year in which the services are rendered. In addition, the Group operates 2 defined benefit pension schemes and participates in 5 other defined benefit schemes, all of which require contributions to be made to separately administered funds. The costs of providing benefits under these schemes are determined separately for each scheme using the projected unit credit actuarial valuation method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of defined benefit obligation) and is based on actuarial advice. Past service costs are recognised in the income statement on a straight-line basis over the vesting period or immediately if the benefits have vested.

When a settlement (eliminating all obligations for benefits already accrued) or a curtailment (reducing future obligations as a result of a material reduction in the scheme membership or a reduction in future entitlement) occurs the obligation and related plan assets are remeasured using current actuarial assumptions and the resultant gain or loss recognised in the income statement during the period in which the settlement or curtailment occurs.

The interest element of the defined benefit cost represents a change in present value of scheme obligations resulting from the passage of time, and is determined by applying the discount rate to the opening present value of the benefit obligation, taking into account material changes in the obligation during the year. The expected return on plan assets is based on an assessment made at the beginning of the year of long term market returns on scheme assets, adjusted for the effect of fair value of plan assets of contributions received and benefits paid during the year.

In respect of 3 of the schemes in which the Group participates, the Group accounts for its legal and constructive obligation over the period of its participation which is for a fixed period only.

Actuarial gains and losses are fully recognised in equity through the statement of recognised income and expense such that the balance sheet reflects the scheme's surplus or liability at the balance sheet date. The employer's portion of current and past service cost is charged to operating profit with the interest cost, net of expected return on assets in the plans, included within administrative expenses.

The defined benefit liability on the balance sheet comprises the total for each scheme, or group of schemes, of the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds), less any past service cost not yet recognised and less the fair value of plan assets out of which the obligations are to be settled directly. Fair value is based on market price information and in the case of quoted securities is the published bid price. The value of a net pension benefit asset is restricted to the sum of any unrecognised past service costs and the present value of any amount the Group expects to recover by way of refunds from the plan or reductions in the future contributions.

(u) Derivative financial instruments

The Group uses derivative financial instruments such as interest rate swaps and foreign currency contracts to hedge risks associated with interest and exchange rate fluctuations. Such derivative financial instruments are stated at fair value. The fair values of interest rate swaps and foreign currency contracts are determined by reference to market rates for similar instruments.

For the purpose of hedge accounting, hedges are classified as either: fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability; or cash flow hedges where they hedge exposure to variability in cash flows that is attributable to either a particular risk associated with a recognised asset or liability or a forecast transaction.

In relation to fair value hedges (e.g. fixed to floating interest rate swaps held as fair value hedges against fixed interest rate borrowings) which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement. The Group does not currently hold any cash flow hedges.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the income statement.

The Group has only applied IAS 32 and IAS 39 from 1 January 2005 as permitted by the transition arrangements in IFRS 1.

(v) Leasing

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Capitalised leased assets are depreciated over the shorter of the estimated life of the asset or the lease term. Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

2 Summary of significant accounting policies (continued)

(w) Income tax

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from the initial recognition of goodwill
- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax assets and unused tax losses can be utilised, except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Income tax relating to items recognised directly in equity are recognised in equity and not in the income statement.

(x) Share-based payments

The Group operates a number of executive and employee share schemes.

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the company (market conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, the number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity.

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period. In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification. No reduction is recognised if this difference is negative.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any cost not yet recognised in the income statement for the award is expensed immediately. Any compensation paid up to the fair value of the award at the cancellation or settlement date deducted from equity, with any excess over the fair value being treated as an expense in the income statement.

The Group has taken advantage of the transitional provisions of IFRS 2 in respect of equity-settled awards and has applied IFRS 2 only to equity-settled awards granted after 7 November 2002 that had not vested before 1 January 2005.

2 Summary of significant accounting policies (continued)

(y) New standards and interpretations not applied

During the year, the IASB and IFRIC have issued the following standards and interpretations with an effective date after the date of these financial statements:

		Effective date
International Accounting Standards (IAS / IFRSs)		
IFRS 1	Amendment relating to IFRS 6	1 January 2006
IFRS 4	Insurance contracts (amendment to IAS 39 and IFRS 4 – Financial Guarantee Contracts)	1 January 2006
IFRS 6	Exploration for and Evaluation of Mineral Assets	1 January 2006
IFRS 6	Amendment relating to IFRS 6	1 January 2006
IFRS 7	Financial Instruments: Disclosures	1 January 2007
IAS 1	Amendment – Presentation of Financial Statements: Capital Disclosures	1 January 2007
IAS 19	Amendment – Actuarial Gains and Losses, Group Plans and Disclosures	1 January 2006
IAS 39	Fair Value Option	1 January 2006
IAS 39	Amendments to IAS 39 – Transition and Initial Recognition of Financial Assets and Financial Liabilities (Day 1 profits)	1 January 2006
IAS 39	Cash Flow Hedge Accounting	1 January 2006
IAS 39	Amendment to IAS 39 and IFRS 4 – Financial Guarantee Contracts	1 January 2006
International Financial Reporting Interpretations Committee (IFRIC)		
IFRIC 4	Determining whether an arrangement contains a lease	1 January 2006
IFRIC 5	Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds	1 January 2006
IFRIC 6	Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment	1 December 2005

The Directors do not anticipate that the adoption of these standards and interpretations will have a material impact on the Group's financial statements in the period of initial application.

Upon adoption of IFRS 7, the Group will have to disclose additional information about its financial instruments, their significance and the nature and extent of risks that they give rise to. More specifically the Group will need to disclose the fair value of its financial instruments and its risk exposure in greater detail. There will be no impact on reported income or net assets.

3 Revenue

Revenue disclosed in the income statement is analysed as follows.

	Notes	2005 £m	2004 £m
Rendering of services		**1,388.2**	1,243.9
Construction contracts	21	**47.3**	38.3
Revenue		**1,435.5**	1,282.2
Finance revenue		**0.4**	0.2
Total revenue		**1,435.9**	1,282.4

No revenue was derived from exchanges of goods or services (2004: £nil).

4 Administrative expenses

Included in the middle column disclosed on the face of the consolidated income statement, against the line item administrative expenses, are the following:

	2005 £m	2004 £m
Share based payment charge	**7.6**	4.7
Intangible amortisation	**4.5**	1.8
Impairment (see note 16)	**12.0**	–
	24.1	6.5

5 Segmental information

The Group's operations are organised and managed separately according to the nature of the services provided, with each segment representing a strategic business unit offering a different package of related services across the Group's markets. A description of the service provision for each segment can be found in the business review in the full Annual Report on pages 22 to 29.

Before eliminating sales between business units on consolidation, the Group accounts for sales between business units as if they were to a third party at market rates. Revenues are attributed to geographic areas based on the location of the assets producing the revenues.

The tables below present revenue, result and certain asset and liability information for the Group's business segments for the years 2005 and 2004. All operations in 2005 are continuing.

Year ended 31 December 2005

Segment revenue	Resourcing services £m	Property services £m	Commercial services £m	Corporate services £m	Integrated services £m	Professional services £m	Total £m
Total segment revenue	187.9	200.7	271.4	245.0	400.8	267.3	1,573.1
Inter-segment revenue	(13.7)	(10.2)	(17.7)	(4.6)	(27.0)	(64.4)	(137.6)
Third party revenue	174.2	190.5	253.7	240.4	373.8	202.9	1,435.5
Segment result							
Result after depreciation	11.4	17.1	25.4	44.8	58.0	34.0	190.7
Share based payment	(0.9)	(1.0)	(1.3)	(1.2)	(1.9)	(1.3)	(7.6)
Intangible amortisation	–	(1.7)	(0.9)	(0.8)	(0.6)	(0.5)	(4.5)
Impairment charge	–	–	–	–	–	(12.0)	(12.0)
	10.5	14.4	23.2	42.8	55.5	20.2	166.6
Finance costs							(13.5)
Profit before tax and minority interests							153.1
Corporation taxation							(45.8)
Minority interests							0.2
Profit after tax and minority interests							107.5
Other segment information							
Assets by segment							
Assets	32.6	58.7	109.7	109.2	144.5	45.0	499.7
Intangible assets	80.9	46.4	206.3	185.2	24.9	45.0	588.7
Assets	113.5	105.1	316.0	294.4	169.4	90.0	1,088.4
Unallocated assets							38.9
Total assets							1,127.3
Liabilities by segment							
Liabilities	17.6	24.9	117.0	73.2	101.7	76.4	410.8
Unallocated liabilities							318.9
Total liabilities							729.7
Total net assets							397.6
Capital expenditure							
Tangible assets	5.1	0.2	5.3	18.0	16.8	4.3	49.7
Depreciation charge	3.3	0.1	3.5	5.4	15.3	4.1	31.7
Intangible assets	–	4.4	43.9	37.5	12.4	11.7	109.9
Intangible amortisation	–	1.7	0.9	0.8	0.6	0.5	4.5

5 Segmental information (continued)

The tables below present revenue by the geographical location of customers, carrying amount of assets and expenditure on tangible and intangible assets by location of those assets.

Revenue	United Kingdom £m	Non-United Kingdom £m	Total £m
Total segment revenue	1,542.3	30.8	1,573.1
Inter-segment revenue	(136.6)	(1.0)	(137.6)
Third party revenue	1,405.7	29.8	1,435.5
Other segment information			
Assets	485.0	14.7	499.7
Intangible assets	574.9	13.8	588.7
Unallocated assets	38.9	–	38.9
Total assets	1,098.8	28.5	1,127.3
Capital expenditure			
Tangible assets	46.3	3.4	49.7
Intangible assets	99.3	10.6	109.9

Year ended 31 December 2004

Revenue	Resourcing services £m	Property services £m	Commercial services £m	Corporate services £m	Integrated services £m	Professional services £m	Continuing operations total £m	Discontinued operations total £m
Total segment revenue	179.4	162.9	261.5	201.5	344.9	247.1	1,397.3	2.9
Inter-segment revenue	(17.3)	–	(20.3)	(11.7)	(6.3)	(59.5)	(115.1)	–
Third party revenue	162.1	162.9	241.2	189.8	338.6	187.6	1,282.2	2.9
Segment result								
Result after depreciation,	6.8	17.2	21.4	35.0	49.4	30.7	160.5	(0.3)
Share based payment	(0.6)	(0.6)	(0.8)	(0.7)	(1.2)	(0.8)	(4.7)	–
Intangible amortisation	–	(1.4)	–	(0.2)	–	(0.2)	(1.8)	–
	6.2	15.2	20.6	34.1	48.2	29.7	154.0	(0.3)
Exceptional item							–	(1.9)
Finance costs							(11.9)	–
Profit before tax and minority interests							142.1	(2.2)
Corporation taxation							(39.4)	–
Minority interests							0.2	–
Profit after tax and minority interests							102.9	(2.2)
Other segment information								
Assets by segment								
Assets	31.0	46.5	58.6	74.3	138.0	47.1	395.5	
Intangible assets	80.9	43.7	168.2	148.5	13.1	45.8	500.2	
Assets	111.9	90.2	226.8	222.8	151.1	92.9	895.7	
Unallocated assets							32.8	
Total assets							928.5	
Liabilities by segment								
Liabilities	7.5	18.4	78.3	72.3	81.3	59.7	317.5	
Unallocated liabilities							250.7	
Total liabilities							568.2	
Total net assets							360.3	
Capital expenditure								
Tangible assets	1.1	3.4	6.0	10.9	19.5	5.3	46.2	
Depreciation charge	1.1	1.8	5.7	4.0	14.1	4.1	30.8	
Intangible assets	–	23.4	17.0	10.9	0.2	2.2	53.7	
Intangible amortisation	–	1.4	–	0.2	–	0.2	1.8	

Unallocated assets include held for sale financial assets and deferred taxation. Unallocated liabilities include overdrafts, corporation taxation, lease obligations, loan notes, currency and interest rate swaps, bonds and the aggregate pension deficit.

5 Segmental information (continued)

The tables below present Revenue by the geographical location of customers, carrying amount of assets and expenditure on tangible and intangible assets by location of those assets.

Revenue	United Kingdom £m	Non-United Kingdom £m	Total £m
Total segment revenue	1,369.1	28.2	1,397.3
Inter-segment revenue	(115.1)	–	(115.1)
Third party revenue	1,254.0	28.2	1,282.2
Other segment information			
Assets	387.4	8.1	395.5
Intangible assets	497.0	3.2	500.2
Unallocated assets	21.6	11.2	32.8
Total assets	906.0	22.5	928.5
Capital expenditure			
Tangible assets	45.2	1.0	46.2
Intangible assets	16.6	1.5	18.1

6 Operating profit

This is stated after charging/(crediting):

	2005 £m	2004 £m
Employee benefits expense (see note 7)	**607.2**	530.5
Amortisation of intangible assets (as shown in amortisation column)	**4.5**	1.8
Depreciation	**31.7**	27.9
Loss on sale of property, plant and equipment	**0.5**	–
Amortisation of other intangible assets (treated as depreciation)**	**4.9**	2.9
Minimum lease payments recognised as an operating lease expense	**59.6**	49.9
Foreign exchange	**(0.1)**	(0.1)
Auditors' remuneration – statutory audit*	**0.8**	0.6
– other UK fees	**0.4**	0.3

*£26,000 (2004: £22,000) of this relates to the parent company.

** Included within operating activities before impairment, amortisation and share based payments.

UK fees paid to the auditors include fees in relation to:	2005 £m	2004 £m
Statutory audit	**0.8**	0.6
Other UK fees:		
Further assurance services	**0.2**	0.1
Taxation advisory services	**0.1**	0.1
Other non-audit services	**0.1**	0.1
	1.2	0.9

There was due diligence work performed in respect of acquisitions which resulted in fees paid to auditors of £0.3m (2004: £0.4m). These amounts have been capitalised as part of the acquisitions to which they relate. In addition £0.7m (2004: £0.9m) was paid to accountancy firms other than the Group's auditor.

7 Employee benefits expense

	2005 £m	2004 £m
Wages and salaries	**527.9**	459.3
Social security costs	**50.3**	44.3
Other pension costs (see note 32)	**21.4**	22.2
Share based payments	**7.6**	4.7
	607.2	530.5

The average number of employees during the year was made up as follows:	2005 Number	2004 Number
Sales	**588**	474
Administration	**1,412**	1,510
Operations	**21,431**	18,720
	23,431	20,704

Details of Directors' remuneration are contained within the Directors' remuneration report on pages 6 to 12.

8 Finance revenue

	2005 £m	2004 £m
Bank interest receivable	**0.4**	0.2
Total finance revenue	**0.4**	0.2

9 Finance costs

	2005 £m	2004 £m
Loan note interest	**0.9**	1.1
Bonds	**8.7**	6.9
Bank loans and overdrafts	**4.1**	3.9
Unwinding of interest on discounted property provision	**0.2**	0.2
Total finance costs	**13.9**	12.1

10 Income tax

The major components of income tax expense for the years ended 31 December 2005 and 2004 are:

Consolidated income statement	2005 £m	2004 £m
Current income tax		
Current income tax charge	43.1	39.2
Adjustment in respect of prior years	(1.0)	(1.7)
Deferred income tax		
Origination and reversal of temporary differences	6.9	4.2
Adjustment in respect of prior years	(3.2)	(2.3)
	45.8	39.4

Consolidated statement of recognised income and expense	£m	£m
Deferred income tax related to items charged/credited directly to equity		
Actuarial losses on defined benefit plans	1.0	5.6
Tax deduction in excess of employee benefits expense charged	2.7	2.7
	3.7	8.3

A reconciliation between tax expense and the product of accounting profit multiplied by UK corporation tax rate for the years ended 31 December 2005 and 2004 is as follows:

	£m	£m
Accounting profit before tax from continuing operations	153.1	142.1
Loss before tax from discontinued operations	–	(2.2)
Accounting profit before income tax	153.1	139.9
Notional charge at UK corporation tax rate of 30% (2004: 30%)	45.9	42.0
Adjustments in respect of current income tax of prior years	(1.0)	(1.7)
Adjustments in respect of deferred tax of prior years	(3.2)	(2.3)
Non-deductible expenses	1.5	2.6
Impairment	3.6	–
Stock option relief	(1.0)	(2.2)
Other	–	1.0
At the effective tax rate of 27.7% (2004: 28.2%)	45.8	39.4
Income tax expense reported in the consolidated income statement	45.8	39.4
Income tax attributable to discontinued operations	–	–
Total tax expense reported in the income statement	45.8	39.4

Deferred income tax

Deferred income tax at 31 December relates to the following:

	Consolidated balance sheet		Consolidated income statement	
	2005 £m	2004 £m	2005 £m	2004 £m
Deferred tax liabilities				
Accelerated capital allowances	(3.0)	(0.3)	3.4	0.7
Fair value adjustments on acquisition	(10.0)	(2.0)	(1.2)	(0.4)
	(13.0)	(2.3)		
Deferred tax assets				
Share based payments	10.9	6.1	(2.1)	(2.0)
Pension schemes	20.4	24.5	5.2	4.3
Provisions	6.3	3.7	(2.3)	(1.0)
Losses available for offset against future taxable income	0.5	0.6	0.7	0.3
	38.1	34.9		
Net deferred tax asset	25.1	32.6		
Deferred income tax expense			3.7	1.9

The Group has tax losses which arose in the UK of £8.5m (2004: £5.7m) that are available for offset against future taxable profits of the companies in which the losses arose. Deferred tax assets have not been recognised in respect of £6.9m (2004: £3.8m) of these losses, as their recoverability is uncertain.

There are no income tax consequences attaching to the payment of dividends by The Capita Group Plc to its shareholders.

11 Discontinued operations

During 2004 the Group disposed of its print business, CTD Capita (included within Integrated Services), and its primary healthcare business (included within Commercial Services) which was acquired with Aon Health Solutions in April 2004. The Group sold fixed assets of £0.6m, net assets of £4.4m and received cash consideration of £3.1m.

The results of the discontinued operations for the year were as follows:

	2005 £m	2004 £m
Revenue	–	2.9
Expenses	–	(3.2)
Gross loss	–	(0.3)
Loss on disposal of net assets	–	(1.9)
Loss before tax from discontinued operations	–	(2.2)
Tax related to pre-tax loss	–	–
Tax related to disposal of net assets	–	–
Loss for the year from discontinued operations	–	(2.2)

The net operating cash outflow attributable to the discontinued operations was £nil (2004: £(0.3m)).

Earnings per share:	*2005*	*2004*
Basic from discontinued operations	–	(0.33)p
Diluted from discontinued operations	–	(0.33)p

12 *Earnings per share*

Basic earnings per share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

The following reflects the income and share data used in the basic and diluted earnings per share computations:

	2005 £m	2004 £m
Net profit attributable to ordinary equity holders of the parent from continuing operations	**107.5**	102.9
Loss attributable to ordinary equity holders of the parent from a discontinued operation	–	(2.2)
Net profit attributable to ordinary equity holders of the parent	**107.5**	100.7

	2005 Number million	2004 Number million
Weighted average number of ordinary shares (excluding treasury shares) for basic earnings per share	**660.1**	665.4
Dilutive potential ordinary shares:		
Employee share options	**9.7**	5.9
Weighted average number of ordinary shares (excluding treasury shares) adjusted for the effect of dilution	**669.8**	671.3

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of completion of these financial statements.

To calculate earnings per share amounts for the discontinued operations, the weighted average number of ordinary shares for both basic and diluted amounts is as per the table above. The following table provides the loss figure used as the numerator:

	2005 £m	2004 £m
Net loss attributable to ordinary equity holders of the parent from discontinued operations for basic and diluted earnings per share calculation	–	(2.2)

The following additional earnings per share figures are calculated based on earnings attributable to ordinary equity holders of the parent before amortisation, share based payments and impairment of £128.3m (2004: £107.0m). They are included as they provide a better understanding of the underlying trading performance of the Group.

	2005 p	2004 p
Basic earnings per share – before amortisation, share based payment and impairment	**19.44**	16.08
– after amortisation, share based payment and impairment	**16.28**	15.13
Diluted earnings per share – before amortisation, share based payment and impairment	**19.16**	15.94
– after amortisation, share based payment and impairment	**16.05**	15.00

13 Dividends paid and proposed

	2005 £m	2004 £m
Declared and paid during the year		
Ordinary shares (equity):		
Final for 2004 paid: 3.6p per share (2003: 2.7p per share)	**24.0**	18.0
Interim for 2005 paid 2.1p per share (2004: 1.75p per share)	**14.0**	11.6
	38.0	29.6
Proposed for approval at AGM (not recognised as a liability at 31 December)		
Ordinary shares (equity):		
Final for 2005: 4.9p per share (2004: 3.6p per share)	**32.0**	23.8

14 Property, plant and equipment

	Leasehold improvements, land and buildings £m	Plant and *machinery* £m	*Total* £m
Cost			
At 1 January 2004	24.9	143.0	167.9
Subsidiaries acquired	3.0	–	3.0
Additions	3.0	43.2	46.2
Disposals	(3.2)	(1.8)	(5.0)
At 31 December 2004	27.7	184.4	212.1
Subsidiaries acquired	1.8	2.1	3.9
Additions	7.7	42.0	49.7
Disposals	(0.8)	(1.5)	(2.3)
At 31 December 2005	**36.4**	**227.0**	**263.4**
Depreciation and impairment			
At 1 *January 2004*	7.8	48.4	56.2
Provided during the year	2.7	25.2	27.9
Disposals	(0.1)	(1.0)	(1.1)
At 31 December 2004	10.4	72.6	83.0
Provided during the year	3.5	28.2	31.7
Disposals	(0.3)	(1.1)	(1.4)
At 31 December 2005	**13.6**	**99.7**	**113.3**
Net book value			
At 31 December 2005	**22.8**	**127.3**	**150.1**
At 31 December 2004	17.3	111.8	129.1
At 1 January 2004	17.1	94.6	111.7

The net book value of plant and machinery includes an amount of £0.2m (2004: £0.2m) in respect of assets held under finance leases.

15 Intangible assets

	Brands £m	Software and licences £m	Contracts and committed sales £m	Customer lists and relationships £m	Goodwill £m	Other intangibles £m	Total £m
Cost							
At 1 January 2004	–	–	–	–	451.2	–	451.2
Subsidiaries acquired	2.6	2.0	5.5	–	35.6	–	45.7
Additions	–	–	–	–	–	8.0	8.0
At 31 December 2004	2.6	2.0	5.5	–	486.8	8.0	504.9
Subsidiaries acquired	2.7	–	1.2	26.7	75.3	–	105.9
Additions	–	–	–	–	–	4.0	4.0
At 31 December 2005	**5.3**	**2.0**	**6.7**	**26.7**	**562.1**	**12.0**	**614.8**
Depreciation and impairment							
At 1 January 2004	–	–	–	–	–	–	–
Amortisation during the year	0.4	0.2	1.2	–	–	2.9	4.7
At 31 December 2004	0.4	0.2	1.2	–	–	2.9	4.7
Amortisation during the year	0.7	0.4	1.7	1.7	–	4.9	9.4
Impairment	–	–	–	–	12.0	–	12.0
At 31 December 2005	**1.1**	**0.6**	**2.9**	**1.7**	**12.0**	**7.8**	**26.1**
Net book value							
At 31 December 2005	**4.2**	**1.4**	**3.8**	**25.0**	**550.1**	**4.2**	**588.7**
At 31 December 2004	2.2	1.8	4.3	–	486.8	5.1	500.2
At 1 January 2004	–	–	–	–	451.2	–	451.2

The amount in 'other intangibles' represents the consideration paid to Aon to acquire the contract for the administration of the miners' personal injury liability claims on behalf of the Department of Trade and Industry.

Customer lists and relationships includes an amount of £11.0m in respect of relationships acquired with the BDML acquisition, which is being amortised over 10 years.

For the year ended 31 December 2005:

- Brands are amortised evenly over their useful economic lives of 5 and 10 years
- Software and licences are amortised over their useful economic lives of 5 years
- Contracts and committed sales are amortised over their useful economic lives of between 1.5 and 10 years
- Customer lists and relationships are amortised over their economic lives of between 4 and 10 years
- Other intangibles are amortised over their useful economic lives of 2.5 years

For the year ended 31 December 2004:

- Brands are amortised evenly over their useful economic lives of 5 years
- Software and licences are amortised over their useful economic lives of 5 years
- Contracts and committed sales are amortised over their useful economic lives of between 1.5 and 10 years
- Other intangibles are amortised over their useful economic lives of 2.5 years

16 Impairment of goodwill

Goodwill acquired through business combinations has been allocated for impairment testing purposes to the groups of cash generating units (CGUs) listed below. These represent the lowest level within the Group at which goodwill is monitored by management for internal reporting purposes.

The significant groups of CGUs identified are property services, resourcing services, insurance services, registrar services, financial services. The remaining groups of CGUs are included in the 'balance of CGUs column'.

The recoverable amount of all the cash generating units is based on a value in use calculation using cash flow projections based on the latest one year budget forecast extrapolated for four future years by a growth rate applicable to each unit; an appropriate terminal value based on a perpetuity calculation using nil real growth is then added. A discount rate of 11.1% is then applied to these projections.

Compound growth rates (years 2–5)	%
Property Services	6
Resourcing Services	6
Insurance Services	9
Registrar Services	12
Financial Services	14
Balance of CGUs (weighted average growth rate)	11

The growth rates used do not exceed published industry estimates. The long term growth rate used does not exceed the UK long term growth rate.

Carrying amount of goodwill allocated to group of cash generating units

	Property services £m	Resourcing services £m	Insurance services £m	Registrar services £m	Financial services £m	Balance of CGUs £m	Total £m
2005							
Goodwill	**43.8**	**80.7**	**166.6**	**88.3**	**89.0**	**81.7**	**550.1**
2004							
Goodwill	40.0	80.7	158.7	88.3	61.6	57.5	486.8

The key assumptions used in the impairment testing were as follows:

- Profit before interest and taxation
- Discount rates
- Rates of growth in cash generating units beyond the budget period.

Profit before interest and taxation

The profit before interest and taxation is based on the margins achieved remaining at the levels currently being achieved.

Discount rate

The discount rate reflects management's estimate of cost of capital employed for the groups of cash generating units listed above. This is the benchmark established to assess operating performance and to evaluate future capital investment proposals.

Rates of growth in cash generating units beyond the budget period

Growth rate assumptions are based on, as far as possible, published industry research.

Goodwill impairment

During the year the goodwill recognised on the acquisition of the Industrial Society's workforce and training business, re-branded as Capita Learning & Development, which was transacted in December 2001 was impaired. Over the period, the business has not performed to expectation largely due to a market decline in this type of training.

The impairment loss recognised against this residual goodwill amounted to £12.0m.

This cash generating unit Capita Learning & Development forms part of the Professional Services segment. The CGU specialises in providing employee training.

The residual valuation after impairment is based on its value in use.

Management believes that no likely change in the key assumptions above would cause any of the identified cash generating units to become impaired, apart from Capita Learning & Development which is carried at value in use.

17 Financial assets

	2005 £m	2004 £m
Available-for-sale investments	12.2	0.2
Interest rate swaps	1.6	–
	13.8	0.2

Available-for-sale financial assets include investments in cash funds, held in the Group's insurance captives, of £12.0m (2004: £nil) and investments in unlisted ordinary shares of £0.2m (2004: £0.2m). Investments in cash funds represents units acquired which are periodically valued based on the underlying performance of the investments held. The unlisted ordinary shares, where there is no immediately identifiable market and have no fixed maturity date or coupon rate, are carried at cost less provision for any impairment.

Details of the interest rate swaps are contained in note 25.

18 Business combinations

2005 acquisitions

The Group has made a number of acquisitions in the year of which only one, the acquisition of the BDML group of companies (BDML), is considered material and is thus disclosed separately. The remainder are shown in aggregate. The book and fair values of the assets acquired are disclosed in the tables below.

BDML	Book values £m	Fair value £m	Fair value to Group £m
Intangible assets	–	12.9	12.9
Property, plant and equipment	0.8	(0.1)	0.7
Deferred tax	1.0	–	1.0
Debtors	38.0	–	38.0
Cash and short term deposits	0.3	–	0.3
Creditors	(40.3)	(0.3)	(40.6)
Corporation tax	0.3	–	0.3
Net assets	0.1	12.5	12.6
Goodwill arising on acquisition			13.4
			26.0
Discharged by:			
Cash			25.7
Associated costs settled in cash			0.3
			26.0

BDML, includes BDML Connect Limited an insurance intermediary and agent that offers instalment debt facilities to its insurance customers and a specialist in pet insurance and policy administration.

The Group acquired 100% of the ordinary share capital of BDML on the 25 July 2005. From the date of acquisition BDML has contributed £1.1m to the net profit after tax of the Group, had the combination taken place at the beginning of the year the profit after tax of the Group would have been £107.9m and the revenue from continuing operations would have been £1,443.7m.

Included within goodwill on acquisition are certain intangibles that were not separable from the acquiree and could not be measured, these include customer loyalty and the assembled workforce.

The acquisition of BDML includes 'insurance debtors subject to a securitisation agreement'. The purpose of this arrangement is to securitise customer receivables, derived through the provision of instalment credit facilities to insurance customers of the company.

The company sells said receivables, with no immediate effect on the P&L, for cash to a third party (Gresham in this case). Gresham take on the rights and responsibilites of these receivables such that the terms of this agreement dictate that Gresham has no recourse to BDML beyond 14% of the total receivable securitised.

Under UK GAAP, the substance of this arrangement was disclosed as linked presentation under the current assets section of the balance sheet, without appearing in the financing section of the balance sheet.

The Group's transition to IFRS has necessitated different disclosure, the impact of which is to reflect on BDML's opening balance sheet an increase in the Groups receivables of £37.1m adding £26.8m of securitised asset financing. The respective balances of this arrangement at 31 December 2005 were £37.9m to receivables and £28.2m to securitised asset financing.

18 Business combinations (continued)

Other acquisitions	Book values £m	Fair value £m	Fair value to Group £m
Intangible assets	0.3	17.4	17.7
Property, plant and equipment	4.0	(0.8)	3.2
Deferred tax	1.3	–	1.3
Debtors	23.3	(0.2)	23.1
Cash and short term deposits	2.4	–	2.4
Creditors	(20.8)	(1.1)	(21.9)
Provisions	(0.1)	(0.1)	(0.2)
Corporation tax	(1.1)	–	(1.1)
Long term debt	(2.9)	–	(2.9)
Net assets	6.4	15.2	21.6
Goodwill arising on acquisition			52.7
			74.3
Discharged by:			
Fair value of shares issued			0.3
Cash			62.1
Deferred consideration paid			13.8
Deferred consideration accrued			4.7
Release of deferred provision			(6.6)
			74.3

As required by IAS 12 Deferred taxation is calculated on intangible assets recognised as a result of an acquisition, the impact of this is to increase goodwill by £9.2m and to create a deferred tax liability of the same amount.

The other acquisitions in the year include Buchanan Consulting Engineers Limited, BMI Health Services Limited, Channel House Financial Services Group Limited, FPS Group of Companies Limited, Lonsdale Travel Limited, Quay Software Solutions Limited, Randall Lyons Limited, Micromedia Limited, MHA Pensions Limited and Norman + Dawbarn. The companies acquired provide a range of property, health, trust, pension, corporate travel and software services.

On 8 November 2005, 0.1 million ordinary 2p shares with an aggregate nominal value of £1,300 were issued at £3.89 each pursuant to the acquisition of a subsidiary undertaking, Lonsdale Travel Limited.

The performance of these acquisitions post their inclusion in the Group cannot be ascertained as they have been fully integrated within existing offerings.

Within goodwill are certain intangibles that were not separable from the acquirees and could not be measured reliably. These items include customer loyalty and the assembled workforce.

Included in the above table is further consideration paid in cash with regard to the acquisition of the Lincoln Life and Pensions business in a previous year of £13.8m against which the Group had provided for accrued deferred consideration payable of £6.6m. There were also further payments on previous acquisitions. The impact of these further payments is to increase goodwill by £9.4m.

In the comparative period the Group made acquisitions of value £52.1m of which £51.4m was settled by cash, £0.4m through the issue of loan notes and £0.3m by way of deferred consideration. Net assets acquired amounted to £19.0m (including intangible assets of £10.1m) resulting in goodwill of £33.1m. The resultant goodwill holds intangibles that were not separable from the acquiree and could not be reliably valued. These include customer loyalty and the assembled workforce. Further consideration was paid on acquisitions prior to 2004 which amounted to £5.0m.

18 Business combinations (continued)

2004 acquisitions

The Group's acquisitions in the comparative year, which are shown in aggregate, are disclosed in the table below.

	Book values £m	Accounting policy adjustments £m	Fair value adjustments £m	Fair value to the Group £m
Tangible fixed assets	3.2	–	(0.2)	3.0
Intangible fixed assets	2.5	–	3.7	6.2
Debtors	17.9	–	–	17.9
Cash	3.8	–	–	3.8
Creditors	(11.1)	(0.6)	0.5	(11.2)
Taxation	(0.9)	–	–	(0.9)
Deferred taxation	1.6	–	–	1.6
Long term debt	(5.2)	–	–	(5.2)
Minority interest share of assets on acquisition	(0.1)	–	–	(0.1)
	11.7	(0.6)	4.0	15.1
Goodwill				37.0
Consideration				52.1
Discharged by:				
Loan notes				0.4
Deferred consideration				0.3
Cash				51.4
				52.1

Symonds Group (Holdings) Limited

	Book values £m	Accounting policy adjustments £m	Fair value adjustments £m	Fair value to the Group £m
Tangible fixed assets	2.6	–	0.3	2.9
Intangible fixed assets	–	–	3.9	3.9
Debtors	12.4	–	–	12.4
Cash	2.9	–	–	2.9
Creditors	(7.1)	–	–	(7.1)
Taxation	(0.6)	–	–	(0.6)
Deferred taxation	0.5	–	–	0.5
Long term debt	(1.6)	–	–	(1.6)
	9.1	–	4.2	13.3
Goodwill				17.3
Consideration				30.6
Discharged by:				
Cash				30.6
				30.6

Symonds Group (Holdings) Limited – on 16 February 2004 the Group acquired Symonds Group (Holdings) Limited for a cash consideration of £30.6m. The Group acquired tangible fixed assets of £2.6m (fair value £2.9m), debtors of £12.4m (fair value £12.4m), creditors, including taxation of £7.7m (fair value £7.7m), long term debt of £1.6m and cash in hand of £2.9m. The unaudited management accounts for the period 1 January 2004 to the effective date of acquisition show profit on ordinary activities after taxation of £0.2m. The audited financial statements for the year ended 31 December 2003 show a profit on ordinary activities after taxation of £1.8m.

The subsidiary has been merged within the existing property operations of the Group but its profitability is visible in that merged operation and so although the Group is able to disclose post acquisition performance of the acquisition it is not possible to determine post acquisition cash inflows.

Capita Health Solutions (formerly Aon Health Solutions) – on 8 April 2004 the Group acquired the occupational health business of Aon Health Solutions for a cash consideration of £2.7m. The Group acquired debtors of £2.7m (fair value £2.7m), and creditors, including taxation of £0.6m (fair value £0.6m). The pre-acquisition performance of the business is unavailable as the figures were not reported separately in the financial statements of the vendor.

18 Business combinations (continued)

The business has been merged within the existing operations of the Group but its profitability is visible in that merged operation. The Group is therefore able to disclose post acquisition performance of the acquisition although it is not possible to determine post acquisition cash inflows.

Personal Pensions Management Limited On 30 June 2004 the Group acquired Personal Pensions Management Limited for a cash consideration of £9.0m. The Group acquired tangible fixed assets of £0.1m (fair value £0.1m), debtors of £1.3m (fair value £1.3m), creditors, including taxation of £1.1m (fair value £1.4m) and cash in hand of £1.3m. The company had been loss making in 2003 due to a high operational cost base and the unaudited management accounts for the period 1 January 2004 to the effective date of acquisition show a loss on ordinary activities after taxation of £1.2m. Since acquisition Capita has initiated a cost and service improvement programme and believe that profitability will be achieved in 2005.

The subsidiary acquired during the year resulted in net operating activities inflows of £4.2m for the Group and outflows of £0.6m in respect of taxation.

Other acquisitions in the year include Brownsword Limited and Learnhow Publications for an aggregate consideration of £9.8m, satisfied by cash of £9.4m (including deferred consideration of £0.3m) and the issue of £0.4m of loan notes. The Group acquired tangible fixed assets of £0.5m (fair value £nil), intangible fixed assets of £2.5m (fair value £nil), debtors of £1.5m (fair value £1.5m), creditors, including taxation of £1.5m (fair value £1.3m), long term debt of £3.6m and overdraft of £0.4m.

Other acquired businesses have been completely integrated within the existing businesses of the Group and consequently it is not possible to determine post acquisition results of the businesses.

During 2004, a further £4.4m deferred consideration became due on the acquisition of Capita Life & Pensions Services Limited. This had been provided along with a further £0.6m in respect of other previous acquisitions and disclosed as deferred consideration payable in the comparative period. The consideration was settled in cash.

The fair value adjustments reflect the Group's estimate of the fair value of intangible assets, fixed assets acquired, and estimates of the recoverability of debtors and liabilities in respect of accruals. Intangible fixed assets relate to goodwill on the acquired companies balance sheets and hence are written off on acquisition. There were no significant impacts on deferred taxation in relation to the fair value adjustments.

19 Trade and other receivables

Current	2005 £m	2004 £m
Trade receivables	**207.6**	138.4
Other receivables	**35.0**	23.5
Gross amounts due from customers on construction contracts	**5.4**	3.3
Prepayments and accrued income	**95.8**	95.1
	343.8	260.3

Non-current	2005 £m	2004 £m
Trade receivables	**4.9**	5.8
Prepayments and accrued income	**0.9**	0.3
	5.8	6.1

Trade receivables have been netted down by the value of bad debt provisions of £4.0m (2004: £3.3m).

20 Trade and other payables

Current	2005 £m	2004 £m
Trade payables	**61.8**	26.4
Other payables	**52.5**	48.0
Other taxes and social security	**49.6**	41.5
Gross amounts due to customers on construction contracts	**2.2**	–
Accruals and deferred income	**211.9**	193.0
	378.0	308.9
Non-current		
Accruals and deferred income	**1.3**	3.1
	1.3	3.1

21 Construction contracts

Presented in the table below are disclosures with regard to the Group's property services business where the provision, as a sub-contractor, is architectural, structural or another service that results in the construction of a new asset.

	2005 £m	2004 £m
Contract revenue recognised in relation to this construction contracts in the year	47.3	38.3
Aggregate costs incurred and recognised profits (less losses) to date	95.2	73.3
Gross amount due from customers for construction contracts	5.4	3.3
Gross amount due to customers on construction contracts	2.2	–

22 Financial liabilities

Current	2005 £m	2004 £m
Bank overdraft	19.3	26.1
Obligations under finance leases (note 23)	0.2	0.2
Unsecured loan notes	2.2	6.7
Asset-based securitised financing (see note 18)	28.2	–
	49.9	33.0
Non-current		
Obligations under finance leases (note 23)	–	–
Unsecured loan notes	20.5	20.5
Bonds	198.6	124.7
Currency swaps	2.6	–
	221.7	145.2

The obligations under finance leases are secured on the assets being financed. The bank overdraft, bonds and loan notes are unsecured.

The bank overdraft bears interest at Barclays Bank standard rates based on LIBOR and the bonds effectively bear interest at 6 month LIBOR plus 1%.

Loan notes were issued pursuant to the satisfaction of consideration due in relation to the acquisition of a subsidiary undertaking. Loan notes issued during the year amounted to £nil (2004: £0.4m) and £4.4m (2004: £6.3m) were repaid. The following loan notes are repayable on demand: £0.3m by 31 December 2006 and £1.9m by 31 May 2007. The remaining loan notes of value £20.5m are repayable in more than 1 year and are repayable upon receipt of 1 year's advance notification of the intent to redeem from either the loan note holder or the company. Consequently, £20.5m of the loan notes are repayable in more than 1 year. The interest rates attributable to the loan notes are fixed for each new issue. These rates range from 3.45% to 5.25%.

During the year the Group issued a further £75m of bonds with maturity dates of £50m on 28 September 2013 and £25m on 28 September 2015 with an interest rate set at 0.525% above 6 month LIBOR.

Existing issues are in the form of £55m sterling and US dollar amounts of $66m and $36m. These issues mature on 20 June 2009, 20 June 2009 and 20 June 2012 and are issued at interest rates of 6.44%, 6.1% and 6.47% respectively. The Group entered into cross currency swaps for the US dollar issues (effectively converting the $66m and $36m bonds into a sterling denominated long term loan of £70m) and an interest rate swap for the sterling issue, the maturity dates being the same as for the issues themselves. Issue costs incurred were £0.5m and these are being spread over the life of the bonds to their maturity. The effect of this interest rate swap is to convert the interest cost on the bond to 6 month LIBOR plus 1%.

23 Obligations under leases and hire purchase contracts

Obligations under finance leases and hire purchase contracts

The Group uses finance leases and hire purchase contracts to acquire plant and machinery. These leases have terms of renewal and purchase options but no escalation clauses. Renewals are at the option of the lessee.

The value of future minimum lease payments and their present value which are the same, is analysed as follows:

	2005 £m	2004 £m
Not later than one year	**0.2**	0.2
	0.2	0.2

Operating lease agreements where the Group is lessee

The Group has entered into commercial leases on certain properties, motor vehicles and items of plant and machinery. These leases have an average duration of between 3 and 10 years.

Future minimum rentals payable under non-cancellable operating leases are as follows:

	2005 £m	2004 £m
Not later than 1 year	**50.5**	53.4
Later than 1 year but not later than 5 years	**120.3**	144.0
Later than 5 years	**68.3**	50.3
	239.1	247.7

24 Provisions

	Property provision £m
At 1 January 2005	5.5
Provisions acquired	0.2
Utilisation	(2.7)
Additional provisions in the year	0.1
Unwinding of interest on discounted provisions	0.2
At 31 December 2005	3.3

The property provision is made on a discounted basis for the future rent expense and related cost of leasehold property (net of estimated sub-lease income) where the space is vacant or currently not planned to be used for ongoing operations. The expectation is that this expenditure will be incurred over the remaining periods of the leases which range from 1 to 6 years.

25 Financial instruments

The Group's treasury policy, risk management objectives and strategies are discussed at length in the business review in the full Annual Report on pages 12 to 14.

As per IFRS 1, the Group has elected not to present comparative information in accordance with IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' (note 2). The disclosure which follows is separated into the following:

- 2005 disclosures prepared under IAS 32 and IAS 39
- 2004 disclosures prepared under UK GAAP

2005 disclosures

Interest rate risk profile of financial assets and liabilities

The interest rate profile of the financial assets and liabilities of the Group as at 31 December is as follows:

At 31 December 2005	Within 1 year £m	Between 1 – 2 years £m	Between 2 – 3 years £m	Between 3 – 4 years £m	Between 4 – 5 years £m	More than 5 years £m	Total £m
Fixed rate							
Loan notes	2.2	20.5	–	–	–	–	22.7
Obligations under finance leases	0.2	–	–	–	–	–	0.2
Floating rate							
Bonds	–	–	–	100.4	–	98.2	198.6
Bank overdraft	19.3	–	–	–	–	–	19.3
Interest rate swap*	–	–	–	(1.6)	–	–	(1.6)
Foreign currency swap**	–	–	–	1.4	–	1.2	2.6

*/** the effect of the interest rate swap and the currency swap are disclosed below. Bonds are classified as floating rate due to the effect of the interest and currency swaps.

At 31 December 2004	Within 1 year £m	Between 1 – 2 years £m	Between 2 – 3 years £m	Between 3 – 4 years £m	Between 4 – 5 years £m	More than 5 years £m	Total £m
Fixed rate							
Loan notes	6.6	20.5	–	–	–	–	27.1
Obligations under finance leases	0.2	–	–	–	–	–	0.2
Floating rate							
Bonds	–	–	–	–	99.8	23.2	123.0
Bank overdraft	26.1	–	–	–	–	–	26.1
Interest rate swap*	–	–	–	–	(1.4)	–	(1.4)
Foreign currency swap**	–	–	–	–	1.7	1.4	3.1

The comparative data above for 31 December 2004 has been restated, to reflect the effect of adopting IAS 32 and IAS 39 on 1 January 2005, in order to provide more useful information. The book values reflected in the financial statements as at 31 December 2004 prior to adoption of IAS 32 and IAS 39 are shown in the following table.

Fair values of financial assets and financial liabilities

Set out below is a comparison by category of carrying amounts and fair values of all the Group's financial instruments that are carried in the financial statements.

	2005		2004	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Financial assets				
Available for sale current assets	12.2	12.2	0.2	0.2
Interest rate swaps	1.6	1.6	–	1.4
Financial liabilities				
Bank overdraft	19.3	19.3	26.1	26.1
Obligations under finance leases	0.2	0.2	0.2	0.2
Loan notes	22.7	22.7	27.1	25.6
Bonds	198.6	198.6	121.6	123.0
Currency swaps	2.6	2.6	3.1	3.1

In addition to the above financial liabilities, at the year-end there is an amount of £28.2m of asset-based securitised financing. This form of financing initially arose as a consequence of the acquisition of BDML Connect Ltd – see note 18.

The fair value of derivatives and borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates.

25 Financial instruments (continued)

2005 disclosures (continued)

Hedges

Fair value hedges

The Group has in issue fixed rate dollar and sterling bonds which it has hedged through a combination of interest rate and currency swaps.

At 31 December 2005 and 31 December 2004, the Group had an interest rate swap in place with a notional amount of £55.0m whereby it receives a fixed rate of interest of 6.44% and pays a variable rate of 1% above LIBOR on this notional amount. The swap is being used to hedge the exposure to changes in the fair value of its £55.0m of 6.44% bonds. The secured loan and interest rate swap have the same critical terms.

Also, at December 2005 and December 2004, the Group had in place currency swaps with notional amounts of $66.0m and $36.0m whereby it receives a fixed rate of interest of 6.1% and 6.47% respectively and pays a variable rate of 1% above LIBOR on these notional amounts. The swap is being used to hedge the exposure to changes in the value of its US Dollar issued bonds. The secured loan and interest rate swap have the same critical terms.

There are no significant concentrations of credit risk within the Group. The maximum credit risk exposure relating to financial assets is represented by the carrying value as at the balance sheet date.

2004 disclosures

Derivatives and other financial instruments

It is, and has been throughout the period under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk and liquidity risk. The Board reviews and agrees policies for managing these risks and they are summarised below. These policies have remained unchanged year on year.

The disclosure below excludes short term debtors and creditors.

The Group's principal financial instruments comprise bank loans, bond issues, loan notes, finance leases and cash. The main purpose of these financial instruments is to raise finance for the Group's operations.

The Group has various other financial instruments such as trade debtors and trade creditors, which arise directly from its operations.

(a) Interest rate risk

The interest rate profile of the financial liabilities of the Group as at the year end was as follows:

Financial liabilities	Floating rate £m	Fixed rate £m	Financial liabilities on which no interest is payable £m	Total £m	Fixed rate weighted average interest rate year end	Weighted average period for which rate is fixed Years	Weighted average period to maturity of non-interest bearing liabilities Years
31 December 2004							
Sterling	**150.8**	**27.3**	**3.1**	**181.2**	**4**	**1**	**1**

The financial liabilities of the Group comprised:	2004 £m
Bank overdraft repayable on demand	**26.1**
Loan notes	**27.1**
Bonds	**124.7**
Obligations under finance leases	**0.2**
Other creditors falling due after more than 1 year	**3.1**
	181.2

The bank overdraft bears interest at Barclays Bank standard rates based on the bank base rate and the bonds effectively bear interest at 6 month LIBOR plus 1%.

Financial assets	Floating rate £m	Financial assets on which no interest is receivable £m	Total £m	Weighted average period to maturity of non interest bearing assets Years
31 December 2004				
Sterling	–	**0.2**	**0.2**	**2**

£0.2m (2003: £5.2m) is represented by current asset investments that have an indefinite life.

The financial assets of the Group comprised:	2004 £m
Cash at bank and in hand	–
Current asset investments	**0.2**
	0.2

The cash investment fund in the comparative and cash at bank bear interest at floating rates based on the bank base rate.

25 Financial instruments (continued)

2004 disclosures (continued)

(b) Borrowing facilities

At 31 December 2004 the Group had total borrowing facilities of £175m, of which £150m was committed. At the year-end the amount of the committed facility drawn down was £60m. The un-drawn committed facilities available at 31 December 2004 in respect of which all conditions and precedent had been met at that date are as follows:

	2004 £m
Expiring in less than 1 year	50.0
Expiring in between 2 to 5 years	40.0
	90.0

2004	Gains £m	Losses £m	Total £m
Gains unrecognised at 31 December 2004	1.4	–	1.4
Losses deferred at 31 December 2004	–	(3.1)	(3.1)
	1.4	(3.1)	(1.7)
Of which:			
Gains expected to be recognised in the profit and loss account in 2005 on the interest rate swap	0.3	–	0.3
Gains expected to be recognised in the profit and loss account in 2005 on the currency swap	–	–	–
Gains included in the profit and loss account that arose in previous years	*0.8*	–	*0.8*

26 Authorised and issued share capital

	2005 Million	2004 Million	2005 £m	2004 £m
Authorised				
Ordinary shares of 2p each	**1,000.0**	1,000.0	**20.0**	20.0
Allotted, called up and fully paid				
Ordinary shares of 2p each				
At 1 January	**670.9**	*666.6*	**13.4**	13.3
Shares repurchased	**(5.0)**	(0.3)	**(0.1)**	–
Issued on exercise of share options	**5.0**	4.6	**0.1**	0.1
Issued on acquisition of subsidiary undertaking	**0.1**	–	–	–
At 31 December	**671.0**	670.9	**13.4**	13.4

On 8 November 2005, 0.1 million ordinary 2p shares with an aggregate nominal value of £1,300 were issued at £3.89 each pursuant to the acquisition of a subsidiary undertaking, Lonsdale Travel Limited.

During the year the Group repurchased 5.0m ordinary 2p shares with an aggregate nominal value of £0.1m at a total cost of £18.7m for which it paid cash at a weighted average cost per share of £3.73. These shares were cancelled.

During the year 5.0m ordinary 2p shares with an aggregate nominal value of £0.1m were issued under share option schemes for a total consideration of £9.9m.

Treasury shares	2005 Million	2004 Million	2005 £m	2004 £m
Ordinary shares of 2p each				
At 1 January	**8.6**	–	**0.2**	–
Shares repurchased	***8.3***	*8.6*	***0.2***	*0.2*
At 31 December	**16.9**	8.6	**0.4**	0.2

During the year the Group has repurchased 8.3m ordinary 2p shares with an aggregate nominal value of £0.2m to be held in treasury for which it paid cash. The weighted average cost of each share was £3.76 and the total consideration for these shares was £31.2m.

The Group has an unexpired authority to repurchase up to 10% of its issued share capital.

27 Share based payment plans

The Group operates several share based payment plans as follows:

Deferred Annual Bonus Plan

This scheme is applicable to Executive Directors and Divisional Executive Directors. Under this scheme awards are made annually consisting of Deferred Shares, which are linked to the payout under the Annual Bonus Scheme (details of which are contained in the Directors' remuneration report) and Matching Shares. The value of Deferred Shares is determined by the payout under the Annual Bonus Scheme: half of the annual bonus is paid in cash and the remainder is compulsorily deferred on a gross basis into Deferred Shares. The Deferred Shares are held for a period of three years from the date of award during which they are not forfeitable, except in the case of dismissal for gross misconduct.

A conditional award of Matching Shares is made at the same time as the award of Deferred Shares. Participants will be eligible to receive up to 1.5 Matching Shares for every Deferred Share. Matching Shares will vest after the 3 year holding period to the extent to which performance conditions have been met. 33.3% of the Matching Shares will vest if growth in the company's earnings per share (EPS) is equal to growth in the UK Retail Price Index (RPI) plus 6% per annum, rising on a straight-line basis to 100% vesting if growth in the company's EPS is equal to or greater than growth in the RPI plus 16% per annum. The performance condition attached to the awards may be amended by the Group Remuneration Committee, sub-committee of the Group Board, from time to time, subject to the new condition being no less demanding than the original condition.

Long term Indexed Share Appreciation Scheme (LTISAS)

This scheme was only open to the Executive Directors and the Divisional Executive Directors. The final grant under this scheme was made in November 2004. Under this scheme, participants were granted two equal tranches of 600,000 share options. The performance criteria are the same for both tranches with performance periods that end on 31 December 2006. The exercise price of the options increases in line with the FTSE All Share Index from the date of grant to 25 November 2007. The final option price at which the awards can be exercised cannot be below the market value of the share at the date of grant. These options are only exercisable subject to the growth in the company's EPS over the performance period.

Options will become exercisable, if over the performance period, the growth in the company's EPS exceeds certain targets as follows: 25% of the options shall vest if growth in the company's EPS exceeds RPI growth by 8% per annum, rising on a straight-line basis to 100% vesting if growth in the company's EPS exceeds growth in the RPI by 12% per annum. The contractual life of options granted is 10 years for the first tranche and 8 years for the second tranche as the options under both schemes are exercisable between 25 November 2007 and 25 November 2012.

1997 Executive Share Option Scheme

This scheme is open to senior employees other than Executive Directors and Divisional Executive Directors. The exercise price of the options is equal to the market price of the shares on the date of grant. Options granted under this scheme become exercisable if the growth in the company's EPS exceeds the growth in RPI by 8% over the 3 year vesting period from the date of grant. The contractual life of each option granted is 7 years. There are no cash settlement alternatives.

Capita Sharesave Scheme

This is an employee Save As You Earn scheme open to all Capita employees. Under this scheme, employees are granted share options at a discount to the market price at the date of grant. The discount is currently 10% but was 20% prior to 2005. The options become exercisable for a 6 month period following completion of a 3 or 5 year savings period. There are no performance conditions attached to these options.

The expense recognised for share based payments in respect of employee services received during the year to 31 December 2005 is £7.6m (2004: £4.7m), all of which arises from equity-settled share based payment transactions.

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the year (excluding Deferred Annual Bonus Plan and LTISAS).

	2005 Number	2005 WAEP	2004 Number	2004 WAEP
Outstanding as at 1 January[1]	**47,937,231**[1]	**£3.16**[1]	46,399,543	£3.04[1]
Granted during the year	**5,226,702**	**£3.57**	7,207,760	£2.66
Exercised	**(4,263,298)**	**£2.29**	(3,767,115)	£1.10
Expired during the year	**(6,221,476)**	**£3.17**	(1,902,957)	£2.46
Outstanding as at 31 December[1]	**42,679,159**	**£3.29**	47,937,231	£3.16
Exercisable at 31 December	**21,096,290**	**£3.96**	16,506,772	£3.96

[1] Included within this balance are options over 21,950,907 (2004: 29,741,702) shares that have not been recognised in accordance with IFRS 2 as the options were granted on or before 7 November 2002. These options have not been subsequently modified and therefore do not need to be accounted for in accordance with IFRS 2.

The options have been exercised on a regular basis throughout the year and the weighted average share price during the year was as follows £3.78 (2004: £3.12).

As noted above under the LTISAS scheme two tranches of 600,000 share options have been issued to each participant in the scheme. Both were deemed to have been granted in November 2002. The first tranche, totalling 5,400,000 share options, was awarded and issued in November 2002 when the share price was £2.16. The second tranche, also totalling 5,400,000 share options, was awarded in November 2002 and issued in November 2004 when the share price was £3.51. Thus the total number of options outstanding under this scheme was 10,800,000 at 31 December 2005 (2004: 10,800,000). As the exercise price of the options increases in line with the FTSE All Share Index from the beginning to the end of the performance period, it is not possible to determine the weighted average exercise price until the end of the performance period. None of the LTISAS options is exercisable until 25 November 2007.

The total cash value of the Deferred Shares awarded during the year under the Deferred Annual Bonus Plan, discussed above, was £1.7m (2004: £nil)

The weighted average fair value of options granted during the year was £1.16 (2004: £0.92). The range of exercise prices for options outstanding at the end of the year was £0.34 to £5.35 (2004: £0.34 to £5.35).

27 Share based payment plans (continued)

The fair value of equity-settled share options granted is estimated as at the date of grant using a multiple simulation option pricing valuation model, taking into account the terms and conditions upon which the options were granted. The following table lists the inputs to the model used for the years ended 31 December 2005 and 31 December 2004.

	2005	2004
Dividend yield (%)	**1.5**	1.6
Expected share price volatility (%)	**37.80**	40.0
Historical volatility (%)	**37.80**	40.0
Risk-free interest rate (%)	**4.5**	4.5
Expected life of option (years)	**4.49**	4.45
Weighted average share price	**£3.78**	£3.12

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome. No other features of options grant were incorporated into the measurement of fair value.

28 Reconciliation of movements in equity

	Share capital £m	Share premium £m	Treasury shares £m	Capital redemption reserve £m	Retained earnings £m	Foreign currency translation reserve £m	Total equity £m	Minority interests £m	Total £m
At 1 January 2004	13.3	242.7	–	0.1	61.7	–	317.8	0.1	317.9
Total recognised income and expense for the year	–	–	–	–	89.3	0.1	89.4	(0.2)	89.2
Share based payment	–	–	–	–	4.7	–	4.7	–	4.7
Purchase of own shares	–	–	(0.2)	–	(27.5)	–	(27.7)	–	(27.7)
Share translation costs	–	–	–	–	(0.2)	–	(0.2)	–	(0.2)
Shares issued	0.1	5.4	–	–	–	–	5.5	–	5.5
Preference shares issued	–	–	–	–	–	–	–	0.5	0.5
Equity dividends paid	–	–	–	–	(29.6)	–	(29.6)	–	(29.6)
At 31 December 2004	13.4	248.1	(0.2)	0.1	98.4	0.1	359.9	0.4	360.3
Effect of implementing IAS 32/39	–	–	–	–	–	–	–	–	–
At 1 January 2005	**13.4**	**248.1**	**(0.2)**	**0.1**	**98.4**	**0.1**	**359.9**	**0.4**	**360.3**
Total recognised income and expense for the year	–	–	–	–	**107.5**	**0.2**	**107.7**	**(0.2)**	**107.5**
Share based payment	–	–	–	–	**7.6**	–	**7.6**	–	**7.6**
Purchase of own shares – held in treasury	–	–	**(0.2)**	–	**(30.8)**	–	**(31.0)**	–	**(31.0)**
Purchase of own shares – cancelled	**(0.1)**	–	–	**0.1**	**(18.6)**	–	**(18.6)**	–	**(18.6)**
Share transaction costs	–	–	–	–	**(0.3)**	–	**(0.3)**	–	**(0.3)**
Shares issued	**0.1**	**10.0**	–	–	–	–	**10.1**	–	**10.1**
Equity dividends paid	–	–	–	–	**(38.0)**	–	**(38.0)**	–	**(38.0)**
At 31 December 2005	**13.4**	**258.1**	**(0.4)**	**0.2**	**125.8**	**0.3**	**397.4**	**0.2**	**397.6**

Share capital – The balance classified as share capital includes the nominal proceeds on issue of the company's equity share capital, comprising 2p ordinary shares.

Share premium – The amount paid to a company by shareholders, in cash or other consideration, over and above the nominal value of shares issued to them.

Treasury shares – Stock that has been bought back by the issuing corporation and is available for retirement or resale; it is issued but not outstanding; it cannot vote and pays no dividends.

Capital redemption reserve – A company can redeem shares which are issued as redeemable shares by repaying the nominal value to the shareholder, whereupon the shares are cancelled. Redemption must normally be from distributable profits, but a procedure exists to allow shares to be redeemed from capital. As this amounts to a reduction of capital, an amount equivalent to the reduction of issued capital may need to be transferred to a capital redemption reserve.

Merger reserve – A capital reserve appearing in the consolidated balance sheet for a group of companies arising where the value of the underlying assets acquired exceeds the value of the consideration given for them.

Foreign currency translation – Gains or losses resulting from the process of expressing amounts denominated or measured in one currency in terms of another currency by use of the exchange rate between the two currencies. This process is generally required to consolidate the financial statements of foreign affiliates into the total company financial statements and to recognise the conversion of foreign currency or the settlement of a receivable or payable denominated in foreign currency at a rate different from that at which the item is recorded. Translation adjustments are not included in determining net income, but are disclosed as separate components of consolidated equity.

Retained earnings – Net profits kept to accumulate in an enterprise after dividends are paid; retained in the business as working capital.

29 Additional cash flow information

Reconciliation of net cash flow to movement in net funds/(debt)

	Net debt at 31 December 2004 £m	Adjustments to comply with IAS 32 and IAS 39 £m	Net debt at 1 January 2005 £m	Acquisitions in 2005 (exc. Cash) £m	Cash flow movements £m	Non-cash flow movements £m	Net debt at 31 December 2005 £m
Cash and cash equivalents	–	–	–	–	–	–	–
Overdrafts	(26.1)	–	(26.1)	–	6.8	–	**(19.3)**
Cash	(26.1)	–	(26.1)	–	6.8	–	**(19.3)**
Loan notes	(27.1)	–	(27.1)	–	4.4	–	**(22.7)**
Long term debt	–	–	–	(2.9)	2.9	–	–
Bonds	(124.7)	1.7	(123.0)	–	(74.9)	(0.7)	**(198.6)**
Finance leases	(0.2)	–	(0.2)	(0.2)	0.2	–	**(0.2)**
Sub-total net debt	(178.1)	1.7	(176.4)	(3.1)	(60.6)	(0.7)	(240.8)
Asset based securitised financing (see note 18)	–	–	–	(26.8)	(1.4)	–	(28.2)
	(178.1)	1.7	(176.4)	(29.9)	(62.0)	(0.7)	(269.0)

	Net debt at 1 January 2004 £m	Acquisitions in 2004 (exc. Cash) £m	Cash flow movements £m	Non-cash flow movements £m	Net debt at 31 December 2004 £m
Cash and cash equivalents	30.7	–	(30.7)	–	–
Overdrafts	–	–	(26.1)	–	(26.1)
Cash	30.7	–	(56.8)	–	(26.1)
Loan notes	(33.0)	(0.4)	6.3	–	(27.1)
Long term debt	–	(5.2)	5.2	–	–
Bonds	(124.6)	–	–	(0.1)	(124.7)
Finance leases	(0.5)	–	0.3	–	(0.2)
Total	(127.4)	(5.6)	(45.0)	(0.1)	(178.1)

30 Capital commitments

At 31 December 2005, amounts contracted for but not provided in the financial statements for the acquisition of property, plant and equipment amounted to £8.1m (2004: £14.1m).

31 Contingent liabilities

(a) The Group has provided through the normal course of its business performance bonds of £4.1m (2004: £12.4m). The Group has also provided indemnities to the value of £0.5m (2004: £2.7m).

(b) Further consideration may be due, dependent on certain performance criteria, on the acquisition of Brownsword Limited (acquired on 17 November 2004) up to a maximum of £5.0m.

(c) Further consideration may be due, dependent on certain performance criteria, on the acquisition of BDML Group of companies (acquired on 25 July 2005) up to a maximum of £9.0m.

(d) Further consideration may be due, dependent on certain performance criteria, on the acquisition of the Channel House Trust Group of companies (acquired 17 September 2005) up to a maximum of £5.0m.

(e) Further consideration may be due, dependent on certain performance criteria, on the acquisition of the Quay Software Solutions Limited (acquired 9 November 2005) up to a maximum of £5.0m.

32 Pensions

The Group operates both defined benefit and defined contribution pension schemes. These pension schemes are funded and the payments of contributions are made to separately administered trust funds. The assets of the pension schemes are held separately from the Group.

The pension charge for the defined contribution pension schemes for the year is £9.4m (2004: £9.1m).

There are two main defined benefit schemes where the Group is the sole employing sponsor: The Capita Pension and Life Assurance Scheme (Capita scheme) and The Eastgate Assistance Retirement Benefit Scheme (Eastgate scheme). Grouped together under 'other schemes' are smaller schemes where Capita is the sole employing sponsor; the Group also has allocated sections of 2 multi-employer schemes, in which the Group is a participating employer; and several schemes to which the Group makes contributions under admitted body status to our customers' defined benefit schemes in respect of certain TUPE employees.

For the three Admitted Body Schemes (Greater Gwent Pension Fund (Gwent), Cumbria Local Government Pension Scheme (Cumbria) and Lancashire County Pension Fund (Lancashire)), which are all part of the Local Government Pension Scheme, Capita Group will only participate in these schemes for a finite period up to the end of the contracts. Capita are required to pay regular contributions as decided by the Scheme Actuary and detailed in the schemes' Schedule of Contributions. In addition, for the Cumbria and Lancashire schemes, at the end of the contract Capita will be required to pay any *deficit (as determined by the Scheme Actuary) that is remaining for their notional section of the scheme.*

The assets and liabilities of the defined benefit schemes (excluding additional voluntary contributions) as at 31 December are:

At 31 December 2005	Capita scheme £m	Eastgate scheme £m	Other schemes £m	Group total £m
Scheme assets at fair value:				
Equities/Hedged funds/Absolute returns	**193.3**	**4.8**	**72.1**	**270.2**
Bonds	**66.3**	**1.2**	**27.6**	**95.1**
Property	**11.1**	**0.7**	**6.5**	**18.3**
Insured contracts	**–**	**2.9**	**0.5**	**3.4**
Other (cash)	**5.5**	**0.3**	**2.6**	**8.4**
Total	**276.2**	**9.9**	**109.3**	**395.4**
Present value of scheme liabilities	**(293.5)**	**(14.6)**	**(130.3)**	**(438.4)**
Net liability	**(17.3)**	**(4.7)**	**(21.0)**	**(43.0)**

At 31 December 2004	Capita scheme £m	Eastgate scheme £m	Other schemes £m	Group total £m
Scheme assets at fair value:				
Equities	134.4	3.5	54.5	192.4
Bonds	27.5	1.2	25.1	53.8
Property	1.7	0.6	5.0	7.3
Insured contracts	–	2.8	–	2.8
Other (cash)[1]	62.4	0.3	–	62.7
Total	226.0	8.4	84.6	319.0
Present value of scheme liabilities	(245.0)	(12.8)	(105.3)	(363.1)
Net liability	(19.0)	(4.4)	(20.7)	(44.1)

[1] This includes the special cash contribution of £50m made by the company to the Capita scheme in December 2004, which in 2005 was invested in line with the pension fund trustees' overall investment strategy.

The pension plans have not invested in any of the Group's own financial instruments nor in properties or other assets used by the Group.

32 Pensions (continued)

The amounts recognised in the consolidated income statement and in the consolidated statement of recognised income and expense for the year are analysed as follows:

Year ended 31 December 2005	Capita scheme £m	Eastgate scheme £m	Other schemes £m	Group total £m
Recognised in the income statement:				
Current service cost	9.4	0.3	2.4	12.1
Past service cost	1.2	–	–	1.2
Recognised in arriving at operating profit	10.6	0.3	2.4	13.3
Expected return on scheme assets	(15.1)	(0.5)	(5.6)	(21.2)
Interest cost on scheme liabilities	13.4	0.7	5.8	19.9
Net finance cost included in administrative expenses	(1.7)	0.2	0.2	(1.3)
Total defined benefit charge	*8.9*	*0.5*	*2.6*	*12.0*
Taken to the statement of recognised income and expense:				
Actual return on scheme assets	40.9	1.1	18.1	60.1
Less: expected return on scheme assets	(15.1)	(0.5)	(5.6)	(21.2)
	25.8	0.6	12.5	38.9
Other actuarial gains and losses	(28.1)	(1.2)	(13.1)	(42.4)
Actuarial gains and losses recognised in the statement of recognised income and expense	(2.3)	(0.6)	(0.6)	(3.5)

Year ended 31 December 2004	Capita scheme £m	Eastgate scheme £m	Other schemes £m	Group total £m
Recognised in the income statement:				
Current service cost	7.3	0.4	2.8	10.5
Past service cost	0.4	–	0.5	0.9
Recognised in arriving at operating profit	7.7	0.4	3.3	11.4
Expected return on scheme assets	(9.8)	(0.5)	(4.9)	(15.2)
Interest cost on scheme liabilities	11.1	0.7	5.1	16.9
Net finance cost included in administrative expenses	1.3	0.2	0.2	1.7
Total defined benefit charge	*9.0*	*0.6*	*3.5*	*13.1*
Taken to the statement of recognised income and expense:				
Actual return on scheme assets	12.4	0.5	7.9	20.8
Less: expected return on scheme assets	(9.8)	(0.5)	(4.9)	(15.2)
	2.6	–	3.0	5.6
Other actuarial gains and losses	(21.3)	0.7	(4.7)	(25.3)
Actuarial gains and losses recognised in the statement of recognised income and expense	(18.7)	0.7	(1.7)	(19.7)

32 Pensions (continued)

Pension contributions are determined with the advice of independent qualified actuaries. Full valuations of the Capita scheme and the FPS scheme are being carried out as at 6 April 2005 and 31 March 2005 respectively. A full valuation of the Eastgate scheme has been carried out as at 1 January 2003 (included within 'other schemes'). For the other schemes, the latest full valuations were carried out as at either 31 March 2004 or 1 April 2004. These valuations are updated by the actuaries at each balance sheet date. Scheme assets are stated at their market valuations at each respective balance sheet date and overall expected rates of return are established by considering published brokers' forecasts for each category of scheme assets.

	Capita scheme		Eastgate scheme		Other schemes	
Main assumptions:	2005 %	2004 %	2005 %	2004 %	2005 %	2004 %
Rate of price inflation	**2.70**	2.75	**2.70**	2.75	**2.70**	2.75
Rate of salary increase	**3.70**	3.75	**3.70**	3.75	**3.70**	3.75
Rate of increase of pensions in payment	**2.70**	2.75	**3.25**	3.25	**2.70**	2.75
Discount rate	**4.80**	5.40	**4.80**	5.25	**4.80**	5.40
Expected rates of return on scheme assets (net of scheme expenses):						
Equities/Hedged funds/Absolute returns	**7.00**	7.00	**7.00**	7.00	**7.00**	7.00
Bonds	**4.40**	5.00	**4.80**	4.00/4.75	**4.60**	5.00
Property	**6.60**	7.00	**6.60**	7.00	**7.00**	7.00
Insured contracts	**–**	–	**4.80**	5.25	**4.80**	–
Other (cash)	***6.30**	6.30	**4.50**	4.75	**4.50**	4.75
Post Retirement Mortality:						
– Current pensioners	PA92 MC (YOB=1935) *rated up 3 years*		90% of PA92(C=2020)		PA92 MC (YOB=1935) *rated up 3 years*	
– Future pensioners	PA92 MC (YOB=1965) rated up 3 years		90% of PA92(C=2020)		PA92 MC (YOB=1965) rated up 3 years	

*The return on assets for the 'Other (cash)' asset class is a weighted average of returns of cash at 4.5% and returns on other classes (Absolute Returns and Hedge Funds) at 6.6%.

The total employer contributions to the defined benefit plans in 2006 are expected to be £12.1m (2005: £12.9m) in respect of the Capita scheme, £0.8m (2005: £0.8m) in respect of the Eastgate scheme and £3.6m (2005: £2.9m) in respect of the Other schemes.

The service costs have been determined using the projected unit credit method, as required. As some of the sections are closed to new entrants, the service cost (expressed as a % of pensionable salaries) would be expected to increase as the average age of the membership increases.

Changes in the present value of the defined benefit pension obligations are analysed as follows:

	Capita scheme £m	*Eastgate* scheme £m	*Other* schemes £m	*Group* total £m
As at 1 January 2004	197.8	12.6	91.7	302.1
Current service cost	7.3	0.4	2.8	10.5
Past service cost	0.4	–	0.5	0.9
Interest cost	11.1	0.7	5.1	16.9
Benefits paid	(5.0)	(0.2)	(0.8)	(6.0)
Actuarial gains and losses	21.3	(0.7)	4.7	25.3
Contributions by employees	2.7	–	1.3	4.0
Contract bulk transfers/ business combinations	9.4	–	–	9.4
As at 31 December 2004	245.0	12.8	105.3	363.1
Current service cost	9.4	0.3	2.4	12.1
Past service cost	1.2	–	–	1.2
Interest cost	13.4	0.7	5.8	19.9
Benefits paid	(6.7)	(0.5)	(1.2)	(8.4)
Actuarial gains and losses	28.1	1.2	13.1	42.4
Contributions by employees	2.1	0.1	1.3	3.5
Contract bulk transfers/ business combinations	1.0	–	*3.6	4.6
As at 31 December 2005	**293.5**	**14.6**	**130.3**	**438.4**

The defined benefit obligation comprises £438.4m (2004: £363.1m) arising from plans that are wholly or partly funded.

32 Pensions (continued)

Changes in the fair value of plan assets are analysed as follows:

	Capita scheme £m	Eastgate scheme £m	Other schemes £m	Group total £m
As at 1 January 2004	144.0	7.4	72.9	224.3
Expected return on plan assets	9.8	0.5	4.9	15.2
Contract bulk transfers/ business combinations	9.4	–	–	9.4
Employer contributions	62.5	0.7	3.3	66.5
Contributions by employees	2.7	–	1.3	4.0
Benefits paid	(5.0)	(0.2)	(0.8)	(6.0)
Actuarial gains and losses	2.6	–	3.0	5.6
As at 31 December 2004	226.0	8.4	84.6	319.0
Expected return on plan assets	15.1	0.5	5.6	21.2
Contract bulk transfers/ business combinations	1.0	–	*3.6	4.6
Employer contributions	12.9	0.8	2.9	16.6
Contributions by employees	2.1	0.1	1.3	3.5
Benefits paid	(6.7)	(0.5)	(1.2)	(8.4)
Actuarial gains and losses	25.8	0.6	12.5	38.9
As at 31 December 2005	**276.2**	**9.9**	**109.3**	**395.4**

* The assets and liabilities for the FPS scheme, determined as at 1 September 2005 (i.e. the date Capita acquired FPS), are included as a business combination.

History of experience gains and losses:

	2005 £m	2004 £m	2003 £m
Capita scheme			
Fair value of scheme assets	**276.2**	226.0	144.0
Present value of defined benefit obligation	**(293.5)**	(245.0)	(197.8)
Scheme deficit	**(17.3)**	(19.0)	(53.8)
Experience adjustments arising on plan liabilities	**(28.1)**	(21.3)	
Experience adjustments arising on plan assets	**25.8**	2.6	
Eastgate scheme			
Fair value of scheme assets	**9.9**	8.4	7.4
Present value of defined benefit obligation	**(14.6)**	(12.8)	(12.6)
Scheme deficit	**(4.7)**	(4.4)	(5.2)
Experience adjustments arising on plan liabilities	**(1.2)**	0.7	
Experience adjustments arising on plan assets	**0.6**	–	
Other schemes			
Fair value of scheme assets	**109.3**	84.6	72.9
Present value of defined benefit obligation	**(130.3)**	(105.3)	(91.7)
Scheme deficit	**(21.0)**	(20.7)	(18.8)
Experience adjustments arising on plan liabilities	**(13.1)**	(4.7)	
Experience adjustments arising on plan assets	**12.5**	3.0	

The cumulative amount of actuarial losses recognised since 1 January 2004 in the consolidated statement of recognised income and expense is £23.4m (2004: £19.7m). The Directors are unable to determine how much of the pension scheme deficit recognised on transition to IFRS of £77.8m (of which an IFRS transitional adjustment of £67.7m was taken directly to equity) is attributable to actuarial gains and losses since inception of those pension schemes. Consequently, the Directors are unable to determine the amount of actuarial gains and losses that would have been recognised in the consolidated statement of recognised income and expense before 1 January 2004.

33 Related party transactions

Other than the information disclosed in the Directors' report and the Directors' remuneration report, the only other related party transactions requiring disclosure are details of key management personnel compensation. These details are set out in the table below.

Compensation of key management personnel (excluding Directors of parent company)

	2005 £m	2004 £m
Short term employment benefits	3.1	2.0
Post employment benefits	0.1	0.1
Share based payments	1.1	0.5
	4.3	2.6

Gains on share options exercised in the year by key management personnel totalled £0.4m (2004: £0.4m).

34 *Transition to IFRS*

For all periods up to and including the year ended 31 December 2004, the Group prepared its financial statements in accordance with United Kingdom generally accepted accounting practice (UK GAAP). As noted above in note 2, these financial statements, for the year ended 31 December 2005, are the first the Group is required to prepare in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

Accordingly, the Group has prepared financial statements which comply with IFRS applicable for periods beginning on or after 1 January 2005 and the significant accounting policies meeting those requirements are described in note 2. In preparing these financial statements the Group has started from an opening balance sheet as at 1 January 2004, the Group's date of transition to IFRS, and made those changes in accounting policies and other restatements as required by IFRS 1 for the first-time adoption of IFRS. This note explains the principal adjustments made by the Group in restating its UK GAAP balance sheet as at 1 January 2004 and its previously published UK GAAP financial statements for the year ended 31 December 2004.

IFRS 1 allows first-time adopters certain exemptions from the general requirement to apply IFRS as effective for December 2005 year-ends retrospectively. Details of the exemptions taken by the Group are set out in note 2.

Note that comparative information on financial instruments is prepared in accordance with UK GAAP and the Group has adopted IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' from 1 January 2005.

Accounting policies applied in the year ended 31 December 2004

As noted above, the Group has adopted IAS 32 and IAS 39 with effect from 1 January 2005 and, as permitted by IFRS 1, the Group has not restated comparative information. The new accounting policies as applied for the year ended 31 December 2005 are set out above in note 2. For accounting periods up to the year ended 31 December 2004 the following accounting policies were applied in respect of financial instruments in the financial statements of the Group:

Derivative financial instruments

The Group uses forward currency contracts to reduce exposure to foreign exchange rates. The Group also makes use of interest rate swaps to adjust interest rate exposures.

The Group considers its derivative instruments qualify for hedge accounting when certain criteria are met.

Forward foreign currency contracts

The criteria for forward foreign currency contracts are:

- the instrument must be related to a firm foreign currency commitment
- it must involve the same currency as the hedged item and
- it must reduce the risk of foreign currency exchange movements on the Group's operations.

The rates under such contracts are used to record the hedged item. As a result, gains and losses are offset against the foreign exchange gains and losses on the related financial assets and liabilities, or where the instrument is used to hedge a committed future transaction, are not recognised until the transaction occurs.

Interest rate swaps

The Group's criteria for interest rate swaps are:

- the instrument must be related to an asset or liability and
- it must change the character of the interest rate by converting a variable rate to a fixed rate or vice versa.

Interest differentials are recognised by accruing with net interest payable. Interest rate swaps are not revalued to fair value or shown on the Group balance sheet at the year end. If they are terminated early, the gain or loss is spread over the remaining maturity of the original instrument.

34 Transition to IFRS (continued)

Nature of the main adjustments to comply with IAS 32 and IAS 39

Had IAS 32 and IAS 39 been applied from 1 January 2004 the following adjustments would have been necessary in the financial statements for the year ended 31 December 2004. All derivatives would have been brought on to the balance sheet at fair value. The impact on the financial statements for the year ended 31 December 2004 would be as follows:

	UK GAAP 31 December 2004 £m	Adjustments to comply with IAS 32 and IAS 39 £m	Comparative had IAS 32 and IAS 39 been adopted at 31 December 2004 £m
Financial assets			
Interest rate swaps	–	1.4	1.4
Financial liabilities			
Bonds	(124.7)	1.7	(123.0)
Currency swaps	–	(3.1)	(3.1)
Retained earnings	–	–	–

Reconciliation of consolidated equity at 1 January 2004 (date of transition to IFRS)

	Notes	Previous GAAP £m	Client balances recognised £m	Proposed dividend £m	Recognise pension liability £m	Deferred taxation £m	IFRS £m
Property, plant and equipment		111.7	–	–	–	–	111.7
Intangible assets		451.2	–	–	–	–	451.2
Available-for-sale financial assets		5.2	–	–	–	–	5.2
Deferred taxation	1	1.6	–	–	–	25.4	27.0
Total non-current assets		569.7	–	–	–	25.4	595.1
Trade and other receivables		136.1	10.6	–	–	–	146.7
Prepayments		83.3	–	–	–	–	83.3
Cash and short term deposits		19.8	10.9	–	–	–	30.7
Total current assets		239.2	21.5	–	–	–	260.7
Total assets		808.9	21.5	–	–	25.4	855.8
Trade and other payables		95.0	21.5	–	–	–	116.5
Interest-bearing loans and borrowings		158.1	–	–	–	–	158.1
Employee benefits	2	10.1	–	–	67.7	–	77.8
Income tax payable		26.1	–	–	–	–	26.1
Proposed dividends	3	18.0	–	(18.0)	–	–	–
Accruals and deferred income		154.8	–	–	–	–	154.8
Provisions		4.6	–	–	–	–	4.6
Total liabilities		466.7	21.5	(18.0)	67.7	–	537.9
Total assets less total liabilities		342.2	–	18.0	(67.7)	25.4	317.9
Issued capital		13.3	–	–	–	–	13.3
Share premium		242.7	–	–	–	–	242.7
Capital redemption reserve		0.1	–	–	–	–	0.1
Retained earnings		86.0	–	18.0	(67.7)	25.4	61.7
Equity shareholders' funds		342.1	–	18.0	(67.7)	25.4	317.8
Minority interest		0.1	–	–	–	–	0.1
Total equity		342.2	–	18.0	(67.7)	25.4	317.9

34 Transition to IFRS (continued)

Reconciliation of consolidated equity at 31 December 2004 (end of last period presented under previous GAAP)

	Notes	Previous GAAP £m	Recognition of pension liability £m	Goodwill amortisation added back £m	Intangible assets and client balances recognised £m	Goodwill de-recognised £m	Amortisation of intangible assets £m	Proposed final dividend £m	Deferred taxation £m	IFRS £m
Property, plant and equipment		129.1	–	–	–	–	–	–	–	129.1
Intangible assets	1	470.2	–	29.3	10.1	(10.1)	(1.8)	–	2.5	500.2
Available-for-sale financial assets		0.2	–	–	–	–	–	–	–	0.2
Trade and other receivables		6.1	–	–	–	–	–	–	–	6.1
Deferred taxation	2	(0.9)	–	–	–	–	–	–	33.5	32.6
Total non-current assets		604.7	–	29.3	10.1	(10.1)	(1.8)	–	36.0	668.2
Trade and other receivables		144.3	–	–	17.3	–	–	–	–	161.6
Prepayments		98.7	–	–	–	–	–	–	–	98.7
Total current assets		243.0	–	–	17.3	–	–	–	–	260.3
Total assets		847.7	–	29.3	27.4	(10.1)	(1.8)	–	36.0	928.5
Trade and other payables		87.8	–	–	28.2	–	–	–	–	116.0
Interest-bearing loans and borrowings		152.0	–	–	–	–	–	–	–	152.0
Employee benefits	3	(43.5)	87.6	–	–	–	–	–	–	44.1
Income tax payable		28.4	–	–	–	–	–	–	–	28.4
Proposed dividends	4	23.8	–	–	–	–	–	(23.8)	–	–
Accruals and deferred income		196.1	–	–	–	–	–	–	–	196.1
Overdrafts		37.0	–	–	(10.9)	–	–	–	–	26.1
Provisions		5.5	–	–	–	–	–	–	–	5.5
Total liabilities		487.1	87.6	–	17.3	–	–	(23.8)	–	568.2
Total assets less total liabilities		360.6	(87.6)	29.3	10.1	(10.1)	(1.8)	23.8	36.0	360.3
Issued capital		13.4	–	–	–	–	–	–	–	13.4
Share premium		248.1	–	–	–	–	–	–	–	248.1
Treasury shares		(0.2)	–	–	–	–	–	–	–	(0.2)
Capital redemption reserve		0.1	–	–	–	–	–	–	–	0.1
Foreign currency translation		0.1	–	–	–	–	–	–	–	0.1
Retained earnings		98.7	(87.6)	29.3	–	–	(1.8)	23.8	36.0	98.4
Equity shareholders' funds		360.2	(87.6)	29.3	–	–	(1.8)	23.8	36.0	359.9
Minority interest		0.4	–	–	–	–	–	–	–	0.4
Total equity		360.6	(87.6)	29.3	–	–	(1.8)	23.8	36.0	360.3

34 Transition to IFRS (continued)

Reconciliation of consolidated profit for the year ended 31 December 2004

	Notes	Previous GAAP £m	Discontinued operations £m	De-recognition/ recognition of pension charge £m	Share based payment charge £m	Goodwill amortisation added back £m	Amortisation of intangible assets £m	Deferred taxation £m	IFRS £m
Continuing operations:									
Revenue		1,285.1	(2.9)	–	–	–	–	–	1,282.2
Cost of sales		958.6	(3.0)	–	–	–	–	–	955.6
Gross profit		326.5	0.1	–	–	–	–	–	326.6
Administrative expenses	1, 2, 3	195.7	(0.2)	(0.1)	4.7	(29.3)	1.8	–	172.6
Operating profit		130.8	0.3	0.1	(4.7)	29.3	(1.8)	–	154.0
Finance costs		(11.9)	–	–	–	–	–	–	(11.9)
Profit before tax		118.9	0.3	0.1	(4.7)	29.3	(1.8)	–	142.1
Income tax expense	4	(41.6)	–	–	–	–	–	2.2	(39.4)
Profit for the year from continuing operations		77.3	0.3	0.1	(4.7)	29.3	(1.8)	2.2	102.7
Discontinued operations:									
Loss on discontinued operations		(1.9)	(0.3)	–	–	–	–	–	(2.2)
Profit for the year		75.4	–	0.1	(4.7)	29.3	(1.8)	2.2	100.5
Attributable to:									
Equity holders of the parent		75.6	–	0.1	(4.7)	29.3	(1.8)	2.2	100.7
Minority interest		(0.2)	–	–	–	–	–	–	(0.2)
		75.4	–	0.1	(4.7)	29.3	(1.8)	2.2	100.5

		UK GAAP	IFRS adjustments	IFRS
Earnings per share	**– basic**	11.36p	3.77p	15.13p
	– diluted	11.21p	3.79p	15.00p
	– basic (excluding discontinued operations)	11.69p	3.74p	15.46p
	– diluted (excluding discontinued operations)	11.54p	3.76p	15.33p

Notes to the reconciliations

Notes to the reconciliation of consolidated equity at 1 January 2004:

1. Deferred taxation recognised.

2. As a first-time adopter of IFRS, the Group has taken advantage of the exception allowed under IFRS 1 not to apply full retrospective application of IAS 19 'Employee Benefits'. Accordingly, the Group has elected to recognise all cumulative actuarial gains and losses at the date of transition to IFRS. Consequently, the full pension liability of £77.8m at 1 January 2004 is recognised under IFRS but was not fully recognised under previous GAAP.

3. Proposed dividends are not recognised under IFRS thus the provision of £18.0m has been written back.

34 Transition to IFRS (continued)

Notes to the reconciliation of consolidated equity at 31 December 2004:

1. Goodwill amortisation under UK GAAP of £29.3m added back. £10.1m of separately identified intangible assets have been recognised in accordance with IFRS 3/IAS 38 (de-recognised in goodwill) as has the deferred taxation liability of £2.5m in relation to this. The deferred taxation liability recognised results in an equal and opposite entry in goodwill. Amortisation of these separately identifiable intangible assets of £1.8m has been charged to the income statement.
2. Deferred taxation recognised.
3. As noted above in the reconciliation of equity at 1 January 2004, the full pension liability of £44.1m at 31 December 2004 is recognised under IFRSs but was not fully recognised under previous GAAP.
4. Proposed dividends are not recognised under IFRS thus the provision of £23.8m has been written back.
5. One of the principal activities of Capita Financial Managers Limited (CFM) is to act as an authorised unit trust manager whereby funds are received on behalf of customers to be invested per instruction by CFM. The transfer of funds to purchase the units is not always done on the same business day. The Group's transition to IFRS has forced us to re-examine certain funds flow arrangements and we have reached the conclusion that this arrangement should be recorded gross on the Group's consolidated balance sheet. The impact for the 2004 closing balance sheet was to increase debtors, creditors and cash balance by £17.3m, £28.2m and £10.9m respectively. The equivalent balances on the 2005 closing balance sheet are £31.1m, £38.0m and £6.9m resulting in timing difference in cash outflow of £4.0m for the year.

Notes to the reconciliation of consolidated profit for the year ended 31 December 2004:

1. The change from accounting for the defined benefit pension schemes under UK GAAP to IFRS has resulted in a reduced charge of £0.1m.
2. Provision for share based payment of £4.7m is recognised under IFRS 2 but was not recognised under UK GAAP.
3. Goodwill amortisation under UK GAAP of £29.3m added back. Provision made for amortisation of £1.8m on separately identified intangibles.
4. Deferred taxation has been recognised.

Reconciliation of consolidated cash and cash equivalents for relevant periods:

1. No restated IFRS cash flow has been presented as there is no difference between the net cash flow presented under IFRSs and the net cash flow presented under the previous GAAP except for the item described in note 5 above.

Independent auditors' report to the shareholders of The Capita Group Plc

We have audited the Group financial statements of The Capita Group Plc for the year ended 31 December 2005 which comprise the consolidated income statement, the consolidated balance sheet, the consolidated cash flow statement, the consolidated statement of recognised income and expense and the related notes 1 to 34. These consolidated financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of The Capita Group Plc for the year ended 31 December 2005 and on the information in the Directors' remuneration report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

The Directors are responsible for preparing the Annual Report & Accounts and the consolidated financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRS) as adopted by the European Union as set out in the statement of Directors' responsibilities.

Our responsibility is to audit the consolidated financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the consolidated financial statements give a true and fair view and whether the consolidated financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors' report is not consistent with the consolidated financial statements, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Director's remuneration and other transactions is not disclosed.

We review whether the corporate governance procedures reflects the company's compliance with the 9 provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover 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 other information contained in the Annual Report & Accounts and consider whether it is consistent with the audited consolidated financial statements. The other information comprises only the Directors' report, the Chairman's statement, the business review and corporate governance. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the consolidated financial *statements. Our responsibilities do not extend to any other information.*

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the consolidated financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the consolidated 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 consolidated 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 consolidated *financial statements.*

Opinion

In our opinion the consolidated financial statements:

- give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the Group's affairs as at 31 December 2005 and of its profit for the year then ended and
- have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

As explained in note 2 to the consolidated financial statements, the Group in addition to complying with its legal obligation to comply with IFRS as adopted by the European Union, has also complied with the IFRS as issued by the International Accounting Standards Board.

In our opinion the consolidated financial statements give a true and fair view, in accordance with IFRS, of the state of the Group's affairs as at 31 December 2005 and of its profit for the year then ended.

Ernst & Young LLP

Ernst & Young LLP
Registered Auditor
London

22 February 2006

Five year summary

for the years ended 31 December	Reported under IFRS		Reported under UK GAAP		
Group balance sheet	*2005* £m	*2004* £m	*2003* £m	*2002 (restated)* £m	*2001* £m
Non-current assets	783.5	668.2	562.9	551.2	462.8
Current assets	343.8	260.3	248.7	202.5	155.4
	1,127.3	928.5	811.6	753.7	618.2
Liabilities	(726.4)	(562.7)	(452.0)	(419.1)	(315.6)
Provisions for liabilities and charges	(3.3)	(5.5)	(17.4)	(17.5)	(18.5)
	397.6	360.3	342.2	317.1	284.1
Capital and reserves	397.4	359.9	342.1	317.1	283.5
Minority interests	0.2	0.4	0.1	–	0.6
	397.6	360.3	342.2	317.1	284.1
Group profit and loss account					
Turnover	1,435.5	1,282.2	1,080.6	897.5	691.2
Profit before interest and intangible amortisation and share based payments	190.7	160.5	131.4	107.3	77.1
Other operating income	–	–	–	5.3	–
Net interest payable	(13.5)	(11.9)	(10.2)	(9.0)	(5.0)
Profit before taxation and intangible amortisation and share based payments	177.2	148.6	121.2	103.6	72.1
Intangible amortisation	(4.5)	(1.8)	(27.7)	(25.5)	(19.0)
Share based payments	(7.6)	(4.7)	–	–	–
Impairment	(12.0)	–			
Discontinued operations	–	(2.2)			
Taxation	(45.8)	(39.4)	(34.1)	(30.2)	(21.5)
Minority interests	0.2	0.2	(0.1)	–	–
Profit after taxation	107.5	100.7	59.3	47.9	31.6
Earnings per share (excluding intangible share based payments, amortisation impairment and other operating income)	19.44p	16.08p	13.04p	10.47p	7.70p
Earnings per share (including intangible share based payments, amortisation impairment and exceptional items)	16.28p	15.13p	8.89p	7.20p	4.80p
Dividend per ordinary share	7.00p	5.35p	4.00p	3.00p	2.25p

2001 figures have been restated for the impact of FRS19.

Company balance sheet

Company balance sheet
at 31 December 2005

	Notes	2005 £m	2004 as restated £m
Fixed assets			
Tangible assets	5	11.1	7.7
Investments	6	293.5	254.7
		304.6	262.4
Current assets			
Trade investments	6	0.1	0.1
Debtors due within 1 year	7	515.4	331.3
Debtors due after more than 1 year	7	–	0.1
		515.5	331.5
Creditors: amounts falling due within 1 year	8	134.9	62.1
Net current assets		380.6	269.4
Total assets		685.2	531.8
Creditors: amounts falling due after more than 1 year	8	220.1	147.4
Provisions for liabilities and charges	9	0.9	–
		464.2	384.4
Capital and reserves			
Called up share capital	10	13.4	13.4
Treasury shares	10	(0.4)	(0.2)
Share premium account	12	258.1	248.1
Capital redemption reserve	12	0.2	0.1
Merger reserve	12	44.6	44.6
Profit and loss account	12	148.3	78.4
		464.2	384.4

The accounts were approved by the Group Board on 22 February 2006 and signed on its behalf by:

R M Aldridge OBE
Executive Chairman

C M Hurst
Group Finance Director

Notes to the accounts

for the year ended 31 December 2005

1 Accounting policies

(a) Basis of preparation

The accounts are prepared under the historical cost convention and in accordance with applicable accounting standards. The accounts comply with the following new Financial Reporting Standards and Urgent Issues Task Force abstracts issued by the UK Accounting Standards Board.

FRS 20 – Share based payment This standard, which is mandatory for accounting periods beginning on or after 1 January 2005 for listed entities, requires that share based payments, measured at fair value, should be recognised as an expense. Accordingly, the company has recognised this expense in its profit and loss account for the year ended 31 December 2005 and has restated its profit and loss account for the prior year. The consolidated financial statements include the full disclosures of IFRS 2/FRS 20 for the Group.

FRS 21 – Events after the balance sheet date This standard, which is mandatory for accounting periods beginning on or after 1 January 2005, requires that dividends declared after the balance sheet date should not be reported as liabilities. The standard instead requires that proposed dividends should be disclosed in the notes to the accounts. Details are contained in note 10 to the accounts.

FRS 25 – Financial Instruments: Disclosure and presentation A separate note dealing with the disclosures of FRS 25 has not been presented as provided by paragraph 3C of FRS 25. The consolidated financial statements include the required disclosures of IAS 32 for the Group.

Further standards in force are listed below and where relevant the companies accounting policy has been adjusted:

FRS 23 – The effects of changes in foreign exchange rates
FRS 26 – Financial Instruments: Measurement
FRS 28 – Corresponding amounts

The following new standards have no impact on the company's financial statements:

FRS 22 – Earnings per share
FRS 24 – Financial reporting in hyperinflationary economies
FRS 27 – Life assurance
FRSSE – Financial reporting standard for smaller entities

A separate profit and loss account dealing with the results of the parent undertaking only has not been presented as provided by section 230 of the Companies Act 1985.

(b) Tangible fixed assets

Depreciation is provided on all tangible fixed assets, other than freehold land, at rates calculated to write off the cost on a straight-line basis over the expected useful lives of the assets concerned, as follows:

Computer equipment	3-10 years
Furniture, fixtures and equipment	4-5 years
Leasehold improvements	over the period of the lease

(c) Investments

Fixed asset investments are shown at cost, less provisions for impairment.

Investments held as current assets are stated at the lower of cost and net realisable value.

The carrying value of fixed asset investments are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

(d) Pension schemes

The company maintains a number of contracted-out defined contribution schemes and contributions are charged to the profit and loss account in the year in which they are due. These schemes are funded and the payment of contributions is made to separately administered trust funds. The assets of these schemes are held separately from the company. The company remits monthly pension contributions to Capita Business Services Limited, a subsidiary undertaking of the company, which pays the Group liability centrally. Any unpaid contributions at the year end have been accrued in the accounts of that company.

(e) Leasing commitments

Assets obtained under finance leases are capitalised in the balance sheet and depreciated over the shorter of the lease term and their useful economic lives.

The finance charges under finance leases and hire purchase contracts are allocated to accounting periods over the period of the lease and represent a constant proportion of the balance of capital repayments outstanding. Rentals due under operating leases are charged on a straight-line basis over the lease term.

1 Accounting policies (continued)

(f) Deferred taxation

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less or to receive more, taxation, with the following exceptions:

- provision is made for taxation on gains arising from the revaluation (and similar fair value adjustments) of fixed assets, and gains on disposal of fixed assets that have been rolled over into replacement assets, only to the extent that, at the balance sheet date, there is a binding agreement to dispose of the assets concerned. However, no provision is made where, on the basis of all available evidence at the balance sheet date, it is more likely than not that the taxable gain will be rolled over into replacement assets and charged to taxation only where the replacement assets are sold
- provision is made for deferred taxation that would arise on remittance of the retained earnings of overseas subsidiaries only to the extent that, at the balance sheet date, dividends have been accrued as receivable
- deferred taxation assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred taxation is measured on an undiscounted basis at the taxation rates that are expected to apply in the periods in which timing differences reverse, based on taxation rates and laws enacted or substantively enacted at the balance sheet date.

(g) Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward exchange contract. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date or if appropriate at the forward contract rate. All differences are taken to the profit and loss account with the exception of differences on foreign currency borrowings, to the extent that they are used to finance or provide a hedge against foreign equity investments, which are taken directly to reserves together with the exchange difference on the carrying amount of the related investments.

(h) National Insurance on share option gains

National Insurance on outstanding share options at the year end has been grossed up and shown as a provision and a receivable on the balance sheet.

(i) Derivative financial instruments

The company uses derivative financial instruments such as interest rate swaps and foreign currency contracts to hedge risks associated with interest and exchange rate fluctuations. Such derivative financial instruments are stated at fair value. The fair values of interest rate swaps and foreign currency contracts are determined by reference to market rates for similar instruments.

For the purpose of hedge accounting, hedges are classified as either: fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability; or cash flow hedges where they hedge exposure to variability in cash flows that is attributable to either a particular risk associated with a recognised asset or liability or a forecast transaction.

In relation to fair value hedges (e.g. fixed to floating interest rate swaps held as fair value hedges against fixed interest rate borrowings) which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the profit and loss account. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the profit and loss account. The company does not currently hold any cash flow hedges.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the profit and loss account.

(j) Share based payments

The company operates a number of executive and employee share schemes.

The cost equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the company (market conditions).

No expense in recognised for awards that do not ultimately vest, except for awards there vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, the number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity.

2 Deferred taxation

	2005 £m	2004 £m
The deferred taxation included in the balance sheet is as follows:		
Included in provisions and liabilities for charges	(0.9)	–
Accelerated capital allowances	(0.9)	–

3 Profit attributable to members of the parent undertaking

The profit after taxation dealt with in the accounts of the parent undertaking was £155.8m (2004: £61.7m).

4 Dividends

	2005 £m	2004 £m
Declared and paid during the year		
Ordinary shares (equity):		
Final for 2004 paid: 3.6p per share (2003: 2.7p per share)	24.0	18.0
Interim for 2005 paid 2.1p per share (2004: 1.75p per share)	14.0	11.6
	38.0	29.6
Proposed for approval at AGM (not recognised as a liability at 31 December)		
Ordinary shares (equity):		
Final for 2005: 4.9p per share (2004: 3.6p per share)	32.0	23.8

5 Tangible fixed assets

	Computer equipment £m	Furniture, fixtures and equipment £m	Short term leasehold improvements £m	Total £m
Cost				
1 January 2005	10.3	0.3	1.6	12.2
Additions	4.3	0.3	0.5	5.1
31 December 2005	14.6	0.6	2.1	17.3
Depreciation				
1 January 2005	3.2	0.3	1.0	4.5
Charge for year	1.4	0.1	0.2	1.7
31 December 2005	4.6	0.4	1.2	6.2
Net Book Value at:				
1 January 2005	7.1	–	0.6	7.7
31 December 2005	10.0	0.2	0.9	11.1

6 Investments

(a) Fixed asset investments

	Shares in subsidiary undertakings £m
Cost	
1 January 2005	254.7
Additions	**38.8**
31 December 2005	**293.5**

Principal investments	Country of registration and operation	Proportion of nominal value of issued shares held by the company	Description of shares held
Capita Business Services Limited	England	100%	Ordinary 1p shares
Equita Limited	England	100%	Ordinary 80p shares
Capita Trust Company Limited*	England	100%	Ordinary £1 shares
Capita Insurance Services Group Limited*	England	100%	Ordinary 10p shares
Capita Insurance Services Limited*	England	100%	Ordinary £1 shares
BDML Connect Limited*	England	100%	Ordinary £1 shares
Capita IRG Plc*	England	100%	Ordinary £1 shares
Capita Resourcing Limited*	England	100%	Ordinary £1 shares
Capita Symonds Limited*	England	100%	Ordinary £1 shares
Capita Gwent Consultancy Limited	England	51%	Ordinary 1p shares
Capita Life & Pensions Services Limited	England	100%	Ordinary £1 shares
Capita Life & Pensions Regulated Services Limited*	England	100%	Ordinary £1 shares
Capita Absence Management Services Limited	England	100%	Ordinary 2.5p shares

*Indirectly held

The activities of The Capita Group Plc undertakings are given on page 63.

(b) Trade investments

	£m
At 1 January and 31 December 2005	0.1

7 Debtors

Debtors due within one year	2005 £m	2004 £m
Trade debtors	–	2.3
Amounts owed by subsidiary undertakings	**478.6**	307.1
Taxation recoverable	**31.9**	17.7
Other debtors	**1.6**	1.2
Prepayments and accrued income	**3.3**	3.0
	515.4	331.3

Debtors due beyond one year	2005 £m	2004 £m
Prepayments and accrued income	–	0.1

8 Creditors

Amounts falling due within 1 year	2005 £m	2004 £m
Bank overdraft	117.8	47.5
Trade creditors	3.8	1.3
Other creditors	0.9	1.0
Unsecured loan notes	2.2	6.7
Other taxes and social security	0.3	0.1
Accruals and deferred income	6.9	3.6
Deferred consideration	3.0	1.9
	134.9	62.1

Amounts falling due after more than 1 year	2005 £m	2004 £m
Unsecured loan notes	20.5	20.5
Bonds	199.6	124.7
Deferred consideration	–	2.2
	220.1	147.4

The bank overdraft and the bonds are unsecured.

9 Provisions for liabilities and charges

	£m
At 1 January 2005	–
New provisions in the year	0.9
As at 31 December 2005	**0.9**

10 Share capital

	2005 Million	2004 Million	2005 £m	2004 £m
Authorised				
Ordinary shares of 2p each	1,000.0	1,000.0	20.0	20.0
Allotted, called up and fully paid				
Ordinary shares of 2p each				
At 1 January	670.9	666.6	13.4	13.3
Shares repurchased	(5.0)	(0.3)	(0.1)	–
Issued on exercise of share options	5.0	4.6	0.1	0.1
Issued on acquisition of subsidiary undertaking	0.1	–	–	–
At 31 December	671.0	670.9	13.4	13.4

On 8 November 2005, 0.1 million ordinary 2p shares with an aggregate nominal value of £1,300 were issued at £3.89 each pursuant to the acquisition of a subsidiary undertaking, Lonsdale Travel Limited.

During the year the company repurchased 5.0m ordinary 2p shares with an aggregate nominal value of £0.1m at a total cost of £18.7m for which it paid cash. The weighted average cost of each share was £3.73. These shares were cancelled.

During the year 5.0m ordinary 2p shares with an aggregate nominal value of £0.1m were issued under share option schemes for a total consideration of £9.9m.

Treasury shares

	2005 Million	2004 Million	2005 £m	2004 £m
Ordinary shares of 2p each				
At 1 January	8.6	–	0.2	–
Shares repurchased	8.3	8.6	0.2	0.2
At 31 December	16.9	8.6	0.4	0.2

During the year the company has repurchased 8.3m ordinary 2p shares with an aggregate nominal value of £0.1m to be held in treasury for which it paid cash. The weighted average cost of each share was £3.76 and the total consideration for these shares was £31.2m.

The company has an unexpired authority to repurchase up to 10% of its issued share capital.

11 Prior year adjustment

FRS 21 'Events after the balance sheet date', which is mandatory for accounting periods beginning on or after 1 January 2005, requires that dividends declared after the balance sheet date should not be reported as liabilities. The standard instead requires that proposed dividends should be disclosed in the notes to the accounts. Consequently, the proposed dividend for the year ended 31 December 2004 of £23.8m has been written back to retained earnings in 2004. Similarly, the proposed dividend for the year ended 31 December 2003 of £18.0m has been written back to retained earnings at 31 December 2003.

12 Reserves

Company	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Treasury shares £m	Profit and loss account £m
At 31 December 2004	248.1	0.1	44.6	(0.2)	54.6
Prior year adjustment – see note 11	–	–	–	–	23.8
At 1 January 2005 – as restated	248.1	0.1	44.6	(0.2)	78.4
Shares issued	10.0	–	–	–	–
Share transaction costs	–	–	–	–	(0.3)
Share repurchase and cancellation	–	0.1	–	–	(18.6)
Share repurchase into treasury	–	–	–	(0.2)	(30.8)
Share based payments	–	–	–	–	1.8
Retained profit for the year	–	–	–	–	117.8
At 31 December 2005	**258.1**	**0.2**	**44.6**	**(0.4)**	**148.3**

13 Reconciliation of movements in shareholders' funds

	2005 £m	2004 £m
Total recognised gains and losses	**155.8**	62.6
Prior year adjustment – share based payment	–	(0.9)
Dividends	**(38.0)**	(29.6)
	117.8	32.1
Share based payment	**1.8**	0.9
Shares issued	**10.1**	5.5
Share transaction costs	(0.3)	(0.2)
Shares purchased	(49.6)	(27.5)
Net movement in shareholders' funds	**79.8**	10.8
Opening shareholders' funds as previously stated	**384.4**	355.6
Prior year adjustment – see note 11	–	18.0
Opening shareholders' funds as restated	**384.4**	373.6
Closing shareholders' funds	**464.2**	384.4

14 Commitments and contingent liabilities

(a) Annual commitments under operating leases were as follows:

	2005		2004	
	Property £m	Other £m	Property £m	Other £m
Operating leases which expire:	–			
Within 1 year	–	–	0.1	–
In second to fifth year inclusive	–	**0.2**	–	0.2
Over 5 years from the balance sheet date	1.2	–	1.2	–
	1.2	**0.2**	1.3	0.2

(b) The company has guaranteed overdraft and loan facilities of Group undertakings amounting to £212.3m (2004: £175.0m). Capita Business Services Limited, Equita Limited, Capita Gwent Consultancy Limited and Capita IRG Trustees Limited have provided, in the normal course of their businesses, performance bonds of £3.3m (2004: £5.5m), £0.5m (2004: £2.0m), £nil (2004: £0.5m), and £0.3m (2004: £0.4m) respectively. The following companies have provided indemnities in the normal course of business: Capita Symonds Limited £10.0m (2004: £4.0), Capita Business Services Limited £0.5m (2004: £0.5m), Capita Insurance Services Group Limited £nil (2004: £0.8m), Capita IRG Plc £nil (2004: £0.9m) and The Capita Group Plc £nil (2004: £0.5m).

(c) Further consideration may be due, dependent on certain performance criteria, on the acquisition of the Channel House Financial Services Group Limited (acquired 17 September 2005) up to a maximum of £5.0m.

15 Borrowings and finance leases

	2005 £m	2004 £m
Bank overdraft payable on demand	**117.8**	47.5
Loan notes	**22.7**	27.1
Bonds	**199.6**	124.7
	340.1	199.3
Repayments fall due as follows:		
Within 1 year:		
Bank overdraft	**117.8**	47.5
Loan notes	**2.2**	6.6
	120.0	54.1
After more than 1 year:		
In more than 1 year but not more than 2 years	**20.5**	20.5
In more than 2 years but not more than 5 years	**100.1**	100.1
In more than 5 years	**99.5**	24.6
	220.1	145.2
Total borrowings and finance leases	**340.1**	199.3

Loan notes were issued pursuant to the satisfaction of consideration due in relation to the acquisition of a subsidiary undertaking.

During the year the company issued a further £75m of bonds with maturity dates of £50m on 28 September 2013 and £25m on 28 September 2015 with an interest rate set at 0.525% above six month LIBOR.

The previous bond issue was in the form of £55m sterling, and US Dollars amounts of $66m and $36m. These issues mature on 20 June 2009, 20 June 2009, and 20 June 2012 and are issued at interest rates of 6.44%, 6.1% and 6.47% respectively. The company entered into cross currency swaps for the US dollar issues (swapping the $66m and $36m bonds into a sterling denominated long term loan of £70m) and an interest rate swap for the sterling issue, the maturity dates being the same as for the issues themselves. Issue costs incurred were £0.5m and these are being spread over the life of the bonds to their maturity. The effect of this interest rate swap is to convert the interest cost on the bond to 6 month LIBOR plus 1%.

16 Acquisitions

During the year the company acquired 100% of the ordinary share capital of Randall Lyons Limited, Lonsdale Limited and BMI Health Solutions Limited for an aggregate consideration satisfied by cash paid of £24.7m and the issue of shares. The company paid further consideration in cash of £14.1m in respect of previous acquisitions.

17 Related party transactions

There were no related party transactions that require disclosure in the year.

18 Pension costs

The company operates a defined contribution scheme.

The pension charge for the defined contribution scheme for the year was £0.6m (2004: £0.4m).

19 Share based payments

The total company expense charged to the profit and loss account in respect of FRS 20 'Share based payment' was £1.8m (2004: £0.9m).

Principal Group investments

Principal Group Investments

Capita Business Services
Providing an integrated range of white collar professional services across the UK including professional support services, transport management services, customer and administrative services, consultancy, IT and software services, printing services and human resource provision.

Capita Insurance Services Group (including subsidiary BDML Connect)
Market leader in providing outsourced administration and support services to the general insurance sector and affinity partnerships.

Equita
Professional debt recovery and certified bailiff services.

Capita Symonds
Providing a comprehensive range of project management, telecommunications engineering and construction related consultancy services.

Capita IRG
Share registration and employee share scheme administration services.

Capita Trust Company
Corporate trustees and providers of trust and administration services.

Sector Treasury Services
Provision of treasury and financial management advisory services primarily to public sector organisations.

Cost Auditing
A leading provider of legal-cost auditing services to the Insurance Services sector.

Capita Absence Management Services
The UK's leading provider of staff absence and associated cost management services to the state education sector.

Capita Life and Pensions
Administration and customer services for life & pensions operations.

Capita Life & Pensions Regulated Services
Administration and customer services for life & pensions regulated operations.

Capita Gwent Consultancy Services
Major supplier of civil engineering, transportation and environmental consultancy advice to public and private sector clients.

Capita Resourcing
Employee recruitment services.

Independent auditors' report to the members of The Capita Group Plc

We have audited the parent company financial statements of The Capita Group Plc for the year ended 31 December 2005 which comprise the Balance Sheet and the related notes 1 to 19. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Group financial statements of The Capita Group Plc for the year ended 31 December 2005.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors
The Directors are responsible for preparing the Annual Report & Accounts, the Directors' remuneration report and the parent company financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) as set out in the statement of Directors' responsibilities.

Our responsibility is to audit the parent company financial statements and the part of the Directors' remuneration report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the Directors' remuneration report to be audited have been 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 parent company 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 regarding Directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the Directors' report, the unaudited part of the Directors' remuneration report, the Chairman's statement and the business review. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent company financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the parent company financial statements, and of whether the accounting policies are appropriate to the company'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 parent company financial statements and the part of the Directors' remuneration report to be audited 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 parent company financial statements and the part of the Directors' remuneration report to be audited.

Opinion
In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2005 and
- the parent company financial statements and the part of the Directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP

Ernst & Young LLP
Registered Auditor
London

22 February 2006

Useful information for shareholders

Shareholder enquiries
Shareholders who have questions relating to the Group's business or wish to receive further copies of Annual or Interim reports should contact Capita's investor relations team on 020 7799 1525 or email corporate@capita.co.uk.

If you have any queries about your shareholding please contact the company's registrar, Capita Registrars, at the address below.

Capita Registrars
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

Tel: 0870 162 3100
email: ssd@capitaregistrars.com

Shareholder portal
The registrar has developed a Shareholder Portal for Capita shareholders. By registering on the site www.capitashares.co.uk shareholders can view their account online, make changes to their account details, or access a range of additional shareholder services.

Share dealing
A quick and easy share dealing service is now available for existing Capita shareholders to either sell or buy more Capita Group shares on-line or by telephone.

For further information on this service or to buy and sell Capita shares online go to:

www.capitadeal.com
or by telephone:
0870 458 4577

eCommunications for shareholders
Capita have teamed up with Capita Registrars and Climate Care to help combat climate change by providing shareholders with the opportunity to receive communications from us electronically. If you are a shareholder – join our campaign and help save trees. We have also pledged to donate £1 to Climate Care for every shareholder that registers for e-communications. By registering your email address, you will receive emails with a web link to information posted on our website. This can include our report and accounts, notice of meetings and other information we communicate to our shareholders.

Visit our website at www.capitashares.co.uk to register for this service.

For more information on climate change, please visit www.climatecare.org.

Financial calendar
Annual General Meeting
25 April 2006

Final Dividend payment
5 May 2006

Interim results
20 July 2006

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Registered number: 2081330

Company Secretary
Gordon Hurst

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33 Canada Square
Canary Wharf
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National Westminster Bank Plc
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Further information

You can find out more information about Capita on our website www.capita.co.uk. Alternatively contact us by email corporate@capita.co.uk.