Balfour Beatty plc
Annual report and accounts 2005

BALFOUR BEATTY:
CREATE CARE

The year in brief

Highlights of the year

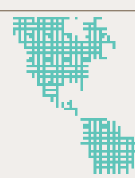
- Strong growth in comparable pre-tax profits
- Strong operating cash performance
- Adjusted earnings per share growth impacted by increased tax charge
- Full year dividend increased by 23%
- Order book at record £7.6bn
- Three PPP concessions reach financial close
- US civil engineering returns to profit

Balfour Beatty is a world-class engineering, construction and services group, well positioned in infrastructure markets which offer significant long-term growth potential. We seek to operate safely and sustainably.

Financial summary

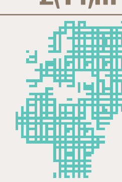
	2005	Pro forma† 2004	Percentage Increase/decrease	2004
Revenue including joint ventures and associates	**£4,938m**	£4,239m	16%	£4,239m
Pre-tax profit from continuing operations				
– before exceptional items	**£134m**	£107m	25%	£122m
– after exceptional items	**£141m**	£106m	33%	£120m
Earnings per share				
– adjusted*	**24.1p**	22.1p	9%	22.5p
– basic	**24.9p**	58.7p	(58)%	57.4p
Financing				
– net cash before PFI/PPP subsidiaries (non-recourse)	**£315m**	£311m		£311m
– net borrowings of PFI/PPP subsidiaries (non-recourse)	**£(14)m**	£(244)m		£(244)m

Revenue by destination



US
£480m

Central and South America
£46m



UK
£3,728m

Europe
£288m

Africa, Middle East, Near East
£138m

Asia Pacific
£258m

* before exceptional items and the premium arising on the buy-back of preference shares, and including the results of discontinued operations.

† including the impact of IAS 32 and IAS 39 on 2004 numbers.

Contents:

WE WORK IN PARTNERSHIP WITH SOPHISTICATED CUSTOMERS WHO VALUE THE HIGHEST LEVELS OF QUALITY, SAFETY AND TECHNICAL EXPERTISE. OUR SKILLS ARE APPLIED IN APPROPRIATE COMBINATION TO MEET INDIVIDUAL CUSTOMER NEEDS.

PLAN PROGRAMME UPGRADE

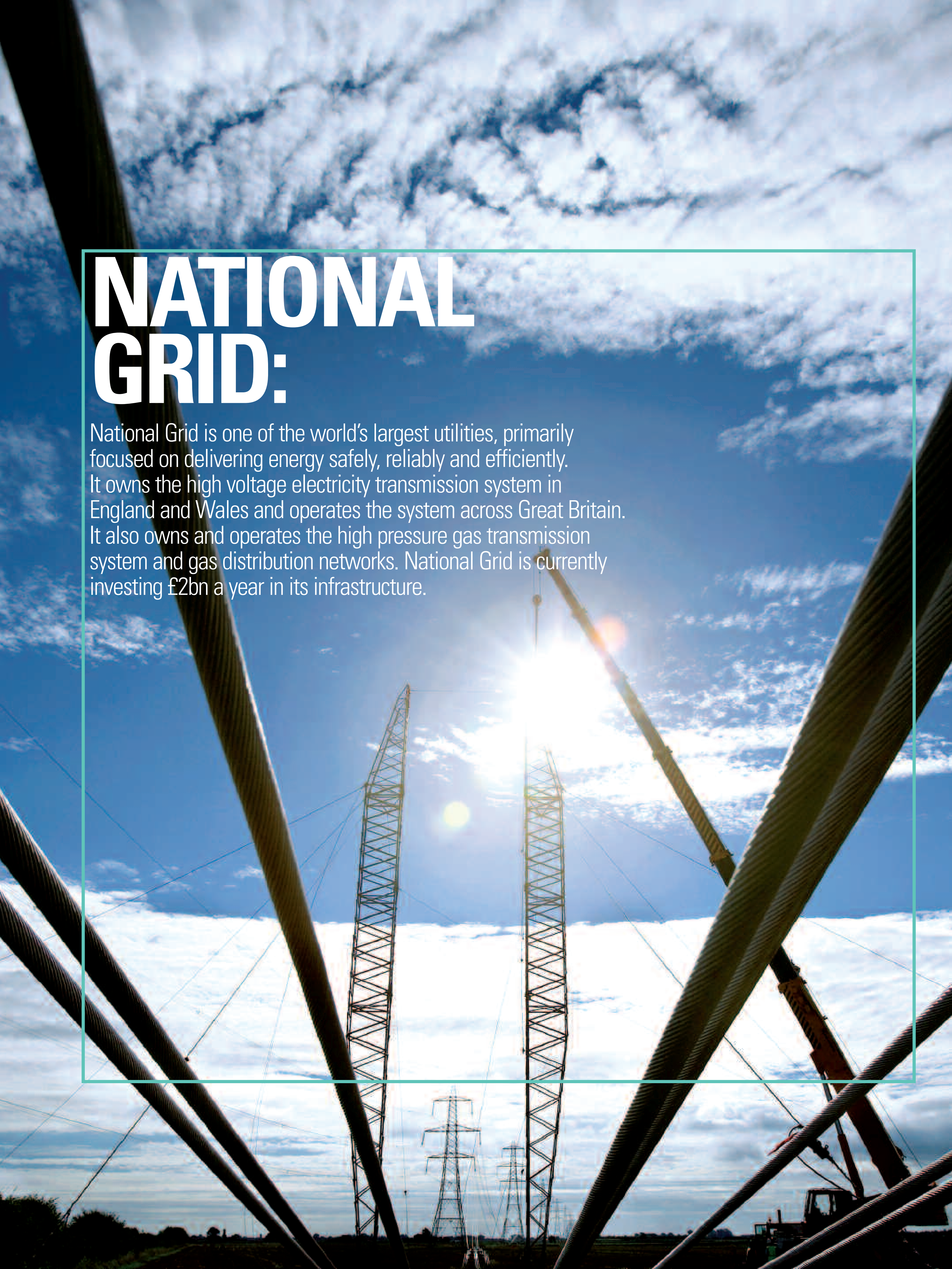
Balfour Beatty is a key partner to National Grid in upgrading and enhancing both its electricity and gas infrastructure.

We are delivering a complete power capability including design, planning, engineering, construction, erection and commissioning for overhead transmission lines, underground cabling systems and distribution networks on a range of major network projects.

In gas, we are delivering project design, project management and construction, installation and maintenance services as a long-term partner in National Grid's 30-year gas mains network replacement and abandonment programme.

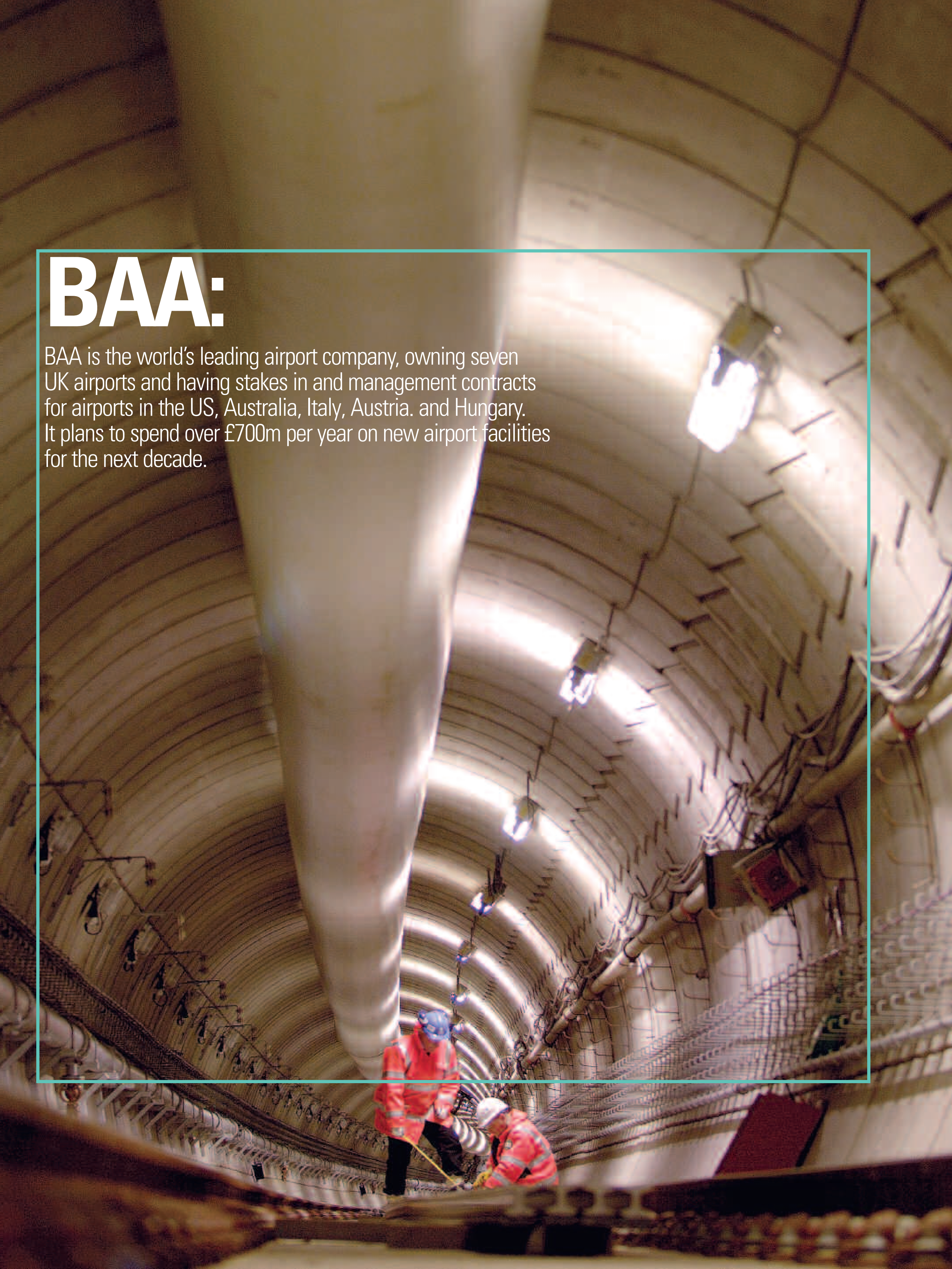
NATIONAL GRID:

National Grid is one of the world's largest utilities, primarily focused on delivering energy safely, reliably and efficiently. It owns the high voltage electricity transmission system in England and Wales and operates the system across Great Britain. It also owns and operates the high pressure gas transmission system and gas distribution networks. National Grid is currently investing £2bn a year in its infrastructure.



BAA:

BAA is the world's leading airport company, owning seven UK airports and having stakes in and management contracts for airports in the US, Australia, Italy, Austria. and Hungary. It plans to spend over £700m per year on new airport facilities for the next decade.

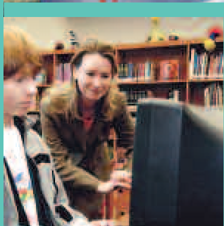


Balfour Beatty is a major partner to BAA in developing and maintaining its airport infrastructure and facilities. We are responsible for some £450m engineering work at Heathrow Terminal 5, including the rail systems for the Heathrow Express and the Piccadilly Line extension, the station construction, project management and electrical and mechanical services and the track transit system. We also maintain BAA's Scottish airports and the Heathrow Express and have made major contributions to the expansion of airports at Glasgow, Edinburgh, Stansted and Aberdeen.

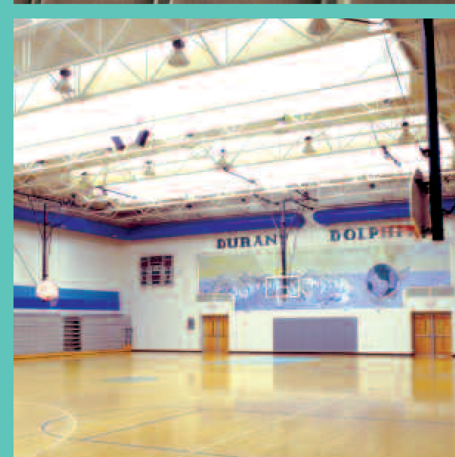
INTEGRATE DESIGN MANAGE

Heery has been a partner to Wake County Public Schools system for almost 20 years, delivering 61 new schools and undertaking 375 extensions, renovations and replacement projects as part of a $2.3bn building programme. Heery's contribution includes full-scope programme management, facility master planning and facility move management.

The relationship has now expanded to include construction management services for one new and one renovated high school in projects with a combined value of over $70m.



DEVELOP INNOVATE BUILD



WAKE COUNTY:

The Wake County Public School system in Raleigh, North Carolina is experiencing a massive population boom. Student numbers have doubled since 1985 and will double again in the next 20 years. Despite the pressures of growth it is a US national role model, aiming for 95% of its students to perform at or above grade level.

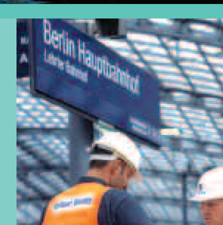
DEUTSCHE BAHN:

Deutsche Bahn is Europe's largest railway company, running 30,000 passenger trains and 5,500 cargo trains every day. It is expected to invest £3.5bn in network maintenance and new infrastructure in 2006.

Balfour Beatty is a strategic partner to Deutsche Bahn in developing and upgrading its fixed infrastructure.

We deliver system studies and design, product supply, project management, system installation and commissioning for catenary systems, power supply systems, network controls, signalling and auxiliary power systems.

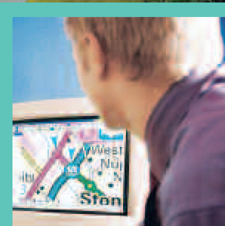
Recent projects include the high speed line between Nuremberg and Ingolstadt, the Berlin North – South connection and multi-disciplinary project management for the Rostock to Berlin line.



ENGINEER INSTALL COMMISSION

Balfour Beatty is a partner to the Highways Agency in a number of its key programmes. It is responsible for motorway and trunk road management and maintenance across the South of England from the Kent Coast to the West Country. It is a leading road builder, with a successful track record in major project works, including public private partnerships in Devon, Dorset, Derbyshire and Yorkshire. It is also the UK's leading specialist road widener.

With six awarded projects, Balfour Beatty is the leader in helping the Agency to pioneer the concept of Early Contractor Involvement, through which the benefits of innovation, better risk management and effective forward planning of work programmes and resources are maximised.



CONSTRUCT ENHANCE MAINTAIN

THE HIGHWAYS AGENCY:

The Highways Agency is responsible for operating, maintaining and improving the strategic road network in England. Its current business plan indicates expenditure of more than £5bn on capital investment and maintenance over the next three years.

The Company continued to make very satisfactory progress during 2005. We remain committed to the continuous improvement of all aspects of our performance as a business.

The Company in 2005

I am pleased to say that the Company continued to make very satisfactory progress during 2005. Profits and earnings moved ahead. Operating cash flows were strong and fully backed our profits. Our balance sheet is strong. Our order books continued to expand.

The proportion of our business deriving from long-term partnerships and alliances with major customers who rely on us for an increasing range and depth of expertise continued to grow. As a result, our revenues and profits are becoming more sustainable and have better long-term forward visibility.

Our performance in non-financial terms also showed significant improvements. Our accident frequency rate fell to a new low. Our measures to reduce our contribution to global warming, our generation of waste and our energy consumption all showed the positive signs of the close management attention which they receive. Our fifth Safety, Environment and Social Report will be published in May.

Although the beginning of the year marked a change in Chief Executive, there has been no deviation from our core principles. We remain careful in our selection of what to bid and how to bid it; proud of our first-class project management, the quality of our engineering judgements and our general attention to detail. We continue to focus very closely on the management of cash.

We are, as a group, very much aware of the full range of responsibilities which we have in running and growing our business. In 2005, we restated and recommunicated our core principles and the commitments we make to all our stakeholders. We also made clear what is expected of both individual employees and our operating companies in terms of their responsibilities and behaviour.

We continued to make progress in the quality of our risk management. Our everyday currency is in identifying, mitigating, pricing and managing risks of all shapes and sizes. We continue to improve in this respect.

It was gratifying to be voted the most admired contruction company in the 2005 Management Today survey and to be the 20th most admired quoted company overall in the UK.

Strategy

We service markets which are largely conditioned by GDP growth rates. In order to grow our business at rates acceptable to our shareholders, we need both a clear picture of our own strengths and key differentiators and the financial flexibility to take opportunities to change and develop the business mix so as to lead in superior growth markets.

In conjunction with the new Chief Executive, and senior Group management, the Board's principal focus this year has been a major strategic review. This has not been an exercise in blue-sky thinking, but a thorough, detailed analysis of what makes us successful and in which business areas we should be concentrating our financial and management capital. Ian Tyler describes the principal outcomes of this exercise in his Chief Executive's Review.

I believe the review has given us a clear way forward and will help ensure we continue to deliver shareholder value growth.

The Board

In December, Group Managing Director, Alistair Wivell, CBE, retired from the Board and the Company after 42 years' service to the Group. He made an enormous contribution to Balfour Beatty and we thank him sincerely for his efforts and offer him every good wish for his retirement.

During the year, both Richard Delbridge and Sir David Wright also announced their retirement as non-executive Directors. Both made a substantial contribution to the affairs of the Group and leave with both our thanks and our good wishes.

Steven Marshall joined the Board as a non-executive Director on 1 November 2005. Steven has held board positions in three major PLCs and has extensive senior management experience at three others. He brings comprehensive experience both as an executive and non-executive director and is thoroughly familiar with construction and support services.

The particular areas of expertise of each of the Directors is shown on pages 38 and 39 and in the Directors' Report.

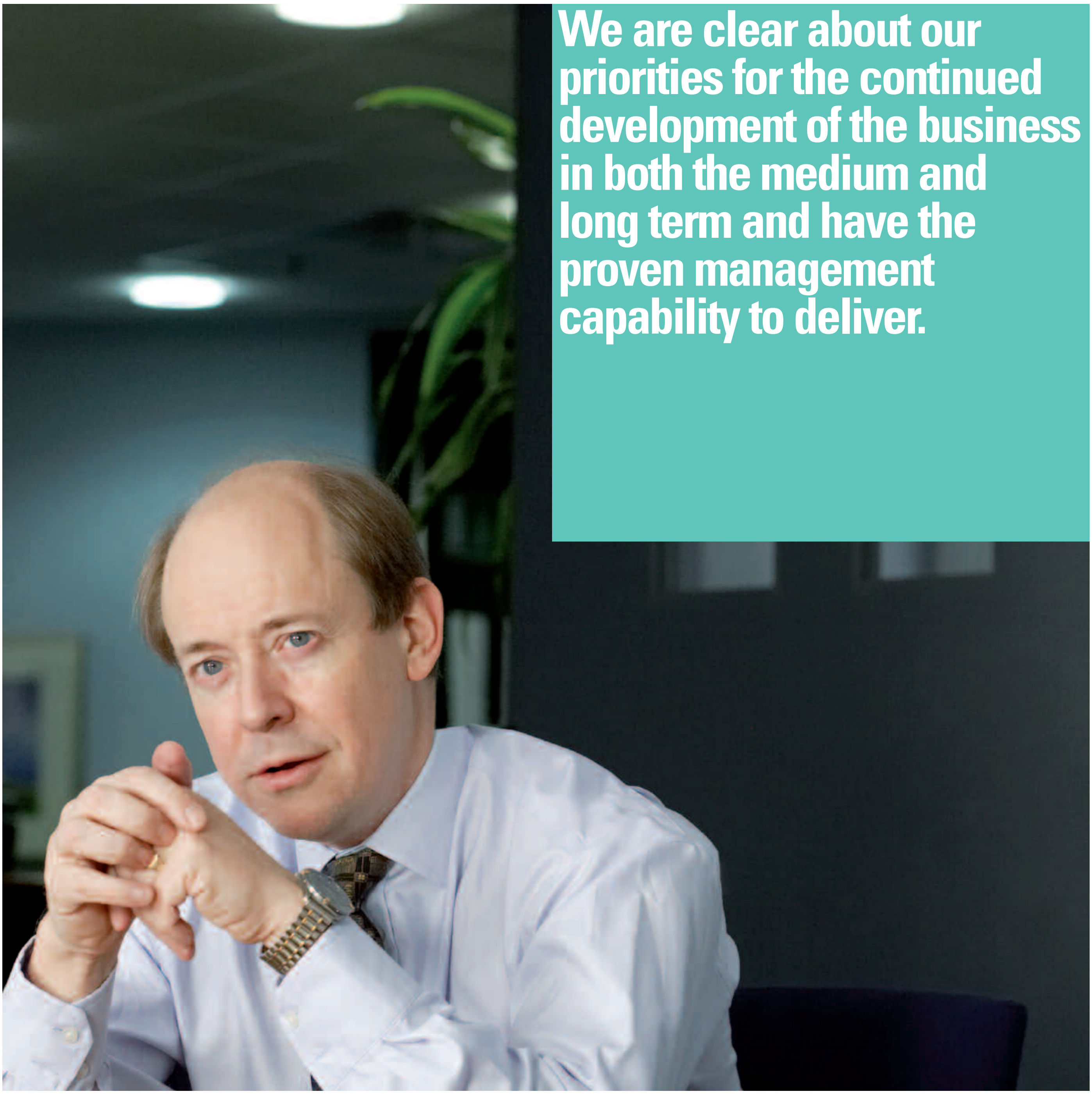
People

Our continued leadership in infrastructure markets depends on our ability to recruit, retain and motivate the best people. This year, we have thoroughly updated our succession plan and are improving our recruitment and rentention methods to ensure we can continue to meet the challenge of growth. We have a strong cadre of talented, highly motivated employees upon whose efforts the success of the business rests. I am sure that, once again, shareholders will wish to join me in thanking all of our people for their efforts and achievements in 2005.

The future

We remain committed to the continuous improvement of all aspects of our performance as a business. We believe that shareholder value will continue to grow in 2006.

Sir David John KCMG Chairman



We are clear about our priorities for the continued development of the business in both the medium and long term and have the proven management capability to deliver.

Financial results

In 2005, pre-tax profits from continuing operations before exceptional items rose by 25% to £134m (2004: £107m*). Revenue, including the Group's share of joint ventures and associates, was up by 16% at £4,938m (2004: £4,239m).

Adjusted earnings per share before exceptional items rose by 9% to 24.1p (2004: 22.1p*), reflecting an increased tax charge following Advance Corporation Tax credits in 2004. Basic earnings per share stood at 24.9p.

There were a number of exceptional items, resulting in a net exceptional profit of £4m.

Profit for the year (after tax and exceptional items) amounted to £106m. In 2004, the comparable figure of £246m* included a £160m profit from the sale of Andover Controls.

Operating cash flow was, once again, strong and in line with profits. Year-end net cash stood at £315m (2004: £311m), before taking account of the consolidation of £14m non-recourse net debt (2004: £244m) held in PPP/PFI subsidiaries.

The year-end order book increased by 12% to £7.6bn (2004: £6.8bn), with well in excess of £1bn of further work at preferred bidder stage.

The Board recommends a final dividend increased by 23% to 4.6p (2004: 3.75p) per ordinary share, making a total dividend for the year of 8.1p (2004: 6.6p).

Sector performance

Building, Building Management and Services

Profit from operations, before exceptional items, in this sector improved by 3% to £35m (2004: £34m). There was another good performance from Mansell and satisfactory progress in other operating companies, including Balfour Beatty Construction, whose profits recovered strongly in the second half of the year following some contract losses in the first half largely as a result of exceptional raw material cost inflation between contract and project execution.

We continued to add to our order book with good-quality work, including major PPP schools projects in Scotland and Nottinghamshire, social housing and office accommodation contracts and major mechanical and electrical works in the public and private sectors.

The first phases of University College London Hospital and Blackburn Hospital were handed over on time and progress was good on all major schemes.

Civil and Specialist Engineering and Services

Profit from operations, before exceptional items, in this sector more than tripled to £49m (2004: £16m). This excellent performance reflected the return to profit of our US civil engineering business as well as good progress elsewhere, particularly in RCS, the road manager and maintainer, and Balfour Beatty Power Networks.

Order books grew substantially, with a number of major contract wins in the gas and water sectors for Balfour Beatty Utilities. These included the contract to renew all the gas mains in Greater Manchester for National Grid and major new contracts and contract renewals for Anglian Water, United Utilities, Severn Trent Water, Yorkshire Water and South West Water.

There were other major wins for road maintenance in Scotland and Essex, the A421 road scheme in Bedfordshire and infrastructure work for Gammon in Hong Kong, including a major portion of the new Kowloon Southern Rail Link and the Venetian Hotel and Casino complex in Macau.

Rail Engineering and Services

Profit from operations, before exceptional items, in this sector fell by 27% to £32m (2004: £44m). Performance was affected by the loss of rail maintenance profits arising from Network Rail's decision to take this discipline in-house in 2004. The fine incurred by Balfour Beatty Rail Infrastructure Services in respect of the Hatfield rail accident of 2000, following its plea of guilty to charges under the Health and Safety at Work Act, was provided for in previous years.

In the UK, otherwise, performance was steady, helped by settlement income on old renewals contracts and good progress on the West Coast Main Line, London Underground track renewals and work at Heathrow Terminal 5. Performance improved in Germany, where the major electrification project from Ingolstadt to Nuremberg and the Berlin Tunnel contract were completed, and continued to be good in Italy. There were, however, continued difficulties on a major signalling contract in the US and further losses have been sustained.

The order book was augmented by new contract wins on the West Coast Main Line electrification programme in the UK and for a major rail link in Australia. Activity levels under major track renewal contracts for Network Rail and under the London Underground PPP were satisfactory.

* including the impact of IAS 32 and IAS 39 on 2004 numbers

Investments and Developments
Profit from operations, before exceptional items, in this sector improved by 18% to £20m (2004: £17m). After taking into account PFI/PPP net finance income and subordinated debt interest income, profits stood at £42m (2004: £42m).

Operating concession performance was satisfactory. During 2005, new concessions came on stream for the M77/GSO in Scotland, major schools schemes in North Lanarkshire and Bassetlaw, Nottinghamshire, and the South Tyneside street lighting scheme. We anticipate that our £521m hospital scheme in Birmingham will reach financial close in the near future. Preferred bidder status was achieved for the Pinderfields and Pontefract and Northern Batched hospitals schemes.

The operational performance of Metronet was broadly satisfactory. Detailed plans are in hand to address the delays which have occurred on some aspects of the capital expenditure programme, most particularly in stations upgrade. We are at a preliminary stage of this very complex, long-term project. There will, inevitably, be many challenges for Metronet to address in conjunction with London Underground as the scope of the major system upgrades becomes clearer.

Barking Power performed strongly with excellent availability and strong open market electricity prices.

In two separate transactions, the Group's shareholding in Consort's Edinburgh Royal Infirmary PFI concession was increased from 42.5% to 73.9% and a 15% interest in three of Connect Roads' projects, previously 100% owned, was sold.

For the first time, we have produced a Directors' valuation of the Group's PFI portfolio, based largely on a discounted cash flow methodology. At a blended average discount rate of 8.2%, the valuation at 31 December 2005 was £289m (2004: £243m).

Exceptional items
There was a net exceptional profit of £4m. Balfour Beatty's share of the distributions made by the administrators of TXU in respect of Barking Power Ltd and a gain on the sale of a 15% interest in three of Connect Roads' PFI concessions were partially offset by the costs of settlement of a legacy legal issue in the US; an adjustment to the carrying value of our interest in Romec; a goodwill impairment charge in respect of Balfour Beatty Rail Inc; exceptional finance costs in respect of retirement of fixed rate debt and the purchase of preference shares; and tax on exceptional items.

Strategic priorities
The Board and management of Balfour Beatty are committed to continue to deliver the reliable, responsible growth which our shareholders have enjoyed over recent years. During 2005, we have undertaken an in-depth analysis of our current business and established a clear strategic context for the future development of the Group.

We are confident that, in the short term, appropriate growth will be delivered from the momentum inherent in our existing mix of businesses. However, double digit compound growth is not an inherent characteristic of most of our markets, which grow in line with GDP at 2 – 4%. To secure medium and longer-term growth at our target levels, we will develop further in areas adjacent to our existing areas of core capability.

Our analysis clearly demonstrates that market leadership is critical to sustained success. We have positions of leadership in many of our markets, excellent people, a strong portfolio of long-term customer relationships, well-developed supply chains and a very substantial order book – a powerful basis on which to build. We also have the cash resources to invest in growth and to ensure that we continue to have a dynamic organisation.

UK infrastructure
The majority of the businesses in which we make our best and most reliable margins are in UK infrastructure markets. Many of those markets have positive growth momentum. The building market is set to grow substantially on the back of PPP/PFI and a buoyant social housing market. In the gas, water and electricity markets, expenditure is strong and growing. The regional civil engineering market, in which we have strong but not comprehensive coverage, is also buoyant.

We will expand further our presence in UK infrastructure markets.

Growing in professional and technical services
There is a clear trend amongst our key customers to demand a broader and more proactive role from us than that represented by our established construction and maintenance services. We will develop a more substantial upstream capability in project and programme management and technical consulting services. The creation of Balfour Beatty Management in 2002 has been an excellent start in developing this process.

Extending our reach in private finance
Our UK PPP/PFI business has substantial skills and in-built growth momentum, much of it already contained in our existing portfolio. The potentially rapid development of PPP markets outside the UK, particularly in the US and Germany, and the emergence of new UK investment opportunities outside PPP offers further scope for growth. We will take our PPP skills beyond their current boundaries.

These three areas of growth, successfully addressed, offer us ample scope to continue the growth momentum of recent years in the medium term.

Growing in overseas markets

The development of our engineering and construction businesses outside the UK is an important part of our strategy, but not an urgent priority. This affords us the opportunity to move carefully and sure-footedly in developing our presence in the markets outside the UK which offer us the best long-term growth potential.

In growing in overseas markets, we will apply four key criteria. The markets must be large enough to make a substantial difference; offer an acceptable business environment and one which does not punish foreign ownership; and have substantial numbers of sophisticated customers who will pay for superior levels of quality, safety and innovation. The markets must also offer us the opportunity to achieve market leadership without undue risk.

Our key target markets will be the United States, Western Europe and South-East Asia, the latter based on our strong presence in Hong Kong.

Acquisitions, investments and disposals

In February 2005, we acquired JCM Group, a project management company in Southern California, for approximately $10m, which has further strengthened Heery International Inc's already strong US market position.

In order to strengthen our UK infrastructure operations, in August, we acquired Pennine Group, the UK ground engineering specialist for £8m. We are already a leader in the piling sector, through Stent, and the acquisition of Pennine gives us a strong complementary presence in ground engineering and provides a comprehensive range of foundations solutions for UK and overseas markets. Growth prospects in the UK and export opportunities are attractive and the integration process has been successful.

Also in August, we acquired SBB, the German rail signalling specialist. Renamed Balfour Beatty Rail Signal, the company strengthens our offer to Deutsche Bahn and broadens our signalling capability following the acquisition in 2004 of Bombardier's solid-state interlocking signalling business in the UK.

On 12 December, we announced that we were considering making an offer for Mowlem plc. On 18 January 2006, we announced our decision not to proceed with an offer. We also announced that we had reached a binding agreement, subject to due diligence, with Carillion plc that, following their acquisition of Mowlem, we would acquire two of Mowlem's businesses. These are Charter, a construction management, design and build and construction services company based in Texas, and Edgar Allen, a UK rail track systems and components manufacturer. The combined consideration for these businesses will be approximately £20m.

In December, Balfour Beatty Capital Projects increased its shareholding in Consort's Edinburgh Royal Infirmary PFI concession from 42.5% to 73.9% for a consideration of £31m. This transaction reflects Balfour Beatty's confidence that the project will continue to deliver attractive returns and will further consolidate our position as the market-leading developer and investor in healthcare PFIs. At the same time, in a separate transaction, we sold 15% of three of the concessions in Connect Roads for £13.5m.

During the year, financial close was achieved on PPP/PFI projects for schools in North Lanarkshire and Bassetlaw, and for South Tyneside street lighting. These projects represent a total equity investment by Balfour Beatty of £18m. The four PPP projects we have at preferred bidder stage involve equity investments totalling £54m.

Safety

It is gratifying to be able to report a further 23% reduction in the Group's accident frequency rate following the 17% and 14% reductions achieved in 2003 and 2004 respectively. However, we treat further improvements as a high priority and our Group-wide system for reporting and tracking health, safety and environmental incidents of all types is now fully bedded in and enabling far better performance benchmarking, trend identification and action plan development. A wide range of other initiatives is being progressed.

Outlook

We have record order books and a number of preferred bidder positions. Our major markets are healthy and continue to offer substantial opportunity. We are clear about our priorities for the continued development of the business in both the medium and long term and have the proven management capability to deliver.

I am confident that we can continue to make progress in 2006.

Ian Tyler Chief Executive

Building, Building Management and Services

Balfour Beatty is an international specialist in the design, construction, equipping, maintaining and management of buildings and selected aspects of their internal environment.

Companies	Specialist areas
Balfour Beatty Construction	Design
Balfour Kilpatrick	Construction
Haden Building Management	Construction and Programme Management
Haden Young	Electrical Engineering
Heery International	Mechanical Engineering
Mansell	Building and Facilities Management
	Refurbishment and Fit-out
	Social Housing

Civil and Specialist Engineering and Services

Balfour Beatty is a leading provider of civil and other specialist engineering, design and management services, principally in transport, energy and water.

Companies	Specialist areas
Balfour Beatty Civil Engineering	Design
Balfour Beatty Construction Inc	Construction
Balfour Beatty Management	Project Management
Balfour Beatty Power Networks	Foundations, Strengthening, Testing
Balfour Beatty Utilities	Civil Engineering
RCS	Transmission Lines
Stent Foundations	Road Management and Maintenance
Devonport Management Ltd (24.5%)	Utility Upgrade and Maintenance
Balfour Beatty Sakti (49%)	Professional and Technical Services
Dutco Balfour Beatty (49%)	
Gammon (50%)	

Rail Engineering and Services

Balfour Beatty is an international leader in the design, construction, equipping, maintenance, management and renewal of rail assets and systems.

Companies	Specialist areas
Balfour Beatty Rail	Design
– Infrastructure Services	Construction
– Projects	Project Management
– Power Systems	Maintenance
– Track Systems	Track Renewals
– Plant	Specialist Plant, Products and Systems
– Technologies	Electrification and Power Supplies
Balfour Beatty Rail Inc	Signalling

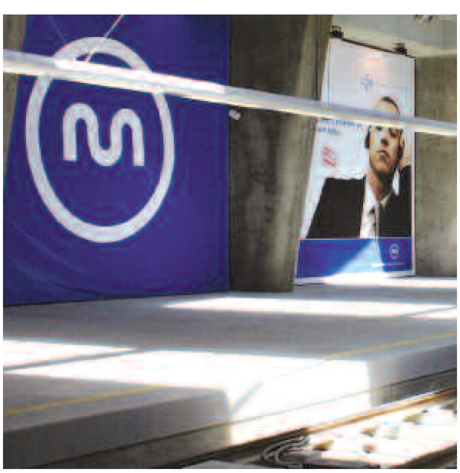
Investments and Developments

Balfour Beatty promotes and invests in privately funded infrastructure projects and developments in selected sectors.

Companies	Specialist areas
Balfour Beatty Capital Projects	Roads
– Aberdeen Environmental Services	Rail
– Connect	Accommodation – Healthcare, Education
– Consort Healthcare	Water
– Health Management (UCLH)	Integrated Transport
– Metronet	Power Systems
– Powerlink (electricity)	Property
– Transform Schools	
Balfour Beatty Property	
Barking Power Ltd	

BALFOUR BEATTY PROVIDES ENGINEERING, CONSTRUCTION AND SERVICE SKILLS TO CUSTOMERS FOR WHOM INFRASTRUCTURE QUALITY, EFFICIENCY AND RELIABILITY ARE CRITICAL.

Some Balfour Beatty customers




Top: London Underground
Middle: GlaxoSmithKline
Bottom: Metro do Porto

Top: BBC
Middle: Marks & Spencer
Bottom: NHS Hospital Trusts

Top: Tesco
Middle: United Utilities
Bottom: Land Securities


Top: Royal Mail
Middle: Kowloon and Canton Railway Corporation
Bottom: Catalyst Housing Group

Top: North Lanarkshire Council
Middle: Network Rail
Bottom: Camelot

Top: British Telecom
Middle: IKEA
Bottom: Texas Department of Transportation

Building, Building Management and Services

Highlights

- Two major PFI building schemes reach financial close
- Further increase in social housing order book
- Good progress on work at Heathrow Terminal 5
- Excellent year of progress for Mansell, Heery and Balfour Kilpatrick

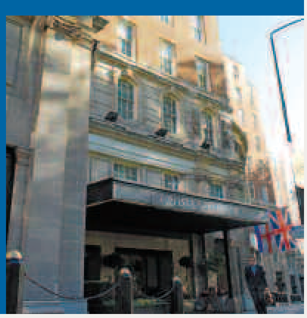
Financial summary

£1,787m
Revenue† (2004: £1,586m)

†Including £113m share of joint ventures and associates

£35m
Profit from operations* (2004: £34m)

*Before £8m exceptional charges



Top: Refurbishment of the London Grosvenor House Hotel – Balfour Beatty Construction.

Above: Programme management for the Georgia Aquarium – Heery International.

2005 performance

Profit from operations, before exceptional items in the Building, Building Management and Services sector rose by 3% to £35m. This reflected good performances in all operating businesses, including a strong recovery in Balfour Beatty Construction following the losses incurred on a small number of contracts in the first half year.

Review of operations

In **Balfour Beatty Construction**, profits for the year were down overall, although performance recovered strongly in the second half of the year following contract losses in the first half on a small number of projects, largely as a result of raw material cost inflation between contract and project execution.

Operating performance was good. The first phases of two major acute hospitals, University College Hospital in London and Blackburn Hospital, were delivered on time and to budget. The major works for the design, construction management and construction of the rail station and associated facilities at Heathrow Terminal 5 progressed to programme. Good progress was also made on the construction programmes under the schools PFI schemes in Stoke and Rotherham and successful starts were made on major new schemes in North Lanarkshire and Bassetlaw.

The refurbishment of the landmark Grosvenor House Hotel in London was completed on time. The stations upgrade for Metronet on the London Underground is now rapidly accelerating following the resolution of design and approvals issues.

After the successful office development project at Waverley Gate in Edinburgh for Castlemore, the company was awarded a second major scheme at Holborn in London.

Other project awards included major education projects for York College and Glasgow City Council.

In the healthcare sector, four substantial schemes, in Glasgow, Manchester, Birmingham and South Yorkshire, should be converted from preferred bidder to contract in 2006.

During the year, the company was reorganised into two separate units in order to address better both current and further anticipated growth.

Balfour Kilpatrick had another good year with sales, profits and order book all well ahead of 2004.

A major factor was significant activity levels under the PFI schools contracts at Stoke and Rotherham; and early work under the new schemes at North Lanarkshire and Bassetlaw. Satisfactory progress was achieved on the power engineering works being undertaken for BAA at Heathrow Terminal 5. These comprise mechanical and electrical engineering in the rail tunnels, the station and the track transit system. Major new projects were secured for Manchester Royal Infirmary and Gateshead Schools. Cruickshanks and Lounsdale, Balfour Kilpatrick's power systems businesses, both had good years.

Work on the Edinburgh Ring project for Scottish Power was successfully completed, as was a substantial portion of the work for the upgrading of London Underground's power system. A major tender for the next tranche of this work will be adjudicated shortly.

In the multi-services business, good progress was made on long-term works for the Ministry of Defence, AWE and BT.

In **Haden Building Management**, revenues were flat, but profits recovered well following some adverse issues in 2004. Major new orders were received for the maintenance portion of the Bassetlaw and North Lanarkshire Schools PFI projects and substantial extra work was won under the Monteray management and maintenance contract for BT.

Operational performance in Romec, the joint venture with the Royal Mail to manage and maintain the latter's entire building stock, improved as a result of increased efficiencies and better service levels, particularly in cleaning.

The company performed well on other major contracts, most notably for the Department for Work and Pensions and for the English regions of the BBC, for whom the London and Scotland contracts are now bidding. Other major long-term customers include Tesco and Land Securities.

There is a high level of current bidding activity in conjunction with the Group's healthcare and education PFI projects and a major tender to supply sorting frames, through Romec, to La Poste in France is currently under adjudication.

Haden Young had another very satisfactory year with sales and profits in line with 2004. Healthcare schemes, in which the company is a clear market leader, continued to be a major revenue generator. Its major role in both the University College London and Blackburn hospital schemes reached successful milestones during the year and £30m of new work was secured for the Churchill Hospital in Oxford. The company has also continued to be successful in winning and executing work under the Procure 21 programme.

Work on major hospital schemes at Addenbrookes, Romford and Stoke Mandeville, amongst others progressed well. 2006 should see financial close on the Birmingham and Pinderfields hospital projects.

Work on the major central London, Cardinal Place mixed-use development for Land Securities was completed and new orders included the Liverpool Arena and Conference Centre.

Heery, the US architectural, engineering and programme management business, had an excellent year with profits well ahead of 2004 and two recent acquisitions successfully integrated.

Heery's business is largely with public sector clients, most notably in education, healthcare, justice facilities and federal government. Progress was good, across the board, in 2005, with successful, on-time completions on a range of projects including the new Georgia Aquarium in Atlanta, the world's largest aquarium.

Early in the year, Heery acquired JCM Group, one of Southern California's premier project management companies. This followed the 2004 acquisition of HLM, a recognised leader in the planning and design of healthcare projects. Both performed well. JCM Group won the US Construction Management Project Achievement Award from the Construction Management Association of America for its work on a medical centre in Burbank, California.

In 2006, Heery will be further augmented by the acquisition of Charter, a Texas-based construction management company with annual sales of approaching £100m, which we have agreed to buy, subject to due diligence.

Mansell had another very good year with sales, profits and its year-end order book increasing significantly. There was particularly strong growth in the social housing market. Among a number of major new projects secured was work for the Metropolitan Housing Trust, Your Homes, Newcastle and Crossway Point. The £35m Hackney Decent Homes programme was successfully progressed. 2005 revenues in social housing were in excess of £180m.

Mansell has also taken advantage of a strong education market with new projects secured for school building in Argyll and Bute, for Unite in London, for the University of London, the College of North West London and a framework contract for Norfolk County Council.

Other successes included a framework contract for BT's 21st Century Network Programme, a three-year job centre programme for the Department for Work and Pensions and the first phase of the five-year, £127m masterplan programme for United States Air Force accommodation at Lakenheath in Suffolk. Mansell has framework agreements with a potential value of over £1bn.

Outlook

With substantial further growth in last year's record order books and over £1bn more work at preferred bidder stage, we anticipate good progress in the building sector in 2006.

Top: North Lanarkshire School, electrical services refurbishment – Balfour Kilpatrick.

Above: Crossway Point social housing development – Mansell.

Civil and Specialist Engineering and Services

Highlights

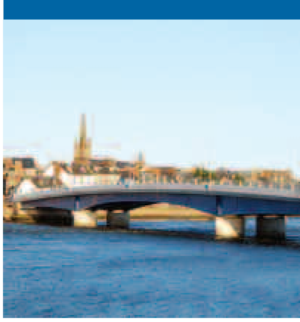
- Almost £1bn of new work secured by Balfour Beatty Utilities
- US civil engineering returns to profit
- Two new long-term road maintenance contracts secured
- Substantial increase in order book for Gammon in Hong Kong

Financial summary

£1,920m
Revenue† (2004: £1,443m)

†Including £554m share of joint ventures and associates

£49m
Profit from operations (2004: £16m)



Top: Ground improvement work in Valencia – Pennine Group.

Above: The new bridge in Montrose – Balfour Beatty Civil Engineering.

2005 performance

Profit from operations, before exceptional items, in Civil and Specialist Engineering and Services more than tripled to £49m in 2005. This excellent result reflected good progress in all the UK businesses, together with a substantially improved performance in civil engineering in the US.

Review of operations

Balfour Beatty Civil Engineering in the UK performed well, in a relatively flat market environment.

In the roads sector, on-time, on-budget completions were achieved on the £130m M77/Glasgow Southern Orbital PFI scheme and the £148m M25 widening scheme adjacent to Heathrow Airport, both very challenging projects. We were awarded the £241m project to widen the M1 motorway between Junction 6A and Junction 10 and the £171m scheme for the A421 in Bedfordshire.

Balfour Beatty now has six major Early Contractor Involvement schemes for the Highways Agency.

Tunnelling works on the Steg Raron rail projects in Switzerland were successfully completed as was the new Manchester Business Park. The award of the civil engineering works for the new ticket hall at King's Cross Station is anticipated in the near future.

The regional civil engineering businesses performed well, with good contributions from the long-term framework agreements for the Highways Agency and Cambridgeshire and Durham County Councils. Airport maintenance work for BAA in Scotland also progressed well. The contract for the maintenance of the Forth Railway Bridge was extended for a further three-year period.

New civils contracts for Network Rail were begun in the year and a major project at the Isle of Grain was secured.

Balfour Beatty Management, the Group's professional services business continued to develop its presence in the markets for project and programme management. It will play a major part in the Greater Manchester Gas Alliance project for National Grid and is also working on projects for BAA and London Underground.

Progress on the programme and project management contract for the major rail development works at King's Cross, was satisfactory.

Top: Yorkshire Water asset upgrading – Balfour Beatty Utilities.

Above: Shenzhen Western Corridor, Hong Kong – Gammon Construction.

Balfour Beatty Power Networks, which designs and constructs power transmission and distribution networks, had a very good year with sales and profits well ahead of 2004. Activity levels were boosted by the 100 kilometre line between the East Midlands and East Anglia. The Central Network contract was also expanded to cover the West Midlands. Volumes of work under a number of other contracts for National Grid continued to be high and the cabling contract for the Western Power Distribution system was renewed.

There was also good progress on the Sunderland Street Lighting PFI project. In December, financial close was reached on the South Tyneside Street Lighting PFI project, under which the company will replace 80% of the existing lighting infrastructure over the first five years.

The company also won contracts for Australia's power transmission expansion programme.

In the gas and water sectors, **Balfour Beatty Utilities'** sales grew substantially as a result of a series of major contract wins following 2004 regulatory review. Profits were in line with those of 2004 despite the substantial mobilisation costs incurred in preparing to service its major new commitments.

In 2005, the company won new long-term contracts for gas mains replacement in Greater Manchester; clean water upgrade and maintenance work for Yorkshire Water, Severn Trent Water, Anglian Water and South West Water; and clean water and sewerage works for United Utilities. These contracts are worth approaching £1bn over their full terms and constitute a step-change in the size and scope of the business.

Performance on the existing contracts and on the early stages of the new ones was satisfactory.

In road management and maintenance, **RCS** had another very successful year with both sales and profits well ahead of 2004 and its order book further extended.

The company performed well on its three long-term Highways Agency contracts for Areas 2, 3 and 4.

Contracts for maintaining local authority roads in Hampshire, North Yorkshire, Westminster and Wokingham and PFI concession roads in Devon, Dorset, Derbyshire, Yorkshire and the West of Scotland also progressed satisfactorily.

Towards the end of the year, RCS won road management and maintenance contracts for north-west Scotland and Mid and East Essex to a total potential value of approximately £200m. Decisions on extending our relationships in Hampshire, Yorkshire and Highways Area 3 are imminent.

Bidding opportunities in 2006 include several county council contracts and the contract for the M25, which is to be let as a single PFI.

Stent, the Group's specialist foundations and piling business, achieved organic sales and profit growth and acquired Pennine Group. Pennine specialises in the treatment and preparation of poor ground using self-manufactured specialist machinery and has been successfully integrated into the business.

During the year, work was completed on the M25 widening project and the new Arsenal football stadium. Progress was good on the multi-use development site at White City in West London. Work on the M1 widening project will begin in the near future.

The performance of BSR Metro, an internal Balfour Beatty joint venture which provides a range of services to Metronet's London Underground PPP concessions was good. Work in support of our construction operation in Dubai increased.

Devonport Management Ltd, in which the Group has a 24.5% interest, continued to perform well and to increase its revenues. The nuclear submarine refuelling programme progressed well with Vanguard completed and Victorious now in dock. The ship repair programme was steady as was performance in the maintenance of the naval base.

DML will, undoubtedly, have an active part to play in the Government's plans for developing and managing the UK's maritime industrial base.

The performance of **Balfour Beatty Construction Inc** in the US showed radical improvement after the heavy losses of 2003 and 2004. The marine engineering business in which the majority of the losses were incurred has been closed and its final project is now nearing completion. 2005 saw some claim settlements on its completed projects. The highways business in Texas continued to perform well with good progress made on the $1.3bn SH 130 toll road project, the $84m SH 121 and other contracts. The Western Division in California performed steadily on a range of projects including road widening schemes in Los Angeles and San Diego, the extension of the Downtown Seattle Bus Terminal and the Roseville Water Treatment Plant.

The Central Division also continued to perform steadily and progress a range of road projects largely in Pennsylvania and Ohio.

During the year, the long-awaited SAFETEA federal transport funding programme, increased federal spending on transportation projects by 38% in the period to 2009.

Tunnelling work for a major water project in Providence Rhode Island and the civil works for the Greenbush commuter rail line refurbishment project in Boston progressed well.

The emergence of a US PFI market offers new opportunities for the business.

In Dubai, **Dutco Balfour Beatty**, in which the Group has a 49% interest, performed steadily in a fast-growing market. Its sales and order book have grown rapidly over recent months. The £400m contract to build the Burj Mall, the world's largest retail complex is making sound progress. The civil engineering and mechanical engineering businesses have also both progressed well.

During the year, a shopping mall for IKEA was completed and the mechanical and electrical work for a new terminal at Dubai Airport made substantial progress.

Balfour Beatty Sakti in Indonesia, in which the Group has a 49% interest, had low activity rates.

In Hong Kong, the performance of **Gammon**, in which Balfour Beatty has a 50% interest, was in line with that of last year. The order book increased sharply during the year. In 2005, Gammon has been undergoing an adaptation of its processes and systems to the Balfour Beatty model.

During the year, the major rail terminus and immigration hall project at Lok Ma Chau progressed well and the Shenzhen Western Corridor and Deep Bay Link projects were substantially completed. The refurbishment of the Mandarin Hotel also made good progress.

The year saw some very substantial project wins including the £175m Venetian Tower Hotel and Casino project in Macau and, later, a £29m extension contract. Macau offers an increasingly strong market opportunity. Gammon also won the £140m civil engineering and tunnelling contract for part of the Kowloon Southern Link. A contract to manage and maintain high-speed roads was also secured.

Prospects for market and performance improvement in Gammon are good.

Outlook

With strong order books and a number of large new contracts in their early stages, we anticipate further growth momentum in 2006 in the engineering sector.

Rail Engineering and Services

Highlights

- Metro do Porto project completed
- Terminal 5 work progressing well
- Strong renewals volumes for Network Rail and London Underground
- On-time delivery of Berlin tunnel project

Financial summary

£766m
Revenue† (2004: £803m)

†Including £3m share of joint ventures and associates

£32m
Profit from operations* (2004: £44m)

*Before £12m exceptional charges

Above: Ballast tamping – Balfour Beatty Rail Infrastructure Services.

2005 performance

Profit from operations, before exceptional items, in Rail Engineering and Services fell by 27% to £32m in 2005. This reflected a sound performance in the core UK and European businesses, but also a first full year without UK maintenance, a generally tighter UK market and some further losses in the rail engineering business in the US.

Review of operations

Balfour Beatty Rail Infrastructure Services, is now concentrated on track renewals following the completion of the transfer of the maintenance activities to Network Rail in 2004. 2005 saw only some residual income as a result of finalising outstanding liabilities from this source. In renewals, 2005 saw a first full year of work under the new Network Rail track contracts which came into force in April 2004 and as a result of which Balfour Beatty has become Network Rail's largest supplier.

Under these contracts, Balfour Beatty is responsible for plain line renewals in the Anglia and Southern regions and switches and crossings renewals in London North-East, Southern and Anglia regions.

Volumes ran broadly at anticipated levels. 2005 profits were augmented by final settlements of the previous generation of track renewal contracts.

In **Balfour Beatty Rail Projects**, profits increased, with significant progress on the West Coast Main Line electrification project, the design and installation work for the Heathrow Express and Piccadilly Line extensions at Heathrow Terminal 5 and an acceleration of the trackwork renewal programme for Metronet under the London Underground PPP. During the year, a further contract on the West Coast Main Line modernisation programme was secured. This involves the delivery of 13 feeder stations and 620 miles of high voltage feeder and is worth £110m.

Outside the UK, work was substantially completed on the project to install trackwork and electrification on the extension of the Santiago Metro.

New projects were secured for the upgrade of the existing rail link between Sydney and Brisbane for the Australian Track Corporation and for the design and construction of trackwork for the latest extension of the mass rapid transit system in Singapore. The company also had some success in the signalling market following the acquisition of Bombardier's solid state signalling resources in the UK last year.

New UK major project work will be slow to materialise in the short term, although the company is prequalifying for the upgrade of the East London Line and Crossrail, Thameslink and the Olympic Games offer good long-term prospects.

Performance in **Balfour Beatty Rail Track Systems** was slightly down on 2004. A reduction in Network Rail's demand for switches and crossings was offset by increased Metronet demand under the London Underground PPP. Early 2006 demand from Network Rail is significantly improved. Export sales to Israel, Taiwan and the US continued.

Investment in the manufacturing facilities continued, with new forging machines installed in February 2006. It was announced in January 2006 that Balfour Beatty had agreed, subject to due diligence, to acquire Edgar Allen, a strong player in the track systems and components market.

In **Balfour Beatty Rail Plant**, profits were down. The UK major rail project market declined, affecting the performance of the road and rail fleet. Despite some early operating setbacks we remain confident that new high output track machines will prove excellent investments in the longer term.

In November, the company secured a three-year contract for the provision of road rail plant for Network Rail and the year ended on a high note when the company was awarded two further new contracts, likely to be worth approximately £65m, for tamping and ballast regulating services in the South East and East Midlands. These contracts, which are for the provision of 28 machines, begin on 1 April 2006.

Balfour Beatty Rail Technologies continued its work on a number of safety-related technical developments, most notably XiTRACK, a polymer-based stabilisation technology for track and other infrastructure.

Above: Track renewals on the London Underground – Balfour Beatty Rail Projects.

A wide range of non-destructive testing programmes for Network Rail was also progressed. A decision is expected soon in respect of a remote condition monitoring system for the West Coast Main Line. A new remote inspection system has been awarded at London Bridge to reduce safety hazard exposure for manual track inspections.

Work is in hand on various life extension and asset condition projects for Metronet.

Balfour Beatty Rail Power Systems, the international electrification and power supply business, had a very good year, with increased profits.

In ***Germany***, despite a difficult domestic market performance was significantly better than last year following cost reductions and reorganisation. Order intake in Germany improved, reflecting the first signs of a recovery in Deutsche Bahn's investment spending patterns. The company secured the largest order let in 2005 by DB Energy for Mannheim substation and increased its overall market share. IVV, its consultancy business, had a solid year.

The contract in central Berlin to project manage, supply and design overhead line, conductor rail, power supply units and electro-technical equipment for the rail system was completed on schedule, as was the high-speed electrification project between Ingolstadt and Nuremberg. Work to electrify and extend Dublin's metro network was also completed on time. Good progress was made in providing the power supply for the new Betuweroute freight line between Rotterdam and the German border. During the year, the company secured a first catenary project in Romania. Wholly Owned Foreign Enterprise Status has now been achieved in China.

In August, the company acquired SBB, a specialist German signalling contractor, for €14m, subsequently renamed Balfour Beatty Rail Signal. It operates, predominantly, in the former East Germany and renews and installs signalling systems under existing framework contracts. Following this acquisition, the company won its first electronic signalling contract in Dortmund, with Bombardier.

In ***Italy***, performance was good. The newly-electrified line between Rome and Naples is now running high-speed trains successfully and good progress was made on the first stage of the line between Milan and Turin and other high-speed electrification projects. It is likely that the contracts for both Milan to Verona and Genoa to Milan will be secured in 2006.

The major Metro do Porto project, for which the Italian business was responsible, was successfully completed with bonuses paid for on-time and on-budget delivery.

In ***Spain***, the market was strong, good progress was made on a number of projects and new projects were secured. A major export contract was won in early 2006 in China on the Tianjin-Shenyang line.

The ***Swedish*** business has grown significantly in 2004 and 2005 and progress on the two major contracts for trackwork and associated system works in the north and electrification on the east coast was satisfactory.

In ***Austria***, performance was steady. Prospects, including a major upgrade to the Vienna train system, are good.

In ***Malaysia***, the installation programme for the Rawang-Ipoh line is accelerating following the appointment of a new civil engineering contractor. Completion of this project is scheduled for 2007.

Balfour Beatty Rail Inc in the United States had another difficult year, largely as a result of continuing problems on a major signalling project in Philadelphia. Discussions with the customer with a view to finding a solution to the project's difficulties are in hand. Elsewhere in the mass transit sector, the major project at Greenbush in Boston made satisfactory progress, as did the Goldline project in Los Angeles.

The rail services business, a branch network of local businesses providing maintenance and project services to a range of industrial customers, performed well. Activities include rail and tie replacement, maintenance, vegetation control and upgrading and operating line sections. Customers include the mineral extraction industry in Wyoming and a range of goods and shunting yards on the US heavy freight network. This business has made rapid progress in recent years and now has 16 branch offices.

A strategy review is now under way in Balfour Beatty Rail Inc. under a new management team. There remains substantial potential for this business as transit and Class 1 volumes continue to grow in an expanding US economy.

Outlook

2006 should see a resumption of progress, based on increased efficiencies and improving volumes on projects on the London Underground and in Germany and Italy.

The potential to strengthen the Group's presence in this sector continues to be explored.

Top: Switches and crossings supplied to Network Rail – Balfour Beatty Rail Track Systems.

Above: High-speed rail electrification between Milan and Turin – Balfour Beatty Rail Power Systems.

Investments and developments

Highlights

- Bassetlaw and North Lanarkshire schools and South Tyneside street lighting projects reach financial close
- Shareholding in Consort's Edinburgh Royal Infirmary concession increased to 73.9%
- Preferred bidder status achieved for Northern Batched Hospitals project
- Another strong performance for Barking Power Ltd

Financial summary

£465m
Revenue† (2004: £407m)

†Including £431m share of joint ventures and associates

£20m
Profit from operations* (2004: £17m)

*Before £36m exceptional profits

Balfour Beatty Capital Projects is a leader in the UK PPP/PFI market with 18 concessions and four further projects at preferred bidder stage. A further ten bids have been submitted or are in preparation. Barking Power is a leading independent power producer with a 1,000MW gas-fired station at Barking Reach, London.

The Market

The PFI market remains buoyant. In healthcare, despite signs of a decline in very large single building PFI acute schemes, Balfour Beatty is tracking the progress of 15 major schemes with a value of £4.4bn and is currently bidding one such scheme.

In education, the "Building Schools for the Future" initiative provides new longer term opportunities alongside traditional PFI education projects. The programme extends to 2020 and is forecast to generate £40bn. Balfour Beatty is currently bidding two BSF and two traditional PFI education projects. The acquisition of Mansell has enhanced the Group's expertise in the social housing market and a joint PFI social housing scheme is being bid in Ashford, Kent. We anticipate a proliferation of opportunities in this sector.

In the roads sector, PPP is the chosen procurement method for the £1.5bn M25 widening project, where bidding will commence in 2006, and there are potential opportunities of a similar scale for the M1, M6 and M4.

Strategy

Balfour Beatty will continue to pursue opportunities in those existing markets where it has clear competitive advantages and market leading positions. Projects will continue to be targeted whose size and complexity offer advantages arising from the Group's unique range of skills and experience.

These projects will, typically, not only provide attractive investment opportunities – but also trade on the proven strengths of, and provide design, construction and service contracts for other parts of the Balfour Beatty Group.

Balfour Beatty will continue to monitor the development of other national markets and is actively pursuing opportunities in both the US and Germany.

2005 performance

Profit from operations, before exceptional items, in Investments and Developments rose by 18% to £20m in 2005. This represents the post-tax concession profits from those PFI and other concessions which are in joint venture with other owners. During the year, three concessions were converted to contract from preferred bidder status and preferred bidder status was achieved for the Northern Batched Hospitals scheme, making four projects at preferred bidder stage at the year end in all.

Outlook

We anticipate that the operating performance of our concessions will continue to meet expectations, that further major projects will reach financial close during the year and that we will make further satisfactory progress in 2006.

Above: M77/Glasgow Southern Orbital Road – Connect.

Above: University College London Hospital – Health Management Group.

Top: Rotherham County Council – Transform Schools.

Above: London Underground – Metronet.

Investments and developments continued

Healthcare

Consort, the established Balfour Beatty business brand in the healthcare market, performed well in 2005, contributing profits and cash at anticipated levels.

Consort Healthcare's portfolio comprises interests in seven major hospital schemes and represents a committed equity investment of £112m, £50m of which is in three projects at preferred bidder stage.

In December 2005, Balfour Beatty increased its shareholding in the Edinburgh Royal Infirmary concession from 42.5% to 73.9% for a consideration of £31m. This underlines the confidence which the Group feels in the value and earning capacity of its concessions.

North Durham Hospital and Edinburgh Royal Infirmary were already fully operational at the beginning of 2005. In May 2005, Phase I of the University College Hospital in London opened on time and on budget. Phase I of Blackburn Hospital was opened, on time and on budget, in October 2005. The £521m Birmingham scheme and the £250m Pinderfields scheme are scheduled to reach financial close during 2006. In November 2005, Consort was appointed preferred bidder for the £190m Northern Batched Hospitals scheme, which will create new and upgraded facilities in Salford and Tameside in Manchester. A bid is in preparation for the Fife Hospital Scheme with an anticipated capital value of approximately £100m.

Consort Healthcare has strengthened its leadership position in the PPP hospitals market and further developed its proven track record and high levels of client satisfaction.

Education

Transform Schools, the established Balfour Beatty brand in the education market, performed well in 2005. Its portfolio comprises interests in five schools schemes, representing £30m of committed equity, of which the Birmingham Schools project is at preferred bidder stage. The Stoke concession is the largest grouped schools scheme in England, covering 98 schools, and has been operational since 2000 to high levels of client satisfaction.

The concession for Rotherham Schools became operational in June 2003 and is also highly successful. In 2005, it was awarded "Best Community Use Project" in the PPP/PFI Journal Awards.

In June 2005, Transform reached financial close on the £140m scheme to build and maintain 21 new schools for North Lanarkshire Council. In July, financial close was also achieved for the £127m scheme in Bassetlaw, North Nottinghamshire, including six new schools, two post-16 learning centres and two new leisure centres. The £56m Birmingham concession is due to reach financial close during 2006. Under this scheme, Transform will provide 12 new and refurbished schools.

Active bids are in hand for new PFI schemes in Newcastle, Aberdeen and Knowsley, with an aggregate total value of £375m. Transform has also prequalified for two schemes under the Building Schools for the Future programme.

Transform Schools, with four operational schemes with an aggregate capital value of over £400m, is now a clear leader in the education market.

Roads

The profit and cash performance of Connect Roads, Balfour Beatty's brand in the highways market, was in line with that of 2004.

In December 2005, 15% of Balfour Beatty's interest in the A30/A35 in Devon and Dorset, the A50 in Derbyshire and the M77/GSO in Scotland was sold to I^2 for a consideration of £13.5m. These concessions had previously been 100% owned. The A30/A35 and A50 projects have been fully operational since 2000 and 1998 respectively. The M77/GSO was completed and opened to traffic in April 2005. As these concessions are now under joint control their finances have been deconsolidated from the Balfour Beatty balance sheet. Balfour Beatty has a 50% interest in the M1/A1 Link near Leeds, which has been operational since 1999.

Connect has 100% owned street lighting projects, in Sunderland, which has been operational since 2003, and South Tyneside, which reached financial close in December 2005.

In all, Balfour Beatty currently has committed equity investment of £61m in UK roads and streetlighting schemes.

Bids are in preparation for a further five schemes. These are the £250m Northern Ireland roads package, the £175m Tyne Tunnel, street lighting schemes in Derby and Surrey with a combined capital value of £105m and the £35m Carlisle Northern Development Route.

Edinburgh Royal Infirmary:	73.9%
University Hospital of North Durham:	50%
University College London Hospital (UCLH):	33%
Blackburn:	50%
Birmingham:	50%†
Pinderfields:	50%†
Northern Batched:	50%†

† Preferred bidder

Consort healthcare

Stoke:	50%
Rotherham:	50%
North Lanarkshire:	50%
Bassetlaw:	50%
Birmingham:	50%†

†Preferred bidder

Transform schools

M1-A1:	50%
A50 Stoke/Derby link:	85%
A30/A35:	85%
M77/Glasgow Southern Orbital:	85%
Sunderland Street Lighting:	100%
South Tyneside Street Lighting	100%

Connect roads

The London Underground

Since April 2003, Metronet has operated and maintained the infrastructure for the Bakerloo, Central, Victoria and the Sub-Surface Lines for London Underground under 30-year concession contracts. Profits from the Group's 20% share in Metronet's concessions were satisfactory. The underlying operational performance of the infrastructure for which Metronet is responsible continued to be on a satisfactorily improving trend and in line with previous expectations. Costs increased as the major investment programmes began to accelerate.

As reported last year, the major station refurbishment programme and some other elements of Metronet's capital works programme were slow in getting under way as design, approvals and mobilisation processes have been further developed and refined. Within the next 4½ years 150 stations will have been refurbished as will have countless other civil assets. The pace of activity continues to accelerate, now under a new management team and a new organisational structure.

The Group has committed £70m of equity investment in Metronet.

Other infrastructure concessions

The Group has two other infrastructure concessions. These are Powerlink, in which the Group has a 10% interest and which is responsible for the upgrade and maintenance of London Underground's high voltage power system. Discussions are currently in hand with London Underground to restructure this concession. Aberdeen Environmental Services, which is responsible for waste water treatment in Aberdeen performed satisfactorily in line with the previous year. The total equity committed to these concessions is £10m.

Barking Power

Barking Power again performed very strongly in 2005. Availability was excellent, with planned maintenance completed on schedule and very few unplanned outages. Electricity prices for the 27% of the station's output that is sold on the open market also continued to be strong.

During the year, Barking Power agreed a claim for damages for breach of contract for £179m following TXU Europe's entry into administration in November 2002. TXU Europe had both an equity investment and a power purchase agreement with Barking Power Limited prior to its insolvency.

Dividends of £164m were received by Barking Power from the settlement for damages during 2005 and, consequently, Balfour Beatty has recognised a net exceptional profit of £30m, after tax of £12m.

Metronet BCV:	20%
Metronet SSL:	20%

Powerlink/PADCO:	10%/25%
Aberdeen Environmental Services:	45%

Barking Power Ltd:	25.5%

Directors' valuation of PFI/PPP concessions

Introduction

Balfour Beatty's PPP concession portfolio has grown in recent years to become a very significant part of the Group's business and a major driver of shareholder value. At 31 December 2005, Balfour Beatty had total committed equity and subordinated debt of £283 million across 22 projects, four of which were at preferred bidder stage. At that date, £149 million had already been invested and £134 million is due over the next six years.

Valuations of PPP equity often rely on the use of multiples to produce a proxy cash flow valuation. This produces somewhat crude benchmarks as such an approach takes no account of the time value of money, expected rate of return of the asset, the performance of the asset or the potential for capital restructuring.

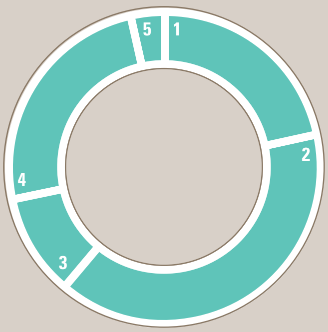
In order to provide a more reliable indicator of value, Balfour Beatty has decided to publish its own valuation benchmark for the Group's PPP investments, based largely on discounting expected future cash flows but without taking into account potential refinancing gains. This will, henceforth, be a regular feature of Balfour Beatty's Annual Report and Accounts.

2005 valuation

At 31 December 2005, the Directors' valuation of Balfour Beatty's portfolio stood at £289 million, at a weighted average, post-tax nominal discount rate of 8.2%; compared with £243 million at the end of 2004. The movement in value arises both through shareholder cash inflows and outflows and through underlying growth in the portfolio arising from the unwinding of the discount rate from year to year. A 1% change in the discount rate impacts value by approximately £30 million.

An analysis of the movement in value between years is shown at the foot of this page.

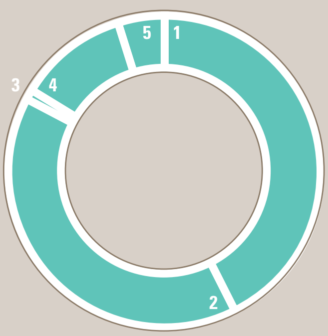
Our portfolio



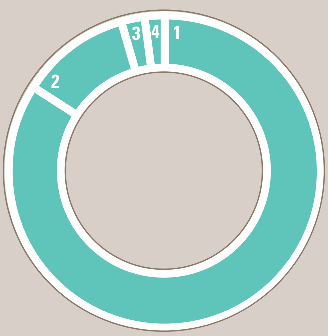
Total equity committed by sector	£283m
1 **Connect:** 6 projects	£61m
2 **Consort:** 7 projects	£112m
3 **Transform:** 5 projects	£30m
4 **Metronet:** 2 projects	£70m
5 **Other:** 2 projects	£10m

Cash invested by December 2005	£149m
1 **Connect:** 6 projects	£56m
2 **Consort:** 7 projects	£59m
3 **Transform:** 5 projects	£0m
4 **Metronet:** 2 projects	£27m
5 **Other:** 2 projects	£7m

Portfolio valuation: December 2005



Value by sector	£289m
1 **Connect**	£123m
2 **Consort**	£116m
3 **Transform**	£3m
4 **Metronet**	£33m
5 **Other**	£14m



Value by phase	£289m
1 **Operations**	£243m
2 **Metronet**	£33m
3 **Preferred bidder**	£7m
4 **Construction**	£6m

Movement in value 2004/2005 (£m)

2004	Equity invested	Distributions	Purchases	Disposals	Rebased	Growth	2005	Growth
243	30	(13)	31	(14)	277	12	**289**	4.3%

The valuation method

The valuation does not set out to estimate the market value of the investments in the portfolio, but rather, through the application of a consistent methodology, illustrates movements in underlying values between periods and highlights the impact of intervening transactions. The valuation covers 18 concessions that have reached financial close and four at preferred bidder stage. One of two methods has been used to establish the value of individual concessions.

DCF

The principal method used to value the portfolio is discounted cash flow (DCF). This is applied to the future forecast cash flows to which Balfour Beatty as a shareholder and a holder of subordinated debt is entitled in order to create a net present value (NPV). DCF has been used on 19 of the 22 investments. For projects which have reached financial close, forecast future cash flows are extracted from detailed financial models, updated in line with operational experience and lenders' requirements. For projects at preferred bidder stage, the current financial model has been used.

Book value

For the other three concessions, the current carrying value in the accounts (book value) has been used. Metronet is at too early a stage in its 30-year concessions to forecast cash flows with the same degree of certainty as the majority of the Group's concessions. In the case of Powerlink, discussions are currently in hand with London Underground over restructuring the concession framework.

Assurance

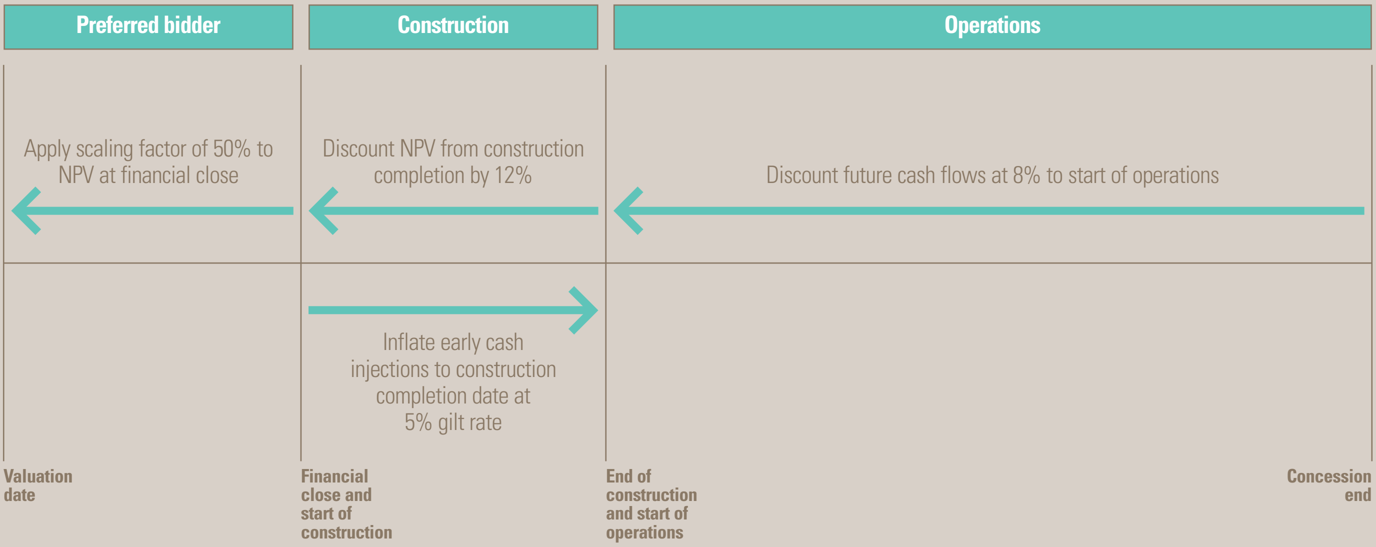
The calculations underpinning the valuation have been independently checked to ensure that the valuation has been accurately carried out in accordance with the specified methodology. However, the detailed financial models have not been audited.

DCF methodology

The DCF methodology discounts forecast cash flows at differing discount rates depending on the project phase, and therefore the risk associated with the cash flows.

- Any investment cash flows occurring during the construction period are rolled forward at a risk free rate (5%) to the final injection of equity at construction completion.
- Cash flows, anticipated to occur during the operations period, are discounted back to the beginning of the operations phase at 8%. Where cash flows occur during operations build up a discount rate of 10% is used during that period (if demand risk is present).
- A net present value is calculated at the end of the construction period by deducting the investment cash flows that occur at this time from the value of the discounted cash flows at the beginning of operations.
- The net present value at the end of the construction period is then discounted back to financial close at 12%.
- Any projects at preferred bidder have a scaling factor of 50% applied to the NPV at financial close.

A diagrammatic illustration of the process is shown below.



The Group has again benefited from a strong cash flow from operations and improvements in working capital management.

International financial reporting standards

This annual report is the Group's first to be presented under International Financial Reporting Standards (IFRS). Reconciliations of the Group's profit for the year 2004 and balance sheet at 31 December 2004, showing the effects of changes in presentation and accounting policies arising from the adoption of IFRS on the figures reported under UK GAAP in March 2005, are included in Note 37.

While the new standards have had little impact on the results in our contracting sectors (Building, Engineering and Rail), two of the new standards, IAS 32 and IAS 39, relating to financial instruments, fundamentally affect the way we account for our interests in PFI/PPP concessions and for our preference shares. The results presented in the formal accounts (pages 52 to 107) reflect the application of these standards to 2005 results but not to those for 2004, with a consequent impact on comparability. In order to provide appropriate period-to-period comparisons, in addition to the formal accounts we have provided unaudited "pro forma" 2004 results, including the impact of IAS 32 and IAS 39, which are set out on pages 108 to 110. In the commentary below, the use of these "pro forma" 2004 comparatives has been indicated with an asterisk (*).

We continue to monitor the development of those financial reporting standards yet to be finalised, particularly in the area of accounting for PFI/PPP concessions.

Results

Revenue in 2005, including the Group's share of the revenue of joint ventures and associates, increased by 16%, of which 3% was attributable to the acquisition of Gammon in August 2004.

Profit from operations before exceptional items increased from £94m to £115m (22%). In the building and building services sector, there was another good performance from Mansell and satisfactory progress in other operating companies, including Balfour Beatty Construction whose profits have recovered strongly in the second half year following some contract losses reported in the first half year. Progress has been very satisfactory in the civil and specialist engineering sector, with the return to profit of US civil engineering as well as good progress elsewhere, particularly in RCS, the Group's road manager and maintainer, and Balfour Beatty Power Networks. Performance in our rail sector was steady in the UK and in the international rail electrification business, but reflected the loss of rail maintenance profits and the continued impact of contract difficulties in the US. Performance has continued to be satisfactory in our investments sector. During 2005, new concessions came on stream for the M77/GSO roads in Scotland, major school schemes in North Lanarkshire and Bassetlaw, and street lighting in South Tyneside.

A more detailed analysis of performance in our operating businesses is contained in the Operating Review.

Acquisitions and goodwill

During December 2005, the Group acquired an additional 31.4% interest in the Consort Edinburgh Royal Infirmary PFI concession for £31m. The Group also made three smaller acquisitions for consideration totalling £25m. Goodwill arising on these acquisitions amounted to £14m.

An exceptional charge of £4m has been made in 2005 for impairments to goodwill in respect of Balfour Beatty Rail Inc (2004: £18m) following the annual review, resulting in £284m goodwill on the Group's balance sheet at 31 December 2005 (2004: £279m).

Disposals

The Group sold a 15% interest in the Connect Roads A30/A35, A50 and M77/GSO PFI concessions to I^2 in December 2005 for £13.5m. The associated £224m non-recourse net debt was then deconsolidated from the Group's balance sheet as, following this transaction, Balfour Beatty and I^2 exercise joint control over these road concessions.

Exceptional items

The Group has recorded a net exceptional gain of £4m. A gain of £30m, after tax of £12m, arose in respect of the Group's share of initial distributions received by Barking Power from the administrators of TXU Europe and a £6m gain was realised on the sale of a 15% interest in three Connect Roads PFI concessions. These gains were partly offset by £8m costs arising from a settlement payment to resolve investigations by the US Government into a joint venture contract completed in 2000 and from the Group's admission of breaches of the Health and Safety at Work Act following the Hatfield derailment in October 2000 for which the associated fine had already been provided; an impairment charge of £8m in respect of the Group's investment in Romec Ltd; £4m goodwill impairment charges; £3m premium on the purchase of preference shares; and £6m cost of repaying the Company's US$120m term loan. These items, along with other prior year tax adjustments relating to exceptional items, have given rise to a £3m net tax charge.

Taxation
The Group's effective tax rate in 2005 was 35% (2004: 32%*) of profit before taxation and exceptional items, excluding the Group's share of the results of joint ventures and associates. The increase in the effective rate follows from the recognition in 2004 of £17m previously written off Advance Corporation Tax (ACT). The Group has continued to benefit from the use of brought forward tax losses in Germany.

Pre-tax profits and earnings
Profits from continuing operations before taxation and exceptional items amounted to £134m (2004: £107m*), an increase of 25%, and adjusted earnings per share were 24.1p (2004: 22.1p*), an increase of 9%.

Cash
The Group has again benefited from a strong cash flow from operations and improvements in working capital management.

	2005 £m	2004 £m
Group operating profit	58	56
Trading profit from discontinued operations	–	8
Depreciation	41	41
Impairment charge	12	18
Other items	(5)	2
Working capital decrease	61	23
Cash generated from operations	167	148

Cash flow from operations provided further capacity to grow the Group's core activities through three acquisitions (£25m outflow) and two transactions in PFI/PPP concessions (net £17m outflow). The level of the Group's net cash at 31 December 2005 increased to £315m (2004: £311m), before taking into account the consolidation of £14m (2004: £244m) of non-recourse net debt held in wholly-owned PFI/PPP project companies.

Pensions

Valuation
The last formal actuarial valuation of the Balfour Beatty Pension Fund was carried out at 31 March 2004 and showed a funding position of 102%. A formal actuarial valuation of the Railways Pension Scheme was carried out at 31 December 2004 and showed a funding position of 92%. Formal actuarial valuations of the Mansell schemes were carried out at 31 March 2005 and 31 July 2005 for the Hall & Tawse Retirement Benefit Plan and the Mansell plc Pension Scheme and showed funding positions of 79% and 78% respectively.

The position of each of the funds has been updated by the actuaries at 31 December 2005 to review ongoing funding levels and details are included in Note 25.2. The Group contributed £29m to the Balfour Beatty Pension Fund for the year ended 31 December 2005 (2004: £30m).

Charges
Pension charges of £49m (2004: £48m, before £8m exceptional settlement gain) have been made to the income statement in accordance with IAS 19, including £37m (2004: £38m) for the Balfour Beatty Pension Fund.

Balance sheet impact
The Group's balance sheet includes the deficits of £280m (2004: £254m) for the Group's funds as required by IAS 19 on the assumptions set out in Note 25.1. The Group recorded net actuarial losses for 2005 on those funds totalling £21m (2004: £10m) as the effect of the lower discount rates applied to the funds' liabilities exceeded the effect of better than expected returns on the assets held by the funds.

Public Private Partnerships (PPP) and the Private Finance Initiative (PFI)
During 2005, the Group invested £61m in a combination of equity in and shareholder loans to its PFI/PPP project companies, including the acquisition of an additional 31.4% interest in the Consort Healthcare Edinburgh Royal Infirmary concession. At 31 December 2005, the Group had invested a total of £149m in equity in and subordinated loans to its 18 project companies and had committed to provide a further £80m over the period 2006 to 2010. The Group has also been appointed preferred bidder for a further four projects to which it is expected at financial close to commit to provide approximately £54m funding.

At 31 December 2005, the Group's share of non-recourse net debt within project companies amounted to £928m (2004: £688m), comprising £914m (2004: £444m) in relation to joint ventures and associates as disclosed in Note 15.2 and £14m (2004: £244m) on the Group balance sheet in relation to wholly-owned project companies as disclosed in Note 23.

The Directors have carried out a valuation of the Group's PFI/PPP concessions and this is set out on pages 32 to 33.

Treasury
The Group's policy remains to carry no significant net debt, other than the non-recourse borrowings of project companies.

The Group's financial instruments, other than derivatives, comprise cash and liquid investments, and borrowings. The Group enters into derivatives transactions (principally forward foreign currency contracts and interest rate swaps) to manage the currency and interest rate risks arising from the Group's operations and its sources of finance.

It is, and has been throughout the period under review, the Group's policy that no speculative trading in financial instruments shall be undertaken. Compliance with policy is monitored through regular reporting and internal audits. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

Finance and liquidity risk

Balfour Beatty's cash and liquid investments comprise cash, term deposits and the use of liquidity funds. Counterparty risk is monitored regularly and mitigated by limiting deposits in value and duration to reflect the credit rating of the counterparty. During 2005, the Group repaid US$120m of fixed rate loan notes maturing in 2008 and entered into a new series of bilateral facilities, the majority of which mature in 2010. Since 31 December 2005, these bilateral facilities have been reduced to £379m. The purpose of these facilities is to provide liquidity from a group of core relationship banks to support Balfour Beatty in its current and future activities.

Currency risk

The Group's businesses hedge their known foreign currency transactional exposures by taking out forward foreign exchange contracts. The Group decided in 2005 not to adopt hedge accounting for its foreign currency transactional exposures. As a result, there was a charge to profit of less than £1m which would otherwise have been charged to equity.

Balfour Beatty also faces currency exposures on the translation into sterling of the profits and net assets of overseas subsidiaries and associates, primarily in the US and Europe, and on its overseas trading transactions.

Balfour Beatty does not hedge these profit translation exposures as these are an accounting rather than cash exposure. However, the effect of volatile short-term currency movements on profits is reduced because the Group accounts for currency profits using average exchange rates.

Balfour Beatty's balance sheet translation exposure is managed by matching approximately 90% of significant net assets denominated in currencies other than sterling by way of currency borrowings and forward foreign exchange contracts. Details of the position and fair values at the year end are shown in Note 20.

Interest rate risk

The Group has no fixed rate borrowings (excluding PFI/PPP non-recourse term loans), following repayment of the Company's US$ fixed rate loan notes and termination of the associated swaps in June 2005.

Going concern

The Directors, having made appropriate enquiries, consider it reasonable to assume that the Group and the Company have adequate resources to continue for the foreseeable future and, for this reason, have continued to adopt the going concern basis in preparing the accounts.

Anthony Rabin Finance Director

Board of Directors

Sir David John KCMG Chairman
Non-executive Director
Age 67
Appointed a Director in 2000 and became Chairman in 2003. He is chairman of Premier Oil Group and The BSI Group, and immediate past chairman of The BOC Group. Formerly a director of Inchcape plc, he is a member of CBI International Advisory Board, and a governor of the School of Oriental and African Studies.

Ian Tyler Chief Executive
Age 45
A chartered accountant. A Director since 1999, he became Chief Executive on 1 January 2005, having been Chief Operating Officer since 2002 and prior to that, Finance Director. He joined Balfour Beatty in 1996 from the Hanson Group where he was finance director of ARC Ltd, one of its principal subsidiaries.

Anthony Rabin Finance Director
Age 50
A chartered accountant and a barrister. A Director since 2002, he is also responsible for the Group's Investments and Developments interests, having previously been managing director of Balfour Beatty Capital Projects. Prior to joining Balfour Beatty, Mr Rabin was a partner at Coopers and Lybrand and before that, a senior assistant director at Morgan Grenfell.

Jim Cohen Managing Director, Rail Engineering and Services
Age 64
An economist. A Director since 2000 having joined the Group in 1993. Prior to joining Balfour Beatty, he held senior management positions with GTE and GEC and prior to those, he was a senior civil servant at the Department of Energy. He is senior independent non-executive director of office2office plc, the office solutions and supplies group.

Peter Zinkin Planning and Development Director
Age 52
Joined the Group in 1981 and became Planning and Development Director in 1991 after a series of senior positions in the finance function. Previously, he worked at the London Business School and UMIST.

Right:
Sir David John
Middle row, left to right:
Ian Tyler; Anthony Rabin
Bottom row, left to right:
Jim Cohen; Peter Zinkin

Chalmers Carr Non-executive Director
Age 68
Appointed a Director in 2003. He is a solicitor who is a legal adviser to Standard Chartered plc, having previously been general manager and group legal adviser to HSBC Holdings plc for eight years. His career experience also includes senior legal and other management positions with Coutts & Co, the Central Electricity Generating Board, Bridon plc and GKN plc.

Steven Marshall Non-executive Director
Age 49
Appointed a Director in November 2005. A Fellow of the Chartered Institute of Management Accountants. He was executive chairman of Queens' Moat Houses plc until November 2004, having been chief executive of Railtrack Group plc, and prior to that group finance director, between 1999 and 2002. Previously, he was group chief executive of Thorn plc, having joined as finance director in 1995. He is currently non-executive chairman of Delta plc and also a non-executive director of Southern Water.

Gordon Sage Non-executive Director
Age 59
Appointed a Director in 2003. A chemical engineer, he is deputy chairman of ERM Holdings Ltd, the environmental services consultancy, and a non-executive director of Merrill Lynch World Mining Trust plc. Between 1970 and 2001 he held a series of increasingly senior positions in Rio Tinto plc, finally as executive director responsible for its industrial minerals and diamonds businesses.

Hans Christoph von Rohr Non-executive Director
Age 67
Appointed a Director in 2003. He is a partner of the international law firm TaylorWessing and a board member of several corporations. He is also chairman of the German Institute for Market Economy and Competition. Previously, he was chairman of the Industrial Investment Council and also chief executive officer of the German manufacturing group, Klöckner-Werke AG.

Robert Walvis Non-executive Director
Age 59
Appointed a Director in 2001. Previously with the Shell Group, latterly as chairman of the Corporate Centre of the Royal Dutch Shell Group of Companies. He is a non-executive director of Johnson Matthey plc. He is the senior independent Director.

Right:
Chalmers Carr

Middle row, left to right:
Steven Marshall; Gordon Sage

Bottom row, left to right:
Hans Christoph von Rohr; Robert Walvis

Remuneration Committee
Robert Walvis (Chair);
Chalmers Carr;
Richard Delbridge†;
Christoph von Rohr;
Steven Marshall*

Audit Committee
Steven Marshall* (Chair‡);
Chalmers Carr;
Christoph von Rohr;
Gordon Sage; Sir David Wright†;
Richard Delbridge†

Nomination Committee
Sir David John (Chair);
Gordon Sage; Ian Tyler;
Robert Walvis; Sir David Wright†;
Steven Marshall*

Business Practices Committee
Sir David John (Chair);
Chalmers Carr;
Christoph von Rohr;
Gordon Sage; Robert Walvis;
Sir David Wright†

* From 1 November 2005
† Retired 31 December 2005
‡ From 1 January 2006

Directors' report

Activities

The Chairman's statement and Chief Executive's review on pages 12 to 17, the Operating review on pages 22 to 31 and the Financial review on pages 34 to 37, report on the principal activities of the Group, its operations during 2005 and future developments in its businesses.

Dividends

The Directors recommend a final dividend on ordinary shares of 4.6p (net) per share, making, with the interim dividend of 3.5p, a total dividend for 2005 of 8.1p (net). Preference dividends totalling 10.75p (gross) per preference share have been paid for 2005.

Directors' interests

No Director had any material interest in any contract of significance with the Group during the period under review. The interests of Directors in the share capital of the Company and its subsidiary undertakings and their interests under the long-term incentive scheme (the Performance Share Plan 2001), and in respect of options, are set out in the tables in the Remuneration report beginning on page 44.

The Company has agreed to indemnify the Directors in the terms set out in Article 155 of the Company's Articles.

Share capital and major shareholders

Details of the share capital of the Company as at 31 December 2005 are set out in Note 27 on pages 85 and 86. During the year to 31 December 2005 no ordinary shares were repurchased for cancellation and 6,837,500 preference shares (representing 5% of the preference share capital) were repurchased for cancellation for a total consideration of £10,722,218 at an average price of 156.8p. 1,814,611 ordinary shares were issued following the exercise of options held under the Company's Savings-Related Share Option Scheme and 1,442,708 ordinary shares were issued following the exercise of options held under the Company's Executive Share Option Schemes. No other shares were issued during the year.

At 31 December 2005, the Directors had authority, under the shareholders' resolutions of 12 May 2005, to purchase through the market 42,397,267 ordinary shares and 19,004,566 preference shares at prices set out in those resolutions. This authority expires at the conclusion of the 2006 Annual General Meeting.

As at 7 March 2006, the Company had been notified in accordance with Sections 198 to 208 of the Companies Act 1985 of the following interests in its ordinary share capital:

Standard Life Investments Ltd	5.01%
HBOS plc	4.01%
Prudential plc (includes the interest of The Prudential Assurance Company Limited)	3.49%
The Prudential Assurance Company Limited (included in the interest of Prudential plc above)	3.47%
Legal and General Group plc	3.02%

Corporate Social Responsibility

Safety, Environment and Social Report

For the fifth year we are publishing a separate Safety, Environment and Social Report. A copy will be available to shareholders attending the Annual General Meeting and to preference shareholders attending the separate class meeting.

Group policies

Our published policies on Health & Safety, the Environment, Ethics and Human Rights remain in place and are subject to regular reviews. Our progress in the areas of Health & Safety and the Environment is described in the Safety, Environment and Social Report.

Employment

As the Group operates across a number of business sectors in different environments it has a decentralised management structure, with employment policies designed to suit the needs of individual businesses. However, each employing company is expected to comply with certain key principles in its design and practice of employment policy.

These are:

- to provide an open, challenging and participative environment;
- to enable all employees to utilise their talents and skills to the full, through appropriate encouragement, training and development;
- to communicate a full understanding of the objectives and performance of the Group and the opportunities and challenges facing it;
- to provide pay and other benefits which reflect good local practices and reward individual and collective performance; and
- to ensure that all applicants and employees receive equal treatment regardless of origin, gender, disability, sexual orientation, marital status, religion or belief.

Individual businesses use a variety of methods to communicate key business goals and issues to employees and also consult and involve their employees through local publications, briefing groups, consultative meetings, training programmes and working groups to assist the process of continuous improvement in the way they operate and do business. Regular publications inform employees of major business and technical achievements. Most of our UK based businesses have either attained or have committed to attain the UK Investors in People standard.

Regular communication is maintained with the in-service and pensioner members of the Balfour Beatty Pension Fund.

Donations

During 2005 the Group has both facilitated the raising of funds for charity and provided donations in cash and kind to charitable organisations, to a total aggregate sum of approximately £265,000. This sum had three main components.

First, the Group's regular efforts have been directed at three main charities: Groundwork, which carries out urban regeneration projects, Marie Curie, the cancer charity, and the Construction Industry Trust for Youth (now renamed Construction Youth Trust), which is active in seeking to support young people in acquiring basic skills through the medium of the construction industry. A total of £20,000 was contributed to Groundwork for two specific regeneration projects, one in Manchester and one in Sheffield. For Marie Curie, employees raised £65,000 through a variety of fund raising activities to which the Company added a further £15,000, making a total of £80,000. £5,000 was contributed to Construction Youth Trust.

Secondly, the Group has provided material assistance in kind, to an estimated value of £50,000, for the charitable organisation Engineers Against Poverty, which carries out small engineering projects in developing countries.

Finally, and as mentioned in the 2004 Annual Report, the Group provided considerable assistance both in practical terms and approximately £110,000 in cash for the relief of those affected by the earthquake and tidal wave on 26 December 2004. This help has been channelled through the Group's long established joint venture company in Indonesia and subsidiary company in Sri Lanka.

The Group continues to enable UK employees to donate through the Give-as-you-Earn scheme to various charities of their choice.

Taxation status

The Company is not a close company for taxation purposes.

Post balance sheet events

Details of post balance sheet events are set out in Note 34 on page 92.

Research and development

The Group continues to be committed to investment in research and development in all its areas of activity. This covers new products and processes and innovation in areas such as information technology and asset management systems.

We continue to undertake a range of development initiatives throughout our businesses which are supported by links with selected universities.

Details of the Group's 2005 research and development expenditure are given in Note 4.1 on page 63.

Political donations

Under the current law, shareholder authority is required for political donations to be made or political expenditure to be incurred by the Company or its subsidiaries in the EU. In common with previous years, no such donations or expenditure were made or incurred in 2005, and there is no intention to do so in the future. Because, however, the current law is so widely drafted, it remains unclear whether, for example, granting paid time off for local government or trade union activity could be regarded as political expenditure. It is for this reason, given the penalties for breaching the law, that the Company has sought, and will continue to seek, limited authority from shareholders to incur "political expenditure" in the EU.

In 2005, the Company's Georgia (US)-based Heery subsidiary made contributions in the US in accordance with state law amounting in aggregate to $10,500 to state political party committees and to campaign committees of various state candidates affiliated with the major parties. The amount and destination of the contributions were decided by US nationals in Heery and the funds in question have not been and will not be reimbursed by any non-US entity or person.

Payment of creditors

In the UK, the Company's policy is to settle the terms of payment with suppliers when agreeing the terms for each transaction or series of transactions; to seek to ensure that suppliers are aware of the terms of payment; and to abide by these terms of payment as and when satisfied that the supplier has provided the goods or services in accordance with the agreed terms. At 31 December 2005 the year end creditors' days of the Company were 21 (2004: 19).

Financial instruments

The Group's financial risk management objectives and policies are described in the Financial Review on pages 36 and 37, and its exposures to price risk, credit risk, liquidity risk and cash flow risk are included in Note 20 on page 74.

Statement of Directors' responsibilities

The following statement, which should be read in conjunction with the Independent Auditors' report on page 51, is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the auditors in relation to the financial statements.

The Directors are required to prepare financial statements for the Group in accordance with International Financial Reporting Standards (IFRS) and have also elected to prepare financial statements for the Company in accordance with IFRS. Company law requires the Directors to prepare such financial statements in accordance with IFRS, the Companies Act 1985 and Article 4 of the International Accounting Standard (IAS) regulation.

IAS 1 requires that financial statements present the Company's and the Group's financial position, financial performance and cash flows fairly (ie. give a true and fair view for each financial year). This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the IAS Board's "Framework for the preparation and presentation of Financial Statements". In nearly all circumstances, a fair presentation will be achieved by compliance with all applicable IFRS. Directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner which provides relevant, reliable, comparable and comprehensible information: and
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's and the Group's financial position and financial performance.

The Directors consider that they have met these requirements in preparing these financial statements. The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group, and are reasonably directed at safeguarding the assets and detecting and preventing fraud and other irregularities. Directors are also responsible for the preparation of a Directors' report and a Remuneration report which comply with the requirements of the Companies Act 1985.

Auditors

Deloitte & Touche LLP have indicated their willingness to continue as auditors to the Company and a resolution for their reappointment will be proposed at the Annual General Meeting.

Annual General Meeting

Sir David John, who chairs the Nomination and Business Practices Committees, Steven Marshall, who chairs the Audit Committee, and Robert Walvis, who chairs the Remuneration Committee, will be available at the Annual General Meeting to answer any questions arising from the work of these Committees. The Board regards the Annual General Meeting as an important occasion on which to communicate with shareholders, and research into subjects of likely interest to shareholders is undertaken so that questions can be answered during the meeting for the benefit of all shareholders present. Shareholders may also put questions in advance of the Annual General Meeting by writing to the Company Secretary. The business to be put to the Annual General Meeting is set out in the separate circular to shareholders.

Corporate governance and the Combined Code

Overview

The Board continues to endorse and apply the principles of good corporate governance reflected in the Combined Code (the "Code"), as appended to the Listing Rules of the UK Listing Authority.

The governance of the Company in the light of the principles and supporting principles and provisions of the Code is described in the following paragraphs. Throughout the year ended 31 December 2005 and save as otherwise explained in the paragraph headed "Compliance with Code" on page 43, we believe that the Company was in compliance with the provisions of the Code.

Honorary President

Viscount Weir is Honorary President of the Company, having been appointed to this position in May 2003, following his retirement as Chairman.

The Board

The Board currently comprises 10 Directors, of whom six, including the Chairman, are non-executive. During most of 2005, the Board comprised 12 Directors, with five executive Directors and seven non-executive Directors. Steven Marshall was appointed a non-executive Director on 1 November 2005. At the end of 2005, Richard Delbridge and Sir David Wright retired as non-executive Directors and Alistair Wivell retired as an executive Director. The Directors believe that the Board continues to include an appropriate balance of skills and, with them, the ability to provide effective leadership for the Group.

The Chairman of the Board is Sir David John, and the Chief Executive is Ian Tyler. Robert Walvis, who was appointed a non-executive Director in 2001 continues as senior independent Director. The chairman of the Audit Committee is Steven Marshall, who succeeded Richard Delbridge in that role on 1 January 2006. Sir David John continues as chairman of the Nomination Committee and Robert Walvis as chairman of the Remuneration Committee. Sir David John also chairs the Business Practices Committee.

The Board operates both formally, through Board and Board Committee meetings, and informally through regular contact between Directors as required. Decisions on a list of specific matters, including the approval of financial statements, major tenders and capital expenditure, and most acquisitions and disposals, are reserved to the Board or Board Committees. Matters falling outside the list are delegated to management.

Meetings of the Board are normally held in London, but meetings are on occasions held in other parts of the UK and overseas to enable Directors to visit the Group's businesses at the same time. In 2005, the July meeting was held at Terminal 5 Heathrow, where BAA kindly acted as host and Directors were able to see the project, in which a number of Group companies are involved, at first hand. The November meeting was held in Dallas, Texas, where the Directors were able to view with US management certain construction projects being carried out by the Group's US business.

Papers for Board meetings are generally sent out at least three days in advance of the meeting. These include a written report from each of the Chief Executive, the Finance Director, the director of Health, Safety and the Environment, and the group managing directors. At Board meetings, oral reports are made on issues arising from the written reports, and both those and other matters of immediate interest or concern are discussed by the Board. Apart from the Board meetings that approve the interim and final results respectively, and the Board meeting prior to the Annual General Meeting ("AGM"), a separate presentation on a topic of interest or concern, such as the operations of a particular business, is normally made to the Board. Each meeting lasts about four hours, but can be longer.

The Board met on 10 occasions in the course of 2005. A table showing attendance at these meetings and at meetings of the Audit Committee, the Nomination Committee, the Remuneration Committee and the Business Practices Committee, is on page 43. In addition, the non-executive Directors held two separate meetings during the year, one being attended by the Chairman and one taking place without the Chairman.

Chairman

Sir David John became Chairman in May 2003, having joined the Board in August 2000. Normally, Sir David spends two days per week on the business of the Company. He has other significant commitments as non-executive chairman of The BSI Group and of Premier Oil plc. The Board considers that his other commitments are not of such a nature as to hinder his activities as chairman of the Company or those as chairman of the Nomination and Business Practices Committees.

Directors
Brief biographical details of the Directors, including the Chairman, are given on pages 38 and 39. All the Directors shown served throughout the year save for Steven Marshall who was appointed on 1 November. In addition, Richard Delbridge, Alistair Wivell and Sir David Wright, who are not pictured, served as Directors throughout the year. Alistair Wivell retired on 31 December having joined the Company as a young engineer in 1966. Richard Delbridge joined the Board in 2002 and Sir David Wright at the beginning of 2003 and both also retired on 31 December. The Board considers that all the non-executive Directors continue to be independent.

From September 2003, non-executive Directors have been appointed for specific three year terms, and it is part of the terms of reference of the Nomination Committee to review all appointments of non-executive Directors at three year intervals and make recommendations to the Board accordingly. Mr Walvis's appointment was reviewed during 2005 and his appointment for a further three years was confirmed, subject to re-election as required by the Articles of Association.

Rotation of Directors, election and re-election
The Articles of Association of the Company provide that each Director shall retire from office in the third year following his last election, and shall be eligible for re-election. This year, the Directors who retire are Ian Tyler and Peter Zinkin. Each is seeking re-election, being eligible. In addition, Steven Marshall, who was appointed on 1 November 2005, seeks election.

Board Committees
The main Board Committees, the membership of which is either wholly or substantially comprised of non-executive Directors, continue to be the Audit Committee, the Nomination Committee, the Remuneration Committee and the Business Practices Committee.

Reports on the workings of these Committees are set out below. The report of the Remuneration Committee can be found in the Remuneration Report beginning on page 44.

– The Audit Committee
The membership of this Committee currently comprises Steven Marshall (the Committee chairman), Chalmers Carr, Christoph von Rohr and Gordon Sage. Christopher Pearson, the Company Secretary, remains secretary of the Committee. The Committee was chaired throughout 2005 by Richard Delbridge, who retired at the end of the year. Sir David Wright, who retired at the same time as Richard Delbridge, also served on the Committee throughout the year. Steven Marshall joined the Committee on 1 November 2005, and took over as chairman on 1 January 2006. All of the members have extensive experience of management in large international organisations. The Committee chairman, Steven Marshall, is an accountant and a former group finance director of Thorn plc and Railtrack plc.

The terms of reference for the Committee, based on the Smith report and the requirements of the Code, were approved by the Board in October 2003 and remain unchanged. They are available on the Company's website. The main responsibilities of the Audit Committee are as stated in last year's report: to monitor the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance; to review the Group's internal financial controls established to identify, assess, manage and monitor financial risks, and receive reports from management on the effectiveness of the systems they have established and the conclusions of any testing carried out by the internal and external auditors; to monitor and review the effectiveness of the internal audit function; to make recommendations to the Board in relation to the appointment of the external auditor and to approve the remuneration and terms of engagement of the external auditor; to assess the independence, objectivity and effectiveness of the external auditor and to develop and implement policy on the engagement of the external auditor to supply non-audit services; and to review arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting.

Appointments to the Committee are made by the Board for a period of up to three years, extendable by no more than two additional three year periods, so long as members continue to be independent. Any additional remuneration of members of the Committee is set by the executive Directors and the Chairman. At the Board meeting following each meeting of the Committee, the Committee chairman provides an oral report on the work of the Committee and any significant issues that may have arisen. The minutes of Committee meetings are circulated to all members of the Board.

In May 2003 it was decided to increase the number of regular meetings each year from three to four, and four principal meetings were held in 2005. A fifth meeting was also held during the year to review and recommend to the Board the announcement (which was made on 23 June) concerning the impact on Group financial statements of the transition from UK GAAP to IFRS. At the invitation of the Committee, partners from the external auditor, the Head of Internal Audit, the Finance Director and the Chairman regularly attend each meeting. In addition, any independent non-executive Director who is not a member has an open invitation to attend meetings.

In 2005, as in previous years, the Committee met prior to the Board meetings at which the interim financial statements and the annual report and accounts were approved. The Committee reviewed significant accounting policies, financial reporting issues and judgements and, in conducting these reviews, considered reports from the external auditor, finance management and internal audit.

Throughout 2005 the Committee continued to review the Group's risk management processes, and to consider findings from the internal audit reviews of internal controls and reports on the status of the correction of any weaknesses in internal controls identified by the internal or external auditors. During the year the Committee reviewed the external auditor's Group management letters on accounting procedures and the systems of internal financial control.

It considered the effectiveness of the external audit process, the audit strategy and plan and the qualifications, expertise and resources of the external auditor, Deloitte & Touche LLP ("Deloitte"). It reviewed and approved the proposed audit fee and terms of engagement for the 2005 audit and recommended to the Board that it propose to shareholders that Deloitte continues as the Company's external auditor.

It reviewed the independence procedures of Deloitte and received a letter from Deloitte confirming that, in their opinion, they remained independent of the Company. Non-audit work remains covered by the policy on non-audit work which was approved by the Board in June 2003. The policy was briefly described in our last Annual Report on page 42, and remains unchanged from last year. An analysis of non-audit fees incurred in 2005 is set out in Note 4.2 on page 63.

Finally, the Committee continued to receive regular reports on the work of the internal audit function and reviewed the effectiveness of the department during the year. The Head of Internal Audit has direct access to the Audit Committee chairman and at each of the four main Committee meetings during the year, the Committee held a separate meeting with each of the Head of Internal Audit, the Finance Director and Deloitte.

– The Nomination Committee
The Committee was established by the Board in November 2003. Its terms of reference are available on the Company's website.

The Committee continues to be chaired by Sir David John. Its other members currently are Gordon Sage, Robert Walvis, Ian Tyler and Steven Marshall. The secretary of the Committee is Paul Raby, director of human resources. Sir David Wright served on the Committee throughout the year until his retirement from the Board.

The Committee met on two occasions in 2005, firstly to consider the terms of reference for the identification of a new non-executive Director, secondly to consider candidates for the position of non-executive Director, and then to recommend to the Board, the appointment of Steven Marshall as a non-executive Director of the Company. The candidates, including Mr Marshall, were interviewed initially and put forward by an external recruitment firm experienced in seeking candidates for non-executive positions.

– The Remuneration Committee
Information about the working and membership of this Committee is contained in the Remuneration report beginning on page 44.

– The Business Practices Committee
The Business Practices Committee is chaired by Sir David John, and throughout the year its other members were Chalmers Carr, Christoph von Rohr, Gordon Sage, Robert Walvis and Sir David Wright. Christopher Pearson, the Company Secretary, is secretary to the Committee. Its terms of reference cover matters of business conduct, ethics, reputation, health, safety and the environment and matters of corporate social responsibility generally. It is also charged with reviewing the effectiveness of the whistle-blowing procedures established in the Group.

The Committee met four times in 2005. Among matters considered by the Committee in 2005 were: the final draft of the Safety, Environmental and Social report (published in May), health & safety statistics from around the Group, reports from the charities committee, the introduction of an expanded ethical framework for the Group and the Group's whistle-blowing policy.

Details of the number of meetings of, and attendances at, the Board and the Audit, Nomination, Remuneration and Business Practices Committees during the year are set out in the table following. The relevant total number of meetings held in 2005 in each case is included in brackets after the name of the Board or Committee.

Name of Director	Board (10)	Audit (5)	Nomination (2)	Remuneration (7)	Business Practices (4)
C Carr	9	5		7	4
J L Cohen	9				
R Delbridge	10	5		7	
Sir David John	9		2	1*	4
S Marshall**	2	1		1	1
A L P Rabin	10				
Dr H C von Rohr	10	3		6	3
G H Sage	9	4	2		3
I P Tyler	10		2		
R J W Walvis	10		1	6	3
A J Wivell	10				
Sir David Wright	9	2	2		2
P J L Zinkin	9				

*Resigned from Remuneration Committee with effect from 1 February 2005.
**Appointed 1 November 2005.

Board, Committee and individual director evaluation

The Board's responsibilities are listed in a schedule of matters reserved for its attention. These were reviewed and updated during the year.

As reported in last year's report, the Board as a whole and its main Committees were the subject of an evaluation exercise carried out in 2004 by an external consultant. The actions agreed which arose from the report have been implemented through 2005, and the process continues.

No further evaluation exercise has been carried out in 2005. In particular, and as reported last year, individual evaluation is seen as the second stage in the process, and most likely to be of benefit when the Directors have had more time to work together as a board. Given the four board changes towards the end of 2005, any individual evaluation is unlikely to be carried out in 2006 but will be considered for 2007, as part of another full board evaluation exercise.

Dialogue with shareholders

The Company has a long-established programme of regular communication with institutional investors and brokers and this continues. Presentations are made to brokers' analysts, the press and institutional investors at the time of the announcement of final and half-year results and there are regular meetings with analysts and investors throughout the year, which are organised through the Company's brokers, so that the investment community can be kept informed of longer term strategic matters and can communicate their views to the Board. We expect to continue this programme, within the constraints of relevant legislation and practice. The Group's website is a regular channel of communication with shareholders and others.

Regular reports are made by executive Directors to the Board on meetings and other contact with major shareholders or their representatives. The Chairman on occasion attends meetings with shareholders. The non-executive Directors believe that, by having direct and ready access to the Chairman at all times, through the senior independent Director and by reports given at Board meetings, they are kept fully aware of the views of the larger shareholders and the wider investment community. It is open to them or any of them to attend or arrange meetings with investors if they wish to do so.

Compliance with Code

The Company believes it is compliant with the Code save in the following respects:

(a) The effectiveness of the Group's whistle-blowing procedures is reviewed by the Business Practices Committee, and not the Audit Committee. This is because, based on experience, the great majority of "whistle-blowing" type complaints arise out of non-financial matters, mainly employment-related. The Audit Committee is copied with all whistle-blowing reports made to the Business Practices Committee.

(b) An individual director evaluation exercise has not yet been carried out, as explained above.

Risk management

The Board takes ultimate responsibility for the Group's systems of risk management and internal control and reviews their effectiveness. The Board has continued to assess the effectiveness of the risk management processes and internal controls during 2005, based on reports made to the Board, the Audit Committee and the Business Practices Committee, including:

- results of internal audit's reviews of internal financial controls;
- a Group-wide certification that effective internal controls had been maintained, or, where any significant non-compliance or breakdown had occurred with or without loss, the status of corrective action; and
- a paper prepared by management on the nature, extent and mitigation of significant risks and on the systems of internal controls.

The Group's systems and controls are designed to ensure that the Group's exposure to significant risk is properly managed, but the Board recognises that any system of internal control 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 misstatement or loss. In addition, not all the material joint ventures in which the Group is involved are treated, for these purposes, as part of the Group. Where they are not, systems of internal control are applied as agreed between the parties to the venture.

Central to the Group's systems of internal control are its processes and framework for risk management. These accord with the Turnbull Guidance on internal controls and were in place throughout the year and up to the date of signing this report.

The Group's systems of internal control operate through a number of different processes, some of which are interlinked. These include:

- the annual review of the strategy and plans of each operating company and of the Group as a whole in order to identify, inter alia, the risks to the Group's achievement of its overall objectives and, where appropriate, any relevant mitigating actions;
- monthly financial reporting against budgets and the review of results and forecasts by executive Directors and line management, including particular areas of business or project risk. This is used to update both management's understanding of the environment in which the Group operates and the methods used to mitigate and control the risks identified;
- individual tender and project review procedures commencing at operating company level and progressing to Board Committee level if value or perceived exposure breaches certain thresholds;
- regular reporting, monitoring and review of health, safety and environmental matters;
- the review and authorisation of proposed investment, divestment and capital expenditure through the Board's Committees and the Board itself;
- the review of specific material areas of Group-wide risk and the formulation and monitoring of risk mitigating actions;
- the formulation and review of properly documented policies and procedures, updated through the free and regular flow of information to address the changing risks of the business;
- specific policies set out in the Group Finance Manual, covering the financial management of the Group, including arrangements with the Group's bankers and bond providers, controls on foreign exchange dealings and management of currency and interest rate exposures, insurance, capital expenditure procedures, application of accounting policies and financial controls;
- a Group-wide risk management framework which is applied to all functions in the Group, whether operational, financial or support. Under it, the key risks facing each part of the Group are regularly reviewed and assessed, together with the steps to avoid or mitigate those risks. The results of those reviews are placed on risk registers and, where necessary, specific action plans are developed;
- reviews and tests by the internal audit team of critical business financial processes and controls and spot checks in areas of perceived high business risk; and
- the Group's whistle-blowing policy.

Directors' report
Signed by order of the Board

C R O'N Pearson
Secretary
7 March 2006

Remuneration Committee

The Remuneration Committee of the Board ("RemCo") is primarily responsible for determining the remuneration policy and conditions of service for executive Directors and the Chairman of the Company. It also reviews and monitors the level and structure of remuneration for senior management immediately below the level of the Board. The terms of reference of the RemCo can be found on the Company's website and are available on request from the Company Secretary.

The RemCo consists entirely of independent non-executive Directors and has been chaired by Robert Walvis since November 2003. Its other members are Chalmers Carr, Steven Marshall (from his appointment on 1 November 2005) and Christoph von Rohr. Sir David John and Richard Delbridge were members of the RemCo until 1 February 2005 and 31 December 2005 respectively when they resigned from this Committee. Since resignation, Sir David John has attended by invitation. No member of the RemCo has any personal financial interest, other than as a shareholder, in the matters to be decided by the RemCo, nor potential conflicts of interest arising from cross-directorships, and no member of the RemCo has any day-to-day involvement in the executive management of the Group.

During 2005 the Chief Executive, Ian Tyler, was invited to join meetings of the RemCo when appropriate. Paul Raby, the human resources director, has acted as secretary of the RemCo since his appointment on 1 July 2005. Prior to this, Peter Johnson, the director of personnel, was secretary of the RemCo.
No Director has any involvement in discussions relating to his own remuneration.

The RemCo is responsible for appointing external independent consultants to advise on executive remuneration matters. This advice and assistance has been provided to the RemCo throughout the year by the Monks Partnership ("Monks"), New Bridge Street Consultants LLP ("NBSC"), and the human resources director. The terms of reference of the independent consultants are available on the Company's website and on request from the Company Secretary. Monks also provided data and advice to the Company regarding the remuneration of senior management below Board level during the year. The RemCo is satisfied that no conflict of interest arises from the provision of this advice to the Company.

Executive Directors' remuneration

General policy

It is the policy of the RemCo to provide an overall remuneration package that is competitive and which facilitates the recruitment and retention of high calibre management. The annual and long-term incentive plans make up an important part of each executive Director's remuneration and are structured so as to motivate senior managers to deliver high standards of performance, without encouraging excessive risk taking. It is intended that the share-based elements of the package will not only drive performance over the long-term but will also assist in aligning the interests of management with those of shareholders.

During the course of 2005, the RemCo, assisted by NBSC, has reviewed the long-term incentive arrangements in place at the Company, as the existing Performance Share Plan ("PSP"), approved by shareholders in 2001, expires in 2006. As a result of this review, a replacement long-term incentive arrangement is being proposed and this is described in the relevant section below. Under the proposed arrangement, if target performance is achieved, basic salary will represent around one half of total earnings. If maximum is achieved, which would involve a superior level of performance substantially in excess of business plan, basic salary will represent around one third of total earnings.

Executive Directors can join the Balfour Beatty Pension Fund. The RemCo has considered the policy it will adopt regarding pension provision after April 2006 in the light of the government's changes to pension taxation, and this is described below.

Basic salaries

It is the policy of the RemCo to set basic salaries at levels which it believes are competitive given the size and complexity of the Company, as well as the broad business sectors in which it operates. To assist in this, Monks and NBSC provide data and independent advice on remuneration levels in companies considered to be comparable in terms of annual sales, market capitalisation and industry sector. The RemCo looks to set basic salaries at around the median of the identified market, but also takes into account its own judgement of the performance of the Group's businesses and the performance of individual Directors. The RemCo intends to continue to use this approach in the foreseeable future.

The basic salaries of executive Directors are reviewed annually at 1 July and the basic salaries following the review at 1 July 2005 are shown in the table below. The average increase was 5.5%.

Name of Director	Salary at 1 July 2005
J L Cohen	£315,000
A L P Rabin	£325,000
I P Tyler	£470,000
A J Wivell	£315,000
P J L Zinkin	£338,000

Annual incentive plan

Each executive Director participates in an annual incentive plan, under which predetermined financial targets must be achieved before any payment is earned. The maximum potential bonus which could have been earned by executive Directors for 2005 was 80% of basic salary and the performance indicator chosen was profit before tax and exceptional items. A bonus of 40% of basic salary would have been earned for the achievement of performance in line with target. Two-thirds of these bonuses are payable in cash, while the remaining one-third is deferred in the form of ordinary shares of the Company. These shares will be released to the Directors after three years, providing they are still employed by the Company at that time. Bonuses are non-pensionable. The actual profit for the year ended 31 December 2005 resulted in a bonus of 46.94% of basic salary for each executive Director. Details are shown in the table on page 47.

The annual incentive plan for 2006 will operate in the same way as for 2005 and the RemCo will continue to review the competitiveness and structure of the annual incentive plan in future years.

Long-term incentive scheme

The RemCo believes that performance related long-term incentives which align executives with both business strategy and shareholders' interests are an important component of overall executive remuneration arrangements.

Following the review of long-term incentives operated by the Company and the expiry of the PSP, proposals for a new Performance Share Plan ("new PSP") will be put to shareholders at the 2006 AGM. Full details of the proposals can be found in the circular accompanying this report and a summary of the policy for 2006 is given below.

Conditional awards of ordinary shares of the Company will be made to executive Directors and other selected operational and functional senior managers. The maximum market value of any award, at the award date, will be 150% of basic salary, other than in exceptional circumstances, where the limit is 200% of basic salary. It is the intention of the RemCo that initially an award of 150% of basic salary will only be made to the Chief Executive, with the other executive Directors receiving conditional awards over shares with a market value of 125% of basic salary.

The awards will vest, subject to the achievement of performance conditions, three years after the date of grant. For the initial award under the new arrangement, there will be two performance conditions each applying to separate parts of an award.

50% of an award will be linked to an earnings per share before exceptional items ("EPS") growth target, and will vest as shown in the table below:

EPS growth over three years	Proportion of award vesting
Less than RPI + 15%	Zero
RPI + 15%	25%
RPI + 45%	100%
Between RPI + 15% and RPI + 45%	Between 25% and 100% pro rata

Growth in EPS will be determined following independent verification of the calculations made internally.

The performance condition attached to the other 50% of an award will be based on total shareholder return ("TSR") performance, measured against a group of UK listed companies operating in comparable markets to the Company. The companies to be used for the initial award are as follows: Aggreko, AMEC, WS Atkins, Babcock International, Capita, Carillion, Costain, Enterprise, Hanson, Interserve, Keller, Kier, John Laing, Alfred McAlpine, Morgan Sindall, Serco, Travis Perkins and Wolseley.

The TSR performance of all companies will be measured over the three year performance period, with the TSR of Balfour Beatty compared to the TSR of the other companies. This part of an award will vest (in part) if Balfour Beatty's TSR is equivalent to that of the company whose TSR performance is at the median, with full vesting if Balfour Beatty's TSR is equivalent to, or above, that of the company whose TSR performance is at the upper quartile. The precise scale of vesting is shown in the table below:

Total shareholder return	Proportion of award vesting
Below median	Zero
Median	25%
Upper quartile	100%
Between median and upper quartile	Between 25% and 100% pro rata

TSR will be independently calculated and verified by the RemCo.

There will be no provision for the re-testing of these performance conditions.

The RemCo considers that the EPS and TSR performance conditions provide a good blend of performance metrics, with EPS growth rewarding strong financial performance and TSR rewarding stock market performance, providing a strong and direct alignment with the interests of shareholders.

If approved by shareholders at the AGM, it is the intention of the RemCo to make awards under the new PSP in 2006 and in future years, subject to review.

Pensions

The Company's pension policy has been reviewed in the light of the changes to the taxation of pensions being introduced from April 2006. The Company will not be compensating any member of the Balfour Beatty Pension Fund ("Fund") (or any other pension scheme operated by the Company) for any additional tax which is payable as a result of the new legislation. In the event of a member choosing to opt out of the Fund as a result of their benefits reaching or exceeding the Lifetime Allowance, a cash supplement will be payable to them. An earnings cap will be maintained in the Fund for those members who are subject to the existing earnings cap and, in line with current policy, a discretionary cash supplement will be paid. Members who are currently benefiting from contributions to a Funded Unapproved Retirement Benefit Scheme ("FURBS") will be given the option of taking a cash supplement of equivalent value.

Share ownership guidelines

To further align the interests of senior management with those of shareholders, executive Directors and other key senior managers are subject to share ownership guidelines. Executive Directors will be required to build up a holding in ordinary shares of the Company to the value of 100% of basic salary. In order to achieve this, they will be expected to retain at least half of the shares (after payment of any taxes due) which vest from awards made under the new PSP and the annual incentive plan.

Executive share options

Since the introduction of the PSP in 2001, it has been the RemCo's policy only to make grants of executive share options to participants in the PSP in exceptional circumstances, for example to recruit a high calibre individual. Grants of options over ordinary shares of the Company were made to executive Directors before this date, some of which remain valid and unexercised and are detailed in the table on page 49. Certain managers below the level of those participating in the PSP have, in 2004 and previous years, been granted options under the Executive Share Option Scheme 2001. For 2005, selected managers have participated in an annual incentive plan with a deferred share element similar to that described above, but with lower levels of maximum bonus. It is intended that no further grants of executive share options will be made to any level of management, except when it is necessary to facilitate the recruitment of an outstanding individual.

Savings-related share option scheme

The Company continues to operate an Inland Revenue approved savings-related share option scheme ("SAYE") under which employees are granted an option to purchase shares in the Company in either three or five years time, dependent upon their entering into a contract to make monthly contributions to a savings account over the relevant period. These savings are used to fund the option exercise. The exercise price for the SAYE options granted in 2005 was at a 20% discount to market value at the date of invitation. This scheme is open to all employees with one year's service who are based in the UK, including executive Directors, and performance conditions are not applied to the exercise of SAYE options.

Executive Directors: notice periods

Since 1999, it has been the Company's policy and practice to include in executive Directors' contracts a 12 month rolling notice period from the Company and six months' notice on the part of the Director. This policy will continue in the future.

Details of the service contracts of the executive Directors are shown in the table below.

Name of Director	Date of contract	Notice period from Company (months)
J L Cohen	11 February 2000	12
A L P Rabin	28 August 2002	12
I P Tyler	22 December 2004	12
A J Wivell*	23 July 2002	12
P J L Zinkin	10 December 1991	12

*Retired from the Company on 31 December 2005.

Service contracts of executive Directors do not include provision for specific payment in the event of early termination, nor do they provide for extended notice periods in the event of a change of control. It is not the RemCo's intention to introduce such provisions. If any existing contract of employment is breached by the Company in the event of termination, the Company would be liable to pay, as damages, an amount approximating to the net loss of salary and contractual benefits for the unexpired notice period. The RemCo will seek to ensure that the Director fulfils his obligation to mitigate his losses and will also give consideration to phased payments where appropriate.

External appointments
The RemCo recognises that benefits can arise from allowing executive Directors to take a non-executive role elsewhere. With approval of the Board in each case, executive Directors may therefore accept one external appointment and retain any related fees. Jim Cohen was appointed as a non-executive Director of office2office plc on 29 June 2004 and fees of £32,972 were paid to him for his services during the year ended 31 December 2005.

Non-executive Directors
Non-executive Directors are appointed by the full Board following recommendations from the Nomination Committee. The Chairman's remuneration falls within the remit of the RemCo and the Board determines the terms on which the services of other non-executive Directors are provided. All non-executive Directors are elected for a term of three years and must retire and if eligible seek re-election at the AGM in the third calendar year following the year they were elected (or last re-elected). They are not eligible to join the Balfour Beatty Pension Fund and cannot participate in any of the Company's share option, annual incentive or long-term incentive schemes. None of the appointment letters for non-executive Directors contain provision for specific payment in the event of termination for whatever cause.

The dates of the letters of appointment or last election of the non-executive Directors are shown in the table below.

Name of Director	Date of appointment or last election	Unexpired period at 31 December 2005 (months)
C Carr	13 May 2004	17
R Delbridge*	12 May 2005	–
Sir David John	13 May 2004	17
S Marshall	1 November 2005	34
G H Sage	13 May 2004	17
Dr H C von Rohr	13 May 2004	17
R J W Walvis	13 May 2004	17
Sir David Wright*	15 May 2003	–

*Retired on 31 December 2005.

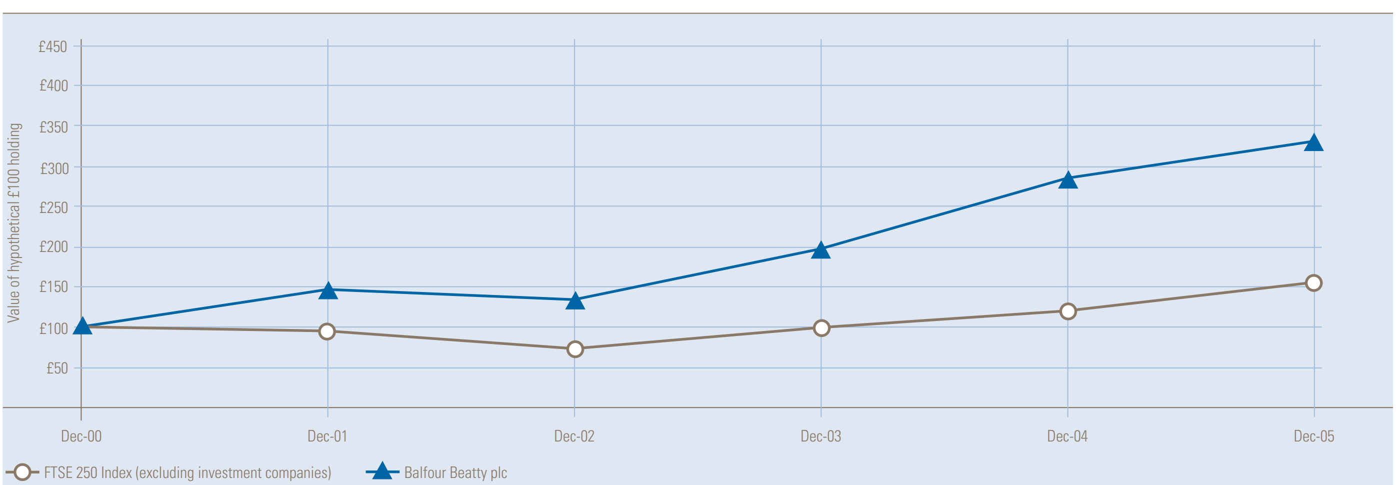
The fees of the non-executive Directors are reviewed from time to time, the last review taking place in 2004, when the Board agreed an annual fee for the non-executive Directors (excluding the Chairman) of £33,000 with effect from 1 July 2004. The RemCo also approved fees of £173,000 per annum for the Chairman with effect from 1 July 2004.

Additional fees of £6,000 per annum were payable to Robert Walvis and Richard Delbridge for their chairmanship of the RemCo and Audit Committees respectively through 2005, and will be paid to Steven Marshall on his appointment as chairman of the Audit Committee from 1 January 2006. A fee of €30,000 per annum is payable to Christoph von Rohr for his chairmanship of the supervisory board of Balfour Beatty Rail GmbH.

Performance graph
The graph below shows Balfour Beatty's Total Shareholder Return ("TSR") performance compared to the FTSE 250 Index (excluding investment companies) TSR over the five financial years ended 31 December 2005.

The values indicated in the graph show the share price growth plus reinvested dividends from a £100 hypothetical holding of ordinary shares in Balfour Beatty plc and in the index at the start of the period and have been calculated using 30 trading day average values.

As in last year's report, the RemCo has elected to compare the TSR on the Company's ordinary shares against the FTSE 250 Index (excluding investment companies) principally because this is a broad index of which the Company is a constituent member.



The detailed information about the Directors' remuneration, set out on pages 47 to 50, has been reported on by the Company's independent auditors, Deloitte & Touche LLP.

Directors' remuneration earned in 2005

Name of Director	Basic salary £	Fees £	Benefits in kind £	Annual bonus £	Total remuneration 2005 £	Total remuneration 2004 £
C Carr	–	33,000	–	–	33,000	31,500
J L Cohen	307,500	–	16,793	98,574	422,867	406,479
R Delbridge	–	39,000	–	–	39,000	37,500
Sir David John	–	173,000	–	–	173,000	169,000
S Marshall	–	5,500	–	–	5,500	–
A L P Rabin	315,000	–	17,352	101,703	434,055	409,282
G H Sage	–	33,000	–	–	33,000	31,500
I P Tyler	455,000	–	24,238	147,079	626,317	476,769
Dr H C von Rohr	–	53,548	–	–	53,548	51,908
R J W Walvis	–	39,000	–	–	39,000	37,000
A J Wivell	307,500	–	20,521	147,861	475,882	404,044
Sir David Wright	–	33,000	–	–	33,000	31,500
P J L Zinkin	331,500	–	15,668	105,771	452,939	439,118
Former Directors	–	–	–	–	–	713,972
Total	1,716,500	409,048	94,572	600,988	2,821,108	3,239,572

Notes:
(i) Basic salary and fees were those paid in respect of the period of the year during which individuals were Directors.
(ii) The performance target for annual bonus was profit before tax and exceptional items ("profit"). The profit for the year ended 31 December 2005 resulted in a bonus of 46.94% of basic salary for each executive Director. For Jim Cohen, Anthony Rabin, Ian Tyler and Peter Zinkin two-thirds of this bonus is payable in cash and these are the amounts shown in the table above. The remaining one-third will be deferred in the form of ordinary shares of the Company which will be released to the Director on 31 March 2009, providing he is still employed by the Company at that time. The number of shares comprising the deferred element will be determined based on the share price at the award date of 31 March 2006. As Alistair Wivell retired on 31 December 2005, the entire bonus is payable in cash in March 2006 and this amount is given in the table above.
(iii) Christoph von Rohr receives a €30,000 per annum fee for his chairmanship of the supervisory board of Balfour Beatty Rail GmbH.
(iv) Benefits in kind are calculated in terms of UK taxable values. For the executive Directors they comprise: a fully expensed car, a fuel card, and private medical insurance for the Director and his immediate family.
(v) No Director receives any expense allowance.

Directors' interests

The interests of the Directors and their immediate families in the share capital of Balfour Beatty plc and its subsidiary undertakings during the year are set out below.

	Number of ordinary shares	
Name of Director	At 1 January 2005	At 31 December 2005
J L Cohen	79,286	120,922
R Delbridge	15,000	15,000
Sir David John	5,000	5,000
A L P Rabin	25,239	56,331
G H Sage	5,000	5,000
I P Tyler	63,981	85,515
R J W Walvis	10,000	10,000
A J Wivell	20,228	30,228
P J L Zinkin	51,049	75,343

Notes:
(i) In common with other employees of the Balfour Beatty Group, the executive Directors have an interest, as potential beneficiaries, in the entire shareholding of the Balfour Beatty Employee Share Ownership Trust, which at 31 December 2005 amounted to1.512m ordinary shares of Balfour Beatty plc.
(ii) All interests at the dates shown are beneficial and are in respect of 50p ordinary shares of Balfour Beatty plc. There were no changes between 31 December 2005 and 7 March 2006.
(iii) Peter Zinkin was also interested at 1 January 2005 and 31 December 2005 in 325 cumulative convertible redeemable preference shares of 1p each of Balfour Beatty plc.

Directors' long-term incentives: the Performance Share Plan

		Maximum number of shares subject to award					
Name of Director	Date granted	At 1 January 2005	Awarded during the year	Lapsed during the year	Vested during the year	At 31 December 2005	Exercisable from
J L Cohen	17 April 2002	105,226	–	35,819	69,407	–	
	16 April 2003	156,376	–	–	–	156,376	April 2006
	19 April 2004	109,439	–	–	–	109,439	April 2007
	18 April 2005	–	98,226	–	–	98,226	April 2008
A L P Rabin	17 April 2002	71,553	–	24,357	47,196	–	
	16 April 2003	150,584	–	–	–	150,584	April 2006
	19 April 2004	107,519	–	–	–	107,519	April 2007
	18 April 2005	–	99,863	–	–	99,863	April 2008
I P Tyler	17 April 2002	105,226	–	35,819	69,407	–	
	16 April 2003	179,543	–	–	–	179,543	April 2006
	19 April 2004	126,719	–	–	–	126,719	April 2007
	18 April 2005	–	144,065	–	–	144,065	April 2008
A J Wivell	17 April 2002	65,307	–	22,231	43,076	–	
	16 April 2003	150,584	–	–	–	150,584	April 2006
	19 April 2004	107,519	–	107,519	–	–	
	18 April 2005	–	98,226	98,226	–	–	
P J L Zinkin	17 April 2002	110,404	–	37,582	72,822	–	
	16 April 2003	167,960	–	–	–	167,960	April 2006
	19 April 2004	119,039	–	–	–	119,039	April 2007
	18 April 2005	–	106,411	–	–	106,411	April 2008

Notes:

(i) All awards are granted for nil consideration and are in respect of 50p ordinary shares of Balfour Beatty plc.

(ii) For the awards made in April 2004 and April 2005, the performance periods are the three years ending 31 December 2006 and 31 December 2007 respectively. The maximum award of shares shown in the table above will vest only if earnings per share before exceptional items, goodwill amortisation and appropriations arising on the buy-back of preference shares ("EPS") grows by at least 70% over the performance period. If EPS growth is 25%, the Directors will be entitled to 30% of the maximum award of shares. If EPS growth is between 25% and 70%, the number of shares vesting will be pro rata to actual growth. No shares will vest if EPS growth is less than 25%, and there is no provision for re-testing.

(iii) For the awards made in April 2003, the performance period was the three years ended 31 December 2005. The maximum award of shares shown in the table above would only vest if EPS grew by at least 100% over the performance period. If EPS growth was 30%, the Directors would have been entitled to 30% of the maximum award of shares. If EPS growth was between 30% and 100%, the number of shares vesting would have been pro rata to actual growth. No shares would vest if EPS growth was less than 30%, and there is no provision for re-testing.

(iv) The performance period for the awards made in April 2003 was completed on 31 December 2005. The growth in EPS for this period was 49.07% and as a result, 49.07% of each participant's conditional award will vest on 16 April 2006.

(v) The performance period for the awards made in April 2002 was completed on 31 December 2004. The growth in EPS for this period was 65.96% and as a result, 65.96% of each participant's conditional award vested on 17 April 2005. The closing middle market price of ordinary shares on the vesting date was 297.0p.

(vi) The awards made to Alistair Wivell in 2004 and 2005 lapsed on his retirement from the Company on 31 December 2005. However, since he had been employed by the Company for the entirety of the performance period for the 2003 award, the RemCo decided it was appropriate to exercise its discretion in his favour and allow him to retain this award on his retirement from the Company, exercisable at the same time and in the same proportion as the awards of other participants.

(vii) The average middle market price of ordinary shares in the Company for the three dealing dates before the date of the 2002 award under the PSP, which was used for calculating the number of awards granted, was 237.583p, for the 2003 award was 172.66p, for the 2004 award was 260.417p and for the 2005 award was 305.417p. The closing middle market price of ordinary shares on the date of the awards was 251p, 170.5p, 260p and 290p respectively.

Directors' share options

Name of Director	Date granted	At 1 January 2005	Granted during the year	Exercised during the year	Lapsed during the year	At 31 December 2005	Exercise price	Exercisable from	Exercisable to
		Number of options							
J L Cohen									
Executive Share Options	13 April 1995	15,340	–	–	15,340	–	311.9p	April 1998	April 2005
Savings-Related Options	8 May 2002	743	–	743	–	–	184.0p	July 2005	December 2005
	5 May 2004	646	–	–	–	646	210.0p	July 2007	December 2007
	4 May 2005	–	803	–	–	803	250.0p	July 2008	December 2008
A L P Rabin									
Executive Share Options	17 April 1996	10,227	–	–	–	10,227	344.2p	April 1999	April 2006
Savings-Related Options	24 May 2000	3,286	–	3,286	–	–	76.0p	August 2005	January 2006
	19 July 2001	1,227	–	–	–	1,227	154.0p	October 2006	March 2007
	8 May 2002	575	–	–	–	575	184.0p	July 2007	December 2007
	7 May 2003	444	–	–	–	444	133.0p	July 2008	December 2008
	5 May 2004	903	–	–	–	903	210.0p	July 2009	December 2009
	4 May 2005	–	1,031	–	–	1,031	250.0p	July 2010	December 2010
I P Tyler									
Savings-Related Options	8 May 2002	640	–	640	–	–	184.0p	July 2005	December 2005
	7 May 2003	511	–	–	–	511	133.0p	July 2006	December 2006
	4 May 2005	–	1,046	–	–	1,046	250.0p	July 2008	December 2008
A J Wivell									
Executive Share Options	13 April 1995	15,340	–	–	15,340	–	311.9p	April 1998	April 2005
P J L Zinkin									
Savings-Related Options	24 May 2000	2,842	–	2,842	–	–	76.0p	August 2005	January 2006
	19 July 2001	2,454	–	–	–	2,454	154.0p	October 2006	March 2007
	8 May 2002	1,151	–	–	–	1,151	184.0p	July 2007	December 2007
	7 May 2003	839	–	–	–	839	133.0p	July 2008	December 2008
	5 May 2004	716	–	–	–	716	210.0p	July 2009	December 2009
	4 May 2005	–	687	–	–	687	250.0p	July 2010	December 2010

Notes:

(i) All options are granted for nil consideration on grant and are in respect of 50p ordinary shares of Balfour Beatty plc.

(ii) All outstanding executive share options held by Directors have satisfied performance conditions that were required to be met before exercise and are, therefore, exercisable at the discretion of the option holder.

(iii) The closing market price of the Company's ordinary shares on 31 December 2005 was 356p. During the year the highest and lowest closing market prices were 362p and 290p.

(iv) Executive share options granted to Jim Cohen and Alistair Wivell in April 1995, exercisable at 311.9p, lapsed unexercised in April 2005.

(v) Details of options exercised and the value realisable on exercise are shown in the table below.

Name of Director	Date granted	Date exercised	Number of options exercised	Exercise price	Closing market price on date exercised	Value realisable on exercise*
J L Cohen						
Savings-Related Options	8 May 2002	8 September 2005	743	184.0p	330.0p	£1,085
A L P Rabin						
Savings-Related Options	24 May 2000	1 August 2005	3,286	76.0p	350.5p	£9,020
I P Tyler						
Savings-Related Options	8 May 2002	22 September 2005	640	184.0p	317.5p	£854
P J L Zinkin						
Savings-Related Options	24 May 2000	1 August 2005	2,842	76.0p	350.5p	£7,801

*The value realisable from shares acquired on exercise is the difference between the closing market price on the date exercised and the exercise price of the options, although the shares may have been retained, in which case they are included in the table on page 47, headed "Directors' interests".

Directors' pensions

Executive Directors participate in the Balfour Beatty Pension Fund. The scheme provides for a pension at a normal retirement age of 62 and each Director pays an annual contribution equal to 5% of pensionable salary. The pension for a Director who can complete 20 or more years' pensionable service at normal retirement age is targeted at two-thirds of final pensionable salary, subject to Inland Revenue limits. Directors have the option to pay additional voluntary contributions, but neither the contributions nor the resulting benefits are included in the tables below. The salaries of Jim Cohen, Anthony Rabin and Ian Tyler were subject to the Inland Revenue earnings cap for pension purposes and details of the Company's contributions to additional arrangements for them are noted underneath the second table below.

The table below sets out the accrued deferred pension which would be paid annually from the scheme at normal retirement age based on each executive Director's service to 31 December 2005 as well as the additional pension benefit secured in respect of service during the year.

Name of Director	Age at 31 December 2005 years	Pensionable service at 31 December 2005 years	Accrued deferred pension at 31 December 2004 £ pa	Increase in accrued deferred pension during the year: Inflation £ pa	Increase in accrued deferred pension during the year: Increase in excess of inflation £ pa	Accrued deferred pension at 31 December 2005 £ pa	Transfer value corresponding to increase in excess of inflation at 31 December 2005 less Director's contributions (Note i) £
J L Cohen	**63**	**12**	36,961	1,146	4,912	**43,019**	**94,874**
A L P Rabin	**50**	**12**	7,701	239	36,129	**44,069**	**72,266**
I P Tyler	**45**	**9**	21,830	677	2,671	**25,178**	**18,104**
A J Wivell	**60**	**32**	177,616	5,506	10,304	**193,426**	**214,116**
P J L Zinkin	**52**	**24**	139,849	4,335	8,315	**152,499**	**91,009**

Notes:

(i) The transfer value of the increase in accrued deferred pension is the present value of the increase in excess of inflation in the deferred pension and associated benefits during the period, less the Director's contributions, calculated using the transfer basis in force at 31 December 2005 and on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11.

(ii) Jim Cohen attained normal retirement age under the Balfour Beatty Pension Fund in February 2004 but has continued in service. As at 31 December 2005 his pension had not commenced payment and it therefore continues to be determined in line with the rules of the fund for members past normal retirement age.

(iii) During the year, Anthony Rabin transferred benefits into the Balfour Beatty Pension Fund from previous pension arrangements. A total amount of £331,324 was received in exchange for which he was awarded additional pensionable service of 9 years 81 days. A significant amount of the increase in deferred pension over the year is therefore due to this additional pensionable service. The transfer value quoted in the final column is the increase in accrued deferred pension in excess of inflation, less Anthony Rabin's contributions over the year, less the transfer values actually received by the Balfour Beatty Pension Fund.

The table below sets out the transfer value at 31 December 2005 of each executive Director's accrued deferred pension at that date as well as the movement in that transfer value over the period. The transfer values represent the cash equivalent values that would have been payable from the scheme had the Directors left service on the dates shown, and reflect the age of the Director, his period of membership of the scheme and his pensionable salary.

Name of Director	Age at 31 December 2005 years	Pensionable service at 31 December 2005 years	Transfer value at 31 December 2004 (Note i) £	Contributions made by Director during the year £	Increase in transfer value during the year less Director's contributions (Note ii) £	Transfer value at 31 December 2005 (Note i) £
J L Cohen	**63**	**12**	666,636	5,292	175,761	**847,689**
A L P Rabin	**50**	**12**	78,832	336,616	77,642	**493,090**
I P Tyler	**45**	**9**	173,491	5,292	39,255	**218,038**
A J Wivell	**60**	**32**	3,374,793	16,000	366,040	**3,756,833**
P J L Zinkin	**52**	**24**	1,617,965	17,248	311,952	**1,947,165**

Notes:

(i) The transfer value is the present value of the accrued deferred pension and associated benefits at the relevant date, calculated using the transfer basis then in force and on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11.

(ii) The figure is the difference between the transfer value of the accrued benefits at the start and end of the period, less the Director's contributions during the period.

(iii) During the year, Anthony Rabin transferred benefits into the Balfour Beatty Pension Fund from previous pension arrangements. A total amount of £331,324 was received in exchange for which he was awarded additional pensionable service of 9 years 81 days. In the above table, contributions made by the Director during the year includes the amount of the transfer values received by the Balfour Beatty Pension Fund.

(iv) Alistair Wivell retired on 31 December 2005 and took immediate pension benefits. The transfer value at 31 December 2005 is the actuarial value of these benefits.

The salaries of Jim Cohen, Anthony Rabin and Ian Tyler were subject to the Inland Revenue earnings cap for pension purposes, and the Company has contributed to a Funded Unapproved Retirement Benefit Scheme ("FURBS") for each of them. In 2005, the Company's contribution to Jim Cohen's plan was £34,004, to Anthony Rabin's £54,418 and to Ian Tyler's £51,133. Benefits under these FURBS are additional to those set out in the tables above.

No past Director of the Company has received or become entitled to receive retirement benefits in excess of his entitlements on the date on which those benefits first became payable, or 31 March 1997 if later.

Remuneration report

Signed by order of the Board

C R O'N Pearson
Secretary
7 March 2006

Independent auditors' report to the members of Balfour Beatty plc

We have audited the Group and Company financial statements (the "financial statements") of Balfour Beatty plc for the year ended 31 December 2005 which comprise the consolidated and Company income statements, the consolidated and Company balance sheets, the consolidated and Company cash flow statements, the consolidated statement of recognised income and expense and the related notes 1 to 37. These 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.

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' responsibilities for preparing the annual report, the Directors' remuneration report and the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted for use in the European Union are set out in the statement of Directors' responsibilities.

Our responsibility is to audit the financial statements and the part of the Directors' remuneration report described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view in accordance with the relevant framework and whether the financial statements and the part of the Directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We report to you if, in our opinion, the Directors' report is not consistent with the financial statements. We also report to you 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 transactions with the Company and other members of the Group is not disclosed.

We also report to you if, in our opinion, the Company has not complied with any of the four Directors' remuneration disclosure requirements specified for our review by the Listing Rules of the Financial Services Authority. These comprise the amount of each element in the remuneration package and information on share options, details of long-term incentive schemes, and money purchase and defined benefit schemes. We give a statement, to the extent possible, of details of any non-compliance.

We review whether the corporate governance statement reflects the Company's compliance with the nine 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 the Directors' report and the other information contained in the annual report including the unaudited part of the Directors' remuneration report and we consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with 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 financial statements and the part of the Directors' remuneration report described as having been audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the 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 financial statements and the part of the Directors' remuneration report described as having been 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 financial statements and the part of the Directors' remuneration report described as having been audited.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted for use in the European Union, of the state of the Group's and the Company's affairs as at 31 December 2005 and of the Group's profit and the Company's profit for the year then ended;
- the financial statements and the part of the Directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

Separate opinion in relation to IFRS

As explained in Note 1, the Group and the Company in addition to complying with their legal obligation to comply with IFRSs adopted for use in the European Union, have also complied with the IFRSs as issued by the International Accounting Standards Board and therefore have applied the full version of IAS 39 (Financial Instruments: Recognition and Measurement). Accordingly, in our opinion the financial statements give a true and fair view, in accordance with IFRSs, of the state of the Group's and the Company's affairs as at 31 December 2005 and the Group's profit and the Company's profit for the year then ended.

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
London
7 March 2006

Group income statement
For the year ended 31 December 2005

	Notes	2005 Before exceptional items £m	2005 Exceptional items (Note 8) £m	2005 Total £m	2004 Before exceptional items £m	2004 Exceptional items (Note 8) £m	2004 Total £m
Continuing operations							
Revenue including share of joint ventures and associates		**4,938**	**–**	**4,938**	4,239	–	4,239
Share of revenue of joint ventures and associates	15	**(1,101)**	**–**	**(1,101)**	(749)	–	(749)
Group revenue	2.1	**3,837**	**–**	**3,837**	3,490	–	3,490
Cost of sales		**(3,528)**	**(14)**	**(3,542)**	(3,199)	7	(3,192)
Gross profit		**309**	**(14)**	**295**	291	7	298
Net operating expenses		**(237)**	**–**	**(237)**	(233)	(9)	(242)
Group operating profit		**72**	**(14)**	**58**	58	(2)	56
Share of results of joint ventures and associates	15	**43**	**30**	**73**	36	–	36
Profit from operations	4	**115**	**16**	**131**	94	(2)	92
Investment income	6	**56**	**–**	**56**	56	–	56
Finance costs	7	**(37)**	**(9)**	**(46)**	(28)	–	(28)
Profit before taxation		**134**	**7**	**141**	122	(2)	120
Taxation	9	**(32)**	**(3)**	**(35)**	(23)	(5)	(28)
Profit for the year from continuing operations		**102**	**4**	**106**	99	(7)	92
Profit for the year from discontinued operations	10	**–**	**–**	**–**	8	160	168
Profit for the year		**102**	**4**	**106**	107	153	260
Preference dividends	7	**–**	**–**	**–**	(13)	–	(13)
Premium paid on buy-back of preference shares	27.2	**–**	**–**	**–**	(6)	–	(6)
Profit for the year attributable to equity shareholders		**102**	**4**	**106**	88	153	241

	Notes	2005 Pence	2004 Pence
Basic earnings per ordinary share			
– continuing operations	11	**24.9**	17.3
– discontinued operations	11	**–**	40.1
		24.9	57.4
Diluted earnings per ordinary share			
– continuing operations	11	**24.7**	17.2
– discontinued operations	11	**–**	39.7
		24.7	56.9
Dividends per ordinary share proposed for the year	12	**8.1**	6.6

Group statement of recognised income and expense
For the year ended 31 December 2005

	2005 £m	2004 £m
Actuarial losses on retirement benefit obligations	**(14)**	(17)
PFI/PPP cash flow hedges – net fair value gains/(losses)	**(17)**	–
– reclassified and reported in net profit	**1**	–
PFI/PPP financial assets – fair value revaluation	**10**	–
– reclassified and reported in net profit	**(4)**	–
Changes in fair value of net investment hedges	**(6)**	7
Currency translation differences	**8**	(6)
Tax on items taken directly to equity	**9**	3
Net expense recognised directly in equity	**(13)**	(13)
Profit for the year from continuing operations	**106**	92
Profit for the year from discontinued operations	**–**	168
Total recognised income for the year	**93**	247
Attributable to:		
Equity	**93**	234
Preference shareholders (2004 only)	**–**	13
	93	247

Company income statement
For the year ended 31 December 2005

	Notes	2005 Before exceptional items £m	2005 Exceptional items (Note 8) £m	2005 Total £m	2004 Before exceptional items £m	2004 Exceptional items (Note 8) £m	2004 Total £m
Revenue	2.2	**65**	**–**	**65**	53	–	53
Net operating expenses		**(11)**	**7**	**(4)**	(10)	–	(10)
Profit from operations		**54**	**7**	**61**	43	–	43
Investment income	6	**21**	**–**	**21**	28	–	28
Finance costs	7	**(41)**	**(9)**	**(50)**	(25)	–	(25)
Profit before taxation		**34**	**(2)**	**32**	46	–	46
Taxation	9	**9**	**2**	**11**	16	–	16
Profit for the year		**43**	**–**	**43**	62	–	62
Preference dividends	7	**–**	**–**	**–**	(13)	–	(13)
Premium paid on buy-back of preference shares	27.2	**–**	**–**	**–**	(6)	–	(6)
Profit for the year attributable to equity shareholders		**43**	**–**	**43**	43	–	43

Balance sheets
At 31 December 2005

	Notes	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Non-current assets					
Goodwill	13	**284**	279	**–**	–
Property, plant and equipment	14	**167**	149	**–**	1
Investments in joint ventures and associates	15	**375**	189	**–**	–
Investments	16	**38**	42	**870**	872
PFI/PPP financial assets	17	**14**	282	**–**	–
Deferred tax assets	24	**83**	87	**1**	10
Derivative financial instruments	20	**2**	–	**–**	–
Trade and other receivables	21	**35**	41	**35**	33
		998	1,069	**906**	916
Current assets					
Inventories	18	**61**	50	**–**	1
Due from customers for contract work	19	**217**	218	**–**	–
Derivative financial instruments	20	**–**	–	**4**	–
Trade and other receivables	21	**619**	563	**395**	369
Cash and cash equivalents – PFI/PPP subsidiaries	23	**–**	30	**–**	–
– other	23	**345**	388	**142**	259
		1,242	1,249	**541**	629
Total assets		**2,240**	2,318	**1,447**	1,545
Current liabilities					
Trade and other payables	22	**(1,038)**	(946)	**(693)**	(739)
Due to customers for contract work	19	**(274)**	(264)	**–**	–
Derivative financial instruments	20	**(4)**	–	**(4)**	–
Current tax liabilities		**(30)**	(38)	**(5)**	(8)
Borrowings – PFI/PPP non-recourse term loans	23	**–**	(13)	**–**	–
– other	23	**(30)**	(15)	**(12)**	(4)
		(1,376)	(1,276)	**(714)**	(751)
Non-current liabilities					
Borrowings – PFI/PPP non-recourse term loans	23	**(14)**	(261)	**–**	–
– other	23	**–**	(62)	**–**	(62)
Liability component of preference shares	27.2	**(98)**	–	**(98)**	–
Derivative financial instruments	20	**(2)**	–	**–**	–
Trade and other payables	22	**(66)**	(58)	**(25)**	(25)
Deferred tax liabilities	24	**(3)**	(2)	**–**	–
Retirement benefit obligations	25	**(280)**	(254)	**(8)**	(6)
Provisions	26	**(109)**	(103)	**(9)**	(9)
		(572)	(740)	**(140)**	(102)
Total liabilities		**(1,948)**	(2,016)	**(854)**	(853)
Net assets		**292**	302	**593**	692
Capital and reserves					
Called-up share capital	27	**214**	213	**214**	213
Share premium account	28	**26**	150	**26**	150
Equity component of preference shares	28	**18**	–	**18**	–
Special reserve	28	**175**	181	**175**	181
Share of joint ventures' and associates' reserves	28	**182**	72	**–**	–
Other reserves	28	**5**	9	**49**	50
Accumulated (losses)/profits	28	**(328)**	(323)	**111**	98
		292	302	**593**	692
Equity		**292**	166	**593**	556
Preference shareholders' interests (2004 only)		**–**	136	**–**	136
Equity/shareholders' funds		**292**	302	**593**	692

On behalf of the Board

Sir David John
Director

A L P Rabin
Director
7 March 2006

Cash flow statements

For the year ended 31 December 2005

	Notes	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Cash flows from operating activities					
Cash generated from operations	35.1	**167**	148	**(3)**	(16)
Income taxes (paid)/received		**(28)**	(41)	**18**	13
Net cash from operating activities		**139**	107	**15**	(3)
Cash flows from investing activities					
Dividends received from joint ventures and associates		**12**	8	**6**	5
Dividends received from subsidiaries		**–**	–	**57**	48
Acquisition of businesses, net of cash and cash equivalents acquired		**(56)**	(17)	**–**	–
Purchase of property, plant and equipment		**(57)**	(51)	**–**	–
Investment in and loans made to joint ventures and associates		**(12)**	(11)	**(9)**	(1)
Investment in and loans (made to)/received from subsidiaries		**–**	–	**(81)**	211
Purchase of investments		**–**	–	**–**	(13)
Investment in financial assets		**(21)**	(65)	**–**	–
Disposal of businesses, net of cash and cash equivalents disposed		**(15)**	217	**–**	–
Disposal of property, plant and equipment		**8**	13	**–**	1
Disposal of investments		**6**	51	**10**	44
Net cash (used in)/from investing activities		**(135)**	145	**(17)**	295
Cash flows from financing activities					
Proceeds from issue of ordinary shares		**6**	4	**6**	4
Purchase of ordinary shares		**(3)**	(2)	**(3)**	(2)
Proceeds from new loans		**6**	6	**–**	–
Repayment of loans		**(80)**	(12)	**(66)**	–
Finance lease principal repayments		**(2)**	(2)	**–**	–
Buy-back of preference shares		**(11)**	(20)	**(11)**	(20)
Ordinary dividends paid		**(28)**	(25)	**(28)**	(25)
Interest received		**64**	47	**26**	25
Interest paid		**(27)**	(24)	**(29)**	(24)
Premium paid on repayment of US Dollar term loan		**(9)**	–	**(9)**	–
Preference dividends paid		**(13)**	(15)	**(13)**	(15)
Net cash used in financing activities		**(97)**	(43)	**(127)**	(57)
Net (decrease)/increase in cash and cash equivalents		**(93)**	209	**(129)**	235
Effects of exchange rate changes		**3**	(1)	**4**	(4)
Cash and cash equivalents at 1 January		**406**	198	**255**	24
Cash and cash equivalents at 31 December	35.2	**316**	406	**130**	255

Notes to the accounts

1 Principal accounting policies

1.1 Basis of accounting

The annual financial statements have been prepared for the first time in accordance with International Financial Reporting Standards (IFRS) adopted for use in the European Union and therefore comply with Article 4 of the EU IAS Regulation and with those parts of the Companies Act 1985 that are applicable to companies reporting under IFRS. The Group has applied all accounting standards and interpretations issued by the International Accounting Standards Board and International Financial Reporting Interpretations Committee relevant to its operations and effective for accounting periods beginning on 1 January 2005. Accounting standards and interpretations in issue at the date of authorisation of the financial statements but not yet effective are not expected to have a material impact on the financial statements of the Group. The disclosures required by IFRS 1 "First-time Adoption of IFRS" concerning the transition from accounting principles generally accepted in the United Kingdom (UK GAAP) to IFRS are given in Note 37.

Balfour Beatty adopted IFRS with a transition date of 1 January 2004. Comparative figures for the year ended 31 December 2004 and the Group's balance sheet as at 31 December 2004 that were previously reported in accordance with UK GAAP, have been restated to comply with IFRS with the exception of IAS 32 "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement" which have been applied prospectively from 1 January 2005, as permitted by IFRS 1.

These standards have a significant impact on the Group and particularly affect the accounting for the Company's convertible redeemable preference shares, the hedging activities of the Group's PFI/PPP concessions and their income which, in accordance with the International Financial Reporting Interpretations Committee's draft interpretations on service concessions, D12 to D14, is determined under IAS 39 to be an available-for-sale financial asset. The adoption of IAS 32 and IAS 39 has reduced the Group's net assets as follows:

	£m
Net assets at 31 December 2004	302
Preference shares – liability element and deferred tax	(113)
Group derivatives	(3)
PFI/PPP concessions – derivatives	(41)
PFI/PPP concessions – financial assets	75
Goodwill adjustment arising from concession share purchase	7
Net assets at 1 January 2005	227

The financial statements have been prepared under the historical cost convention, except as described under Note 1.28. The principal accounting policies adopted are set out below.

Balfour Beatty has applied IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations" to assets and related liabilities that met the criteria to be classified as held for sale, and operations that met the criteria to be classified as discontinued on or after 1 January 2004.

IFRS 1 "First-time Adoption of IFRS" allows certain exemptions from the retrospective application of IFRS prior to 1 January 2004. Balfour Beatty has adopted the following exemptions:

a) Business combinations

The Group has chosen not to restate business combinations that occurred prior to 1 January 2004 to comply with IFRS 3 "Business Combinations". As a result the carrying value of goodwill recorded under UK GAAP as at 1 January 2004 has been fixed at transition date. Also goodwill previously written off to reserves under UK GAAP will be deemed to be zero and will not be taken into account in determining any gain or loss on the disposal of the acquired entity.

b) Property, plant and equipment

Property, plant and equipment that were revalued under UK GAAP are deemed to be carried at cost for subsequent accounting under IFRS.

c) Employee benefits

All cumulative actuarial gains and losses on defined benefit pension schemes have been recognised in equity at the transition date, 1 January 2004.

d) Share-based payments

IFRS 2 "Share-based Payment" has been applied retrospectively to equity-settled awards that had not vested as at 1 January 2005 and were granted on or after 7 November 2002.

e) Cumulative foreign currency translation

All cumulative foreign currency translation differences arising on the re-translation into Sterling of the Group's net investments in foreign operations have been deemed to be zero at 1 January 2004 for all overseas subsidiaries, joint ventures and associates.

f) Financial instruments

The Group has elected to apply IAS 32 and IAS 39 prospectively from 1 January 2005.

In accordance with IFRS the Group has not revised estimates required under IFRS that were also required under UK GAAP as at 31 December 2003 and 2004, and, in addition, where estimates were not required under UK GAAP, they have been based on information known at that time, and not on subsequent events.

1.2 Basis of consolidation

The Group accounts include the accounts of the Company and its subsidiaries, together with the Group's share of the results of associates and joint ventures drawn up to 31 December each year.

a) Subsidiaries

Subsidiaries are entities over which the Group has control, being the power to govern the financial and operating policies of the investee entity so as to obtain benefits from its activities. The results of subsidiaries acquired or sold in the year are consolidated from the effective date of acquisition or to the effective date of disposal, as appropriate.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. On acquisition, the assets, liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the fair value of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired (discount on acquisition) is credited to the income statement in the period of acquisition. The interest of minority shareholders is stated at the minority's proportion of the fair value of the assets and liabilities recognised.

Accounting policies of subsidiaries are adjusted where necessary to ensure consistency with those used by the Group. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

b) Joint ventures and associates

Joint ventures are those entities over which the Group exercises joint control through a contractual arrangement. Associates are entities over which the Group is in a position to exercise significant influence but not control or joint control, through participation in the financial and operating policy decisions of the investee. The results, assets and liabilities of joint ventures and associates are incorporated in the financial statements using the equity method of accounting except when classified as held for sale (see below). Investments in joint ventures and associates are initially carried in the balance sheet at cost (including goodwill arising on acquisition) and adjusted by post-acquisition changes in the Group's share of the net assets of the joint venture or associate, less any impairment in the value of individual investments. Losses of joint ventures or associates in excess of the Group's interest in those joint ventures and associates are not recognised.

Unrealised gains and losses on transactions with joint ventures and associates are eliminated to the extent of the Group's interest in the relevant joint venture or associate.

Any excess of the cost of acquisition over the Group's share of the fair values of the identifiable net assets of the associate or joint venture entity at the date of acquisition is recognised as goodwill. Any deficiency of the cost of acquisition below the Group's share of the fair values of the identifiable net assets of the joint venture or associate at the date of acquisition (discount on acquisition) is credited to the income statement in the period of acquisition.

c) Jointly controlled operations

The Group's share of the results and net assets of contracts carried out in joint venture are included under each relevant heading in the income statement and balance sheet.

1 Principal accounting policies continued

1.3 Foreign currencies
Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the rates of exchange prevailing at the balance sheet date.

In order to hedge its exposure to certain foreign exchange risks, the Group enters into forward contracts and swaps (see below for details of the Group's accounting policies in respect of such derivative financial instruments).

Results of overseas subsidiaries, associates and joint venture entities are translated at average rates of exchange for the year unless exchange rates fluctuate significantly and their assets and liabilities are translated at the rates of exchange prevailing at the balance sheet date.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the rates of exchange prevailing at the balance sheet date. Exchange differences arising together with exchange differences on borrowings and other currency instruments designated as hedges of such investments are classified as equity and transferred to the Group's foreign currency translation reserve. Such exchange differences are recognised in the income statement in the period in which the relevant entity is disposed of.

1.4 Revenue recognition
Revenue is measured at the fair value of the consideration received or receivable for goods and services provided, net of trade discounts, value added and similar sales-based taxes, after eliminating sales within the Group. Revenue is recognised as follows:
- revenue from contracting and service activities represents the value of work carried out during the year, including amounts not invoiced;
- revenue from manufacturing activities is recognised when goods are delivered and title has passed;
- interest income is accrued on a time basis, by reference to the principal outstanding and the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. Dividend income is recognised when the shareholder's right to receive payment is established.

1.5 Segmental reporting
Segmental information is based on two segment formats, of which the primary format is for business areas in accordance with the Group's management and internal reporting structure and the secondary format is for geographical areas. Further information on the business activities of each segment are set out in the Operating Review on pages 22 to 31. Segment results represent the contribution directly attributable for the different segments to corporate overheads and the profit of the Group. Transactions between segments are conducted at arm's length market prices. Segment assets and liabilities comprise those assets and liabilities directly attributable to the segments, including the subordinated loans to PFI/PPP investments. Corporate assets and liabilities include cash balances, bank borrowings, tax balances and dividends payable.

1.6 Construction and service contracts
When the outcome of individual contracts can be foreseen with reasonable certainty and can be estimated reliably, margin is recognised by reference to the stage of completion, based on the lower of the percentage margin earned to date and that prudently forecast at completion. Full provision is made for all known or expected losses on individual contracts immediately once such losses are foreseen. Variations in contract work, claims and incentive payments are included to the extent that it is probable they will result in revenue. Gross profit for the year includes the benefit of claims settled on contracts completed in prior years.

Pre-contract costs are expensed as incurred until it is virtually certain that a contract will be awarded, from which time further pre-contract costs are recognised as an asset and charged as an expense over the period of the contract. Amounts recovered in respect of costs that have been written off are deferred and amortised over the life of the contract.

1.7 Profit from operations
Profit from operations is stated after the share of the post-tax results of equity accounted associates and joint venture entities, but before investment income and finance costs.

1.8 Finance costs
Finance costs of debt, including premiums payable on settlement and direct issue costs, are charged to the income statement on an accruals basis over the term of the instrument, using the effective interest method.

1.9 Research and development
Research expenditure is written off in the period in which it is incurred.

Internally-generated intangible assets arising from the Group's development would be recognised only if all the following conditions are met:
- an asset is created that can be identified;
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

1.10 Exceptional items
Material and non-recurring items of income and expense are disclosed in the income statement as "Exceptional items". Examples of items which may give rise to disclosure as "Exceptional items" include gains or losses on the disposal of businesses, investments and property, plant and equipment, costs of restructuring and reorganisation of businesses, litigation settlements, asset impairments and pension fund settlements and curtailments.

1.11 Taxation
The tax charge is composed of current tax and deferred tax, calculated using tax rates that have been enacted or substantively enacted by the balance sheet date. Current tax and deferred tax are charged or credited to the income statement, except when they relate to items charged or credited directly to equity, in which case the relevant tax is also dealt with in equity.

Current tax is based on the profit for the year.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax on such assets and liabilities is not recognised if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. The carrying amount of deferred tax assets is reviewed at each balance sheet date.

Deferred tax is provided on temporary differences arising on investments in subsidiaries, associates and joint venture entities, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

1.12 Property, plant and equipment
Property, plant and equipment are stated at cost less accumulated depreciation and any recognised impairment loss. Cost includes expenditure associated with bringing the asset to its operating location and condition.

Certain land and buildings were revalued under UK GAAP. On transition to IFRS, the Group has elected to use the revalued amount as deemed cost.

Assets held under finance leases are treated as property, plant and equipment and depreciation is provided accordingly.

Except for land and assets in the course of construction, the cost of property, plant and equipment is depreciated over their expected useful lives, on a straight-line basis at rates of 2.5% for buildings and 4% to 33% for plant and equipment, or the life of the lease.

1 Principal accounting policies continued

1.13 Leasing
Leases which transfer substantially all of the risks and rewards of ownership to the lessee are classified as finance leases. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability.

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

1.14 Goodwill
Goodwill represents the excess of the fair value of consideration over the fair value of the identifiable assets and liabilities acquired, arising on the acquisition of subsidiaries and other business entities, joint ventures and associates. Goodwill on acquisitions of subsidiaries and other business entities is included in non-current assets. Goodwill on acquisitions of joint ventures and associates is included in investments in joint ventures and associates.

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

Goodwill arising on acquisitions before the date of transition to IFRS has been retained at the previous UK GAAP amounts subject to being tested for impairment at that date. Goodwill written off or negative goodwill credited to reserves under UK GAAP prior to 1998 has not been reinstated and is not included in determining any subsequent profit or loss on disposal.

1.15 Impairment of assets
Goodwill arising on acquisitions and other assets that have an indefinite useful life and are not subject to amortisation are reviewed at least annually for impairment. Other intangible assets and property, plant and equipment are reviewed for impairment whenever there is any indication that the carrying amount of the asset may not be recoverable. If the recoverable amount of an asset is less than its carrying amount, an impairment loss is recognised. Recoverable amount is the higher of fair value less costs to sell and value in use. Value in use is assessed by discounting the estimated future cash flows that the asset is expected to generate. For this purpose assets, including goodwill, are grouped into cash generating units representing the lowest levels for which there are separately identifiable cash flows. Impairment losses for goodwill are not reversed in subsequent periods. Reversals of other impairment losses are recognised in income when they arise.

1.16 Non-current assets held for sale
Non-current assets and groups of assets to be disposed of are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. Held for sale assets are measured at the lower of carrying amount and fair value less costs to sell.

1.17 Inventories
Inventories are valued at the lower of cost and net realisable value. Cost, where appropriate, includes a proportion of manufacturing overheads incurred in bringing inventories to their present location and condition and is determined using the first-in first-out method. Net realisable value represents the estimated selling price less all estimated costs of completion and cost to be incurred in marketing, selling and distribution.

1.18 Financial instruments
Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

1.19 Trade receivables
Trade receivables are initially recorded at fair value and subsequently measured at amortised cost as reduced by appropriate allowances for estimated irrecoverable amounts.

1.20 Investments
Investments are recognised and derecognised on a trade date where a purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at cost, including transaction costs.

From 1 January 2005, investments are classified as either available-for-sale or held to maturity. Available-for-sale investments are measured at subsequent reporting dates at fair value. Gains and losses arising from changes in the fair value of available-for-sale investments are recognised directly in equity, until the investment is disposed of or is determined to be impaired, at which time the cumulative gain or loss is included in the net profit or loss for the period. Held to maturity investments are measured at subsequent reporting dates at amortised cost.

1.21 Financial liability and equity
Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

1.22 Bank borrowings
Interest-bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are charged to income on an accruals basis using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

1.23 Trade payables
Trade payables are not interest-bearing and are stated at their nominal value.

1.24 Equity instruments
Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

1.25 Provisions
Provisions for environmental restoration, legal claims, onerous leases and other onerous commitments are recognised at the best estimate of the expenditure required to settle the Group's liability. Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event; it is probable that an outflow of resources will be required to settle the obligation; and the amount of the obligation can be estimated reliably.

1.26 Retirement benefit costs
The Group, through trustees, operates pension schemes the majority of which are of the defined benefit type and are funded. Contributions are determined in accordance with independent actuarial advice.

For defined benefit retirement benefit schemes, the cost of providing benefits recognised in the income statement and the defined benefit obligation is determined at the balance sheet date using the projected unit credit method by independent actuaries. The liability recognised in the balance sheet comprises the present value of the defined benefit pension obligation, determined by discounting the estimated future cash flows using the rate of interest on a high quality corporate bond, less the fair value of the plan assets. Actuarial gains and losses are recognised in full outside the income statement in the period in which they occur in the statement of recognised income and expense.

Contributions to defined contribution pension schemes are charged to the income statement as they fall due.

1.27 Share-based payments
Employee services received in exchange for the grant of share options, performance share plan awards and deferred bonus plan awards since 7 November 2002 are charged in the income statement over the vesting period, based on the fair values of the options or awards at the date of grant and the numbers expected to become exercisable. The credits in respect of the amounts charged are included within separate reserves in equity until such time as the options or awards are exercised, when the proceeds received in respect of share options are credited to share capital and share premium or the shares held by the employee trust are transferred to employees in respect of performance share plan awards and deferred bonus plan awards.

1 Principal accounting policies continued

1.28 Financial instruments

a) Prospective adoption of IAS 32 and IAS 39
As permitted by IFRS 1, the Group has elected to apply IAS 32 "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement" prospectively from 1 January 2005. As a result, the relevant comparative information for the year ended 31 December 2004 does not reflect the impact of these standards and is accounted for in accordance with UK GAAP.

b) Cumulative convertible redeemable preference shares
From 1 January 2005 onwards, the Company's cumulative convertible redeemable preference shares are regarded as a compound instrument, consisting of a liability component and an equity component. The fair value of the liability component at the date of issue was estimated using the prevailing market interest rate for a similar non-convertible instrument. The difference between the proceeds of issue of the preference shares and the fair value assigned to the liability component, representing the embedded option to convert the liability into the Company's ordinary shares, is included in equity.

The interest expense on the liability component is calculated by applying the market interest rate for similar non-convertible debt prevailing at the date of issue to the liability component of the instrument. The difference between this amount and the dividend paid is added to the carrying amount of the liability component and is included in finance charges, together with the dividend payable, in the income statement.

c) Derivative financial instruments and hedge accounting
The Group uses derivative financial instruments to manage interest rate risk and to hedge exposures to fluctuations in foreign currencies. The Group does not use derivative financial instruments for speculative purposes. A description of the Group's objectives, policies and strategies with regard to derivatives and other financial instruments is set out in the Financial Review on pages 34 to 37.

From 1 January 2005 onwards:

Derivatives are initially recognised on the balance sheet at fair value on the date the derivative transaction is entered into and are subsequently remeasured at their fair values.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recognised in the income statement together with any changes in the fair value of the hedged item that are attributable to the hedged risk.

Changes in the fair value of the effective portion of derivatives that are designated and qualify as cash flow hedges are recognised in equity. Changes in the fair value of the ineffective portion of cash flow hedges are recognised in the income statement. Amounts accumulated in equity are transferred to the income statement when the underlying transaction occurs or, if the transaction results in a non-financial asset or liability, are included in the initial cost of that asset or liability.

Changes in the fair value of the effective portion of derivatives that are designated and qualify as hedges of net investments in foreign operations are recognised in equity. Changes in the fair value of the ineffective portion of net investment hedges are recognised in the income statement. Amounts accumulated in equity are transferred to the income statement when the foreign operation is disposed of.

Changes in the fair value of derivative financial instruments that do not qualify for hedge accounting are recognised in the income statement as they arise.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. At that time, any cumulative gain or loss on the hedging instrument recognised in equity is retained in equity until the forecasted transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to net profit or loss for the period.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives and recorded on the balance sheet at fair value when their risks and characteristics are not closely related to those of the host contract. Changes in the fair value of those embedded derivatives recognised on the balance sheet are recognised in the income statement as they arise.

d) PFI/PPP concessions
From 1 January 2005 onwards, assets constructed by PFI/PPP concession companies are classified as "available-for-sale financial assets".
Income is recognised by allocating a proportion of total cash projected to be received over the life of the project to service costs, by means of a deemed constant rate of return on those costs. The residual element of projected cash is allocated to the financial asset, using the effective interest method, giving rise to interest income which is recognised in the income statement.

The fair value of the financial asset is measured at each balance sheet date by computing the discounted future value of the cash flows allocated to the financial asset. The movement in the fair value of the financial asset since the previous balance sheet date is taken to equity.

1.29 Key sources of estimation uncertainty

The preparation of consolidated financial statements under IFRS requires management to make estimates and assumptions that effect amounts recognised for assets and liabilities at the balance sheet date and the amounts of revenue and the expenses incurred during the reporting period. Actual outcomes may therefore differ from these estimates and assumptions. The estimates and assumptions that have the most significant impact on the carrying value of assets and liabilities of the Group within the next financial year are discussed below.

a) Revenue and margin recognition
The Group's revenue recognition and margin recognition policies, which are set out in 1.4 and 1.6 above, are central to the way the Group values the work it has carried out in each financial year. These policies require forecasts to be made of the outcomes of long-term construction and service contracts, which require assessments and judgements to be made on recovery of pre-contract costs, changes in work scopes, contract programmes and maintenance liabilities.

b) Impairment of goodwill
Determining whether goodwill is impaired requires an estimation of the value in use of the cash generating units to which the goodwill has been allocated. The value in use calculation requires an estimate to be made of the timing and amount of future cash flows expected to arise from the cash generating unit and a suitable discount rate in order to calculate the present value. The discount rates used are based on the Group's weighted average cost of capital adjusted to reflect the specific economic environment of the relevant cash-generating unit. The carrying value of goodwill at 31 December 2005 was £284m, after an impairment loss of £4m was recognised in 2005. Details of the impairment loss calculation are provided in Note 13.

c) Available-for-sale financial assets
Assets constructed by the Group's PFI/PPP subsidiary, joint venture and associate companies are classified as "available-for-sale financial assets" and at 31 December 2005 had a value of £1,269m. The fair value of these financial assets is measured at each balance sheet date by discounting the future value of the cash flows allocated to the financial asset. A range of discount rates, varying from 6% to 11%, are used which reflect the prevailing risk-free interest rates and the different risk profiles of the various concessions. A £10m gain was taken to equity in 2005 as a result of movements in the fair value of these financial assets.

d) PFI/PPP derivative financial instruments
The Group's PFI/PPP subsidiary, joint venture and associate companies use derivative financial instruments (principally swaps) to manage the interest rate and inflation rate risks to which the concessions are exposed by their long-term contractual agreements. These derivatives are initially recognised as assets and liabilities at their fair value and subsequently remeasured at each balance sheet date at their fair value. The fair value of derivatives constantly changes in response to prevailing market conditions. At 31 December 2005, a cumulative fair value loss of £88m had arisen on these financial instruments and a loss of £17m was taken to equity in 2005.

e) Retirement benefit obligations
Details of the Group's defined benefit pension schemes are set out in Note 25 and have been valued in accordance with IAS 19 "Employee Benefits". At 31 December 2005, the defined benefit obligation recognised on the Group's balance sheet was £280m (2004: £254m). The benefit obligation is calculated using a number of assumptions including future salary increases, increases in pension benefits, mortality rates and inflation and the future investment returns from scheme assets. The present value of the benefit obligation is calculated by discounting the benefit obligation using market rates on relevant AA corporate bonds at the balance sheet date.

1 Principal accounting policies continued

e) Retirement benefit obligations continued

The schemes' assets are valued at market rates at the balance sheet date. Effects of changes in the actuarial assumptions underlying the benefit obligation, discount rates and the differences between expected and actual returns on the schemes' assets are classified as actuarial gains and losses. During 2005 the Group recognised a net actuarial loss of £14m in equity (2004: £17m), including its share of the actuarial gains and losses arising in joint ventures and associates.

f) Taxation

The Group is subject to tax in a number of jurisdictions and judgement is required in determining the worldwide provision for income taxes.

The Group provides for future liabilities in respect of uncertain tax positions where additional tax may become payable in future periods, and such provisions are based upon management's assessment of exposures.

As set out in 1.11 above, deferred tax is accounted for on temporary differences using the liability method, with deferred tax liabilities generally being provided for in full and deferred tax assets being recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised. Note 24.2 details the unused tax losses for which deferred tax assets have not been recognised and the undistributed reserves of subsidiaries for which deferred tax liabilities have not been provided, together with the judgements which the Group has made at 31 December 2005 in respect of these matters. These judgements may change in the future and they will be reviewed at each balance sheet date.

2 Revenue

	Group 2005 £m	Group 2004 £m	**Company 2005 £m**	Company 2004 £m
Revenue from contracting activities – construction	**3,247**	3,004	**–**	–
– services	**506**	414	**–**	–
Revenue from manufacturing activities	**82**	72	**–**	–
Proceeds on sale of development land	**2**	–	**2**	–
Dividends from subsidiaries	**–**	–	**57**	48
Dividends from joint ventures and associates	**–**	–	**6**	5
	3,837	3,490	**65**	53

3 Segment analysis – continuing operations

3.1 Total Group

	Building, building management and services 2005 £m	**Civil and specialist engineering and services 2005 £m**	**Rail engineering and services 2005 £m**	**Investments and developments 2005 £m**	**Corporate costs, assets and liabilities 2005 £m**	**Total 2005 £m**
Performance by activity:						
Results						
Group revenue	**1,674**	**1,366**	**763**	**34**	**–**	**3,837**
Group operating profit	**32**	**39**	**32**	**(10)**	**(21)**	**72**
Share of results of joint ventures and associates	**3**	**10**	**–**	**30**	**–**	**43**
Profit from operations before exceptional items	**35**	**49**	**32**	**20**	**(21)**	**115**
Exceptional items	**(8)**	**–**	**(12)**	**36**	**–**	**16**
Profit from operations	**27**	**49**	**20**	**56**	**(21)**	**131**
Investment income						**56**
Finance costs						**(46)**
Profit before taxation						**141**
Assets and liabilities						
Goodwill	**66**	**85**	**133**	**–**	**–**	**284**
Investments in joint ventures and associates	**4**	**67**	**–**	**304**	**–**	**375**
Other assets	**388**	**376**	**318**	**54**	**445**	**1,581**
Total assets	**458**	**528**	**451**	**358**	**445**	**2,240**
Total liabilities	**(671)**	**(519)**	**(443)**	**(70)**	**(245)**	**(1,948)**
	(213)	**9**	**8**	**288**	**200**	**292**
Other information						
Capital expenditure	**3**	**27**	**27**	**–**	**–**	**57**
Depreciation	**4**	**18**	**17**	**–**	**2**	**41**
Impairment of goodwill	**–**	**–**	**4**	**–**	**–**	**4**

3 Segment analysis – continuing operations continued

3.1 Total Group continued

	Europe 2005 £m	North America 2005 £m	Other 2005 £m	Total 2005 £m
Performance by geographic origin:				
Group revenue	**3,332**	**483**	**22**	**3,837**
Profit from operations before exceptional items	**134**	**(20)**	**1**	**115**
Exceptional items	**28**	**(12)**	**–**	**16**
Profit from operations	**162**	**(32)**	**1**	**131**
Segment assets (net)	**(24)**	**24**	**52**	**52**
Liability component of preference shares				**(98)**
Net cash				**301**
Tax and dividends				**37**
Net assets				**292**
Capital expenditure	**45**	**11**	**1**	**57**

	Building, building management and services 2004 £m	Civil and specialist engineering and services 2004 £m	Rail engineering and services 2004 £m	Investments and developments 2004 £m	Corporate costs, assets and liabilities 2004 £m	Total 2004 £m
Performance by activity:						
Results						
Group revenue	1,468	1,144	800	78	–	3,490
Group operating profit	32	7	45	(9)	(17)	58
Share of results of joint ventures and associates	2	9	(1)	26	–	36
Profit from operations before exceptional items	34	16	44	17	(17)	94
Exceptional items	–	1	(3)	–	–	(2)
Profit from operations	34	17	41	17	(17)	92
Investment income						56
Finance costs						(28)
Profit before taxation						120
Assets and liabilities						
Goodwill	61	78	136	4	–	279
Investments in joint ventures and associates	11	52	1	125	–	189
Other assets	365	360	264	330	531	1,850
Total assets	437	490	401	459	531	2,318
Total liabilities	(633)	(488)	(383)	(76)	(436)	(2,016)
	(196)	2	18	383	95	302
Other information						
Capital expenditure	4	15	30	2	–	51
Depreciation	6	14	18	–	2	40
Impairment of goodwill	–	–	18	–	–	18

	Europe 2004 £m	North America 2004 £m	Other 2004 £m	Total 2004 £m
Performance by geographic origin:				
Group revenue	3,107	377	6	3,490
Profit from operations before exceptional items	137	(45)	2	94
Exceptional items	15	(18)	1	(2)
Profit from operations	152	(63)	3	92
Segment assets (net)	111	40	47	198
Net cash				67
Tax and dividends				37
Net assets				302
Capital expenditure	39	11	1	51

3 Segment analysis – continuing operations continued

3.2 Investments and developments

The Investments and developments segment includes the Group's PFI/PPP activities (Balfour Beatty Capital Projects) details of which are set out below.

	Group 2005 £m	Share of joint ventures and associates 2005 £m	Total 2005 £m	Group 2004 £m	Share of joint ventures and associates 2004 £m	Total 2004 £m
Revenue						
PFI/PPP						
– joint ventures and associates (Note 15)	–	368	368	–	283	283
– subsidiaries (Note 3.3)	32	–	32	78	–	78
Balfour Beatty Capital Projects	32	368	400	78	283	361
Barking Power Ltd (Note 15)	–	63	63	–	46	46
Property development and other	2	–	2	–	–	–
	34	431	465	78	329	407

	Group 2005 £m	Share of joint ventures and associates 2005 £m	Total 2005 £m	Group 2004 £m	Share of joint ventures and associates 2004 £m	Total 2004 £m
Profit from operations – before exceptional items*						
PFI/PPP						
– joint ventures and associates (Note 15)	–	22	22	–	19	19
– subsidiaries (Note 3.3)	–	–	–	1	–	1
– bidding costs and overheads	(10)	–	(10)	(9)	–	(9)
Balfour Beatty Capital Projects	(10)	22	12	(8)	19	11
Barking Power Ltd (Note 15)	–	8	8	–	7	7
Property development and other	–	–	–	(1)	–	(1)
	(10)	30	20	(9)	26	17

*Profit from operations before exceptional items includes the Group's share of profit after taxation of joint ventures and associates (excluding exceptional items).

	Group 2005 £m	Share of joint ventures and associates 2005 £m	Total 2005 £m	Group 2004 £m	Share of joint ventures and associates 2004 £m	Total 2004 £m
Segment assets (net)						
PFI/PPP						
– joint ventures and associates (Note 15)	–	249	249	–	108	108
– subsidiaries (Note 3.3)	14	–	14	285	–	285
– bidding costs, overheads and goodwill	(4)	–	(4)	(6)	–	(6)
– loans from joint ventures and associates	(25)	–	(25)	(25)	–	(25)
Balfour Beatty Capital Projects	(15)	249	234	254	108	362
Barking Power Ltd (Note 15)	–	55	55	–	17	17
Property development and other	(1)	–	(1)	4	–	4
	(16)	304	288	258	125	383

3 Segment analysis – continuing operations continued

3.3 PFI/PPP subsidiaries

At 31 December 2005, the Group had a 100% interest in two PFI/PPP concessions through its shareholdings in Connect Roads Sunderland Holdings Ltd and Connect Roads South Tyneside Holdings Ltd. The Group also had a 100% interest in three PFI/PPP concessions through its shareholdings in Connect Roads Ltd and Connect M77/GSO Holdings Ltd until 20 December 2005, when the Group disposed of a 15% interest in those companies and they became joint ventures. The performance of the wholly-owned PFI/PPP concessions (since becoming subsidiaries as appropriate) and their balance sheets are summarised below.

	2005 £m	2004 £m
Income statement		
Group revenue	32	78
Profit from operations	–	1
Investment income	36	34
Finance costs	(19)	(18)
Profit before taxation	17	17
Taxation	(5)	(5)
Profit for the year	12	12
Cash flow		
Profit from operations	–	1
Decrease in working capital	–	6
Income taxes paid	(3)	(4)
Net cash (outflow)/inflow from operating activities	(3)	3
Net cash outflow from investing activities	(20)	(7)
Net cash inflow from financing activities	29	–
Net cash inflow/(outflow)	6	(4)
Net borrowings at beginning of year/date of acquisition	(244)	(240)
Net borrowings at date of disposal	224	–
Net borrowings at end of year	(14)	(244)
Balance sheet		
PFI/PPP financial assets (Note 17)	14	282
Current and deferred taxation	–	(9)
Other net current assets	–	3
Cash and cash equivalents	–	30
Non-recourse term loans	(14)	(274)
Net assets	–	32

4 Profit from operations

4.1 Profit from operations is stated after charging/(crediting):

	2005 £m	2004 £m
Research and development costs	4	8
Depreciation of property, plant and equipment	41	41
Impairment of goodwill	4	18
Impairment of trade receivables	1	3
(Profit)/loss on disposal of property, plant and equipment	(2)	1
Cost of manufacturing inventory recognised as an expense	48	41
Auditors' remuneration	2	2
Hire charges for plant and equipment	77	82
Other operating lease rentals	42	44

4.2 Analysis of fees paid to auditors:

		2005 £m	2004 £m
Services as auditors		2.1	1.9
Further assurance services	– acquisition due diligence	0.6	0.4
	– IFRS transition	0.4	0.2
	– other assurance services	–	0.3
Tax services	– compliance	0.1	0.1
	– advisory	0.2	0.1
		3.4	3.0

Included in the Group auditors' remuneration is an amount of £0.5m (2004: £0.4m) which was paid in respect of the parent Company.

5 Employee costs

5.1 Group employee costs during the year amounted to:

	2005 £m	2004 £m
Wages and salaries	835	828
Social security costs	84	80
Other pension costs (Note 25)	49	48
Share-based payments	3	3
	971	959

5.2 The average number of Group employees (including executive Directors) was:

	2005 Number	2004 Number
Building, building management and services	10,913	11,066
Civil and specialist engineering and services	10,455	9,957
Rail engineering and services	5,992	6,566
Investments and developments	136	112
Corporate	96	82
Discontinued operations	–	342
	27,592	28,125

At 31 December 2005, the total number of Group employees was 27,351 (2004: 27,030).

5.3 The average number of employees of Balfour Beatty plc was 80 (2004: 70). Total employee costs of Balfour Beatty plc were £12m (2004: £11m).

6 Investment income

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
PFI/PPP non-recourse – interest on financial assets	**36**	34	**–**	–
PFI/PPP subordinated debt interest receivable	**5**	9	**3**	7
Interest receivable from subsidiaries	**–**	–	**10**	16
Other interest receivable and similar income	**15**	13	**8**	5
	56	56	**21**	28

7 Finance costs

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
PFI/PPP non-recourse – other interest payable	**19**	18	**–**	–
Interest payable to subsidiaries	**–**	–	**21**	15
Other interest payable				
– bank loans and overdrafts	**1**	2	**3**	6
– finance leases	**–**	1	**–**	–
– other loans	**4**	7	**4**	4
	24	28	**28**	25
Preference shares – finance cost	**13**	–	**13**	–
	37	28	**41**	25
Exceptional items				
– premium on buy-back of preference shares	**3**	–	**3**	–
– net premium on repayment of US Dollar term loan	**6**	–	**6**	–
	46	28	**50**	25

The finance cost and premium on buy-back of preference shares are treated as finance costs under IAS 32 from adoption on 1 January 2005, but were previously treated as appropriations of profit for the year.

A preference dividend of 5.375p gross (4.8375p net) per cumulative convertible redeemable preference share of 1p was paid in respect of the six months ended 30 June 2005 on 1 July 2005 to holders of these shares on the register on 27 May 2005. A preference dividend of 5.375p gross (4.8375p net) per cumulative convertible redeemable preference share was paid in respect of the six months ended 31 December 2005 on 1 January 2006 to holders of these shares on the register on 25 November 2005.

8 Exceptional items

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
8.1 Credited to/(charged against) profit from operations				
Group operating profit				
– litigation settlements and fines	**(8)**	–	**–**	–
– profit on sale of interest in Connect Roads	**6**	–	**7**	–
– impairment of investment in Romec Ltd	**(8)**	–	**–**	–
– cancellation of Network Rail maintenance contracts	**–**	7	**–**	–
– pension settlement gain	**–**	8	**–**	–
– profit on sale of Hong Kong business	**–**	1	**–**	–
– impairment of goodwill in Balfour Beatty Rail Inc	**(4)**	(18)	**–**	–
	(14)	(2)	**7**	–
Share of results of joint ventures and associates				
– TXU distributions to Barking Power Ltd	**30**	–	**–**	–
	16	(2)	**7**	–
8.2 Charged to finance costs				
– premium on buy-back of preference shares	**(3)**	–	**(3)**	–
– net premium on repayment of US Dollar term loan	**(6)**	–	**(6)**	–
Credited to/(charged against) profit before taxation	**7**	(2)	**(2)**	–
8.3 Taxation thereon	**(3)**	(5)	**2**	–
Credited to/(charged against) profit for the year from continuing operations	**4**	(7)	**–**	–
8.4 Credited to profit for the year from discontinued operations				
– profit on sale of operations	**–**	160	**–**	–
Credited to profit for the year	**4**	153	**–**	–

8.1 The exceptional items charged against Group operating profit in 2005 arose from litigation and settlement costs of £8m which includes a payment to the US Government by Balfour Beatty Construction Inc, for its share of a settlement payment to resolve allegations arising from investigations into a joint venture contract awarded in 1995 and completed in 2000 and the costs awarded against Balfour Beatty Rail Infrastructure Services Ltd for admitted breaches of the Health and Safety at Work Act following the Hatfield derailment in October 2000, provision for the associated fine having been made in prior years; a profit of £6m on the disposal of a 15% interest in Connect Roads Ltd and Connect M77/GSO Holdings Ltd; an impairment charge of £8m in respect of the Group's investment in Romec Ltd; and a goodwill impairment charge of £4m in respect of Balfour Beatty Rail Inc. The exceptional item credited to profit from operations in share of results of joint ventures and associates in 2005 arises in Barking Power Ltd in which the Group holds a 25.5% interest. The £30m gain represents the Group's share, after charging taxation of £12m, of the first three distributions received by Barking Power Ltd from the administrator of TXU Europe following the damages agreement reached in December 2004 of £179m.

Exceptional items credited to profit from operations in 2004 arose in respect of the resolution of certain matters (£7m) previously provided for in 2003 in relation to the cancellation of three Network Rail maintenance contracts; an £8m settlement gain on curtailment of the Railways Pension Scheme; a profit of £1m arising on the transfer of the Group's construction contracts in progress in Hong Kong to the Gammon Skanska Group following the acquisition of a 50% interest in that business; and a goodwill impairment charge of £18m in respect of Balfour Beatty Rail Inc.

8 Exceptional items continued

8.2 The exceptional items charged against finance charges in 2005 are the premium of £3m arising on the repurchase for cancellation of 6.8m preference shares at a cost of £11m, and the net premium of £6m arising from the repayment of the US Dollar term loan.

8.3 The exceptional items in 2005 along with other prior year tax adjustments relating to exceptional items have given rise to a net tax charge of £3m.

8.4 The exceptional item credited to profit for the year from discontinued operations in 2004 comprised the gain arising on the disposal of Andover Controls amounting to £160m, after charging taxation of £12m.

9 Taxation

9.1 Taxation charge

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
UK current tax				
– corporation tax for the year at 30% (2004: 30%)	**34**	39	**(6)**	(1)
– double tax relief	**(6)**	(2)	**–**	–
– adjustments in respect of previous periods	**(9)**	(8)	**(6)**	(3)
	19	29	**(12)**	(4)
UK advance corporation tax				
– written back against current year UK current tax	**–**	(11)	**–**	(11)
– adjustments in respect of other periods	**–**	(6)	**–**	(6)
	–	(17)	**–**	(17)
Foreign current tax				
– foreign tax on profits for the year	**5**	5	**–**	–
– adjustments in respect of previous periods	**1**	(1)	**–**	–
	6	4	**–**	–
Total current tax	**25**	16	**(12)**	(21)
Deferred tax				
– UK	**3**	7	**–**	3
– foreign tax	**2**	–	**–**	–
– adjustments in respect of previous periods	**5**	5	**1**	2
Total deferred tax	**10**	12	**1**	5
Total tax charge/(credit)	**35**	28	**(11)**	(16)

The Group tax charge above does not include any amounts for joint ventures and associates, whose results are disclosed in the income statement net of tax (see Note 15).

In addition to the Group tax charge above are amounts credited directly to equity for current tax of £4m (2004: charge £2m) and deferred tax of £10m (2004: £5m), which less a charge in respect of joint ventures and associates of £5m (2004: £nil) totals £9m (2004: £3m). Further there is an amount of £nil (2004: £12m) which relates to tax on discontinued operations as in Note 10.

In addition to the Company tax charge above are amounts credited directly to equity for current tax of £1m (2004: £3m) and deferred tax of £1m (2004: £3m).

The weighted average applicable tax rate is 35% (2004: 27%) based on profit before taxation and exceptional items, excluding the results of joint ventures and associates. The increase is caused by the effects of the introduction of IAS 32 and IAS 39 from 1 January 2005, and in addition there is no offset of Advance Corporation Tax recognised in 2005.

9.2 Taxation reconciliation

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Profit before taxation	**141**	120	**32**	46
Less: Share of results of joint ventures and associates	**(73)**	(36)		
Group profit before taxation	**68**	84		
Tax on Group/Company profit before taxation at standard UK corporation tax rate of 30% (2004: 30%)	**20**	25	**10**	14
Effects of:				
Expenses not deductible for tax purposes including impairment of goodwill	**6**	11	**–**	4
Dividend income not taxable	**–**	–	**(19)**	(16)
Preference shares finance costs not deductible	**5**	–	**5**	–
Movement in deferred tax not recognised	**(3)**	–	**–**	–
Losses not available for offset	**9**	13	**–**	–
Higher/(lower) tax rates on foreign earnings	**3**	1	**–**	–
Disposal of investments and other assets not taxable	**(2)**	(1)	**(2)**	–
Advance corporation tax written back	**–**	(11)	**–**	(11)
Adjustments in respect of other periods	**(3)**	(10)	**(5)**	(7)
Total tax charge/(credit)	**35**	28	**(11)**	(16)

10 Discontinued operations

Andover Controls, sold in July 2004, and previously included in Building, building management and services, has been classified as discontinued. During 2004, Andover Controls contributed £6m to the Group's cash generated from operations and paid £1m in respect of investing activities. The results of its operations were as follows:

	2005 £m	2004 £m
Revenue	–	51
Cost of sales and net operating expenses	–	(43)
Profit before taxation	–	8
Attributable taxation	–	–
	–	8
Profit on disposal	–	172
Attributable taxation	–	(12)
Profit for the year from discontinued operations	–	168

11 Earnings per share

	Basic 2005 £m	Diluted 2005 £m	Basic 2004 £m	Diluted 2004 £m
Earnings				
– continuing operations	106	106	73	73
– discontinued operations	–	–	168	168
	106	106	241	241
Premium on buy-back of preference shares	–		6	
Exceptional items	(4)		(153)	
Adjusted earnings	102		94	

	Basic 2005 m	Diluted 2005 m	Basic 2004 m	Diluted 2004 m
Weighted average number of ordinary shares	424.2	428.7	419.4	423.6

	Basic 2005 Pence	Diluted 2005 Pence	Basic 2004 Pence	Diluted 2004 Pence
Earnings per share				
– continuing operations	24.9	24.7	17.3	17.2
– discontinued operations	–	–	40.1	39.7
	24.9	24.7	57.4	56.9
Premium on buy-back of preference shares	–		1.5	
Exceptional items	(0.8)		(36.4)	
Adjusted earnings per share	24.1		22.5	

The calculation of basic earnings is based on profit from continuing operations after charging, in 2004, preference dividends and appropriations arising on the buy-back of preference shares. The weighted average number of shares used to calculate diluted earnings per share has been adjusted for the conversion of share options. No adjustment has been made in respect of the potential conversion of the cumulative convertible redeemable preference shares, the effect of which would have been antidilutive throughout each year. Adjusted earnings per ordinary share, before exceptional items and, in 2004, appropriations arising on the buy-back of preference shares and including the results of discontinued operations, have been disclosed to give a clearer understanding of the Group's underlying trading performance.

12 Dividends on ordinary shares

	Per share 2005 Pence	Amount 2005 £m	Per share 2004 Pence	Amount 2004 £m
Proposed dividends for the year:				
Interim – current year	**3.50**	**15**	2.85	12
Final – current year	**4.60**	**20**	3.75	16
	8.10	**35**	6.60	28
Recognised dividends for the year:				
Final – prior year		**16**		14
Interim – current year		**15**		12
		31		26

An interim dividend of 3.5p (2004: 2.85p) per ordinary share was paid on 3 January 2006. Subject to approval at the Annual General Meeting on 11 May 2006, the final 2005 dividend will be paid on 3 July 2006 to holders of ordinary shares on the register on 28 April 2006 by direct credit or, where no mandate has been given, by cheque posted on 29 June 2006 payable on 3 July 2006. These shares will be quoted ex-dividend on 26 April 2006.

13 Goodwill

	Cost £m	Accumulated impairment losses £m	Carrying amount £m
At 1 January 2004	308	–	308
Exchange adjustments	(2)	–	(2)
Businesses acquired	13	–	13
Businesses sold	(22)	–	(22)
Impairment losses for the year	–	(18)	(18)
At 31 December 2004	297	(18)	279
Implementation of IAS 32 and IAS 39	(5)	–	(5)
At 1 January 2005	**292**	**(18)**	**274**
Exchange adjustments	**2**	**(2)**	**–**
Businesses acquired (see Note 29)	**14**	**–**	**14**
Impairment losses for the year	**–**	**(4)**	**(4)**
At 31 December 2005	**308**	**(24)**	**284**

The carrying amounts of goodwill by business segment are as follows:

			2005			2004
	Europe £m	**North America £m**	**Total £m**	Europe £m	North America £m	Total £m
Building, building management and services	**58**	**8**	**66**	57	4	61
Civil and specialist engineering and services	**68**	**17**	**85**	62	16	78
Rail engineering and services	**123**	**10**	**133**	124	12	136
Investments and developments	**–**	**–**	**–**	4	–	4
	249	**35**	**284**	247	32	279

The recoverable amount of goodwill has been based on value in use. Forecast cash flows are based on approved budgets and plans for the next three years. Subsequent cash flows have been increased in line with projected GDP for each territory. The cash flows have been discounted using a pre-tax discount rate of 12.9% based on the Group's weighted average cost of capital. The cash flows assume a residual value based on a multiple of earnings before interest and tax.

During 2005 Balfour Beatty Rail Inc. continued to suffer losses on a major contract which was acquired in 2001 as part of the Group's acquisition of ABC NACO. Cash outflows are now expected to occur on the contract until its completion in 2007 and as a result, a further goodwill impairment charge of £4m has been taken. Residual goodwill carried by this business is £10m.

14 Property, plant and equipment

14.1 Movements

	Land and buildings £m	Plant and equipment £m	Assets in course of construction £m	Group Total £m	Company Plant and equipment £m
Cost or deemed cost					
At 1 January 2004	46	341	3	390	2
Exchange adjustments	–	(7)	–	(7)	–
Additions	1	46	4	51	–
Disposals	(3)	(32)	–	(35)	–
Businesses sold	(2)	(15)	–	(17)	–
Transfers	–	2	(2)	–	–
At 1 January 2005	**42**	**335**	**5**	**382**	**2**
Exchange adjustments	**–**	**9**	**–**	**9**	**–**
Additions	**3**	**51**	**3**	**57**	**–**
Disposals	**(3)**	**(52)**	**–**	**(55)**	**–**
Businesses acquired	**3**	**3**	**–**	**6**	**–**
Transfers	**–**	**5**	**(5)**	**–**	**–**
At 31 December 2005	**45**	**351**	**3**	**399**	**2**
Accumulated depreciation					
At 1 January 2004	11	223	–	234	1
Exchange adjustments	–	(5)	–	(5)	–
Charge for the year	1	40	–	41	–
Disposals	–	(24)	–	(24)	–
Businesses sold	(1)	(12)	–	(13)	–
At 1 January 2005	**11**	**222**	**–**	**233**	**1**
Exchange adjustments	**–**	**7**	**–**	**7**	**–**
Charge for the year	**2**	**39**	**–**	**41**	**1**
Disposals	**(3)**	**(46)**	**–**	**(49)**	**–**
At 31 December 2005	**10**	**222**	**–**	**232**	**2**
Carrying amount					
At 31 December 2005	**35**	**129**	**3**	**167**	**–**
At 31 December 2004	31	113	5	149	1

The carrying amount of the Group's property, plant and equipment held under finance leases was £1m (2004: £1m). The Company has no land and buildings and no property, plant and equipment held under finance leases.

14.2 Analysis of carrying amount of land and buildings

	Group 2005 £m	Group 2004 £m
Freehold	**27**	25
Long leasehold – over 50 years unexpired	**2**	3
Short leasehold	**6**	3
	35	31

15 Investments in joint ventures and associates

15.1 Movements

	Net assets £m	Loans £m	Provisions £m	Total £m
At 1 January 2004	100	70	(28)	142
Income recognised	36	–	–	36
Actuarial losses on retirement benefit obligations	(7)	–	–	(7)
Exchange adjustments	(2)	–	–	(2)
Tax on items taken directly to equity	2	–	–	2
Dividends	(8)	–	–	(8)
Additions	9	–	–	9
Loans granted/(repaid)	–	(7)	–	(7)
Business acquired	36	–	–	36
Disposals and transfers	(15)	–	3	(12)
At 31 December 2004	151	63	(25)	189
Implementation of IAS 32 and IAS 39	14	–	–	14
At 1 January 2005	**165**	**63**	**(25)**	**203**
Income recognised	**73**	**–**	**–**	**73**
Impairment of investment	**(8)**	**–**	**–**	**(8)**
Actuarial gains on retirement benefit obligations	**7**	**–**	**–**	**7**
Fair value revaluation of PFI/PPP cash flow hedges	**(20)**	**–**	**–**	**(20)**
Fair value revaluation of PFI/PPP financial assets	**29**	**–**	**–**	**29**
Exchange adjustments	**5**	**–**	**–**	**5**
Tax on items taken directly to equity	**(6)**	**–**	**–**	**(6)**
Dividends	**(12)**	**–**	**–**	**(12)**
Additions	**11**	**–**	**–**	**11**
Loans granted/(repaid)	**–**	**1**	**–**	**1**
Business acquired (see Note 29)	**25**	**6**	**–**	**31**
Transfers	**40**	**21**	**–**	**61**
At 31 December 2005	**309**	**91**	**(25)**	**375**

Principal joint ventures and associates are shown in Note 36(b). The original cost of the Group's investments in joint ventures and associates was £121m (2004: £73m). The Group's share of borrowings of joint ventures and associates is shown in 15.2 below. The amount of these which was supported by the Group and the Company was £nil (2004: £nil). The borrowings of Barking Power Ltd and the PFI/PPP joint venture and associate companies are repayable over periods extending up to 2040. As disclosed in Note 31, the Company has committed to provide its share of further equity funding of joint ventures and associates in PFI/PPP projects. Further, in respect of a number of these investments, the Company has committed not to dispose of its equity interest until the relevant construction has been accepted. As is customary in such projects, dividend payments and other distributions are restricted until certain banking covenants are met.

15 Investments in joint ventures and associates continued

15.2 Share of results and net assets of joint ventures and associates

	Building, building management and services 2005 £m	Civil and specialist engineering and services 2005 £m	Rail engineering and services 2005 £m	Investments and developments PFI/PPP 2005 £m	Investments and developments Barking Power 2005 £m	Investments and developments Total 2005 £m	Total 2005 £m
Revenue	113	554	3	368	63	431	1,101
Operating profit before exceptional items	4	16	–	15	15	30	50
Investment income	–	1	–	69	–	69	70
Finance costs	–	(1)	–	(52)	(3)	(55)	(56)
Profit before taxation and exceptional items	4	16	–	32	12	44	64
Taxation	(1)	(6)	–	(10)	(4)	(14)	(21)
Exceptional items (net of taxation)	–	–	–	–	30	30	30
Profit after taxation	3	10	–	22	38	60	73
Non-current assets							
Goodwill	–	25	2	2	–	2	29
Property, plant and equipment	1	66	1	29	109	138	206
PFI/PPP financial assets	–	–	–	1,255	–	1,255	1,255
Other non-current assets	–	15	–	46	–	46	61
Current assets							
Cash and cash equivalents	–	76	6	200	40	240	322
Other current assets	18	165	–	112	22	134	317
Total assets	19	347	9	1,644	171	1,815	2,190
Current liabilities							
Borrowings	(3)	(17)	–	(64)	(12)	(76)	(96)
Other current liabilities	(12)	(220)	(9)	(170)	(16)	(186)	(427)
Non-current liabilities							
Borrowings	–	(4)	–	(1,050)	(60)	(1,110)	(1,114)
Other non-current liabilities	–	(39)	–	(111)	(28)	(139)	(178)
Total liabilities	(15)	(280)	(9)	(1,395)	(116)	(1,511)	(1,815)
Net assets	4	67	–	249	55	304	375

15 Investments in joint ventures and associates continued

15.2 Share of results and net assets of joint ventures and associates continued

	Building, building management and services 2004 £m	Civil and specialist engineering and services 2004 £m	Rail engineering and services 2004 £m	Investments and developments: PFI/PPP 2004 £m	Investments and developments: Barking Power 2004 £m	Investments and developments: Total 2004 £m	Total 2004 £m
Revenue	118	299	3	283	46	329	749
Operating profit before exceptional items	3	14	(1)	13	15	28	44
Investment income	–	1	–	66	–	66	67
Finance costs	–	(1)	–	(54)	(5)	(59)	(60)
Profit before taxation and exceptional items	3	14	(1)	25	10	35	51
Taxation	(1)	(5)	–	(6)	(3)	(9)	(15)
Profit after taxation	2	9	(1)	19	7	26	36
Non-current assets							
Goodwill	7	25	2	–	–	–	34
Property, plant and equipment	–	64	1	34	111	145	210
PFI/PPP financial assets	–	–	–	562	–	562	562
Other non-current assets	–	12	–	20	1	21	33
Current assets							
Cash and cash equivalents	3	59	6	206	14	220	288
Other current assets	16	118	–	44	14	58	192
Total assets	26	278	9	866	140	1,006	1,319
Current liabilities							
Borrowings	–	(15)	–	(33)	(11)	(44)	(59)
Other current liabilities	(15)	(168)	(8)	(81)	(11)	(92)	(283)
Non-current liabilities							
Borrowings	–	(13)	–	(617)	(72)	(689)	(702)
Other non-current liabilities	–	(30)	–	(27)	(29)	(56)	(86)
Total liabilities	(15)	(226)	(8)	(758)	(123)	(881)	(1,130)
Net assets	11	52	1	108	17	125	189

15.3 PFI/PPP investments

The Group's investment in PFI/PPP joint ventures and associates comprises:

	Net investment 2005 £m	**Reserves 2005 £m**	**Total 2005 £m**	Net investment 2004 £m	Reserves 2004 £m	Total 2004 £m
Metronet	**27**	**6**	**33**	16	7	23
Roads	**44**	**60**	**104**	11	11	22
Hospitals	**58**	**46**	**104**	23	31	54
Schools	**–**	**3**	**3**	–	–	–
Other concessions	**5**	**–**	**5**	8	1	9
	134	**115**	**249**	58	50	108

15 Investments in joint ventures and associates continued

15.4 Cash flow from/(to) joint ventures and associates

Net cash flow from/(to) joint ventures and associates comprises:

	PFI/PPP 2005 £m	Other 2005 £m	Total 2005 £m	PFI/PPP 2004 £m	Other 2004 £m	Total 2004 £m
Cash flows from investing activities						
Dividends from joint ventures and associates	3	9	12	2	6	8
Investment in and loans made to joint ventures and associates	(12)	–	(12)	(11)	–	(11)
– Equity	(11)	–	(11)	(9)	–	(9)
– Subordinated debt	(4)	–	(4)	(2)	–	(2)
– Subordinated debt repaid	3	–	3	–	–	–
Cash flows from financing activities						
Subordinated debt interest received	6	–	6	8	–	8
Net cash flow (to)/from joint ventures and associates	(3)	9	6	(1)	6	5

15.5 Share of joint ventures' and associates' reserves

	Accumulated profit/(loss) £m	Hedging reserves £m	PFI/PPP financial assets £m	Currency translation reserves £m	Total £m
At 1 January 2004	54	–	–	–	54
Income recognised	36	–	–	–	36
Actuarial losses on retirement benefit obligations	(7)	–	–	–	(7)
Exchange adjustments	–	–	–	(1)	(1)
Tax on items taken directly to equity	2	–	–	–	2
Dividends paid	(8)	–	–	–	(8)
Transfers	(4)	–	–	–	(4)
At 31 December 2004	73	–	–	(1)	72
Implementation of IAS 32 and IAS 39	–	(35)	49	–	14
1 January 2005	73	(35)	49	(1)	86
Income recognised	73	–	–	–	73
Actuarial gains on retirement benefit obligations	7	–	–	–	7
Fair value revaluation of PFI/PPP cash flow hedges	–	(20)	–	–	(20)
Fair value revaluation of PFI/PPP financial assets	–	–	29	–	29
Exchange adjustments	–	–	–	5	5
Tax on items taken directly to equity	(2)	5	(9)	–	(6)
Dividends paid	(12)	–	–	–	(12)
Transfers	14	(2)	8	–	20
At 31 December 2005	153	(52)	77	4	182

The Group has not recognised losses of joint ventures and associates during the year of £nil (2004: £1m) and cumulatively of £1m (2004: £1m).

16 Investments

16.1 Group

Investments of the Group comprise £38m (2004: £42m) worth of bonds held by Delphian Insurance Company Ltd, the Group's captive insurance company, the market value of which is not significantly different to the book value. These investments comprise fixed rate bonds or Treasury Stock with an average interest rate of 6.4% and weighted average life of five years. Market value is determined by using the market price of the bonds at the relevant valuation date.

16.2 Company

	2005 £m	2004 £m
Investment in subsidiaries	**1,000**	1,065
Investment in joint ventures and associates	**16**	4
Provisions	**(146)**	(197)
	870	872

17 PFI/PPP subsidiaries' financial assets

	Roads £m	Street lighting £m	Total £m
At 1 January 2004	–	3	3
Cash expenditure	58	7	65
Cash received	(32)	(1)	(33)
Interest	34	–	34
Businesses acquired	213	–	213
At 31 December 2004	273	9	282
Implementation of IAS 32 and IAS 39	60	(2)	58
At 1 January 2005	**333**	**7**	**340**
Cash expenditure	**14**	**7**	**21**
Cash received	**(38)**	**(3)**	**(41)**
Interest	**35**	**1**	**36**
Fair value adjustment	**(21)**	**2**	**(19)**
Businesses sold	**(323)**	**–**	**(323)**
At 31 December 2005	**–**	**14**	**14**

18 Inventories

	Group 2005 £m	Group 2004 £m	**Company 2005 £m**	Company 2004 £m
Unbilled work in progress	**24**	23	**–**	–
Development and housing land and work in progress	**14**	9	**–**	1
Manufacturing work in progress	**3**	3	**–**	–
Raw materials and consumables	**17**	14	**–**	–
Finished goods and goods for resale	**3**	1	**–**	–
	61	50	**–**	1

19 Construction contracts

Contracts in progress at balance sheet date:

	2005 £m	2004 £m
Due from customers for contract work	**217**	218
Due to customers for contract work	**(274)**	(264)
	(57)	(46)

The aggregate amount of costs incurred plus recognised profits (less recognised losses) for all contracts in progress at the balance sheet date was £13,368m (2004: £12,369m).

20 Derivative financial instruments

20.1 Group

	Assets 2005 £m	Liabilities 2005 £m	Assets 2004 £m	Liabilities 2004 £m
Current				
Forward foreign exchange contracts – net investment in foreign operations hedges	**–**	**(4)**	–	–
	–	**(4)**	–	–
Non-current				
Interest-rate swaps – PFI/PPP cash flow hedges	**2**	**(2)**	–	–
	2	**(2)**	–	–
	2	**(6)**	–	–

Interest-rate swaps:
The notional principal amounts of the outstanding PFI/PPP interest-rate swaps outstanding at 31 December 2005 were £14m. At 31 December 2005, the fixed interest rates range from 4.565% to 5.055% and principal floating rates are LIBOR. Other than in respect of PFI/PPP concessions, all interest-rate swaps were terminated during 2005.

Forward foreign exchange contracts:
The notional principal amounts of forward foreign exchange contracts designated as hedges of net investments in foreign operations at 31 December 2005 was £151m (2004: £105m). The gains and losses in equity on hedges of net investments in foreign operations will be released to the income statement on the disposal of the underlying net investment.

The credit risk on derivative financial instruments is limited because the counterparties are banks with high credit ratings assigned by international credit agencies.

Since the Group has only applied IAS 32 and IAS 39 from 1 January 2005, the comparatives above are £nil. In 2004 a net investment in foreign operations hedges of £1m was included within trade and other receivables in the Group balance sheet and £1m was included within both trade and other receivables and trade and other payables in the Company balance sheet.

20.2 Company

	Assets 2005 £m	Liabilities 2005 £m	Assets 2004 £m	Liabilities 2004 £m
Current				
Forward foreign exchange contracts – net investment in foreign operations hedges	**4**	**(4)**	–	–

21 Trade and other receivables

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Current				
Trade receivables	507	441	15	14
Less: Provision for impairment of trade receivables	(9)	(11)	–	–
	498	430	15	14
Due from subsidiaries	–	–	371	346
Due from joint ventures and associates	16	13	–	–
Due from jointly controlled operations	6	9	–	–
Contract retentions	67	75	–	–
Prepayments and accrued income	24	28	1	1
Advance corporation tax recoverable	8	8	8	8
	619	563	395	369
Non-current				
Trade and other receivables	7	10	2	9
Due from joint ventures and associates	–	–	33	24
Contract retentions	28	31	–	–
	35	41	35	33
	654	604	430	402

The Group's credit risk is primarily attributable to its trade receivables. Based on prior experience and an assessment of the current economic environment, management believes there is no further credit risk provision required in excess of the normal provision for impairment of trade receivables.

The Directors consider that the carrying values of current trade and other receivables approximate their fair values. The fair value of non-current trade and other receivables amounts to £32m (2004: £37m) and has been determined using yield curves and exchange rates prevailing at the balance sheet date and discounting future cash flows at interest rates prevailing at the balance sheet date.

It is Group policy that forward foreign exchange contracts are taken out as soon as a foreign currency receivable is identified.

22 Trade and other payables

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Current				
Trade and other payables	398	360	4	5
Due to subsidiaries	–	–	645	694
Due to jointly controlled operations	2	2	–	–
VAT, payroll taxes and social security	64	60	10	9
Dividends on ordinary shares	15	12	15	12
Dividends on preference shares	6	6	6	6
Accruals and deferred income	536	468	8	6
Due on acquisitions	6	7	5	7
Advance payments on contracts	11	31	–	–
	1,038	946	693	739
Non-current				
Trade and other payables	36	30	–	–
Due to joint ventures and associates	25	25	25	25
Accruals and deferred income	5	3	–	–
	66	58	25	25
	1,104	1,004	718	764

22 Trade and other payables continued

The maturity profile of the Group's non-current trade and other payables at 31 December was:

	Trade and other payables 2005 £m	Due to joint ventures and associates 2005 £m	Accruals and deferred income 2005 £m	Total 2005 £m	Trade and other payables 2004 £m	Due to joint ventures and associates 2004 £m	Accruals and deferred income 2004 £m	Total 2004 £m
Due within one to two years	**12**	**–**	**5**	**17**	11	–	3	14
Due within two to five years	**9**	**–**	**–**	**9**	2	–	–	2
Due after more than five years	**15**	**25**	**–**	**40**	17	25	–	42
	36	**25**	**5**	**66**	30	25	3	58
Fair values	**34**	**14**	**5**	**53**	28	15	3	46

The fair value of non-current trade and other payables has been determined by using yield curves and exchange rates prevailing at the balance sheet date and discounting future cash flows at interest rates prevailing at the balance sheet date.

It is Group policy that forward foreign exchange contracts are taken out as soon as a foreign currency trade and other payable is identified. Amounts due to joint ventures and associates and accruals and deferred income are all denominated in sterling.

23 Cash and cash equivalents and borrowings

23.1 Group

	Current 2005 £m	Non-current 2005 £m	Total 2005 £m	Current 2004 £m	Non-current 2004 £m	Total 2004 £m
Unsecured borrowings:						
– US dollar fixed rate term loan 8.06% (2008)	**–**	**–**	**–**	–	(62)	(62)
– bank overdrafts	**(29)**	**–**	**(29)**	(12)	–	(12)
– other short-term loans	**–**	**–**	**–**	(1)	–	(1)
Secured borrowings:						
– finance leases	**(1)**	**–**	**(1)**	(2)	–	(2)
	(30)	**–**	**(30)**	(15)	(62)	(77)
Cash and deposits	**146**	**–**	**146**	119	–	119
Term deposits	**199**	**–**	**199**	269	–	269
	315	**–**	**315**	373	(62)	311
PFI/PPP non-recourse term loans						
– sterling floating rate term loan (2008–2027)	**–**	**(13)**	**(13)**	–	(8)	(8)
– sterling floating rate term loan (2011–2030)	**–**	**(1)**	**(1)**	–	–	–
– sterling floating rate term loan (2005–2011)	**–**	**–**	**–**	(2)	(23)	(25)
– sterling floating rate term loan (2005–2012)	**–**	**–**	**–**	(11)	(82)	(93)
– sterling fixed rate bond (2006–2034)	**–**	**–**	**–**	–	(148)	(148)
	–	**(14)**	**(14)**	(13)	(261)	(274)
PFI/PPP term deposits	**–**	**–**	**–**	30	–	30
	–	**(14)**	**(14)**	17	(261)	(244)
Net cash/(borrowings)	**315**	**(14)**	**301**	390	(323)	67

The PFI/PPP project finance sterling debt obligations at 31 December 2005 arise under non-recourse facilities in the concession companies Connect Roads Sunderland Ltd and Connect Roads South Tyneside Ltd. The borrowings are secured by fixed and floating charges over each concession company's right, title and interest in certain assets and/or revenues and over each concession company's shares held by their immediate parent companies, Connect Roads Sunderland Holdings Ltd and Connect Roads South Tyneside Holdings Ltd. At 31 December 2004, the PFI/PPP project finance sterling debt obligations included those arising under non-recourse facilities in the concession companies, Connect A30/A35 Ltd, Connect A50 Ltd and Connect M77/GSO plc, which became joint ventures following the sale of a 15% interest to I^2 in December 2005.

A significant part of the PFI/PPP non-recourse project finance floating rate term loans have been swapped into fixed rate debt by the use of interest rate swaps. The interest rate obligations under the US dollar fixed rate term loan were swapped into floating rate sterling obligations. The loan and associated interest rate swaps were repaid in 2005 resulting in a net exceptional loss of £6m (see Note 8).

Cash, deposits and term deposits include the Group's share of amounts held by contracting joint arrangements of £110m (2004: £88m).

23 Cash and cash equivalents and borrowings continued

23.1 Group continued

The interest rate risk profile of the Group's net cash at 31 December 2005 was:

	Fixed rate £m	Floating rate £m	Total £m	Fixed rate: Weighted average interest rate %	Fixed rate: Weighted average period for which rate is fixed Years
Currency					
Cash					
Sterling – excluding PFI/PPP non-recourse project finance	**–**	**258**	**258**	**–**	**–**
US dollar	**–**	**46**	**46**	**–**	**–**
Other	**–**	**41**	**41**	**–**	**–**
	–	**345**	**345**	**–**	**–**
Borrowings					
Sterling – excluding PFI/PPP non-recourse project finance	**1**	**29**	**30**	**5.0**	**0.7**
Sterling – PFI/PPP non-recourse project finance	**14**	**–**	**14**	**5.0**	**11.7**
	15	**29**	**44**	**5.0**	**10.9**
Net (borrowings)/cash	**(15)**	**316**	**301**		

The interest rate risk profile of the Group's net cash at 31 December 2004 was:

	Fixed rate £m	Floating rate £m	Total £m	Fixed rate: Weighted average interest rate %	Fixed rate: Weighted average period for which rate is fixed Years
Currency					
Cash					
Sterling – excluding PFI/PPP non-recourse project finance	–	344	344	–	–
Sterling – PFI/PPP non-recourse project finance	–	30	30	–	–
US dollar	–	26	26	–	–
Other	–	18	18	–	–
	–	418	418	–	–
Borrowings					
Sterling – excluding PFI/PPP non-recourse project finance	–	5	5	–	–
Sterling – PFI/PPP non-recourse project finance	266	8	274	7.3	2.5
US dollar	2	70	72	9.1	0.5
	268	83	351	7.3	2.4
Net (borrowings)/cash	(268)	335	67		

The maturity profile of the Group's borrowings at 31 December was as follows:

	PFI/PPP non-recourse project finance 2005 £m	Other 2005 £m	Total 2005 £m	PFI/PPP non-recourse project finance 2004 £m	Other 2004 £m	Total 2004 £m
Due on demand or within one year	**–**	**30**	**30**	13	15	28
Due within one to two years	**–**	**–**	**–**	14	–	14
Due within two to five years	**3**	**–**	**3**	54	62	116
Due after more than five years	**11**	**–**	**11**	193	–	193
	14	**30**	**44**	274	77	351

23 Cash and cash equivalents and borrowings continued

23.1 Group continued

The Group's undrawn committed borrowing facilities in respect of which all conditions precedent were satisfied at 31 December were:

	PFI/PPP non-recourse project finance 2005 £m	Other 2005 £m	Total 2005 £m	PFI/PPP non-recourse project finance 2004 £m	Other 2004 £m	Total 2004 £m
Expiring in one year or less	–	–	–	–	–	–
Expiring in more than one year but not more than two years	–	–	–	–	210	210
Expiring in more than two years	42	484	526	19	–	19
	42	484	526	19	210	229

The table below compares the book values and the fair values of the Group's borrowings at 31 December:

	Book value 2005 £m	Fair value 2005 £m	Book value 2004 £m	Fair value 2004 £m
Unsecured borrowings				
– US dollar fixed rate term loan 8.06% (2008)	–	–	62	62
– bank overdrafts	29	29	12	12
– other short-term loans	–	–	1	1
Secured borrowings				
– finance leases	1	1	2	1
	30	30	77	76
PFI/PPP non-recourse term loans				
– sterling floating rate term loan (2008–2027)	13	13	8	8
– sterling floating rate term loan (2011–2030)	1	1	–	–
– sterling floating rate term loan (2005–2011)	–	–	25	26
– sterling floating rate term loan (2005–2012)	–	–	93	86
– sterling fixed rate bond (2006–2034)	–	–	148	156
	14	14	274	276
Borrowings	44	44	351	352

The fair values have been determined by using yield curves and exchange rates prevailing at the balance sheet date and discounting future cash flows at interest rates prevailing at the balance sheet date.

23.2 Company

	Current 2005 £m	Non-current 2005 £m	Total 2005 £m	Current 2004 £m	Non-current 2004 £m	Total 2004 £m
Unsecured borrowings						
– US dollar fixed rate term loan 8.06% (2008)	–	–	–	–	(62)	(62)
– bank overdrafts	(12)	–	(12)	(4)	–	(4)
	(12)	–	(12)	(4)	(62)	(66)
Term deposits	142	–	142	259	–	259
Net cash/(borrowings)	130	–	130	255	(62)	193

The unsecured borrowings and term deposits are sterling denominated and variable rate instruments. No interest rate risk is attributable to these. The bank overdrafts are repayable on demand and the term deposits have a range of maturities but are no longer than one month.

24 Deferred taxation

24.1 Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities. The net deferred tax position at 31 December was:

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Deferred tax assets	**83**	87	**1**	10
Deferred tax liabilities	**(3)**	(2)	**–**	–
	80	85	**1**	10

The movement for the year in the net deferred tax position was as follows:

	Group £m	Company £m
At 1 January 2004	100	12
Charged to income statement	(12)	(5)
Credited to equity	5	3
Businesses acquired	(8)	–
At 31 December 2004	85	10
Implementation of IAS 32 and IAS 39	(23)	(9)
At 1 January 2005	**62**	**1**
Charged to income statement	**(10)**	**(1)**
Credited to equity	**10**	**1**
Businesses sold	**18**	**–**
At 31 December 2005	**80**	**1**

24.2 Group
The following are the major deferred tax assets and liabilities recognised and the movements thereon during the year:

Deferred tax assets	Accelerated tax depreciation £m	Retirement benefit obligations £m	Unrelieved trading losses £m	Share-based payments £m	Provisions £m	Total £m
At 1 January 2004	7	68	–	4	27	106
Charged to income statement	(1)	(1)	–	1	(10)	(11)
Credited to equity	–	3	–	1	–	4
Businesses acquired	(3)	–	2	–	(5)	(6)
At 31 December 2004	3	70	2	6	12	93
Implementation of IAS 32 and IAS 39	–	–	–	–	–	–
Balance at 1 January 2005	**3**	**70**	**2**	**6**	**12**	**93**
Charged to income statement	**(3)**	**2**	**–**	**1**	**(4)**	**(4)**
Credited to equity	**–**	**4**	**–**	**–**	**–**	**4**
Businesses sold	**3**	**–**	**(2)**	**–**	**8**	**9**
At 31 December 2005	**3**	**76**	**–**	**7**	**16**	**102**

24 Deferred taxation continued

24.2 Group continued

Deferred tax liabilities	Revaluation of properties £m	Goodwill £m	Fair value adjustments £m	Undistributed earnings of joint ventures and associates £m	Preference shares £m	Total £m
At 1 January 2004	(2)	(2)	–	(2)	–	(6)
Charged to income statement	–	–	–	(1)	–	(1)
Credited to equity	1	–	–	–	–	1
Businesses acquired	–	–	–	(2)	–	(2)
At 31 December 2004	(1)	(2)	–	(5)	–	(8)
Implementation of IAS 32 and IAS 39	–	–	(13)	–	(10)	(23)
Balance at 1 January 2005	**(1)**	**(2)**	**(13)**	**(5)**	**(10)**	**(31)**
Charged to income statement	**–**	**(4)**	**(1)**	**(1)**	**–**	**(6)**
Credited to equity	**–**	**–**	**5**	**–**	**1**	**6**
Businesses sold	**–**	**–**	**9**	**–**	**–**	**9**
At 31 December 2005	**(1)**	**(6)**	**–**	**(6)**	**(9)**	**(22)**

Total net deferred tax asset	**80**

At the balance sheet date, the Group has unused tax losses that arose over a number of years of approximately £260m (2004: £220m) which are available for offset against future profits. No deferred tax has been recognised owing to the unpredictability of future profit streams. Of this total, £160m (2004: £120m) will expire 20 years after the year in which they arose, using losses incurred in earlier years before those incurred in later years, with the first expiry in 2015. The remaining losses may be carried forward indefinitely.

At the balance sheet date, the aggregate amount of temporary differences associated with undistributed reserves of subsidiaries for which deferred tax liabilities have not been recognised is £130m (2004: £150m). No liability has been recognised in respect of these differences because the Group is in a position to control the timing of the reversal of the temporary differences and it is probable that such differences will not reverse in the foreseeable future.

24.3 Company

The following represents the major deferred tax assets and liabilities recognised by the Company and the movement thereon during the year:

	Deferred tax liability	Deferred tax assets					
	Preference shares £m	Fair value adjustments £m	Share-based payments £m	Retirement benefit obligations £m	Provisions £m	Total £m	Net deferred tax asset £m
At 1 January 2004	–	–	4	2	6	12	12
Charged to income statement	–	–	1	(2)	(4)	(5)	(5)
Credited to equity	–	–	1	2	–	3	3
At 31 December 2004	–	–	6	2	2	10	10
Implementation of IAS 32 and IAS 39	(10)	1	–	–	–	1	(9)
Balance at 1 January 2005	**(10)**	**1**	**6**	**2**	**2**	**11**	**1**
Charged to income statement	**–**	**(1)**	**1**	**–**	**(1)**	**(1)**	**(1)**
Credited to equity	**1**	**–**	**–**	**–**	**–**	**–**	**1**
At 31 December 2005	**(9)**	**–**	**7**	**2**	**1**	**10**	**1**

25 Retirement benefit obligations

a) Group

The Group, through trustees, operates a number of pension schemes, the majority of which are of the defined benefit type and are funded. Contributions are determined in accordance with independent actuarial advice. Details of the IAS 19 valuations are set out in 25.1 below. Details of the last actuarial valuations and reviews and the assumptions used by the actuaries are set out in 25.2 below.

25.1 IAS 19 valuations

The latest actuarial funding valuations of the Group's principal defined benefit schemes have been updated by the actuaries to 31 December 2005 on the basis prescribed by IAS 19. In particular, scheme liabilities have been discounted using the rate of return on a high quality corporate bond rather than the expected rate of return on the assets in the scheme used in the funding valuations.

Other than the mortality assumptions set out in 25.2, the principal actuarial assumptions used were as follows:

	2005			2004		
	Balfour Beatty Pension Fund %	**Railways Pension Scheme %**	**Mansell schemes %**	Balfour Beatty Pension Fund %	Railways Pension Scheme %	Mansell schemes %
Inflation rate	**2.80**	**2.80**	**2.80**	2.80	2.80	2.80
Discount rate	**4.75**	**4.75**	**4.75**	5.30	5.30	5.30
Future salary increases	**4.30**	**4.30**	**4.30**	4.30	4.30	4.30
Future pension increases	**2.80**	**2.80**	**2.80**	2.80	2.80	2.80
Expected return on plan assets	**5.98**	**7.00**	**6.60**	6.11	7.11	7.06

The amounts recognised in the balance sheet are determined as follows:

	2005					2004				
	Balfour Beatty Pension Fund £m	**Railways Pension Scheme £m**	**Mansell schemes £m**	**Other schemes £m**	**Total £m**	Balfour Beatty Pension Fund £m	Railways Pension Scheme £m	Mansell schemes £m	Other schemes £m	Total £m
Present value of funded obligations	**(1,820)**	**(159)**	**(212)**	**(14)**	**(2,205)**	(1,638)	(125)	(190)	(12)	(1,965)
Fair value of plan assets	**1,643**	**136**	**160**	**12**	**1,951**	1,479	111	133	12	1,735
Deficit	**(177)**	**(23)**	**(52)**	**(2)**	**(254)**	(159)	(14)	(57)	–	(230)
Present value of unfunded obligations	**–**	**–**	**–**	**(26)**	**(26)**	–	–	–	(24)	(24)
Liability in the balance sheet	**(177)**	**(23)**	**(52)**	**(28)**	**(280)**	(159)	(14)	(57)	(24)	(254)

Other schemes comprise funded and unfunded post-retirement benefit obligations in Europe and North America, the majority of which arrangements are closed to new entrants.

The amounts recognised in the income statement are as follows:

	2005					2004				
	Balfour Beatty Pension Fund £m	**Railways Pension Scheme £m**	**Mansell schemes £m**	**Other schemes £m**	**Total £m**	Balfour Beatty Pension Fund £m	Railways Pension Scheme £m	Mansell schemes £m	Other schemes £m	Total £m
Current service cost	**(41)**	**(3)**	**(3)**	**(1)**	**(48)**	(43)	(4)	(3)	(1)	(51)
Interest cost	**(85)**	**(6)**	**(10)**	**(2)**	**(103)**	(80)	(7)	(9)	(1)	(97)
Expected return on plan assets	**89**	**8**	**9**	**1**	**107**	85	9	9	–	103
Total, included in employee costs (Note 5)	**(37)**	**(1)**	**(4)**	**(2)**	**(44)**	(38)	(2)	(3)	(2)	(45)
Pension settlement gain (included in exceptional items)	**–**	**–**	**–**	**–**	**–**	–	8	–	–	8

Pension expense, net of expected return on plan assets, is charged to contracts or overheads based on the function of scheme members and is included in cost of sales, net operating expenses and amounts due to or from customers. Actuarial gains and losses have been reported in the statement of recognised income and expense. The actual return on plan assets was £248m (2004: £155m).

Pension costs recognised in the income statement in respect of other defined contribution schemes was £5m (2004: £3m).

25 Retirement benefit obligations continued

25.1 IAS 19 valuations continued

The movement in the present value of obligations is as follows:

	2005 Balfour Beatty Pension Fund £m	2005 Railways Pension Scheme £m	2005 Mansell schemes £m	2005 Other schemes £m	2005 Total £m	2004 Balfour Beatty Pension Fund £m	2004 Railways Pension Scheme £m	2004 Mansell schemes £m	2004 Other schemes £m	2004 Total £m
At 1 January	**(1,638)**	**(125)**	**(190)**	**(36)**	**(1,989)**	(1,522)	(168)	(178)	(35)	(1,903)
Service cost	**(41)**	**(3)**	**(3)**	**(1)**	**(48)**	(43)	(4)	(3)	(1)	(51)
Interest cost	**(85)**	**(6)**	**(10)**	**(2)**	**(103)**	(80)	(7)	(9)	(1)	(97)
Settlement gains	**–**	**–**	**–**	**–**	**–**	–	49	–	–	49
Actuarial gains and losses	**(120)**	**(25)**	**(13)**	**(4)**	**(162)**	(53)	(4)	(5)	–	(62)
Contributions from members	**(12)**	**–**	**(2)**	**–**	**(14)**	(12)	–	(1)	–	(13)
Benefits paid	**76**	**–**	**6**	**3**	**85**	72	9	6	1	88
At 31 December	**(1,820)**	**(159)**	**(212)**	**(40)**	**(2,231)**	(1,638)	(125)	(190)	(36)	(1,989)

The movement in the fair value of plan assets is as follows:

	2005 Balfour Beatty Pension Fund £m	2005 Railways Pension Scheme £m	2005 Mansell schemes £m	2005 Other schemes £m	2005 Total £m	2004 Balfour Beatty Pension Fund £m	2004 Railways Pension Scheme £m	2004 Mansell schemes £m	2004 Other schemes £m	2004 Total £m
At 1 January	**1,479**	**111**	**133**	**12**	**1,735**	1,383	142	118	12	1,655
Expected return on plan assets	**89**	**8**	**9**	**1**	**107**	85	9	9	–	103
Settlement gains	**–**	**–**	**–**	**–**	**–**	–	(41)	–	–	(41)
Actuarial gains and losses	**110**	**16**	**15**	**–**	**141**	41	8	3	–	52
Contributions from employer	**29**	**1**	**7**	**–**	**37**	30	2	8	–	40
Contributions from members	**12**	**–**	**2**	**–**	**14**	12	–	1	–	13
Benefits paid	**(76)**	**–**	**(6)**	**(1)**	**(83)**	(72)	(9)	(6)	–	(87)
At 31 December	**1,643**	**136**	**160**	**12**	**1,951**	1,479	111	133	12	1,735

The fair value of and expected rate of return on the assets held by the schemes at 31 December are as follows:

	Balfour Beatty Pension Fund		Railways Pension Scheme		Mansell schemes		Other schemes	
	Expected rate of return 2005 %	Fair value 2005 £m	Expected rate of return 2005 %	Fair value 2005 £m	Expected rate of return 2005 %	Fair value 2005 £m	Expected rate of return 2005 %	Fair value 2005 £m
Equities	**8.1**	**679**	**8.1**	**91**	**8.1**	**95**	**–**	**–**
Bonds	**4.5**	**963**	**4.1**	**33**	**4.4**	**63**	**5.3**	**12**
Property	**–**	**–**	**6.1**	**12**	**–**	**–**	**–**	**–**
Cash and other net current assets	**3.8**	**1**	**–**	**–**	**3.8**	**2**	**–**	**–**
Rate of return/total	**6.0**	**1,643**	**7.0**	**136**	**6.6**	**160**	**5.3**	**12**

25 Retirement benefit obligations continued

25.1 IAS 19 valuations continued

	Balfour Beatty Pension Fund		Railways Pension Scheme		Mansell schemes		Other schemes	
	Expected rate of return 2004 %	Fair value 2004 £m	Expected rate of return 2004 %	Fair value 2004 £m	Expected rate of return 2004 %	Fair value 2004 £m	Expected rate of return 2004 %	Fair value 2004 £m
Equities	8.3	581	8.3	70	8.3	85	–	–
Bonds	4.7	871	4.8	26	4.9	47	4.9	12
Property	–	–	6.6	10	–	–	–	–
Cash and other net current assets	3.8	27	3.8	5	3.8	1	–	–
Rate of return/total	6.1	1,479	7.1	111	7.1	133	4.9	12

The expected rate of return on scheme assets assumption was determined as the average of the expected returns on the assets held by the scheme on 31 December. The rates of return for each class were determined as follows:

– equities and property: the rate adopted is consistent with the median assumption used in the actuary's asset modelling work as at 31 December;

– bonds: the overall rate has been set to reflect the yields available on the gilts and corporate bond holdings held at 31 December;

– cash and other net current assets: this class is mostly made of up of cash holdings and the rate adopted reflects current short-term returns on such deposits.

The estimated amounts of contributions expected to be paid to the funded schemes during 2006 is £42m. Contributions paid in 2005 for the principal schemes were £29m (2004: £30m) for the Balfour Beatty Pension Fund, £1m (2004: £2m) for the Railways Pension Scheme and £7m (2004: £8m) for the Mansell schemes.

The Railways Pension Scheme is a shared cost scheme. Accordingly the surplus/(deficit) shown above assumes that the Group will obtain economic benefit from, or be required to finance, only a proportion of the surplus or deficit in the Balfour Beatty section of the scheme. This proportion has been based on the apportionment of the surplus/(deficit) which has already been agreed together with the relevant provisions of the Trust Deed and Rules and Trustee guidelines regarding future surplus apportionments and deficit financing.

Year end historic information for the Group's post-retirement defined benefit plans is:

	2005 £m	2004 £m
Defined benefit obligation at end of year	**(2,231)**	(1,989)
Fair value of assets at end of year	**1,951**	1,735
Funded status at end of year	**(280)**	(254)
Experience adjustment for liabilities	**21**	(59)
Experience adjustment for assets	**141**	52

25.2 Funding valuations

The last formal valuation of the Balfour Beatty Pension Fund was carried out by the actuary at 31 March 2004 using the projected unit method and disclosed an excess of assets over past service liabilities of 1.7%. The assets and liabilities of the defined contribution section are included within the reported results of the Balfour Beatty Pension Fund. Due to the size of the membership of the Balfour Beatty Pension Fund (BBPF) (37,833 members at 31 December 2005) the scheme's actuary undertakes regular mortality investigations based on the experience exhibited by pensioners of the BBPF and is able to make statistically credible comparisons of this experience with the mortality rates set out in the various published mortality tables. The actuary is also able to monitor rates of improvement in the exhibited mortality over time. As a result of these reviews the Group is able to adopt with a measure of confidence consistent mortality assumptions for its IAS 19 valuations across its various defined benefit schemes.

The mortality tables adopted for these valuations and that of the BBPF's 2004 formal valuation are the 1992 series CMI tables as shown below:

	Mortality table (1992 series)	With average life expectancy at 65 years of age
Members in receipt of a pension		
– Male	PMA92c04	+18.4 years
– Female	PFA92c04	+21.3 years
Members not yet in receipt of a pension		
– Male	PMA92c22	+20.0 years
– Female	PFA92c22	+22.9 years

Certain Group employees are members of the Balfour Beatty Shared Cost section of the Railways Pension Scheme ("Railways Pension Scheme"). The last formal valuation of this defined benefit scheme was carried out by independent actuaries at 31 December 2004 using the projected unit method and disclosed that the market value of the scheme's assets represented 92.4% of the benefits that had accrued to members of which, being a shared cost scheme, the economic cost to the Group is circa 60% as represented in the scheme's assets and liabilities shown below. This proportion has been based on the apportionment of the surplus which has already been agreed together with the relevant provisions of the Trust Deed and Rules and Trustee guidelines regarding future surplus apportionments.

25 Retirement benefit obligations continued

25.2 Funding valuations continued

Mansell plc operates two funded defined benefit schemes, the Mansell plc Pension Scheme and the Hall & Tawse Retirement Benefit Plan ("Mansell schemes"), and two funded defined contribution schemes. The most recent actuarial valuation of the Mansell plc Pension Scheme, which was closed to new members from 31 December 2001, was carried out by independent actuaries at 31 July 2005 using the projected unit method. The valuation showed that the market value of the scheme's assets represented 78.0% of the benefits that had accrued to members on an ongoing funding basis. The most recent actuarial valuation of the Hall & Tawse Retirement Benefit Plan, which was closed to new members from 1 July 1998, was carried out by independent actuaries at 31 March 2005 using the projected unit method. The valuation showed that the market value of the scheme's assets represented 79.0% of the benefits that had accrued to members on an ongoing funding basis.

The Group's actuaries have reviewed the funding valuations of the Balfour Beatty Pension Fund, the Railways Pension Scheme and the Mansell schemes at 31 December 2005. The results of these reviews along with the assumptions used by the actuaries are set out below together with comparatives at 31 December 2004.

	At the last formal actuarial funding valuation				At 31 December 2005 valuation review			At 31 December 2004 valuation review		
			Mansell schemes							
	Balfour Beatty Pension Fund 31/3/2004 %	Railways Pension Scheme 31/12/2004 %	H&T Plan 31/3/2005 %	Mansell plc Scheme 31/7/2005 %	**Balfour Beatty Pension Fund %**	**Railways Pension Scheme %**	**Mansell schemes %**	Balfour Beatty Pension Fund %	Railways Pension Scheme %	Mansell schemes %
Principal actuarial valuation assumptions:										
Inflation assumption	2.7	2.8	2.9	2.8	**2.8**	**2.8**	**2.8**	2.8	2.8	2.8
Rate of increase in salaries	4.2	4.3	4.4	4.3	**4.3**	**4.3**	**4.3**	4.3	4.3	4.3
Rate of increase in pensions in payment (or such other fixed rate as is guaranteed)	2.7	2.8	2.9	3.0	**2.8**	**2.8**	**2.8**	2.8	2.8	2.8
Return on existing investments:										
– actives and deferred members										
– pre-retirement	8.1	6.8	6.6	6.4	**7.7**	**7.7**	**7.7**	7.8	7.8	7.8
– post-retirement	5.6	6.8	5.0	4.7	**5.0**	**5.0**	**5.0**	5.5	5.5	5.5
– pensioners, widows and dependants	5.1	4.8	5.0	n/a	**4.5**	**4.5**	**4.5**	5.0	5.0	5.0
Number of members:										
Active members	8,465	590	225	414	**8,392**	**627**	**604**	7,706	655	676
Deferred pensioners	11,540	1,776	1,001	610	**12,148**	**1,624**	**1,607**	12,020	1,664	1,609
Pensioners, widows and dependants	16,989	1,018	980	181	**17,293**	**1,091**	**1,186**	16,442	1,008	1,149
Total	36,994	3,384	2,206	1,205	**37,833**	**3,342**	**3,397**	36,168	3,327	3,434

	£m	£m	£m	£m	**£m**	**£m**	**£m**	£m	£m	£m
Scheme surplus/(deficit):										
Market value of assets	1,398	120	90	51	**1,644**	**136**	**160**	1,480	111	133
Present value of scheme liabilities	(1,374)	(130)	(113)	(65)	**(1,637)**	**(137)**	**(182)**	(1,479)	(105)	(169)
Surplus/(deficit) in scheme	24	(10)	(23)	(14)	**7**	**(1)**	**(22)**	1	6	(36)
Funding level	101.7%	92.4%	79.0%	78.0%	**100.4%**	**99.0%**	**88.0%**	100.1%	106.1%	78.9%

b) Company

Certain employees of the Company are members of the Balfour Beatty Pension Fund. Assets, liabilities, income and expenditure relating to this fund are allocated to Group companies participating in the scheme in proportion to pensionable payroll for the year. The Company's share of the net IAS 19 deficit was £8m (2004: £6m).

26 Provisions

	Group				**Company**
	Employee provisions £m	**Contract provisions £m**	**Other provisions £m**	**Group total £m**	**Other provisions £m**
At 1 January 2005	**20**	**28**	**55**	**103**	**9**
Charged to the income statement					
– additional provisions	**5**	**19**	**13**	**37**	**–**
– unused amounts reversed	**–**	**(9)**	**(6)**	**(15)**	**–**
Used during the year	**(2)**	**(4)**	**(10)**	**(16)**	**–**
At 31 December 2005	**23**	**34**	**52**	**109**	**9**

Employee provisions comprise obligations to employees other than retirement or post-retirement obligations. Contract provisions relate to provisions on contracts, including fault and warranty provisions, and other provisions principally comprise environmental, lease, legal claims and costs and other onerous commitments. The majority of provisions, other than employee provisions, are expected to be utilised within five years. Provision is made for the Directors' best estimate of known legal claims, investigations and legal actions in progress.

27 Share capital

27.1 Ordinary shares of 50p each

	Authorised		Issued	
	Million	£m	Million	£m
At 1 January 2004	696	348	420	210
Shares issued	–	–	4	2
At 1 January 2005	**696**	**348**	**424**	**212**
Shares issued	**–**	**–**	**3**	**2**
At 31 December 2005	**696**	**348**	**427**	**214**

All issued ordinary shares are fully paid.

	2005		2004	
	Number of ordinary shares	**Cash consideration £m**	Number of ordinary shares	Cash consideration £m
Ordinary shares issued during the year credited as fully paid:				
Savings-related share options exercised	**1,814,611**	**2**	1,696,608	2
Executive share options exercised	**1,442,708**	**4**	1,779,667	2
	3,257,319	**6**	3,476,275	4

At 31 December share options outstanding were as follows:

Year of issue	Exercise prices Pence	Normally exercisable in periods to	2005 **Ordinary shares Number**	2004 Ordinary shares Number
Savings-related				
1999	91.0	May 2005	**–**	115,000
2000	76.0	January 2006	**51,582**	1,188,937
2001	154.0	March 2007	**762,994**	852,334
2002	184.0	December 2007	**687,961**	1,432,521
2003	133.0	December 2008	**1,431,154**	1,593,566
2004	210.0	December 2009	**1,700,912**	1,911,059
2005	250.0	December 2010	**1,914,410**	–
			6,549,013	7,093,417
Executive				
1995	311.9	April 2005	**–**	1,165,850
1996	288.5	February 2006	**–**	153,404
1996	344.2	April 2006	**459,181**	459,181
1997	231.0	May 2007	**219,000**	265,000
1998	181.0	May 2008	**120,000**	167,500
1999	110.0	November 2009	**192,318**	255,818
2000	79.0	April 2010	**256,772**	304,366
2001	200.0	June 2011	**445,825**	675,150
2002	238.0	April 2012	**762,395**	1,466,000
2003	146.0	January 2013	**100,000**	100,000
2003	173.0	April 2013	**1,622,000**	1,762,500
2004	261.0	April 2014	**1,700,506**	1,835,000
2004	268.0	September 2014	**55,970**	55,970
			5,933,967	8,665,739

On 4 May 2005, options were granted over 1,983,110 ordinary shares under the Balfour Beatty savings-related share option scheme, at 250p per share, and these are normally exercisable in the periods from July 2008 to December 2008 and from July 2010 to December 2010 depending upon the length of savings contract chosen by the participant.

27 Share capital continued

27.2 Cumulative convertible redeemable preference shares of 1p each

	Authorised		Issued	
	Million	£m	Million	£m
At 1 January 2004	177	2	150	2
Shares repurchased	–	–	(14)	(1)
At 31 December 2004	177	2	136	1
Implementation of IAS 32 and IAS 39	–	–	–	(1)
At 1 January 2005	**177**	**2**	**136**	**–**
Shares repurchased	**–**	**–**	**(7)**	**–**
At 31 December 2005	**177**	**2**	**129**	**–**

All issued preference shares are fully paid. During the year, 6,837,500 preference shares (2004: 13,710,755) were repurchased for cancellation by the Company for a total consideration of £10,722,218 (2004: £19,859,291) at an average price of 156.8p (2004: 144.6p).

The preference shares are convertible at the option of the holder on the first day of the next calendar month following receipt of the conversion notice into new Balfour Beatty plc ordinary shares effectively on the basis of 21.05263 ordinary shares for every 100 preference shares based on the current conversion price of 475p per ordinary share, which is subject to adjustment in certain circumstances. Holders are entitled to a preferential dividend equivalent to a gross payment of 10.75p per preference share per annum, payable half yearly. Any preference shares still outstanding are redeemable on 1 July 2020 at £1 each, together with any arrears or accruals of dividend, unless the holder exercises any option granted by the Company to extend the redemption date. The maximum redemption value of all of the issued and outstanding preference shares, excluding any arrears or accruals of dividend, was £129m at 31 December 2005 (2004: £136m). The Company is entitled to convert all outstanding preference shares into ordinary shares if there are fewer than 44,281,239 preference shares in issue or if the average of the closing mid-market price for a Balfour Beatty plc ordinary share during a 30 day period exceeds 200% of the conversion price. The preference shares carry no voting rights at a general meeting of the Company, except where the dividend is six months or more in arrears, or where the business of the meeting includes a resolution which directly affects the rights and privileges attached to the preference shares or a resolution for the winding-up of the Company. On a winding-up of the Company, holders are entitled to receive the sum of £1 per preference share, together with any arrears or accruals of dividend, in priority to any payment on any other class of shares.

With the Group's adoption of IAS 32 and IAS 39 from 1 January 2005, the preference shares are regarded as a compound instrument, consisting of an equity and a liability component. The fair value of the liability component at the date of issue, included under non-current liabilities, was estimated using the prevailing market interest rate for a similar non-convertible instrument. The difference between the proceeds of issue of the preference shares and the fair value assigned to the liability component, representing the value of the equity conversion component, is included in shareholders' equity, net of deferred tax.

The liability component recognised on the balance sheet is calculated as follows:

	2005 £m	2004 £m
Redemption value of shares in issue at 1 January	**136**	–
Equity component	**(19)**	–
Deferred tax and interest element	**(14)**	–
Liability component at 1 January	**103**	–
Buy-back of preference shares	**(5)**	–
Liability component at 31 December	**98**	–

The fair value of the liability component of the preference shares at 31 December 2005 amounted to £98m. The fair value is calculated using the cash flows discounted at a rate based on the borrowings rate of 13.5%. Interest expense on the shares is calculated using the effective interest method.

28 Movements in equity/shareholders' funds

28.1 Group

						Other reserves					
	Called-up share capital £m	Share premium account £m	Equity component of preference shares £m	Special reserve £m	Share of joint ventures' and associates' reserves £m	Hedging reserves £m	PFI/PPP financial assets £m	Currency translation reserves £m	Other £m	Accumulated losses £m	Total £m
At 1 January 2004	212	328	–	–	54	–	–	–	9	(497)	106
Net profit for the year	–	–	–	–	36	–	–	–	–	224	260
Actuarial losses on retirement benefit obligations	–	–	–	–	(7)	–	–	–	–	(10)	(17)
Changes in fair value of net investment hedges	–	–	–	–	–	–	–	7	–	–	7
Currency translation differences	–	–	–	–	(1)	–	–	(5)	–	–	(6)
Tax on items taken directly to equity	–	–	–	–	2	–	–	(2)	–	3	3
Total recognised income for the year	–	–	–	–	30	–	–	–	–	217	247
Ordinary dividends	–	–	–	–	–	–	–	–	–	(26)	(26)
Joint ventures' and associates' dividends	–	–	–	–	(8)	–	–	–	–	8	–
Preference dividends	–	–	–	–	–	–	–	–	–	(13)	(13)
Premium paid on buy-back of preference shares	–	–	–	–	–	–	–	–	–	(6)	(6)
Issue of ordinary shares	1	3	–	–	–	–	–	–	–	–	4
Buy-back of preference shares – carrying value in shareholders' funds	–	–	–	–	–	–	–	–	–	(14)	(14)
Cancellation of share premium account and capital redemption reserve fund	–	(181)	–	185	–	–	–	–	(4)	–	–
Movements relating to share-based payments	–	–	–	–	–	–	–	–	4	–	4
Transfers	–	–	–	(4)	(4)	–	–	–	–	8	–
At 31 December 2004	213	150	–	181	72	–	–	–	9	(323)	302
Implementation of IAS 32 and IAS 39	(1)	(135)	19	–	14	(6)	26	–	–	8	(75)
At 1 January 2005	**212**	**15**	**19**	**181**	**86**	**(6)**	**26**	**–**	**9**	**(315)**	**227**
Net profit for the year	**–**	**–**	**–**	**–**	**73**	**–**	**–**	**–**	**–**	**33**	**106**
Actuarial gains/(losses) on retirement benefit obligations	**–**	**–**	**–**	**–**	**7**	**–**	**–**	**–**	**–**	**(21)**	**(14)**
PFI/PPP cash flow hedges:											
– net fair value (losses)/gains	**–**	**–**	**–**	**–**	**(20)**	**3**	**–**	**–**	**–**	**–**	**(17)**
– reclassified and reported in net profit	**–**	**–**	**–**	**–**	**–**	**1**	**–**	**–**	**–**	**–**	**1**
PFI/PPP financial assets:											
– fair value revaluation	**–**	**–**	**–**	**–**	**29**	**–**	**(19)**	**–**	**–**	**–**	**10**
– reclassified and reported in net profit	**–**	**–**	**–**	**–**	**–**	**–**	**(4)**	**–**	**–**	**–**	**(4)**
Changes in fair value of net investment hedges	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(6)**	**–**	**–**	**(6)**
Currency translation differences	**–**	**–**	**–**	**–**	**5**	**–**	**–**	**3**	**–**	**–**	**8**
Tax on items taken directly to equity	**–**	**–**	**1**	**–**	**(6)**	**–**	**5**	**1**	**–**	**8**	**9**
Total recognised income for the year	**–**	**–**	**1**	**–**	**88**	**4**	**(18)**	**(2)**	**–**	**20**	**93**
Ordinary dividends	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(31)**	**(31)**
Joint ventures' and associates' dividends	**–**	**–**	**–**	**–**	**(12)**	**–**	**–**	**–**	**–**	**12**	**–**
Issue of ordinary shares	**2**	**4**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**6**
Buy-back of preference shares	**–**	**7**	**(2)**	**–**	**–**	**–**	**–**	**–**	**–**	**(8)**	**(3)**
Movements relating to share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(2)**	**2**	**–**
Transfers	**–**	**–**	**–**	**(6)**	**20**	**2**	**(8)**	**–**	**–**	**(8)**	**–**
At 31 December 2005	**214**	**26**	**18**	**175**	**182**	**–**	**–**	**(2)**	**7**	**(328)**	**292**

28 Movements in equity/shareholders' funds continued

28.2 Company

	Called-up share capital £m	Share premium account £m	Equity component of preference shares £m	Special reserve £m	Other reserves £m	Accumulated profits £m	Total £m
At 1 January 2004	212	328	–	–	50	91	681
Net profit for the year	–	–	–	–	–	62	62
Ordinary dividends	–	–	–	–	–	(26)	(26)
Preference dividends	–	–	–	–	–	(13)	(13)
Premium paid on buy-back of preference shares	–	–	–	–	–	(6)	(6)
Issue of ordinary shares	1	3	–	–	–	–	4
Buy-back of preference shares – carrying value in shareholders' funds	–	–	–	–	–	(14)	(14)
Cancellation of share premium account and capital redemption reserve fund	–	(181)	–	185	(4)	–	–
Movements relating to share-based payments	–	–	–	–	4	–	4
Transfers	–	–	–	(4)	–	4	–
At 31 December 2004	213	150	–	181	50	98	692
Implementation of IAS 32 and IAS 39	(1)	(135)	19	–	–	3	(114)
At 1 January 2005	**212**	**15**	**19**	**181**	**50**	**101**	**578**
Net profit for the year	**–**	**–**	**–**	**–**	**–**	**43**	**43**
Actuarial losses on retirement benefit obligations	**–**	**–**	**–**	**–**	**–**	**(1)**	**(1)**
Ordinary dividends	**–**	**–**	**–**	**–**	**–**	**(31)**	**(31)**
Issue of ordinary shares	**2**	**4**	**–**	**–**	**–**	**–**	**6**
Buy-back of preference shares	**–**	**7**	**(2)**	**–**	**–**	**(8)**	**(3)**
Movements relating to share-based payments	**–**	**–**	**–**	**–**	**(1)**	**1**	**–**
Tax on items taken directly to equity	**–**	**–**	**1**	**–**	**–**	**–**	**1**
Transfers	**–**	**–**	**–**	**(6)**	**–**	**6**	**–**
At 31 December 2005	**214**	**26**	**18**	**175**	**49**	**111**	**593**

The accumulated profits of Balfour Beatty plc are wholly distributable.

28.3 The accumulated losses in the Group and the accumulated profits of the Company are stated net of investments in Balfour Beatty plc ordinary shares of 50p each acquired by the Group's employee discretionary trust, the Balfour Beatty Employee Share Ownership Trust, to satisfy awards under the Balfour Beatty Performance Share Plan. In 2005, 1.1m (2004: 0.8m) shares were purchased at a cost of £3.5m (2004: £2.0m). The market value of the 1.5m (2004: 1.2m) shares held by the Trust at 31 December 2005 was £5.4m (2004: £3.7m). Following confirmation of the performance criteria at the end of the performance period, the appropriate number of shares will be unconditionally transferred to participants. In 2005, 0.8m shares were transferred to participants in relation to the April 2002 awards (2004: 1.4m shares for the June 2001 awards). The trustees have waived the rights to dividends on shares held by the Trust. Other reserves in the Group and the Company include £2.8m relating to unvested Performance Share Plan awards (2004: £1.4m) and £3.9m relating to unvested share options (2004: £2.0m).

29 Acquisitions

On 17 February 2005, the Group acquired 100% of the issued share capital of JCM Group in the USA for an initial consideration of US$8.9m, deferred consideration of US$1.2m and costs of US$1.4m. The provisional fair value of net assets acquired was US$4.0m and goodwill arising was US$7.5m. The goodwill recognised is attributable to the benefit obtained from JCM's position being particularly strong in the higher education, healthcare and government markets.

On 9 August 2005, the Group acquired 100% of the issued share capital of Pennine Group, the UK ground engineering business, for an initial consideration of £7.3m, deferred consideration of £0.5m and costs of £0.3m. The provisional fair value of net assets acquired was £2.3m and provisional goodwill arising was £5.8m, pending finalisation of the post-acquisition review of the fair value of the net assets. The goodwill recognised is attributable to the acquisition giving the Group a strong, complementary presence in ground engineering.

On 24 August 2005, the Group acquired 100% of the issued share capital of Signalbau Bahn GmbH, the specialist German rail signalling contractor, for a consideration of €14.0m, before adjustment to reflect the value of net assets acquired, estimated at €0.8m. The provisional fair value of net assets acquired was €6.8m and provisional goodwill arising was €6.4m, pending finalisation of the post-acquisition review of the fair value of the net assets. The goodwill recognised is attributable to the acquisition giving the Group the opportunity to broaden its signalling capability in Germany.

On 16 December 2005, the Group acquired a further 31.4% interest in Consort Healthcare (Edinburgh Royal Infirmary) Holdings Ltd for a consideration of £31.1m and costs of £0.1m.

The provisional fair value of the net assets acquired, consideration paid and provisional goodwill arising on these transactions were:

	Book value of assets acquired £m	Fair value adjustments £m	Fair value of assets acquired £m
Net assets acquired:			
Goodwill	14	–	14
Property, plant and equipment	6	–	6
Investments in joint ventures and associates	31	–	31
Working capital	5	(1)	4
Term loans	(1)	–	(1)
	55	(1)	54
Due on acquisitions			2
Total consideration			56
Satisfied by:			
Cash consideration			55
Costs incurred			1
			56

The subsidiary businesses acquired earned revenues of £30m and profits from operations of £1.2m for the full year, of which £16m and £1.2m respectively were earned in the period since acquisition.

In 2005, £2.2m deferred consideration was paid in respect of acquisitions completed in earlier years.

30 Share-based payments

30.1 The Company operates four equity-settled share-based payment arrangements, namely the savings-related share option scheme, the executive share option scheme, the performance share plan and the deferred bonus plan. The Group recognised total expenses related to equity-settled share-based payment transactions since 7 November 2002 of £3.3m in 2005 (2004: £2.4m).

30.2 Savings-related share options:
The Company operates an Inland Revenue approved savings-related share option scheme ("SAYE") under which employees are granted an option to purchase ordinary shares in the Company in either three or five years time, dependent upon their entering into a contract to make monthly contributions to a savings account over the relevant period. These savings are used to fund the option exercise. This scheme is open to all employees based in the UK and performance conditions are not applied to the exercise of SAYE options. Employees normally have a period of six months after completion of the savings contributions during which to exercise the SAYE options, failing which they lapse. Details of SAYE options granted during the year are shown in Note 27. The information required under IFRS 2 "Share-based Payment" in relation to SAYE options granted since 7 November 2002 was:

	SAYE options 2005 Number	Weighted average exercise price 2005 Pence	SAYE options 2004 Number	Weighted average exercise price 2004 Pence
Outstanding at 1 January	**3,504,625**	**175.0**	1,927,211	133.0
Granted during the year	**1,983,110**	**250.0**	1,983,018	210.0
Forfeited during the year	**(413,624)**	**189.9**	(357,110)	148.2
Exercised during the year	**(27,635)**	**157.4**	(48,494)	135.6
Expired during the year	**–**	**–**	–	–
Outstanding at 31 December	**5,046,476**	**203.3**	3,504,625	175.0
Exercisable at 31 December	**–**		–	

The weighted average share price at the date of exercise for those SAYE options exercised during the year was 342.0p (2004: 265.0p). Those SAYE options outstanding at 31 December 2005 had a weighted average remaining contractual life of 3.1 years (2004: 3.6 years).

The principal assumptions used by the consultants in the stochastic model for the SAYE options granted in 2005, including expected volatility determined from the historic weekly share price movements over the three year period immediately preceding the invitation date, were:

Invitation date	Exercise price Pence	Closing share price before invitation Pence	Expected dividend yield %	Expected volatility of shares %	Expected term of options Years	Risk free interest rate %	Calculated fair value of an option Pence
12 April 2005	**250.0**	**313.0**	**2.11**	**38**	**3.25**	**4.62**	**111.4**
12 April 2005	**250.0**	**313.0**	**2.11**	**38**	**5.25**	**4.64**	**128.3**

30 Share-based payments continued

30.3 Executive share options:

The Company has not granted any executive share options in 2005, but has previously operated the scheme under which employees are granted an option to purchase ordinary shares in the Company, which is exercisable between three and ten years after the date of grant provided that any performance condition has been met. For the executive options granted since 7 November 2002, earnings per share before goodwill amortisation and exceptional items ("eps") for the last year of the minimum three year performance period must have grown from their respective fixed base eps by a total of at least 3% per annum plus the increase in RPI over the relevant period. The performance condition allows for re-testing from the fixed base eps after a four or five year performance period. The information required under IFRS 2 "Share-based Payment" in relation to executive options granted since 7 November 2002 was:

	Executive options 2005 Number	**Weighted average exercise price 2005 Pence**	Executive options 2004 Number	Weighted average exercise price 2004 Pence
Outstanding at 1 January	**3,753,470**	**216.7**	1,895,000	171.6
Granted during the year	**–**	**–**	1,890,970	261.2
Forfeited during the year	**(263,500)**	**214.1**	(20,000)	173.0
Exercised during the year	**(11,494)**	**261.0**	(12,500)	173.0
Expired during the year	**–**	**–**	–	–
Outstanding at 31 December	**3,478,476**	**216.8**	3,753,470	216.7
Exercisable at 31 December	**–**		–	

The weighted average share price at the date of exercise for those executive options exercised during the year was 323.9p (2004: 267.5p). Those executive options outstanding at 31 December 2005 had a weighted average remaining contractual life of 7.8 years (2004: 8.8 years).

30.4 Performance share plan awards:

The Company operates a performance share plan under which executive Directors and key senior employees are granted conditional awards of ordinary shares in the Company, which are exercisable within three months of the third anniversary of the date of award. These awards will only vest to the extent that an earnings per share growth target is met over a three year performance period. On 18 April 2005 a maximum of 1,708,394 conditional shares were awarded which are normally exercisable in the period between April 2008 and July 2008: the maximum award of shares is made only where the Company's eps increases by at least 70% in the relevant performance period; 30% of the award is made where the Company's eps increases by 25% over the period; if growth in eps is between 25% and 70%, the number of shares will be awarded pro rata to the growth in eps; and no shares can be awarded if growth in eps is less than 25% over the period. The information required under IFRS 2 "Share-based Payment" in relation to performance share awards granted since 7 November 2002 was:

	Conditional awards 2005 Number	Conditional awards 2004 Number
Outstanding at 1 January	**3,766,120**	2,456,982
Granted during the year	**1,708,394**	1,857,700
Forfeited during the year	**(665,263)**	(548,562)
Exercised during the year	**–**	–
Expired during the year	**–**	–
Outstanding at 31 December	**4,809,251**	3,766,120
Exercisable at 31 December	**–**	–

Those performance share awards outstanding at 31 December 2005 had a weighted average remaining contractual life of 1.2 years (2004: 1.7 years).

As the awards are satisfied by the transfer of shares for no consideration, the fair values of those awards are the closing share price before award date (297.0p) as adjusted for the expected dividends which will not accrue to the awardee over the performance period. The assumed dividend yield for the 2005 awards was 2.22% and the resulting calculated fair value was 278.0p.

30.5 Deferred bonus plan awards:

The Company has introduced a deferred bonus plan in 2005 under which one-third of the annual bonus of executive Directors and key senior employees will be deferred in the form of ordinary shares in the Company, which will be released after three years, providing the individual is still in the Group's employment at that time. The first allocation of shares under this scheme will be made in March 2006.

31 Commitments

Capital expenditure authorised and contracted for which has not been provided for in the accounts amounted to £5m (2004: £15m) in the Group and at £nil (2004: £nil) in the Company.

The Company has committed to provide its share of further equity funding and subordinated debt of joint ventures and associates in PFI/PPP projects amounting to £75m (2004: £73m) and £5m (2004: £18m) in respect of PFI/PPP subsidiaries.

The Group leases land and buildings, equipment and other various assets under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights. The lease expenditure charged to the income statement is disclosed under Note 4.

Future operating lease expense commitments comprise:

	Land and buildings 2005 £m	Other 2005 £m	Land and buildings 2004 £m	Other 2004 £m
Group				
Due within one year	**23**	**24**	22	22
Due between one and five years	**63**	**43**	57	43
Due after more than five years	**44**	**–**	43	–
	130	**67**	122	65
Company				
Due within one year	**3**	**–**	3	–
Due between one and five years	**13**	**–**	13	–
Due after more than five years	**14**	**–**	17	–
	30	**–**	33	–

Future operating lease income commitments comprise:

	Land and buildings 2005 £m	Plant 2005 £m	Land and buildings 2004 £m	Plant 2004 £m
Group				
Due within one year	**3**	**3**	3	3
Due between one and five years	**5**	**1**	7	4
	8	**4**	10	7

32 Contingent liabilities and assets

32.1 Contingent liabilities:

Contingent liabilities, which are not expected to give rise to any material loss, include:

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Guarantees of subsidiary undertakings and other support	**–**	–	**–**	2

The Company and certain subsidiary undertakings have, in the normal course of business, given guarantees and entered into counter-indemnities in respect of bonds relating to the Group's own contracts and given guarantees in respect of the Group's share of certain contractual obligations of joint ventures and associates. The Company has given limited indemnities up to a maximum of £11m to Halliburton Company and Brown & Root Ltd in respect of the performance of Devonport Management Ltd on certain construction contracts and a further limited guarantee in respect of operational contracts undertaken for the Ministry of Defence.

Prior to 1999, the Group owned large cable manufacturing businesses, predominantly in Europe and North America. These businesses have subsequently been sold through a number of sale and purchase agreements. In common with many such agreements, the Group gave certain indemnities in respect of environmental and other matters which extend until 2007. The Group maintains provisions against all identified issues based on current available information and carries some insurance cover against further liabilities that may arise.

As stated in Note 26, provision has been made for the Directors' best estimate of the known legal claims, investigations and legal actions in progress. The Group takes legal advice as to the likelihood of success of claims and actions and no provision is made where the Directors consider, based on that advice, that the action is unlikely to succeed or a sufficiently reliable estimate of the potential obligation cannot be made.

32.2 Contingent assets:

In November 2002, TXU Europe, whose subsidiaries are respectively a shareholder and customer of Barking Power Ltd, in which the Group holds a 25.5% interest, entered administration. As a result, the long-term electricity supply contract with a TXU subsidiary was terminated, triggering an entitlement to payment for damages, for which Barking Power Ltd lodged a substantial claim. In December 2004, Barking Power Ltd reached an agreement in principle with the administrators on the value of its claim at £179m. Barking Power Ltd received dividends from the settlement totalling £176m during the year ended 31 December 2005, comprising damages of £164m and £12m for a pre-liquidation receivable. The final dividend of £3m remains outstanding.

33 Related party transactions

Joint ventures and associates:

The Group has contracted with, provided services to, and received management fees from, certain joint ventures and associates amounting to £431m (2004: £266m). These transactions occurred in the normal course of business at market rates and terms. In addition, the Group procured equipment and labour on behalf of certain joint ventures and associates which were recharged at cost with no mark-up. The amounts due to or from joint ventures and associates at 31 December are disclosed within trade and other receivables and trade and other payables in Notes 21 and 22 respectively.

Pension schemes:

The Group recharged the Balfour Beatty Pension Fund with the costs of administration and advisers' fees borne by the Group amounting to £3.0m in 2005 (2004: £2.9m).

Key personnel:

The remuneration of key personnel of Balfour Beatty plc was:

	2005 £m	2004 £m
Short-term benefits	**3.771**	3.701
Post employment benefits	**1.553**	2.003
Termination benefits	**–**	0.040
Share-based payments	**0.678**	0.464
	6.002	6.208

Further details of Directors' emoluments, pension benefits and interests are set out in the Remuneration report on pages 44 to 50.

Key personnel comprise the Board and 3 Group Managing Directors (2004: 2) who are directly responsible for the Group's operating companies.

34 Post balance sheet events

No post balance sheet events have occurred since 31 December 2005.

35 Notes to the cash flow statement

35.1 Cash generated from operations comprises:

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Profit from operations – continuing	**131**	92	**61**	43
Trading profit from discontinued operations	**–**	8	**–**	–
Share of results of joint ventures and associates	**(73)**	(36)	**–**	–
Dividends received	**–**	–	**(63)**	(53)
Depreciation of property, plant and equipment	**41**	41	**–**	–
Impairment charge	**12**	18	**–**	–
Movements relating to share-based payments	**3**	2	**3**	2
(Profit)/loss on disposal of property, plant and equipment	**(2)**	1	**–**	–
Profit on disposal of businesses	**(6)**	(1)	**–**	–
Profit on disposal of investment	**–**	–	**(7)**	–
Operating cash flows before movements in working capital	**106**	125	**(6)**	(8)
Decrease in working capital	**61**	23	**3**	(8)
Cash generated from operations	**167**	148	**(3)**	(16)

35.2 Cash and cash equivalents comprise:

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Cash and deposits	**131**	119	**–**	–
Term deposits	**199**	269	**142**	259
UK PFI/PPP project finance – cash and deposits	**15**	–	**–**	–
– term deposits	**–**	30	**–**	–
Bank overdrafts	**(29)**	(12)	**(12)**	(4)
	316	406	**130**	255

Cash and cash equivalents include cash in hand deposits held at call with banks, other short-term highly liquid investments with original maturities of less than three months and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities within the balance sheet.

35.3 Analysis of movement in net cash/(borrowings):

	Group 2005 £m	Group 2004 £m	Company 2005 £m	Company 2004 £m
Opening net cash/(borrowings)	**67**	124	**193**	(42)
Net (decrease)/increase in cash and cash equivalents	**(93)**	209	**(129)**	235
Acquisitions – borrowings at date of acquisition	**(1)**	(278)	**–**	–
Businesses sold – borrowings at date of disposal	**253**	–	**–**	–
New loans	**(6)**	(6)	**–**	–
Repayment of loans	**80**	12	**66**	–
Finance lease principal repayments	**2**	2	**–**	–
Exchange adjustments	**(1)**	4	**–**	–
Closing net cash	**301**	67	**130**	193

35.4 Acquisitions of businesses:

	Group 2005 £m	Group 2004 £m
Net assets acquired:		
Goodwill	**14**	13
Property, plant and equipment	**6**	–
Investments in joint ventures and associates	**31**	36
PFI/PPP financial assets	**–**	213
Working capital	**4**	59
Current tax liabilities	**–**	(4)
Deferred tax liabilities	**–**	(6)
Term loans	**(1)**	–
PFI/PPP non-recourse term loans	**–**	(278)
	54	33
Due on acquisitions	**2**	4
	56	37
Satisfied by:		
Cash consideration	**56**	58
Cash, deposits and overdrafts acquired	**–**	(41)
Cash outflow	**56**	17
Interest in joint ventures transferred	**–**	20
	56	37

35.5 Disposals of businesses:

	Group 2005 £m	Group 2004 £m
Net assets disposed of:		
Goodwill	**–**	22
Property, plant and equipment	**–**	4
Investments in joint ventures and associates	**–**	3
PFI/PPP financial assets	**323**	–
Working capital	**(8)**	17
Current tax liabilities	**(1)**	(2)
Deferred tax liabilities	**(18)**	–
PFI/PPP non-recourse term loans	**(253)**	–
	43	44
Profit on sale	**6**	173
Fair value movements	**(3)**	–
	46	217
Satisfied by:		
Cash consideration	**14**	221
Cash, deposits and overdrafts sold	**(29)**	(4)
	(15)	217
Interest in joint venture retained	**61**	–
	46	217

36 Principal subsidiaries, joint ventures and associates

	Country of incorporation or registration
a) Principal subsidiaries	
Building, civil and rail engineering	
Balfour Beatty Civil Engineering Ltd	
Balfour Beatty Construction Inc	USA
Balfour Beatty Construction Northern Ltd	Scotland
Balfour Beatty Construction Scottish and Southern Ltd	Scotland
Balfour Beatty Group Ltd	
Balfour Beatty Management Ltd	
Balfour Beatty Power Networks (Distribution Services) Ltd	
Balfour Beatty Power Networks Ltd	
Balfour Beatty Rail GmbH	Germany
Balfour Beatty Rail Infrastructure Services Ltd	
Balfour Beatty Rail Ltd	
Balfour Beatty Rail Projects Ltd	
Balfour Beatty Rail Services Inc	USA
Balfour Beatty Rail SpA	Italy
Balfour Beatty Rail Track Systems Ltd	
Balfour Beatty Refurbishment Ltd	
Balfour Beatty Utilities Ltd	
Balfour Kilpatrick Ltd	Scotland
Balfour Kilpatrick International Ltd	Scotland
Balvac Ltd	
Cruickshanks Ltd*	Scotland
Haden Building Management Ltd	
Haden Building Services Ltd	
Haden Young Ltd	
Heery International Inc	USA
Heery International Ltd	
Lounsdale Electric Ltd	Scotland
Mansell Construction Services Ltd	
Mansell plc	
Marta Track Constructors Inc	USA
Metroplex Corporation	USA
National Engineering and Contracting Company	USA
Painter Brothers Ltd	
Pennine Projects Ltd	
Raynesway Construction Ltd	
Raynesway Construction Southern Ltd	
Signalbau Bahn GmbH	Germany
Stent Foundations Ltd	
Investments and developments	
PFI/PPP:	
Balfour Beatty Capital Projects Ltd	
Balfour Beatty Infrastructure Investments Ltd*	
Connect Roads South Tyneside Holdings Ltd	
Connect Roads Sunderland Holdings Ltd	
Property:	
Balfour Beatty Property Ltd*	
Others	
Balfour Beatty Inc	USA
Balfour Beatty Investment Holdings Ltd*	
BICC Finance BV	Holland
BICC Overseas Investments Ltd	
Bruton Investments Ltd	
Delphian Insurance Company Ltd*	Isle of Man
Fielden & Ashworth Ltd	
Guinea Investments Ltd	
Mayfair Place Investments Ltd	

	Country of incorporation or registration	Proportion of ownership interest %
b) Principal joint ventures and associates		
Building, civil and rail engineering		
Balfour Beatty Abu Dhabi LLC	Abu Dhabi	49.0
BK Gulf LLC	Dubai	49.0
Devonport Management Ltd*		24.5
Dutco Balfour Beatty LLC	Dubai	49.0
Dutco Construction Co LLC	Dubai	49.0
Gammon Asia Ltd	British Virgin Islands	50.0
Gammon China Ltd	Hong Kong	50.0
Gammon Construction Holdings Ltd	British Virgin Islands	50.0
Kerjaya Balfour Beatty Cementation Sdn Bhd	Malaysia	35.0
Monteray Ltd		24.5
PT Balfour Beatty Sakti Indonesia	Indonesia	49.0
Romec Ltd		49.0
Trans4m Ltd		25.0
Investments and developments		
PFI/PPP:		
Aberdeen Environmental Services (Holdings) Ltd	Scotland	45.0
Connect M1-A1 Holdings Ltd*		50.0
Connect M77/GSO Holdings Ltd (Note v)		85.0
Connect Roads Ltd* (Note v)		85.0
Consort Healthcare (Blackburn) Holdings Ltd		50.0
Consort Healthcare (Durham) Holdings Ltd*		50.0
Consort Healthcare (Edinburgh Royal Infirmary) Holdings Ltd* (Note v)	Scotland	73.9
EDF Energy Powerlink Ltd (Note vi)		10.0
Health Management (UCLH) Holdings Ltd		33.3
Metronet Rail BCV Holdings Ltd		20.0
Metronet Rail SSL Holdings Ltd		20.0
Power Asset Development Company Ltd		25.0
Transform Schools (Bassetlaw) Holdings Ltd		50.0
Transform Schools (North Lanarkshire) Holdings Ltd		50.0
Transform Schools (Rotherham) Holdings Ltd		50.0
Transform Schools (Stoke) Holdings Ltd		50.0
Other		
Thames Power Ltd* (Note iv)		50.0

c) Principal jointly controlled operations

The Group carries out a number of its larger construction contracts in joint arrangement with other contractors so as to share resources and risk. The principal construction projects in progress are given below:

Greenbush Light Rail	USA	50.0
I-15 Highway	USA	30.0
La Mesa Light Rail	USA	40.0
M1, Junctions 6A-10		50.0
SH130 Highway	USA	35.0
Steg/Raron	Switzerland	25.0
University College London Hospital		50.0

Notes:

(i) Subsidiaries, joint ventures and associates whose results did not, in the opinion of the Directors, materially affect the results or net assets of the Group are not shown.

(ii) *Indicates held directly by Balfour Beatty plc, except Consort Healthcare (Edinburgh Royal Infirmary) Holdings Ltd, 42.5% held directly by Balfour Beatty plc.

(iii) Unless otherwise stated, 100% of the equity capital is owned and companies are registered in England. The principal operations of each company are conducted in its country of incorporation.

(iv) Thames Power Ltd owns 51% of the equity capital in Barking Power Ltd.

(v) Due to the Connect Roads Ltd, Connect M77/GSO Holdings Ltd and Consort Healthcare (Edinburgh Royal Infirmary) Holdings Ltd shareholder agreements between Balfour Beatty and the other shareholders requiring unanimity of agreement in respect of significant matters related to the financial and operating policies of those companies, the Directors are of the opinion that, as at the balance sheet date, the Group did not control those companies and they have been accounted for as joint ventures.

(vi) The Group exercises significant influence through its participation in the management of EDF Energy Powerlink Ltd and therefore accounts for its interest as an associate.

36 Principal subsidiaries, joint ventures and associates continued

d) PFI/PPP concessions

Metronet

Summary: Balfour Beatty is a promoter, developer and 20% investor in Metronet Rail BCV Ltd and Metronet Rail SSL Ltd, which are modernising two thirds of the London Underground.

Project description: Metronet is upgrading, replacing and maintaining infrastructure and procuring the associated financing on the Bakerloo, Central, Victoria and Waterloo & City lines (Metronet Rail BCV Ltd) and the Metropolitan, District, Circle, Hammersmith and City and East London lines (Metronet Rail SSL Ltd).

Contractual arrangements: For each concession the principal contract is a 30 year project agreement with London Underground Ltd (LUL) with a review interval every 7½ years under which the concession company will maintain and upgrade the rolling stock, civil engineering infrastructure and stations and undertake routine maintenance, major overhauls and life cycle replacement on the underground lines for an inflation indexed periodic fee subject to performance related deductions and incentives. Operation of the trains and stations, ticketing and collection of fares remain the responsibility of LUL. The majority of the track renewal work has been subcontracted to Balfour Beatty Rail Projects. The majority of the civil engineering work and the refurbishment and modernisation of the stations has been subcontracted to Trans4m, a company owned 25% by Balfour Beatty. Replacement of the rolling stock has been subcontracted to another shareholder. All assets transfer to the client LUL at the end of the concession.

							Equity and subordinated debt	
Concession company	Project	Total debt and equity funding	Shareholding	Financial close	Duration years	Construction completion	Invested to 31 December 2005	Committed post 31 December 2005
Metronet Rail BCV Ltd	London Underground modernisation	£1,783m	20%	April 2003	30	2033	£14m	£21m
Metronet Rail SSL Ltd	London Underground modernisation	£2,108m	20%	April 2003	30	2033	£13m	£22m
							£27m	£43m

Roads

Summary: Balfour Beatty is a promoter, developer and investor in roads projects under Balfour Beatty's Connect brand, to construct new roads and upgrade and maintain existing roads and to replace and maintain street lighting.

Project descriptions: The roads projects comprise the design, construction, operation, maintenance and associated financing of the following roads: the M1-A1 link road; A30 Honiton to Exeter and A35 Tolpuddle to Puddletown bypass; A50 Stoke-Derby; the M77 from Fenwick to Malletsheugh and the Glasgow Southern Orbital. The street lighting projects are for the replacement and maintenance and associated financing over a 25 year period of the street lighting and highway signs in Sunderland and South Tyneside. All construction is new build rather than refurbishment.

Contractual arrangements: The principal contract in the roads concessions is the project agreement with the governmental highway authority setting out the obligations for the construction, operation and maintenance of the roads including life cycle replacement by Connect for the life of the concession to specified standards. In the case of the M1-A1, A30/A35 and A50 the inflation indexed payment is related to traffic volumes. In the case of the M77/GSO the inflation indexed payment is partly based on availability and partly on traffic volumes and subject to any performance related deductions. Construction of the roads was subcontracted to construction joint ventures in which Balfour Beatty had a 50% interest or, in the case of the M77/GSO, to Balfour Beatty Civil Engineering Ltd. On the street lighting projects payment is by a periodic inflation indexed availability payment subject to performance deductions and the replacement and maintenance obligations have been subcontracted to Balfour Beatty Power Networks Ltd. There are no provisions to reprice the contracts and all assets transfer to the client at the end of the concession.

							Equity and subordinated debt	
Concession	Project	Total debt and equity funding	Shareholding	Financial close	Duration years	Construction completion	Invested to 31 December 2005	Committed post 31 December 2005
Connect M1-A1 Ltd	M1-A1 30km road	£290m	50%	March 1996	30	1999	£14m	–
Connect A50 Ltd	A50 57km road	£42m	85%	May 1996	30	1998	£6m	–
Connect A30/A35 Ltd	A30/A35 102km road	£127m	85%	July 1996	30	2000	£20m	–
Connect M77/GSO plc	M77/GSO 25km road	£167m	85%	May 2003	32	2005	£16m	–
Connect Roads Sunderland Ltd	Street lighting apparatus in Sunderland	£27m	100%	August 2003	25	2008	–	£3m
Connect Roads South Tyneside Ltd	Street lighting apparatus in South Tyneside	£28m	100%	December 2005	25	2010	–	£2m
							£56m	£5m

Hospitals

Summary: Balfour Beatty is a promoter, developer and investor in four hospitals, three of which are under Balfour Beatty's Consort Healthcare brand, comprising the building or refurbishment of hospital accommodation and associated financing and the provision of certain non-medical facilities management services over the remainder of the concession period.

Project descriptions: The projects comprise University Hospital of North Durham, Edinburgh Royal Infirmary, Queens Park Hospital Blackburn and University College London Hospital. Construction is principally new build rather than refurbishment.

Contractual arrangements: The principal contract is the project agreement between the concession company and the NHS Trust. An inflation indexed payment is primarily based upon availability of the hospital subject to any performance related deductions. Construction of the hospitals has been subcontracted to construction joint ventures in which Balfour Beatty subsidiaries participated 100% (University Hospital of North Durham and Queens Park Hospital Blackburn), 85% (Edinburgh Royal Infirmary), and 50% (University College London Hospital). In the case of Edinburgh Royal Infirmary, University Hospital of North Durham and Queens Park Hospital Blackburn, facilities management has been subcontracted to a Balfour Beatty subsidiary, Haden Building Management Ltd. In the case of University College London Hospital, facilities management has been subcontracted to a subsidiary of another shareholder. The payments for the facilities management services are repriced every five years. All assets transfer to the client at the end of the concession, with the exception of Edinburgh Royal Infirmary, where the client has the option to terminate the arrangement for the provision of the hospital and services in 2028.

36 Principal subsidiaries, joint ventures and associates continued

Concession company	Project	Total debt and equity funding	Shareholding	Financial close	Duration years	Construction completion	Equity and subordinated debt: Invested to 31 December 2005	Equity and subordinated debt: Committed post 31 December 2005
Consort Healthcare (Durham) Ltd	District general hospital	£90m	50%	March 1998	30	2001	£7m	–
Consort Healthcare (Edinburgh Royal Infirmary) Ltd	Teaching hospital and medical school	£220m	73.9%	August 1998	30	2003	£40m	–
Consort Healthcare (Blackburn) Ltd	District general hospital	£116m	50%	July 2003	38	2006	£3m	£3m
Health Management (UCLH) Ltd	University College London teaching hospital	£282m	33.3%	July 2000	40	2008	£9m	–
							£59m	£3m

Schools

Summary: Balfour Beatty is a promoter, developer and investor in four grouped schools projects under Balfour Beatty's Transform Schools brand to design, build or refurbish schools and to provide certain non-educational services over the concession period.

Project descriptions: The projects comprise 98 schools in the city of Stoke-on-Trent, 15 schools in Rotherham, 21 schools in North Lanarkshire and six new schools, two post-16 learning centres and two leisure centres in Bassetlaw, Nottinghamshire. Construction in Bassetlaw and North Lanarkshire is all new build. On Stoke, construction comprises £16m of new build and £63m of refurbishment and on Rotherham, £78m of new build and £21m of refurbishment.

Contractual arrangements: The principal contract is the project agreement between the concession company and the local authority that provides for an inflation indexed availability based payment subject to any performance related deductions. Construction is subcontracted to a construction joint venture of Balfour Beatty subsidiaries and the facilities management services are subcontracted to a Balfour Beatty subsidiary, Haden Building Management Ltd. The payments for the facilities management services are repriced every five years. All assets transfer to the client at the end of the concession.

Concession company	Project	Total debt and equity funding	Shareholding	Financial close	Duration years	Construction completion	Equity and subordinated debt: Invested to 31 December 2005	Equity and subordinated debt: Committed post 31 December 2005
Transform Schools (Stoke) Ltd	Grouped schools project in Stoke-on-Trent	£74m	50%	October 2000	25	2005	–	£5m
Transform Schools (Rotherham) Ltd	Grouped schools project in Rotherham	£113m	50%	June 2003	31	2006	–	£5m
Transform Schools (North Lanarkshire) Ltd	Grouped schools project in North Lanarkshire	£140m	50%	June 2005	32	2008	–	£8m
Transform Schools (Bassetlaw) Ltd	Grouped schools project in Bassetlaw, Notts	£127m	50%	July 2005	27	2007	–	£8m
							–	£26m

Other concessions:

Summary: Balfour Beatty is a promoter, developer and investor in a number of other infrastructure concessions.

Project descriptions: Aberdeen Environmental Services Limited (AES) has a contract to design, build and finance wastewater treatment facilities in North Eastern Scotland and operate them for the remainder of a 30 year period. The construction is principally new build. The Powerlink project comprises two companies: EDF Energy Powerlink Ltd (EDFEPL), which operates the London Underground high voltage power system under a 30 year contract and is responsible for procuring various new power assets, and Power Asset Development Company Ltd (PADCO), which is constructing the new build power assets and leasing them to EDFEPL.

Contractual arrangements: For AES the principal agreement is the project agreement with Scottish Water under which AES receives inflation indexed payments on the basis of flows and loads of influent to the treatment works less any performance related deductions. AES subcontracted construction to a construction joint venture in which Balfour Beatty Civil Engineering Ltd had a 50% interest and subcontracted operations and maintenance to a subsidiary of one of the other shareholders. For the Powerlink project the principal project agreement is the power services contract between EDFEPL and LUL that provides for an inflation indexed availability payment subject to any performance deductions. EDFEPL operates and maintains the power network using its own staff and is leasing the new power assets from PADCO, which has subcontracted construction to a construction joint venture in which a Balfour Beatty group company, Balfour Kilpatrick Ltd, has a 40% interest. There are no provisions to reprice the contracts and all assets transfer to the client at the end of the concession.

Concession company	Project	Total debt and equity funding	Shareholding	Financial close	Duration years	Construction completion	Equity and subordinated debt: Invested to 31 December 2005	Equity and subordinated debt: Committed post 31 December 2005
Aberdeen Environmental Services Ltd	Wastewater treatment in North East Scotland	£92m	45%	May 2000	30	2002	£3m	–
EDF Energy Powerlink Ltd/Power Asset Development Company Ltd	London Underground power system	£184m	10%/25%	August 1998	30	2006	£4m	£3m
							£7m	£3m
Total of PFI/PPP concessions							£149m	£80m

37 Explanation of transition to IFRS

37.1 As described in Note 1, the 2005 financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). On 23 June 2005, the Company published restated consolidated financial information for 2004. Following completion of the required conversion work on all the Group's PFI/PPP concessions resulting from the adoption of IAS 32 and IAS 39 "Financial Instruments" and the draft interpretations on PFI/PPP concession accounting prospectively from 1 January 2005, the Company made further amendments to the restated 2004 financial information in relation to the accounting for five of its PFI/PPP concessions to conform with IFRIC 4. Revised reconciliations showing the changes between UK GAAP and IFRS disclosure format and the changes arising from the adoption of IFRS were placed on the Company's website (at www.balfourbeatty.com/bbeatty/ir/ifrs/) on 17 August 2005.

Reconciliations of the Group's profit and cash flow statement for the year ended 31 December 2004 and balance sheets as at 1 January 2004 and at 31 December 2004, showing the effects of changes in presentation and accounting policies arising from the adoption of IFRS on the figures published under UK GAAP on 9 March 2005, are set out on the following pages, with the principal changes described below.

37.2 Principal changes in presentation (reformat)

The financial statements prepared under UK GAAP have been reformatted in accordance with the requirements of IFRS as follows:

(i) Under IFRS, the post-tax results of discontinued operations include the profit on sale of those operations and are reported on a single line after "Profit for the year from continuing operations". Non-current assets and groups of assets to be disposed of and associated liabilities are separately classified if their carrying amount will be recovered through a sale transaction rather than through continuing use;

(ii) Interests in associates and joint venture entities are accounted for using the equity method under UK GAAP and IFRS. Under UK GAAP, the Group's share of their operating profits, interest and taxation were included under those respective captions in the income statement. Under IFRS, the Group's share of the post-tax profits of joint ventures and associates are disclosed in a single line within "Profit from operations";

(iii) Deferred tax assets, included within debtors under UK GAAP, are separately classified within "Non-current assets" under IFRS. Current and deferred tax liabilities, included within other creditors under UK GAAP, are separately classified within "Current liabilities" and "Non-current liabilities" under IFRS;

(iv) Debtors due after one year, included within current assets under UK GAAP, are reclassified within "Non-current assets" under IFRS; and

(v) Balances arising on long-term contracts are reclassified as "Due from customers for contract work" and "Due to customers for contract work" in accordance with the requirements of IAS 11 "Construction Contracts".

37.3 Principal changes in accounting policy (restatement):

The transition to IFRS has resulted in the following restatements as a result of changes in accounting policies:

(i) Under UK GAAP, goodwill was amortised on a straight-line basis over its economic useful life of up to 20 years, tested for impairment and provided for as necessary. Under IFRS, goodwill is no longer amortised but is carried at cost and subject to annual review for impairment at 31 December. This change increased "Profit from operations" for the year ended 31 December 2004 and "Net assets" at 31 December 2004 by £17m.

Under UK GAAP, the gain on disposal of businesses was determined after taking into account goodwill previously written-off to reserves. Such goodwill is not included in determining the profit on disposal under IFRS. This change increased "Profit for the year" for the year ended 31 December 2004 by £38m;

(ii) Under UK GAAP, the Group accounted for its defined benefit pension schemes in accordance with the requirements of SSAP 24 "Accounting for Pension Costs". The cost of providing the defined benefit pensions was charged against "Operating profit" with surpluses and deficits arising in the funds amortised to "Operating profit" over the remaining service lives of participating employees. Under IAS 19 "Employee Benefits", the cost of providing pension benefits (current service cost) for defined benefit pension schemes is recognised in the income statement and the defined benefit pension obligation is determined annually by independent actuaries and recognised on the balance sheet. The Group has elected to include within "Group operating profit" the interest cost arising on the projected obligations and the returns on the schemes' assets in addition to the current service cost. Actuarial gains and losses are recognised in the Statement of recognised income and expense in the period in which they occur. The effect of this change is to decrease "Profit from operations" for the year ended 31 December 2004 by £4m and "Net assets" at 31 December 2004 by £174m;

(iii) Under IFRS 2 "Share-based Payment", a charge is recognised in the Income statement for all share-based payments granted after 7 November 2002 but not vested, based on the fair values of the grants and the number expected to become exercisable. £3m of current and deferred tax credits recognised in the Income statement for the year ended 31 December 2004 are, under IAS 12 "Income Taxes", required to be credited directly to Equity. As a result "Profit for the year" is reduced through the revised recognition of these credits.

In the UK, the tax relief arising from share-based payments is not related to the expense recognised under IFRS 2. IAS 12 specifies how both the current tax relief and deferred tax arising on share-based payments should be assessed. Recognition of the deferred tax asset gives rise to an increase of £5m in "Net assets" at 31 December 2004;

(iv) Under UK GAAP, proposed dividends were recognised as a liability in the year to which they related. Under IAS 10 "Events after the Balance Sheet Date", dividends are not recognised as a liability until they are declared. As a result, "Net assets" at 31 December 2004 increase by £16m;

(v) IAS 12 requires the recognition of deferred tax on property revaluations and, subject to certain conditions, on the undistributed reserves of foreign subsidiaries, associates and joint ventures. Under UK GAAP such provisions were not required. The effect of this change is to reduce "Net assets" at 31 December 2004 by £4m; and

(vi) IFRIC 4 requires arrangements which convey the right to use assets in return for a payment or series of payments to be treated as a lease and accounted for in accordance with IAS 17 "Leases". This change in accounting for certain of the Group's PFI/PPP concessions results in an increase of £12m in "Profit before taxation" for the year ended 31 December 2004 and an increase of £29m in "Net assets" at 31 December 2004.

Reformat of Group income statement

For the year ended 31 December 2004

UK GAAP	UK GAAP as previously reported £m	Discontinued operations £m	Joint ventures' and associates' tax and interest £m	Exceptional items £m	Ordinary dividend to reserves £m	UK GAAP in IFRS format £m	UK GAAP in IFRS format
Turnover including share of joint ventures and associates	4,171	(51)	–	–	–	4,120	Revenue including share of joint ventures and associates
Share of turnover of joint ventures and associates	(672)	–	–	–	–	(672)	Share of revenue of joint ventures and associates
Group turnover	3,499	(51)	–	–	–	3,448	Group revenue
Cost of sales	(3,154)	26	–	(2)	–	(3,130)	Cost of sales
Gross profit	345	(25)	–	(2)	–	318	Gross profit
Net operating expenses	(271)	17	–	–	–	(254)	Net operating expenses
Group operating profit	74	(8)	–	(2)	–	64	Group operating profit
– before exceptional items	67	(8)	–	(2)	–	57	– before exceptional items
– exceptional items	7	–	–	–	–	7	– exceptional items
Share of operating profits of joint ventures and associates	71	–	(41)	–	–	30	Share of results of joint ventures and associates
Profit on sale of operations	135	(137)	–	2	–	–	
Provision for loss on sale of operations	2	–	–	(2)	–	–	
Loss on sale of tangible fixed assets	(2)	–	–	2	–	–	
Profit on ordinary activities before interest	280	(145)	(41)	–	–	94	Profit from operations
Interest receivable	23	–	–	–	–	23	Investment income
Interest payable	(23)	–	–	–	–	(23)	Finance costs
Share of joint ventures' and associates' net interest payable	(23)	–	23	–	–	–	
Profit on ordinary activities before taxation	257	(145)	(18)	–	–	94	Profit before taxation
Profit on ordinary activities before goodwill amortisation, exceptional items and taxation	150	(8)	(18)	(2)	–	122	Profit before goodwill amortisation and impairment, exceptional items and taxation
Goodwill amortisation and impairment	(35)	–	–	–	–	(35)	Goodwill amortisation and impairment
Exceptional items	142	(137)	–	2	–	7	Exceptional items
Tax on profit on ordinary activities	(54)	13	18	–	–	(23)	Taxation
Profit for the financial year	203	(132)	–	–	–	71	Profit for the year from continuing operations
	–	132	–	–	–	132	Profit for the year from discontinued operations
	203	–	–	–	–	203	Profit for the year
Dividends	(41)	–	–	–	28	(13)	Preference dividends
Premium paid on buy-back of preference shares	(6)	–	–	–	–	(6)	Premium paid on buy-back of preference shares
Transfer to reserves	156	–	–	–	28	184	Profit for the year attributable to equity shareholders

UK GAAP	UK GAAP as previously reported Pence	Discontinued operations Pence	Joint ventures' and associates' tax and interest Pence	Exceptional items Pence	Ordinary dividend to reserves Pence	UK GAAP in IFRS format Pence	UK GAAP in IFRS format
Basic earnings per ordinary share							Basic earnings per ordinary share
– continuing operations	–	12.4	–	–	–	12.4	– continuing operations
– discontinued operations	–	31.4	–	–	–	31.4	– discontinued operations
	43.8	–	–	–	–	43.8	

Restatement of Group income statement
For the year ended 31 December 2004

	UK GAAP in IFRS format £m	Goodwill amortisation £m	Goodwill in reserves £m	Discontinued operations £m	Retirement benefit obligations £m	Share-based payments £m	Impact of IFRIC 4 on PFI/PPP concessions £m	IFRS £m
Revenue including share of joint ventures and associates	4,120	–	–	–	–	–	119	4,239
Share of revenue of joint ventures and associates	(672)	–	–	–	–	–	(77)	(749)
Group revenue	3,448	–	–	–	–	–	42	3,490
Cost of sales	(3,130)	–	–	–	–	–	(62)	(3,192)
Gross profit	318	–	–	–	–	–	(20)	298
Net operating expenses	(254)	15	1	–	(4)	–	–	(242)
Group operating profit	64	15	1	–	(4)	–	(20)	56
– before exceptional items	57	33	–	–	(12)	–	(20)	58
– exceptional items	7	(18)	1	–	8	–	–	(2)
Share of results of joint ventures and associates	30	2	–	–	–	–	4	36
Profit from operations	94	17	1	–	(4)	–	(16)	92
Investment income	23	–	–	–	–	–	33	56
Finance costs	(23)	–	–	–	–	–	(5)	(28)
Profit before taxation	94	17	1	–	(4)	–	12	120
Profit before goodwill amortisation and impairment, exceptional items and taxation	122	–	–	–	(12)	–	12	122
Goodwill amortisation and impairment	(35)	17	–	–	–	–	–	(18)*
Exceptional items*	7	–	1	–	8	–	–	16*
Taxation	(23)	–	–	–	–	(3)	(2)	(28)
Profit for the year from continuing operations	71	17	1	–	(4)	(3)	10	92
Profit for the year from discontinued operations	132	–	37	(1)	–	–	–	168
Profit for the year	203	17	38	(1)	(4)	(3)	10	260
Preference dividends	(13)	–	–	–	–	–	–	(13)
Premium paid on buy-back of preference shares	(6)	–	–	–	–	–	–	(6)
Profit for the year attributable to equity shareholders	184	17	38	(1)	(4)	(3)	10	241

	UK GAAP in IFRS format Pence	Goodwill amortisation Pence	Goodwill in reserves Pence	Discontinued operations Pence	Retirement benefit obligations Pence	Share-based payments Pence	Impact of IFRIC 4 on PFI/PPP concessions Pence	IFRS Pence
Basic earnings per ordinary share								
– continuing operations	12.4	3.9	0.3	–	(0.7)	(0.9)	2.3	17.3
– discontinued operations	31.4	–	8.8	(0.1)	–	–	–	40.1
	43.8	3.9	9.1	(0.1)	(0.7)	(0.9)	2.3	57.4

Reformat of Group balance sheet

At 31 December 2004

UK GAAP	UK GAAP as previously reported £m	Taxation £m	Debtors £m	Contract balances £m	Other £m	UK GAAP in IFRS format £m	UK GAAP in IFRS format
Fixed assets							Non-current assets
Intangible assets – goodwill	265	–	–	–	–	265	Goodwill
Tangible assets							Property, plant and equipment
– PFI/PPP constructed assets	288	–	–	–	–	288	– PFI/PPP constructed assets
– other	149	–	–	–	–	149	– other
Investments in joint ventures	100	–	–	–	81	181	Investments in joint ventures and associates
Investments in associates	81	–	–	–	(81)	–	
Investments	42	–	–	–	–	42	Investments
	–	20	–	–	–	20	Deferred tax assets
	–	–	79	(4)	–	75	Trade and other receivables
	925	20	79	(4)	–	1,020	
Current assets							Current assets
Stocks	102	–	–	(52)	–	50	Inventories
	–	–	–	218	–	218	Due from customers for contract work
Debtors							
– due within one year	738	(18)	–	(156)	–	564	Trade and other receivables
– due after one year	79	–	(79)	–	–	–	
Cash and deposits							Cash and cash equivalents
– PFI/PPP subsidiaries	30	–	–	–	–	30	– PFI/PPP subsidiaries
– other	388	–	–	–	–	388	– other
	1,337	(18)	(79)	10	–	1,250	
	2,262	2	–	6	–	2,270	Total assets
Creditors: amounts falling due within one year							Current liabilities
Other creditors	(1,209)	38	–	209	–	(962)	Trade and other payables
	–	–	–	(264)	–	(264)	Due to customers for contract work
	–	(38)	–	–	–	(38)	Current tax liabilities
Borrowings							Borrowings
– PFI/PPP non-recourse term loans	(13)	–	–	–	–	(13)	– PFI/PPP non-recourse term loans
– other	(15)	–	–	–	–	(15)	– other
	(1,237)	–	–	(55)	–	(1,292)	
Creditors: amounts falling due after more than one year							Non-current liabilities
Borrowings							Borrowings
– PFI/PPP non-recourse term loans	(261)	–	–	–	–	(261)	– PFI/PPP non-recourse term loans
– other	(62)	–	–	–	–	(62)	– other
Other creditors	(110)	–	–	26	–	(84)	Trade and other payables
	–	(2)	–	–	–	(2)	Deferred tax liabilities
Provisions for liabilities and charges	(179)	–	–	23	–	(156)	Provisions
	(612)	(2)	–	49	–	(565)	
	(1,849)	(2)	–	(6)	–	(1,857)	Total liabilities
	413	–	–	–	–	413	Net assets
Capital and reserves							Capital and reserves
Called-up share capital	213	–	–	–	–	213	Called-up share capital
Share premium account	150	–	–	–	–	150	Share premium account
Special reserve	181	–	–	–	–	181	Special reserve
Revaluation reserves	70	–	–	–	(2)	68	Share of joint ventures' and associates' reserves
Other reserves	4	–	–	–	2	6	Other reserves
Profit and loss account	(205)	–	–	–	–	(205)	Accumulated losses
Shareholders' funds	413	–	–	–	–	413	Shareholders' funds

Restatement of Group balance sheet

At 31 December 2004

	UK GAAP in IFRS format £m	Goodwill £m	Retirement benefit obligations £m	Share-based payments £m	Proposed dividends £m	Deferred taxation £m	Impact of IFRIC 4 on PFI/PPP concessions £m	IFRS £m
Non-current assets								
Goodwill	265	15	–	–	–	–	(1)	279
Property, plant and equipment								
– PFI/PPP constructed assets	288	–	–	–	–	–	(288)	–
– other	149	–	–	–	–	–	–	149
Investments in joint ventures and associates	181	2	(16)	–	–	2	20	189
Investments	42	–	–	–	–	–	–	42
PFI/PPP financial assets	–	–	–	–	–	–	282	282
Deferred tax assets	20	–	67	5	–	(6)	1	87
Trade and other receivables	75	–	(26)	–	–	–	(8)	41
	1,020	17	25	5	–	(4)	6	1,069
Current assets								
Inventories	50	–	–	–	–	–	–	50
Due from customers for contract work	218	–	–	–	–	–	–	218
Trade and other receivables	564	–	(1)	–	–	–	–	563
Cash and cash equivalents								
– PFI/PPP subsidiaries	30	–	–	–	–	–	–	30
– other	388	–	–	–	–	–	–	388
	1,250	–	(1)	–	–	–	–	1,249
Total assets	2,270	17	24	5	–	(4)	6	2,318
Current liabilities								
Trade and other payables	(962)	–	–	–	16	–	–	(946)
Due to customers for contract work	(264)	–	–	–	–	–	–	(264)
Current tax liabilities	(38)	–	–	–	–	–	–	(38)
Borrowings								
– PFI/PPP non-recourse term loans	(13)	–	–	–	–	–	–	(13)
– other	(15)	–	–	–	–	–	–	(15)
	(1,292)	–	–	–	16	–	–	(1,276)
Non-current liabilities								
Borrowings								
– PFI/PPP non-recourse term loans	(261)	–	–	–	–	–	–	(261)
– other	(62)	–	–	–	–	–	–	(62)
Trade and other payables	(84)	–	3	–	–	–	23	(58)
Deferred tax liabilities	(2)	–	–	–	–	–	–	(2)
Retirement benefit obligations	–	–	(254)	–	–	–	–	(254)
Provisions	(156)	–	53	–	–	–	–	(103)
	(565)	–	(198)	–	–	–	23	(740)
Total liabilities	(1,857)	–	(198)	–	16	–	23	(2,016)
Net assets	413	17	(174)	5	16	(4)	29	302
Capital and reserves								
Called-up share capital	213	–	–	–	–	–	–	213
Share premium account	150	–	–	–	–	–	–	150
Special reserve	181	–	–	–	–	–	–	181
Share of joint ventures' and associates' reserves	68	–	(16)	–	–	–	20	72
Other reserves	6	–	–	4	–	(1)	–	9
Accumulated losses	(205)	17	(158)	1	16	(3)	9	(323)
Shareholders' funds	413	17	(174)	5	16	(4)	29	302

Reformat of Group cash flow statement

For the year ended 31 December 2004

UK GAAP	UK GAAP as previously reported £m	Discontinued operations £m	Joint ventures' and associates' results £m	Exceptional items £m	Cash equivalents £m	Operating £m	Investing £m	Financing £m	UK GAAP in IFRS format £m	UK GAAP under IFRS
Group operating profit before exceptional items	67	(8)	30	5	–	–	–	–	94	Profit from continuing operations
	–	8	–	–	–	–	–	–	8	Trading profit from discontinued operations
	–	–	(30)	–	–	–	–	–	(30)	Share of results of joint ventures and associates
Depreciation	50	–	–	–	–	–	–	–	50	Depreciation of property, plant and equipment
Goodwill amortisation	33	–	–	–	–	–	–	–	33	Goodwill amortisation and impairment
Charge relating to Performance Share Plan	2	–	–	–	–	–	–	–	2	Movements relating to share-based payments
(Profit)/loss on sale of tangible fixed assets	(1)	–	–	2	–	–	–	–	1	Loss on disposal of property, plant and equipment
Exceptional items – cash expenditure	(6)	–	–	6	–	–	–	–	–	
Working capital decrease	26	–	–	(13)	–	–	–	–	13	Working capital decrease
	171	–	–	–	–	–	–	–	171	Cash generated from operations
	–	–	–	–	–	(41)	–	–	(41)	Income taxes paid
Net cash inflow from operating activities	171	–	–	–	–	(41)	–	–	130	Net cash from operating activities
Dividends from joint ventures and associates	8	–	–	–	–	–	(8)	–	–	
Returns on investments and servicing of finance	(21)	–	–	–	–	–	–	21	–	
Taxation	(41)	–	–	–	–	41	–	–	–	
Capital expenditure and financial investment	(57)	–	–	–	–	–	57	–	–	
Acquisitions and disposals	161	–	–	–	39	–	(200)	–	–	
Ordinary dividends paid	(25)	–	–	–	–	–	–	25	–	
	–	–	–	–	–	–	151	–	151	Net cash from investing activities
Management of liquid resources	(206)	–	–	–	206	–	–	–	–	
Financing	(26)	–	–	–	–	–	–	26	–	
	–	–	–	–	–	–	–	(72)	(72)	Net cash used in financing activities
Decrease in cash in the period	(36)	–	–	–	245	–	–	–	209	Net increase in cash and cash equivalents

Restatement of Group cash flow statement

For the year ended 31 December 2004

	UK GAAP in IFRS format £m	Goodwill amortisation £m	Goodwill in reserves £m	Retirement benefit obligations £m	Impact of IFRIC 4 on PFI/PPP concessions £m	IFRS £m
Profit from continuing operations	94	17	1	(4)	(16)	92
Trading profit from discontinued operations	8	–	–	–	–	8
Share of results of joint ventures and associates	(30)	(2)	–	–	(4)	(36)
Depreciation of property, plant and equipment	50	–	–	–	(9)	41
Goodwill amortisation and impairment	33	(15)	–	–	–	18
Movements relating to share-based payments	2	–	–	–	–	2
Loss on disposal of property, plant and equipment	1	–	–	–	–	1
Profit on disposal of businesses	–	–	(1)	–	–	(1)
Working capital decrease	13	–	–	4	6	23
Cash generated from operations	171	–	–	–	(23)	148
Income taxes paid	(41)	–	–	–	–	(41)
Net cash from operating activities	130	–	–	–	(23)	107
Net cash from investing activities	151	–	–	–	(6)	145
Net cash used in financing activities	(72)	–	–	–	29	(43)
Net increase in cash and cash equivalents	209	–	–	–	–	209

Reformat of Group balance sheet

At 1 January 2004

UK GAAP	UK GAAP as previously reported £m	Discontinued operations £m	Taxation £m	Debtors £m	Contract balances £m	Other £m	UK GAAP in IFRS format £m	UK GAAP in IFRS format
Fixed assets								Non-current assets
Intangible assets – goodwill	306	–	–	–	–	–	306	Goodwill
Tangible assets	158	–	–	–	–	–	158	Property, plant and equipment
Investments in joint ventures	89	(2)	–	–	–	47	134	Investments in joint ventures and associates
Investments in associates	47	–	–	–	–	(47)	–	
Investments	36	–	–	–	–	–	36	Investments
	–	–	38	–	–	–	38	Deferred tax assets
	–	–	–	60	–	–	60	Trade and other receivables
	636	(2)	38	60	–	–	732	
Current assets								Current assets
Stocks	109	–	–	–	(54)	–	55	Inventories
	–	–	–	–	198	–	198	Due from customers for contract work
Debtors								
– due within one year	759	–	(36)	–	(151)	–	572	Trade and other receivables
– due after one year	60	–	–	(60)	–	–	–	
Cash and deposits	202	–	–	–	–	–	202	Cash and cash equivalents
	1,130	–	(36)	(60)	(7)	–	1,027	
	–	2	–	–	–	–	2	Non-current assets classified as held for sale
	1,766	–	2	–	(7)	–	1,761	Total assets
Creditors: amounts falling due within one year								Current liabilities
Other creditors	(1,195)	–	43	–	196	–	(956)	Trade and other payables
	–	–	–	–	(226)	–	(226)	Due to customers for contract work
	–	–	(43)	–	–	–	(43)	Current tax liabilities
Borrowings	(7)	–	–	–	–	–	(7)	Borrowings
	(1,202)	–	–	–	(30)	–	(1,232)	
Creditors: amounts falling due after more than one year								Non-current liabilities
Borrowings								Borrowings
– PFI/PPP non-recourse term loans	(3)	–	–	–	–	–	(3)	– PFI/PPP non-recourse term loans
– other	(68)	–	–	–	–	–	(68)	– other
Other creditors	(95)	–	–	–	26	–	(69)	Trade and other payables
	–	–	(2)	–	–	–	(2)	Deferred tax liabilities
Provisions for liabilities and charges	(167)	–	–	–	11	–	(156)	Provisions
	(333)	–	(2)	–	37	–	(298)	
	(1,535)	–	(2)	–	7	–	(1,530)	Total liabilities
	231	–	–	–	–	–	231	Net assets
Capital and reserves								Capital and reserves
Called-up share capital	212	–	–	–	–	–	212	Called-up share capital
Share premium account	328	–	–	–	–	–	328	Share premium account
Revaluation reserves	48	–	–	–	–	(2)	46	Share of joint ventures' and associates' reserves
Other reserves	8	–	–	–	–	2	10	Other reserves
Profit and loss account	(365)	–	–	–	–	–	(365)	Accumulated losses
Shareholders' funds	231	–	–	–	–	–	231	Shareholders' funds

Restatement of Group balance sheet

At 1 January 2004

	UK GAAP in IFRS format £m	Goodwill £m	Retirement benefit obligations £m	Share-based payments £m	Proposed dividends £m	Deferred taxation £m	Impact of IFRIC 4 on PFI/PPP concessions £m	IFRS £m
Non-current assets								
Goodwill	306	2	–	–	–	–	–	308
Property, plant and equipment	158	(2)	–	–	–	–	–	156
Investments in joint ventures and associates	134	–	(11)	–	–	–	19	142
Investments	36	–	–	–	–	–	–	36
PFI/PPP financial assets	–	–	–	–	–	–	3	3
Deferred tax assets	38	2	63	4	–	(4)	–	103
Trade and other receivables	60	–	(19)	–	–	–	(3)	38
	732	2	33	4	–	(4)	19	786
Current assets								
Inventories	55	–	–	–	–	–	–	55
Due from customers for contract work	198	–	–	–	–	–	–	198
Trade and other receivables	572	2	(4)	–	–	–	–	570
Cash and cash equivalents	202	–	–	–	–	–	–	202
	1,027	2	(4)	–	–	–	–	1,025
Non-current assets classified as held for sale	2	–	–	–	–	–	–	2
Total assets	1,761	4	29	4	–	(4)	19	1,813
Current liabilities								
Trade and other payables	(956)	–	–	–	14	–	–	(942)
Due to customers for contract work	(226)	–	–	–	–	–	–	(226)
Current tax liabilities	(43)	–	–	–	–	–	–	(43)
Borrowings	(7)	–	–	–	–	–	–	(7)
	(1,232)	–	–	–	14	–	–	(1,218)
Non-current liabilities								
Borrowings								
– PFI/PPP non-recourse term loans	(3)	–	–	–	–	–	–	(3)
– other	(68)	–	–	–	–	–	–	(68)
Trade and other payables	(69)	–	4	–	–	–	–	(65)
Retirement benefit obligations	–	–	(247)	–	–	–	–	(247)
Deferred tax liabilities	(2)	–	–	–	–	–	–	(2)
Provisions	(156)	(4)	56	–	–	–	–	(104)
	(298)	(4)	(187)	–	–	–	–	(489)
Total liabilities	(1,530)	(4)	(187)	–	14	–	–	(1,707)
Net assets	231	–	(158)	4	14	(4)	19	106
Capital and reserves								
Called-up share capital	212	–	–	–	–	–	–	212
Share premium account	328	–	–	–	–	–	–	328
Share of joint ventures' and associates' reserves	46	–	(11)	–	–	–	19	54
Other reserves	10	–	–	–	–	(1)	–	9
Accumulated losses	(365)	–	(147)	4	14	(3)	–	(497)
Shareholders' funds	231	–	(158)	4	14	(4)	19	106

Reformat and restatement of Company income statement
For the year ended 31 December 2004

UK GAAP	UK GAAP as previously reported £m	Ordinary dividend to reserves £m	Dividends £m	UK GAAP in IFRS format £m	Retirement benefit obligations £m	Share-based payments £m	Proposed dividends £m	IFRS £m	IFRS
Turnover	–	–	23	23	–	–	30	53	Revenue
Net operating expenses	(9)	–	–	(9)	(1)	–	–	(10)	Net operating expenses
Operating profit	(9)	–	23	14	(1)	–	30	43	Profit from operations
Dividend income	23	–	(23)	–	–	–	–	–	
Interest receivable	28	–	–	28	–	–	–	28	Investment income
Interest payable	(25)	–	–	(25)	–	–	–	(25)	Finance costs
Profit on ordinary activities before taxation	17	–	–	17	(1)	–	30	46	Profit before taxation
Tax on profit on ordinary activities	19	–	–	19	–	(3)	–	16	Taxation
Profit for the financial year	36	–	–	36	(1)	(3)	30	62	Profit for the year
Dividends	(41)	28	–	(13)	–	–	–	(13)	Preference dividends
Premium paid on buy-back of preference shares	(6)	–	–	(6)	–	–	–	(6)	Premium paid on buy-back of preference shares
Transfer to reserves	(11)	28	–	17	(1)	(3)	30	43	Profit for the year attributable to equity shareholders

Reformat and restatement of Company balance sheet
At 31 December 2004

UK GAAP	UK GAAP as previously reported £m	Investments £m	Taxation £m	Debtors £m	UK GAAP in IFRS format £m	Retirement benefit obligations £m	Share-based payments £m	Proposed dividends £m	IFRS £m	IFRS
Fixed assets										Non-current assets
Tangible assets	1	–	–	–	1	–	–	–	1	Property, plant and equipment
Investments	534	338	–	–	872	–	–	–	872	Investments
	–	–	1	–	1	4	5	–	10	Deferred tax assets
	–	–	–	33	33	–	–	–	33	Trade and other receivables
	535	338	1	33	907	4	5	–	916	
Current assets										Current assets
Stocks	1	–	–	–	1	–	–	–	1	Inventories
Debtors										
– due within one year	48	326	(1)	–	373	(4)	–	–	369	Trade and other receivables
– due after one year	9	24	–	(33)	–	–	–	–	–	
Cash and deposits	259	–	–	–	259	–	–	–	259	Cash and cash equivalents
	317	350	(1)	(33)	633	(4)	–	–	629	
	852	688	–	–	1,540	–	5	–	1,545	Total assets
Creditors: amounts falling due within one year										Current liabilities
Other creditors	(75)	(688)	8	–	(755)	–	–	16	(739)	Trade and other payables
	–	–	(8)	–	(8)	–	–	–	(8)	Current tax liabilities
Borrowings	(4)	–	–	–	(4)	–	–	–	(4)	Borrowings
	(79)	(688)	–	–	(767)	–	–	16	(751)	
Creditors: amounts falling due after more than one year										Non-current liabilities
Borrowings	(62)	–	–	–	(62)	–	–	–	(62)	Borrowings
Other creditors	(25)	–	–	–	(25)	–	–	–	(25)	Trade and other payables
	–	–	–	–	–	(6)	–	–	(6)	Retirement benefit obligations
Provisions for liabilities and charges	(9)	–	–	–	(9)	–	–	–	(9)	Provisions
	(96)	–	–	–	(96)	(6)	–	–	(102)	
	(175)	(688)	–	–	(863)	(6)	–	16	(853)	Total liabilities
	677	–	–	–	677	(6)	5	16	692	Net assets
Capital and reserves										Capital and reserves
Called-up share capital	213	–	–	–	213	–	–	–	213	Called-up share capital
Share premium account	150	–	–	–	150	–	–	–	150	Share premium account
Special reserve	181	–	–	–	181	–	–	–	181	Special reserve
Other reserves	46	–	–	–	46	–	4	–	50	Other reserves
Profit and loss account	87	–	–	–	87	(6)	1	16	98	Accumulated profits
Shareholders' funds	677	–	–	–	677	(6)	5	16	692	Shareholders' funds

Reformat and restatement of Company cash flow statement

For the year ended 31 December 2004

UK GAAP	UK GAAP as previously reported £m	Cash equivalents £m	Operating £m	Investing £m	Financing £m	UK GAAP in IFRS format £m	Retirement benefit obligations £m	Proposed dividends £m	IFRS £m	IFRS
Operating profit before exceptional items	(9)	–	–	23	–	14	(1)	30	43	Profit from continuing operations
	–	–	–	(23)	–	(23)	–	(30)	(53)	Dividends received
Charge relating to Performance Share Plan	2	–	–	–	–	2	–	–	2	Movements relating to share-based payments
Working capital increase	(9)	–	–	–	–	(9)	1	–	(8)	Working capital increase
	(16)	–	–	–	–	(16)	–	–	(16)	Cash generated from operations
	–	–	13	–	–	13	–	–	13	Income taxes received
Net cash inflow from operating activities	(16)	–	13	–	–	(3)	–	–	(3)	Net cash from operating activities
Dividends from joint ventures, associates and subsidiaries	53	–	–	(53)	–	–	–	–	–	
Returns on investments and servicing of finance	(14)	–	–	–	14	–	–	–	–	
Taxation	13	–	(13)	–	–	–	–	–	–	
Capital expenditure and financial investment	242	–	–	(242)	–	–	–	–	–	
Ordinary dividends paid	(25)	–	–	–	25	–	–	–	–	
	–	–	–	295	–	295	–	–	295	Net cash from investing activities
Management of liquid resources	(222)	222	–	–	–	–	–	–	–	
Cash outflow from financing activities	(18)	–	–	–	18	–	–	–	–	
	–	–	–	–	(57)	(57)	–	–	(57)	Net cash used in financing activities
Increase in cash in the period	13	222	–	–	–	235	–	–	235	Net increase in cash and cash equivalents

Reformat and restatement of Company balance sheet

At 1 January 2004

UK GAAP	UK GAAP as previously reported £m	Investments £m	Taxation £m	Debtors £m	UK GAAP in IFRS format £m	Retirement benefit obligations £m	Share-based payments £m	Deferred taxation £m	Proposed dividends £m	IFRS £m	IFRS
Fixed assets											Non-current assets
Tangible assets	1	–	–	–	1	–	–	–	–	1	Property, plant and equipment
Investments	775	168	–	–	943	–	–	–	–	943	Investments
	–	–	5	–	5	3	–	4	–	12	Deferred tax assets
	–	–	–	46	46	(2)	–	–	–	44	Trade and other receivables
	776	168	5	46	995	1	–	4	–	1,000	
Current assets											Current assets
Stocks	1	–	–	–	1	–	–	–	–	1	Inventories
Debtors											
– due within one year	56	433	(5)	–	484	1	–	–	(30)	455	Trade and other receivables
– due after one year	14	32	–	(46)	–	–	–	–	–	–	
Cash and deposits	37	–	–	–	37	–	–	–	–	37	Cash and cash equivalents
	108	465	(5)	(46)	522	1	–	–	(30)	493	
	884	633	–	–	1,517	2	–	4	(30)	1,493	Total assets
Creditors: amounts falling due within one year											Current liabilities
Other creditors	(61)	(633)	6	–	(688)	–	–	–	14	(674)	Trade and other payables
	–	–	(6)	–	(6)	–	–	–	–	(6)	Current tax liabilities
Borrowings	(14)	–	–	–	(14)	–	–	–	–	(14)	Borrowings
	(75)	(633)	–	–	(708)	–	–	–	14	(694)	
Creditors: amounts falling due after more than one year											Non-current liabilities
Borrowings	(66)	–	–	–	(66)	–	–	–	–	(66)	Borrowings
Other creditors	(35)	–	–	–	(35)	–	–	–	–	(35)	Trade and other payables
	–	–	–	–	–	(6)	–	–	–	(6)	Retirement benefit obligations
Provisions for liabilities and charges	(11)	–	–	–	(11)	–	–	–	–	(11)	Provisions
	(112)	–	–	–	(112)	(6)	–	–	–	(118)	
	(187)	(633)	–	–	(820)	(6)	–	–	14	(812)	Total liabilities
	697	–	–	–	697	(4)	–	4	(16)	681	Net assets
Capital and reserves											Capital and reserves
Called-up share capital	212	–	–	–	212	–	–	–	–	212	Called-up share capital
Share premium account	328	–	–	–	328	–	–	–	–	328	Share premium account
Other reserves	50	–	–	–	50	–	(4)	4	–	50	Other reserves
Profit and loss account	107	–	–	–	107	(4)	4	–	(16)	91	Accumulated profits
Shareholders' funds	697	–	–	–	697	(4)	–	4	(16)	681	Shareholders' funds

Pro forma financial statements

For the year ended 31 December 2005 based on unaudited figures

As permitted by IFRS 1 "First-time Adoption of IFRS", the Group has elected to adopt IAS 32 and IAS 39 "Financial Instruments" prospectively from 1 January 2005, and comparative figures have not been restated. These standards have a significant impact on the Group and particularly affect the accounting for the Company's convertible redeemable preference shares, the hedging activities of the Group and those of the PFI/PPP concessions, and the assets and income of the PFI/PPP concessions.

Pro forma IFRS financial statements, which include the impact of IAS 32 and IAS 39 as if the Group had adopted them for the year ended 31 December 2004, are included below with the IFRS financial statements for 2005. These pro forma statements assume the full adoption of IAS 32 and IAS 39, and the application of hedge accounting where management believes it is appropriate to assume the relevant accounting criteria regarding documentation and effectiveness could have been met. The changes which the adoption of IAS 39 and the IFRIC draft interpretations in respect of PFI/PPP concessions would have made on the restated IFRS profit for the year and net assets if these standards had been adopted for the year ended 31 December 2004 are summarised below.

			2004
	Profit before taxation* £m	Profit for the year £m	Net assets £m
IFRS restated	122	260	302
Preference shares			
– dividend restated as a finance cost	(13)	(13)	–
– additional accrued interest	(1)	(1)	–
– premium on buy-back restated as a finance cost	–	(6)	–
– liability element and deferred tax	–	–	(113)
Derivatives			
– Group interest rate swaps	(1)	(1)	(3)
– Group PFI/PPP concessions	–	–	(6)
– Joint venture and associate PFI/PPP concessions	–	–	(35)
PFI/PPP financial assets			
– Group PFI/PPP concessions	–	–	26
– Joint venture and associate PFI/PPP concessions	–	–	49
Goodwill adjustment arising from concession share purchase	–	7	7
Pro forma IFRS	107	246	227

*Before exceptional items.

Pro forma Group income statement

For the year ended 31 December 2005 based on unaudited figures

			2005	Pro forma IFRS including IAS 32 and IAS 39		2004
	Before exceptional items £m	**Exceptional items £m**	**Total £m**	Before exceptional items £m	Exceptional items £m	Total £m
Revenue including share of joint ventures and associates	**4,938**	**–**	**4,938**	4,239	–	4,239
Share of revenue of joint ventures and associates	**(1,101)**	**–**	**(1,101)**	(749)	–	(749)
Group revenue	**3,837**	**–**	**3,837**	3,490	–	3,490
Group operating profit	**72**	**(14)**	**58**	58	5	63
Share of results of joint ventures and associates	**43**	**30**	**73**	36	–	36
Profit from operations	**115**	**16**	**131**	94	5	99
Investment income	**56**	**–**	**56**	56	–	56
Finance costs	**(37)**	**(9)**	**(46)**	(43)	(6)	(49)
Profit before taxation	**134**	**7**	**141**	107	(1)	106
Taxation	**(32)**	**(3)**	**(35)**	(23)	(5)	(28)
Profit for the year from continuing operations	**102**	**4**	**106**	84	(6)	78
Profit for the year from discontinued operations	**–**	**–**	**–**	8	160	168
Profit for the year attributable to equity shareholders	**102**	**4**	**106**	92	154	246

	2005 Pence	2004 Pence
Basic earnings per ordinary share		
– continuing operations	**24.9**	18.6
– discontinued operations	**–**	40.1
	24.9	58.7
Exceptional items	**(0.8)**	(36.6)
Adjusted earnings per share	**24.1**	22.1

Pro forma Group balance sheet

At 31 December 2005 based on unaudited figures

	2005 £m	Pro forma IFRS including IAS 32 and IAS 39 2004 £m
Non-current assets		
Goodwill	**284**	274
Property, plant and equipment	**167**	149
Investments in joint ventures and associates	**375**	204
Investments	**38**	42
PFI/PPP financial assets	**14**	340
Deferred tax assets	**83**	64
Derivative financial instruments	**2**	–
Trade and other receivables	**35**	41
	998	1,114
Current assets		
Inventories	**61**	50
Due from customers for contract work	**217**	218
Derivative financial instruments	**–**	1
Trade and other receivables	**619**	562
Cash and cash equivalents		
– PFI/PPP subsidiaries	**–**	30
– other	**345**	388
	1,242	1,249
Total assets	**2,240**	2,363
Current liabilities		
Trade and other payables	**(1,038)**	(946)
Due to customers for contract work	**(274)**	(264)
Derivative financial instruments		
– PFI/PPP subsidiaries	**–**	(13)
– other	**(4)**	(4)
Current tax liabilities	**(30)**	(38)
Borrowings		
– PFI/PPP non-recourse term loans	**–**	(13)
– other	**(30)**	(15)
	(1,376)	(1,293)
Non-current liabilities		
Borrowings		
– PFI/PPP non-recourse term loans	**(14)**	(261)
– other	**–**	(62)
Liability component of preference shares	**(98)**	(103)
Derivative financial instruments	**(2)**	–
Trade and other payables	**(66)**	(58)
Deferred tax liabilities	**(3)**	(2)
Retirement benefit obligations	**(280)**	(254)
Provisions	**(109)**	(103)
	(572)	(843)
Total liabilities	**(1,948)**	(2,136)
Net assets	**292**	227
Capital and reserves		
Called-up share capital	**214**	212
Share premium account	**26**	15
Equity component of preference shares	**18**	19
Special reserve	**175**	181
Share of joint ventures' and associates' reserves	**182**	86
Other reserves	**5**	40
Accumulated losses	**(328)**	(326)
Equity	**292**	227

Pro forma segmental analysis

For the year ended 31 December 2005 based on unaudited figures

Performance by activity:	Building, building management and services £m	Civil and specialist engineering and services £m	Rail engineering and services £m	Investments and developments £m	Corporate costs £m	Total £m
Group revenue	**1,674**	**1,366**	**763**	**34**	**–**	**3,837**
Group operating profit	**32**	**39**	**32**	**(10)**	**(21)**	**72**
Share of results of joint ventures and associates	**3**	**10**	**–**	**30**	**–**	**43**
Profit from operations before exceptional items	**35**	**49**	**32**	**20**	**(21)**	**115**
Exceptional items	**(8)**	**–**	**(12)**	**36**	**–**	**16**
Profit from operations	**27**	**49**	**20**	**56**	**(21)**	**131**
Investment income						**56**
Finance costs						**(46)**
Profit before taxation						**141**

Performance by geographic origin:

	Europe £m	North America £m	Other £m	Total £m
Group revenue	**3,332**	**483**	**22**	**3,837**
Profit from operations before exceptional items	**134**	**(20)**	**1**	**115**
Exceptional items	**28**	**(12)**	**–**	**16**
Profit from operations	**162**	**(32)**	**1**	**131**

For the year ended 31 December 2004 based on unaudited figures

Performance by activity:	Building, building management and services £m	Civil and specialist engineering and services £m	Rail engineering and services £m	Investments and developments £m	Corporate costs £m	Total £m
Group revenue	1,468	1,144	800	78	–	3,490
Group operating profit	32	7	45	(9)	(17)	58
Share of results of joint ventures and associates	2	9	(1)	26	–	36
Profit from operations before exceptional items	34	16	44	17	(17)	94
Exceptional items	–	1	(3)	7	–	5
Profit from operations	34	17	41	24	(17)	99
Investment income						56
Finance costs						(49)
Profit before taxation						106

Performance by geographic origin:

	Europe £m	North America £m	Other £m	Total £m
Group revenue	3,107	377	6	3,490
Profit from operations before exceptional items	137	(45)	2	94
Exceptional items	22	(18)	1	5
Profit from operations	159	(63)	3	99

Group five-year summary

IFRS	2005 £m	2004 pro forma £m	2004 £m
Income			
Revenue (including share of joint ventures and associates)	**4,938**	4,239	4,239
Profit from continuing operations before exceptional items	**115**	94	94
Exceptional items	**16**	5	(2)
Profit from continuing operations	**131**	99	92
Net investment income	**10**	7	28
Profit from continuing operations before taxation	**141**	106	120
Profit from discontinued operations before taxation	**–**	180	180
	141	286	300
Capital employed			
Equity/shareholders' funds	**292**	227	302
Liability component of preference shares	**98**	103	–
Net cash	**(301)**	(67)	(67)
	89	263	235
Statistics			
Adjusted earnings per ordinary share*	**24.1p**	22.1p	22.5p
Basic earnings per ordinary share	**24.9p**	58.7p	57.4p
Diluted earnings per ordinary share	**24.7p**	58.1p	56.9p
Proposed dividends per ordinary share	**8.1p**	6.6p	6.6p
Profit from continuing operations before exceptional items: revenue	**2.3%**	2.2%	2.2%

Notes
Figures for the two years ended 31 December 2005 shown above were prepared under International Financial Reporting Standards (IFRS) with pro forma figures shown for the year ended 31 December 2004 which include the impact of IAS 32 and IAS 39 as if the Group had adopted them for that year as explained on page 108.
*Adjusted earnings per ordinary share before exceptional items and appropriations arising on the buy-back of preference shares and including the results of discontinued operations have been disclosed to give a clearer understanding of the Group's underlying trading performance.

UK GAAP	2004 £m	2003 as restated £m	2002 as restated £m	2001 as restated £m
Profits				
Turnover (including share of joint ventures and associates)	4,171	3,678	3,441	3,071
Operating profit – before goodwill amortisation and exceptional items	173	161	149	136
Goodwill amortisation and impairment	(35)	(17)	(21)	(12)
Exceptional items	142	5	(9)	13
Profit on ordinary activities before interest	280	149	119	137
Net interest payable	(23)	(31)	(31)	(34)
Profit before taxation	257	118	88	103
Capital employed				
Shareholders' funds	413	231	192	185
Net cash	(67)	(124)	(67)	(63)
	346	107	125	122
Statistics				
Adjusted earnings per ordinary share**	23.4p	20.6p	16.1p	14.1p
Basic earnings per ordinary share	43.8p	16.9p	8.5p	13.8p
Diluted earnings per ordinary share	43.4p	16.7p	8.4p	13.6p
Proposed dividends per ordinary share	6.6p	6.0p	5.4p	5.0p
Operating profit before goodwill amortisation and exceptional items: turnover	4.2%	4.4%	4.3%	4.4%

Notes
Figures for the four years ended 31 December 2004 shown above were prepared under UK generally accepted accounting principles (UK GAAP) as applied in the Company's annual report and accounts 2004. An explanation of the transition from UK GAAP to IFRS and reconciliations showing the effects of changes in presentation and accounting policies arising from the adoption of IFRS are set out in Note 37.
**Adjusted earnings per ordinary share before goodwill amortisation, exceptional items and appropriations arising on the buy-back of preference shares have been disclosed to give a clearer understanding of the Group's underlying trading performance.

Shareholder information

Financial calendar

	2006
26 April	Ex-dividend date for final 2005 ordinary dividend
28 April	Final 2005 ordinary dividend record date
11 May	Annual General Meeting
24 May	Ex-dividend date for July 2006 preference dividend
26 May	July 2006 preference dividend record date
12 June	Final date for receipt of DRIP mandate forms (see below)
1 July	Preference dividend payable
3 July*	Final 2005 ordinary dividend payable
16 August*	Announcement of 2006 half-year results
	2007
1 January	Preference dividend payable
2 January*	Interim 2006 ordinary dividend payable

*Provisional dates.

Registrar and transfer office

All administrative enquiries relating to shareholdings should, in the first instance, be directed to the Company's Registrars and clearly state the shareholder's registered name and address and, if available, the full shareholder reference number. Please write to:

The Balfour Beatty plc Registrar
Computershare Investor Services PLC
PO Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH
Telephone 0870 702 0122 or by e-mail to: web.queries@computershare.co.uk
or visit www.computershare.com

They can help you to:
- check your shareholding;
- register a change of address or name;
- obtain a replacement dividend cheque or tax voucher;
- record the death of a shareholder;
- amalgamate multiple accounts;
- resolve any other question about your shareholding.

Dividend mandates

If you wish dividends to be paid directly into your bank or building society account, you should contact the Registrars for a dividend mandate form.

Dividends paid in this way will be paid through the Bankers Automated Clearing System (BACS).

Information about Balfour Beatty's Dividend Reinvestment Plan ("DRIP") can also be obtained from the Registrars.

Subject to shareholder approval, the final dividend for 2005 will be paid on 3 July 2006. If you have already elected to join the DRIP, then you need take no further action. If you wish to join the DRIP, then you should complete a mandate form and return it to the Registrars by no later than 12 June 2006 in order to participate in the DRIP for this dividend. If you do not have a DRIP mandate form, please contact the Registrars.

Shareholder information on the Internet and electronic communications

The Balfour Beatty website at www.balfourbeatty.com offers shareholders and prospective investors a wealth of information about the Company, its people and businesses and its policies on corporate governance and corporate responsibility. It should be regarded as your first point of reference for information on any of these matters.

Computershare Investor Services have introduced a facility enabling Balfour Beatty shareholders to access details of their shareholding over the internet subject to complying with an identity check. You can access this service via the shareholder information section of the Balfour Beatty website at www.balfourbeatty.com. You can also obtain information on recent trends in Balfour Beatty's share price.

Balfour Beatty actively supports eTree, a programme designed to promote shareholder communication through electronic means rather than paper, by rewarding every shareholder who switches with a sapling to be planted on behalf of the Woodland Trust's Tree for All campaign. To register, or to find out more, please visit www.etreeuk.com/balfourbeatty. This service enables you to save paper, contribute to a better environment and give a child the chance to plant a tree.

In order to receive shareholder communications such as notices of shareholder meetings and the annual report and accounts electronically rather than by post, you need to register your details on www.etree.uk.com.

Unsolicited mail

Balfour Beatty is obliged by law to make its share register available on request to other organisations who may then use it as a mailing list. This may result in you receiving unsolicited mail. If you wish to limit the receipt of unsolicited mail, you may do so by writing to the Mailing Preference Service, an independent organisation whose services are free to you. Once your name and address have been added to its records, it will advise the companies and other bodies that support the service that you no longer wish to receive unsolicited mail. If you would like more details, please write to:

Mailing Preference Service
Freepost 29 LON20771, London W1E 0ZT
or visit the Mailing Preference Service website at www.mpsonline.org.uk.

Gifting shares to your family or to charity

To transfer shares to another member of your family as a gift, please ask the Registrars for a Balfour Beatty gift transfer form. Alternatively, if you only have a small number of shares whose value makes it uneconomic to sell them, you may wish to consider donating them to the share donation charity ShareGift (registered charity no. 1052686), whose work Balfour Beatty supports. Any shares that you donate to ShareGift will be aggregated, sold when possible, and the proceeds will be donated to a growing list of charities. Since ShareGift was launched, nearly £8m has been given to more than 1,000 charities. The relevant share transfer form may be obtained from the Registrars; further information about the scheme is available from the ShareGift Internet site www.ShareGift.org.

Share dealing services

The Company has established an execution-only postal share dealing service, through JPMorgan Cazenove Limited, for private investors who wish to buy or sell Balfour Beatty plc's shares. Further details can be obtained from:

The Balfour Beatty Share Dealing Service
JPMorgan Cazenove Limited
20 Moorgate, London EC2R 6DA
Telephone: 020 7155 5155

Alternatively, Hoare Govett Limited also offers a low-cost, execution-only, postal share dealing service. Further details can be obtained from:

Hoare Govett Limited (LCSD)
250 Bishopsgate, London EC2M 4AA
Telephone: 020 7678 8300

Both JPMorgan Cazenove Limited and Hoare Govett Limited are authorised and regulated by the Financial Services Authority.

Share price

The Balfour Beatty share price can be found at the Balfour Beatty website at www.balfourbeatty.com and in the appropriate sections of national newspapers under the classification "Construction and Building Materials". It is also available on Ceefax and Teletext and a number of personal finance websites on the Internet. Historic share prices are available from the library at Hoare Govett. Telephone: 020 7678 5926.

The London Stock Exchange Daily Official List (SEDOL) codes are:
Ordinary shares: 0096162
Preference shares: 0097820

The London Stock Exchange "ticker" codes are:
Ordinary shares: BBY
Preference shares: BBYB

Capital gains tax

For capital gains tax purposes the market value on 31 March 1982 of Balfour Beatty plc's ordinary shares of 50p each was 307.3p per share. This has been adjusted for the 1-for-5 rights issue in June 1992 and the 2-for-11 rights issue in September 1996.

Enquiries

Enquiries relating to Balfour Beatty's results, business and financial position should be made in writing to the Corporate Communications Department at the Company's Registered Office address or by e-mail to info@balfourbeatty.com.

PROSHARE
PRIVATE INVESTOR AWARDS
2003 WINNER

Designed and produced by Radley Yeldar (London)
Board photography by Edward Webb
Texas Department of Transportation image on page 21 courtesy of TxDot
BAA images on pages 4 and 5 courtesy of www.baa.com/photolibrary

Balfour Beatty

Balfour Beatty plc
130 Wilton Road
London SW1V 1LQ
Telephone: 44 (0) 20 7216 6800
Facsimile: 44 (0) 20 7216 6950
www.balfourbeatty.com