Building confidence

Kier Group plc
Annual report and accounts 2006

KIER GROUP

Kier Group plc is a leading construction, development and services group specialising in building and civil engineering, support services, public and private housebuilding, property development and the Private Finance Initiative (PFI). The Group employs 8,700 people worldwide and has an annual revenue in excess of £1.8bn.

The combined skills of our businesses create a winning formula to deliver a wide range of development schemes through a single source. Such schemes include property developments, mixed-use schemes and PFI projects, bringing together cross-divisional expertise for a total in-house solution.

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Group highlights

Fourteenth successive year of growth

Yet again, the Group is pleased to report further growth in revenue, profit and earnings per share. We remain firmly focused on continuing this pattern and are well positioned to do this, backed by our highly talented and well motivated management teams.

Kier Group operates though five main divisions, each focused on being best in its class.

Construction
A comprehensive building service delivered through a nationwide network of locally managed businesses complemented by a major projects and social housing capability. Civil engineering and mining in the UK and overseas.

Support Services
Comprehensive facilities management, reactive and planned building maintenance, M&E design and installation, plant hire, engineering design solutions and other outsourced services for both private and public sectors.

Residential
High quality private housebuilding through well respected and locally established brands.

Property
Commercial property development with capacity to maximise potential across a broad range of schemes.

Infrastructure Investment
Promotes and manages the Group's interests in the Private Finance Initiative, bringing together Kier's expertise and resources in worldwide construction, development and facilities management.

+23.6%

Pre-tax profit
Pre-tax profit* up 23.6% to £59.1m (2005: £47.8m**)

+25.1%

Earnings per share
Earnings per share up 25.1% to 120.8p (2005: 96.6p**)

+17.1%

Dividend per share
Full year dividend increased by 17.1% to 26.0p (2005: 22.2p)

£96.6m

Cash
£96.6m of cash generated from operating activities

£2.7bn

Construction and Support Service order books
Construction and Support Services order books at record levels

45%

Homes order book at 31 August 2006
Homes order book at 31 August 45% ahead of last year

* Pre-tax profits are stated after deducting joint venture tax of £1.4m (2005: £1.2m)
** Before exceptional items

Inside front cover image:
Designed & built by Kier London for Newlon Housing Trust, 105 key worker flats providing 300-bed spaces and ground floor commercial space. Temporary works design and accommodation were provided by Kier Engineering Services and Kier Plant respectively. Sister company Wallis provided hoists.

Front cover image:
Kier Eastern's fast track refurbishment of the central catering facility at the University of East Anglia in Norwich. It involved a total upgrade of all three servery areas and associated back of house facilities, the construction of a three storey steel frame and a glazed atrium. Temporary works design and accommodation were provided by Kier Engineering Services and Kier Plant respectively.

Working enthusiastically

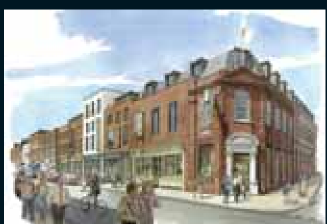
Our highly motivated teams approach everything they do professionally and with an infectious enthusiasm. This can-do attitude is prevalent across the Group and is a major force in the successful conclusion of even the most challenging schemes. A series of award-winning projects this year reflects the extraordinary performances that brought them to fruition.

Building value

We are intent on passing value to our clients. Our diverse skills mean that all our businesses are backed by a Group-wide resource including specialist teams that can support and advise at any stage of a project. This means we are often able to save our clients time, money, materials and energy during the course of a project by proposing innovative, alternative solutions.

23%

Annual growth rate in earnings per share
Compound annual growth rate of 23% since flotation 10 years ago.



Artist's impression of the completed development.

Project: Brownfield redevelopment, Chichester
Acquired as part of a six-strong development portfolio from Sainsbury's property arm in 2004, this is a key retail-led regeneration scheme for Chichester. The town centre mixed-use project will see the disused former Shippams food factory transformed into top-end retail and residential space that gels with the historical surroundings of this Roman town. Henry Jones, part of Kier Regional, is carrying out the work which includes a retained façade.

Working safely

The need to conduct all our operations safely and to protect those around us is given top priority at all times. Our below-average accident incident rate, together with numerous RoSPA and British Safety Council awards won, reflects our constant drive towards accident-free sites and our refusal to allow complacency to stand in the way of continuous improvement in all aspects of safety, health & environment.

Building standards

We remain focused on continuous improvement in all parts of the business. Fuelled by the need to set standards for others to follow, our teams regularly share information with our supply chain in order to bring about the highest possible standards of workmanship and service for all projects. We now have ISO quality accreditation for most of our businesses and are approaching our target for unilateral qualification.

£1.8bn

Revenue
Revenue for the year at £1,838.3m was 13.3% ahead of last year.

Interior of the new canine rehoming centre built in Harefield for the Dogs Trust by Kier Southern.

Project: Rehoming centre, Harefield for the Dogs Trust
A canine rehoming centre at Harefield for the Dogs Trust, the UK's largest welfare charity, recently completed by Kier Southern. The centre includes 75 kennels with air conditioning and underfloor heating and is likely to cater for some 2,000 dogs per year. Kier Managed Services provides FM services for the centre. Kier Plant and Kier Engineering Services provided equipment and temporary works design respectively.

Working with commitment

An underlying commitment to succeed is part of the Kier culture. Where possible Kier companies maintain the same team from bid process to completion, providing continuity and predictability, and ensuring that we live, breathe and exceed our clients' expectations. We are committed to developing our staff to enable them to get the best from their career. In return, we seek commitment from them that they will work towards achieving their individual goals and ultimately, our vision as a Group.

Building together

There are few better examples of the saying 'greater than the sum of its parts' than the Kier Group. While each individual company has its own expertise, we flourish to greatest effect when combining our company strengths. Kier company partnerships operate to great success throughout the UK on a wide range of mixed-use schemes, proving that we are one of very few who can truly offer a 'one stop shop'.

£96.6m

Cash
£96.6m of cash generated from operating activities.

The South Hook project used a 3,300 tonne capacity shearleg crane to remove sections of the old structure.

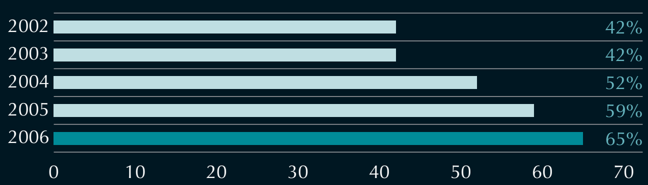
Project: South Hook Jetty
Kier Construction's project, in joint venture with Besix, at South Hook Jetty in Milford Haven will form part of the largest liquefied natural gas (LNG) terminal in Europe. This new state-of-the-art facility will provide a significant import facility of natural gas to the UK's national transmission network. Active work areas were encapsulated in order to minimise environmental impact. Kier Engineering Services provided temporary works design to facilitate this. Over 100 temporary accommodation units and crawler cranes were supplied by Kier Plant.

Working openly

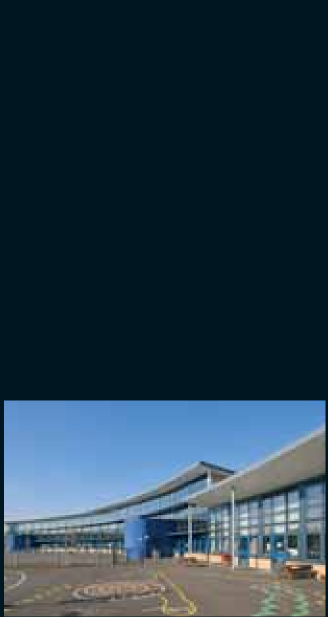
Repeat business accounts for a high percentage of our revenue and this could not be realised without the degree of openness and close communication afforded to our clients and all those with whom we do business. Knowledge and information sharing, assisted by investment in the latest technology, is extended to our clients and supply chain to ensure that best practice is communicated as widely as possible for maximum benefit.

Building confidence

With fourteen successive years of growth behind us, we have built a firm foundation on which to take the business further forward. With the right teams in place to continue our development and to make the most of new opportunities and markets, we are confident of further growth and success in the year ahead. Individually, our businesses are able to go forward confidently as part of a financially strong Group.



Percentage of negotiated and two-stage tenders awarded within the Regional Construction division



Playground and classroom at Downsell Primary School.

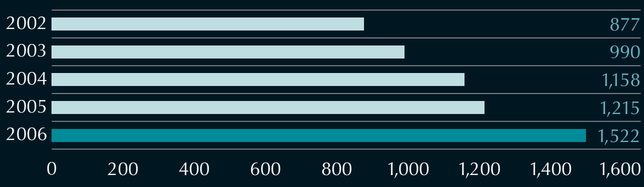
Project: Downsell Primary School
Downsell Primary School is a design & build project to provide a new two-storey primary school and replaces a variety of existing school buildings. It is one of seven schools Kier Project Investment has provided for the London Borough of Waltham Forest via Academy Services, as part of the government's PFI. Kier London, Kier Southern and Kier Eastern built the schools and Kier Managed Services provides facilities management.

Working honestly

Key to building trust is honesty. Kier companies open up clear lines of communication with all parties from the outset, making for an open and honest relationship. It is this approach which not only makes for a trusted company, but also for projects which are completed on time, and to everybody's satisfaction, often exceeding our clients' expectations. We believe in being upfront and realistic with our clients – a policy which we trust earns us respect and credibility from all with whom we do business.

Building relationships

We value our long-standing client portfolio and the importance of securing repeat and negotiated business. Our strategic alliances that bring together the best in retail, health, education and custodial, have led to long-term partnering frameworks and we are proud of the long-standing partnering and joint venture contracts of which we are part.



Housing completions

A Kier Plant crane in use at Bellwinch Homes' Grand Central development in Aylesbury.

Project: Grand Central, Bellwinch Homes
A Bellwinch Homes show apartment at Grand Central in Aylesbury which comprises a selection of one, two and three-bedroom apartments. Kier Plant is providing temporary accommodation and craneage at the development.

Chairman's statement

Peter Warry Chairman

I am pleased to report another record result for Kier Group plc for the year to 30 June 2006. Profits before tax have grown by 23.6% to £59.1m (2005: £47.8m before exceptional items); and earnings per share, after deducting the amortisation of intangible assets, have increased by 25.1% to 120.8p (2005: 96.6p before exceptional items), representing a compound annual growth rate of 23% since flotation some 10 years ago.

Activity across all of our divisions was high during the year and order intake was strong, resulting in a record £1.8bn of revenue for the year (2005: £1.6bn) and record year-end order books for Construction and Support Services of £2.7bn (2005: £2.2bn). Our Homes division had an excellent year with the number of unit sales 25% ahead of last year and order books at 31 August 45% ahead of the same time last year.

The cash performance, one of our key measures, was exceptionally strong, particularly within our Construction businesses, with £96.6m generated from operating activities during the year, despite special pension contributions of £31.5m in the period. The net cash balance at 30 June 2006 was £111.2m (2005: £58.1m).

This is the first set of full year results presented under International Financial Reporting Standards as adopted for use in the EU (IFRS) and comparative figures for the year to 30 June 2005 have been restated on this basis. The most significant impact arising from changes in accounting standards is on the Group's net asset position, which has reduced by £42.1m as a result of reflecting the net pension scheme deficit on the balance sheet.

The Board proposes a final dividend of 17.8p (2004: 15.2p) making 26.0p for the year (2005: 22.2p), an increase of 17.1% which is covered 4.6 times by earnings per share. The dividend will be paid on 5 December to shareholders on the register on 29 September 2006 and there will be a scrip dividend alternative.

Kier Plant has added a contingent of self-erecting remote controlled cranes to its growing fleet. The Potain Igo 50s have a maximum jib length of 40 metres and can lift up to four tonnes. These electrically-operated cranes are clean and quiet to run and are used mainly on small, low-rise residential and brownfield sites where space in restricted.

£111.2m

Closing net cash balances.

£1,311m

Construction awards during year.

Board appointments

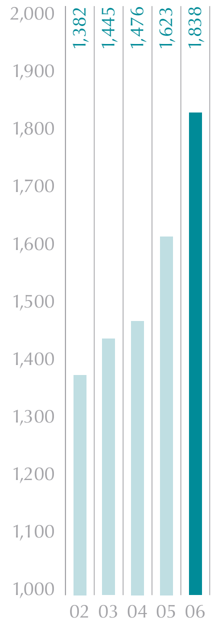
I am very pleased to welcome Phil White to our Board as a non-executive director from 1 July 2006. Phil was chief executive of National Express for nearly 10 years transforming it into one of the UK's leading transportation groups. He is already playing a very constructive role on the Kier Board and, with his experience, will contribute significantly to the future growth of the Group.

I am delighted to announce that, with effect from 1 October 2006, Mick O'Farrell, managing director of Kier Residential, will be joining the Board. Mick, aged 45, joined the Group in May 2003 as managing director of Allison Homes and became managing director of Kier Residential in August 2005. Mick has many years of experience in housebuilding having held senior positions in other major housing businesses. Our housing activities contribute significantly to the results and the strength of the Group and Mick's position on the Board is well deserved – I wish him well.

Prospects

The record levels of revenue, cash generation and contracting order books provide a firm foundation for the future and we are therefore well placed for further profitable growth in 2007.

Peter Warry
Chairman



Revenue
(£m)

Operating and financial review
Chief executive's review

John Dodds Chief Executive

The year to 30 June 2006 has been another successful one for the Group. Activity levels have been high, with revenue across most of the divisions at record levels; cash generation has been strong and all of the divisions have seen increased operating margins. Our growth record in earnings per share has continued with a 25.1% increase on last year (excluding the impact of last year's exceptional items) and compound annual growth of 23% since flotation in 1996.

Good progress has been made this year on multi-skilled projects where two or more of the divisions within the Group are working together. This is an area in which Kier has a competitive advantage and which, I believe, will continue to strengthen our position in the marketplace.

Financial performance

Revenue for the year at £1,838.3m (2005: £1,623.2m) was 13.3% ahead of last year with strong growth from our Construction, Support Services and Homes divisions. Operating profit, after the amortisation of intangible assets and joint venture interest and tax, was 20.8% ahead of last year at £59.2m (2005: £49.0m) and profit before tax increased by 23.6% to £59.1m (2005: £47.8m before exceptional profits of £6.7m).

Adjusted earnings per share before the amortisation of intangible assets and last year's exceptional profits and tax increased by 24.4% to 124.8p (2005: 100.3p).

The trading result for the year was supported by strong cash generation. Overall there was an inflow of £53.1m resulting in a year end net cash balance of £111.2m (2005: £58.1m) after an outflow of £31.5m relating to special pension contributions to the Kier Group Pension Scheme in the last quarter of the financial year. The strong cash balance is a reflection of excellent cash management in the Construction and Support Services divisions and the timing of land expenditure within the Homes division including the purchase of a number of sites on deferred terms.

Group structure and strategic developments

Kier Group comprises five divisions: Construction; Support Services; Homes; Property Development and Infrastructure Investment (investment under the Private Finance Initiative). The Group's management structure and segmental analysis for reporting purposes are based on the five divisions.

The Group has a well established business model that has underpinned its growth and development over a number of years providing both financial and operational synergies. Financially, the construction activities generate cash, albeit at relatively low operating margins whilst activities such as housebuilding and property require cash investment for growth but generate higher operating margins. By combining the cash generative construction activities with housebuilding and property, we have created an efficient financial model that achieves excellent returns on capital. Operationally the combined skills of our businesses are delivering a wide range of development schemes through a single source. Such schemes include regeneration projects, mixed-use schemes and PFI projects, bringing together cross-divisional expertise in a total in-house solution.

The Group strategy is to build on our skills and expertise and grow each of the divisions by maximising opportunities in the markets in which we operate. Much of our growth has occurred organically, particularly in the Construction division where our reputation for delivery and multi-skilled services has attracted a large number of opportunities. In Support Services our growth continues to emanate, largely, from new contracts in the local authority outsourcing sector through our Building Maintenance division.

£1,270m

Record Construction order book at 30 June 2006.

1,522

Unit sales from housebuilding.

£22.8m

Committed investment in the PFI portfolio.

1. Built by Kier Partnership Homes for Presentation Housing Association on brownfield land in Dagenham, The Fanshawe development comprises 58 units of one and two-bedroom flats including two disabled units, all built in timber frame. The development is a mixture of shared ownership and key worker accommodation. This new development has revitalised what was previously a run-down area.

2. Built by Kier Northern for the University of Sheffield, the bio-incubator building embraces the principles of sustainability and is dedicated to scientific research and development. It enables the Sheffield Universities to commercialise bio-science research whilst allowing other organisations to locate close to a centre of excellence in bio-sciences.

Our Homes division is one in which we have generated growth both organically and through acquisition. We have continued this strategy with the acquisition, in July 2006, of Hugh Bourn Developments (Wragby) Limited (Hugh Bourn Homes) which has formed the basis for the fifth housing operation within our Homes division.

Our Property development business has also grown both organically and through acquisition including, in December 2005, the acquisition of a portfolio of nine properties to add to our existing holdings. The strategy for Infrastructure Investment continues to be to grow a portfolio of PFI projects yielding long-term income streams while providing a flow of negotiated construction contracts and operational facilities management contracts for the Group's other operating divisions.

Business review, markets and outlook

Construction

The Construction division comprises Kier Regional and Kier Construction. Kier Regional benefits from unrivalled UK regional construction coverage focusing largely on mid-range building contracts, and encompasses our affordable homes and major building projects operations. Kier Construction includes the Group's infrastructure and overseas business with rail, mining and remediation capability.

Revenue in the Construction division reached a record £1,218.1m for the year, 12.1% ahead of 2005's revenue of £1,086.3m. Growth within this division was fuelled by a strong market supported by a high level of public sector expenditure. Operating profit increased by 30.4% to £18.0m (2005: £13.8m) and the operating margin reached our short-term target of 1.5% compared with 1.3% last year.

Cash generation, one of our key performance measures, has been exceptionally strong, with cash balances at 30 June 2006 over £40m higher than the previous year end and average cash balances for the year £38m ahead. Contract awards were very strong during the year at £1,311m (2005: £1,372m), providing a record order book of £1,270m at 30 June 2006 (2005: £1,030m).

Kier Regional business review

Kier Regional, with its wide network of UK construction businesses, continues to go from strength to strength and, once again, has achieved a number of records in the key performance measures of revenue, cash and new orders. Revenue, at £1,092.8m, was 14.5% ahead of 2005; year-end cash balances of £243.0m were £38.2m ahead; and contract awards of £1,216m were 19.4% ahead of 2005's £1,018m.

The high proportion of negotiated and repeat business from long-standing clients, as well as national framework agreements, has remained a constant theme across all regional businesses. Representing around 65% of work secured (2005: 59%), this provides us with a lower risk, more sustainable order book, particularly when combined with the fact that the average size of contracts within this business remains relatively low at £3.2m, (2005: £2.9m).

Operating and financial review
Chief executive's review
continued

A number of the framework agreements and strategic alliances are with public sector clients including those designed to deliver an increasing number of social housing units. Of particular note are our framework agreements with Newlon Housing Trust and Dominion Housing Group, both Registered Social Landlords, which are providing high-rise affordable housing in London and which have contributed to the £180m of residential awards for the year. The continuing high level of public expenditure has led to an increase in public sector awards to 43% of the total compared with 41% in 2005.

Education has remained a very strong sector for Kier Regional, with over £350m of work secured this year, representing 29% of total awards (2005: 24%). £95m has been awarded under the private finance initiative, including Norwich Schools and Oldham Schools both with Kier as an equity partner in the special purpose vehicle.

Our involvement with private sector clients continues through partnering style arrangements with food retailers including Tesco, Waitrose, Morrisons and Sainsbury's and developers such as Land Securities Trillium, for whom we are carrying out the multi-phased refurbishment of the DVLA headquarters in Swansea. From this contract, our relationship with Land Securities has strengthened.

As previously reported, in November 2005 our client Castlepoint announced the closure of a retail centre in Bournemouth due to concerns over health & safety. We, as main contractor, worked around the clock to install temporary props allowing the centre to fully re-open in mid January. We are discussing with Castlepoint the dismantling and rebuilding of the car park and the minimisation of any disruption on trading. The costs of this exercise are expected to be covered predominately by insurance, with no material effect anticipated on the Group's trading position.

1. Completed by Moss Construction, remodelling of the Camp Hopson department store in Newbury comprised the demolition of existing buildings to the rear of the store and construction of a new three-storey extension plus the refurbishment of the Grade II listed façade. A new restaurant and two new shells for independent retail units were incorporated at ground level.

2. Kier Caribbean and Industrial is delivering a new terminal building at Jamaica's Norman Manley International Airport in Kingston. The total expansion works will encompass the ticketing and departure concourse, access roadways and public car parks, reconfiguration of the customs hall to ensure more efficient passenger movement and the creation of a cargo village.

Kier Construction business review
Revenue remained relatively stable in the year to 30 June 2006 at £125.3m (2005: £131.7m). In the UK, the civil engineering arm of Kier Construction saw the commencement of a rail framework for the renewal of railway structures in East Anglia under a five-year agreement with Network Rail. The five-year Asset Management Programme 4 for United Utilities, in joint venture, has successfully completed its first year of operation, albeit with a longer lead-in time than envisaged. Our major infrastructure projects capability continues with the successful completion of CTRL contract 103 and increasing activity at Milford Haven for South Hook LNG.

Our mining business had another productive year at our opencast coal site at Greenburn, East Ayrshire, with coal production having exceeded one million tonnes. 1.3m tonnes of coal have now been extracted to date and over 66% of that remaining in the ground has been forward-sold at favourable fixed prices.

Our remediation capability, where brownfield sites are redeveloped for commercial, residential or mixed use, is being enhanced with a number of projects for other Group companies. In Peterborough, work has commenced on a former Anglian Water site for our Homes business and in Uxbridge, Kier Construction is working with Kier Property to remediate a British Gas site ahead of development of a mixed-use scheme.

Overseas, our activities in the Caribbean continue to perform well. Good progress has been made on a large transportation centre in downtown Kingston, Jamaica and the extension to Kingston's Norman Manley Airport has started well with certain areas expected to be ready for the Cricket World Cup next year. Our long-term alliance with Alcoa continues to provide extensive work on projects at aluminium refineries in Suriname and Jamaica.

Construction markets and outlook
In the UK demand for building remains high, both in the public and private sectors and there is an increasing emphasis on remediation projects. This demand can be satisfied by the combined skills of our Construction division and development expertise from elsewhere in the Group.

Our mining activities have good potential to contribute to future growth. The current area in which we are mining in Ayrshire is expected to continue production until 2009, however, extensions are being pursued and a new planning application has been made to operate an opencast mine at an adjacent site. If successful, this will extend the life of the mine into 2011.

Overseas, our established contacts are providing us with good opportunities, particularly in the Caribbean, with Alcoa, and in Romania, where we have recently secured a contract for a shopping mall and residential apartments with our joint venture partner. In Dubai, where construction activity is plentiful, we remain focused on our key area of expertise, infrastructure, and we have recently been awarded a new contract to build roads and infrastructure works for the new 'City of Arabia'.

Our Construction order books, represented by confirmed contracts in hand, are at the highest levels ever at £1,270m (2005: £1,030m), supported by a significant pipeline of contracts in the final stages of negotiation. With these strong, good quality order books, we can expect further growth in our Construction activities in the new financial year.

Project: Sainsbury Centre for Visual Arts
Refurbished by Kier Eastern, the Sainsbury Centre for Visual Arts at the University of East Anglia included new exhibition areas, a larger reception area, education studio, refurbished café and a lift for easier disabled access. Temporary works design and accommodation were provided by Kier Engineering Services and Kier Plant respectively.

Operating and financial review
Chief executive's review continued

Support Services

Support Services comprises four business streams: Kier Managed Services, providing facilities management services to public and private clients; Kier Building Maintenance, providing reactive and planned maintenance mainly to local authority clients, housing associations and Arms Length Management Organisations; Kier Building Services Engineers, a specialist mechanical and electrical design and installation and maintenance business; and Kier Plant, specialising in plant hire to Kier Group companies and external clients.

Support Services business review

Revenue in the Support Services division increased by 18.5% in the year to £281.3m (2005: £237.4m), driven largely by our Building Maintenance business. Operating profit, before deducting the amortisation of intangibles of £1.9m in both years, increased by 26.1% to £8.7m (2005: £6.9m), providing an operating margin of 3.1% (2005: 2.9%), slightly ahead of our short-term target of 3.0%. The cash performance within the division has been strong with £14.6m generated in the year to give a closing cash balance of £12.5m (2005: overdraft of £2.1m). Order books have also grown during the year to £1,396m at 30 June 2006 (2005: £1,204m).

In Managed Services volumes have remained steady. An increasing contribution to revenue arises from services provided under PFI; however, other private sector work has reduced in volume as we continue our focus on margin improvement. New services have begun during the year for the National Offenders Management Service in Newport and the Dogs Trust site in Harefield; both achieved through introductions from our Construction division.

Good results were achieved by the Building Maintenance division, which now looks after around 185,000 homes for local authority clients including Sheffield City Council, Islington Borough Council and Leeds City Council. Revenue increased from £136.9m to £172.5m, mainly due to the inclusion of Decent Homes work and a whole year of revenue from the Leeds contract. During the year we secured a five-year contract for the City of Lincoln which, whilst currently in the mobilisation phase, will provide £7m of revenue per annum under the Decent Homes initiative. Kier Sheffield, our partnership with Sheffield City Council, has achieved an increase in the volume of work carried out under the Decent Homes initiative. It continues to benefit from Sharrow Industries, a sheltered workshop run by Kier Sheffield which supplies and manufactures kitchens, windows and doors under an exclusivity agreement with all five contractors under the Decent Homes initiative in the City, one of which is Kier Sheffield. We were delighted that Sheffield City Council achieved Beacon status, the highest accolade a council can receive. Kier Sheffield's work was also influential in Sheffield's housing services being awarded a three star rating (the highest) by the Audit Commission.

Support Services markets and outlook

Whilst opportunities continue to emerge within the facilities management market for Kier Managed Services, we will continue to be selective in the contracts for which we bid.

In Building Maintenance both local authority expenditure, through housing repairs and maintenance budgets, and central government expenditure, through the Decent Homes initiative, are providing good potential for new work. A strong list of opportunities is emerging in the £10m to £40m per annum range and, although disappointingly, we were unsuccessful on a bid for Manchester, we have recently been confirmed as preferred bidder, subject to negotiations on the heads of terms, on a contract for Harlow. With a revenue stream of £17m per annum this contract will provide repairs and maintenance to housing stock, street scene works and grounds maintenance. In addition, we have been confirmed as preferred bidder on a £6.5m per annum contract in Southwark and have been short-listed as one of three on a £35m per annum repairs and maintenance contract for Stoke.

With our proven ability to fulfil these higher value contracts, we are well placed to secure further work in this area.

Homes

Kier Residential, our housebuilding division, was structured through four companies during the year: Allison Homes, which operates throughout Lincolnshire and north Cambridgeshire; Bellwinch Homes, with sites in the south and south east; Kier Homes, operating across the central belt of Scotland; and Twigden Homes, with activities in East Anglia and the West Midlands. In July 2006 we acquired Hugh Bourn Homes operating in North Lincolnshire, which has formed the basis of a fifth operating area.

Homes business review

Kier Residential experienced a changed pattern to the timing of unit sales in the year to 30 June 2006 with a greater bias towards the

1. Kier Building Services Engineers provide planned and reactive maintenance in addition to full M&E design and installation services.

2. Kier Building Maintenance (KBM) London won a British Safety Council International Safety Award 2005. KBM quality inspector Eddie Skiff and KBM business support manager Josephine O'Connor attended the presentation.

Project: Pannier Market
Situated in the centre of Tiverton, the recently completed Pannier Market has undergone an extensive refurbishment by Kier Western. The scheme has enhanced the setting of the historic and listed market buildings, creating a more flexible and extensive trading space, and a safer shopping experience for pedestrians.

second half of the year than in 2005. Overall we sold 1,522 homes in the year, a 25% increase over 2005's 1,215 homes achieved from an 11% increase in outlets. Average selling prices of £180,100 (2005: £181,700) provided revenue of £274.2m from housing sales (2005: £220.8m). A land disposal, of part of a large site, generated a further £3.7m of revenue at a nominal profit of £0.1m. The slight reduction in average selling prices reflects a 2% reduction in unit size and an increase in the proportion of affordable housing sales from 12% of total sales in 2005 to 16% in 2006. Operating profit from housing sales increased by 26.1% to £41.5m (2005: £32.9m) at a margin of 15.1% on housing revenue (2005: 14.9%) in line with our targets for this business.

During the year £93.3m was spent on selective land purchases, including a significant amount on deferred terms, and at 30 June 2006 the land bank contained 5,863 units with planning consent (2005: 5,178 units) which, at 3.9 years' worth of sales, is in line with our target holding of four years' unit sales. In addition to land with planning consent, we also hold approximately 12,000 units of strategic land, mostly under option. Strategic land is proving a valuable route for land acquisition as, historically, approximately 18% of our annual unit sales have originated from this process.

Continuing the theme of mixed-use and regeneration sites, Kier Residential is making good progress on remediating a former Anglian Water site near the centre of Peterborough. Kier Construction is carrying out the work, which, when completed, will provide a site for 550 residential units, comprising a combination of flats and houses. In Aylesbury, at a former Kier Property site, sales targets are being achieved following remediation of the site adjacent to the station. Planning consent has now been granted at Poole Harbour, subject to signing the agreement for the Section 106 works, for redevelopment of a mixed-use site previously owned by Network Rail. Kier Construction will relocate the rail sidings and carry out other infrastructure works which, in time, will provide a development site for a new hotel, some 250 apartments, offices, shops and a new railway station.

In Sunbury, a development of 96 homes and a hotel is progressing on remediated land, in conjunction with Kier Property. Bellwinch is constructing three apartment blocks and Kier Property is building the 120-bedroom hotel. Our affordable housing business, Kier Partnership Homes, worked with Bellwinch to obtain a housing association contract for 48 units within the scheme.

On 31 July 2006 we acquired the shares in Hugh Bourn Homes for a total consideration of £53.3m, representing the market value of land, work in progress and other assets and liabilities. £20m was paid on completion, with the balance due in instalments on 2 July 2007 and 1 July 2008. Hugh Bourn Homes forms the foundation for a fifth trading division of Kier Residential, expanding its reach to the north of Allison Homes' operating area. The majority of the 1,197 residential plots we acquired with the business benefit from a combination of outline and detailed planning consent and included a small number of built and partially built units. In its first year of operation within Kier, Hugh Bourn Homes is expected to trade from 21 outlets.

Housing markets and outlook

The housing market saw its usual quietening during the holiday season in July and most of August, although there are clear signs that it has begun to pick up in recent weeks. Reservations during the new financial year, on a like-for-like basis, excluding the effects of the acquisition of Hugh Bourn Homes, are 46% ahead of the same period last year and, taking Hugh Bourn Homes into account, they are some 68% ahead of last year. This has given rise to an order book at 31 August 2006 some 45% ahead of the same time last year (38% excluding Hugh Bourn Homes).

We will be selling from approximately 27% more outlets during the year compared with last year and therefore we anticipate growth in unit sales for the full year of which 42% are already secure. Similar to 2006 we expect the balance of sales to be skewed towards the second half of the year.

We anticipate further land expenditure this financial year, in addition to the expenditure for Hugh Bourn Homes, in order to maintain our land bank at approximately four years' worth of sales.

Property

Our Property development business comprises activity across commercial, industrial, retail and mixed-use sectors largely on a non-speculative basis. It operates through Kier Ventures, a wholly owned subsidiary; and Kier Developments a joint venture with the Bank of Scotland.

Property business review

Kier Property has had another active year, cementing its position as one of the UK's leading commercial property developers. Despite the commercial property market in the UK experiencing high levels of investment demand, with investors chasing limited availability of stock, Kier Property acquired some 15 new sites during the year and crystallised considerable value on several existing properties through lettings, sales and obtaining planning consents.

Notwithstanding all this activity, the number of developments sold during the year fell resulting in a reduction in revenue from £62.2m in 2005 to £47.5m in 2006. Operating profit, similarly, reduced

1. The award-winning new 224-bedroom Marriott hotel in Leicester, a design & build project by Marriott Construction. The six-storey building features a central atrium with restaurant and lounge area, a leisure club with swimming pool, sauna and steam rooms, conference facilities and meeting rooms. Marriott Construction won a 2006 East Midlands LABC Built in Quality Award in the 'best commercial project' category.

2. Land acquired from Kier Property on a prime location in Loughton has been developed and now accommodates a BMW car showroom and new offices for Kier London.

from £10.4m to £9.2m in the year, although operating margins moved ahead from 16.7% to 19.4%.

Kier Property has developed a portfolio that now totals over 5m sq ft of developments, with a prospective completed value of around £734m. The portfolio offers a diverse spread of office, retail and mixed-use schemes with a particular commitment to regeneration. In December 2005, we acquired a £10m portfolio including nine sites from Warner Estates. One of the sites, in Lincoln, has planning consent for residential use on which Allison Homes has commenced the infrastructure works for a major residential development. Remaining sites include a mixture of short-term and long-term developments across all sectors and we will work through the portfolio to maximise value.

During the year, Kier Property continued to augment its industrial portfolio, with the successful 'Trade City' brand as a platform. A 2.9-acre site on London's North Circular Road was acquired for a 115,000sq ft scheme, of which almost an acre is expected to be sold to a self-storage company. An 11-acre former British Gas site in Uxbridge was also purchased and is being remediated by Kier Construction ahead of a 215,000sq ft employment-led mixed-use scheme. At our Crown Road scheme in Enfield, the first phase was pre-let and completed during the year, comprising a 20,000sq ft Renault car showroom and a 50,000sq ft Selco builders' merchant. The scheme was then sold to a financial institution at a very satisfactory yield. We have now secured planning permission for a second, 80,000sq ft phase at the site and work will begin during the coming year.

At our Loughton development the prime site was sold to Sytner for a BMW car showroom and the remainder of the site was developed into a new office for Kier Regional's operating business, Kier London.

In the offices portfolio, Kier Property continued to establish itself as one of the foremost players in the pre-let development arena. During the year, Kier Property was selected as preferred developer to deliver a new head office for Ordnance Survey in Southampton. Kier Regional will build the new 145,000sq ft head office on a new site with Kier Building Services Engineers carrying out the mechanical and electrical installation. Kier Managed Services will then provide the facilities management services when it is complete. This will enable Kier Property to work up Ordnance Survey's existing 25-acre site into a major regeneration project comprising 10 acres of employment use and over 400 homes, to be developed with Kier Residential.

A further pre-let office scheme was signed during the year to develop a new 140,000sq ft head office campus for global IT company Electronic Data Systems. Work has begun on phase one of the £35m scheme with Kier Regional as the contractor.

On other regeneration projects, Kier Regional has begun work on a mixed-use redevelopment of the former Shippams food factory in Chichester. The scheme will include 45,000sq ft of retail space, most of which has been let to high street retailers, and a residential development of 165 flats the land for which has been sold to a house builder during the year.

In March 2006 we secured planning for a new 175,000sq ft produce and flower hall at the Western International Market near Heathrow. On completion of the new facility, we will develop a 300,000sq ft distribution scheme on the old market site.

Project: Oratory School
Kier Southern completed the second phase of new boarding facilities at the all-boys Oratory School in Reading. The project to house 80 new boarders occupied a tightly confined site and a Kier Plant tower crane was used to minimise movements within the school grounds.

Operating and financial review Chief executive's review continued

Property markets and outlook

Looking ahead, major schemes such as the three-phase, 600,000sq ft Reading Central office development and a 800 home regeneration site close to Ashford town centre will gather pace and we anticipate further growth in the business through both acquisitions and enhancement of existing properties.

We are particularly pleased to have been selected as preferred bidder for the new UK Supreme Court in London's Parliament Square. Planning consent has recently been granted and work is expected to commence in spring 2007.

Infrastructure Investment

Kier Project Investment (KPI) manages the Group's interests procured under the PFI. The core strength of KPI is the ability to bring together the diverse range of skills and resources within the Group and combine these with a financial package that will deliver high quality buildings and services to meet the public sector's needs.

Infrastructure Investment business review

This has been another successful year for KPI, bringing our committed equity investment in the government's PFI to £22.8m and securing a further £230m of future revenue for the Group through associated construction and facilities management contracts.

Three projects reached financial close during the year: one health scheme, the Garrett Anderson Centre, a significant addition to the existing Ipswich Hospital; and two schools schemes providing six schools in Norwich for Norfolk County Council and two schools, for Oldham Metropolitan Borough Council. Construction work with a combined value of £120m is now under way by Kier Regional. Facilities management services will be provided by Kier Managed Services on completion of the buildings.

A contract to provide a new headquarters building in Gravesend for Kent Police reached financial close in July 2006. This new £32m facility will be constructed by Kier Regional.

Construction was successfully completed on a number of projects during the year. Eleven schools including two in Tendring, seven in Waltham Forest and two in Sheffield; Hinchingbrooke Hospital and Oldham Library were all handed over on time and Kier Managed Services commenced facilities management operations on each of these new facilities. Construction continues on two further schools in Sheffield.

We were disappointed not to have been selected for either of the 'Building Schools for the Future' (BSF) projects for which we were bidding. BSF has been a costly exercise for us and we have written off costs of £2.2m in the two years to 30 June 2006. However, we are not ruling out BSF projects and our Construction companies remain keen to pursue the construction opportunities.

Infrastructure Investment markets and outlook

The PFI market continues to provide sensible opportunities for our businesses in the key sectors in which we operate. Our strategy continues to be to invest in PFI opportunities that provide the Group either with the construction work or the facilities management contracts, and preferably both. As a Group we can tackle a wide range of sectors from hospitals and schools to street services, which provides us with a broad market and plenty of scope for new projects.

1. Procured by Kier Project Investment under the government's PFI, the Oldham Library and Lifelong Learning Centre is part of Oldham's regeneration programme. It incorporates a sedum-covered green roof and a unique copper-clad performance hall in a prominent location in Oldham town centre. It was built by Kier North West and Kier Managed Services undertakes the facilities management.

2. The pathfinder Greenwich Neighbourhood Resource Centres PFI project by Kier Project Investment provides residential, intermediate care and nursing care together with hotel services for 167 local elderly residents. Built by Kier London, the project was completed and operational some five weeks ahead of programme and within budget. Kier Managed Services manage the facilities. The project was recognised in 2006, receiving the 'Best Operational Local Government Project' award in the Public Private Finance Awards.

KPI is currently short-listed, supported by other Group companies, on bids for the Three Counties Police Investigation Centres project in East Anglia and the Leicester Hospitals scheme.

Pensions
At 30 June 2006 the net pension deficit shown on the balance sheet, calculated as required by IAS 19 'Employee Benefits', is £42.1m (June 2005: £85.3m). The movement in the year includes special contributions, amounting to £31.5m, paid into the pension scheme in the last quarter of the financial year. These contributions form part of a schedule of payments designed to eliminate the pension scheme deficit over 10 years. A further £5.0m was contributed in July 2006 and the Group is making further special contributions of £0.5m per month. These contributions are in addition to a special contribution of £12.0m made in March 2005, bringing the total payments to the scheme, over and above normal contributions, to £43.5m in the two years to 30 June 2006.

The special contributions have no effect on the income statement for the year, but are shown as a reduction in cash and a reduction in the pension deficit.

Health & Safety
Kier has continued to build on the positive approach to health & safety valued in all of our employees and supply chain members. This approach, together with our 'Don't Walk By' campaign and continuing focus on behavioural issues, has created a proactive approach identifying and correcting health & safety issues. By addressing the risk and not the symptom, Kier has brought about significant reductions in its accident incidence rate, which now stands at 522 per 100,000 staff and subcontractors, comparing favourably with the Health & Safety Executive benchmark of 902.

In recognition, the Group received nine gold, two silver, and one bronze award from RoSPA and seven British Safety Council Awards.

Through their positive, proactive attitude, our staff and supply chain work tirelessly to reduce the potential for accidents to happen, and to protect the long-term health of those working on Kier sites. The roll-out of the ISO 18001/14001 registration programme has ensured that already high standards and levels of awareness continue to be raised and the third party audit carried out by BSI ensures that the Group continues to deliver best practice. This continuing improvement approach culminated in Kier Group being awarded the highly coveted Quality in Construction Health & Safety Management Award 2006.

People
The success and reputation of a business is a reflection of the quality of the people who work together to form it. We have many excellent, committed and enthusiastic people in this Group. Whether we are building a tunnel, servicing an office, changing a boiler or grappling with a complex planning issue, the wealth of talent in this Group to bring any project to fruition is immense. I am very proud of what this Group can achieve and I also sense a great pride in our employees: pride, not just for the work they are doing, but as employees of Kier. I should like to thank all of our employees for their continuing contribution to making Kier Group the success it is today.

Objectives and prospects
The year to 30 June 2006 has seen the Group firing on all cylinders and our objective for the new financial year is to maintain this momentum and to continue to provide clients with a high quality service.

Our Construction order books at 30 June 2006 were at the highest level ever and, with a strong pipeline of virtually secure work, our Construction division is in an excellent position to grow further. In Support Services the market for local authority outsourcing contracts continues to expand. Our housing land bank contains sites of good quality in saleable locations and we anticipate an increase in unit sales for Kier Residential this year enhanced by the acquisition of Hugh Bourn Homes which provides us with a new operating area. Our Property portfolio contains a range of development sites that will continue to be enhanced in value, and in Infrastructure Investment we can see a number of good projects coming forward.

Opportunities for our businesses to work together are becoming more prolific as complex planning issues continue to require resolution and clients' requirements become more intricate.

Against this backdrop, the prospects for the Group are excellent and I am confident that we will continue to deliver further growth in 2007 and thereafter.

John Dodds
Chief Executive

Kier Sheffield's technical training centre was refurbished during the year, doubling the size of the facility and allowing for a greater range of industrial and commercial-scale training equipment. The centre offers a range of domestic and commercial gas, heating and plumbing-related training and assessment courses available to aligned tradespeople. It is currently the only Accredited Certification Scheme Centre allowed to carry out commercial assessments in Sheffield.

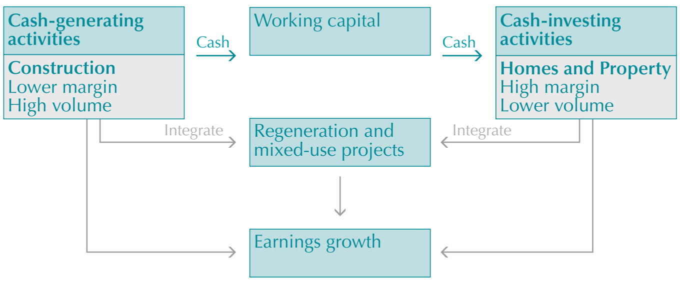
Project: Visitor centre, Welney
A new energy-efficient visitor centre at Welney in Norfolk built by Kier Eastern for the Wildlife and Wetlands Trust.

Operating and financial review
Financial review

Deena Mattar Finance Director

These are the Group's first annual consolidated financial statements prepared in accordance with IFRS. The Group's IFRS accounting policies have been applied in preparing the consolidated financial statements for the year to June 2006, the comparative information for the year to 30 June 2005 and the preparation of an opening IFRS balance sheet at 1 July 2004 (the date of transition from UK GAAP to IFRS).

Kier integrated business model



Financially – cash generated from construction activities provides investment for homes and property operations.

Operationally – skills can be combined from various divisions to provide a totally integrated solution to clients' increasingly complex requirements.

Profit before tax
Profit before tax increased by 23.6% to £59.1m (2005: £47.8m). This is stated after deducting joint venture tax of £1.4m (2005: £1.2m) and before the exceptional profits of £6.7m recorded in the year to 30 June 2005. The exceptional profits in 2005 included: £0.8m on the sale of the Group's remaining interest in Kier Hong Kong Limited; £3.8m on the sale of a property fixed asset; and £2.1m on the sale of the Group's interest in a PFI concession.

Taxation
The Group's effective tax rate, including joint venture tax on joint venture profits, is 29.0%. This compares with an effective rate of 34.3% in 2005. However, the effective tax rate for the year to 30 June 2005 included £2.5m of exceptional tax relating to refinancing one of the Group's PFI concessions, for which no profit was recognised; and £1.8m relating to exceptional items. Disregarding the exceptional items, the 2005 effective rate, including joint venture tax on joint venture profit, was 30.2%.

The reduction to 29.0% largely reflects the utilisation of some brought forward capital losses and tax benefits relating to contaminated land remediation.

Interest and cash
The interest charge for the year comprises the following:

	Years to 30 June	
	2006	2005
	£m	£m
Group interest receivable	**5.3**	4.0
Interest payable	**(2.8)**	(2.5)
Unwinding of discount	**(2.6)**	(2.7)
Share of joint venture interest	**(2.6)**	(3.1)
	(2.7)	(4.3)

The Group interest receivable arises from average treasury balances of £60m for the year. The charge of £2.6m relating to unwinding of discounts includes £2.0m relating to land creditor balances payable over a number of years (2005: £2.1m).

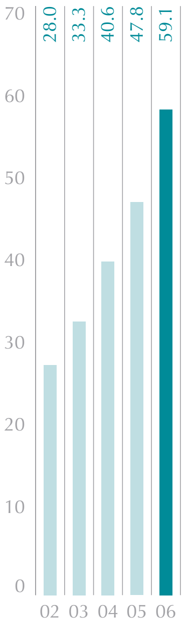
Net cash at 30 June 2006 was £111.2m (2005: £58.1m) after deducting £30.1m relating to loan notes. £96.6m was generated from operations during the year after deducting £31.5m in respect of the special pension contributions made during the year.

42%

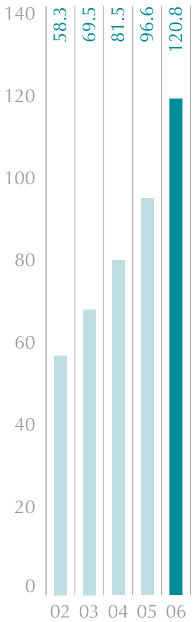
Of targeted 2007 unit housing sales secure.

£31.5m

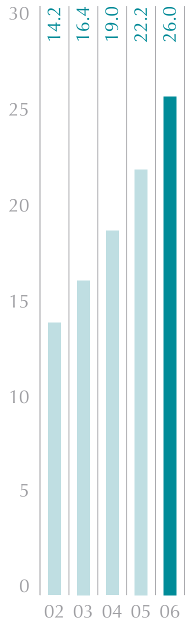
Special contributions to pension scheme.



Profit before tax*
(£m)



Earnings per share*
(pence)



Dividend per share
(pence)

Figures for the years 2005 and 2006 are stated under IFRS and those for 2002 to 2004 are stated under UK GAAP.

* Excluding exceptional items

Cash, net of debt, at 30 June 2006, includes £37.6m (2005: £22.8m) of cash which is not generally available for Group purposes, including that held by joint arrangements, overseas and by the Group's captive insurance company. The liquid cash position is affected by seasonal, monthly and contract-specific cycles. In order to accommodate these flows the Group maintains a range of bank facilities which were increased by £40.0m during the year. The facilities at 30 June 2006, of £120.0m, comprise £12.5m of overdraft facilities, and £107.5m of committed, revolving credit facilities all on an unsecured basis. £15.0m of this expires in January 2007 and £92.5m expires in January 2011.

Treasury policy and risk management

The Group has a centralised treasury function which manages funding, liquidity and financial risks. The Group's policy is to use the cash generated by the Construction business to invest in the asset based Homes and Property businesses. This financial model is supplemented with bank facilities amounting to £120m and long-term debt of £30m.

The Group's financial instruments comprise cash and liquid investments. The Group, largely through its PFI and Property joint ventures, enters into derivatives transactions (principally interest rate swaps) to manage interest rate risks arising from the Group's operations and its sources of finance. We do not enter into speculative transactions.

There are minor foreign currency risks arising from operations. The Group has a small number of branches and subsidiaries operating overseas in different currencies. Currency exposure to overseas assets is hedged through inter-company balances and borrowings, such that assets denominated in foreign currencies are matched, as far as possible, by liabilities. Where there may be further exposure to foreign currency fluctuations, forward exchange contracts are entered into to buy and sell foreign currency.

Balance sheet and shareholders' funds

The balance sheet at 30 June 2006 includes intangible assets of £14.8m of which £9.6m relates to the outsourcing contract at Sheffield which is being amortised over 10 years, being the life of the contract, with £1.9m (2005: £1.9m) charged to profits in the year.

Shareholders' funds have more than doubled during the year to £108.5m (2005: £52.8m) arising from retained profits of £42.9m, dividends of £(8.3)m, currency translation of £(0.3)m, movement in the share scheme reserve of £0.7m, movement in the net pension deficit of £21.0m, issue of shares of £2.1m and the introduction of IAS 32 and 39 this financial year, which has a £(2.4)m impact.

Pensions

The Group participates in two principal schemes, the Kier Group Pension Scheme, which includes a defined benefit section, and a defined benefit scheme on behalf of its employees in Kier Sheffield LLP. The financial statements reflect the pension scheme deficits and surpluses calculated in accordance with IAS 19. At 30 June 2006 the net deficit under the Kier Group Pension Scheme was £46.9m (2005: £86.6m). The market value of the scheme's assets was £467.0m (2005: £393.5m) and the net present value of the liabilities was £534.0m (2005: £517.2m). £31.5m of the movement in asset value related to the special contributions made to the pension scheme during the year.

Under the scheme relating to Kier Sheffield LLP there was a net surplus of £4.8m at 30 June 2006 (2005: £1.3m).

Pension charges of £16.9m (2005: £15.3m) have been made to the income statement in accordance with IAS 19.

Deena Mattar
Finance Director

Operating and financial review
Business risks

Core to our continued success is our ability to identify and effectively manage the risks to our business. Accordingly the Group has well defined, rigorous policies and processes designed to identify, mitigate and control risk. Risks are specific to each of our businesses and are controlled through the Group's risk management processes. The primary risks that have the potential to adversely impact on our business over the next twelve months are considered to be as follows:

- Contract and build risk: We carry out several hundred contracts annually and the risks to which the Group is exposed are dependent upon the nature of the work, the duration of the contract and the legal form of the contract. The Group's appetite for very long-term, large, competitively tendered construction contracts is limited, driven by the desire to manage risk. Tenders for contracts are subject to approval by the Board, chief executive and finance director or divisional directors depending on the value and nature of the contract. Contracts in progress are controlled and managed through the Group's operating structure and procedures including rigorous and regular review of forecast revenue and costs to complete;

- Land acquisition risk: The cost and quality of land is fundamental to the profitability of a housing development business. Site evaluation is a key process and site appraisals are carried out in detail including external advice where appropriate. Land acquisitions are subject to approval by the Board, chief executive and finance director or divisional directors depending on the value and nature of the development. Sites under development are controlled and managed through the Group's operating structure and procedures including rigorous and regular review of forecast revenue and costs to complete;

- The housing market: Our ability to sell houses depends on the demand for housing which, in turn, is linked to consumer sentiment. We manage the exposure by ensuring that we closely control levels of work in progress to match the level of demand. Prices and incentives are reviewed regularly and adjusted as appropriate;

- Property development risk: Similar to housing land acquisition, acquiring the right property at the right price is fundamental to the profitability of the Property division. The division controls its development risk by commencing construction generally when it has either pre-sold or pre-let the development. Divisional and Group Board approvals are required depending upon the value and nature of the development;

- Investment risk: The Group is selective in the PFI projects for which it bids, primarily concentrating on the education, health, libraries, housing, custody centres and care homes sectors where we have established expertise;

- People are the key to this business and good people are a scarce resource. It is important that we attract the best, look after them and retain them. Health & safety is a key feature and we have rigorous health & safety policies aimed at minimising health & safety incidents that may affect any staff, subcontractors and members of the public coming into contact with our business activities;

- Pension scheme deficit: The pension scheme liabilities and assets are subject to market movements and, although a long-term issue, new regulations require us to respond to these long-term issues over the short-term. Steps have been taken to eradicate our calculated deficit over a timeframe agreed with the Scheme Trustees.

1. First Start is an award-winning training initiative introduced by Kier Islington in conjunction with Islington Council. Kier provides training for 14-18 year olds in construction-related trades and this year 28 trainees graduated. The scheme, now in its third year, has been so successful that it is being rolled out elsewhere within the Group.

2. Constructed on land sourced from Kier Property, Kier London's self-built new offices in Loughton.

Corporate social responsibility

By providing our clients with the highest possible quality of service and through sustainable, profitable growth, our vision is to be the most highly respected company in the industry. We will continue to build on our strengths and further develop our areas of expertise for the benefit of all associated with the Group.

Kier Building Maintenance was praised for its diverse workforce and practices as winner of the first ever Diversity Award at the 10th Contract Journal Awards.

Objectives

The Board recognises that the Group's short and long-term economic development can and should be achieved only through a responsible approach to social, environmental and ethical issues (SEE). To this end it has identified the following objectives which are derived from the Board's assessment of the primary SEE risks and opportunities facing the Group:

1 To increase profitability by making more efficient use of resources, including labour, materials, water and energy.

2 To reduce the environmental impact of our operations through effective waste management, appropriate choice of materials and careful consideration of design and management of our supply chain.

3 To provide leadership in the raising of awareness and understanding of sustainability in our workforce, members of our supply chain, our clients and other stakeholders and to encourage participation in achieving our goals.

4 To continue to support local communities, through public consultation, by pursuing opportunities for employment, interaction with schools and support for local wellbeing.

5 To continue to recruit apprentices and graduates and to develop and train our workforce to raise aspirations and to meet the demands of the future.

6 To set targets to achieve greater sustainability year on year.

7 To provide a safe working environment for all our staff and the general public and to continuously strive to improve our health & safety performance.

The executive directors are responsible for the implementation of these objectives within their divisions and report to the Board periodically as to progress or when material issues arise. The Board is also kept informed of SEE issues through the mechanisms described further below.

Environmental

We are committed to our sustainability policy, to environmental protection and improved performance. The policy will be implemented in all that we do via the aims and objectives stated below:

- Strict compliance with the letter and intent of all relevant legal requirements, codes of practice and regulations.

- The organisation of our operations in order to minimise pollution and disturbance to our neighbours and the general public.

- The efficient use of materials and resources with particular regard to the long-term sustainability of consumable items, both directly and through our supply chain.

- Minimising the need to travel but where travel is unavoidable, consider the least environmentally damaging system.

- The establishment and maintenance of management structures with specific responsibility for the implementation of our sustainability policy within our operating companies and divisions.

- The establishment of targets to measure our environmental performance in key areas as set out on page 31.

- Regular management reviews of the content and implementation of environmental policy with the objective of achieving continuous improvement in performance through the ongoing establishment of best practice.

Individual operating companies have appointed directors responsible for the environmental policy, some of whom form the Group's Sustainability Committee chaired by Paul Sheffield. These directors monitor implementation and are responsible for the management of environmental risk providing regular reports to the Kier Group Board via John Dodds who is responsible for environmental matters.

The full Group environmental policy is available on our website, which also has details of environmental news and awards attained by our various businesses.

Kier in the community

Kier Group and its trading companies enjoy positive relationships within the communities where we operate and where our employees live.

We will seek to enhance these relationships by learning to understand the needs of these communities, supporting projects which increase well-being within the community. Wherever appropriate, we donate to local charities and sponsor many sports teams, supporting our own employees in their local fund-raising initiatives. We also donate the resources of our craft based teams to assist needy causes where their skills are best suited.

We will continue to put safety first and support our staff with occupational and lifestyle advice.

We carry out safety presentations for schools at every opportunity and have published educational literature aimed at pupils and young people and produced a range of supporting promotional merchandise.

Employment

In order for our business to be sustainable, Kier Group will continue to attract, develop and retain employees of the calibre to deliver our vision as the most highly respected Group in the marketplace. We are committed to offering good career opportunities for youngsters in construction skills through innovative apprenticeship and training programmes. These award-winning initiatives are based on recruiting young people from the local communities within which we work to offer on-the-job training delivered by our own experts. With good calibre people, upholding our core values, at the forefront of all our operations, we are focused on sustaining our business for the future and adding value for our clients, customers, shareholders and all those with whom we do business.

We are a committed equal opportunities employer. Our equality and diversity policy is available on our website. John Dodds is the director responsible for human resource matters, including health & safety. He meets regularly with the head of personnel and reports to the Board on any risks or issues that are identified.

Recognising the need to meet our commitment in the future to our past and present employees, we have taken significant steps this year to address our pensions deficit as described in more detail on page 24.

Training and people development

The Kier Group is committed to the lifelong development of all its employees. Our approach involves recruiting talented people into the industry, supported by a career development framework that supports people from entry level to senior leadership and prepares our teams to meet and exceed our customers' requirements. Our career development framework incorporates a series of programmes, supporting people at all stages of their careers.

At the introductory level of the career development programme, we recruited over 60 graduates and 70 students to start their professional careers with Kier. We offer a comprehensive and structured graduate scheme that includes technical and managerial training to recognised professional standards. This helps to motivate people in the Group to achieve their career goals, and to attract high levels of new recruits. The Group continues to work with schools, colleges, universities and careers advisors to promote the construction industry as a career choice and has over 100 people currently studying for technical qualifications on various training schemes having joined the Group as school leavers. We also have over 160 craft apprentices in construction skills. Over 10% of our workforce is on new entry training programmes, and this helps us to maintain and improve the talent of our workforce. This balanced approach will be enhanced further over the next year.

The Group actively encourages all employees to achieve full professional membership in their relevant discipline. To support this, the Group has in place a Graduate development programme taking graduate level employees to full membership in over 10 recognised professional institutions. Kier is a National Vocational Qualification (NVQ) centre, and is recognised by the Joint Awarding Body as a model of best practice for the delivery of NVQs in construction management. We currently have over 60 professional and technical staff working towards construction management NVQs. Additionally, we are delivering specialist plant operations NVQs at our Greenburn opencast mining site.

Safety training is a priority for all staff. Kier has introduced a comprehensive accredited safety training system covering all staff over the last year, with over 550 people attending accredited health & safety programmes in the last year. Our technical training is

Kier Caribbean and Industrial's Antiguan health & safety programme involves all members of the site team. Every operative spends a week working as part of the health & safety team, receives in-depth training in all aspects of site safety and sits an exam at the end of the week. All staff at the Sandals expansion project in Antigua have now received pass certificates in recognition of their health & safety awareness.

1. Former Home Secretary David Blunkett at the formal reopening of Kier Sheffield's Sharrow Industries workshop following its refurbishment. Sharrow Industries supplies all PVCu windows and kitchen furniture for the Sheffield Decent Homes programme. More than half of the 39 employees have disabilities or medical conditions ranging from auditory and visual impairment through to learning difficulties and epilepsy. Individual employee programmes of training, adaptation and support from organisations such as Work Step contribute to employee and business development on an ongoing basis. In the last year the workshop has produced 22,000 window units, 18,000 kitchen units, and 4,000 composite doors.

2. Phased reinstatement at our opencast coal mining operations at Greenburn in Ayrshire. To achieve maximum value from these operations, we are also extracting fireclay. This is then made into buff-coloured bricks for use by Kier Homes in the construction of their new developments in Scotland. This has reduced overall lorry movements and the end product blends sympathetically with local architecture.

based around the findings of various best practice groups and helps to disseminate knowledge around the Group.

Our management development programmes support the Group's aim of developing people within the business. During 2005 the number of promotions within Kier almost doubled from the previous year as people were prepared for more senior roles.

Kier has been running an Executive Leadership Programme based around defined competencies that is giving structured development to senior management and directors. This is linked to the Group's strategy of sharing best practice. During 2006, Kier has introduced a Directors Development Programme aimed at supporting our business leaders.

Health & Safety

Throughout the year Kier Group continued to build on the positive approach to health & safety that it values in all its employees and supply chain members. This approach, coupled with the Group's 'Don't Walk By' campaign and its ongoing focus on behavioural issues, has made everyone more vigilant and proactive in identifying and correcting health & safety issues, preventing them from becoming major problems. By addressing the risk and not the symptom, Kier has brought about significant reductions in its accident incident rate referred to on page 24.

In recognition, the Group received nine gold, two silver, and one bronze award from RoSPA and seven British Safety Council Awards.

Through their positive, proactive attitude, Kier Group's staff and supply chain work tirelessly to reduce the potential for accidents to happen, and to protect the long-term health of those working on Kier sites. The continuous roll-out of the ISO18001/14001 registration programme has ensured that high standards and awareness continue to be raised and the third party audit carried out by BSI ensures that the Group continues to deliver best practice.

This continuing improvement approach culminated in Kier Group being awarded the highly coveted Quality in Construction Health & Safety Management Award 2006. This was truly a magnificent team effort for both Kier Group's staff and supply chain.

Our health & safety policy, along with relevant news and awards can be found on our website. The Group head of safety, health & environment reports to the Board on a monthly basis in order that material issues, risks and developing trends are quickly addressed.

Customers

Good customer care is one of our fundamental principles and we have a high level of involvement with our customers and clients to give them every opportunity to provide valuable feedback. Many of our customers are included in project groups, surveys, conferences, workshops and social functions. Maintaining respect for our customers – who include the thousands of tenants in whose homes we frequently work – is based on the need to consult with and listen to them. We are committed to providing our customers and clients with a reliable service based on continuous improvement and delivering what we promise.

Environmental key performance indicators

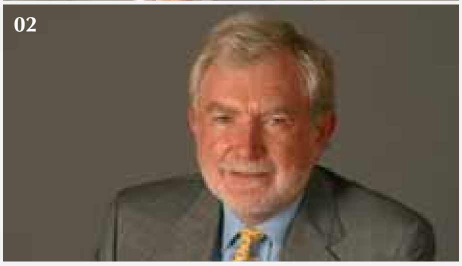
	Actual 03/04	Actual 04/05	**Actual 05/06**
Waste as % of Construction revenue	0.30	0.26	**0.30***
Energy use £/m^2 (including Support Services)	10.29	9.91	**13.24****
CO_2 emissions from staff vehicles (including Support Services)	8,972	8,412	**8,986**
Environmental training days per person/year	0.13	0.19	**0.10**
Infringements	2	0	**0**

* Cost of waste adjusted by 15% to allow for landfill tax increase
** No adjustment has been made to reflect increased energy costs over the year

Board members

01

02



03

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01 Peter Warry (non-executive chairman)
Aged 57, was appointed as non-executive chairman of the Group in November 2004, having joined as non-executive director in 1998, and is chairman of the Nomination Committee. He is also chairman of Victrex PLC and BSS Group PLC. Previously he was an executive director of British Energy plc and chief executive of its English generating company.

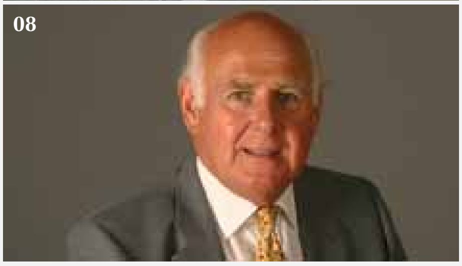
02 John Dodds (chief executive)
Aged 61, was appointed chief executive in May 2003 and has been with the Group since 1970. He has spent time working overseas particularly in Africa and Hong Kong returning to the UK to lead the civil engineering business. Following the employee buyout he was responsible for major projects, mining and international operations and was chairman of Kier Project Investment. He holds the position of director with overall responsibility for safety, health & environmental matters and is a member of the Nomination Committee.

03 Deena Mattar (finance director)
Aged 41, was appointed to the Board as an executive director in September 2001. She joined Kier in 1998 from KPMG where she developed an in-depth knowledge of construction. She held the role of finance director of the Group's major projects, mining and international projects arm until July 2001 and was appointed Group finance director in November 2001. She is also chairman of Kier Project Investment.

04 Ian Lawson
Aged 49, rejoined Kier in November 2000 as managing director of the Group's Infrastructure Investment operations, having previously held senior management positions elsewhere in the industry. His knowledge of major overseas and UK contracting was established early in his career within the Group. He was appointed managing director of Kier Eastern in July 2002 and joined the Kier Regional board in January 2003. He was promoted to the Support Services division as managing director in September 2004 and in October 2005 was appointed main board director responsible for Support Services.

05 Paul Sheffield
Aged 45, joined the Group as a graduate engineer in 1983. He has extensive knowledge of both UK and overseas contracting and was appointed managing director of Kier Construction in 2001, chairman of Kier Construction in 2003 and joined the Kier Regional board in 2004. He was appointed to the main board in October 2005 and has responsibility for the Group's infrastructure and overseas businesses as well as his position of deputy managing director of Kier Regional.

06 Dick Side
Aged 60, joined Wallis in 1983 as managing director of its Construction Division. His 23-year career with the Group has been spent in regional contracting and he was appointed managing director of Kier Regional in 2001. In January 2003 he became main board director responsible for the Group's Regional construction division.



07 Dick Simkin
Aged 58, joined the Group in 1989 and has made a significant contribution to strengthening Kier's presence in the property sector. He played a key part in the Group's acquisition of Laing Property and was appointed to the Board in January 2003 as director responsible for the Group's Property division.

08 Peter Berry (non-executive)
Aged 62, is chairman of The Crown Agents for Oversea Governments and Administrations. He is also chairman of Martin Currie Portfolio Investment Trust plc, a non-executive director of Henderson TR Pacific Investment Trust PLC and an advisor to the Corporation of London on international and economic development. He was appointed to the Board in 1997 and is senior independent director, chairman of the Remuneration Committee and a member of the Audit and Nomination Committees.

09 Simon Leathes (non-executive)
Aged 58, is vice chairman for support services at Barclays Capital, the investment banking division of Barclays PLC. He previously held senior appointments at Lend Lease Corporation, Hambros PLC and SG Warburg Group plc. He was appointed to the Board in March 2001 and is chairman of the Audit Committee and a member of the Nomination and Remuneration Committees.

10 Phil White (non-executive)
Aged 57, was appointed to the Board in July 2006. He served as chief executive of National Express Group plc from January 1997 to September 2006. He is a chartered accountant and has extensive experience of both listed and private companies. He is currently president of the Confederation of Passenger Transport and chairman of Lookers Plc. He is a member of the Audit, Nomination and Remuneration Committees.

11 Matthew Barton (company secretary)
Aged 32, was appointed company secretary in July 2005. He joined the Group in September 2004 as corporate counsel from lawyers Cleary, Gottlieb, Steen and Hamilton, where he advised the Group on a variety of issues. At Cleary Gottlieb he had a wide-ranging commercial practice including advising both public and private clients on major domestic and cross-border transactions. He is responsible for corporate governance within the Group and, as corporate counsel, has oversight of corporate legal affairs.

Directors' report

The directors present their annual report and audited financial statements for the year ended 30 June 2006.

Principal activities and business review

The Group's principal activities are construction, support services, residential and commercial development and infrastructure project investment.

A review of the Group's business and progress is given within the operating and financial review, on pages 14 to 28.

Results and dividends

The Group profit for the year after taxation was £42.9m (2005: £36.6m).

An interim dividend of 8.2p per share (2005: 7.0p) amounting to £2.9m (2005: £2.5m) was paid on 18 May 2006. The directors propose a final dividend of 17.8p per share (2005: 15.2p per share) amounting to £6.3m (2005: £5.4m) payable on 5 December 2006 to shareholders on the Register of Members at the close of business on 29 September 2006.

Share capital

Details of shares allotted by the Company during the year appear in note 22 to the consolidated financial statements.

Directors

The directors of the Company during the year are shown on pages 32 and 33. Mr M P Sheffield and Mr I M Lawson were appointed as directors on 1 October 2005. Mr P M White was appointed a director on 1 July 2006.

At the forthcoming Annual General Meeting resolutions will be proposed for the re-election of Mr P F Berry, Mr S W Leathes and Mr P T Warry. Mr P M White will be proposed for election for the first time.

Details of directors' interests are disclosed in the directors' remuneration report on page 42.

The Articles of Association of the Company provide for the indemnification of its directors out of the assets of the Company in the event that they suffer any loss or liability in the execution of their duties as directors and the Company has entered into deeds of indemnity with its directors entitling them to be indemnified to the extent permitted by statute.

The Company has insurance in favour of its directors and officers in respect of certain losses or liabilities to which they may be exposed due to their office.

Substantial shareholdings

At 13 September 2006 the Company had been notified of the following interests in the Ordinary Share Capital of the Company:

Barclays PLC	4.95%
Legal & General plc	3.29%

Employees

The companies in the Group are equal opportunity employers. The Group provides relevant information on matters of concern to employees through newsletters and formal and informal meetings with local management. The Group encourages and assists, whenever practicable, the recruitment, training and career development of disabled people and the retention of those who become disabled during the course of their employment and who can be employed in a safe working environment. The Company operates a Sharesave scheme for all eligible employees and makes available a dealing service to enable employees to buy and sell its shares with a minimum of formality and on attractive commission terms. The Group also operates an AESOP scheme for all employees.

Combined Code

A statement on corporate governance is set out on pages 36 to 38.

Going concern basis

After making enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.

Donations

Group cash donations to charity in the United Kingdom were £51,000 (2005: £73,000). In addition the Group spends considerable time and effort contributing to charitable events in the community. No political donations were made (2005: nil).

Policy on payment of creditors

The Group agrees payments with its suppliers and subcontractors on an individual contract basis rather than following a standard code. The policy is to abide by these agreed terms whenever it is satisfied that the suppliers or subcontractors have provided the goods or services in accordance with the contract terms and conditions. The aggregate amount owed to trade creditors by the Company at the end of the year was nil (2005: nil).

Subsidiary trading companies within the Group, acting in accordance with the above policy, exhibit creditor days averaging 37 (2005: 32) in respect of suppliers of invoiced goods and services and 20 (2005: 20) in respect of certified amounts due to subcontractors. These figures exclude amounts not currently due for payment but included within trade creditors.

Financial instruments

Details of the financial risk management objectives and policies of the Group along with its exposure to material financial risks are set out in notes 1 and 26 to the consolidated financial statements.

Auditors

A resolution for the reappointment of the auditors, KPMG Audit Plc, (KPMG) will be proposed at the Annual General Meeting. The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the auditors are unaware; and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Signed on behalf of the Board.

M D Barton
Secretary

13 September 2006
Tempsford Hall
Sandy
Bedfordshire
SG19 2BD

Corporate governance statement

The Code

The Board recognises the importance of high standards of corporate conduct and is committed to managing the Group's operations in accordance with the best principles of corporate governance as contained within Section 1 of the Combined Code on Corporate Governance (the Code) issued in July 2003 and has complied with the Code throughout the year except as explained below.

Throughout the reporting year, the Nomination Committee was not comprised of a majority of independent non-executive directors. This was addressed as at 1 July 2006 with the appointment of Mr P M White as a non-executive director to the Board along with the Remuneration, Nomination and Audit Committees.

Board of directors

The Board of Kier Group plc is responsible to its shareholders for the success of the Company. It sets the strategic and financial policies of the Group, monitors and reviews business performance and controls risk. As part of the Group's organisational structure (described on page 38 under 'Internal Control') the Board has put in place standing orders which are designed to ensure the provision to it of relevant information on a timely basis, which set authorisation limits and which reserve certain matters for the Board or its committees, including:

- strategy and financial policy;
- the approval of financial statements;
- risk management;
- major capital expenditure;
- major project approval;
- acquisitions and disposals; and
- certain aspects of human resource policy, including senior appointments, general salary reviews, employee share plans and pension provision.

The principal matters considered by the Board during the year included:

- the Group's budgets, strategy and financial requirements;
- the full and interim reports and accounts (taking into account the views of the Audit Committee), including the implications of the introduction of International Financial Reporting Standards;
- the appointments of Mr I M Lawson, Mr M P Sheffield and Mr P M White as directors (upon the recommendations of the Nomination Committee);
- appropriate measures to address the deficit in the Group's final salary pension scheme;
- the implications of and proper approach to the issues with the Castlepoint shopping centre car park;
- potential acquisitions, including Hugh Bourn Developments (Wragby) Limited and a commercial property portfolio from Warner Estates;
- the management and organisation of the Residential division;
- a review of the adequacy of Group standing orders, separation of authorities and reporting lines;
- health & safety strategies and particular issues as they arose; and
- presentations on divisional strategic issues from the senior management of each of the divisions.

The Group's chairman is Mr P T Warry who leads the Board, is responsible for its effectiveness and sets its agenda. He facilitates the effective contribution of the non-executive directors and ensures a positive and constructive relationship between the executive and non-executive directors. The chairman is also responsible for effective communication with shareholders.

The chief executive is Mr J Dodds who is responsible for the operational management of the Group and is accountable to the Board for the implementation of the Group's strategy. In order to facilitate this, the chief executive meets monthly with a management committee comprised of the other executive directors, he also chairs monthly management meetings with each of the divisions. As director responsible for human resource matters and health & safety he also meets regularly with the head of personnel and the Group head of safety, health & environment.

The senior independent non-executive director is Mr P F Berry.

Biographical details of all the directors are set out on pages 32 and 33. All the directors with the exception of Mr I M Lawson, Mr M P Sheffield and Mr P M White served throughout the year. The Board considers Mr P F Berry, Mr S W Leathes and Mr P M White to be independent. In considering the independence of the non-executive directors, the Board took into account the fact that as of April 2006, Mr P F Berry had held his directorship for nine years and concluded that this did not affect his independence. Mr P F Berry is standing for re-election at the forthcoming Annual General Meeting. He has however, informed the Board of his intention to retire as a non-executive director at the end of the financial year, after completing 10 years' service as a director. The Nomination Committee will shortly commence a search for a non-executive director to fill the vacancy created by Mr P F Berry's retirement.

A table of attendance of directors at meetings of the Board and its various committees is set out on page 37. In addition to these meetings, the full Board attends away-days which focus on strategy on a divisional basis, material issues facing the Group and succession planning. Outside of the formal schedule of meetings, the non-executive directors met without the executive directors a number of times during the year.

All directors have access to the advice and services of the company secretary and the directors are able to seek independent professional advice if necessary at the Company's expense. Training is available for new directors and other directors as necessary. Mr I M Lawson and Mr M P Sheffield attended a two-day seminar on corporate governance subsequent to their appointment. All directors are subject to election by shareholders at the first Annual General Meeting following their appointment, and to re-election thereafter at intervals of no more than three years. Executive directors are required to seek approval from the Board before accepting any external non-executive positions, although none is currently held.

Board evaluation

The chairman carried out an evaluation of the Board in the spring/summer of 2006 by way of an externally developed objective based questionnaire. This included all the committees of the Board. The chairman held individual meetings with each director to discuss their views and to canvass suggestions. The conclusions were discussed collectively by the Board and a number of minor operational improvements agreed. The Board separately reviewed the performance of the chairman without the chairman being present.

The terms and conditions of appointment of the non-executives are available for inspection at the registered office and will be on display prior to and at the Annual General Meeting.

Audit Committee

The Audit Committee comprises the three independent non-executive directors under the chairmanship of Mr S W Leathes, a chartered accountant with recent and relevant financial experience. Mr P M White was appointed to the Committee with effect from 1 July 2006. The Committee met three times during the year in September, March and June prior to the Board meetings. These Committee meetings were also attended by the finance director and the head of internal audit. The KPMG audit engagement director attended the September and March meetings. The chairman and executive directors were also invited to attend the meetings. The Committee also met with KPMG without the presence of the management.

The Committee has clearly defined terms of reference which outline its objectives and responsibilities relating to financial reporting, internal controls, risk management and the application of appropriate accounting policies and procedures. Specific responsibilities include reviewing and recommending for approval the annual and interim financial statements, reviewing the Group's accounting policies, reviewing the effectiveness of internal controls and risk management and reviewing the scope and results of the external audit.

The Audit Committee also has responsibility for overseeing the Group internal audit function including approval of the annual risk-based audit plan and monitoring the work, recommendations and effectiveness of the function. The head of internal audit reports directly to the chairman of the Audit Committee.

At each of its meetings the Committee received and reviewed a report from the head of internal audit which highlighted the status of the Group risk management processes and audit activity against the approved plan together with the findings from internal audits. The chairman of the Audit Committee also met regularly with the head of internal audit and the Committee has met with the head of internal audit without the presence of management. The Committee carried out a review of the effectiveness of the internal audit function at the June meeting.

The Committee is responsible for monitoring the independence and objectivity of KPMG, the external auditor, and agreeing the level of remuneration and extent of non-audit services. The Committee received a presentation from KPMG on its audit strategy and the scope of work at the March meeting which it agreed. It also discussed the firm's professional ethical standards.

The Committee reviewed the performance of KPMG and the level of non-audit fees paid to them during the year which are set out in note 3 to the consolidated financial statements. The provision of non-audit services, other than tax compliance and routine taxation advice, must be referred to and agreed by the Committee over a pre-determined cost threshold and any work costed below that threshold must be pre-approved by the Group finance director.

No consultancy related work has been carried out by the auditors during the year. The Committee was satisfied, following its review, that KPMG's objectivity and independence had not been impaired.

The Committee agreed and approved the audit fee at the June meeting following discussions between divisional management and the divisional KPMG audit teams.

The Committee's terms of reference are reviewed annually and were updated in 2004 in line with the guidance and recommendations of the revised Combined Code. The terms of reference are available on request and on the Company's website.

Remuneration Committee

The Remuneration Committee comprises the three independent non-executive directors, under the chairmanship of Mr P F Berry. Mr P M White was appointed to the Committee with effect from 1 July 2006.

Information about the workings of this Committee is contained in the directors' remuneration report on page 39. The Committee makes recommendations to the Board on the Company's framework of executive remuneration and determines, on its behalf, specific remuneration packages for each of the executive directors and the chairman. In doing so it takes the advice of independent external consultants. The terms of reference are available on the Company's website.

Nomination Committee

The Nomination Committee presently comprises the chairman, the chief executive and the non-executive directors.
Mr P M White was appointed to the Committee with effect from 1 July 2006. It is responsible for monitoring the composition and balance of the Board, making recommendations to the Board on new Board appointments and succession planning. The Committee met four times during the year. Recruitment consultants were retained in relation to the appointment of Mr P M White. The Committee's terms of reference are available on the Company's website.

Board and Committee Meetings

Details of the number of meetings of, and attendances at, the Board, the Audit, Remuneration and Nomination Committees are set out in the table below.

Name of director	Board – (11)	Audit – (3)	Remuneration – (3)	Nomination – (4)
P T Warry	11	–	–	4
J Dodds	11	–	–	4
I M Lawson[1]	8	–	–	–
D E Mattar	11	–	–	–
M P Sheffield[1]	8	–	–	–
R W Side	11	–	–	–
R W Simkin	11	–	–	–
P F Berry	11	3	3	4
S W Leathes	11	3	3	4

[1] Mr I M Lawson and Mr M P Sheffield were appointed on 1 October 2005

Internal control

The Combined Code requires that the directors review the effectiveness of the Group's system of internal control. This extends the directors' review to cover all material controls, including operational, compliance and financial controls and risk management systems. The directors are satisfied that procedures are in place to ensure that the Group complies with the Turnbull Committee guidance published by the Institute of Chartered Accountants in England and Wales and that the procedures have been applied during the year.

The Board of directors has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. The Board considers that the Group's systems and controls are appropriately designed to ensure that the Group's exposure to significant risks is properly managed. However, such a system is designed to manage rather than eliminate the risks of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement. In reviewing the effectiveness of internal controls, which have been developed and refined over many years, the directors have considered the key risks and exposures within the Group.

The key features of the Group's system of internal controls and principal controls are:

- an established management structure operating throughout the Group with clearly defined levels of responsibility and delegation of authorities;

- clearly defined operating guidelines and procedures with authorisation limits set at appropriate levels. These are set out in the Group and divisional standing orders;

- a comprehensive budgeting and forecasting system in place which is regularly reviewed and updated;

- a formal quarterly review of each division's year-end forecast, business performance, risk and internal control matters is carried out by the directors of each division with the chief executive and finance director in attendance;

- monthly management reporting including regular comparison of actual results against latest forecasts;

- established policies and procedures governing the Group's investment in land, property and other significant assets, including acquisitions and disposals. These include detailed appraisals, appropriate authorisation levels and Board approval depending on value or perceived exposure;

- investment decisions, including Private Finance Initiative (PFI) projects and tenders for contracts are subject to approval by the Board, the chief executive and finance director or divisional directors depending on the value and nature of the investment or contract. Individual tender and project review procedures are in place prior to bidding and before contract award;

- internal audits are carried out to assess the adequacy and effectiveness of internal controls. The scope of the internal audit work is planned to cover the key risks faced by the business and supplemented by cyclical reviews of the core financial process. Internal audit findings are reported to the Audit Committee and the executive directors on a regular basis;

- risk registers are in place for each business unit which highlight the key risks facing that business together with an assessment of the effectiveness of controls to mitigate those risks. The risk registers are updated regularly and at 31 March;

- an annual process of risk and control self assessment is used in the Group whereby all operating companies are required to review and confirm that appropriate internal controls are in place and operating effectively across the key risk areas identified in individual company risk registers. This assessment was carried out on 31 March 2006 and the findings reviewed by the Audit Committee;

- regular monitoring, review and reporting of safety, health & environmental matters; and

- the provision of a confidential method of reporting any suspected fraud or other misfeasance to the head of internal audit.

The Board receives regular reports from all operating units to monitor their performance and all directors are properly briefed on issues arising at Board meetings.

During the course of the year members of the Board visit all companies and monitor the control framework of each business. The Audit Committee reviews the appropriateness and effectiveness of internal controls.

Relations with shareholders

The Board uses the Annual General Meeting to communicate with shareholders and encourages their attendance and participation. The chairmen of the Audit Committee and the Remuneration Committee are available to answer questions from shareholders. The Group also maintains a regular dialogue with institutional investors to assist in the understanding of the Group's objectives and the Company has a programme of regular communication with investors, analysts and brokers. Presentations are made to investors, analysts and press at the time of the announcement of the final and half-year results and there are regular meetings with analysts and investors which are arranged through the Company's brokers so that the investment community can be kept informed. The Board is provided with independent feedback from analysts and institutional shareholders periodically.

The Kier website is also maintained to aid communication with investors, employees, customers, suppliers and the general public.

Directors' remuneration report

The Remuneration Committee

The Remuneration Committee is a Board committee consisting entirely of independent non-executive directors. The following directors were members of the Committee for the year ended 30 June 2006:

Mr P F Berry (chairman)
Mr S W Leathes

Mr P M White was appointed as a non-executive director on 1 July 2006 and became a member of the Remuneration Committee on that date.

The secretary of the Committee is Mrs A Sale, the head of personnel.

The terms of reference of the Committee are available on the Group's website and on request from the company secretary. The Committee meets when necessary, but not less than once a year. The Committee consults the Group chairman and chief executive concerning its proposals (except in relation to their own remuneration) and takes external professional advice as appropriate. In respect of the year ended 30 June 2006 the Committee appointed New Bridge Street Consultants LLP as its independent remuneration advisors. New Bridge Street Consultants LLP provides no other service to the Company. Where necessary, or appropriate, the Committee instigates consultation with major institutional shareholders on remuneration matters.

Remuneration policy

The Committee makes recommendations to the Board on executive remuneration policy for adoption by the Board and determines specific remuneration packages for each of the executive directors on behalf of the Board. The Committee also monitors remuneration packages of other senior executives throughout the Group. Remuneration and benefits are set at market levels comparable with companies of similar size and scope of activity in order to be able to attract, retain and motivate high calibre individuals. The Committee's policy is to maintain an appropriate balance between fixed elements of remuneration (basic salary, benefits in kind and pension) and performance-related elements (annual bonus and long-term incentives) and to place much greater emphasis on rewarding executives by reference to the Group's long-term performance rather than its short-term results. The Committee and Board encourage directors and staff at all levels to acquire shares in the Company and to hold them for the longer term. This sense of ownership is an important element of Kier's culture and of its focus on long-term performance. As far as possible the Group prefers to promote individuals from within. The remuneration received by each of the directors, together with details of share interests and pension benefits, are set out on pages 41 to 43.

Executive directors' remuneration consists of a basic salary together with an annual bonus, benefits in kind, awards under a Long-Term Incentive Plan (LTIP), and membership of a pension scheme. The remuneration components are set out below:

Basic salary

Salaries for executive directors take account of external market data, as described above, the individual's responsibilities, experience and performance. Salaries are reviewed annually.

Benefits in kind

Benefits in kind comprise membership of private health insurance, provision of a fuel card and the provision of a company car or a car allowance.

Annual bonus arrangements

A bonus is paid to all executive directors at a percentage of annualised basic salary (not exceeding 20% for the year ended 30 June 2006) if Group pre-tax profit attains targets pre-set each year. These targets are agreed by the Committee; they are not published externally for reasons of commercial confidentiality.

Retirement benefits

Executive directors participate in the final salary section of the Kier Group Pension Scheme. Prior to 6 April 2006 ('A' day), in cases where the executive directors' pensionable pay was limited by the earnings cap provisions of the Finance Act 1989, the director was paid a salary supplement above the earnings cap to reflect the loss of pension coverage. This supplement is recorded in the directors' emoluments table and is not taken into account in determining bonuses or any other form of remuneration.

Post 5 April 2006, all executive directors will be able to accrue pension up to the value of the lifetime allowance. Where the value of pension exceeds the lifetime allowance, future pension accrual will cease and executive directors will receive a pension allowance of 20% of salary. Executive directors whose pensionable pay was previously subject to the earnings cap, will remain capped for benefits accrued pre 6 April 2006.

Only the basic salary of directors is pensionable. Details of individual directors' pension arrangements are shown in a separate table on page 41.

Long-term incentives

Under the Kier Group 1999 LTIP directors can receive awards of shares worth up to 100% of salary per annum. Awards granted in the year to 30 June 2006 are subject to the Group achieving the following adjusted earnings per share growth targets:

- the directors will receive 100% of the award if earnings per share increase by at least 20% per annum in excess of inflation (the maximum target) over the relevant three-year performance period;
- no awards will vest unless earnings per share over the same period increase by at least 5% per annum in excess of inflation (the base target) at which point 25% of the award will vest; and
- the proportion of the awards which will vest for performance between the base target and the maximum target will be calculated on a straight line basis.

The above targets were selected by the Committee to ensure that the Group would have to attain a substantial improvement in underlying financial performance before the awards could vest. Growth in earnings per share is the key performance measure used by the Group. The attainment of the performance targets is verified by the Remuneration Committee and reviewed by the Company's auditors. The calculation for earnings per share is carried out on a consistent basis such that the opening and closing earnings per share will both be calculated under UK Generally Accepted Accounting Practice (GAAP) or both under International Financial Reporting Standards, as appropriate at the time.

24.4% of executive directors' remuneration for the year to 30 June 2006 was represented by the vesting under the LTIP on the basis of the share values at the time of the vesting. This calculation includes lower levels of award for directors within three years of their appointment to the Board.

The Remuneration Committee has set a policy whereby it encourages executive directors to build up a shareholding in the Company equal to at least one year's salary over a period of up to five years.

Service contracts

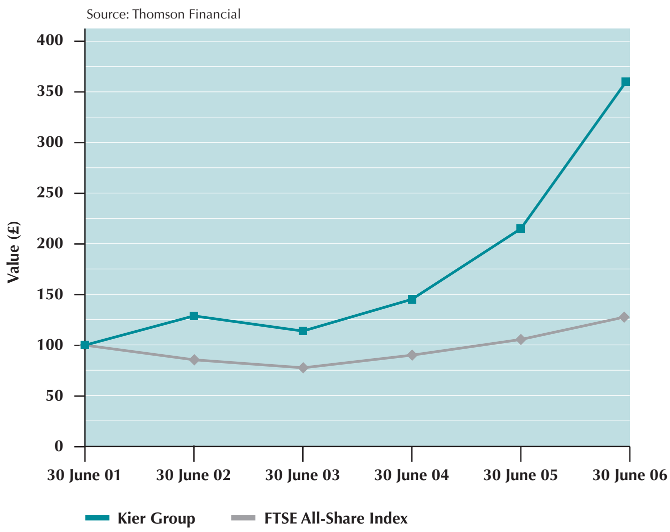
The Company has service agreements with its executive directors which have a notice period of one year. In the event of early termination of their service agreements, the executive directors are entitled to compensation of up to one year's salary. As stated in the corporate governance statement, executive directors are required to seek approval from the Board before accepting any external non-executive positions. Any emoluments arising from such positions are taken into account by the Remuneration Committee. Currently no external non-executive positions are held by executive directors.

Non-executive directors

The remuneration of the non-executive directors is determined by the Board and reflects the anticipated time commitment to fulfil their duties. Non-executive directors do not receive bonuses, long-term incentive awards, pension provision or compensation on termination of their appointment.
The Company has agreements for services with each of the non-executive directors, all of which are terminable on no more than 12 months' notice by either party.

Total shareholder return

The following graph charts total cumulative shareholder return of the Company over the last five financial years. The index selected was the FTSE All-Share Index as the Company has been a constituent throughout the period.



The graph shows the value, by 30 June 2006, of £100 invested in Kier Group plc on 30 June 2001 compared with the value of £100 invested in the FTSE All-Share Index. The other points plotted are the values at intervening financial year-ends.

Audited information

Except for the disclosure on directors' interests the following information on pages 41 to 43, has been audited by the Company's auditors, KPMG Audit Plc.

Directors' emoluments

The value of all emoluments receivable by each director in respect of the year ended 30 June 2006 was as follows:

	Salary and fees £000	Benefits £000	Bonus £000	**2006 £000**	Total 2005 £000
P T Warry[1]	104	1	–	**105**	74
J Dodds[2]	387	20	70	**477**	379
P F Berry	35	–	–	**35**	30
I M Lawson[3]	125	8	36	**169**	–
S W Leathes	33	–	–	**33**	30
D E Mattar[2]	256	20	50	**326**	308
M P Sheffield[3]	125	6	36	**167**	–
R W Side[2]	242	15	50	**307**	270
R W Simkin[2]	240	16	47	**303**	280
C R W Busby[4]	–	–	–	–	48
R W Gregory[5]	–	–	–	–	203
	1,547	86	289	**1,922**	1,622

1 Mr P T Warry was appointed chairman on 27 November 2004.
2 Salary includes a pension-related salary supplement explained in the pensions section below. The supplement included above was £52,500 for Mr J Dodds, £20,410 for Miss D E Mattar, £12,500 for Mr R W Side and £11,450 for Mr R W Simkin.
3 Mr I M Lawson and Mr M P Sheffield were appointed to the Board on 1 October 2005.
4 Mr C R W Busby retired on 13 December 2004.
5 Mr R W Gregory resigned from the Board on 27 April 2005 and, in addition to the above, he received a settlement of £276,140. Consequently his emoluments for the year ended 30 June 2005 were £479,140.

Directors' pensions

Pension benefits earned by the directors during the year as members of the Kier Group Pension Scheme (the Scheme) are disclosed below.

	Increase in accrued pension over the year £000	Increase in accrued pension over the year (adjusted)[1] £000	Transfer value of increase in accrued pension[2] £000	Accumulated total accrued pension at 30 June 2006 £000	Transfer value of accrued pension at 30 June 2005 £000	Increase in transfer value[2] £000	Transfer value of accrued pension at 30 June 2006 £000
J Dodds[8]	26	21	415	228	3,716	884	4,600
I M Lawson[7]	7	6	54	19	97	107	204
D E Mattar[4]	5	5	35	30	165	54	219
M P Sheffield	18	17	124	58	256	160	416
R W Side[6]	27	24	352	145	2,012	629	2,641
R W Simkin[4]	6	5	66	61	835	173	1,008

1 The increase in a member's accrued pension over the year shown above is the adjusted figure after allowing for inflation during the year.
2 Transfer values have been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11 less directors' contributions.
3 Members also have the option to pay additional voluntary contributions. Neither these contributions nor resulting benefits are included in the above table.
4 In addition to the above pension benefits, the salary and fees paid to Miss D E Mattar and Mr R W Simkin for the period to 5 April 2006 included a pensionable allowance equal to 20% of salary in excess of the statutory earnings cap.
5 All member contributions to the Scheme are payable via a salary sacrifice arrangement.
6 Mr R W Side was granted an augmentation to his scale pension of £6,500 pa during the year. At 6 April 2006, Mr R W Side elected for enhanced protection under the new HMRC rules and will accrue no further pensionable service in the Scheme after this date. He receives a pensionable allowance of 20% of salary in compensation for this change.
7 Mr I M Lawson elected to transfer benefits into the Scheme during the year. The accrued pension and transfer value as at 30 June 2006 make allowance for this transfer in.
8 Mr J Dodds reached his normal retirement date on 21 September 2005. Any increase in his accrued pension after this date is due to the application of an actuarial late retirement factor to compensate him for late payment of his benefits. For the period after 21 September 2005, he receives a pensionable allowance equal to 20% of salary.

Directors' interests

The directors of the Company at 30 June 2006 had the following beneficial interest (including interests of dependent family members) in the Ordinary Shares of the Company:

	30 June 2006	1 July 2005 (or date of appointment)
P T Warry (chairman)	**7,737**	7,595
J Dodds (chief executive)	**587,262**	576,566
P F Berry (non-executive)	**6,650**	6,650
I M Lawson[1]	**3,893**	3,773
S W Leathes (non-executive)	**10,000**	10,000
D E Mattar	**68,795**	57,946
M P Sheffield[1]	**19,148**	20,274
R W Side	**168,299**	162,286
R W Simkin	**284,114**	281,909

[1] The opening position of the interests of Mr I M Lawson and Mr M P Sheffield are shown as at 1 October 2005 being the date of their appointment.

Mr R W Side had a non-beneficial interest in 5,878 Ordinary Shares at 30 June 2006 (1 July 2005: 5,770).

In addition, the executive directors, as potential beneficiaries of the Kier Group 1999 Employee Benefit Trust, are deemed along with all other UK employees to have an interest in 355,167 (2005: 256,331) Ordinary Shares with a nominal value of £3,552 (2005: £2,563) representing 0.99% of the called up share capital of the Company, held by the Trust.

At 13 September 2006 the following directors had acquired beneficial interests in further Ordinary Shares: Mr J Dodds, 23 shares; Mr I M Lawson, 23 shares; Miss D E Mattar, 23 shares and Mr R W Side, 23 shares. There had been no changes in the interests of the other directors since 30 June 2006.

Directors' share options

Mr J Dodds, Mr I M Lawson, Miss D E Mattar and Mr M P Sheffield each held 590 Sharesave Scheme Options granted on 29 October 2003 at an exercise price of 625p. The Sharesave Scheme Options are, as for all company employees under the scheme, not subject to a performance condition. The options are exercisable from 1 January 2007 until 1 July 2007.

LTIP

Outstanding awards made to executive directors of the Company under the LTIP are in the form of a deferred right to acquire, at no cost, the following maximum number of Ordinary Shares in the Company:

				Cumulative Total	
	2004 award	2005 award	2006 award	30 June 2006	30 June 2005
J Dodds	21,912	33,798	24,647	80,357	79,640
I M Lawson	5,000	7,500	12,676	25,176	12,878
D E Mattar	16,733	24,141	17,605	58,479	63,022
M P Sheffield	5,000	7,500	12,676	25,176	16,238
R W Side	15,537	24,141	17,605	57,283	49,678
R W Simkin	14,342	23,068	16,549	53,959	42,410
Date of award	1 October 2003	1 December 2004	3 October 2005		
Share price	627.5p	699.0p	1065.0p		
End of performance period	30 June 2006	30 June 2007	30 June 2008		

For the 2003 and 2004 awards, 25% of the award vests if earnings per share grows by at least 7.5% per annum compound over the performance period, increasing on a sliding scale to 100% vesting if growth is at least 25% per annum compound. For the 2005 and 2006 award, 25% of the award vests if earnings per share grows by at least 5% per annum in excess of inflation over the performance period, increasing on a sliding scale to 100% vesting if growth is at least 20% per annum in excess of inflation.

Directors' interests, continued

For the three-year period ended 30 June 2005 earnings per share increased by 19.68% per annum compound. Accordingly the directors received 74.77% of the 2003 award (granted on 1 October 2002 when the share price was 451.5p) and were entitled to receive a combination of shares, at no cost, and cash. Shares vested during the year in executive directors of the Company under the 2003 award of the LTIP, together with the cash element received, were:

	2003 award number	Shares lapsed number	Shares vested number	Received as shares number	Market price pence	Received as cash £	Total LTIP award £
J Dodds	23,930	6,038	17,892	10,556	1065	78,128	190,549
I M Lawson	5,000	1,262	3,738	2,205	1065	16,326	39,809
D E Mattar	22,148	5,588	16,560	9,770	1065	72,314	176,365
M P Sheffield	5,000	1,262	3,738	2,205	1065	16,326	39,809
R W Side	10,000	2,523	7,477	4,411	1065	32,653	79,630
R W Simkin	5,000	1,262	3,738	2,205	1065	16,326	39,809
							565,971
						2005:	491,474

For the three-year period ended 30 June 2006 earnings per share increased by 20.60% per annum compound. Accordingly the directors will receive 79.01% of the 2004 award and will be entitled to receive the number of shares set out below, at no cost, on 29 September 2006 on which income tax and national insurance will be payable.

	Number of shares
J Dodds	17,312
I M Lawson	3,950
D E Mattar	13,220
M P Sheffield	3,950
R W Side	12,275
R W Simkin	11,331

Approval of report

As in previous years, Mr P F Berry, chairman of the Remuneration Committee, intends to attend the forthcoming Annual General Meeting and will be available to answer any questions shareholders may have concerning the Group's policy on directors' remuneration. The directors' remuneration report will be submitted for approval by the Company at the forthcoming Annual General Meeting.

Signed on behalf of the Board

P F Berry
Chairman Remuneration Committee

Statement of directors' responsibilities

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

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRS as adopted by the EU and have elected to prepare the parent company financial statements in accordance with UK Accounting Standards.

The Group financial statements are required by law and IFRS as adopted by the EU to present fairly the financial position and the performance of the Group; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

The parent company financial statements are required by law to give a true and fair view of the state of affairs of the parent company.

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

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- for the Group financial statements, state whether they have been prepared in accordance with IFRS as adopted by the EU;
- for the parent company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a directors' report, directors' remuneration report and corporate governance statement that comply with that law and those regulations.

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

Independent auditors' report to the members of Kier Group plc

We have audited the Group and parent company financial statements (the financial statements) of Kier Group plc for the year ended 30 June 2006 which comprise the consolidated income statement, the consolidated statement of recognised income and expense, the consolidated balance sheet, the company balance sheet, the consolidated cash flow statement and the related notes. 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 auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards as adopted by the EU (IFRS), and for preparing the parent company financial statements and the directors' remuneration report in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities on page 44.

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

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the Group financial statements, Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the directors' report is consistent with the financial statements. The information given in the directors' report includes that specific information presented in the operating and financial review that is cross referenced from the business review section of the directors' report. We also report to you if in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We 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 other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the directors' remuneration report to be audited. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and 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 to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the directors' remuneration report to be audited.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRS of the state of the Group's affairs as at 30 June 2006 and of its profit for the year then ended;

- the parent company financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the parent company's affairs as at 30 June 2006;

- the financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the Group financial statements, Article 4 of the IAS Regulation; and

- the information given in the directors' report is consistent with the financial statements.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
London
13 September 2006

Consolidated income statement for the year ended 30 June 2006

	Notes	2006 £m	2005 £m
Revenue – continuing operations			
Group and share of joint ventures	2	**1,838.3**	1,623.2
Less share of joint ventures		**(55.1)**	(50.2)
Group revenue		**1,783.2**	1,573.0
Cost of sales		**(1,623.7)**	(1,433.8)
Gross profit		**159.5**	139.2
Administrative expenses		**(103.5)**	(91.1)
Share of post tax profits from joint ventures	14	**3.2**	0.9
Profit from operations	2	**59.2**	49.0
Other non-operating income (exceptional items)	4	**–**	6.7
Finance income	5	**5.3**	4.0
Finance cost	5	**(5.4)**	(5.2)
Profit before tax	2	**59.1**	54.5
Income tax	9	**(16.2)**	(17.9)
Profit for the year		**42.9**	36.6
Earnings per share	11		
– basic		**120.8p**	103.4p
– diluted		**118.8p**	102.5p
Underlying earnings per share (excluding other non-operating income – exceptional items)			
– basic		**120.8p**	96.6p
– diluted		**118.8p**	95.8p

Consolidated statement of recognised income and expense for the year ended 30 June 2006

	Notes	2006 £m	2005 £m
Foreign exchange translation differences		**(0.3)**	0.1
Fair value movements in cash flow hedging instruments		**4.1**	–
Actuarial gains and losses on defined benefit pension schemes		**30.0**	(41.5)
Deferred tax on items recognised directly in equity		**(10.2)**	12.5
Income and expense recognised directly in equity		**23.6**	(28.9)
Profit for the year		**42.9**	36.6
Total recognised income and expense for the year	23	**66.5**	7.7
Change in accounting policy			
Effect of adoption of IAS 32 and IAS 39 on 1 July 2005 (with June 2005 not restated)			
on cash flow hedge reserve		**(7.5)**	–
Deferred tax on above		**2.2**	–
		61.2	7.7

Consolidated balance sheet
at 30 June 2006

	Notes	2006 £m	2005 £m
Non-current assets			
Intangible assets	12	**14.8**	16.7
Property, plant and equipment	13	**78.5**	75.8
Investment in joint ventures	14	**20.8**	22.9
Retirement benefit surplus	8	**6.8**	1.8
Deferred tax assets	15	**20.9**	38.3
Other financial assets	26	**0.6**	–
Trade and other receivables	18	**16.1**	14.6
Non-current assets		**158.5**	170.1
Current assets			
Inventories	16	**377.8**	325.7
Other financial assets	26	**0.6**	–
Trade and other receivables	18	**258.4**	233.3
Cash and cash equivalents	19	**141.3**	93.5
Current assets		**778.1**	652.5
Total assets		**936.6**	822.6
Current liabilities			
Bank overdrafts and loans	19	**–**	(5.3)
Trade and other payables	20	**(670.5)**	(566.5)
Tax liabilities		**(2.7)**	(9.5)
Provisions	21	**(0.9)**	(1.2)
Current liabilities		**(674.1)**	(582.5)
Non-current liabilities			
Long-term borrowings	19	**(30.1)**	(30.1)
Trade and other payables	20	**(36.8)**	(17.2)
Retirement benefit obligations	8	**(67.0)**	(123.7)
Provisions	21	**(18.1)**	(16.3)
Deferred tax liabilities	15	**(2.0)**	–
Non-current liabilities		**(154.0)**	(187.3)
Total liabilities		**(828.1)**	(769.8)
Net assets	2	**108.5**	52.8
Equity			
Share capital	22	**0.4**	0.4
Share premium	23	**20.0**	17.9
Capital redemption reserve	23	**2.7**	2.7
Retained earnings	23	**88.0**	31.7
Cash flow hedge reserve	23	**(2.4)**	–
Translation reserve	23	**(0.2)**	0.1
Total equity		**108.5**	52.8

The financial statements were approved by the Board of directors on 13 September 2006 and were signed on its behalf by:

J Dodds
D E Mattar
Directors

Consolidated cash flow statement
for the year ended 30 June 2006

	Notes	2006 £m	2005 £m
Cash flows from operating activities			
Profit before tax		**59.1**	54.5
Adjustments			
Other non-operating income (exceptional items)		**–**	(6.7)
Share of post tax profits from joint ventures	14	**(3.2)**	(0.9)
Normal contributions to pension fund in excess of pension charge		**(0.2)**	(0.1)
Share-based payments charge	24	**1.1**	0.6
Amortisation of intangible assets	12	**1.9**	1.9
Depreciation charges	13	**13.5**	12.3
Profit on disposal of property, plant & equipment		**(1.1)**	(0.5)
Net finance cost	5	**0.1**	1.2
Operating cash flows before movements in working capital		**71.2**	62.3
Special contributions to pension fund		**(31.5)**	(12.0)
(Increase)/decrease in inventories		**(49.3)**	19.7
Increase in receivables		**(26.7)**	(16.7)
Increase in payables		**131.8**	31.3
Increase in provisions		**1.1**	1.8
Cash inflow from operating activities		**96.6**	86.4
Interest received		**5.3**	3.7
Income taxes paid		**(11.3)**	(12.8)
Net cash generated from operating activities		**90.6**	77.3
Cash flows from investing activities			
Proceeds from sale of property, plant & equipment		**4.6**	6.0
Proceeds from sale of investments		**1.4**	5.8
Refinancing of PFI joint venture		**–**	8.1
Dividends received from joint ventures	14	**1.3**	0.4
Purchases of property, plant & equipment		**(23.2)**	(19.9)
Acquisition of subsidiaries	29	**(10.1)**	(16.5)
Investment in joint ventures	14	**(0.6)**	(1.5)
Net cash used in investing activities		**(26.6)**	(17.6)
Cash flows from financing activities			
Proceeds from the issue of share capital		**–**	0.2
Purchase of own shares		**(2.0)**	(0.4)
Interest paid		**(2.7)**	(2.6)
Dividends paid		**(6.2)**	(6.4)
Net cash used in financing activities		**(10.9)**	(9.2)
Net increase in cash and cash equivalents		**53.1**	50.5
Opening net cash and cash equivalents		**88.2**	37.7
Closing net cash and cash equivalents		**141.3**	88.2
Reconciliation of net cash flow to movement in net funds			
Net increase in cash and cash equivalents		**53.1**	50.5
Opening net funds		**58.1**	7.6
Closing net funds		**111.2**	58.1
Net funds consist of:			
Cash and cash equivalents		**141.3**	93.5
Overdrafts		**–**	(5.3)
Net cash and cash equivalents		**141.3**	88.2
Long-term borrowings		**(30.1)**	(30.1)
Net funds	19	**111.2**	58.1

Notes to the consolidated financial statements

1 Significant accounting policies

Kier Group plc (the Company) is a company domiciled in the United Kingdom (UK). The consolidated financial statements of the Company for the year ended 30 June 2006 comprise the Company and its subsidiaries (together referred to as the Group) and the Group's interest in jointly controlled entities.

The consolidated financial statements were approved by the directors on 13 September 2006.

Statement of compliance

The Group's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as adopted for use in the EU (IFRS). The Company has elected to prepare its parent company financial statements in accordance with UK Generally Accepted Accounting Practice (GAAP). These are presented on pages 74 to 77.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance, and cash flows of the Group, and reconciliations of total equity and profit for the comparative period reported under UK GAAP to those reported under IFRS is given in note 31.

Basis of preparation

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Group's financial statements with the exception of certain policies subject to the transitional arrangements of IFRS, as detailed below.

The financial statements are presented in pounds sterling. They have been prepared on the historical cost basis except for derivative financial instruments which are stated at their fair value and certain payables on extended terms which are stated at discounted cost.

In March 2005, the International Financial Reporting Interpretations Committee (IFRIC) issued draft guidance on accounting for service concession arrangements (drafts D12 to D14). IFRIC are currently considering the comments received on this draft guidance, with the final guidance expected to be issued in late 2006. Until the final guidance is issued and endorsed by the EU and in absence of specific guidance within IFRS, the Group has continued to account for PFI assets in the same way as previously accounted for under UK GAAP. This measures PFI contract assets (i.e. property, plant and equipment and finance debtors) on the basis of historical cost. However following the introduction of IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement', the interest rate swaps held by the PFI joint ventures for the purpose of hedging floating rate liabilities are measured at fair value both initially and subsequently. If the IFRIC draft interpretations are finalised in the current form, to the extent that PFI contract assets are recognised as financial assets (finance debtors) they also may be measured initially and subsequently at fair value.

In addition at the date of issue of these financial statements the following standards and interpretations, which have not been applied in these financial statements, were in issue but not yet effective:

IFRS 6	Explorations for and Evaluation of Mineral Resources.
IFRS 7	Financial Instruments: Disclosures: and the related amendments to IAS 1 'Presentation of Financial Statements' on capital disclosures.
IFRS 39	Amendments to fair value option, forecast intra-group transactions and financial guarantee contracts.
IFRIC 4	Determining whether an Arrangement contains a lease.
IFRIC 5	Right to Interest arising from Decommissioning, Restoration and Environmental Rehabilitation Funds.
IFRIC 8	Scope of IFRS 2.
IFRIC 9	Reassessment of Embedded Derivatives.

The directors anticipate that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements of the Group, except for additional disclosures on capital and financial instruments when the relevant standards come into effect for periods commencing on or after 1 January 2007.

Transition to IFRS

IFRS 1 'First-time Adoption of International Financial Reporting Standards' sets out the procedures that the Group must follow when it adopts IFRS for the first time as the basis for preparing its consolidated financial statements.

The Group is required to establish its IFRS accounting policies as at 30 June 2006 and, in general, apply these retrospectively to determine the IFRS opening balance sheet at its date of transition, 1 July 2004.

IFRS 1 provides a number of optional exemptions to this general principle. The most significant of these are set out below together with a description, in each case, of the exemption adopted by the Group.

Business combinations that occurred before the opening IFRS balance sheet date

The Group has elected not to apply IFRS 3 'Business Combinations' retrospectively to business combinations that took place before the date of transition. As a result, in the opening balance sheet, goodwill arising from past business combinations of £5.2m remains as stated under UK GAAP at 1 July 2004.

Employee benefits – actuarial gains and losses

The Group has elected to recognise all cumulative actuarial gains and losses in relation to employee benefit schemes at the date of transition. The Group has chosen to early adopt the amendments to IAS 19 'Employee Benefits' and has recognised actuarial gains and losses in full directly to reserves via the statement of recognised income and expense in the period in which they occur.

1 Significant accounting policies, continued

Share-based payments
The Group has elected to apply IFRS to relevant share-based payment transactions only where rights were granted after 7 November 2002 and not vested as at 1 January 2005.

Financial instruments
The Group has taken advantage of the exemption in IFRS 1 that enables the Group to apply IAS 32 and IAS 39 from 1 July 2005 only, with no restatement for prior periods. A reconciliation of total equity at 1 July 2005 following the adoption of IAS 32 and IAS 39 is given in note 31.

Cumulative translation differences
The Group has elected to set the previously accumulated translation differences relating to investments in overseas subsidiaries to nil at 1 July 2004.

Basis of consolidation
a) Subsidiaries
The consolidated financial statements comprise the financial statements of the Company and subsidiaries controlled by the Company drawn up to 30 June 2006. Control exists when the Group has direct or indirect power to govern the financial and operating policies of an entity so as to obtain economic benefits from its activities. Subsidiaries are included in the consolidated financial statements from the date that control transfers to the Group until the date that control ceases. The purchase method is used to account for the acquisition of subsidiaries.

b) Joint ventures
A joint venture is a contractual arrangement whereby the Group undertakes an economic activity that is subject to joint control with third parties.

The Group's interests in jointly controlled entities are accounted for using the equity method. Under this method the Group's share of the profits less losses of jointly controlled entities is included in the consolidated income statement and its interest in their net assets is included in investments in the consolidated balance sheet. Where the share of losses exceeds the Group's interest in the entity and there is no obligation to fund these losses the carrying amount is reduced to nil and recognition of further losses is discontinued, future profits are not recognised until unrecognised losses are extinguished. Interest in the entity is the carrying amount of the investment together with any long-term interests that, in substance, form part of the net investment in the entity.

Where a Group company is party to a jointly controlled operation, that company accounts for the assets it controls, the liabilities and expenses it incurs and its share of the income. Such joint arrangements are reported in the consolidated financial statements on the same basis.

Goodwill and other intangible assets
Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary or jointly controlled entity at the date of acquisition.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed. Negative goodwill is recognised in the income statement immediately.

On disposal of a subsidiary or jointly controlled entity, the attributable carrying amount of goodwill is included in the determination of the profit or loss on disposal.

Goodwill arising on acquisitions before 1 July 2004, being the date of transition to IFRS, has been retained at the previous UK GAAP amounts at 1 July 2004 subject to being tested for impairment. Goodwill written off 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.

Other intangible assets which comprise contract rights are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to the income statement on a straight line basis over the relevant contract period.

Revenue and profit recognition
Revenue comprises the fair value of the consideration received or receivable, net of value added tax, rebates and discounts and after eliminating sales within the Group. It also includes the Group's proportion of work carried out under jointly controlled operations.

Revenue and profit are recognised as follows:

a) Private housing and land sales
Revenue from housing sales is recognised at the fair value of the consideration received or receivable on legal completion, net of incentives. Revenue from land sales and land exchanges is recognised on the unconditional exchange of contracts. Profit is recognised on a site by site basis by reference to the expected out-turn result from each site. The principal estimation technique used by the Group in attributing profit on sites to a particular period is the preparation of forecasts on a site by site basis. These focus on revenues and costs to complete and enable an assessment to be made of the final out-turn on each site. Consistent review procedures are in place in respect of site forecasting.

b) Property development
Revenue in respect of property developments is taken on unconditional exchange of contracts on disposal of finished developments. Profit taken is subject to any amounts necessary to cover residual commitments relating to development performance. Provision is made for any losses foreseen in completing a development as soon as they become apparent.

Where developments are sold in advance of construction being completed, revenue and profit are recognised from the point of sale and as the significant outstanding acts of construction and development are completed.

c) Construction contracts
Revenue arises from increases in valuations on contracts and includes the Group's share of revenue from joint arrangements, and goods and services provided.

Revenue is normally determined by external valuations and is the gross value of work carried out for the period to the balance sheet date (including retentions) but excludes claims until they are actually certified.

Profit on contracts is calculated in accordance with accounting standards and industry practice and may not relate directly to revenue. The principal estimation technique used by the Group in attributing profit on contracts to a particular period is the

1 Significant accounting policies, continued

preparation of forecasts on a contract by contract basis. These focus on revenues and costs to complete and enable an assessment to be made of the final out-turn on each contract. Consistent contract review procedures are in place in respect of contract forecasting.

The general principles for profit recognition are:

- profits on short duration contracts (generally less than 12 months) are taken when the contract is complete;
- profits on other contracts are recognised on a percentage of completion basis when the contract's outcome can be foreseen with reasonable certainty;
- provision is made for losses incurred or foreseen in bringing the contract to completion as soon as they become apparent; and
- claims receivable are recognised as income when received or certified for payment except that, in preparing contract forecasts to completion, a prudent and reasonable evaluation of claims receivable may be included to mitigate foreseeable losses but only to the extent that there is reasonable assurance of recovery.

Percentage completion is normally calculated by taking certified value to date as a percentage of estimated final value unless the adjusted value is materially different in which case the adjusted value is used.

Pre-contract costs

Costs associated with bidding for contracts are written off as incurred (pre-contract costs). When it is probable that a contract will be awarded, usually when the Group has secured preferred bidder status, external costs incurred from that date to the date of financial close are carried forward in the balance sheet.

When financial close is achieved on PFI or Public Private Partnership (PPP) contracts, external costs are recovered from the special purpose vehicle and pre-contract costs within this recovery that were not previously capitalised are credited to the income statement, except to the extent that the Group retains a share in the special purpose vehicle. The amount not credited is deferred and recognised over the life of the construction contract to which the costs relate.

Property, plant and equipment and depreciation

Depreciation is based on historical or deemed cost, less the estimated residual value, and the estimated economic lives of the assets concerned. Freehold land is not depreciated. Other tangible assets are depreciated in equal annual instalments over the period of their estimated economic lives, which are principally as follows:

Freehold buildings	25-50 years
Leasehold buildings and improvements	Period of lease
Plant, equipment and vehicles	3-10 years

Assets held under finance leases are depreciated over the shorter of the term of the lease or the expected useful life of the asset.

Leases

Operating lease rental charges are charged to the income statement on a straight-line basis over the life of each lease.

Employee benefits

a) Retirement benefit obligations

For defined contribution pension schemes operated by the Group, amounts payable are charged to the income statement as they fall due.

For defined benefit pension schemes, the cost of providing benefits is calculated annually by independent actuaries using the projected unit credit method. The charge to the income statement reflects the current and past service costs of such obligations, and the interest cost on scheme liabilities less the expected return on plan assets.

The retirement benefit obligation represents the difference between the fair value of scheme assets and the present value of scheme liabilities. It is determined bi-annually by independent actuaries and recognised in full in the balance sheet. Differences between the actual and expected returns on assets and experience gains and losses arising on scheme liabilities during the year, together with differences arising from changes in assumptions, are recognised in full directly to reserves via the statement of recognised income and expense in the year. In accordance with the transitional provisions of IFRS 1 cumulative actuarial gains and losses at 1 July 2004 are presented within the opening retained earnings reserve at that date.

The Group's contributions to the schemes are paid in accordance with the rules of the schemes and the recommendation of the actuary.

b) Share-based payments

In accordance with the transitional provisions, IFRS 2 'Share-based payments' has been applied for all payments granted after 7 November 2002. This requires that share-based payments granted after that date, but not vested, should be valued at the fair value of the shares at the date of grant. This affects the Sharesave and LTIP schemes. The fair value of these schemes at date of award is calculated using the Black-Scholes model.

The cost to the Group of awards to employees under the LTIP scheme is spread on a straight line basis over the relevant performance criteria period. The scheme awards to senior employees a number of shares which will vest after three years if particular criteria are met. The award may be taken either as shares or as a combination of shares and cash based on the share price prevailing when the shares vest. The cost of the share-based payment element of the scheme is based on the fair value of the shares at the date the options are granted, and the cost of the cash based payment element is based on the market value of the share options at the balance sheet date.

Shares purchased and held in trust in connection with the Group's share schemes are deducted from retained earnings. No gain or loss is recognised within the income statement on the market value of these shares compared to the original cost.

Finance income and costs

Interest receivable and payable on bank deposits is credited or charged to the income statement as incurred.

Borrowing costs are capitalised where the Group constructs qualifying assets and has separately identifiable funding. All other borrowing costs are written off to the income statement as incurred.

1 Significant accounting policies, continued

Borrowing costs incurred within the Group's jointly controlled entities relating to the construction of assets in PFI and PPP projects are capitalised until the relevant assets are brought into operational use.

Notional interest payable, representing the unwinding of the discount on long-term liabilities, is charged to finance costs.

Infrequently a long-term land creditor arises for a parcel or parcels of land where the Group has exchanged unconditional contracts, and so recognised the creditor and the land inventory, but in practice does not have title or access to the land. In these few cases the notional interest payable already charged to finance costs is then credited to finance costs and added to the cost of inventory in accordance with IAS 23 'Borrowing Costs' and IAS 2 'Inventories'. In no circumstances will the cost of such land inventory exceed the contracted sum payable.

Taxation
Income tax comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is also recognised in equity.

Current tax is the expected tax payable on taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Foreign currencies
Transactions denominated in foreign currencies are recorded at the exchange rates in effect when they take place. Resulting foreign currency denominated assets and liabilities are translated at the exchange rates ruling at the balance sheet date. Exchange differences arising from foreign currency transactions are reflected in the income statement.

The assets and liabilities of overseas subsidiary undertakings are translated at the rate of exchange ruling at the balance sheet date. Trading profits or losses are translated at average rates prevailing during the accounting period. Differences on exchange arising from the retranslation of net investments in overseas subsidiary undertakings at the year-end rates are recognised in the translation reserve. All other translation differences are reflected in the income statement.

In accordance with the transitional provisions of IFRS 1 the Group has elected to set the previously accumulated translation differences relating to investments in overseas subsidiary undertakings to nil at 1 July 2004.

Mining assets
Opencast expenditure incurred prior to the commencement of operating opencast sites is capitalised and the cost less the residual value is depreciated over the coaling life of the site on a coal extraction basis. The total cost of restoration is recognised as a provision as soon as the mine becomes operational. The amount provided represents the present value of the anticipated costs. Costs are charged against the provision as incurred and the unwinding of the discount is included within interest costs. A tangible asset is created for an amount equivalent to the initial provision and depreciated on a coal extraction basis over the life of the asset.

Inventories
Inventories and work in progress, including land held for and in the course of development, are valued at the lower of cost and net realisable value. Cost comprises direct materials and, where appropriate, labour and production overheads which have been incurred in bringing the inventories and work in progress to their present location and condition. Cost in certain circumstances also includes notional interest as explained in the accounting policy for finance income and costs. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Construction work in progress is included within inventories in the balance sheet. It is measured at cost plus profit less losses recognised to date less progress billings. If payments received from customers exceed the income recognised, the difference is included within trade and other payables in the balance sheet.

Land inventory is recognised at the time a liability is recognised – generally after exchange of unconditional contracts.

Property inventory, which represents all development land and work in progress, is included at cost less any losses foreseen in completing and disposing of the development less any amounts received or receivable as progress payments or part disposals. Where a property is being developed, cost includes cost of acquisition and development to date, including directly attributable fees, expenses and finance charges net of rental or other income attributable to the development. Where development property is not being actively developed, net rental income and finance costs are taken to the income statement.

Share capital
The Ordinary Share Capital of the Company is recorded at the proceeds received, net of directly attributable incremental issue costs.

Provisions
Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event, and where it is probable that an outflow will be required to settle the obligation and the amount can be reliably estimated.

1 Significant accounting policies, continued

Financial instruments
Financial assets and financial liabilities are recognised in the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Group are as follows:

a) Trade receivables and trade payables
Given the varied activities of the Group it is not practicable to identify a common operating cycle. The Group has therefore allocated receivables and payables due within 12 months of the balance sheet date to current with the remainder included in non-current.

Trade receivables do not carry interest and are stated at their initial value reduced by appropriate allowances for estimated irrecoverable amounts.

Trade payables on normal terms are not interest bearing and are stated at their nominal value. Trade payables on extended terms, particularly in respect of land purchases, are discounted and recorded at their fair value.

b) Cash and cash equivalents
Cash and cash equivalents in the cash flow statements comprise cash at bank and in hand, including bank deposits with original maturities of three months or less, net of bank overdrafts. Bank overdrafts are included within financial liabilities in current liabilities in the balance sheet.

c) Bank and other borrowings
Interest bearing bank and other loans 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 accounted for on an accruals basis in the income statement using the effective interest method and are added to the carrying value of the instrument to the extent that they are not settled in the period in which they arise.

d) Derivative financial instruments
Derivatives are initially recognised at fair value on the date that the contract is entered into and subsequently re-measured in future periods at their fair value. The method of recognising the resulting change in fair value is dependent on whether the derivative is designated as an effective hedging instrument.

A number of the Group's PFI joint ventures have entered into interest rate derivatives as a means of hedging interest rate risk under cash flow hedges, which are initially recognised at fair value. The effective part of the change in fair value of these derivatives is recognised directly in equity. Any ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are recycled to the income statement in the periods when the hedged items will affect profit or loss. The fair value of interest rate derivatives is the estimated amount that the Group would receive or pay to terminate the derivatives at the balance sheet date.

The Group also enters into forward contracts in order to hedge against transactional foreign currency exposures. In cases where these derivative instruments are significant, hedge accounting is applied as described above. Where hedge accounting is not applied, changes in fair value of derivatives are recognised in the income statement. Fair values are based on quoted market prices at the balance sheet date.

Accounting estimates and judgements
The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, relate to revenue and profit recognition and the valuation of defined pension scheme assets and liabilities.

a) Revenue and profit recognition
Details of the estimation techniques used for revenue and profit recognition in respect of private housing and land sales, property development and construction contracts are given on pages 50 to 51.

b) Defined benefit pension scheme valuations
In determining the valuation of defined benefit pension scheme assets and liabilities, a number of key assumptions have been made. The key assumptions, which are given below, are largely dependent on factors outside the control of the Group:

- expected return on plan assets
- inflation rate
- mortality
- discount rate
- salary and pension increases.

Details of the assumptions used are included in note 8.

2 Segmental analysis

For management purposes the Group is organised into five operating divisions: Construction, Support Services, Homes, Property and Infrastructure Investment. These divisions are the basis on which the Group reports its primary segmental information.

	Construction £m	Support Services £m	Homes £m	Property £m	Infrastructure Investment £m	Centre £m	Group £m
Year to 30 June 2006							
Revenue							
Group and share of joint ventures	**1,218.1**	**281.3**	**277.9**	**47.5**	**13.5**	**–**	**1,838.3**
Less share of joint ventures	(2.6)	–	–	(40.0)	(12.5)	–	**(55.1)**
Group revenue	1,215.5	281.3	277.9	7.5	1.0	–	**1,783.2**
Profit							
Group operating profit	17.2	6.8	41.6	4.2	(2.1)	(11.7)	**56.0**
Share of joint ventures' operating profit	0.8	–	–	5.0	1.4	–	**7.2**
Group and share of joint ventures	**18.0**	**6.8**	**41.6**	**9.2**	**(0.7)**	**(11.7)**	**63.2**
Share of joint ventures – finance cost	–	–	–	(2.1)	(0.5)	–	**(2.6)**
– tax	(0.1)	–	–	(0.8)	(0.5)	–	**(1.4)**
Profit from operations	**17.9**	**6.8**	**41.6**	**6.3**	**(1.7)**	**(11.7)**	**59.2**
Finance income/(cost)	13.7	(0.5)	(13.1)	(0.9)	1.2	(0.5)	**(0.1)**
Profit before tax	**31.6**	**6.3**	**28.5**	**5.4**	**(0.5)**	**(12.2)**	**59.1**
Balance sheet							
Investment in joint ventures	–	–	–	21.7	(0.9)	–	**20.8**
Other assets	281.3	77.3	351.1	22.9	0.8	41.1	**774.5**
Total liabilities	(496.6)	(78.2)	(112.3)	(5.2)	(3.2)	(102.5)	**(798.0)**
Net operating assets/(liabilities)	(215.3)	(0.9)	238.8	39.4	(3.3)	(61.4)	**(2.7)**
Cash, net of debt	298.7	12.5	(165.8)	(23.8)	(3.8)	(6.6)	**111.2**
Net assets	**83.4**	**11.6**	**73.0**	**15.6**	**(7.1)**	**(68.0)**	**108.5**
Other information							
Inter-segmental revenue	8.1	21.4	–	7.3	–	–	**36.8**
Amortisation of intangible assets	–	1.9	–	–	–	–	**1.9**
Capital expenditure	11.9	5.6	3.0	1.3	–	0.7	**22.5**
Depreciation of property, plant and equipment	5.7	6.3	0.5	–	–	1.0	**13.5**

2 Segmental analysis, continued

	Construction £m	Support Services £m	Homes £m	Property £m	Infrastructure Investment £m	Centre £m	Group £m
Year to 30 June 2005							
Revenue							
Group and share of joint ventures	1,086.3	237.4	225.5	62.2	11.8	–	1,623.2
Less share of joint ventures	(7.3)	–	–	(32.0)	(10.9)	–	(50.2)
Group revenue	1,079.0	237.4	225.5	30.2	0.9	–	1,573.0
Profit							
Group operating profit	14.2	5.0	32.9	5.6	(1.7)	(7.9)	48.1
Share of joint ventures' operating profit	(0.4)	–	–	4.8	0.8	–	5.2
Group and share of joint ventures	13.8	5.0	32.9	10.4	(0.9)	(7.9)	53.3
Share of joint ventures – finance cost	–	–	–	(2.2)	(0.9)	–	(3.1)
– tax	0.1	–	–	(0.8)	(0.5)	–	(1.2)
Profit from operations	13.9	5.0	32.9	7.4	(2.3)	(7.9)	49.0
Other non-operating income (exceptional items)	0.8	–	–	–	2.1	3.8	6.7
Finance income/(cost)	11.5	(1.1)	(11.5)	(0.6)	1.1	(0.6)	(1.2)
Profit before tax	26.2	3.9	21.4	6.8	0.9	(4.7)	54.5
Balance sheet							
Investment in joint ventures	1.6	–	–	20.1	1.2	–	22.9
Other assets	243.5	77.3	320.2	11.5	0.6	53.1	706.2
Total liabilities	(431.2)	(66.2)	(74.6)	(7.2)	(3.5)	(151.7)	(734.4)
Net operating assets/(liabilities)	(186.1)	11.1	245.6	24.4	(1.7)	(98.6)	(5.3)
Cash, net of debt	258.2	(2.1)	(185.5)	(12.6)	(2.0)	2.1	58.1
Net assets	72.1	9.0	60.1	11.8	(3.7)	(96.5)	52.8
Other information							
Inter-segmental revenue	12.5	27.1	–	2.2	–	–	41.8
Amortisation of intangible assets	–	1.9	–	–	–	–	1.9
Capital expenditure	8.0	9.8	1.3	–	–	1.7	20.8
Depreciation of property, plant and equipment	5.5	5.7	0.4	–	–	0.7	12.3

The 30 June 2005 segmental information for Construction and Support Services has been restated to reflect the reclassification of Kier Plant from Construction to Support Services to align segmental reporting with the Group's management and internal reporting structure. This has increased revenue by £9.9m and operating profit by £1.8m in Support Services with a corresponding reduction in Construction.

Inter-segmental pricing is determined on an arm's length basis.

As the Group's activities are primarily within the UK, no geographical segmental analysis is required.

Net operating assets represent assets excluding cash, bank overdrafts, long-term borrowings and interest-bearing inter-company loans.

3 Profit for the year

Profit before taxation is stated after charging:

	2006 £m	2005 £m
Remuneration of auditors – audit fees	**0.6**	0.6
– other fees	**–**	–
Hire of plant and machinery	**18.0**	16.3
Operating lease rentals:		
Land and buildings	**2.6**	2.8
Plant and machinery	**9.4**	9.6

4 Other non-operating income (exceptional items)

For the purpose of these financial statements the terms other non-operating income and exceptional items are interchangeable where they relate to the prior year.

Exceptional items for the year to 30 June 2005 arose from the following:

	Profit before tax £m	Tax £m	Net profit/(loss) £m
Disposal of investment in Kier Hong Kong Limited	0.8	–	0.8
Disposal of investment in a PFI joint venture	2.1	(0.6)	1.5
Refinancing of a PFI joint venture	–	(2.5)	(2.5)
Disposal of a property held in property, plant and equipment	3.8	(1.2)	2.6
	6.7	(4.3)	2.4

5 Finance income and cost

	2006 £m	2005 £m
Finance income		
Interest receivable	**5.3**	4.0
Finance cost		
Interest payable on bank overdrafts and loans	**(0.8)**	(0.5)
Interest payable on long-term borrowings	**(2.0)**	(2.0)
Unwinding of discount on long-term liabilities	**(2.6)**	(2.7)
	(5.4)	(5.2)

6 Information relating to employees

	Note	**2006 No**	2005 No
Average number of persons employed during the year including executive directors was:			
United Kingdom		**7,465**	7,026
Rest of world		**1,251**	1,273
		8,716	8,299
		£m	£m
Group staff costs are as follows:			
United Kingdom		**260.1**	234.2
Rest of world		**9.2**	9.2
		269.3	243.4
Wages and salaries		**222.1**	204.9
Social security costs		**21.6**	18.4
Other pension costs		**21.9**	18.5
Share-based payment plans	24	**3.7**	1.6
		269.3	243.4

7 Information relating to directors

Information relating to directors' emoluments, pension entitlements, share options and LTIP interests appears in the directors' remuneration report on pages 39 to 43.

8 Retirement benefit obligations

Kier operates a number of pension schemes for eligible employees as disclosed below.

Kier Group Pension Scheme

This is the principal Scheme and includes a defined benefit section and a defined contribution plan. The assets of the Scheme are held under trust separately from those of the Group; the Trustees are responsible for investing the assets and delegate day-to-day decisions to independent professional investment managers.

The defined benefit section of the Scheme was closed to new entrants on 1 January 2002, existing members continue to accrue benefits for future service.

An actuarial valuation of the Scheme was undertaken by the Trustees' independent actuaries as at 1 April 2005 using the projected unit method. The market value of the Scheme's assets at that date were £369.8m which represented approximately 82% of the benefits that had accrued to members at that date, after allowing for future increases in salaries. The contributions paid during the year were £46.5m (2005: £24.5m) which include special contributions of £31.5m (2005: £12.0m).

Going forward contributions will include an allowance for funding the past service deficit identified at the 2005 valuation date not covered by the above special contributions over a 10-year period to March 2016. The Group expects to pay contributions for future service of £13.2m being 19.1% of pensionable pay plus £11.0m for funding the past service deficit (of which £5.5m was paid in July 2006) in the year to June 2007.

The Pension Protection Fund (PPF) levy is payable in addition to the above contributions.

Following closure of the defined benefit section of the Scheme to new entrants most new employees are offered membership of the Retirement Savings Plan, a defined contribution arrangement. The Group is required to pay contributions in respect of those employees in accordance with the rates specified in the Plan. The contributions paid to the Retirement Savings Plan during the year and the pension charge, amounted to £2.6m (2005: £1.8m).

Kier Sheffield LLP

Kier participates in this defined benefits scheme through its subsidiary Kier Sheffield LLP which has participated as an admitted body in the South Yorkshire Pension Fund since 1 April 2003. As an admitted body it was granted a fully funded past service position at that date, with assets and ongoing past service liabilities of £65.0m.

The scheme covers 1,146 employees who transferred from Sheffield Council's employment to Kier Sheffield LLP upon the start of the contract. New employees are offered membership of the Retirement Savings Plan section of the Kier Group Pension Scheme. Kier Sheffield LLP is required to pay contributions in respect of these employees in accordance with the rates specified in the rules of the Retirement Savings Plan.

Kier Sheffield LLP's pension costs in respect of the defined benefit scheme are assessed on the advice of an independent qualified actuary using the project unit method. Based on the fully funded past service position at 1 April 2003, it has paid contributions at the rate of 10.0% of pensionable pay which the funds actuary has determined is sufficient to meet ongoing benefits. In addition it has paid additional contributions to fund certain pension benefits payable upon redundancy.

Other Schemes

Contributions are also made in respect of hourly paid operatives to an industry-wide stakeholder pension scheme, and in respect of employees who are members of a local government pension scheme. The pension costs for these have been taken as the actual contributions paid over the year.

8 Retirement benefit obligations, continued

IAS 19 disclosures

Kier has adopted immediate recognition of any actuarial gains or losses through the statement of recognised income and expense as permitted under IAS 19.

The principal assumptions used by the independent qualified actuaries and the expected rate of return on assets in providing the IAS 19 position as detailed below were:

Kier Group Pension Scheme

	2006 %	2005 %	2004 %
Rate of general increases in salaries	**4.3**	4.0	4.3
Rate of increase to pensions in payment liable for Limited Price Indexation	**2.8**	2.5	2.8
Discount rate	**5.3**	5.0	5.9
Inflation rate	**2.8**	2.5	3.0

The mortality assumptions adopted estimate life expectancies from age 60 for men and women of 24.6 years and 27.3 years respectively.

	Long-term rate of return expected			**Value**		
	2006 %	2005 %	2004 %	**2006** £m	2005 £m	2004 £m
Equities	**7.8**	7.5	8.5	**238.2**	195.0	158.5
Corporate bonds	**5.0**	4.8	5.5	**170.4**	144.5	100.8
Government bonds	**4.5**	4.3	5.0	**58.4**	54.0	66.2
Total market value of assets				**467.0**	393.5	325.5
Present value of liabilities				**(534.0)**	(517.2)	(426.3)
Deficit				**(67.0)**	(123.7)	(100.8)
Related deferred tax asset				**20.1**	37.1	30.2
Net pension liability				**(46.9)**	(86.6)	(70.6)

Kier Sheffield LLP

	2006 %	2005 %	2004 %
Rate of general increases in salaries	**4.3**	4.0	4.3
Rate of increase to pensions in payment liable for Limited Price Indexation	**2.8**	2.5	3.1
Discount rate	**5.3**	5.0	5.9
Inflation rate	**2.8**	2.5	3.0

The mortality assumptions adopted estimate life expectancies from age 60 for men and women of 23.0 years and 26.0 years respectively.

	Long-term rate of return expected			**Value**		
	2006 %	2005 %	2004 %	**2006** £m	2005 £m	2004 £m
Equities	**7.8**	7.5	8.5	**90.2**	75.7	60.9
Corporate bonds	**5.0**	4.8	5.5	**9.3**	7.2	5.0
Government bonds	**4.5**	4.3	5.0	**19.8**	19.5	17.2
Total market value of assets				**119.3**	102.4	83.1
Present value of liabilities				**(112.5)**	(100.6)	(74.8)
Surplus				**6.8**	1.8	8.3
Related deferred tax liability				**(2.0)**	(0.5)	(2.5)
Net pension asset				**4.8**	1.3	5.8

8 Retirement benefit obligations, continued

Amounts recognised in the financial statements in respect of these defined benefit schemes are as follows:

	2006 Kier Group Pension Scheme £m	2006 Kier Sheffield LLP £m	2006 Total £m	2005 Kier Group Pension Scheme £m	2005 Kier Sheffield LLP £m	2005 Total £m
(Charged)/credited to operating profit in the income statement						
Current service cost	**(14.9)**	**(2.7)**	**(17.6)**	(12.4)	(2.7)	(15.1)
Past service cost	**(0.1)**	**1.1**	**1.0**	–	(0.2)	(0.2)
Expected return on scheme assets	**23.5**	**6.9**	**30.4**	22.7	6.4	29.1
Interest cost on scheme liabilities	**(25.6)**	**(5.1)**	**(30.7)**	(24.7)	(4.4)	(29.1)
	(17.1)	**0.2**	**(16.9)**	(14.4)	(0.9)	(15.3)
Amount recognised in the statement of recognised income and expense						
Actual return less expected return on assets	**19.3**	**8.3**	**27.6**	31.9	9.7	41.6
Experience gains and losses arising on liabilities	**8.0**	**(5.6)**	**2.4**	(64.9)	(18.2)	(83.1)
	27.3	**2.7**	**30.0**	(33.0)	(8.5)	(41.5)
Changes in the fair value of scheme assets						
Fair value at 1 July	**393.5**	**102.4**	**495.9**	325.5	83.1	408.6
Expected return on scheme assets	**23.5**	**6.9**	**30.4**	22.7	6.4	29.1
Actual return less expected return on scheme assets	**19.3**	**8.3**	**27.6**	31.9	9.7	41.6
Contributions by the employer	**46.5**	**2.1**	**48.6**	24.5	2.9	27.4
Contributions by scheme participants	**0.1**	**1.0**	**1.1**	4.2	1.1	5.3
Net benefits paid out	**(15.9)**	**(1.4)**	**(17.3)**	(15.3)	(0.8)	(16.1)
Fair value at 30 June	**467.0**	**119.3**	**586.3**	393.5	102.4	495.9
Changes in the present value of the defined benefit obligation						
Present value at 1 July	**(517.2)**	**(100.6)**	**(617.8)**	(426.3)	(74.8)	(501.1)
Current service cost	**(14.9)**	**(2.7)**	**(17.6)**	(12.4)	(2.7)	(15.1)
Past service cost	**(0.1)**	**1.1**	**1.0**	–	(0.2)	(0.2)
Interest cost on scheme liabilities	**(25.6)**	**(5.1)**	**(30.7)**	(24.7)	(4.4)	(29.1)
Experience gains and losses on scheme liabilities	**8.0**	**(5.6)**	**2.4**	(64.9)	(18.2)	(83.1)
Contributions by scheme participants	**(0.1)**	**(1.0)**	**(1.1)**	(4.2)	(1.1)	(5.3)
Net benefits paid out	**15.9**	**1.4**	**17.3**	15.3	0.8	16.1
Present value at 30 June	**(534.0)**	**(112.5)**	**(646.5)**	(517.2)	(100.6)	(617.8)
Amounts included in the balance sheet						
Fair value of scheme	**467.0**	**119.3**	**586.3**	393.5	102.4	495.9
Net present value of the defined benefit obligation	**(534.0)**	**(112.5)**	**(646.5)**	(517.2)	(100.6)	(617.8)
Net (deficit)/surplus	**(67.0)**	**6.8**	**(60.2)**	(123.7)	1.8	(121.9)
Related deferred tax asset/(liability)	**20.1**	**(2.0)**	**18.1**	37.1	(0.5)	36.6
Net pension (liability)/asset	**(46.9)**	**4.8**	**(42.1)**	(86.6)	1.3	(85.3)

8 Retirement benefit obligations, continued

IAS 19 disclosures, continued

History of experience gains and losses for defined benefit schemes in aggregate

	2006 £m	2005 £m	2004 £m	2003 £m	2002 £m
Fair value of scheme assets	**586.3**	495.9	408.9	292.7	296.8
Net present value of the defined benefit obligation	**(646.5)**	(617.8)	(495.8)	(406.5)	(362.9)
Net deficit	**(60.2)**	(121.9)	(86.9)	(113.8)	(66.1)
Related deferred tax asset	**18.1**	36.6	26.1	34.1	19.8
Net pension liability	**(42.1)**	(85.3)	(60.8)	(79.7)	(46.3)
Difference between expected and actual return on assets	**27.6**	41.6	15.1	(28.5)	(36.7)
Experience gains and losses on scheme liabilities	**2.4**	(83.1)	8.2	(17.4)	(8.6)

It is not practical to produce figures for 2002 to 2004 in accordance with IAS 19. The figures included for these years are as originally published and calculated under UK GAAP (FRS 17 'Retirement Benefits') which it is considered would not be materially different under IAS 19.

9 Income tax

Recognised in the income statement

	2006 £m	2005 £m
Current tax expense		
UK corporation tax: current year on profit before exceptional items	**7.6**	11.7
: on exceptional items	**–**	4.3
Overseas tax	**0.8**	0.3
Adjustments for prior years	**(3.9)**	0.4
Total current tax	**4.5**	16.7
Deferred tax expense		
Origination and reversal of temporary differences	**7.2**	1.6
Adjustments for prior years	**4.5**	(0.4)
Total deferred tax	**11.7**	1.2
Total income tax expense in the income statement	**16.2**	17.9
Reconciliation of effective tax rate		
Profit before tax	**59.1**	54.5
Add: tax on joint ventures	**1.4**	1.2
Underlying profit before tax	**60.5**	55.7
Income tax at UK corporation tax rate of 30%	**18.2**	16.7
Tax on refinancing of a PFI joint venture	**–**	2.5
Non-deductible expenses	**0.5**	0.5
Tax reliefs not recognised in the income statement	**(1.4)**	–
Capital items not taxable	**–**	(0.5)
Effect of tax losses utilised	**–**	(0.2)
Effect of tax rates in foreign jurisdictions	**–**	0.1
Under provision in respect of prior years	**0.3**	–
Total tax (including joint ventures)	**17.6**	19.1
Tax on joint ventures	**(1.4)**	(1.2)
Group income tax expense	**16.2**	17.9

At the balance sheet date the Group has unused tax losses of £11.2m (2005: £11.8m) available for offset against future profits. This is made up of £7.3m (2005: £7.9m) of income losses and £3.9m (2005: £3.9m) of capital losses. A deferred tax asset has been recognised in respect of £3.4m (2005: £4.0m) of income losses. No deferred tax asset has been recognised in respect of the remaining losses, due to the unpredictability of future profit streams against which these losses could be offset. Under present tax legislation, these losses may be carried forward indefinitely.

10 Dividends

Amounts recognised as distributions to equity holders in the year.

	2006 £m	2005 £m
Final dividend for the year ended 30 June 2005 of 15.2p (2004: 13.0p)	**5.4**	4.6
Interim dividend for the year ended 30 June 2006 of 8.2p (2005: 7.0p)	**2.9**	2.5
	8.3	7.1

The proposed final dividend of 17.8p (2005: 15.2p) had not been approved at the balance sheet date and so has not been included as a liability in these financial statements. The dividend totalling £6.3m will be paid on 5 December 2006 to shareholders on the register at the close of business on 29 September 2006. A scrip dividend alternative will be offered.

11 Earnings per share

A reconciliation of profit and earnings per share, as reported in the income statement, to underlying and adjusted profit and earnings per share is set out below. The adjustments are made to illustrate the impact of exceptional items and the amortisation of intangible assets.

	2006		2005	
	Basic £m	**Diluted £m**	Basic £m	Diluted £m
Profit for the year	**42.9**	**42.9**	36.6	36.6
Less: exceptional items	**–**	**–**	(6.7)	(6.7)
Add: tax on exceptional items	**–**	**–**	4.3	4.3
Underlying profit	**42.9**	**42.9**	34.2	34.2
Add: amortisation of intangible assets	**1.9**	**1.9**	1.9	1.9
Less: tax on amortisation of intangible assets	**(0.5)**	**(0.5)**	(0.6)	(0.6)
Adjusted profit	**44.3**	**44.3**	35.5	35.5
	million	**million**	million	million
Weighted average number of shares	**35.5**	**35.5**	35.4	35.4
Weighted average number of unexercised options – dilutive effect	**–**	**0.3**	–	0.1
Weighted average impact of LTIP	**–**	**0.3**	–	0.2
Weighted average number of shares used for EPS	**35.5**	**36.1**	35.4	35.7
	pence	**pence**	pence	pence
Earnings per share	**120.8**	**118.8**	103.4	102.5
Underlying earnings per share (excluding exceptional items)	**120.8**	**118.8**	96.6	95.8
Adjusted earnings per share (excluding exceptional items and amortisation of intangible assets)	**124.8**	**122.7**	100.3	99.4

12 Intangible assets

	Goodwill £m	Contract rights £m	Total £m
Cost			
At 1 July 2005 and 30 June 2006	**5.2**	**15.8**	**21.0**
Amortisation			
At 1 July 2005	–	4.3	4.3
Charge for the year	–	1.9	1.9
At 30 June 2006	**–**	**6.2**	**6.2**
Net book value			
At 30 June 2006	**5.2**	**9.6**	**14.8**
At 30 June 2005	5.2	11.5	16.7
Cost			
At 1 July 2004 and 30 June 2005	5.2	15.8	21.0
Amortisation			
At 1 July 2004	–	2.4	2.4
Charge for the year	–	1.9	1.9
At 30 June 2005	–	4.3	4.3
Net book value			
At 30 June 2005	5.2	11.5	16.7
At 30 June 2004	5.2	13.4	18.6

Goodwill relates to the acquisition of Partnership First Limited in 2002. This balance has been subject to an annual impairment review but continues to be maintained at the 30 June 2004 carrying value.

Contract rights relate to the acquisition by the Group of the business and assets of the construction and building services operation of Sheffield City Council in 2003, which is being amortised on a straight line basis over the remaining life of the contract.

13 Property, plant and equipment

	Land and buildings £m	Plant, vehicles and fixtures £m	Mining assets £m	Total £m
Cost				
At 1 July 2005	27.5	76.9	19.0	123.4
Additions	12.4	10.0	0.1	22.5
Reclassifications	(2.8)	–	–	(2.8)
Disposals	(3.0)	(8.3)	–	(11.3)
Currency realignments	–	(0.1)	–	(0.1)
At 30 June 2006	**34.1**	**78.5**	**19.1**	**131.7**
Accumulated depreciation				
At 1 July 2005	1.0	42.7	3.9	47.6
Charge for the year	0.3	9.9	3.3	13.5
Disposals	–	(7.8)	–	(7.8)
Currency realignment	–	(0.1)	–	(0.1)
At 30 June 2006	**1.3**	**44.7**	**7.2**	**53.2**
Net book value				
At 30 June 2006	**32.8**	**33.8**	**11.9**	**78.5**
At 30 June 2005	26.5	34.2	15.1	75.8
Cost				
At 1 July 2004	23.2	68.9	17.7	109.8
Additions	5.2	14.0	1.3	20.5
Acquisitions	–	0.3	–	0.3
Disposals	(0.9)	(6.4)	–	(7.3)
Currency realignments	–	0.1	–	0.1
At 30 June 2005	27.5	76.9	19.0	123.4
Accumulated depreciation				
At 1 July 2004	0.9	39.7	0.3	40.9
Charge for the year	0.1	8.6	3.6	12.3
Disposals	–	(5.7)	–	(5.7)
Currency realignment	–	0.1	–	0.1
At 30 June 2005	1.0	42.7	3.9	47.6
Net book value				
At 30 June 2005	26.5	34.2	15.1	75.8
At 30 June 2004	22.3	29.2	17.4	68.9

Reclassifications of £2.8m during the current year relate to a property previously occupied by the Group which is now under development and therefore has been transferred to inventories.

14 Investment in joint ventures

a) Movements in year

	2006 £m	2005 £m
Investment in joint ventures		
At 1 July	**22.9**	31.1
Additions	**0.6**	1.5
Disposals	**(1.4)**	(10.3)
Share of profit after taxation	**3.2**	0.9
Net expense recognised directly in equity	**(4.5)**	–
Deferred tax on items recognised directly in equity	**1.3**	–
Dividends received	**(1.3)**	(0.4)
Currency realignments	**–**	0.1
At 30 June	**20.8**	22.9

b) Analysis of investment

	2006 Kier Developments Limited £m	2006 Prospect Healthcare (Hairmyres) Limited £m	2006 Other joint ventures £m	2006 Total £m	2005 Total £m
Investment in joint ventures					
Property, plant and equipment	**4.5**	**–**	**–**	**4.5**	5.0
Deferred tax assets	**0.2**	**0.3**	**–**	**0.5**	–
Current assets	**85.5**	**45.0**	**129.9**	**260.4**	213.1
Gross assets	**90.2**	**45.3**	**129.9**	**265.4**	218.1
Payables – current	**(3.4)**	**(1.8)**	**(7.6)**	**(12.8)**	(30.5)
Payables – non-current	**(83.9)**	**(53.6)**	**(122.2)**	**(259.7)**	(192.0)
Net external assets/(liabilities)	**2.9**	**(10.1)**	**0.1**	**(7.1)**	(4.4)
Loans provided to joint ventures	**18.9**	**4.3**	**4.7**	**27.9**	27.3
Total investment in joint ventures	**21.8**	**(5.8)**	**4.8**	**20.8**	22.9

The liabilities of the joint ventures are without recourse to the Group. The carrying value of the investment in Prospect Healthcare (Hairmyres) Limited is a negative balance after adjusting for an unrealised refinancing gain. Details of the Group's interest in joint ventures are given on page 79.

15 Deferred tax

The following are the major deferred tax assets and liabilities recognised by the Group and movements thereon during the current and prior reporting year.

	Property, plant and equipment £m	Short-term temporary differences £m	Retirement benefit obligations £m	Tax losses £m	Total £m
At 1 July 2004	(2.3)	0.4	27.7	1.2	27.0
Credit/(charge) to income	0.3	2.1	(3.6)	–	(1.2)
Credit to equity	–	–	12.5	–	12.5
At 30 June 2005	(2.0)	2.5	36.6	1.2	38.3
Charge to income	(1.0)	(1.0)	(9.5)	(0.2)	(11.7)
Charge direct to recognised income and expense	–	(0.3)	(9.0)	–	(9.3)
Share-based payments credited to equity	–	1.6	–	–	1.6
At 30 June 2006	**(3.0)**	**2.8**	**18.1**	**1.0**	**18.9**

Deferred tax assets and liabilities are attributed to temporary differences relating to the following:

	Assets		Liabilities		Net	
	2006 £m	2005 £m	**2006 £m**	2005 £m	**2006 £m**	2005 £m
Property, plant and equipment	**0.8**	1.2	**(3.8)**	(3.2)	**(3.0)**	(2.0)
Inventories	**2.7**	2.9	**(0.6)**	(1.5)	**2.1**	1.4
Payables	**3.0**	2.0	**(5.3)**	(1.8)	**(2.3)**	0.2
Financial instruments	**–**	–	**(0.3)**	–	**(0.3)**	–
Retirement benefit obligations	**20.1**	36.6	**(2.0)**	–	**18.1**	36.6
Share-based payments	**3.3**	0.9	**–**	–	**3.3**	0.9
Tax losses	**1.0**	1.2	**–**	–	**1.0**	1.2
Total	**30.9**	44.8	**(12.0)**	(6.5)	**18.9**	38.3
Set-off tax	**(10.0)**	(6.5)	**10.0**	6.5	**–**	–
Net tax assets/(liabilities)	**20.9**	38.3	**(2.0)**	–	**18.9**	38.3

16 Inventories

	2006 £m	2005 £m
Raw materials and consumables	**2.8**	2.4
Construction contracts in progress	**19.4**	6.0
Land and work in progress held for development	**343.0**	302.9
Other work in progress	**12.6**	14.4
	377.8	325.7

17 Construction contracts

Contracts in progress at the balance sheet date comprise contract costs incurred plus recognised profits less losses of £3,971.3m, less progress billings received and receivable of £4,056.1m.

The net balance is analysed into assets and liabilities as follows:

	2006 £m	2005 £m
Inventories	**19.4**	6.0
Trade and other payables	**(104.2)**	(96.1)
	(84.8)	(90.1)

18 Trade and other receivables

	2006 £m	2005 £m
Current:		
Trade receivables	**200.6**	185.5
Construction contract retentions	**27.7**	28.5
Amounts receivable from joint ventures	**5.6**	0.6
Other receivables	**11.6**	9.0
Prepayments and accrued income	**12.9**	9.7
	258.4	233.3
Non-current:		
Construction contract retentions	**10.7**	8.5
Other receivables	**5.4**	6.1
	16.1	14.6

19 Cash, cash equivalents and borrowings

This note provides information about the contractual terms of the Group's bank balances, interest-bearing loans and borrowings. For more information about the Group's exposure to interest rate and foreign currency risk, see note 26.

	2006 £m	2005 £m
Bank balances and cash in hand	**126.6**	79.3
Bank deposits with a maturity of less than three months	**14.7**	14.2
Cash and cash equivalents	**141.3**	93.5
Bank overdrafts and loans	**–**	(5.3)
Long-term borrowings	**(30.1)**	(30.1)
Net funds in the statement of cash flows	**111.2**	58.1

All bank overdrafts and loans are unsecured and bear interest at floating rates linked to the London Inter Bank Offering Rate (LIBOR).

Long-term borrowings comprise a 10-year private placement of loan notes made in February 2003. The borrowings are unsecured and fixed at an interest rate of 6.4% per annum for 10 years. Further information on these borrowings are detailed in note 26.

Cash and cash equivalents includes £12.6m (2005: £6.2m) being the Group's share of cash and liquid resources held by joint arrangements and £25.0m (2005: £16.6m) of cash not readily available to the Group.

20 Trade and other payables

	2006 £m	2005 £m
Current:		
Payments received on account	**5.2**	3.8
Trade payables	**444.7**	374.1
Construction contract balances	**104.2**	96.1
Other taxation and social security costs	**17.8**	18.1
Other payables	**19.1**	17.2
Accruals and deferred income	**79.5**	57.2
	670.5	566.5
Non-current:		
Trade payables	**33.0**	13.4
Accruals and deferred income	**3.8**	3.8
	36.8	17.2

21 Provisions

	Restoration of mining sites £m	Other provisions £m	Total £m
At 1 July 2005	4.7	12.8	17.5
Utilised	–	(5.8)	(5.8)
Unwinding of discount	0.4	–	0.4
Additions	–	6.9	6.9
At 30 June 2006	**5.1**	**13.9**	**19.0**

Other provisions include £12.2m (2005: £11.1m) held in the Group's captive insurance company.

It is anticipated that the amounts provided will be utilised as follows:

	2006 £m	2005 £m
Due within one year	**0.9**	1.2
Due after one year	**18.1**	16.3
	19.0	17.5

22 Share capital

The share capital of the Company comprises:

	2006 Number	2006 £m	2005 Number	2005 £m
Ordinary Shares of 1p each authorised	**45,000,000**	**0.5**	45,000,000	0.5
Issued and fully paid	**35,887,131**	**0.4**	35,686,844	0.4

During the year 200,287 Ordinary Shares were issued at a total premium of £2.1m, of which 182,683 were issued as a scrip dividend alternative at a premium of £2.1m and 17,604 were issued under Performance Options and the Sharesave Scheme.

23 Reconciliation of movement in reserves and changes in total equity

	Share capital £m	Share premium £m	Capital redemption reserve £m	Retained earnings £m	Cash flow hedge reserve £m	Translation reserve £m	Total equity £m
At 1 July 2004	0.4	17.1	2.7	31.0	–	–	51.2
Total recognised income and expense	–	–	–	7.6	–	0.1	7.7
Dividends paid	–	–	–	(7.1)	–	–	(7.1)
Issue of own shares	–	0.8	–	–	–	–	0.8
Purchase of own shares	–	–	–	(0.4)	–	–	(0.4)
Share-based payments charge	–	–	–	0.6	–	–	0.6
At 30 June 2005	0.4	17.9	2.7	31.7	–	0.1	52.8
Effect of adoption of IAS 32 and IAS 39 (net of tax)	–	–	–	–	(5.3)	–	(5.3)
At 1 July 2005 (restated)	0.4	17.9	2.7	31.7	(5.3)	0.1	47.5
Total recognised income and expense	–	–	–	63.9	2.9	(0.3)	66.5
Dividends paid	–	–	–	(8.3)	–	–	(8.3)
Issue of own shares	–	2.1	–	–	–	–	2.1
Purchase of own shares	–	–	–	(2.0)	–	–	(2.0)
Share-based payments charge	–	–	–	1.1	–	–	1.1
Deferred tax on share-based payments	–	–	–	1.6	–	–	1.6
At 30 June 2006	**0.4**	**20.0**	**2.7**	**88.0**	**(2.4)**	**(0.2)**	**108.5**

Cash flow hedge reserve
This reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred, together with any related deferred taxation.

Translation reserve
This reserve comprises the cumulative difference on exchange arising from the retranslation of net investments in overseas subsidiary undertakings. In accordance with the transitional provisions of IFRS 1 this reserve was set to nil at 1 July 2004.

24 Share-based payments

Options and awards over the Company's Ordinary Shares at 30 June 2006 were as follows:

	Sharesave scheme	LTIP 2004 award	LTIP 2005 award	LTIP 2006 award	Total
Date of grant	29 October 2003	1 October 2003	1 December 2004	3 October 2005	
Awards outstanding at 30 June 2006					
– directors	2,360	78,524	120,148	101,758	**302,790**
– employees	506,158	118,765	217,500	181,500	**1,023,923**
	508,518	197,289	337,648	283,258	**1,326,713**

Sharesave scheme
Options were granted on 29 October 2003 at an exercise price of 625p, these are exercisable at the holders' discretion from 1 January 2007 until 1 July 2007.

LTIP
Awards made under the scheme are normally able to vest following the third anniversary of the date of the grant. Vesting may be in full or in part (with the balance of the award lapsing), and is subject to the Company achieving specific performance targets.

The awards may be taken as shares or as a combination of shares and cash based on the share price prevailing when the shares vest.

The share element of the award are intended to be satisfied from the following shares held by the Kier Group 1999 Employee Benefit Trust rather than from the issue of new shares. These shares are accounted for as a deduction from retained earnings.

	2006 Number of shares	**£m**	2005 Number of shares	£m
At 1 July	**256,331**	**1.4**	267,414	1.2
Acquired during the year	**167,000**	**2.0**	50,000	0.4
Issued in satisfaction of awards	**(68,164)**	**(0.3)**	(61,083)	(0.2)
At 30 June	**355,167**	**3.1**	256,331	1.4

The market value of these shares at 30 June 2006 was £5.4m. The dividends on these shares have been waived.

A description of these schemes and the terms and conditions of each scheme are included in the directors' remuneration report on page 42.

Value of share schemes
The fair value per option granted has been calculated using the Black-Scholes model using the following assumptions:

	Sharesave scheme	LTIP 2004 award	LTIP 2005 award	LTIP 2006 award
Date of grant	29 October 2003	1 October 2003	1 December 2004	3 October 2005
Share price at grant	604.5p	627.5p	699.0p	1065.0p
Exercise price	625.0p	nil	nil	nil
Option life	3 years	3 years	3 years	3 years
Expected volatility	27.8%	N/A	N/A	N/A
Dividend yield	3.0%	2.9%	2.8%	2.0%
Risk-free interest rate	4.8%	N/A	N/A	N/A
Value per option	114.0p	578.0p	633.0p	1043.0p

The expected volatility is based on historical volatility over the last three years. The risk free rate of return is the yield on zero-coupon UK government bonds of a term consistent with the assumed option life.

The total charge for the year relating to share-based payment plans was:

	2006 £m	2005 £m
Equity-settled	**1.1**	0.6
Cash-settled	**2.6**	1.0
Total expense recognised as employee costs	**3.7**	1.6

24 Share-based payments, continued

Included in other payables is an amount of £3.5m (2004: £1.6m) relating to provisions for cash settled share-based payment plans.

A reconciliation of option movements is shown below:

	Number of options 2006	Weighted average exercise price 2006	Number of options 2005	Weighted average exercise price 2005
Outstanding at 1 July	**1,319,351**	**266.3p**	1,309,924	311.8p
Forfeited	**(190,065)**	**151.3p**	(213,664)	192.3p
Exercised	**(85,831)**	**56.1p**	(145,125)	110.1p
Granted	**283,258**	**–**	368,216	–
Outstanding at 30 June	**1,326,713**	**239.6p**	1,319,351	266.3p
Exercisable at 30 June	**–**	**–**	–	–

25 Guarantees and contingent liabilities

There are contingent liabilities in respect of performance bonds, guarantees and claims under contracting and other arrangements, including joint arrangements and joint ventures, entered into in the normal course of business.

26 Financial instruments

Exposure to credit, interest rate and currency risk arises in the normal course of the Group's business. Derivative financial instruments are used to hedge exposure to fluctuations in interest and exchange rates.

Credit risk

Credit risk arises on financial instruments such as trade receivables, short-term bank deposits and interest rate and currency hedges.

Policies and procedures exist to ensure that customers have an appropriate credit history.

Short-term bank deposits and hedging transactions are executed only with highly credit-rated authorised counter-parties based on ratings issued by the major ratings agencies. Counter-party exposure positions are monitored regularly so that credit exposures to any one counter-party are within predetermined limits. At the balance sheet date there were no significant concentrations of credit risk.

Interest rate risk

The Group has hedged its exposure to interest rate movements through a private placement of £30.1m of loan notes for 10 years from February 2003, which bear interest on a fixed rate basis at 6.4% p.a. The balance of the Group's borrowings are to finance short-term working capital requirements. Such borrowings are subject to floating rates of interest linked to LIBOR.

In addition, a number of the Group's PFI and Property joint ventures have entered into interest rate swaps.

Foreign currency risk

The Group operates primarily within the UK such that its exposure to currency risk is not considered to be significant.

Where foreign currency exposures are identified these are hedged using forward foreign exchange contracts.

Derivative financial instruments

At 30 June 2006	Current assets £m	Non-current assets £m	Total assets £m	Total liabilities £m
Forward foreign currency contracts	**0.1**	**–**	**0.1**	**–**
Fuel price forward contracts	**0.5**	**0.6**	**1.1**	**–**
	0.6	**0.6**	**1.2**	**–**

In addition to the above, a number of the Group's PFI joint ventures have entered into interest rate derivatives as a means of hedging interest rate risk. Interest bearing debts and associated interest rate derivatives within these joint ventures have a typical term of between 25 and 30 years and are without recourse to the Group. At 30 June 2006 the aggregate amount outstanding on these interest bearing debts against which interest rate derivatives are held is £137.4m. The Group's share of the total net fair value liability of these interest rate derivatives at 30 June 2006 amounted to £4.5m which, together with the related deferred tax asset of £1.3m, has been treated as an effective hedge and recognised directly in equity.

26 Financial instruments, continued

Financial assets and liabilities – analysis by currency and maturity dates

At 30 June 2006 the Group had cash, overdrafts and long-term borrowings denominated in the following currencies:

	2006 Financial assets £m	2006 Financial liabilities £m	2006 Aggregate £m	2005 Financial assets £m	2005 Financial liabilities £m	2005 Aggregate £m
Currency:						
Sterling	**133.0**	**(16.7)**	**116.3**	89.4	(21.9)	67.5
US dollar	**5.4**	**(13.4)**	**(8.0)**	2.2	(13.4)	(11.2)
Euro	**1.7**	**–**	**1.7**	–	–	–
Other	**1.2**	**–**	**1.2**	1.9	(0.1)	1.8
Total	**141.3**	**(30.1)**	**111.2**	93.5	(35.4)	58.1

There is no material difference between the carrying value and fair value of the Group's aggregate financial assets and liabilities. The maturity of the Group's financial liabilities is shown in the table below:

	2006 £m	2005 £m
Due in one year or less	**–**	(5.3)
Due in more than five years	**(30.1)**	(30.1)
Total	**(30.1)**	(35.4)

Amounts due in more than five years represent a £17.0m UK sterling loan and a £13.4m US dollar loan, net of £0.3m of capitalised finance costs, from the private placement of loan notes made in February 2003. The loans are repayable in one payment in February 2013. The UK sterling loan is at a fixed interest rate of 6.4% for the term of the loan. The Group has entered into interest payment and repayment swaps for the US dollar loan, which give an effective 6.4% fixed interest rate for the term of the loan.

The remaining financial assets and liabilities are cash, short-term deposits and overdrafts at floating rates based on LIBOR.

Borrowing facilities

The Group has £107.5m (2005: £67.5m) of unsecured committed borrowing facilities due for renewal as follows:

	Undrawn facility £m
2007	15.0
2011	92.5
	107.5

In addition the Group has £12.5m (2005: £12.5m) of unsecured overdraft facilities repayable on demand.

27 Financial and capital commitments

	2006 £m	2005 £m
Commitments for capital expenditure in subsidiaries	**2.9**	2.1
Commitments for equity and subordinate debt in PFI joint ventures	**13.7**	6.8
	16.6	8.9

Non-cancellable operating lease rentals are payable as follows:

	2006 Property £m	2006 Plant and machinery £m	2005 Property £m	2005 Plant and machinery £m
Within one year	**1.5**	**2.9**	1.6	3.2
Between one and five years	**5.3**	**14.1**	5.5	14.0
Over five years	**9.8**	**0.2**	11.6	0.4
	16.6	**17.2**	18.7	17.6

The Group leases properties and vehicles for operational purposes. Property leases vary considerably in length up to a maximum period of 99 years. Vehicle leases typically run for a period of four years. None of the leases includes contingent rentals.

28 Related parties

Identity of related parties

The Group has a related party relationship with its joint arrangements, joint ventures and key management personnel.

Transactions with key management personnel

The Group's key management personnel are the executive and non-executive directors as identified on pages 32 and 33. Other than disclosed in the directors' remuneration report, there were no other transactions with key management personnel in either the current or preceding year.

Sales of goods to joint arrangements and joint ventures

	2006 £m	2005 £m
Construction services and materials	**71.1**	37.7
Staff and associated costs	**13.8**	9.4
Management services	**1.0**	2.0
	85.9	49.1

Amounts due from joint ventures are analysed below:

	2006 £m	2005 £m
Academy Services (Norwich) Limited	**0.1**	–
Academy Services (Oldham) Limited	**1.5**	–
Academy Services (Sheffield) Limited	**2.7**	–
Academy Services (Tendring) Limited	**0.7**	0.4
Academy Services (Waltham Forest) Limited	**0.7**	0.2
ASK (Greenwich) Limited	**0.8**	0.8
Information Resources (Bournemouth) Limited	**0.8**	0.7
Prospect Healthcare (Hairmyres) Limited	**4.5**	4.5
Prospect Healthcare (Hinchingbrooke) Limited	**1.2**	0.8
Prospect Healthcare (Reading) Limited	**1.7**	1.7
Kier Developments Limited	**18.8**	18.8
	33.5	27.9

29 Acquisitions

Acquisition of the business and assets of the construction and building services operation of Sheffield City Council

On 31 March 2003 the Group, through its subsidiary Kier Sheffield LLP, acquired the business and assets of the construction and building services operation of Sheffield City Council. The consideration, payable wholly in cash was £16.7m, representing the value of the net assets acquired.

The consideration is payable as follows:

	£m
Total consideration payable	16.7
Paid at 30 June 2005	(12.6)
Paid during the year ended 30 June 2006	(1.6)
Unwinding of discount	0.9
Deferred at 30 June 2006	3.4
Due in one year or less	1.1
Due between one and five years	2.3
	3.4

Acquisition of Ashwood Homes

On 10 June 2005 the Group acquired 100% of the business of Ashwood Homes. The consideration payable was £23.5m representing the value of the net assets acquired. (Tangible fixed assets £0.3m, inventories £24.1m, and payables £(0.9)m). The consideration was paid as follows:

	£m
Paid at 30 June 2005	15.0
Paid during the year ended 30 June 2006	8.5
	23.5

30 Post balance sheet events

On 31 July 2006 the Group acquired the entire share capital of Hugh Bourn Developments (Wragby) Limited. The consideration payable was £53.3m with £20.0m paid in cash on 31 July 2006 and the balance due in equal instalments on 2 July 2007 and 1 July 2008.

31 Explanation of transition to IFRS

These are the Group's first consolidated financial statements prepared in accordance with IFRS.

The accounting policies set out in note 1 have been applied in preparing the consolidated financial statements, including comparative information for the year to 30 June 2005 and in preparation of an opening IFRS balance sheet at 1 July 2004 (the Group's date of transition).

In preparing its opening IFRS balance sheet and comparative information for the year to 30 June 2005, the Group has adjusted amounts previously reported in financial statements prepared in accordance with UK GAAP. In addition, following the adoption of IAS 32 and IAS 39, the Group has adjusted previously restated total equity at 1 July 2005.

The reconciliation of total equity at 1 July 2004 and 30 June 2005 is as follows:

	30 June 2005 £m	I July 2004 £m
Total equity as previously reported under UK GAAP	**147.4**	**116.4**
Adjustments on adoption of IFRS		
Employee benefits	(93.7)	(64.8)
Sales and marketing costs	(3.9)	(2.6)
Deferred land payments	(1.1)	–
Property transactions	–	(0.3)
Proposed dividends	5.4	4.6
Deferred taxation	(2.0)	(2.1)
Share-based payments	0.1	–
Goodwill not amortised	0.6	–
Total equity under IFRS	**52.8**	**51.2**

The reconciliation of total equity at 1 July 2005 following the adoption of IAS 32 and IAS 39 is as follows:

	£m
Total equity as reported under IFRS at 30 June 2005	**52.8**
Adjustments on adoption of IAS 32 and IAS 39	
Group share of fair value on interest rate swaps in PFI joint ventures	(8.5)
Fair value of other cash flow hedges	1.0
	(7.5)
Deferred tax on above	2.2
Total IAS 32 and IAS 39 adjustments	**(5.3)**
Total equity under IFRS at 1 July 2005	**47.5**

The reconciliation of profits for the year to 30 June 2005 is as follows:

	Year to 30 June 2005 £m
Profit for the year after tax under UK GAAP	**37.8**
Adjustments on adoption of IFRS	
Employee benefits	0.1
Sales and marketing costs	(1.3)
Deferred land payments	(1.1)
Property transactions	0.3
Deferred taxation	0.2
Goodwill not amortised	0.6
Total IFRS adjustments	**(1.2)**
Profit for the year under IFRS	**36.6**

31 Explanation of transition to IFRS, continued

The principal differences between UK GAAP and IFRS for the Group are:

a) Employee benefits

Under UK GAAP the Group accounted for its defined benefit schemes in accordance with 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 the cost of providing pension benefits (current service cost) for defined benefit pensions schemes is recognised in profit or loss, together with the interest cost arising on the projected obligations, returns on scheme assets and past service costs. The defined benefit obligation is determined bi-annually by independent actuaries and recognised on the balance sheet. Actuarial gains and losses are recognised in full in the statement of recognised income and expense in the period in which they occur.

b) Sales and marketing costs

Under UK GAAP sales and marketing costs for the Residential and Property divisions are capitalised in site work in progress and written off through cost of sales as the site progresses. Under IAS 2 'Inventories' costs relating to sales and marketing activities are required to be written off as incurred.

c) Deferred land payments

Under UK GAAP deferred land payments (land creditors) are included in 'creditors' at their gross value. Under IAS 2 imputed interest is recognised on deferred land payments with the result that the land creditors are carried in the balance sheet at net present value and the value of land held on the balance sheet in inventories is reduced. The unwinding of the imputed interest (or discount) on land creditors is charged to finance cost and the reduction in land values in inventories will result in an eventual reduction in cost of sales as the land is traded out.

d) Property transactions

Under UK GAAP where property developments are sold in advance of construction, turnover and profit are recognised over the life of the contract in accordance with SSAP 9 'Stocks and Long-Term Contracts'. Under IAS 18 'Revenue', where property developments are sold in advance of construction being completed, revenue and profit are recognised from the point of sale, and as the significant outstanding acts of construction and development are completed.

e) Proposed dividends

Under UK GAAP as applicable for the year ended 30 June 2005, proposed dividends were recognised as a liability in the period to which they relate. Under IAS 10 dividends are not recognised as a liability until they are appropriately authorised and no longer at the discretion of the Company.

f) Deferred taxation

IAS 12 'Income Taxes' requires deferred tax to be recognised on all temporary differences and not just timing differences as previously under UK GAAP. Deferred tax liabilities are recognised in full but deferred tax assets are only recognised if future taxable profits are available to cover the assets.

g) Share-based payments

As permitted by the exemption from retrospective application in IFRS 1, the Group has adopted IFRS 2 for all payments granted after 7 November 2002. This requires that share-based payments granted after that date, but not vested, should be valued at the fair value of the shares at the date of grant. This affects the Sharesave and Long-Term Incentive Plan schemes. The fair value of these shares at date of award is calculated using the Black-Scholes model.

h) Goodwill and intangible assets

Under UK GAAP, goodwill is amortised on a straight line basis over its useful economic life (in the case of Kier for up to 10 years) tested for impairment and provided for as necessary. Under IFRS 3 'Business Combinations' goodwill is no longer amortised but is carried at cost and subject to annual review for impairment at 30 June. It is effectively frozen at June 2004 with amounts amortised subsequently under UK GAAP being reinstated.

At June 2004 the Group balance sheet contained £18.6m of goodwill. £13.4m of this relates to the business and assets of the Construction and Building Services operation of Sheffield City Council. This has been reclassified from goodwill to intangible assets in respect of contract rights under IFRS and will continue to be amortised on a straight line basis over the remaining life of the contract. The balance of £5.2m relates to the acquisition of Partnerships First in 2002. This balance has been maintained at the 30 June 2004 carrying value.

Company balance sheet at 30 June 2006

	Notes	2006 £m	2005 restated £m
Fixed assets			
Investment in subsidiary undertakings		**55.3**	55.3
Current assets			
Debtors	6	**39.2**	18.0
Cash at bank and in hand		**207.4**	195.2
		246.6	213.2
Current liabilities			
Creditors – amounts falling due within one year	7	**(235.1)**	(198.0)
Net current assets		**11.5**	15.2
Total assets less current liabilities		**66.8**	70.5
Creditors – amounts falling due after more than one year	7	**(30.1)**	(37.6)
Net assets		**36.7**	32.9
Capital and reserves			
Called up share capital	8	**0.4**	0.4
Share premium account	9	**20.0**	17.9
Merger relief reserve	9	**1.2**	1.2
Capital redemption reserve	9	**2.7**	2.7
Profit and loss account	9	**12.4**	10.7
Shareholders' funds	10	**36.7**	32.9

The financial statements were approved by the Board of directors on 13 September 2006 and were signed on its behalf by:

J Dodds
D E Mattar
Directors

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material.

Changes in accounting policy

During the year the Company adopted FRS 20 'Share-based payments', FRS 21 'Events after the balance sheet date', FRS 25 'Financial instruments: disclosure and presentation', FRS 26 'Financial instruments: measurement' and FRS 28 'Corresponding amounts'.

Under FRS 21 dividends are not recognised until they are appropriately authorised and no longer at the discretion of the Company.

The adoption of these standards represents a change in accounting policy and the comparative figures have been restated accordingly. The effect of the restatement on the retained profit and net assets for the current and prior years are detailed in note 2 to the Company financial statements.

Basis of preparation

The financial statements have been prepared under the historical cost convention and in accordance with UK GAAP.

A cash flow statement has not been presented as permitted by FRS 1 (revised) 'Cash flow statements'.

Fixed asset investments

Investments in subsidiary undertakings are included in the balance sheet at cost less any provision for diminution in value.

Deferred taxation

In accordance with FRS 19 'Deferred tax', deferred taxation is provided fully and on a non-discounted basis at expected future corporation tax rates in respect of timing differences between profits computed for taxation and accounts purposes.

Own shares

The cost of the Company's investment in its own shares which comprise shares held by the Kier Group 1999 Employee Benefit Trust for the purpose of funding of the Company's share option plans, is shown as a reduction in shareholders' funds in retained earnings.

Share-based payments

In accordance with the transitional provisions FRS 20 has been applied to share options granted after 7 November 2002 that had not vested at 1 January 2005.

The Company issues equity-settled share-based payments under the Sharesave and LTIP schemes. The fair value of these schemes at the date of grant is expressed on a straight line basis over the vesting period, based on the estimate of shares that will eventually vest.

Financial instruments

The Company's principal financial assets and liabilities are cash at bank and borrowings. Cash at bank is carried in the balance sheet at nominal value. Borrowings are recognised initially at fair value and subsequently at amortised cost.

2 Prior year adjustment

The effect of the adoption of FRS 20 and FRS 21 are as follows:

	Net assets as originally reported £m	FRS 20 £m	FRS 21 £m	Net assets restated £m
At 1 July 2004	30.9	0.1	(2.0)	29.0
Profit for the year	7.9	(0.1)	2.5	10.3
Dividends paid	(7.9)	–	0.8	(7.1)
Issue of shares	0.8	–	–	0.8
Share-based payments	(0.2)	0.1	–	(0.1)
At 30 June 2005	31.5	0.1	1.3	32.9

The effect of the prior year adjustment on the current year has been a decrease of £1.6m in retained profit.

The adoption of FRS 25 and FRS 26 has had no effect on net assets or retained profits in the current year.

3 Profit for the year

As permitted by section 230 of the Companies Act 1985, the Company has elected not to present its own profit and loss account for the year.

The auditors' remuneration for audit services to the Company was £4,450 (2005: £4,450).

4 Information relating to directors and employees

Information relating to directors' emoluments, pension entitlements, share options and LTIP interests appears in the directors' remuneration report on pages 39 to 43. The Company has no other employees other than the directors.

5 Dividends

Details of the dividends paid by the Company are included in note 10 to the consolidated financial statements.

6 Debtors

	2006 £m	2005 restated £m
Amounts falling due within one year:		
Amounts due from subsidiary undertakings	**34.9**	14.6
Other debtors	**3.8**	2.8
Corporation tax	**0.5**	0.6
	39.2	18.0

7 Creditors

	2006 £m	2005 restated £m
Amounts falling due within one year:		
Bank overdrafts and loans	**202.0**	174.4
Amounts due to subsidiary undertakings	**27.9**	21.7
Other creditors	**5.2**	1.9
	235.1	198.0
Amounts falling due after one year:		
Long-term borrowings	**30.1**	30.1
Amounts due to subsidiary undertakings	**–**	7.5
	30.1	37.6

Long-term borrowings due after more than one year comprises borrowings in respect of a 10-year private placement of loan notes made in February 2003. The borrowings are unsecured and fixed at an interest rate of 6.4% per annum for 10 years.

8 Share capital

Details of the share capital of the Company are included in note 22 to the consolidated financial statements.

9 Reserves

The movement on reserves is as follows:

	Share premium £m	Merger relief reserve £m	Capital redemption reserve £m	Profit and loss £m
At 30 June 2004 as previously stated	17.1	1.2	2.7	9.5
Prior year adjustments:				
Adoption of FRS 20	–	–	–	0.1
Adoption of FRS 21	–	–	–	(2.0)
At 1 July 2004 restated	17.1	1.2	2.7	7.6
Issue of shares	0.8	–	–	–
Increase in investment in own shares	–	–	–	(0.2)
Share-based payments charge	–	–	–	0.1
Profit for the year	–	–	–	10.3
Dividends paid	–	–	–	(7.1)
At 30 June 2005	17.9	1.2	2.7	10.7
Issue of shares	2.1	–	–	–
Increase in investment in own shares	–	–	–	(1.7)
Share-based payments charge	–	–	–	0.5
Profit for the year	–	–	–	11.2
Dividends paid	–	–	–	(8.3)
At 30 June 2006	**20.0**	**1.2**	**2.7**	**12.4**

Details of the shares held by the Kier Group 1999 Employee Benefit Trust and of the share-based payment schemes are included in note 24 to the consolidated financial statements.

10 Reconciliation of movement in shareholders' funds

	2006 £m	2005 £m
Opening shareholders' funds as previously stated	**31.5**	30.9
Prior year adjustments (note 2)	**1.4**	(1.9)
Opening shareholders' funds as restated	**32.9**	29.0
Profit for the year	**11.2**	10.3
Dividends paid	**(8.3)**	(7.1)
Issue of shares	**2.1**	0.8
Increase in investment in own shares	**(1.7)**	(0.2)
Share-based payment charge	**0.5**	0.1
Closing shareholders' funds	**36.7**	32.9

Principal operating subsidiaries and business units

Construction	**Kier Regional Limited** Kier Build Kier Eastern Kier London Kier Northern Kier North West Kier Partnership Homes Limited Kier Scotland Kier South East Kier Southern Kier Western Marriott Construction Moss Construction **Kier Construction Limited** Kier Caribbean and Industrial Limited
Support Services	**Kier Support Services Limited** Kier Building Maintenance Kier Building Services Engineers Kier Engineering Services Kier Islington Limited Kier Managed Services Limited Kier Plant Limited Kier Sheffield LLP
Homes	**Kier Residential Limited** Allison Homes Eastern Limited Bellwinch Homes Limited Hugh Bourn Developments (Wragby) Limited Kier Homes Limited Twigden Homes Limited
Property	**Kier Property Limited** Kier Developments Limited (50% owned and accounted for as a joint venture) Kier Ventures Limited
Infrastructure Investment	**Kier Project Investment Limited**
Group Services	**Kier Limited**

Notes:

i) Each company is registered in England and Wales and operates principally within the United Kingdom.
Kier Construction Limited also operates in the Middle East, the Caribbean and Romania.

ii) The Ordinary Share Capital of each company is wholly owned. Kier Group plc holds directly all the shares of Kier Limited and Kier Residential Limited. The shares of the other companies are held by subsidiary undertakings.

iii) A full list of the Group's subsidiaries is included in the Company's Annual Return.

Principal joint arrangements and joint ventures

Joint arrangements

Building and/or civil engineering construction

The following joint arrangements, in which the Group participation is between 33% and 50%, operate in England:

Besix/Kier a joint arrangement between Kier Construction and NV Besix SA

Kier/Nuttall a joint arrangement between Kier Construction and Edmund Nuttall Limited

Kier/Murphy/ Interserve a joint arrangement between Kier Construction, J Murphy & Sons Limited and Interserve Project Services Limited

KMI Plus a joint arrangement between Kier Construction, J Murphy & Sons Limited, Interserve Project Services Limited and Mouchel Parkman Services Limited

The following joint arrangements, in which the Group participation is between 40% and 50%, operate overseas, in the territory indicated:

Jamaica

Besix/Kier a joint arrangement between Kier Construction and NV Besix SA

Kier/CCC a joint arrangement between Kier Construction and Commercial Contracting Company of San Antonio, Inc.

Suriname

Kier/CCC a joint arrangement between Kier Construction and Commercial Contracting Company of San Antonio, Inc.

Romania

Mivan/Kier a joint arrangement between Mivan Limited and Kier Construction

Commercial Property Development

The Group has a 25% participation in a joint arrangement in England between Kier Property and Norwich Union Life and Pensions Limited.

Joint ventures

	Interest held
Long-term concession holding under the Private Finance Initiative	
Academy Services (Holdings) Limited	50%
Academy Services (Norwich) Holdings Limited	50%
Academy Services (Oldham) Holdings Limited	50%
Academy Services (Sheffield) Holdings Limited	50%
Academy Services (Waltham Forest) (Holdings) Limited	50%
ASK (Holdings) Limited	50%
Information Resources (Holdings) Limited	50%
Information Resources (Oldham) Holdings Limited	50%
Justice Support Services (North Kent) Holdings Limited	42.5%
Prospect Healthcare (Hairmyres) Group Limited	50%
Prospect Healthcare (Hinchingbrooke) Holdings Limited	50%
Prospect Healthcare (Ipswich) Holdings Limited	50%
Prospect Healthcare (Reading) Holdings Limited	50%
Commercial property development	
Kier Developments Limited	50%
Kier Warth Limited	50%

Notes:

i) Joint arrangements are contracted agreements to co-operate on a specific project which is an extension of the Group's existing business. Joint ventures are ongoing businesses carrying on their own trade.

ii) Except where otherwise stated the companies are incorporated and operate in the United Kingdom.

Financial record

Year ended 30 June	IFRS 2006 £m	IFRS 2005 £m	UK GAAP 2004 £m	UK GAAP 2003 £m	UK GAAP 2002 £m
Revenue: Group and share of joint ventures	**1,838.3**	1,623.2	1,476.5	1,445.6	1,382.7
Group operating profit	**56.0**	48.1	39.4	33.1	24.8
Joint ventures – share of operating profit	**7.2**	5.2	3.2	3.1	1.4
Total finance (cost)/income net	**(2.7)**	(4.3)	(2.0)	(0.6)	1.1
Joint venture tax	**(1.4)**	(1.2)	–	–	–
Other	**–**	6.7	–	(2.3)	0.7
Profit before tax	**59.1**	54.5	40.6	33.3	28.0
Income tax	**(16.2)**	(17.9)	(12.0)	(9.5)	(7.7)
Profit for the year	**42.9**	36.6	28.6	23.8	20.3
Earnings per share					
– undiluted	**120.8p**	103.4p	81.5p	69.5p	60.4p
Dividend per share	**26.0p**	22.2p	19.0p	16.4p	14.2p
At 30 June					
Shareholders' funds	**£108.5m**	£52.8m	£116.4m	£92.7m	£73.8m
Net assets per share	**302.3p**	148.0p	327.7p	265.9p	214.2p

The figures for 2005 were restated in 2006 in respect of the transition from UK GAAP to IFRS. The figures for 2002 to 2004 above have not been restated to an IFRS basis as it is not practicable to do so.

Corporate information

Directors
P T Warry MA FREng *Chairman*
J Dodds *Chief Executive*
I M Lawson FCIOB
D E Mattar BSc FCA
M P Sheffield BSc CEng MICE
R W Side FCIOB FFB MCMI
R W Simkin BSc MRTPI
P F Berry CMG MA
S W Leathes MA FCA
P M White CBE FCA (appointed 1 July 2006)

M O'Farrell (appointed 1 October 2006)

M D Barton LLB *Secretary*

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128 Queen Victoria Street
London
EC4V 4BJ

Financial calendar

25 November 2006
Annual General Meeting

5 December 2006
Payment of final dividend for 2005/06

March 2007
Announcement of half-year results and interim dividend for 2006/07

May 2007
Payment of interim dividend

September 2007
Announcement of preliminary full-year results and final dividend for 2006/07

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