



AEA

AEA Technology plc
Interim Report 2005

Group overview

AEA is a technical services and consultancy business. Its key markets are environment and rail. AEA is a market leader in both these sectors because of its strong proprietary technology and solid customer relationships. AEA operates in the UK, EU and North America. The Company employs 1700 people worldwide.

AEA Environment

AEA Environment is a leading supplier of environmental consulting services to the UK Government and agencies. It also has a growing international business helping governments to meet their environmental obligations.

AEA Environment leads the market in the sectors where it operates with a robust portfolio of services and products in the areas of:

- **Energy** – renewables, energy management, power generation and transmission
- **Environment** – environmental monitoring, waste management, environment health & safety compliance and reporting
- **Programme management** – helping government turn policy into practice

AEA Rail

AEA Rail is a leading independent adviser and supplier of advanced technical services.

It has subsidiaries in The Netherlands, Spain and France.

The business consists of three divisions:

- **Engineering Systems**
- **Products**
- **Signalling Operations & Consultancy**

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Highlights

Business highlights

- Environment sales up 12% to £41 million, Adjusted Operating Profit up 85% to £6.3 million
- Rail – market tough but signalling promising
- Rail – £9 million per annum off cost base and more than 200 jobs cut
- Group – £14 million per annum cost savings achieved to date
- Sale of non-core businesses for £40 million
- Successful fund raising – £30 million
- Reduced pension liability by £35 million
- Proforma net debt at 30 September 2005 reduced to £24.3 million
- Profit before income tax rose to £3.0 million

Financial highlights

For the half-year ended 30 September	2005 £m	2004 £m
Turnover	69.8	83.5
Operating profit/(loss)	3.9	(0.9)
Adjusted operating loss ¹	(0.5)	–
Profit/(loss) before income tax	3.0	(3.6)
Cash used in operations	(12.8)	(9.8)
Basic earnings per share (pence)	3.6	(6.1)
Adjusted earnings per share (pence) ²	(1.2)	(6.5)

1 Reconciliation of adjusted operating profit

	Operating profit/(loss) £m	Redundancy charge £m	Pensions curtailment gain/(charge) £m	Impairment charge £m	Re-financing costs £m	Adjusted profit/(loss) £m
Six months ended 30 September 2005						
AEA Environment	19.8	(0.3)	13.8	–	–	6.3
AEA Rail	(9.2)	(4.0)	11.4	(15.0)	–	(1.6)
Nuclear Programmes	0.5	(0.5)	1.5	–	–	(0.5)
Other	(7.2)	(0.8)	1.0	–	(2.7)	(4.7)
	3.9	(5.6)	27.7	(15.0)	(2.7)	(0.5)
Six months ended 30 September 2004						
AEA Environment	3.4	–	–	–	–	3.4
AEA Rail	4.2	–	–	–	–	4.2
Nuclear Programmes	0.3	–	–	–	–	0.3
Other	(8.8)	(0.8)	(0.1)	–	–	(7.9)
	(0.9)	(0.8)	(0.1)	–	–	–

2 Adjusted earnings per share is stated for continuing businesses before impairment of tangible and intangible assets of £15.0 million (2004: nil). See note 9 for details of the adjusted earnings per share calculation.

Chairman's statement

In the first six months AEA Technology has made very good progress in undertaking the fundamental changes necessary to build a new base for the Company.

Overall turnover declined in the first-half from £83.5 million to £69.8 million. This was entirely due to a lower level of activity in AEA Rail as a result of the very tough market conditions. The adjusted operating loss* was £0.5 million compared to a breakeven position last year.

Our first priority in rebuilding the Company was to reduce debt. This was achieved through a Placing and Open Offer in July, which raised £33.0 million gross. At the same time, the Group successfully negotiated new banking arrangements. The sale of the non-core businesses for £40.0 million at the end of September was another significant step in debt reduction. It also met the Board's second priority which was to improve the focus of the Group through disposals.

A further priority was to reduce the cost base of the Group, particularly in the Centre and in Rail. In the first six months some £14.0 million of annualised cost reductions have been achieved involving the departure of over 250 staff. Further reductions, principally in Rail, are planned in the second half.

The result of all these actions is that AEA Technology is now focused and in a much stronger financial and operational position. AEA Environment is well placed to win work in global markets driven by regulation. Its reputation is high and its expertise in areas like air quality monitoring, energy and waste is world leading. AEA Rail has been downsized to reflect the new market reality.

The Board would like to record its thanks to investors and employees for their support in this period of unparalleled change.



Dr Bernard Bulkin
Chairman
7 December 2005

* See footnote 1 on page 1.

Chief Executive Officer's statement

The business has made progress in the first six months. The prospects are now brighter. We still have many opportunities to improve and we are determined to succeed.

AEA Environment has continued to make strong progress in this half year. Turnover has increased by 12% to £41.0 million, while adjusted operating profits have risen to £6.3* million. There was a significant improvement in operating cash flow which rose to £3.1 million (2004: £0.3 million).

In the UK, AEA Environment secured over £29.0 million in new orders. These included contract extensions and renewals with long-standing customers like Defra, the DTI, the Carbon Trust and the Energy Saving Trust.

AEA Environment also continues to extend its sector reach. In agriculture, two contracts were won totalling £1.8 million, to deliver the Government's Farm Business Advisory Service in two regions, South East & London and West Midlands, through to March 2007.

A world leading reputation in air quality, energy and waste is providing opportunities driven by the international environmental agenda. The expansion of the EU is an additional market driver in Eastern Europe.

In Canada, Kinectrics made good progress with revenues up by 18%. In September, it received its largest ever order with the award of a c£5 million contract for the design and supply of a Kinectrics-patented SorbWeb®Plus secondary transformer oil containment system for Bruce Power, in Ontario. In addition, the Master Services Agreement with its largest customer Ontario Power Generation was renewed for a further three years.

In the US Engineering Services Inc. (ESI), which operates in sectors similar to Kinectrics, made good progress with operating profits 25% higher. Projects were completed with the Tennessee Valley Authority, the US Department of Energy and SOGIN, in Italy.

Overall, the improved business performance in AEA Environment has been achieved by a combination of management action and a strong market. The growth of European legislation and the focus of the UK Government on the environment has been very good for this business. Management have acted to drive sales, reduce costs and improve cash flow. Going forward, they will increasingly focus on making the business more agile to anticipate market opportunities as well as building an international capability of selling to overseas Governments.

In AEA Rail turnover fell by 39% to £23.7 million and the adjusted operating loss was £1.6 million, compared to a profit of £4.2 million last year.

In the face of market conditions, which have remained tough, we have substantially restructured this business through the year. Management has been strengthened and the business reorganised into three operational divisions; Engineering Systems, Products and Signalling Operations & Consultancy.

Despite the difficult market, there were some encouraging wins. In signalling operations, the period saw the successful completion of a design and development contract for Edinburgh Waverley Integrated Electronic Control Centre (IECC) and the winning of a new contract to supply and install an IECC for Heathrow Terminal 5. Both contracts were awarded by Network Rail. Consultancy also enjoyed an improved first-half, helped by winning contracts relating to franchise bidding support for certain Train Operating Companies (TOCs).

In October, we announced a partnership with EuroMaint AB, one of Sweden's leading suppliers of maintenance solutions for the rail sector, creating international opportunities for AEA Rail's products and services. A strategic partnership with US-based Spear Inc., the market leader in enterprise asset management solutions for the transport industry, is also opening up further opportunities outside the UK.

The restructuring in AEA Rail continues. Staff numbers have reduced by more than 200. This is expected to generate full year savings of £9.0 million with a further £2.0 million from lower overheads. A further 100 compulsory redundancies across the business are being implemented with additional annual savings of £3.5 million. This forms part of the ongoing process to ensure that AEA Rail can be profitable on a sustained basis.

In summary, there has been substantial change in the first six months. Improvements have been made to AEA Environment, whilst AEA Rail has been downsized to reflect the tough market conditions. Going forward the Group is in much better shape. I am encouraged by the progress to date but there is still much to do.



Andrew McCree
Chief Executive Officer
7 December 2005

* See footnote 1 on page 1.

Financial review

The Group raised £30.9 million from shareholders and £23.2 million from non-core disposals. This was used to reduce proforma debt from £56.5 million to £24.3 million. A £32.7 million reduction in pension liabilities was negotiated and costs cut by £14.0 million per annum.

Financial review

The Group raised £30.9 million from shareholders and £23.2 million from non-core disposals. This was used to reduce debt from £56.5 million to a proforma net debt of £24.3 million. A £32.7 million reduction in pension liabilities was negotiated and costs cut by £14.0 million per annum.

Operating results

The Interim Report 2005 has been prepared in accordance with International Financial Reporting Standards (IFRS). The comparative figures for 2004 and the year ended 31 March 2005 have been restated accordingly. The notes to the Interim Report contain reconciliations of these restatements.

Management actions

The Group's performance in the half-year reflects the significant management action during the period.

On 7 July, at an EGM the shareholders approved a refinancing plan for the Company. In accordance with the plan Senior Credit facilities of £83.0 million were put in place and £30.9 million was raised through a Placing and Open Offer. The cash raised from shareholders was used to repay debt and the Senior Credit Facilities were reduced to £72.8 million.

A significant divestment of a portfolio of companies was approved by shareholders at an EGM held on 30 September 2005. This divestment generated net proceeds of £23.2 million that was used to repay bank debt and the Senior Credit Facilities were reduced to the current £53.7 million. The sale of non-core business resulted in a provisional profit of £1.8 million. The discontinued operations generated a profit of £0.5 million (2004: (£1.0) million).

During the half-year a substantial cost reduction programme was carried out with more than 250 staff leaving the Group to save £12.0 million p.a. at a cost of £5.6 million.

Management re-negotiated the terms of the AEA Technology plc Pension Scheme as noted below in Pension liabilities.

Segmental analysis

A segmental analysis of adjusted operating profits is given on page 4 Financial highlights. A segmental analysis of turnover and operating profit, as required by IFRS, is given in note 4.

AEA Environment had a strong first half-year with turnover up 12% at £41.0 million and operating profit rose to £19.8 million including a pension curtailment gain of £13.8 million.

AEA Rail's performance reflects the tough market conditions in the rail industry. Turnover was £23.7 million, down 39% on the corresponding period last year. The Operating loss of £9.2 million is after charging redundancy costs of £4.0 million, impairment costs of £15.0 million and crediting pension curtailment gains of £11.4 million. Excluding these one-off costs, performance was down significantly against the £4.2 million profit in the first half-year last year.

Pension liabilities

Pension liabilities were reduced by £32.7 million due to the re-negotiation of members benefits contribution rates and the rail redundancy programme. Of this £27.7 million was attributable to continuing business and £5.0 million to the disposals. Curtailment gains of £32.7 million that arose during the period were as a result of the renegotiation of contribution rates and the redundancy exercise.

Pension costs

Pension costs have been included using the full liability method under IFRS. The pension cost is analysed in note 6.

Impairment

Due to the performance of the Rail business, an impairment review was carried out during the period. A £15.0 million charge (2004: nil) arose due to the calculated impairment of certain tangible and intangible assets.

Profit before tax

Loss before tax is after crediting dividend received from the Company's investment in Hunting BRAE Limited. The finance charges include the interest on the New Senior Credit facilities.

Taxation

The overall credit to the Group was £0.3 million (2004: charge of £0.5 million). The tax comprises current tax due in various jurisdictions, offset by a credit relating to deferred tax, principally in Canada.

At 30 September the deferred tax asset was £9.0 million (2004: £10.8 million).

Cash flow and borrowings

Net debt decreased from £56.5 million to £47.5 million. The net debt further reduced to a proforma £24.3 million on 7 October when the £23.2 million proceeds from the portfolio divestment were received.

Post balance sheet events

There were no post balance sheet events.



David Lindsay
Group Finance Director
7 December 2005

Independent review report to AEA Technology plc

Introduction

We have been instructed by the Company to review the financial information for the six months ended 30 September 2005 which comprises the interim balance sheet as at 30 September 2005, the consolidated statement of income, cash flow, statement of recognised income and expense and changes in shareholders' equity for the six months then ended, and related notes. We have read the other information contained in the Interim Report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

Directors' responsibilities

The Interim Report, including the financial information contained therein, is the responsibility of, and has been approved by the Directors. The Directors are responsible for preparing the Interim Report in accordance with the Listing Rules of the Financial Services Authority.

As disclosed in note 2, the next annual financial statements of the Company will be prepared in accordance with accounting standards adopted for use in the European Union. This Interim Report has been prepared in accordance with the basis set out in note 2.

The accounting policies are consistent with those that the Directors intend to use in the next annual financial statements. As explained in note 2 there is, however, a possibility that the Directors may determine that some changes are necessary when preparing the full annual financial statements for the first time in accordance with accounting standards adopted for use in the European Union. The IFRS standards and IFRIC *International Financial Reporting Interpretations Committee* interpretations that will be applicable and adopted for use in the European Union at 31 March 2006 are not known with certainty at the time of preparing this Interim Report.

Review work performed

We conducted our review in accordance with guidance contained in Bulletin 1999/4 issued by the Auditing Practices Board for use in the United Kingdom. A review consists principally of making enquiries of management and applying analytical procedures to the financial information and underlying financial data and, based thereon, assessing whether the disclosed accounting policies have been applied. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance. Accordingly we do not express an audit opinion on the financial information. This report, including the conclusion, has been prepared for and only for the Company for the purpose of the Listing

Rules of the Financial Services Authority and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 30 September 2005.

PricewaterhouseCoopers LLP

Chartered Accountants
Reading
7 December 2005

Notes:

- (a) The maintenance and integrity of the AEA Technology plc website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Interim Report since it was initially presented on the website.
- (b) Legislation in the United Kingdom governing the preparation and dissemination of financial information may differ from legislation in other jurisdictions.

Consolidated interim income statement

(unaudited)

	Notes	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Continuing operations				
Turnover	4	69.8	83.5	156.9
Cost of sales		(44.6)	(50.9)	(113.5)
Gross profit				
Other operating income		0.7	0.7	1.4
Curtailment gain/(loss) in pension scheme	6	27.7	(0.1)	(0.3)
Redundancy costs	13	(5.6)	(0.8)	(1.2)
Other exceptional costs		–	(1.8)	(5.3)
Administrative expenses		(29.1)	(31.5)	(47.7)
Impairment of assets		(15.0)	–	–
Operating profit/(loss)				
	4	3.9	(0.9)	(9.7)
Share in loss of joint ventures and associates		–	–	(0.1)
Investment income		1.4	–	–
Finance costs	7	(12.7)	(12.6)	(24.2)
Finance income	7	10.4	9.9	18.1
Profit/(loss) before income tax				
		3.0	(3.6)	(15.9)
Income tax credit/(expense)	8	0.3	(0.5)	(5.3)
Profit/(loss) for the period from continuing operations				
		3.3	(4.1)	(21.2)
Discontinued operations				
Profit/(loss) for the period from discontinued operations	12	0.5	(1.0)	(8.3)
Release of termination provision		–	1.0	0.6
Profit on disposal of businesses	12	1.8	1.4	0.6
Discontinued operations				
		2.3	1.4	(7.1)
Profit/(loss) for the period				
		5.6	(2.7)	(28.3)
Attributable to:				
Equity holders of the Company		5.7	(2.6)	(28.1)
Minority interest		(0.1)	(0.1)	(0.2)
Earnings per share attributable to the equity holders of the Company during the period				
Basic (pence)	9	3.6	(6.1)	(31.4)
Diluted (pence)	9	3.2	(6.1)	(31.4)
Earnings per share on discontinued operations attributable to the equity holders of the Company during the period				
Basic and diluted (pence)	9	0.5	(1.5)	(12.3)

The notes on pages 10 to 29 are an integral part of this Interim Report.

Consolidated interim statement of recognised income and expense (unaudited)

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Exchange difference for translation	1.5	0.7	(0.7)
Actuarial (losses)/gains on defined benefit plans	(8.0)	7.7	15.3
Net income/(expense) recognised directly in equity	(6.5)	8.4	14.6
Profit/(loss) for the period	5.6	(2.7)	(28.3)
Total recognised income and expense	(0.9)	5.7	(13.7)

Consolidated interim statement of changes in shareholders' equity (unaudited)

	Attributable to equity holders of the Company						Total equity £m
	Share capital (note 5) £m	Share premium (note 5) £m	Fair value and other reserves £m	Cumulative translation adjustment £m	Retained earnings £m	Minority interest £m	
Balance as at 1 April 2004	8.3	10.6	1.0	–	(170.7)	0.9	(149.9)
Currency translation adjustments	–	–	–	0.7	–	–	0.7
Loss for the period	–	–	–	–	(2.6)	(0.1)	(2.7)
Dividend on ordinary shares	–	–	–	–	(2.5)	–	(2.5)
Fair value of employee share option schemes	–	–	0.3	–	–	–	0.3
Issue of shares in the period	–	0.1	–	–	–	–	0.1
Actuarial gains on defined benefit plans	–	–	7.7	–	–	–	7.7
Balance as at 30 September 2004	8.3	10.7	9.0	0.7	(175.8)	0.8	(146.3)
Currency translation adjustments	–	–	–	(1.4)	–	–	(1.4)
Loss for the period	–	–	–	–	(25.5)	(0.1)	(25.6)
Dividend on ordinary shares	–	–	–	–	(1.0)	–	(1.0)
Fair value of employee share option schemes	–	–	0.5	–	–	–	0.5
Actuarial gains on defined benefit plans	–	–	7.6	–	–	–	7.6
Balance as at 31 March 2005	8.3	10.7	17.1	(0.7)	(202.3)	0.7	(166.2)
Currency translation adjustments	–	–	–	1.5	–	–	1.5
Profit/(loss) for the period	–	–	–	–	5.7	(0.1)	5.6
Disposal of subsidiaries	–	–	–	(1.2)	(3.8)	(0.6)	(5.6)
Fair value of employee share option schemes	–	–	0.6	–	–	–	0.6
Issue of shares in the period	6.9	24.0	–	–	–	–	30.9
Actuarial losses on defined benefit plans	–	–	(8.0)	–	–	–	(8.0)
Balance as at 30 September 2005	15.2	34.7	9.7	(0.4)	(200.4)	–	(141.2)

The notes on pages 10 to 29 are an integral part of this Interim Report.

Consolidated interim balance sheet (unaudited)

Notes	At 30 September 2005 £m	At 30 September 2004 £m	At 31 March 2005 £m
ASSETS			
Non-current assets			
Intangible assets including goodwill	17.8	37.0	37.6
Property, plant and equipment	13.2	35.5	25.1
Investment in associates and other companies	2.1	3.4	3.1
Deferred income tax assets	9.0	10.8	5.9
	42.1	86.7	71.7
Current assets			
Inventories	7.4	23.6	22.4
Trade and other receivables	78.9	72.8	68.1
Current income tax assets	0.3	–	–
Cash and cash equivalents	12.3	9.6	7.4
	98.9	106.0	97.9
Total assets	141.0	192.7	169.6
EQUITY			
Capital and reserves attributable to the Company's equity shareholders			
Share capital and premium	5	49.9	19.0
Fair value and other reserves		9.3	9.7
Retained earnings		(200.4)	(175.8)
		(141.2)	(202.3)
Minority interest		–	(147.1)
		0.8	0.7
Total equity		(141.2)	(146.3)
LIABILITIES			
Non-current liabilities			
Trade and other payables		1.6	9.2
Retirement benefit liabilities	6	122.0	160.3
Provisions and other liabilities and charges		27.1	18.9
		150.7	188.4
Current liabilities			
Trade and other payables		71.7	90.5
Current income tax liabilities		–	–
Borrowings		59.8	60.1
		131.5	150.6
Total liabilities		282.2	339.0
Total equity and liabilities		141.0	192.7

The notes on pages 10 to 29 are an integral part of this Interim Report.
This Interim Report was approved by the Board on 7 December 2005.

Signed on behalf of the Board of Directors



Dr Bernard Bulkin
Chairman



Andrew McCree
Chief Executive Officer

Consolidated interim cash flow statement

(unaudited)

	Notes	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Cash flows from operating activities				
Cash used in operations	10	(12.8)	(9.8)	(1.2)
Interest paid		(2.2)	(2.1)	(4.7)
Interest received		1.4	0.5	0.8
Dividends paid to minority interests		–	(0.2)	(0.3)
Income tax paid		(1.3)	(1.3)	(2.0)
Net cash used in operating activities		(14.9)	(12.9)	(7.4)
Cash flows from investing activities				
Purchases of property, plant and equipment		(3.2)	(2.8)	(5.7)
Purchases of intangible assets		(1.5)	(1.7)	(3.2)
Cash disposed of in subsidiaries divested		(2.1)	–	(1.9)
Payments for acquisitions of associates and subsidiaries		–	(0.1)	(0.1)
Loans to associates		–	–	(0.5)
Proceeds from disposals		–	0.1	0.3
Dividends received		1.4	–	–
Net cash used in generated from investing activities		(5.4)	(4.5)	(11.1)
Cash flows from financing activities				
Repayment of borrowings		(61.5)	–	–
Draw down of bank facilities		55.8	5.7	8.1
Dividends paid to Company equity holders		–	–	(3.5)
Proceeds from new equity issues	5	30.9	0.1	0.1
Net cash generated from financing activities		25.2	5.8	4.7
Net increase/(decrease) in cash and bank overdrafts		4.9	(11.6)	(13.8)
Cash and bank overdrafts at beginning of period		7.4	21.2	21.2
Cash and bank overdrafts at end of period		12.3	9.6	7.4

The notes on pages 10 to 29 are an integral part of this Interim Report.

Notes to the Interim Report (unaudited)

1 General information

AEA Technology plc ("the Company") and its subsidiaries (together "AEA Technology Group" or "the Group") is one of Britain's leading technology companies. The Group provides consultancy and technical services in two core markets, Rail and Environment. The Group operates from locations worldwide including Harwell, Derby, London, and Glasgow in the UK and also has offices in Europe and North America.

During the period, the Group disposed of several companies that the Board considered to be operating in non-core activities.

The Company is a public limited company, incorporated and domiciled in the United Kingdom. The address of the registered office is 329 Harwell, Didcot, Oxfordshire, OX11 0QJ.

The Company has its primary listing on the London Stock Exchange.

This Interim Report for the six months ended 30 September 2005 was approved for issue by the Board on 7 December 2005.

2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of this Interim Report are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Basis of preparation

The Group has previously prepared its financial statements under UK Generally Accepted Accounting Principles ("UK GAAP").

Following a directive issued by the European Parliament in July 2002, the Group is required to prepare its 2005/6 consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS"). Accordingly, this unaudited Interim Report has been prepared using IFRS accounting policies consistent with those which management expects to apply in the Group's first IFRS Annual Report and Financial Statements for the year ending 31 March 2006. The accounting policies followed in this Interim Report have been applied consistently to all periods under review, and comparative figures restated to reflect adjustments required to comply with IFRS.

The Group has taken the exemption within IFRS 1 *First Time Adoption of IFRS* to apply IAS 32 *Financial Instruments: Presentation and Disclosure* and IAS 39 *Financial Instruments: Recognition and Measurement* from 1 April 2005 and not to restate prior period comparatives upon adoption. The disclosures required by IFRS 1 concerning the transition from UK GAAP to IFRS are provided in note 3.

IFRS currently in issue are subject to ongoing review and endorsement by the European Commission, as well as possible amendment by the IASB ("International Accounting Standards Board"), and are therefore subject to possible change. Further standards or interpretations may also be issued that could be applicable for the full year consolidated financial statements. These potential changes could result in the need to change the basis of accounting or presentation of certain financial information from that presented in this document.

This Interim Report for the six months ended 30 September 2005 does not constitute statutory financial statements as defined in section 240 of The Companies Act 1985.

Comparative figures for the period ended 30 September 2004 and the year ended 31 March 2005 are set out in note 3.

Basis of accounting

This Interim Report has been prepared under the historical cost convention as modified by the revaluation of financial assets and financial liabilities, including derivative instruments, at fair value with the gains or losses recognised in the income statement.

The areas involving a higher degree of judgment or complexity, or areas where assumptions or estimates are significant to the Interim Report, are disclosed in the notes.

Basis of consolidation

(a) Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group; they are de-consolidated from the date on which control ceases. The purchase method of accounting is used for the acquisition of subsidiaries of the Group. The cost of an acquisition is measured as the fair value of assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributed to the acquisition. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the Group's share of the identifiable net assets acquired, the difference is recognised directly in the income statement.

b) Associates and joint ventures

Associates are all entities over which the Group has significant influence, but no control; generally accompanying a shareholding of between 20% and 50% of the voting rights. Joint ventures are entities subject to joint control. Investments in associates and joint ventures are accounted for on the equity method of accounting and initially recognised at cost. The Group's investment in associates and joint ventures includes goodwill, net of any accumulated impairment loss.

Turnover and revenue recognition

Group turnover represents the total value of income (excluding sales taxes and intra-group sales) earned in respect of products delivered and services rendered to customers, royalties and contributions receivable in support of programmes, and the value of long-term contract work completed. Turnover relates to ordinary activities and is stated after trade discounts.

Income from licences where the underlying intellectual property is secure and on which the Group will not incur future costs is recognised on signing of the contract with the licensee. Where the Group will incur future maintenance and support costs and all components of the contract do not operate independently the full contract value is recognised rateably over the period of the contract. Where the components do operate independently and fair values can be allocated to the individual components each component is treated as if it were a separate contract. Any invoices raised or cash received in advance of recognition of the income is included within payments received on account in trade and other payables. As detailed on page 13, income on long-term contracts is recognised based on the value of work completed under the contract.

Segmental reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular geographical region that is subject to risks and returns that are different from those of segments operating in other geographical region.

Government grants

Capital based government grants are included within accruals and deferred income in the balance sheet and credited to operating profit over the expected useful economic lives of the assets to which they relate. Revenue based government grants are credited to operating profit to match the expenditure to which they relate.

Investment income

Income from fixed asset investments comprises dividend income which is recognised when the right to receive payment is established.

Property, plant and equipment

All property, plant and equipment is shown at cost less depreciation and impairment. Cost includes expenditure directly related to the acquisition of the assets.

Depreciation is calculated using the straight line method to allocate the costs of each asset to its residual value over its estimated useful life, as follows:

Freehold buildings	up to 30 years
Plant and equipment:	
– computers and vehicles	up to 5 years
– other plant and equipment	5 to 10 years
Assets in course of construction	not depreciated

The assets' residual values and useful lives are reviewed and adjusted if appropriate at each balance sheet date. An asset's carrying value is written down immediately to its recoverable amount if it is greater than its estimated recoverable amount.

Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of net identifiable assets acquired. Goodwill on acquisitions of subsidiaries is included in intangible assets; goodwill on acquisitions of associates is included in investments in associates. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units for the purposes of impairment testing.

(b) Research and development

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when it is probable that the project will be a success, considering its commercial and technical feasibility, and costs can be measured reliably. Other development expenditure is recognised as an expense. Development costs that have a finite useful life and that have been capitalised are amortised from the commencement of commercial sale of the product on a straight-line basis over the period of its expected benefit, not exceeding twenty years.

Notes to the Interim Report (unaudited) continued

2 Summary of significant accounting policies *continued*

(c) *Other intangible assets*

Intangible assets acquired separately are capitalised at cost and those acquired in a business combination are capitalised at fair value as at the date of acquisition.

Intangible assets, excluding development costs, that are created within the business are not capitalised and expenditure is charged against profits in the year in which it is incurred.

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Intangible assets arising from a business combination are amortised over their remaining useful lives.

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of the intangible asset. The estimated useful lives are as follows:

Acquired software licenses	3 to 5 years
Trademarks and licenses	up to 20 years
Other intangibles	5 to 10 years

Intangible assets are tested for impairment annually or at the cash generating unit level. Useful lives are also examined on an annual basis and adjustments, where applicable, are made on a prospective basis.

Income tax

Income tax expense represents the sum of the tax currently payable and deferred tax.

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

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition, other than in a business combination, of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and amended to the extent that it is probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Employee benefits

(a) Pension obligations

The Group operates a number of pension schemes in the UK and overseas. The Group has both defined benefit and defined contribution schemes.

The liability recognised in the balance sheet in respect of defined benefit pension schemes is the present value of the defined benefit obligation at the balance sheet date less the fair value of scheme assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension liability. The defined benefits schemes are funded through payments to insurance companies or trustee-administered funds, determined by periodic actuarial calculations.

Cumulative actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are recognised in the statement of recognised income and expense.

For defined contribution scheme, the Group pays contributions to privately administered pension insurance plans on a mandatory, contractual or voluntary basis. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or reduction in future payment is available.

(b) Other post-retirement benefit obligations

Some Group companies provide post-retirement healthcare benefits to their retirees. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age and the completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment using an accounting methodology similar to that used for defined benefit pension schemes.

(c) Share-based plans

The Group's management awards high-performing employees bonuses in the form of share options from time to time, on a discretionary basis. The options are subject to three to five year service vesting conditions. The fair value determined at the grant date of the option is recognised as an employee benefit expense on a straight-line basis over the vesting period. The liability is recognised in "Fair value and other reserves" until the options are exercised when the proceeds received, net of attributable transaction costs, are credited to share capital and premium.

(d) Short-term employee benefits

Accruals are included to reflect the cost of short-term compensation to employees for absences such as paid annual leave.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle the obligation.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the balance sheet date and are discounted to present value where the effect is material.

Provision is made for future costs arising from the closure and decontamination of certain experimental facilities and the management and final disposal of wastes where these activities are a Group responsibility. Full liability is recognised when operations commence and the facility becomes contaminated.

Stock and work in progress (excluding long-term contract work in progress)

Stock is valued at the lower of cost and net realisable value. Where necessary, provision is made for obsolete, slow moving and defective stock. Work in progress is valued at cost, less the cost of work invoiced on incomplete contracts and less foreseeable losses. Cost comprises purchase cost plus production and related overheads.

Long-term contracts

Turnover on long-term contracts is recognised according to the stage reached in the contract by reference to the value of work completed. An appropriate estimate of the profit attributable to work completed is recognised once the outcome of the contract can be assessed with reasonable certainty. The amount by which the turnover exceeds payments on account is shown under debtors as amounts recoverable on contracts. The costs on long-term contracts not yet taken to the profit and loss account less related foreseeable losses and payments on account are shown in stocks as long-term contract work in progress.

Notes to the Interim Report (unaudited) continued

2 Summary of significant accounting policies *continued*

Leases

Costs in respect of operating leases are charged on a straight-line basis over the lease term. Assets acquired under finance leases are capitalised and the outstanding future lease obligations are shown as creditors.

Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to risk from foreign exchange and interest rate fluctuations. The Group does not hold or issue derivative financial instruments for speculative purposes or for trade in those instruments.

To achieve hedge accounting, the Group is required to designate these financial instruments against specific assets, liabilities, income and expenses. All such instruments are recognised initially at cost and subsequently measured at fair value as at the balance sheet date and the effectiveness of each hedge tested against defined criteria. Changes in the fair value of the financial instruments are recognised either in the profit or loss for the period or, in the case of a cash flow hedge, directly in equity and subsequently recognised in the profit or loss for the period when the underlying transaction is realised. For financial instruments designated as fair value hedges, changes in the fair value of the hedged item and the derivative instrument are recognised in the profit or loss for the period. Gains and losses on financial instruments both realised and unrealised, that do not qualify for hedge accounting, are included in the profit or loss for the period. All financial instruments are recognised as either financial assets or financial liabilities.

Foreign currencies

Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates ruling at the balance sheet date. These exchange differences are recognised in the income statement unless they qualify for hedging accounting treatment, in which case they are recognised directly in reserves.

For consolidation purposes the assets and liabilities of overseas subsidiaries, joint ventures and associates are translated at the exchange rates ruling at the balance sheet date. The income statements of overseas operations are translated at average rates of exchange during the year. All resulting exchange differences including exchange differences arising from translation of borrowings and other currency instruments designated as hedges of investments are recognised directly in a separate component of reserves. Translation differences that arose before the transition date to IFRS are presented in equity but not as a separate component. When the foreign operation is sold, the cumulative exchange differences recognised since the adoption of IFRS are recognised in the income statement as part of the profit or loss on disposal.

3 Transition to IFRS

3.1 Application of IFRS 1 *First Time Adoption of IFRS*

The Group's financial statements for the year ended 31 March 2006 will be the first annual financial statements that comply with IFRS. This Interim Report has been prepared as described in note 2. The Group has applied IFRS 1 in preparing this Interim Report.

The Group's transition date is 1 April 2004. The Group prepared its opening IFRS balance sheet at that date. The reporting date of this Interim Report is 30 September 2005. The Group's IFRS adoption date is 1 April 2005.

In preparing this Interim Report in accordance with IFRS 1, the Group has applied the mandatory exemptions and certain of the optional exemptions from full retrospective application of IFRS.

Exemptions from full retrospective application elected by the Group

(a) *Business combinations*

The Group has elected to apply IFRS 3 *Business Combinations* prospectively. Consequently, acquisitions made before 1 April 2004 have not been restated for the effects of IFRS 3 and IAS 21 *The Effects of Changes in Foreign Exchange Rates* on goodwill arising on those acquisitions.

(b) *Property, plant and equipment*

The Group has elected to adopt the UK GAAP accounting values as the deemed cost for IFRS.

(c) *Employee benefits*

The Group has elected to fully recognise all actuarial gains and losses on its pension schemes.

(d) *Cumulative translation differences*

The Group has elected to apply IAS 21 and disclose separately the exchange differences arising on the translation of foreign subsidiaries' results as a component of equity with effect from 1 April 2004.

(e) Compound financial instruments

The Group has elected not to separate the equity and liability components of the instrument provided that the liability was settled before 1 April 2005.

(f) Designation of previously recognised financial instruments

The Group has elected that all financial instruments, except those classified as a hedge, are designated as a financial asset or liability and value at fair value at each balance sheet date, with the movement taken to the income statement with effect from 1 April 2005.

(g) Share based payment transactions

The Group has elected not to apply IFRS 2 *Share-Based Payments* to equity instruments that were granted before 1 April 2004.

Exceptions from full retrospective application followed by the Group*(a) De-recognition of financial assets and liabilities*

The Group has elected not to apply the IAS 39 *Financial Instruments: Recognition and Measurement* de-recognition requirements for non-derivative financial assets and liabilities before 1 April 2004.

(b) Hedge accounting

The Group has applied IFRS 1 with effect from 1 April 2005 to all qualifying hedging instruments so that they have been measured at fair value and any deferred gains or losses on the hedging instruments have been eliminated and reported as assets or liabilities.

(c) Estimates

All estimates made by the Group in preparing the Interim Report under IFRS as at 1 April 2004 are consistent with estimates made under UK GAAP at that date.

(d) Assets classified as held for sale and discontinued operations

The transitional provisions of IFRS 5 *Non-current Assets Classified as Held for Sale and Discontinued Operations*, which requires the prospective application of the standard from 1 April 2005, have been applied by the Group.

3.2 Reconciliations between IFRS and UK GAAP**Summary of equity**

	Notes	1 April 2004	30 September 2004	31 March 2005
Total equity under UK GAAP		12.3	10.4	(13.7)
Minority interest		0.9	0.9	0.8
		13.2	11.3	(12.9)
Capitalisation of development costs	3.3.1	5.8	7.1	8.4
Annual leave accrual	3.3.2	(1.4)	(0.9)	(1.6)
Reversal of goodwill amortisation	3.3.3	–	1.2	2.1
Reclassification of leases as finance leases	3.3.4	(0.7)	(0.5)	(0.9)
Change in revenue recognition policy	3.3.5	–	(0.6)	(0.8)
Net effect of changes in pension accounting	3.3.6	(167.5)	(162.9)	(158.3)
Change in accounting for dividends	3.3.7	2.5	1.0	–
Share option cost recognition	3.3.8	(0.1)	(0.1)	(0.2)
Deferred tax adjustments	3.3.9	(1.7)	(1.8)	(1.9)
Impact of other non-material items	3.3.10	–	(0.1)	(0.1)
Total equity under IFRS		(149.9)	(146.3)	(166.2)

Notes to the Interim Report (unaudited) continued

3 Transition to IFRS *continued*

Reconciliation of equity at 1 April 2004

	UK GAAP £m	Effect of transition to IFRS £m	IFRS £m
ASSETS			
Non-current assets			
Intangible assets including goodwill	29.0	6.8	35.8
Property, plant and equipment	33.4	2.2	35.6
Investment in associates and other companies	3.3	–	3.3
Deferred income tax assets	12.5	(1.6)	10.9
	78.2	7.4	85.6
Current assets			
Inventories	23.2	(0.1)	23.1
Trade and other receivables	92.6	(16.0)	76.6
Cash and cash equivalents	22.3	(1.1)	21.2
	138.1	(17.2)	120.9
Total assets	216.3	(9.8)	206.5
EQUITY			
Capital and reserves attributable to the Company's equity shareholders			
Share capital and premium	18.9	–	18.9
Fair value and other reserves	0.7	0.3	1.0
Retained earnings	(7.3)	(163.4)	(170.7)
	12.3	(163.1)	(150.8)
Minority interest	0.9	–	0.9
Total equity	13.2	(163.1)	(149.9)
LIABILITIES			
Non-current liabilities			
Trade and other payables including borrowings	11.3	1.0	12.3
Retirement benefit liabilities	–	165.1	165.1
Provisions and other liabilities	38.4	(12.4)	26.0
	49.7	153.7	203.4
Current liabilities			
Trade and other payables	96.1	0.7	96.8
Current income tax liabilities	0.6	–	0.6
Borrowings	56.7	(1.1)	55.6
	153.4	(0.4)	153.0
Total liabilities	203.1	153.3	356.4
Total equity and liabilities	216.3	(9.8)	206.5

Reconciliation of equity at 30 September 2004

	UK GAAP £m	Effect of transition to IFRS £m	IFRS £m
ASSETS			
Non-current assets			
Intangible assets including goodwill	27.7	9.3	37.0
Property, plant and equipment	33.3	2.2	35.5
Investment in associates and other companies	3.4	–	3.4
Deferred income tax assets	12.7	(1.9)	10.8
	77.1	9.6	86.7
Current assets			
Inventories	23.8	(0.2)	23.6
Trade and other receivables	90.2	(17.4)	72.8
Cash and cash equivalents	10.8	(1.2)	9.6
	124.8	(18.8)	106.0
Total assets	201.9	(9.2)	192.7
EQUITY			
Capital and reserves attributable to the Company's equity shareholders			
Share capital and premium	19.0	–	19.0
Fair value and other reserves	0.7	9.0	9.7
Retained earnings	(9.3)	(166.5)	(175.8)
	10.4	(157.5)	(147.1)
Minority interest	0.9	(0.1)	0.8
Total equity	11.3	(157.6)	(146.3)
LIABILITIES			
Non-current liabilities			
Trade and other payables including borrowings	7.8	1.4	9.2
Retirement benefit liabilities	–	160.3	160.3
Provisions and other liabilities	33.2	(14.3)	18.9
	41.0	147.4	188.4
Current liabilities			
Trade and other payables	88.3	2.2	90.5
Borrowings	61.3	(1.2)	60.1
	149.6	1.0	150.6
Total liabilities	190.6	148.4	339.0
Total equity and liabilities	201.9	(9.2)	192.7

Notes to the Interim Report (unaudited) continued

3 Transition to IFRS *continued*

Reconciliation of equity at 31 March 2005

	UK GAAP £m	Effect of transition to IFRS £m	IFRS £m
ASSETS			
Non-current assets			
Intangible assets including goodwill	26.0	11.6	37.6
Property, plant and equipment	23.3	1.8	25.1
Investment in associates and other companies	3.1	–	3.1
Deferred income tax assets	7.8	(1.9)	5.9
	60.2	11.5	71.7
Current assets			
Inventories	22.5	(0.1)	22.4
Trade and other receivables	84.7	(16.6)	68.1
Cash and cash equivalents	12.4	(5.0)	7.4
	119.6	(21.7)	97.9
Total assets	179.8	(10.2)	169.6
EQUITY			
Capital and reserves attributable to the Company's equity shareholders			
Share capital and premium	19.0	–	19.0
Fair value and other reserves	0.7	15.7	16.4
Retained earnings	(33.4)	(168.9)	(202.3)
	(13.7)	(153.2)	(166.9)
Minority interest	0.8	(0.1)	0.7
Total equity	(12.9)	(153.3)	(166.2)
LIABILITIES			
Non-current liabilities			
Trade and other payables including borrowings	4.1	1.6	5.7
Retirement benefit liabilities	–	156.9	156.9
Provisions and other liabilities	34.5	(14.2)	20.3
	38.6	144.3	182.9
Current liabilities			
Trade and other payables	83.5	3.8	87.3
Current income tax liabilities	1.7	–	1.7
Borrowings	68.9	(5.0)	63.9
	154.1	(1.2)	152.9
Total liabilities	192.7	143.1	335.8
Total equity and liabilities	179.8	(10.2)	169.6

Reconciliation of net income for six months ended 30 September 2004

	UK GAAP £m	UK GAAP discontinued operations £m	Effect of transition to IFRS £m	IFRS £m
Continuing operations				
Turnover	117.4	(34.5)	0.6	83.5
Cost of sales	(72.0)	17.8	3.3	(50.9)
Gross profit/(loss)	45.4	(16.7)	3.9	32.6
Other operating income	1.4	(0.7)	–	0.7
Curtailment loss on pension scheme	–	–	(0.1)	(0.1)
Redundancy costs	(0.8)	–	–	(0.8)
Other exceptional costs	(1.8)	–	–	(1.8)
Administrative expenses	(45.5)	18.4	(4.4)	(31.5)
Operating loss	(1.3)	1.0	(0.6)	(0.9)
Share in (loss)/profit of joint ventures and associates	(0.3)	0.3	–	–
Finance costs	(3.0)	0.7	(10.3)	(12.6)
Finance income	1.3	(0.1)	8.7	9.9
Loss before income tax	(3.3)	1.9	(2.2)	(3.6)
Income tax (expense)/credit	(0.5)	0.1	(0.1)	(0.5)
Loss for the period from continuing operations	(3.8)	2.0	(2.3)	(4.1)
Discontinued operations				
Loss for the period from discontinued operations	–	(2.0)	1.0	(1.0)
Release of termination provision	1.0	–	–	1.0
Profit on disposal of business	1.4	–	–	1.4
Discontinued operations	2.4	(2.0)	1.0	1.4
Loss for the period	(1.4)	–	(1.3)	(2.7)
Attributable to:				
Equity holders of the Company	(1.3)	–	(1.3)	(2.6)
Minority interest	(0.1)	–	–	(0.1)

Notes to the Interim Report (unaudited) continued

3 Transition to IFRS *continued*

Reconciliation of net income for year ended 31 March 2005

	UK GAAP £m	UK GAAP discontinued operations £m	Effect of transition to IFRS £m	IFRS £m
Continuing operations				
Turnover	236.7	(78.9)	(0.9)	156.9
Cost of sales	(171.2)	49.7	8.0	(113.5)
Gross profit/(loss)	65.5	(29.2)	7.1	43.4
Other operating income	2.6	(1.2)	–	1.4
Curtailement loss on pension scheme	–	–	(0.3)	(0.3)
Redundancy costs	(1.2)	–	–	(1.2)
Other exceptional costs	(5.4)	(0.6)	0.7	(5.3)
Administrative expenses	(69.7)	28.9	(6.9)	(47.7)
Impairment of assets	(6.8)	6.8	–	–
Operating loss	(15.0)	4.7	0.6	(9.7)
Share in (loss)/profit of joint venture and associates	(0.6)	0.6	(0.1)	(0.1)
Finance costs	(4.9)	1.5	(20.8)	(24.2)
Finance income	0.7	(0.1)	17.5	18.1
Loss before income tax	(19.8)	6.7	(2.8)	(15.9)
Income tax (expense)/credit	(5.5)	0.4	(0.2)	(5.3)
Loss for the period from continuing operations	(25.3)	7.1	(3.0)	(21.2)
Discontinued operations				
Loss for the period from discontinued operations	–	(7.1)	(1.2)	(8.3)
Release of termination provision	0.6	–	–	0.6
Profit on disposal of business	0.6	–	–	0.6
Discontinued operations	1.2	(7.1)	(1.2)	(7.1)
Loss for the period	(24.1)	–	(4.2)	(28.3)
Attributable to:				
Equity holders of the Company	(23.9)	–	(4.2)	(28.1)
Minority interest	(0.2)	–	–	(0.2)

Reconciliation of equity at 1 April 2005

The adoption of IAS 32 and IAS 39 did not have a material effect on the equity of the Group, so no reconciliation of equity between 31 March 2005 and 1 April 2005 has been included.

Reconciliation of cash flows for the six months ended 30 September 2005

The adoption of IFRS did not have a material effect on the Group's consolidated cash flow statement, so no reconciliation of cash flows has been included.

3.3 Notes to the reconciliations

- 3.3.1 Capitalisation of development costs – writing back development costs previously expensed. Under UK GAAP development costs were written off as incurred, however under IFRS, qualifying development costs must be capitalised and amortised over their useful lives.
- 3.3.2 Annual leave accrual – the cost of providing annual and other long-term leave for employees.
- 3.3.3 Reversal of goodwill amortisation – writing back goodwill amortised in the comparative period. Under IFRS there is no annual amortisation of goodwill. This has been replaced by an annual impairment test. The Group elected to adopt the carrying value under UK GAAP as at 1 April 2004 as the initial cost for IFRS purposes.

- 3.3.4 Reclassification of leases as finance leases – the reclassification of certain leases recognised as operating leases under UK GAAP as finance leases in accordance with IAS 17 *Leases*.
- 3.3.5 Revenue recognition – recognition of income over the life of a software license as required by IFRS rather than at the start of the license under UK GAAP.
- 3.3.6 Pension accounting – adjustments required to remove the UK GAAP method of accounting for pensions under SSAP 24 *Accounting for Pension Costs* and replace these entries with the IFRS method of accounting under IAS 19 *Employee Benefits*.
- 3.3.7 Accounting for dividends – recognition of dividends when approved by the shareholders or the Board rather than on a proposed basis.
- 3.3.8 Share option costs – the allocation of the fair value of the options granted to employees over the vesting period. The fair value of the share option is calculated using option pricing models and adjusted to reflect the actual and expected levels of vesting.
- 3.3.9 Deferred taxation – reflects the tax effect of the IFRS adjustments listed above.
- 3.3.10 Other non-material items – adjustments to comply with IFRS in respect of provisions for rehabilitation and contamination and the adjustment of overheads allocated to stock and work-in-progress.
- 3.3.11 Cash equivalents under IFRS includes bank overdrafts and other short term cash equivalents; overdrafts were classified as borrowings under UK GAAP.

4 Segmental information

(a) Business segments

At 30 September 2005, the Group is organised into two core business segments AEA Environment and AEA Rail. Nuclear Programmes and the 'Other' segment includes the Group's non-core activities and the costs of Group's head office.

The segmental turnover is as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
AEA Environment – UK	25.2	21.8	49.9
Kinectrics	12.0	10.2	22.2
Engineering Services Inc	3.8	4.7	9.4
AEA Environment	41.0	36.7	81.5
AEA Rail	23.7	39.1	59.8
Nuclear Programmes	4.1	4.1	10.3
Other	1.0	3.6	5.3
Total turnover	69.8	83.5	156.9

The segmental operating profit/(loss) is as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
AEA Environment – UK	18.5	2.8	7.3
Kinectrics	0.8	0.2	0.2
Engineering Services Inc	0.5	0.4	1.0
AEA Environment	19.8	3.4	8.5
AEA Rail	(9.2)	4.2	(0.6)
Nuclear Programmes	0.5	0.3	(1.3)
Other	(7.2)	(8.8)	(16.3)
Total operating profit/(loss)	3.9	(0.9)	(9.7)

Notes to the Interim Report (unaudited) continued

4 Segmental information *continued*

(b) *Geographical segments*

The home-country of the Company, which is also the main operating company, is the United Kingdom. The Group's sales are mainly in the United Kingdom, Europe, and North America.

Turnover by destination

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
United Kingdom	47.6	56.9	103.4
Europe	6.0	9.6	17.6
North America	15.3	14.3	30.3
Rest of the World	0.9	2.7	5.6
Total turnover	69.8	83.5	156.9

Sales are allocated based on the region in which the customer is located.

Turnover by origin

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
United Kingdom	50.5	64.0	115.5
Europe	3.4	4.2	9.2
North America	15.8	14.5	30.7
Rest of the World	0.1	0.8	1.5
Total turnover	69.8	83.5	156.9

Sales are allocated based on the region in which the Group company is located.

5 Share capital and share premium

	Number of ordinary shares (millions)	Nominal value of ordinary shares £m	Value of share premium £m	Total share capital and premium £m
At 1 April 2004	67.5	8.3	10.6	18.9
New issues	0.1	—	0.1	0.1
At 30 September 2004 and 31 March 2005	67.6	8.3	10.7	19.0
Placing and Open Offer	50.7	6.9	24.0	30.9
At 30 September 2005	118.3	15.2	34.7	49.9

On 14 June 2005 the Company announced details of a refinancing of the Group through including a Placing and Open Offer of 50,682,656 new ordinary shares at 65 pence per share to raise £33.0 million gross (£30.9 million net of expenses). Applications were received from qualifying shareholders in respect of 44,575,931 of the 50,682,656 new ordinary shares offered under the Placing and Open Offer. This represented approximately 88% of the new ordinary shares offered under the Open Offer. 6,106,725 new ordinary shares not applied for by qualifying shareholders under the Open Offer were taken up under the Placing pursuant to the Placing and Open Offer agreement.

The total authorised number of ordinary shares is 196,399,329 shares (March 2005: 98,181,810 shares) with a par value of 12.2 pence per share (March 2005: 12.2 pence per share). The authorised share capital was increased by a special resolution at the Company's Extraordinary General Meeting on 7 July 2005. All issued shares are fully paid.

6 Retirement benefit liabilities

	At 30 September 2005 £m	At 30 September 2004 £m	At 31 March 2005 £m
Balance sheet liabilities for:			
Pension benefits	115.1	154.2	150.2
Post-employment medical benefits	6.9	6.1	6.7
	122.0	160.3	156.9
Income statement (credit)/charge for:			
Pension benefits	(24.8)	8.3	16.8
Post-employment medical benefits	0.3	0.3	0.6
	(24.5)	8.6	17.4

(a) *Pension benefits*

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

	At 30 September 2005 £m	At 30 September 2004 £m	At 31 March 2005 £m
Present value of funded obligations	494.1	479.1	491.5
Fair value of plan assets	(379.0)	(324.9)	(341.3)
Liability in the balance sheet	115.1	154.2	150.2

The amounts recognised in the income statement are as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Continuing operations			
Current service cost	3.7	4.6	9.4
Interest cost	10.0	10.2	20.4
Expected return on plan assets	(9.1)	(8.8)	(17.5)
Curtailment (gain)/loss during the period	(27.7)	0.1	0.3
Past service cost	0.1	1.0	1.7
Continuing operations	(23.0)	7.1	14.3
Discontinued operations			
Current service cost	0.5	0.7	1.4
Interest cost	1.6	1.6	3.2
Expected return on plan assets	(1.2)	(1.1)	(2.3)
Past service cost	–	–	0.2
Curtailment gain during the period	(5.0)	–	–
Curtailment loss on disposal of subsidiaries	2.3	–	–
Discontinued operations	(1.8)	1.2	2.5
Total (credited)/charged to the income statement	(24.8)	8.3	16.8

The curtailment gain of £32.7 million arises from changes in benefits in the AEA Technology Pension Scheme and redundancies affecting the AEA Technology Pension Scheme and the three Rail pension schemes.

Notes to the Interim Report (unaudited) continued

6 Retirement benefit liabilities *continued*

(b) *Post-employment medical benefits*

The Group operates an unfunded post-employment medical benefits scheme in Canada.

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

	At 30 September 2005 £m	At 30 September 2004 £m	At 31 March 2005 £m
Present value of liabilities	6.9	6.1	6.7

The amounts recognised in the income statement are as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Current service cost	0.1	0.1	0.2
Interest cost	0.2	0.2	0.4
Total charged to the income statement	0.3	0.3	0.6

7 Finance cost and finance income

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Finance costs			
Interest on bank borrowings	(2.7)	(2.4)	(3.8)
Accretion of discount of defined pension contribution obligation	(10.0)	(10.2)	(20.4)
Finance costs	(12.7)	(12.6)	(24.2)
Finance income			
Interest income	1.3	1.1	0.6
Expected return on pension scheme assets	9.1	8.8	17.5
Finance income	10.4	9.9	18.1
Net finance costs	(2.3)	(2.6)	(6.1)

8 Income tax credit/(expense)

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Current tax	(1.1)	(0.5)	(0.6)
Deferred tax	1.4	–	(4.7)
Total income tax	0.3	(0.5)	(5.3)

9 Earnings per share

(a) Basic

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the period.

	Six months ended 30 September 2005	Six months ended 30 September 2004	Year ended 31 March 2005
Profit/(loss) attributable to equity holders of the Company (£ millions)	3.3	(4.1)	(21.2)
Weighted average number of ordinary shares in issue (millions)	91.1	67.5	67.6
Basic earnings per share (pence)	3.6	(6.1)	(31.4)

(b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares in issue to assume conversion of all potential dilutive ordinary shares. The Company has only one category of potential dilutive ordinary shares, share options. The calculation is performed for the share options to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	Six months ended 30 September 2005	Six months ended 30 September 2004	Year ended 31 March 2005
Profit/(loss) attributable to equity holders of the Company (£ millions)	3.3	(4.1)	(21.2)
Weighted average number of ordinary shares in issue (millions)	91.1	67.5	67.6
Adjustment for share options (millions)	11.1	–	–
Weighted average number of ordinary shares for diluted earnings per share (millions)	102.2	67.5	67.6
Diluted earnings per share (pence)	3.2	(6.1)	(31.4)

(c) Adjusted earnings basis

The adjusted earnings per share is calculated as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Profit/(loss) attributable to equity holders of the Company	3.3	(4.1)	(21.2)
Release of provisions for operating loss on termination	–	(1.0)	(0.6)
Impairment of assets	15.0	–	0.5
Pension curtailment gain	(27.7)	(0.1)	(0.3)
Redundancy costs	5.6	0.8	1.2
Refinancing costs	2.7	–	–
Profit on sale of tangible fixed assets	–	–	2.4
Adjusted loss	1.1	(4.4)	(18.0)
Weighted average number of ordinary shares in issue (millions)	91.1	67.5	67.6
Adjusted earnings per share (pence)	(1.2)	(6.5)	(26.6)

Notes to the Interim Report (unaudited) continued

9 Earnings per share *continued*

(d) *Basic and diluted – discontinued operations*

	Six months ended 30 September 2005	Six months ended 30 September 2004	Year ended 31 March 2005
Loss attributable to equity holders of the Company (£ millions)	0.5	(1.0)	(8.3)
Weighted average number of ordinary shares in issue (millions)	91.1	67.5	67.6
Basic and diluted earning per share (pence)	0.5	(1.5)	(12.3)

10 Cash generated from operations

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Profit/(loss) for the period	5.6	(2.7)	(28.3)
Adjustments for:			
tax	(0.3)	0.6	5.7
depreciation and amortisation	3.9	3.5	7.1
goodwill impairment charge	12.1	–	0.5
net movements in pension liabilities	(34.2)	(4.0)	(0.7)
impairment of assets	3.2	–	6.6
(profit)/loss on disposal of subsidiaries	(1.8)	(1.4)	1.8
share of loss from associates	0.3	0.3	0.6
interest	12.7	14.7	28.7
investment income	(10.5)	(11.1)	(20.5)
other	3.1	0.2	0.4
Changes in working capital:			
inventories	(0.9)	(0.5)	0.8
trade and other receivables	1.5	2.5	11.5
trade and other payables	(7.5)	(11.9)	(15.4)
Cash used in operations	(12.8)	(9.8)	(1.2)

11 Contingencies

The Group has contingent liabilities in respect of contracts entered into in the normal course of business and in respect of previous and current disposals of businesses and subsidiaries. It is not expected that these will have a material effect on the financial position of the Group.

AEA Technology plc guarantees the credit facilities, overdraft facilities, BACS facilities and leasing obligations of certain subsidiary companies. At 30 September 2005 these guarantees totalled £0.7 million (2004: £1.1 million).

12 Disposal of a portfolio of companies

Under an agreement signed on 13 September 2005, the Group agreed to dispose of a portfolio of companies to funds managed by Coller Capital. The agreement became unconditional on 30 September 2005. Completion took place on 7 October 2005. The disposal was completed for £40.0 million in cash on 7 October 2005. The Group companies disposed of with their country of incorporation (where this is not the United Kingdom) were:

AEA Technology Battery Systems Limited	SoMat Systems Limited
Safeguard International Solutions Limited	SoMat Corporation Inc (USA)
ESR Technology Limited	Lexware International Limited
RiskSol Consulting Limited	AEA Technology SARL (France)
EASA Limited	AEA Technology QSA GmbH (Germany)
Accentus plc	AEA Technology QSA Inc (USA)
nCode International Limited	AEA Technology Limited (Hong Kong, China)
nCode International Inc (USA)	Shenzen CIC-AEA Technology Manufacturing Co Ltd (China)
nCode GmbH (Germany)	

The results of the companies that were disposed of were as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
Turnover	34.5	34.5	78.9
Cost of sales	(17.8)	(17.8)	(49.7)
Gross profit	16.7	16.7	29.2
Other operating income	1.4	0.6	1.2
Impairment of assets	–	–	(6.8)
Administrative expenses	(15.1)	(16.9)	(28.7)
Operating profit	3.0	0.4	(5.1)
Share in loss in joint ventures and associates	(0.3)	(0.3)	(0.6)
Finance costs – net	(1.3)	(1.0)	(2.2)
Profit/(loss) before income tax	1.4	(0.9)	(7.9)
Income tax expense	(0.9)	(0.1)	(0.4)
Profit/(loss) for the period from discontinued operations	0.5	(1.0)	(8.3)
Provisional profit on disposal			
Proceeds	40.0		
Net assets	(16.3)		
Curtailed loss on pension scheme	(2.3)		
Provisions	(14.6)		
Costs of disposal	(6.2)		
Foreign exchange reserves released	1.2		
Provisional profit on disposal	1.8		

Notes to the Interim Report (unaudited) continued

12 Disposal of a portfolio of companies *continued*

The aggregated balance sheets of the companies that were disposed of during the period were as follows:

	At 30 September 2005 £m
ASSETS	
Non-current assets	
Intangible assets including goodwill	8.8
Property, plant and equipment	5.0
Investment in associates and other companies	0.7
	14.5
Current assets	
Inventories	14.4
Trade and other receivables	16.8
Current income tax assets	0.3
Cash and cash equivalents	2.2
	33.7
Total assets	48.2
EQUITY	17.3
LIABILITIES	
Non-current liabilities	
Retirement benefit liabilities	3.9
Deferred income tax liability	1.7
Provisions and other liabilities and charges	6.5
	12.1
Current liabilities	
Trade and other payables	18.8
Total liabilities	30.9
Total equity and liabilities	48.2
	Six months ended 30 September 2005 £m
The net proceeds of the deal were as follows:	
Cash received	40.0
Payments to pension scheme	(8.1)
Cash divested	(2.5)
Disposal costs	(6.2)
	23.2
Net proceeds	23.2
Reduction of banking facilities	(19.1)
Net change in headroom	4.1

	At 30 September 2005 £m
Reconciliation of equity	
Equity	17.3
Minority interest	(1.0)
Net assets disposed of	16.3

13 Redundancy costs – continuing operations

During the six months ended 30 September 2005 the Group made 186 (c2004: 17) staff redundant through a voluntary redundancy programme. These included 146 (2004: 5) staff from Rail, 10 (2004: nil) staff from Nuclear Programmes and 30 (2004: 12) staff from other businesses.

The Group has incurred redundancy costs as follows:

	Six months ended 30 September 2005 £m	Six months ended 30 September 2004 £m	Year ended 31 March 2005 £m
AEA Environment – UK	0.1	–	0.2
Kinectrics	0.2	–	–
AEA Environment	0.3	–	0.2
AEA Rail	4.0	–	0.2
Nuclear Programmes	0.5	–	–
Other	0.8	0.8	0.8
Total redundancy costs	5.6	0.8	1.2

Financial calendar

Year End

31 March 2006

Results

Annual Report and Accounts – circulation June 2006

Annual General Meeting – 27 July 2006

The latest financial information on AEA Technology is available on the internet: **www.aeat.co.uk**



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