

directors and advisers

Directors	Malcolm Brighton* OBE, Chairman Anthony Christopher Lee Stephen Mark Beats Simon John Day Nigel Victor Turnbull*† Arthur Mark Tebbutt Ann Limb* Gary Brighton Lord Kinnock of Bedwellty* Chris Batterham*	*non-Executive †Senior Independent Director
Company Secretary	Arthur Mark Tebbutt	
Registered Head Office	1 Danbury Court Linford Wood Milton Keynes Buckinghamshire MK14 6LR	
Stockbrokers	KBC Peel Hunt Ltd 3 Brindley Place Birmingham West Midlands B1 2JB	
Auditors	Grant Thornton UK LLP Registered Auditors & Chartered Accountants Grant Thornton House 202 Silbury Boulevard Central Milton Keynes Buckinghamshire MK9 1LW	
Principal Bankers	Barclays Bank plc 669 Midsummer Boulevard Central Milton Keynes Buckinghamshire MK9 3BQ	
Registrars	Capita Registrars The Registry 34 Beckenham Road Beckenham Kent BR3 4TU	

contents

	Page
chairman's statement	2
operating and financial review	4
the directors	8
report of the directors	10
report on directors' remuneration	13
corporate governance disclosure statement	18
report of the independent auditors	22
income statement	24
balance sheet	25
statement of changes in shareholders' equity	26
cash flow statement	27
notes to the financial statements	28

chairman's statement

2005 has been a challenging year with no large contracts in the first half and substantial development of e-Marker® continuing throughout the year. Financial results for 2005 show a decrease in turnover and profit compared with 2004, the year which included turnover of approximately £4,000,000 from the Greater London Authority and European election project. Profit for the year has been impacted as a result of the planned investment in new products and services associated with e-Marker®.

Turnover for the calendar year 2005 was £12,452,000 with pre-tax profits of £17,000 compared with £14,408,000 and £437,000 respectively for 2004.

In view of the results for the year, the directors do not recommend payment of a final dividend for 2005. The directors will review the payment of a dividend in September based on the interim results for the first six months of 2006.

e-Marker®

2005 was very much a watershed year for our e-Marker® products and services. DRS has been developing electronic marking services for many years and they have been used successfully in various forms by all the major awarding bodies in the UK. A major

element in the success of e-Marker® has been the flexibility of its development to meet the needs of UK and international awarding bodies and their examinations. DRS works closely with a number of awarding bodies to transfer their examination marking processes into an electronic system which is intuitive to use and which enhances the efficiency and accuracy of the overall process. The system can be tailored to a particular examination type and is configurable by the awarding body to their style of working. These factors have led to e-Marker® being used by more UK awarding bodies than any other system of its type.

other products

Last year was also a year of change for some of our traditional OMR (Optical Mark Recognition) markets. The launch of our PhotoScribe® range of full Imaging scanners has triggered replacements of their predecessors, the CD400 and CD800 OMR scanners. Existing and new international customers are realising the benefits of the PhotoScribe® PS900 scanner and are switching away from pure OMR applications. Also, our schools' market is starting to change. A high percentage of schools already use DRS CD200 series scanners for pupil registration and other educational

"The launch of our PhotoScribe® range of full Imaging scanners has triggered replacements of their predecessors."

applications and consequently there are fewer new prospects to pursue. Also the number of new schools deciding to use OMR is decreasing as other forms of IT equipment become available. However, this changing technology provides an opportunity for DRS to supply new services to schools and this is part of our current strategy.

staff

As always, the employees of DRS have performed extremely well during this year of change. Many new people joined the company as we built our project management resources and e-Marker® team, and as from 2006 we also have two completely new teams of people, one in the US and another in the UK, within Peladon. I would like to thank all of our staff for their contribution to yet another very busy and demanding year.

Peladon

In January 2006 the acquisition of Peladon Software was completed, bringing both Peladon Software Inc and Peladon Software Limited into the DRS group. Peladon was acquired for a total consideration of \$4,865,000 (£2,748,000). In order to expand our range of products, services and expertise, DRS has been actively seeking suitable businesses to acquire for several years, however our strategy requires potential companies to meet exacting standards, recognising that an ill-judged purchase could stretch our managerial resources. We have therefore resisted the temptation to acquire companies whose results depend upon the application of a different set of management skills. We are extremely pleased to have found a company that meets our criteria and to have completed the deal successfully. DRS plans to maintain this acquisition strategy and is continuing to look for suitable prospects.

summary

Our consistent strategy of building the company in key areas of data capture is being maintained and demonstrates great potential. Our performance continues to be affected by the timing of one-off contracts, but DRS' skills and experience are proving successful in winning an increasing level of larger contracts. For example, we have just completed our largest print order for the Nigerian census and have been awarded what is potentially our largest election counting contract by the Scottish Executive. The success of e-Marker® and the acquisition of Peladon will enhance our operations and position in both UK and international markets. I therefore remain confident that DRS will yield profitable growth in 2006 and beyond.

Malcolm Brighton

Chairman

24 March 2006

operating and financial review

The profit for the year before taxation amounted to £17,000 (2004: £437,000). Loss per share was 0.02p (2004: Earnings per share 1.31p).

dynamics of the business

The profile of the business in 2005 was different from that of the previous year for several reasons. The first half did not include e-Counting for an election of the size seen for the 2004 Greater London Authority and European project. Election work was undertaken for Argyll and Bute and a number of London boroughs, however, although they generated good revenue it was not on a comparable scale to the GLA election. e-Marker® projects did follow the predicted increase in volumes and this work has started to replace the examination and assessment work which was lost from Edexcel in 2003/2004. Lastly, the end of the year saw an increase in the level of print business due to the Nigerian census work.

The strategy employed to build the business in key growth areas has led to some changes in the shape of the company. Strategic elements of the business are:

- Increased emphasis on project management, providing integrated services to our customers across the breadth of product offerings and market segments.
- Continued investment in e-Marker® services and associated Internet and IT structures. The main thrust of our sales and marketing activity is focused around modernising examination marking and is aimed at UK educational and professional awarding bodies but does include activities in the rest of the world.
- UK and Worldwide provision of e-Counting and other election services.

- UK schools, further and higher education – traditional OMR solutions where we supply scanners and forms continues to be solid business but is unlikely to see further growth. New products and services such as pupil admissions forms for schools, and surveys in the further and higher education sector are starting to be established in the market.
- Print business in UK and internationally for national examinations, voter registration and census. Our services are used in more than 20 countries.
- OMR and Imaging scanner sales, particularly in international territories.
- Provision of data capture services to UK commercial and public sector areas such as police forces.

highlights of the year

2005 saw the first high volume use of e-Marker® as part of our UK examination and assessment business. The partnership between DRS and AQA (Assessment and Qualifications Alliance) created the largest proportion of the work supplying e-Marker® services for AQA's summer series of GCSE examinations. The highly successful implementation of this technology enabled examiners and markers to use the Internet to assess examination scripts and mark them on-line. Although substantial investment is still required to develop e-Marker® it is already adding significant revenue to the business.

e-Marker® services also continued with other awarding bodies including WJEC (Welsh Joint Education Committee) and the CCEA (Council for the Curriculum, Examinations and Assessment) in Northern Ireland. We were also pleased to introduce the first international use of marking technology in Australia towards the end of the year. Scanning and marking of examination scripts was undertaken in Australia while the hosting of the main e-Marker® services were centred in the UK.

Although the largest growth in exams and assessment was associated with e-Marker®, our other business in this area continued with the supply of services to a number of educational establishments. Also the markets of higher, further and adult education were maintained at levels similar to those of 2004.

New services into the schools market were achieved with our admissions product. An increasing number of Local Authorities are using DRS to process parental preference application forms for pupil admissions to schools. This business is starting to produce significant revenue with good promise for growth.

Election projects were successfully implemented in the first half of the year with both e-Counting work and printing of ballot papers. The Argyll and Bute Community Council elections were counted in record time using DRS technology in April. Also five London boroughs chose DRS to print their ballot papers for the General Election in May.

International sales of our PhotoScribe® scanner range remain buoyant. The PS900 scanner was sold to ten different countries including three new sales areas: Slovenia, Mozambique and Rwanda.

The international market started the year well with a voter registration project for the United Nations in Liberia which included printing 3,000,000 forms as well as the supply of PS900 scanners. The year ended on an even higher note, with the award of the largest single print contract that the company has ever won. This contract was with the EU development fund for the supply of forms for the March 2006 Nigerian census. DRS had successfully completed the trial census in September 2005 and the main census involved the printing of over 50,000,000 A3 forms. Over half of the total order was printed by the end of the year.

Immediately following the end of the year, the company completed a major restructuring of the business, with DRS Data & Research Services plc becoming a Group holding company and the formation of DRS Data Services Limited as the trading company for all existing DRS operations. This restructuring was implemented in advance of any potential acquisitions to facilitate incorporation of new businesses into DRS Data & Research Services plc without disruption to our operations.

research and development

Development of the PhotoScribe® scanner range continued, following its successful use in the 2004 London Greater London Authority and European elections. The first release of this product was produced especially for the elections and significant new features have been added subsequently. Some of the main features are:

- improved paper handling
- introduction of image enhancement technology
- increased speed
- a third output hopper
- longer paper length handling
- real time Intelligent Character Recognition techniques.

These enhancements have created a product range suitable for the diverse international marketplace into which the PhotoScribe® series sells. In particular, requirements for the American election market have been incorporated so that US e-Counting applications can be addressed.

Research and development of e-Marker® continues to use substantial internal and external resource. A roadmap of e-Marker® services is being followed to meet customer requirements for examination types and volumes. The complex technology required involves several new areas of expertise as well as many existing specialities of the company.

Our election e-Counting product has been developed over a number of years for counting ballot papers with standard 'cross' marked votes. In 2005 this has been extended to enable STV (Single Transferable Vote) ballot papers to be counted electronically.

operating and financial review continued

STV elections request the voter to express preferences for candidates by writing numbers on the ballot paper, rather than a traditional 'X'. Therefore to incorporate STV into the DRS product, Intelligent Character Recognition techniques have been included in the scanning process. Also the main e-Counting software has been enhanced to enable STV elections to be processed.

As part of our strategy to grow the business through acquisition, in the second half of 2005 we entered into negotiations with the Peladon Group. We were pleased to announce the successful acquisition of the Peladon Group at the end of January 2006. Peladon's products are centred on a suite of software marketed as DocXP. This contains an extensive range of powerful applications for specific needs:

- **DocXP – Capture**, scanning and indexing of documents.
- **DocXP – Automated Data Capture**, automatically recognises forms and document types and then captures hand printed information.
- **DocXP – Intelligent Data Capture**, intelligently finds and reads information within documents without having seen the document type before.
- **DocXP – Electronic Document Filing**, indexes electronic documents such as word processor files, spreadsheets, and emails into DocXP's structured storage system, or for use in any other document management systems.
- **DocXP – Retrieval**, fast and powerful document retrieval system.
- **DocXP – Archive**, manages document storage for large and complex, online and offline, storage structures.

A major element of the intellectual property contained in these solutions is the ability to automatically read structured and semi-structured documents. Examples of these document types are; invoices, purchase orders, tax forms, application forms, and cheques. Peladon's products are capable of analysing and interpreting such documents so that all necessary data contained on them is automatically converted into an electronic format. Form types can either be 'read' in this way without prior knowledge of the document format, or the form type can be 'learned' for repeated use.

funds from operating activities and current liquidity

The balance sheet remains strong. Current investments and cash that are readily convertible to cash at 31 December 2005 were £3,300,000 (2004: £4,900,000).

During March 2006, following the acquisition of the Peladon Group for £2,748,000 on 31 January 2006, the loan secured by a fixed charge against the Linford Wood head office was renegotiated to £2,250,000 with Barclays Bank. An additional overdraft facility in the subsidiary DRS Data Services Limited of £1,000,000, provides sufficient cash to meet budgeted operational commitments.

treasury policy

Surplus funds are currently invested with and by UK banks. The Board monitors the company's deployment of funds with a view to minimising risk. The company maintains funds in various major foreign currencies but does not hold, nor speculate in, such currencies at levels outside of its normal trading requirements.

formal statement on the continuing use of the going concern basis

After making enquiries, the directors have a reasonable expectation, at the date of approval of these financial statements, that the company has adequate resources to continue operations for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

current trading and outlook

The contract to print forms for the Nigerian census spanned the end of 2005 and start of 2006. The number of forms required by the customer had increased from the original order, and printing continued into the first two months of 2006, keeping the Print Department running at maximum capacity, and providing a good start to the year. The order book for the Print Department is also very healthy for the first half of the year.

The volume of e-Marker® work in 2006 will be substantially greater than in the previous year. The main growth is expected to be with AQA and a long term plan for implementing their examinations has been agreed, with volume and pricing structures. Development of the product and associated services will continue, requiring significant investment, but the projected returns in revenue have been realised in 2005 and are expected to increase over the next three years.

Although AQA is currently our largest customer using e-Marker®, sales continue with other customers. The first use of e-Marker® in Australia was encouraging and potential business in Europe looks very promising.

In the second half of 2005 we responded, in partnership with ERS (Electoral Reform Services) to an invitation to tender from the Scottish Executive for electronic counting of the 2007 Scottish Elections. Three election contests will be combined on this occasion and STV will be introduced for the first time. Such complex elections, and in particular the STV form of proportional representation, benefit the most from the advantages of e-Counting. The ability to simultaneously count multiple contests of different variants and generate multistage results electronically, dramatically improves the efficiency and accuracy of the election process.

We were therefore pleased to be awarded the e-Counting contract by the Scottish Executive in February 2006. As part of the contract, trials of our election system have already taken place with the 32 local authorities in Scotland. These trials were extremely successful and will be followed by an acceptance test in the second quarter of the year. Once acceptance has been completed we will be working with all local authorities in Scotland who wish to utilise electronic counting for their elections in 2007. This project is expected to be of a scale larger than the GLA elections in 2004 and the revenue potential is also higher.

Our elections team has also been working with the Department of Constitutional Affairs to provide services for the UK local elections in May 2006. Two contracts have been awarded from the London boroughs of Westminster and Lewisham who will both use the DRS e-Counting system to process their elections. Preparations are also underway to bid for the 2008 GLA and London Mayor elections.

As was stated in the last annual report, the profile of the DRS business is changing. First, the progression of e-Marker® services from development and trials, to high volume production work has been implemented over the past three years. Although development is still continuing, revenue growth is now making a major contribution to the business. Secondly, some of our more traditional OMR markets are being replaced by Optical and Intelligence Character Recognition technologies. The acquisition of Peladon and development of the PhotoScribe® range of scanners ensures that DRS is able to maintain its prominent position in these data capture markets. The above, combined with the major election projects expected to take place over the next three years, and our comprehensive international markets, give DRS a very strong future.

The change of business profile and substantial investment in future technology and markets was expected to delay our return to profitability. The very encouraging expansion of e-Marker® during 2005 and the acquisition of the Peladon Group at the beginning of this year has confirmed our confidence that the business will generate revenue growth from 2006.

Tony Lee
Managing Director
24 March 2006

the directors

Malcolm Brighton OBE, DL

Chairman

Malcolm Brighton was Managing Director from the company's establishment in 1969 until 2001.

An Economics graduate, he previously worked in market research and served as Vice Chairman of the British Market Research Society. He is currently Chairman of Milton Keynes City Orchestra and a Council Member for the Milton Keynes, Oxford and Bucks Learning and Skills Council. He is also a director of three small private companies: Acorn Childcare Limited, Daybright Limited and Hintlesham Hall Limited.

Tony Lee BSc, MPhil

Managing Director

Tony Lee joined the company in March 1997 as Technical Director, having previously been European Technical Director for

Dolch Computer Systems. He has worked in the electronics and computer industry for more than 20 years. In the late 1980s he was Head of Research and Development for Epson and was involved in a number of international projects developing printing, communications, image scanning and recognition technologies. He was appointed to the Board in September 1997, and appointed Managing Director in March 2001.

Steve Beats

Technical Director

After joining DRS in a consultancy role in 1998, Steve Beats was appointed Development Manager six months later and

subsequently to the Board in May 2001. With a diverse background, including boat building, archaeology and fitness instruction, Steve has over 20 years' experience in varied software and product development disciplines, including 12 years with Commodore Business Machines in the USA.

Simon Day BSc, MBA

Commercial Director

Simon Day joined the company in 1992 as International Business Development Manager.

An Electronics Engineering graduate, he subsequently gained an MBA in International Business and Export Management. He previously worked for Zenith Data Systems, and in manufacturing and sales in both Britain and France with Mars Electronics. He was appointed to the Board in September 1999.

Nigel Turnbull FCA, FCT, BSc

non-Executive Director

Nigel Turnbull was appointed as a non-Executive Director in May 2001. He trained as a Management Accountant

with a US chemical company before joining an oil company as General Manager of their industrial group. He ultimately became Finance Director. In 1987 he joined Rank Group plc as Finance Director until his retirement at the end of 1999. He is also Chairman of the Erinaceous Group plc, Risk Advisory Group and Hotbed Limited.

Mark Tebbutt ACMA

*Finance Director/
Company Secretary*

Mark Tebbutt joined the company in 2001 as Head of Finance. He was appointed to the Board in March 2002 and appointed Company Secretary in March 2003. Having qualified as a Chartered Management Accountant in 1984, Mark gained a broad operational knowledge of financial management with Bass, GrandMet, and Misys where he had director status, and Stanley Works.

Ann Limb PhD, MA

non-Executive Director

Ann Limb was appointed to the Board of DRS as a non-Executive Director in March 2003. A modern linguist and teacher by profession, she worked extensively in further education for 25 years spending over half her career as Principal and Chief Executive, firstly at Milton Keynes College and then Cambridge Regional College. Between 2001 and 2004, Ann was Group Chief Executive of the University for Industry, the government's national e-learning flagship responsible for the operation of Learndirect and UK on-line. Ann currently works as an educational adviser to government and serves on the boards of a number of other companies, charities and public bodies. She is founder and Chair of the Helena Kennedy Foundation for social justice.

Gary Brighton *Operations Director*

Gary Brighton joined DRS Bureau Operations in 1997. He was appointed Bureau Manager in 1998 and Associate Director in 2001 with responsibility for both Bureau and Print Operations before his subsequent appointment to the Board in March 2003. Prior to joining DRS, Gary was involved in IT consultancy for nine years,

for companies including Credit Suisse in Zurich and Proctor & Gamble UK, before spending four years as Head of IT for Countrywide Independent Advisers, a part of the Misys group.

Lord Kinnock of Bedwellty

non-Executive Director

Neil Kinnock was appointed as a non-Executive Director of DRS in March 2005. An Industrial Relations and History graduate, he taught policy and trade union studies before being elected Member of Parliament for Bedwellty and Islwyn in 1970. In 1979 he was appointed Labour's Chief Opposition Spokesperson on Education and was elected Leader of the Labour Party in 1983, a position he held until 1992. He was appointed to the European Commission in 1995, with the Transport portfolio to 1999 and then as Vice President 1999-2004. He is currently Chairman of the British Council.

Chris Batterham *non-Executive Director*

Chris Batterham was appointed as a non-Executive Director in September 2005. Chris qualified as a Chartered Accountant with Arthur Andersen. He was Finance Director of Unipalm plc, the first internet company to IPO and stayed with the company for five years following its takeover by UUnet. More recently he was CFO of Searchspace Group until 2005 and is currently a non-Executive Director of SDL plc, The Risk Advisory Group Ltd, Iomart plc and The Sporting Exchange Group Limited (Betfair). He has also served on the boards of Staffware plc, DBS Management plc and The Invesco Techmark Enterprise Trust plc. Chris brings a wealth of experience in the strategic development of companies within the IT sector.

report of the directors

The directors present their report together with the audited financial statements for the year ended 31 December 2005.

principal activities

The principal activities of the company continue to be the provision of data capture services, the manufacture and sale of Optical and Image scanning equipment and complementary services.

A review of the business during the year, likely future developments and the company's activities in research and development are given in the chairman's statement and the operating and financial review.

results and dividends

The results this year have been prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union. The effects of adopting IFRS are set out in the notes to the financial statements on pages 28 to 57.

The loss for the year after taxation amounted to £7,000 (2004 profit: £435,000).

The directors do not recommend a dividend for 2005 (2004: 1.5p).

statement of responsibilities

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and International Financial Reporting Standards as adopted by the European Union.

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

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

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

The directors are responsible for ensuring that the report of the directors and other information included in the annual report is prepared in accordance with Company law in the United Kingdom. They are also responsible for ensuring that the annual report includes information required by the Listing Rules of the Financial Services Authority.

risk management

Details of the financial risk management objectives and policies of the Group and exposures to risks are given in Note 3 to the financial statements.

acquisition of treasury shares

The company continues to hold 1,930,000 ordinary shares of 5p purchased between 3 June and 15 July 2004 for a total consideration of £1,166,000 as treasury shares. This represents 5.57% of the company's called up share capital.

directors and interests

The names of the current directors and their biographical details are given on pages 8 and 9.

Christopher Michael Batterham was appointed Director on 12 September 2005. In accordance with Article 74 of the Articles of Association, members will be asked to confirm his appointment.

A C Lee and A G Limb retire by rotation and, being eligible, offer themselves for re-election.

The interests of the directors in the ordinary share capital of the company, details of directors' service contracts and details of the gains made by the directors on share options are given in the report on directors' remuneration on pages 13 to 17.

No director has any material interest in any contractual agreement subsisting during or at the end of the year which is or may be significant to the company.

substantial shareholdings

At the date of this report the company has been notified of the following interests over its ordinary shares in accordance with Sections 198 to 208 of the Companies Act 1985:

	Ordinary shares of 5p each	Percentage holding
Malcolm Brighton	7,079,697	20.45%
S D Stewart	2,200,000	6.35%
HSBC Global Custody Nominee (UK) Ltd	2,085,000	6.02%
Gary Brighton	2,000,000	5.78%
J A Brighton	2,000,000	5.78%
Mark Brighton	2,000,000	5.78%
DRS Data & Research Services plc	1,930,000	5.57%
HSBC Client Holdings Nominee (UK) Ltd	1,653,950	4.78%
J P MacArthur	1,139,400	3.29%

political and charitable donations

Charitable donations in the year amounted to £19,520 (2004: £13,367). No contributions were made for political purposes (2004: £Nil).

creditor payment policy

The company's normal practice is to agree terms and conditions with all suppliers before business takes place. Payment is then made on these terms subject to satisfactory performance by the supplier. Trade creditors at the year end represented 40 days (2004: 40 days) of average supplies for the year.

report of the directors continued

annual general meeting

The Annual General Meeting of the company will be held on 15 May 2006, at which shareholders will be asked, as items of special business, to give power to the directors to allot shares and to give power to the directors to disapply the pre-emption requirements of Section 89 of the Companies Act 1985.

renewal of authority to allot

The current authority to allot relevant securities within the meaning of Section 80 of the Companies Act 1985 will expire on 30 June 2006 or at the 2006 Annual General Meeting, if earlier. Resolution 7 as set out in the Notice of the Annual General Meeting, will be proposed as an Ordinary Resolution to authorise the directors to allot ordinary shares in the capital of the company up to an aggregate nominal amount of £568,920. The authority (unless previously varied, revoked or renewed) will expire on 30 June 2007 or at the 2007 Annual General Meeting.

disapplication of pre-emption rights

The current authority for directors to allot equity securities for cash without first being required to offer such securities to existing shareholders in proportion to their existing holdings expires on 30 June 2006 or at the 2006 Annual General meeting, if earlier. Resolution 8 as set out in the Notice of Annual General Meeting, will be proposed as a special resolution to renew the authority of the directors under Section 95 of the Companies Act 1985 to allot shares for cash otherwise than on a pre-emptive basis. The number of shares which may be allotted will be limited to an aggregate nominal value of £86,554 (representing 5% of the issued share capital of the company). The authority (unless previously varied, revoked or re-worked) will expire on the earlier of 30 June 2007 or the 2007 Annual General Meeting.

Although there is no present intention of issuing any shares (other than pursuant to the company's share option schemes), the directors consider it is desirable to maintain the flexibility afforded by these provisions.

auditors

Grant Thornton UK LLP offer themselves for re-appointment as auditors in accordance with Section 385(2) of the Companies Act 1985 and a resolution to re-appoint them will be proposed at the Annual General Meeting.

BY ORDER OF THE BOARD

Mark Tebbutt

Company Secretary

24 March 2006

report on directors' remuneration

remuneration committee

At the beginning of 2005, the Remuneration Committee comprised of two independent non-Executive Directors, Nigel Turnbull (the Chairman), and Ann Limb. At the Board Meeting in March 2005 Lord Kinnock was appointed to the Committee and at the Board Meeting in September Chris Batterham was also appointed to the Committee, so that once again, it consisted of at least three independent non-Executive Directors. None of the Committee members has any personal financial interests (other than as shareholders), potential conflicts of interest arising from cross-directorships, or any day-to-day involvement in running the business. The Chairman and Chief Executive, at the invitation of the Committee, attend the meetings but are not present when their own remuneration is discussed.

The Committee meets formally at least once a year in January, but it is the practice of the Committee to meet on an ad hoc basis throughout the year to address matters that arise. As well as considering the conditions in the company as a whole, the Committee takes into account the position of the company relative to other companies and is aware of what companies are paying, although comparisons are treated with caution to avoid remuneration escalation. The Committee met on four occasions in 2005.

Advisers – During 2005, external independent professional advice was sought from Halliwell Consulting by the Board and the Committee on remuneration issues in respect of the structure and appropriateness of the total remuneration packages of the Executive Directors. In 2004, advice was sought from Watson Wyatt on the remuneration packages of the non-Executive Directors.

remuneration policy

The company's policy on directors' remuneration is that the packages are designed to attract, motivate and retain directors of the calibre necessary to maintain the company's position as a market leader and so reward them for enhancing shareholder value. The Remuneration Committee determines the contract terms, basic salary and other remuneration for each of the Executive Directors, including performance-related share options, bonuses and pension rights.

remuneration packages

The Executive Directors' remuneration package includes fixed and variable elements to provide rewards for both the short and long term. Details of the individual elements of the remuneration package and employment contracts are:

Basic salary and benefits – An Executive Director's basic salary is determined by the Remuneration Committee in January of each year, having regard to individual responsibilities, performance and comparative information. In addition the company provides benefits comprising a company car fully funded for business mileage, or a cash allowance in lieu of company car, settlement by the company of professional fees in respect of personal tax affairs, private healthcare arrangements, life assurance cover and permanent health insurance.

Performance related cash bonus – The Remuneration Committee, in awarding annual bonuses, considers the company's financial performance during the year in respect of turnover, profitability, EPS and an assessment of the individual Executive Director's performance against non-financial criteria.

Long term equity based incentive plans – The Remuneration Committee's policy has been to grant to Executive Directors share options that relate to the company's growth in EPS, in order to align the interests of directors more closely with those of the shareholders. The company's policy is now to reward senior executives by way of options up to a total of £30,000 and by the grant of a Long Term Incentive Plan (LTIP).

In February 2005 the Revenue & Customs approved a Share Incentive Plan (SIP) for all employees of the company including the directors. The SIP allows participants to invest up to £1,500 per annum by way of salary deduction in the company's shares. For every two partnership shares purchased by the participant, one additional matching share is gifted by the company. The scheme is operated in accordance with Revenue & Customs rules.

In November 2005, at an Extraordinary General Meeting the shareholders approved a Long Term Incentive Plan (LTIP) for Executive Directors and key senior executives. Awards under the scheme are based on the company's EPS and Total Shareholder

report on directors' remuneration continued

Return (TSR) performance being at least at the median compared to the companies constituting the FTSE All Share Software & Computer Services Index.

Pensions – Each of the Executive Directors is a member of one of the company's money purchase pension schemes. Pension arrangements for each Executive Director provide for a pension on retirement at the age of 65 based on a contribution by the company of a sum equivalent to 20% of basic salary. Base salary is the only component of remuneration which is pensionable. There is no requirement for an individual director to contribute to his/her pension scheme. Their dependants are eligible for Dependant's Pension and the payment of a lump sum equivalent to four times basic salary in the event of death in service.

directors' contracts

The Executive Directors have rolling contracts with six months' notice which are in line with the recommendations of the Combined Code.

The contracts date from the dates of appointment to the Board as set out in directors' Interests below. There is no defined provision for compensation payable upon early termination of the contract.

It is the intention of the Remuneration Committee that any future Executive Director appointment will be based on contracts similar to those in effect for the current Executive Directors.

The non-Executive Directors each have letters of appointment, which refer to the re-election requirements under the Company's Articles of Association. Each appointment is for a period of three years, or when individual directors are required to offer themselves for retirement by rotation, whichever is the earlier. The appointment may, however, be terminated by three months' notice from either party at any time. There is no provision for compensation payable upon early termination. Copies of the letters of appointment will be available for inspection at the AGM.

directors' interests

The interests of directors (including their spouses' holdings) in the ordinary shares of the company as recorded in the register maintained by the company in accordance with the provisions of the Companies Act 1985 were as follows:

	Date of appointment to Board	Ordinary shares of 5p		
		As at 24/03/2006	As at 31/12/2005	As at 01/01/2005
C M Batterham	12/09/2005	40,000	40,000	–
S M Beats	14/05/2001	97,679	96,282	92,948
G Brighton	17/03/2003	2,000,000	2,000,000	2,000,000
M Brighton OBE (Chairman)	16/09/1969	9,079,697	9,079,697	9,079,697
S J Day	17/09/1999	103,254	102,127	98,307
Lord Kinnock	14/03/2005	–	–	–
A C Lee	15/09/1997	105,217	103,820	100,000
A G Limb	17/03/2003	15,000	15,000	15,000
A M Tebbutt	25/03/2002	464,931	463,534	449,856
N V Turnbull	15/05/2001	150,000	150,000	150,000

On the 16 January 2006, S M Beats, S J Day and G Brighton resigned from the DRS Data & Research Services plc Board to take up similar positions on the subsidiary DRS Data Services Limited Board.

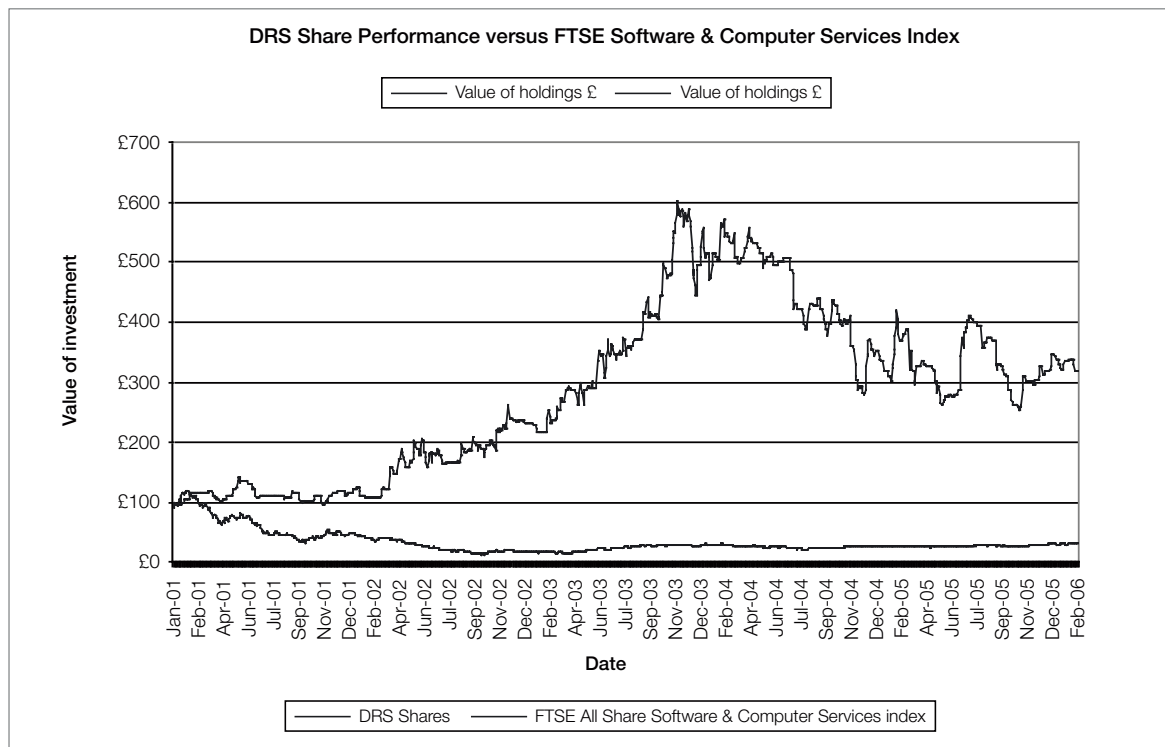
Lord Kinnock and C M Batterham were appointed to the Board during the year and held no shares at the date of their appointment.

Lord Kinnock, on appointment, said he would have to review his position after 12 months to confirm he is able to give sufficient time to fulfil his objectives and obligations of this position. He has agreed to continue in this role for a further year.

performance graphs

The graph below compares the company's total shareholder return performance against the FTSE All Share Software & Computer Services index. The FTSE All Share Software & Computer Services index is considered the most appropriate for comparison purposes.

The graph shows the change in hypothetical value of £100 invested in the company's ordinary shares on 1 January 2001 compared with the change in hypothetical value of £100 invested in the FTSE All Share Software & Computer Services index.



report on directors' remuneration continued

INFORMATION SUBJECT TO AUDIT

directors' remuneration

The remuneration of the individual directors listed is as follows:

	Salary and fees	Annual performance- related bonus*	Benefits	Total 2005	Total 2004	Money purchase pension contributions		
	£000	£000	%	£000	£000	2005 £000	2004 £000	
Executive								
S M Beats	78	–	–	11	89	89	16	16
G Brighton	70	–	–	11	81	80	14	14
S J Day	77	–	–	12	89	89	15	15
A C Lee (CE)	95	–	–	13	108	108	19	19
A M Tebbutt	83	–	–	11	94	93	17	17
	403	–	–	58	461	459	81	81
non-Executive								
C M Batterham	6	–	–	–	6	–	–	–
M Brighton (Ch)	25	–	–	–	25	25	–	–
S Henderson	–	–	–	–	–	8	–	–
Lord Kinnock	13	–	–	–	13	–	–	–
A G Limb	20	–	–	–	20	20	–	–
N V Turnbull	20	–	–	–	20	20	–	–
	84	–	–	–	84	73	–	–
TOTAL	487	–	–	58	545	532	81	81

* Annual performance-related bonus is expressed as a percentage of annual salary. The maximum bonus achievable is, for the Chief Executive, 50% of salary and for other directors 40%.

The Executive Directors waived their rights to any potential non financial performance-related bonus.

Executive Director benefits – S M Beats took up the assistance with personal tax matters, but he did not take up the medical insurance.

share option schemes

Share options are awarded by the Remuneration Committee. There are four company share option schemes currently in operation for Executive Directors and employees: 1996 DRS Restricted Share Scheme, the DRS Data & Research Services plc Enterprise Management Incentive Scheme, the DRS Data & Research Services plc Executive Share Option Plan 2003 and the DRS 2005 Long Term Incentive Plan.

During 2005 options have been granted to the Executive Directors under the terms of the DRS 2005 Long Term Incentive Plan. The performance criteria is based on the level of EPS in the most recently reported financial year on the third anniversary of the date of grant and the TSR

over these three years being at least at the median compared to the companies constituting the FTSE All Share Software & Computer Services Index. The proportion of the award that shall be released is set out on a sliding scale dependent upon the EPS reported in the 2007 audited annual accounts being greater than 3.0p per share. 25% of the qualifying option will be exercisable if the EPS equals 3.0p and 100% will be exercisable if the EPS is 6.0p per share, with pro-rata award between these levels. In any financial year a participant may not be awarded options over ordinary shares with an aggregate value of more than their basic salary calculated by reference to the market value of the ordinary shares at the time of the grant.

INFORMATION SUBJECT TO AUDIT

directors' share options

Details of directors' share options are given below:

	Scheme	Options granted to 01/01/2005	Granted in year	Exercised during year	Options held at 31/12/2005	Exercise price	Exercisable date	Expiry date
A C Lee	RSS	100,000	–	–	100,000	18.0p	10/09/03	10/09/10
A C Lee	EMI	239,437	–	–	239,437	35.5p	28/05/06	28/05/13
A C Lee	EMI	24,793	–	–	24,793	60.5p	26/03/07	26/03/14
A C Lee	ESOP	53,719	–	–	53,719	60.5p	26/03/07	26/03/14
A C Lee	LTIP	–	195,000	–	195,000	NIL	04/11/08	04/11/15
S M Beats	EMI	186,413	–	–	186,413	35.5p	28/05/06	28/05/13
S M Beats	EMI	41,322	–	–	41,322	60.5p	26/03/07	26/03/14
S M Beats	ESOP	11,605	–	–	11,605	60.5p	26/03/07	26/03/14
S M Beats	LTIP	–	107,000	–	107,000	NIL	04/11/08	04/11/15
G Brighton	EMI	140,017	–	–	140,017	35.5p	28/05/06	28/05/13
G Brighton	EMI	42,627	–	–	42,627	60.5p	26/03/07	26/03/14
G Brighton	LTIP	–	96,000	–	96,000	NIL	04/11/08	04/11/15
S J Day	EMI	180,691	–	–	180,691	35.5p	28/05/06	28/05/13
S J Day	EMI	43,239	–	–	43,239	60.5p	26/03/07	26/03/14
S J Day	ESOP	7,672	–	–	7,672	60.5p	26/03/07	26/03/14
S J Day	LTIP	–	105,000	–	105,000	NIL	04/11/08	04/11/15
A M Tebbutt	EMI	186,413	–	–	186,413	35.5p	28/05/06	28/05/13
A M Tebbutt	EMI	41,322	–	–	41,322	60.5p	26/03/07	26/03/14
A M Tebbutt	EMI	17,889	–	–	17,889	60.5p	26/03/07	26/03/14
A M Tebbutt	LTIP	–	113,000	–	113,000	NIL	04/11/08	04/11/15

directors' other rights to shares

During the year G Brighton renounced his rights to 20,000 shares provisionally granted in November 2002 under the Restricted Share Scheme before he was appointed to the Board.

The market price of the company's shares at 31 December 2005 was 37.5p (2004: 42.75p) and the high and low values during the year were 49.5p and 30p respectively.

ON BEHALF OF THE BOARD

N V Turnbull

Chairman of Remuneration Committee

24 March 2006

corporate governance disclosure statement

The Board is committed to ensuring that high standards of corporate governance are maintained by the company and has applied the principles of good governance contained in the revised Combined Code on Corporate Governance issued by the Financial Reporting Council in July 2003, except as referred below.

board of directors

The company supports the concept of an effective Board leading and controlling the company. The Board provides leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board sets the company's strategic aims, ensures the necessary financial and human resources are in place for the company to meet its objectives and reviews management performance. The Board sets the company's values and standards and ensures that the company's obligations to its shareholders and others are understood and met.

As part of their role as members of the Board, non-Executive Directors constructively challenge and help develop proposals on strategy. They satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are adequate. They are responsible for determining appropriate levels of remuneration of Executive Directors and have a prime role in appointing, and where necessary removing, Executive Directors, and in succession planning.

The Board met six times in 2005 and has a schedule of matters specifically reserved to it for decision. Management supply the Board with appropriate and timely information and the directors are free to seek any further information they consider necessary. All directors have access to advice from the Company Secretary and independent professionals at the company's expense.

At the year end, the Board consisted of five Executive Directors who hold the key operational positions in the company and five non-Executive Directors who bring a breadth of experience and knowledge.

Two non-Executive Directors were appointed during the year, Lord Kinnock was appointed on the 14 March 2005 and Christopher Batterham was appointed on 12 September 2005.

Four of the non-Executive Directors, Christopher Batterham, Ann Limb, Lord Kinnock and Nigel Turnbull are independent of management and any business or other relationship which could interfere with the exercise of their independent judgement. This provides a balance whereby the Board's decision making cannot be dominated by an individual or a small group. The Chairman of the Board is Malcolm Brighton and the company's business is run by Tony Lee, the Managing Director and Chief Executive. The Board has named Nigel Turnbull as the Senior Independent Director. The Board members are described on pages 8 and 9.

All directors are subject to re-election every three years and on appointment at the first AGM after appointment.

attendance at meetings

The following table details the number of Board and Committee meetings held during the year ended 31 December 2005 and the attendance record of each director.

	Board Meetings	Committee Meetings		
		Audit	Remuneration	Nomination
Number of meetings held in year	6	3	4	2
C M Batterham* (1)	2	1	2	–
S M Beats	6			
G Brighton	6			
M Brighton*	6	2 [#]	4	2
S J Day	6			
Lord Kinnock* (2)	4	1	3	1
A C Lee	6	3 [#]		
A G Limb*	5	3	4	1
A M Tebbutt	6	3 [#]		
N V Turnbull*	6	3	4	2

* non-Executive Director

[#] Attendance by invitation (for all or part of meeting)

(1) C M Batterham was appointed a Director in September 2005

(2) Lord Kinnock was appointed a Director in March 2004

board evaluation

In November 2004, TBSP Limited was appointed to carry out a 360° appraisal of all the Board members. The results were presented and discussed at the January 2005 Remuneration Committee meeting. One-to-one feedback was subsequently arranged for each member of the Board.

The impact of the appointment of two additional non-Executive Directors during 2005 is still to be assessed and a performance appraisal of the Board has not been undertaken as a result.

board committees

The Board has established three Principal Committees and there are clear written Terms of Reference for the responsibilities delegated to these Committees.

nominations committee

This Committee meets as required to initiate the selection process and the appointment of members to the Board. The members of the Nominations Committee are the Chairman, the Chief Executive, and the four other non-Executive Directors. The Chief Executive is available to members to provide supporting information. The Committee is chaired by Malcolm Brighton. Two Nomination Committee meetings were held during 2005.

audit committee

At the end of 2004, the Audit Committee comprised Nigel Turnbull, Malcolm Brighton and Ann Limb. At the Board meeting in March 2005, Lord Kinnock was appointed to the Committee and Malcolm Brighton retired from the Committee. Chris Batterham was appointed to the Committee in September 2005. The Committee is still chaired by Nigel Turnbull, and all four non-Executive Directors are independent in accordance with the Combined code (2003).

corporate governance disclosure

statement continued

The Committee reviews the independence and objectivity of the external auditors and obtains confirmation of independence from them on an annual basis. The Audit Committee reviews the nature and extent of all audit services supplied by the external auditors, seeking to balance objectivity and value for money. In determining the policy, the Audit Committee has taken into account relevant ethical guidance regarding the provision of non-audit services by the external audit firm, and does not agree to the auditor providing a service if, having regard to the ethical guidance, the result is that:

- the external auditor audits its own firm's work;
- the external auditor makes management decisions for the company;
- a mutuality of interest is created; or
- the external auditor is put in the role of advocate for the company.

remuneration committee

The Remuneration Committee is responsible for determining the remuneration of the Executive Directors and for recommending and monitoring the level and structure of remuneration for certain senior executives.

The report on directors' remuneration set out on pages 13 to 17 contain further information on the Remuneration Committee and the company's remuneration policy for Executive and non-Executive Directors.

internal control

The Board is responsible for maintaining a sound system of internal control to assist with safeguarding shareholders investment and the company's assets and to enable the company to achieve its objectives. The directors acknowledge their responsibility for the company's system of internal control and for reviewing its effectiveness. The Board has continued to operate an internal process to review formally the operation and effectiveness of the company's internal control. It should be noted that such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurances against material errors, losses or fraud.

The Board and senior managers are involved in an ongoing process of risk assessment and evaluation of internal controls and procedures to meet the standards outlined in the "Internal Control Guidance for Directors on the Combined Code". The Board has adopted a schedule of matters which are required to be brought to it for decision. This procedure is intended to ensure the directors maintain full and effective financial and operational control over the business and at least one issue of strategic risk is reviewed in detail at each Board meeting.

Internal financial controls are based upon a budgetary process which involves senior managers working with the Executive Directors to prepare an annual budget that is in line with corporate objectives. Senior managers' performance is then monitored against the agreed financial targets in management accounts that are prepared on a four weekly basis. The overall approach is supported by detailed internal financial controls operated on a day to day basis on all aspects of the business.

Internal operational controls are based on project management teams assigned to each major customer contract or internal development. Such project teams are cross functional to reflect the needs of the project and to encourage the interaction of skills and knowledge throughout the company.

The Board has considered the need for an internal audit function but has decided the size of the company does not justify it at present. However, it will keep the decision under annual review.

environmental policy

It is the company's policy to support and encourage environmentally sound business operations. Recognising that the company's own operations have minimal direct environmental impact, our policy is to:

- meet all statutory obligations placed on us
- where sensible, encourage working practices, such as electronic information exchange, that reduce environmental load
- recycle waste products wherever possible, encourage use of environmentally friendly materials and dispose safely of any non-recyclable materials.

health and safety

The company recognises the importance of this and recognises the high standard required to ensure the health, safety and welfare of its employees at work, its customers and the general public.

relations with shareholders

The company is committed to ensuring that there is effective communication with all shareholders. The company operates a well developed and up-to-date website which provides all regulatory news announcements, press releases and initiatives of direct interest to shareholders. An electronic version of the Annual Report and Accounts is available to allow this information to be easily downloaded. That website address is www.drs.co.uk.

Following the publication of the interim and full year results, the Chief Executive and Finance Director meet with the major institutional shareholders. Fund managers and analysts are also given the opportunity to meet with a member of the executive board, if they so require. In May 2005 the decision was taken to appoint KBC Peel Hunt as the company's stockbrokers.

The AGM is used to communicate with private investors and they are encouraged to participate. The Chairmen of the Audit and Remuneration Committees are available to answer questions. Separate resolutions are proposed on each issue so that they can be given proper consideration and there is a resolution to adopt the Annual Report and Accounts. The company counts all proxy votes and will indicate the level of proxies lodged on each resolution before it has been dealt with by a show of hands.

compliance

Combined Code (2003)

The company is committed to applying the highest principles of Corporate Governance and is taking relevant action to work towards compliance as is appropriate for a company of its size. The Board believes that the company has been in compliance with the provisions of the Combined Code (2003) during the year other than the following items detailed below:

- A.2.2 The Chairman does not meet the independence criteria set out in the Combined Code (2003). He is one of the founding directors of the company who continues to have a significant role owning 20% of the company's share capital.
- A.6.1 The company did not carry out a performance evaluation of the Board and its Committees during 2005.
- C.2.1 The company is not fully compliant with the standards outlined in the "Internal Control Guidance for Directors on the Combined Code". The directors believe that a company of this size cannot justify the cost of putting in place all the formal review procedures.
- D.1.2 The responsibility of communicating with the major shareholder and institutional investors rests with the Chief Executive and the Finance Director. It is the company's policy to make the directors available at the shareholders request.

BY ORDER OF THE BOARD

A M Tebbutt

Company Secretary

24 March 2005

Volatility assumptions

Annualized expected volatility was determined by calculating the average of standard deviations of daily continuously compounded returns of the company's share price calculated over one, two and three years back from the date of grant of each instrument.

Options outstanding

	Type	Date of grant	Number	Vesting period	Exercisable	Expiry date	Weighted exercise price
At 31 December 2004							
	Ordinary	29/05/2003	932,971	3 years	35.5p	28/05/2013	12.75p
	Ordinary	26/03/2004	284,188	3 years	60.5p	26/03/2014	21.62p
	Ordinary	07/04/2004	160,000	3 years	Nil	06/04/2007	56.76p
			1,377,159				19.69p

There have been no movements in the brought forward options.

	Type	Date of grant	Number	Vesting period	Exercisable	Expiry date	Weighted exercise price
At 31 December 2005							
	Ordinary	29/05/2003	932,971	3 years	35.5p	28/05/2013	12.75p
	Ordinary	26/03/2004	284,188	3 years	60.5p	26/03/2014	21.62p
	Ordinary	07/04/2004	160,000	3 years	Nil	06/04/2007	56.76p
	Ordinary	02/11/2005	616,000	3 years	Nil	06/04/2007	26.00p
			1,993,159				21.64p

31 post balance sheets events

On the 1 January 2006, DRS Data & Research Services plc transferred its existing ongoing business to a fully owned subsidiary called DRS Data Services Limited which was created for the purpose.

On the 31 January 2006, DRS Data & Research Services plc acquired Peladon Software Inc. together with its 100% owned subsidiary, Peladon Software Limited. Due to the timing of the deal, it has only been possible to prepare provisional accounts to the 31 January 2006. These provisional accounts show an insignificant net asset deficit before considering fair value adjustments in respect of unpatented technology and know how. It is considered impractical to give the additional disclosures required by IFRS3 at this stage.

report of the independent auditors to the members of DRS Data & Research Services plc

We have audited the financial statements of DRS Data & Research Services plc for the year ended 31 December 2005, which comprise the income statement, the balance sheet, the state of changes in shareholders' equity cash flow statement and notes 1 to 31. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the report on directors' remuneration that is described as having been audited.

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

respective responsibilities of directors and auditors

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

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

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you if, in our opinion, the report of the directors is not consistent with the financial statements, 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 other information contained in the annual report, and consider whether it is consistent with the audited financial statements. This other information comprises only the chairman's statement, the operating and financial review, the report of the directors, the unaudited part of the report on directors' remuneration, and the corporate governance disclosure statement. 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. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

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

opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the company's affairs as at 31 December 2005 and of its loss for the year then ended; and
- 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 Article 4 of the IAS Regulation.

separate opinion in relation to IFRSs

As explained in Note 2.1 to the financial statements, the company in addition to complying with its legal obligation to comply with IFRSs as adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board.

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

GRANT THORNTON UK LLP

Registered Auditors

Chartered Accountants

Central Milton Keynes

24 March 2005

1 The maintenance and integrity of the DRS Data & Research Services 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 financial statements since they were initially presented on the website.

2 Legislation in the United Kingdom governing the preparation and dissemination of the financial statements may differ from legislation in other jurisdictions.

income statement for the year ended
31 december 2005

	Notes	2005 £000	2004 £000
Sales	6	12,452	14,408
Cost of sales		(7,835)	(9,993)
Gross profit		4,617	4,415
Other operating income	8	146	249
Selling and marketing costs		(1,266)	(1,055)
Administrative expenses		(3,420)	(3,103)
Finance costs	10	(60)	(69)
Profit before income tax		17	437
Tax charge	11	(24)	(2)
(Loss)/Profit for the period		(7)	435

(Loss)/Earnings per share for profit attributable to the equity holders of the company during the year (expressed in pence per share)

- basic	23	(0.02p)	1.31p
- diluted	23	(0.02p)	1.29p

balance sheet at 31 december 2005

	Notes	2005 £000	2004 £000
ASSETS			
Non-current assets			
Property, plant and equipment	12	4,103	4,333
Intangible assets	13	788	27
Deferred income tax assets	20	20	18
		4,911	4,378
Current assets			
Inventories	14	1,517	1,751
Trade and other receivables	15	3,133	1,978
Other financial assets at fair value through profit or loss	16	1,063	3,419
Cash and cash equivalents	17	2,284	1,478
		7,997	8,626
Total assets		12,908	13,004
EQUITY			
Capital and reserves attributable to the company's equity holders			
Share capital	18	1,731	1,731
Share premium account	19	5,377	5,377
Capital redemption reserve	19	115	115
Treasury shares		(1,166)	(1,166)
Own shares reserve	19	(120)	(122)
Profit and loss account		2,411	2,692
Total equity		8,348	8,627
LIABILITIES			
Non-current liabilities			
Borrowings		–	1,000
Deferred income tax liabilities	20	30	56
		30	1,056
Current liabilities			
Trade and other payables	21	3,477	3,255
Current income tax liabilities		53	66
Borrowings	22	1,000	–
		4,530	3,321
Total liabilities		4,560	4,377
Total equity and liabilities		12,908	13,004

The financial statements were approved by the Board of Directors on 24 March 2006 and signed on its behalf by:

A C Lee
Chief Executive

A M Tebbutt
Finance Director

statement of changes in shareholders' equity

	Share capital £000	Share premium account £000	Capital redemption reserve £000	Treasury shares £000	Own shares reserve £000	Profit and loss account £000	Total £000
At 1 January 2004	1,731	5,377	115	–	(122)	2,716	9,817
Purchase of Treasury shares	–	–	–	(1,166)	–	–	(1,166)
Profit for the period	–	–	–	–	–	435	435
Employee share-based compensation	–	–	–	–	–	42	42
Dividend	–	–	–	–	–	(501)	(501)
At 31 December 2004	1,731	5,377	115	(1,166)	(122)	2,692	8,627
Loss for the period	–	–	–	–	–	(7)	(7)
Employee share-based compensation	–	–	–	–	–	47	47
Deferred tax on items relating to equity	–	–	–	–	–	2	2
Dividend	–	–	–	–	–	(321)	(321)
Own shares vesting	–	–	–	–	2	(2)	–
At 31 December 2005	1,731	5,377	115	(1,166)	(120)	2,411	8,348

cash flow statement for the year ended
31 december 2005

	Note	2005 £000	2004 £000
Cash flows from operating activities			
Cash generated (used) from operations	25	189	(72)
Interest paid		(57)	(54)
Income tax paid		(62)	(648)
Net cash generated (used) in operating activities		70	(774)
Cash flows from investing activities			
Purchases of property, plant and equipment (PPE)		(496)	(299)
Proceeds from sale of PPE		15	36
Purchase of intangible assets		(960)	(8)
Purchases of financial assets at fair value through profit or loss		(1,032)	(1,600)
Proceeds from sale of financial assets at fair value through profit or loss		3,392	4,484
Interest received		138	239
Net cash generated from investing activities		1,057	2,852
Cash flows from financing activities			
Purchase of treasury shares		–	(1,166)
Dividends paid to company's shareholders		(321)	(501)
Net cash used in financial activities		(321)	(1,667)
Net increase in cash and cash equivalents			
Cash and cash equivalents at beginning of period		1,478	1,063
Exchange gains on cash		–	4
Cash and cash equivalents at end of period		2,284	1,478

notes to the financial statements for the year ended 31 december 2005

1 general information

1.1 nature of operations

DRS Data & Research Services plc is a public limited company with a full listing on the London Stock Exchange incorporated and domiciled in England. The address of the registered office is 1 Danbury Court, Linford Wood, Milton Keynes.

On the 1 January 2006, DRS Data & Research Services plc transferred its operational activities to a fully owned subsidiary called DRS Data Services Limited. Up to the close of business on the 31 December 2005, the principal activity of providing data capture services, the manufacture and sale of Optical and Image scanning equipment and complementary services was undertaken by the holding company. Thereafter it shall be undertaken by the subsidiary, DRS Data Services Limited.

On the 31 January 2006, DRS Data & Research Services plc entered into an agreement to acquire the Peladon Software Group for a total consideration of \$4,865,000 (£2,748,000). The Group comprises of Peladon Software Inc, which is based in San Diego, California and has a fully owned subsidiary, Peladon Software Limited, based in Andover, England. Peladon Software is a leading provider of data capture solutions designed to manage business critical information obtained from paper using its own internally developed DocXP4 software. The operating and financial review on pages 4 to 7 provides further details about the Peladon Software Group's operational activities.

1.2 accounting convention

The financial statements of the company have been prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union and as developed and published by the International Accounting Standards Board (IASB).

DRS Data & Research Services plc has adopted IFRS for the first time in its financial statements for the year ending 31 December 2005. The transition to IFRS reporting has resulted in a number of changes in the reported financial statements, notes thereto and accounting policies compared to previous annual reports. (See Note 4.2)

2 summary of significant accounting policies

2.1 basis of preparation

These financial statements are for the year ended 31 December 2005. The transition to IFRS has been accounted for in accordance with IFRS1, First time adoption of IFRS.

DRS Data & Research Services plc's financial statements were prepared in accordance with United Kingdom's Generally Accepted Accounting Practice (UKGAAP) until 31 December 2004. UKGAAP differs in some areas from IFRS; IFRS1 mandates that most IFRS are to be applied fully retrospectively. The transition balance sheet as at 1 January 2004 has been restated assuming that the IFRS accounting policies had always been applied. The comparative figures in respect of 2004 were restated to reflect these adjustments, except as described in the accounting policies.

Reconciliations and descriptions of the effect of the transition from UKGAAP to IFRS on the company's equity and its net income and cash flows are provided in Note 4. The transition from UKGAAP to IFRS has no effect upon the cash flows generated by the company. The IFRS cash flow statement is presented in a different format to that previously reported under UKGAAP with cash flows split into three categories – operating activities, investing activities and financing activities. The reconciling items between the two reporting formats have no net impact on cash flows generated.

2.2 revenue recognition

Turnover is the total amount receivable by the company for goods supplied and services provided net of VAT and trade discounts.

Sales of goods are recognised when the company has delivered products to the customer and collectability of the related receivables is reasonably assured.

Sales of services are recognised in the accounting period in which the work on the services is performed in accordance with the customers' agreed requirements.

Rental income is recognised on a straight-line basis over the period of the lease.

In the case of long-term contracts, turnover is recognised to the extent that the company has obtained the right to consideration, and is primarily the proportion of total contract value that costs incurred to date bear to total expected contract costs.

2.3 leases

(a) The company is the lessee

Leases where the lessor retains substantially all the risks and rewards of ownership are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

(b) The company is the lessor

Scanning equipment leased to third parties under operating leases are included in property, plant and equipment in the balance sheet. They are depreciated over their expected useful lives. Rental income is recognised on a straight-line basis over the lease term.

2.4 dividends

Under IFRS proposed dividends do not meet the definition of a liability until such time as they have been approved by shareholders at the Annual General Meeting. Therefore, DRS will no longer recognise a liability in any period for dividends that have been proposed but will not be approved until after the balance sheet date.

2.5 segment reporting

Segmental data in this statement is analysed across the core functions of data handling (being scanning equipment, print, software and bureau services). The analysis reflects the work undertaken by the direct cost centres within the company. The cost of resources managed by indirect cost centres has been apportioned to the core functions by the most appropriate methods that can be consistently applied. Many of these support services are shared.

2.6 foreign currency translation

The company tries to deal in Sterling wherever possible in order to avoid the risk of foreign currency exchange rate movements.

Foreign currency transactions are translated into Sterling using the exchange rates prevailing at the dates of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of period-end monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

2.7 property, plant and equipment

Land and buildings relate to the company's Head Office at Linford Wood, Milton Keynes. All property, plant and equipment are shown at cost less depreciation, except for land which is shown at cost. Cost includes expenditure that is directly attributable to the acquisition of the item.

Depreciation is provided on a straight-line basis to allocate the cost of each asset less its estimated residual value over its estimated useful life, as follows:

Freehold buildings	50 years
Computer equipment	3 years
Fixtures and fittings	5 years
Plant and machinery	3 – 10 years
Rental machines	3 years
Motor vehicles	5 years

Items of property, plant and equipment are subject to review for impairment where indications of impairment exist. Any impairment is charged to the income statement as it arises.

notes to the financial statements for the year ended 31 december 2005 continued

2.8 intangible assets

(a) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and to bring into use the specific software. These costs are amortised over their estimated useful lives of three years.

Costs associated with maintaining computer software programs are recognised as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the company, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets.

Computer software that has been capitalised is amortised on a straight-line basis over three years from the date it is put to operational use.

(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 technological feasibility, and costs can be measured reliably. Development costs that have a finite useful life and that have been capitalised are amortised from the commencement of their use on a straight-line basis over the period of their expected benefit, not exceeding three years.

2.9 investments – financial assets at fair value through profit or loss

The company uses financial instruments comprising fixed interest corporate bonds and fixed interest funds which it has classified as financial assets at fair value through profit or loss. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated. Assets in this category are classified as current if they are either

held for trading or are expected to be realised within 12 months of the balance sheet date. Realised and unrealised gains and losses arising from changes in fair value are included in the income statement. The fair values of quoted investments are based on current bid prices.

2.10 inventories

Inventories are valued at the lower of cost and net realisable value. Cost is determined using the first-in, first-out method. The cost of finished goods and work-in-progress comprises raw materials, direct labour, other direct costs and, where appropriate, a proportion of attributable production overheads. Net realisable value is the estimated selling price in the ordinary course of business less applicable variable selling expenses.

2.11 trade and other receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement.

2.12 cash and cash equivalents

Cash and cash equivalents include short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

2.13 share capital

Comprises ordinary shares with a nominal value of 5p each.

Where the company purchases treasury shares, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the company's equity holders until the shares are cancelled, re-issued or disposed of. Where such shares are subsequently sold or re-issued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the company's equity holders.

2.14 borrowings

The company's only borrowing is a secured loan taken out in June 2001 to purchase the freehold land and buildings. The loan is shown at fair value at point of recognition, net of transactions costs incurred, thereafter at amortised cost using the effective interest rate method. Interest thereon is charged to the income statement as it accrues.

2.15 accounting for income taxes

The 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 net 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 company's liability for current tax is calculated by using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount 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 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.

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

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

2.16 employee benefits

(a) Pension obligations

The company operates defined contribution pension schemes under which the company pays fixed contributions into separate entities. The company has no legal or constructive obligations to pay further contributions after payment of the fixed contribution. The contributions to the pension schemes are charged to the income statement as they accrue, thereby matching the cost of the company's pension obligations to the period of employment to which they relate.

(b) Bonus plans and profit sharing

The company recognises a liability and expense for bonuses and profit sharing. Managers may be entitled to a bonus based on a formula that takes into consideration turnover, EPS, residual income in relation to employees' responsibilities and an assessment of the individual's performance which includes non financial criteria. Employees who do not participate in the bonus scheme are entitled to participate in a profit sharing scheme based on the company's profitability. The cost of providing these schemes is accrued against profits in the period in which the bonus is earned.

notes to the financial statements for the year ended 31 december 2005 continued

(c) Share-based employee remuneration

All share-based payment arrangements granted after 7 November 2002 and not vested by 1 January 2005 are recognised in the financial statements. The company operates equity-settled share-based remuneration plans for remuneration of certain of its employees.

All employee services received in exchange for the grant of any share-based remuneration are measured at their fair values. These are indirectly determined by reference to the fair value of the share options or shares awarded. Their value is appraised at the grant date and excludes the impact of any non-market vesting conditions (for example, profitability and sales growth targets).

All share-based remuneration is ultimately recognised as an expense in the income statement with a corresponding credit to shareholders' funds. If vesting periods or other vesting conditions apply, the expense is allocated over the vesting period, based on the best available estimate of the number of share options or shares expected to vest. Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. Estimates are subsequently revised if there is any indication that the number of share options expected to vest differs from previous estimates. No adjustment is made to expense recognised in prior periods if fewer share options ultimately are exercised than originally estimated.

Upon exercise of share options fulfilled by the issue of new shares, the proceeds received net of any directly attributable transaction costs up to the nominal value of the shares issued, are allocated to share capital with any excess being recorded as share premium. Options or share grants fulfilled from shares held by employee share trusts are credited to the own share reserve.

2.17 new accounting standards and IFRIC interpretations

Certain new accounting standards and IFRIC interpretations have been published that are mandatory for accounting periods beginning on or after 1 January 2006. The company believes that these new standards and interpretations will have little effect on the company and the impact on reporting requirements is minimal.

3.0 financial risk management

3.1 financial risk factors

The company's activities expose it to a variety of financial risks. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

(a) Currency risk

The company operates internationally and is subject to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar and the Euro. The company does not hedge any transactions, and foreign exchange differences on retranslation of foreign assets and liabilities are recognised in the income statement.

(b) Credit risk

The company has no significant concentrations of credit risk other than the one item mentioned in Note 15. Where appropriate, sales to overseas customers are usually underwritten using letters of credit unless the customer makes a significant up front payment. A summary of all customers with indebtedness greater than £100,000 is prepared on a monthly basis for the directors and senior managers to review.

(c) Price risk

The company is exposed to a price risk on fixed interest corporate bonds which are classified on the balance sheet as financial assets at fair value through profit or loss.

(d) Interest rate risk

The company finances its operations through a mixture of shareholders' funds and bank loans. The company's exposure to interest rate fluctuations on its borrowings is managed by the use of capped floating facilities. The company mixes the duration of its deposits to reduce the impact of interest rate fluctuations.

(e) Liquidity risk

The company takes a prudent approach to managing liquidity risk to ensure sufficient cash is available to meet foreseeable needs and to invest cash assets safely and profitably.

4.0 transition to IFRS

4.1 basis of transition to IFRS

The company's financial statements for the year ended 31 December 2005 are the first financial statements that comply with IFRS. These financial statements have been prepared to comply with IFRS as described in Note 2.1.

In preparing these financial statements in accordance with IFRS1, the company has applied the mandatory exceptions and certain of the optional exemptions from full respective application of IFRS as set out below.

4.1.2 exemptions from full retrospective application elected by the company

The company has taken advantage of the following exemptions. No other exemptions are considered relevant.

(a) Fair value as deemed cost exemption

DRS has elected to measure the land and buildings at Linford Wood, Milton Keynes at fair value as at 1 January 2004. The application of this exemption is detailed in Note 4.2.4(a).

(b) Share-based payment transaction exemption

The company has elected to apply the share-based payment exemption. It applies IFRS2 from 1 January 2004 to those options that were issued after 7 November 2002 but have not vested by 1 January 2005. The application of this exemption is detailed in Note 4.2.2(a).

notes to the financial statements for the year ended
31 december 2005 continued

4.2.1 summary of equity

	01/01/2004	31/12/2004
Total equity under UKGAAP	9,651	8,493
Restatement of Linford Wood office to fair value	(158)	(163)
Reversal of ordinary dividend proposed	341	321
Deferred tax on items relating to equity	(17)	(24)
	9,817	8,627

4.2.2. reconciliation of net income for year ended 31 December 2004

	Note	UKGAAP £000	Effect of transition to IFRS £000	IFRS £000
Sales		14,408		14,408
Cost of sales		(9,993)		(9,993)
Gross profit		4,415		4,415
Other operating income		249		249
Selling and marketing costs		(1,055)		(1,055)
Administrative expenses	(a)	(3,088)	(15)	(3,103)
Finance costs – net		(69)		(69)
Profit before tax		452	(15)	437
Income tax expense	(b)	5	(7)	(2)
Profit for the period		457	(22)	435

explanation of the effect of the transition to IFRS

The following explains the material adjustments to the balance sheet and income statement.

(a)	Administrative expenses	
	Restatement of Linford Wood head office to fair value	(5)
	Share-based payment charge under IFRS2	(10)
		(15)
(b)	Total effect of measuring deferred tax in accordance with IAS12	(7)

The company has changed its reporting format from nature of expense to a functional breakdown. This decision allows the presentation of income statements in a format that operationally reflects the running of the business, further details of which are given in the segmental information provided in Note 5.

4.2.3. reconciliation of equity at 1 January 2004

	Note	UKGAAP £000	Effect of transition to IFRS £000	IFRS £000
ASSETS				
Non-current assets				
Property, plant and equipment	a	5,005	(200)	4,805
Intangible assets	b	–	42	42
Deferred income tax assets		–	–	–
		5,005	(158)	4,847
Current assets				
Inventories		2,107	–	2,107
Trade and other receivables		1,999	–	1,999
Other financial assets at fair value through profit or loss		6,312	–	6,312
Cash and cash equivalents		1,063	–	1,063
		11,481	–	11,481
Total assets		16,486	(158)	16,328
EQUITY				
Capital and reserves attributable to equity holders				
Share capital		1,731	–	1,731
Treasury shares		–	–	–
Fair value and other reserves		5,370	–	5,370
Retained earnings and other reserves	e	2,550	166	2,716
Total equity		9,651	166	9,817
LIABILITIES				
Non-current liabilities				
Borrowings		1,000	–	1,000
Deferred income tax liabilities	c	60	17	77
		1,060	17	1,077
Current liabilities				
Trade and other payables	d	5,102	(341)	4,761
Current income tax liabilities		673	–	673
Borrowings		–	–	–
Provisions and other liabilities		–	–	–
		5,775	(341)	5,434
Total liabilities		6,835	(324)	6,511
Total equity and liabilities		16,486	(158)	16,328

notes to the financial statements for the year ended
31 december 2005 continued

explanation of the effect of the transition to IFRS

The following explains the material adjustments to the balance sheet and income statement.

(a)	Property, plant and equipment	
	Restatement of Linford Wood head office to fair value	(158)
	Reclassification of software licences as an intangible asset	(42)
		<hr/>
		(200)
(b)	Intangible assets	
	Reclassification of software licences as an intangible asset	42
(c)	Deferred income tax liabilities	
	Overall impact of recognising deferred tax in accordance with IAS12	17
(d)	Trade and other payables (current)	
	Reversal of proposed ordinary dividend payable	(341)
(e)	Retained earnings	
	Restatement of Linford Wood head office to fair value	(158)
	Overall impact of recognising deferred tax in accordance with IAS12	(17)
	Reversal of proposed ordinary dividend payable	341
		<hr/>
	Total impact – increase in retained earnings	<hr/> 166

4.2.4. reconciliation of equity at 31 December 2004 and 1 January 2005

	Note	UKGAAP £000	Effect of transition to IFRS £000	IFRS £000
ASSETS				
Non-current assets				
Property, plant and equipment	a	4,523	(190)	4,333
Intangible assets	b	–	27	27
Deferred income tax assets		18	–	18
		4,541	(163)	4,378
Current assets				
Inventories		1,751	–	1,751
Trade and other receivables		1,978	–	1,978
Other financial assets at fair value through profit or loss		3,419	–	3,419
Cash and cash equivalents		1,478	–	1,478
		8,626	–	8,626
Total assets		13,167	(163)	13,004
EQUITY				
Capital and reserves attributable to equity holders				
Share capital		1,731	–	1,731
Treasury shares		(1,166)	–	(1,166)
Fair value and other reserves		5,370	–	5,370
Retained earnings and other reserves	e	2,558	134	2,692
Total equity		8,493	134	8,627
LIABILITIES				
Non-current liabilities				
Borrowings		1,000	–	1,000
Deferred income tax liabilities	c	32	24	56
		1,032	24	1,056
Current liabilities				
Trade and other payables	d	3,576	(321)	3,255
Current income tax liabilities		66	–	66
Borrowings		–	–	–
Provisions and other liabilities		–	–	–
		3,642	(321)	3,321
Total liabilities		4,674	(297)	4,377
Total equity and liabilities		13,167	(163)	13,004

notes to the financial statements for the year ended 31 december 2005 continued

explanation of the effect of the transition to IFRS

The following explains the material adjustments to the balance sheet and income statement.

(a)	Property, plant and equipment	
	Restatement of Linford Wood head office to fair value	(163)
	Reclassification of software licences as an intangible asset	(27)
		<hr/>
		(190)
(b)	Intangible assets	
	Reclassification of software licences as an intangible asset	27
(c)	Deferred income tax liabilities	
	Overall impact of recognising deferred tax in accordance with IAS12	24
(d)	Trade and other payables (current)	
	Reversal of proposed ordinary dividend payable	(321)
(e)	Retained earnings	
	Restatement of Linford Wood head office to fair value	(163)
	Overall impact of recognising deferred tax in accordance with IAS12	(24)
	Reversal of proposed ordinary dividend payable	321
		<hr/>
	Total impact – increase in retained earnings	134

4.2.5. reconciliation of cash flows

The change from UKGAAP to IFRS does not change the actual cash held in the company.

The format of the cash flow statement itself has changed, but the cash generated remains the same.

(a) for the year ended 31 December 2004

Under IFRS the profit before tax figure is reduced by £15,000, the depreciation charge is increased by £5,000 and amortisation of the share based payment charge under IFRS2 is increased by £10,000 leaving the cash generated from operations unchanged.

(b) for the year ended 31 December 2005

Under IFRS the profit before tax figure is reduced by £38,000, the depreciation charge is increased by £6,000 and amortisation of the share based payment charge under IFRS2 is increased by £32,000 leaving the cash generated from operations unchanged.

5 segment information

The principal activities of the company continue to be the provision of data capture services, the manufacture, sale and support of Optical and Image scanning equipment, design and printing of documentation used for data capture and associated software and bureau services. Approximately half the company's revenue relates to products and services, and the other half relates to providing tailored data capture solutions. The company is organised functionally, with each function of the business specialising in its own area of expertise. Project managers look to the functional areas in providing the appropriate tailored mix of products and services to fulfil each specific contract. In turn the functional areas are supported by indirect cost centre departments such as Research and Development, Communication and Information Development and I.T. Support.

The segments reflect the principal activities of the company: Scanning equipment; Print; and Software and Bureau services.

Business segments for the year ended 31 December 2005

	Scanning equipment £000	Print £000	Software and services £000	Total £000
Revenue	3,741	4,499	4,212	12,452
Apportioned costs	(2,632)	(3,704)	(4,452)	(10,788)
Operating margin	1,109	795	(240)	1,664
Unallocated costs				(1,647)
Profit before tax				17
Segmented assets	3,842	3,511	2,204	9,557
Unallocated assets				3,351
Total assets				12,908
Segmented liabilities	(1,927)	(1,572)	(976)	(4,475)
Unallocated liabilities				(85)
Total liabilities				(4,560)
Capital additions	74	48	1,334	1,456
Depreciation and amortisation	215	251	457	923

Geographical segments for the year ended 31 December 2005

	United Kingdom £000	Africa £000	Rest of world £000	Total £000
Revenue	8,101	3,739	612	12,452

All revenue is generated from DRS Data & Research Services plc operations in Milton Keynes, England.

notes to the financial statements for the year ended
31 december 2005 continued

Comparative figures for the year ended 31 December 2004 are as follows:

Business segments

	Scanning equipment	Print	Software and services	Total
	£000	£000	£000	£000
Revenue	5,954	5,230	3,224	14,408
Apportioned costs	(4,536)	(3,838)	(4,154)	(12,528)
Operating margin	1,418	1,392	(930)	1,880
Unallocated costs				(1,443)
Profit before tax				437
Segmented assets	4,139	1,385	2,544	8,068
Unallocated assets				4,936
Total assets				13,004
Segmented liabilities	(1,839)	(1,618)	(777)	(4,234)
Unallocated liabilities				(143)
Total liabilities				(4,377)
Capital additions	103	75	129	307
Depreciation and amortisation	293	310	189	792

Geographical segments for the year ended 31 December 2004

	United Kingdom	Africa	Rest of world	Total
	£000	£000	£000	£000
Revenue	10,685	3,278	445	14,408

All revenue is generated from DRS Data & Research Services plc operations in Milton Keynes, England.

6 revenue and profit before tax

	2005	2004
	£000	£000
The significant categories of revenue recognised during the period are:		
Sale of goods	3,493	3,394
Rendering of services including operating lease income	8,959	11,014
	12,452	14,408

Profit on ordinary activities before taxation is stated after:

Auditors' remuneration:

– audit services	26	24
– advice on implementation of IFRS	23	–
– other compliance and reporting services	10	18
– other non audit services	2	2
Depreciation	724	769
Amortisation	199	23
Hire of plant and machinery	34	260
Operating lease expense	285	316
R&D expense	1,136	1,544

7 operating lease income

Operating lease income relates to the leasing of CD230 and CD360 scanners into UK schools. All of the machines are on a standard agreement which can be terminated on its anniversary date by the customer provided they give three months' notice prior to the anniversary date of their intention to terminate the contract. The minimum future lease income at the 31 December 2005 is £347,000.

8 other operating income

	2005	2004
	£000	£000
Interest income		
Other financial assets at fair value through profit or loss	103	215
Bank interest	35	24
– fair value gains (realised and unrealised)	7	6
Net foreign exchange transaction gains	1	4
	146	249

notes to the financial statements for the year ended
31 december 2005 continued

9 directors and employee benefit expense

	2005	2004
	£000	£000
Staff costs during the year were:		
Wages and salaries	4,789	4,712
Social security costs	514	505
Share options granted to directors and employees	48	43
Pension costs – defined contribution plans	279	266
	5,630	5,526

The average number of employees of the company during the year was:

	2005	2004
Scanning equipment	55	58
Print	40	44
Software and services	70	60
	165	162

Remuneration in respect of directors was as follows:

	2005	2004
	£000	£000
Emoluments	545	532
Pension contributions to money purchase pension schemes	81	81
	626	613

Further details on directors' remuneration and share options are set out in the directors' remuneration report.

10 finance costs

	31/12/2005	31/12/2004
	£000	£000
Interest expense:		
– bank borrowings	(57)	(54)
– fair value losses (realised and unrealised)	(3)	(15)
	(60)	(69)

11 income tax expense

	31/12/2005	31/12/2004
	£000	£000
Current tax – domestic	53	66
Adjustment in respect of previous period	(3)	(18)
Total current tax	50	48
Deferred tax (Note 20)	(26)	(46)
	24	2

Domestic income tax is calculated at 19% (2004: 30%) of the estimated assessable profit for the year. The movement in tax rate from 30% to 19% is due to levels of profitability.

The charge for the year can be reconciled to the profit per the income statement as follows:

	2005	2004
	£000	£000
Profit before tax	17	437
Tax at domestic income tax rate of 19% (2004: 30%)	3	131
Tax effect of expenses that are not deductible in determining taxable profit	32	29
Additional relief for R&D expenditure	–	(125)
Effect of marginal rate	–	(15)
Effect of change in tax rates	(8)	–
Adjustment in respect of previous periods	(3)	(18)
Tax expense	24	2

notes to the financial statements for the year ended
31 december 2005 continued

12 property, plant and equipment

	Total £000	Freehold land & building £000	Computer equipment £000	Furniture & fittings £000	Plant & machinery £000	Rental machines £000	Motor vehicles £000
At 1 January 2004							
Cost	8,890	2,900	1,654	1,472	2,273	591	–
Accumulated depreciation	(4,085)	–	(1,301)	(964)	(1,410)	(410)	–
Net book amount	4,805	2,900	353	508	863	181	–
For the year ended 31 December 2004							
Opening net amount at 1 January 2004	4,805	2,900	353	508	863	181	–
Additions	299	–	135	51	70	43	–
Disposals (Note 25)	(2)	–	(1)	1	–	(2)	–
Depreciation charge	(769)	(40)	(235)	(176)	(198)	(120)	–
Closing net book amount at 31 December 2004	4,333	2,860	252	384	735	102	–
At 31 December 2004							
Cost	9,078	2,900	1,698	1,522	2,334	624	–
Accumulated depreciation	(4,745)	(40)	(1,446)	(1,138)	(1,599)	(522)	–
Net book amount	4,333	2,860	252	384	735	102	–
For the year ended 31 December 2005							
Opening net amount at 1 January 2005	4,333	2,860	252	384	735	102	–
Additions	496	–	26	306	129	29	6
Disposals (Note 25)	(2)	–	(1)	–	–	(1)	–
Depreciation charge	(724)	(40)	(171)	(225)	(216)	(71)	(1)
Closing net book amount at 31 December 2005	4,103	2,820	106	465	648	59	5
At 31 December 2005							
Cost	9,238	2,900	1,403	1,828	2,452	649	6
Accumulated depreciation	(5,135)	(80)	(1,297)	(1,363)	(1,804)	(590)	(1)
Net book amount	4,103	2,820	106	465	648	59	5

Bank borrowings are secured on Linford Wood land and buildings for the value of £1,000,000 (2004: £1,000,000). See note 22.

13 intangible assets

	Total £000	Computer software £000	Development expenditure £000
At 1 January 2004			
Cost	135	135	–
Accumulated amortisation	(93)	(93)	–
Net book amount	42	42	–
For the year ended 31 December 2004			
Opening net amount at 1 January 2004	42	42	–
Additions	8	8	–
Amortisation charge	(23)	(23)	–
Closing net book amount at 31 December 2004	27	27	–
At 31 December 2004			
Cost	143	143	–
Accumulated amortisation	(116)	(116)	–
Net book amount	27	27	–
For the year ended 31 December 2005			
Opening net amount at 1 January 2005	27	27	–
Additions	960	375	585
Amortisation charge	(199)	(96)	(103)
Closing net book amount at 30 June 2005	788	306	482
At 31 December 2005			
Cost	1,103	518	585
Accumulated amortisation	(315)	(212)	(103)
Net book amount	788	306	482

Computer software relates to the third party software licences purchased by the company to be used in the normal course of its business.

The capitalised development expenditure covers the cost of designing and writing the core e-Marker® software used to electronically mark examination scripts within the education marketplace. Due to the uncertainty of the potential benefits of investing in automated examination marking processes, the criteria for capitalising development expenditure was not met until 2005.

All intangible amortisation is charged to cost of sales within the income statement.

notes to the financial statements for the year ended
31 december 2005 continued

14 inventories

	31/12/2005	31/12/2004
	2005	2004
	£000	£000
Raw materials	602	757
Work in progress	258	137
Finished goods	657	857
	1,517	1,751

Provisions held against the manufacturing inventory have been created in the past when the company over orders on raw materials used in the manufacture of its scanning machines. However, from the start of 2004 obsolescence provisions have been increased to cover the risk of holding scanning machines and materials that are obsolete or do not comply with the requirements of the Restrictions of Hazardous Substances (RoHS) legislation that will come into force from July 2006.

	31/12/2005	Movement	31/12/2004	Movement	31/12/2003
	£000	during year	£000	during year	£000
		£000		£000	
Inventory provision					
PS900 scanners	329	(156)	485	485	–
Other scanners	202	141	61	40	21
Print	–	–	–	–	–
Total	531	(15)	546	525	21

Related carrying value

PS900 scanners	941	–	857	–	502
Other scanners	325	–	678	–	1,374
Manufacturing inventory	1,266	–	1,535	–	1,876
Print inventory	251	–	216	–	231
Total	1,517	–	1,751	–	2,107

300 PS900 scanning machines were produced in 2004 for use in the 2004 GLA contract. The provision that was created in 2004 reflected the potential risk of holding these scanners in light of the forthcoming legislation and future product development. The release of provision in 2005 reflects a higher level of usage than originally expected.

The cost of inventories recognised as an expense and included in “Cost of sales” amounted to £1,937,000 (2004: £2,404,000).

15 trade and other receivables

	31/12/2005	31/12/2004
	£000	£000
Trade receivables	2,474	1,464
Less provision for impairment of receivables	(117)	(117)
Trade receivables – net	2,357	1,347
Amounts recoverable on contracts	406	254
Prepayments and accrued income	370	377
	3,133	1,978

The fair values of trade and other receivables are as follows:

	31/12/2005	31/12/2004
	£000	£000
Trade and other receivables	2,357	1,347
Amounts recoverable on contracts	406	254
Prepayments and accrued income	370	377
	3,133	1,978

There is one significant balance included in trade debtors of £532,000 in respect of the printing of census forms being undertaken for National Planning Commission, Nigeria which is being funded by the EU. There is no other concentration of credit risk.

The company has recognised an expense of £311 for the impairment of its trade receivables during the year (2004: £26,194). The expense has been included in "Administrative expenses" in the income statement.

16 financial assets at fair value through profit or loss

Year ended 31 December 2005	Bonds	Liquidity fund	Total company
	£000	£000	£000
At 1 January 2005 – book value equals fair value	2,388	1,031	3,419
Additions	–	1,032	1,032
Disposals	(2,392)	(1,000)	(3,392)
Fair value adjustment	4	–	4
At 31 December 2005	–	1,063	1,063

Year ended 31 December 2004			
At 1 January 2004 – book value equals fair value	3,741	2,571	6,312
Additions	–	1,600	1,600
Disposals	(1,344)	(3,140)	(4,484)
Fair value adjustment	(9)	–	(9)
At 31 December 2004	2,388	1,031	3,419

The investments above consisted of:

Sterling fixed interest corporate bonds and fixed interest funds confined to investment grade defined minimum rating of "BBB+", where average rating of the portfolio is 'A' or above.

Sterling Liquidity Fund is a UCITS certified open-ended fund with an investment objective of providing investors with daily liquidity and security of capital in a diversified portfolio of short-term securities, instruments and obligations which carry a minimum rating of A1/P1.

notes to the financial statements for the year ended
31 december 2005 continued

17 cash and cash equivalents

	31/12/2005	31/12/2004
	£000	£000
Cash at bank and in hand	393	328
Short term bank deposits	1,891	1,150
	2,284	1,478

The effective interest rate on short term bank deposits was 3.125% (2004: 3.53%). These deposits have an average maturity of 4 days (December 2004: 7 days).

Cash and bank overdrafts include the following for the purposes of the cash flow statement:

	31/12/2005	31/12/2004
	£000	£000
Cash and cash equivalents	2,284	1,478
Bank overdrafts	-	-
	2,284	1,478

Currency risk

The company operates in overseas markets and is subject to currency exposures on transactions undertaken during the year. The company does not hedge any transactions, and foreign exchange differences on retranslation of foreign assets and liabilities are taken to the profit and loss account.

The tables below show the extent to which the company has monetary assets in currencies other than Sterling.

	2005	2005	2004	2004
	US Dollars	Other currencies	US Dollars	Other currencies
	£000	£000	£000	£000
Sterling equivalent	42	266	23	19

18 share capital

	Number of shares	Ordinary shares	Treasury shares	Total
At 1 January 2004	34,621,600	34,621,600	–	34,621,600
Balance at 31 December 2004	34,621,600	34,621,600	(1,930,000)	32,691,600
Balance at 31 December 2005	34,621,600	34,621,600	(1,930,000)	32,691,600

Ordinary shares of 5p each At 31/12/2005 and 31/12/2004

	Number	£000
Authorised	46,000,000	2,300
Allotted, issued, called up and fully paid	34,621,600	1,731

The company acquired 1,930,000 of its own shares through purchase between 3 June and 15 July 2004. The price of these shares ranged between 60p and 59p. The total amount paid to acquire these shares, net of income tax, was £1,166,000 and has been deducted from shareholders' equity. The shares are held as treasury shares. The company has the right to re-issue these shares at a later date. All issued shares are fully paid.

19 other reserves

	Share premium £000	Capital redemption £000	Own share reserve £000	Total Company £000
As at 1 January 2004	5,377	115	–	5,492
Own shares purchased (see Note 4.1.2)	–	–	(122)	(122)
Balance at 31 December 2004	5,377	115	(122)	5,370
Own shares vesting	–	–	2	2
Balance at 31 December 2005	5,377	115	(120)	5,372

The Own Share Reserve represents the cost of shares purchased under the Restricted Share Scheme, less those unconditionally vested in employees. At 31 December 2005, 570,529 (2004: 580,529) shares with a market value of £213,948 (2004: £248,176) were held. Of these 450,000 (2004: 450,000) had been conditionally gifted to employees and a further 100,000 (2004: 100,000) are vested to a director at an option price of 18p. The Scheme authorises the Trustees to purchase up to 5% of the issued share capital, funded by loans from the company. Shares so acquired, are conditionally gifted to employees at the discretion of the Board.

notes to the financial statements for the year ended
31 december 2005 continued

20 deferred income tax

	31/12/2005 £000	31/12/2004 £000
Analysis for financial reporting purposes		
Deferred tax liabilities	30	56
Deferred tax assets	(20)	(18)
	10	38

The movement in the year in the company's net deferred tax position was as follows:

	31/12/2005 £000	31/12/2004 £000
At 1 January 2005	38	77
Charge to income for the year	(26)	(46)
Charge to equity for the year	(2)	7
	10	38

The following are the major deferred tax liabilities and assets recognised by the company and the movements thereon during the period:

	Accelerated tax depreciation £000	Revaluation of property £000	Share options £000	EBT obligations £000	General provision £000	Total £000
At 1 January 2005	32	22	2	(14)	(4)	38
Charge to income for the year	(24)	–	–	–	(2)	(26)
Charge to equity for the year	–	–	(2)	–	–	(2)
At 31 December 2005	8	22	–	(14)	(6)	10

21 trade and other payables

	31/12/2005 £000	31/12/2004 £000
Trade payables	925	622
Deferred income	782	1,585
Social security and other taxes	156	286
Accrued expenses	1,614	762
	3,477	3,255

Fair value equates to carrying value.

22 borrowings

	31/12/2005 £000	31/12/2004 £000
Non-current		
Bank borrowings – secured loan	–	1,000
Current		
Bank borrowings – secured loan	1,000	–
Total borrowings	1,000	1,000

At the end of the year, total borrowings consist of a secured loan taken out in June 2001 to purchase the freehold land and buildings of the company. The loan of £1,000,000 at 15 July 2005 was secured by a fixed charge against the freehold land and buildings. The £1,000,000 was borrowed at a variable rate of 1% over base rate with a 6.5% cap repayable June 2006.

During March 2006, the loan was rearranged for £2,250,000, secured by a fixed charge against the freehold land and buildings at a variable rate of 0.85% over base rate repayable March 2011.

23 (loss)/earnings per share

The calculation of the basic earnings per share is based on the earnings attributable to ordinary shareholders divided by the weighted average number of shares in issue during the year. Shares held in employee share trusts are treated as cancelled for the purposes of this calculation.

The calculation of diluted earnings per share is based on the basic earnings per share, adjusted to allow for the issue of shares and the post tax effect of dividends and/or interest, on the assumed conversion of all dilutive options and other dilutive potential ordinary shares.

Reconciliations of the earnings and weighted average number of shares used in the calculations are set out below:

	Loss £	31/12/2005 Weighted average number of shares	Per share	Earnings £	31/12/2004 Weighted average number of shares	Per share
Basic earnings per share						
Earnings attributable to ordinary shareholders	(7,000)	32,111,400	(0.02p)	435,000	33,093,359	1.31p
Dilutive effect of shares in restricted share scheme		–			323,919	
Dilutive effect of options under unapproved share option scheme		–			67,334	
Dilutive effect of options under the Enterprise Management Incentive Scheme		–			331,904	
Dilutive earnings per share	(7,000)	32,111,400	(0.02p)	435,000	33,816,516	1.29p

notes to the financial statements for the year ended
31 december 2005 continued

24 dividends per share

	Amount payable £000	Dividend per share Pence
Dividend on ordinary shares		
Final paid May 2004	341	1.0
Interim paid November 2004	160	0.5
Total	501	1.5
<hr/>		
Final paid May 2005	321	1.0
Total	321	1.0

The directors do not recommend a dividend.

25 cash generated from operations

	31/12/2005 £000	31/12/2004 £000
(Loss)/profit for the period	(7)	435
Adjustments for:		
– income tax (Note 11)	24	2
– depreciation of property, plant and equipment (Note 12)	724	769
– amortisation of intangible assets (Note 13)	199	23
– IFRS2 charge in respect of EBT (Note 19)	39	42
– IFRS2 charge in respect of LTIP shares	8	–
– profit on sale of property, plant and equipment	(13)	(34)
– fair value losses (including loss on disposal) on other financial assets at fair value through profit or loss (Note 10)	3	15
– fair value gains (including profit on disposal) on other financial assets at fair value through profit or loss (Note 8)	(7)	(6)
– exchange gains on cash holdings (Note 8)	(1)	(4)
– interest income (Note 8)	(138)	(239)
– interest expense (Note 10)	57	54
Changes in working capital (excluding the effects of acquisition and exchange differences on consolidation):		
– inventories	234	356
– trade and other receivables	(1,155)	21
– trade and other payables	222	(1,506)
Cash generated from operations	189	(72)

In the cash flow statement, proceeds from sale of property, plant and equipment comprise:

	31/12/2005	31/12/2004
	£000	£000
Net book amount	2	2
Profit/(loss) on sale of property, plant and equipment	13	34
Proceeds from sale of property, plant and equipment	15	36

26 reconciliation of movements in cash and cash equivalents

	01/01/2005	Cash flow	31/12/2005
	£000	£000	£000
Cash at bank and in hand	328	65	393
Term deposits	1,150	741	1,891
	1,478	806	2,284
Other financial assets at fair value	3,419	(2,356)	1,063
	4,897	(1,550)	3,347

27 contingencies

The company has contingent liabilities in respect of bank guarantees and other matters arising in the ordinary course of business. It is not anticipated that any material liabilities will arise from the contingent liabilities.

notes to the financial statements for the year ended 31 december 2005 continued

28 commitments

(a) Capital commitments

There were no capital commitments at 31 December 2005 or 31 December 2004.

(b) Operating lease commitments

The company has the following lease commitments:

	Lease of land and buildings		Other leases	
	December 2005 £000	December 2004 £000	December 2005 £000	December 2004 £000
Within one year	142	131	83	92
Within two to five years	352	432	57	68
Over five years	–	29	–	–
	494	592	140	160

The company holds three property leases for the five business units occupied by operations in Kiln Farm, Milton Keynes. All three leases are for a period of ten years, two of which expire 7 December 2008 and the third on 30 November 2010. Rent is payable quarterly in advance.

Other leases are all three year contracts. They relate to company vehicles that have an up front payment of three months in advance followed by a monthly payment and a photocopier lease payable quarterly in advance.

29 pension commitments

During 2004 and 2005 the company operated separate defined contribution schemes for the benefit of employees and Executive Directors respectively. In all cases the assets of the schemes are administered by Trustees in funds independent of the company. Pension contributions are shown in Note 9.

30 share based payments

		Type	Number	Vesting period	Term	Exercise price	Method of settlement
Year end 31 December 2003							
29 May 2003	Granted	directors	932,971	3 years	10 years	35.5p	equity
	Exercised						
	Lapsed						
	Forfeited						
Year end 31 December 2004							
26 March 2004	Granted	directors	284,188	3 years	10 years	60.5p	equity
	Exercised						
	Lapsed						
	Forfeited						
7 April 2004	Granted	employees	170,000	3 years	3 years	Nil	equity
	Exercised						
	Lapsed		10,000				
	Forfeited						
Year end 31 December 2005							
2 November 2005	Granted	directors	616,000	3 years	10 years	Nil	equity
	Exercised						
	Lapsed						
	Forfeited						

Calculation of the fair value

	Valuation model	Share price at grant	Exercise price	Expected volatility	Inputs			Fair Value of 1 unit
					Expected life	Expected dividends	Risk-free interest rate	
Year end 31 December 2003								
29 May 2003	Binomial	35.5p	35.5p	44.36%	6 years	–	4.63%	12.75p
Year end 31 December 2004								
26 March 2004	Binomial	60.5p	60.5p	45.87%	6 years	–	4.64%	21.62p
7 April 2004	Binomial	60.5p	0p	45.13%	3 years	3.67%	4.92%	56.76p
Year end 31 December 2005								
2 November 2005	Monte Carlo	34.0p	0p	45.58%	6 years	–	4.50%	26.00p

notes to the financial statements for the year ended 31 december 2005 continued

Performance criteria

Non-market

The share options granted to the Executive Directors are subject to performance criteria set out on a sliding scale dependent upon the increase in Earnings Per Share (EPS), based on the EPS reported in the audited annual accounts for the three years following the granting of the option. 25% of the qualifying option will be exercisable if the rate of growth equals RPI, 50% will be exercisable if the rate of growth equals RPI + 5% per annum and 100% will be exercisable if the rate of growth exceeds RPI + 10% per annum, with pro-rata award between these levels. The probability of the performance criteria being met is minimal and as consequence, no charge has been recognised because no options are expected to vest.

The share options granted to employees are subject to the employees remaining in the employment of the company throughout the three year vesting period, after which time the shares are gifted to the employee.

Valuation methodologies

In order to calculate fair values of the options under consideration we have taken into account factors that knowledgeable, willing market participants would consider in valuing the options.

The fair values of the options with no additional market conditions were estimated using a Binomial option pricing model.

The fair value of the LTIP award, where an element of the release of shares is contingent upon relative performance of the company's Total Shareholder Return (TSR) against the TSRs of the companies in the comparator group, was calculated using a Monte Carlo Simulation model.