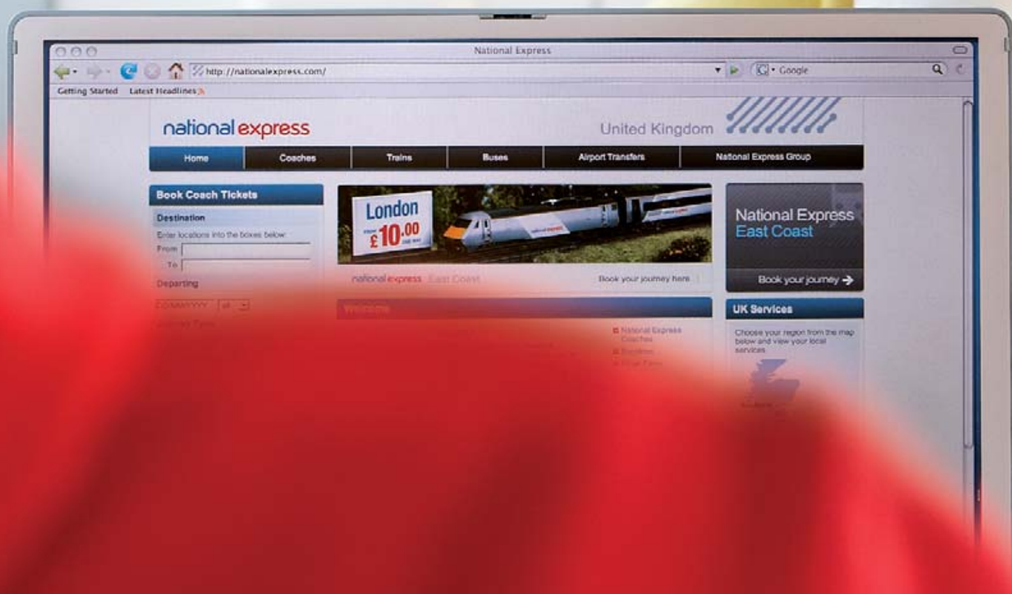
**National Express Group PLC**
Annual Report and Accounts 2007

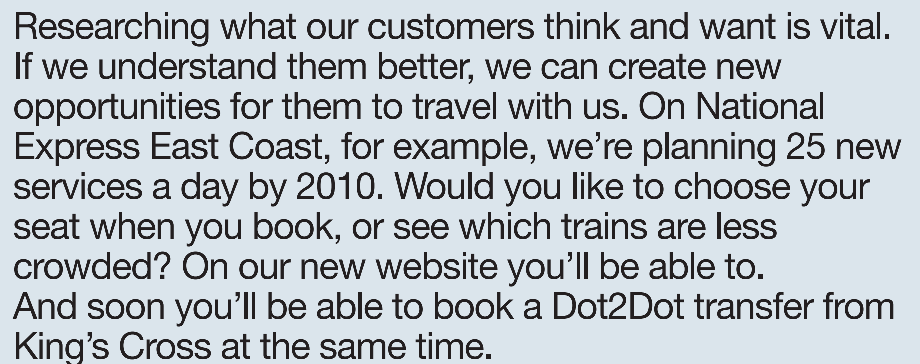
# Making travel simpler...

# ...by working as one



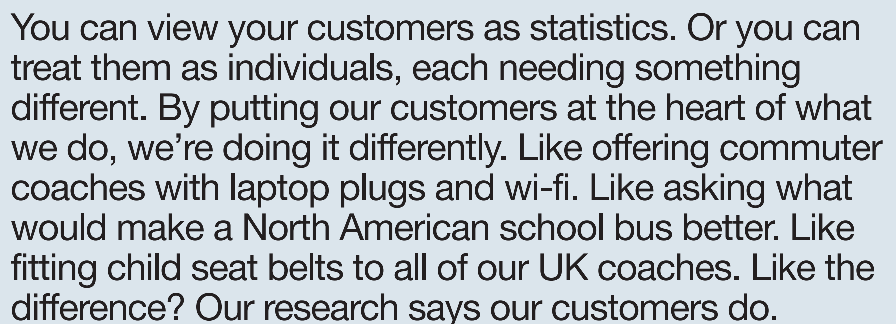
Four individual train businesses, four bus businesses, a coach operator and an airport transfer service, all in the UK. That’s the way we were. Now when we talk to a customer who wants to get from Gatwick to Glasgow or Norwich to Newcastle, we present a more joined-up approach. One organisation. One brand. One website. And one much happier customer.

# ...by creating new opportunities



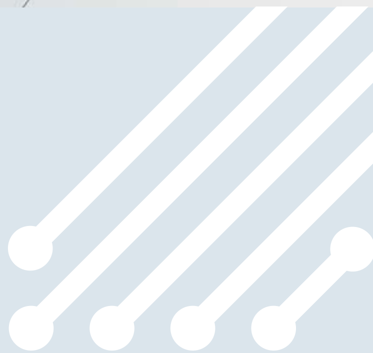
Researching what our customers think and want is vital. If we understand them better, we can create new opportunities for them to travel with us. On National Express East Coast, for example, we're planning 25 new services a day by 2010. Would you like to choose your seat when you book, or see which trains are less crowded? On our new website you'll be able to. And soon you'll be able to book a Dot2Dot transfer from King's Cross at the same time.

# ...by making customers our priority



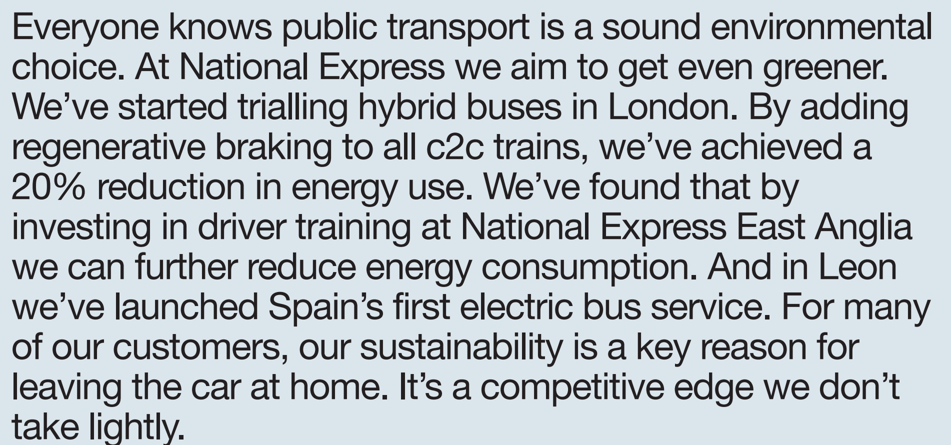
You can view your customers as statistics. Or you can treat them as individuals, each needing something different. By putting our customers at the heart of what we do, we're doing it differently. Like offering commuter coaches with laptop plugs and wi-fi. Like asking what would make a North American school bus better. Like fitting child seat belts to all of our UK coaches. Like the difference? Our research says our customers do.

# ...by working together



We're joining-up with other organisations to create more opportunities for our customers and our business. In partnership with the West Midlands transport authority, Centro, we've transformed six Birmingham bus routes. Result: 10% more customers within months on some routes, and plans for a much more far-reaching partnership. We're partnering with airlines and tour operators to make Dot2Dot transfers part of their service. And we've become transport partner for major event venues and organisers such as Twickenham and Wembley stadiums. Result!

# ...by protecting the future

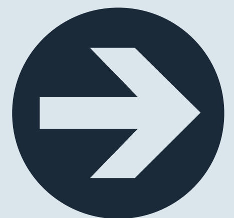


Everyone knows public transport is a sound environmental choice. At National Express we aim to get even greener. We've started trialling hybrid buses in London. By adding regenerative braking to all c2c trains, we've achieved a 20% reduction in energy use. We've found that by investing in driver training at National Express East Anglia we can further reduce energy consumption. And in Leon we've launched Spain's first electric bus service. For many of our customers, our sustainability is a key reason for leaving the car at home. It's a competitive edge we don't take lightly.

# Making our strategy work

**Contents**

6 Highlights
7 Chairman's Statement
10 Chief Executive's Review
14 Divisional Overview
16 Operating and Financial Review
Trains
Buses
Coaches
North America
Spain
28 Financial Review
34 Corporate Responsibility
36 Board of Directors and Company Secretary
38 Directors' Report
42 Corporate Governance Report
47 Directors' Remuneration Report
54 Independent Auditors' Report to the Members of National Express Group PLC
55 Group Primary Financial Statements
59 Notes to the Consolidated Accounts
105 Company Balance Sheet
106 Notes to the Company Accounts
114 Five Year Summary
115 Shareholder information
116 Dividends and Financial Calendar
Corporate Information
117 Glossary



# Highlights

- Results at the top end of market expectations
- Strong passenger growth in all divisions – 6% in trains, 3% in coaches, 2% in buses and 4% in Spain
- Completion of the acquisition of Continental Auto for £459.8 million (€659.3 million) to create Spain's leading coach and bus operator
- Award – with launch in December – of National Express East Coast franchise
- Restructuring of UK operations to form one division, releasing £11 million of annualised savings
- Record North American bid season and Business Transformation project on course
- Positive start to 2008
- Commitment to increase the Group's dividend by 10% per annum for the next three years reflecting the Board's confidence in the Group's future prospects

# Financial Highlights

Revenue
**£2.6bn**
(2006: £2.5bn)

Normalised operating profit*
**+11%**
to £205.6m (2006: £184.8m)

Normalised diluted earnings per share*
**+10%**
to 83.9p (2006: 76.5p)

Normalised profit before tax*
**+13%**
to £177.0m (2006: £156.1m)

Total dividend for the year per share
**37.96p**
(2006: 34.75p)

* Normalised results are the statutory results excluding the profit or loss on the sale of businesses, exceptional profit or loss on sale of non-current assets and charges for goodwill impairment, intangible asset amortisation, exceptional items and tax relief on qualifying exceptional items.

# Chairman's Statement

"We have announced a commitment to increase our dividend by 10% per annum for the next three years. This reflects the Board's confidence in the Group's future prospects."

**David Ross**
Chairman

**Results and dividend**
I am delighted to announce that we traded strongly throughout the year and that our results are at the top end of market expectations. All divisions provided a healthy contribution. We have delivered 10% earnings growth and increased the Group margin to 7.9%.

Revenue was £2.6 billion (2006: £2.5 billion) and normalised Group operating profit was £205.6 million (2006: £184.8 million). After interest and the Group's share of profits from associated undertakings, normalised profit before tax was £177.0 million (2006: £156.1 million). Normalised diluted earnings per share from continuing operations were 83.9 pence (2006: 76.5 pence).

We are recommending a final dividend of 26.4 pence per ordinary share (2006: 24.0 pence), an increase of 10%, to be paid on 9 May 2008 to shareholders on the register at 25 April 2008. Including the interim dividend, the proposed total dividend for the year is 37.96 pence (2006: 34.75 pence).

Based on the Board's confidence in the Group's prospects and the greater visibility of rail earnings following the completion of the recent round of rail franchising, we have announced a commitment to increase our dividend by 10% per annum for the next three years. This reflects the Board's confidence in the Group's future prospects.

**Safety**
Safety continues to be of paramount importance to us. During 2007 we saw two serious coach accidents, one tragically involving the loss of three lives. Our condolences and thoughts remain with those families affected. In our coach business, as with all our operations, our policy is one of continuous improvement in safety.

# Chairman's Statement continued

"Our Spanish bus and coach operations traded very well. Our acquisition of Continental Auto makes us the number one private operator of public transport services in Spain."

**Operations**
We have restructured our three UK divisions into a single UK business. This will enable us to put much greater focus on the needs of our customers and be more responsive to new opportunities. We are well on track to deliver the £11 million of annualised savings from this project and we are already seeing the benefits of a much more integrated approach to product and service design and delivery.

Our trains business has seen revenue growth of 11%. We believe the addition of National Express East Coast ("NXEC"), the UK's premier railway business, to our trains portfolio significantly strengthens our position in the key long distance market.

Our bus business delivered revenue growth of 7% and we are particularly pleased that the voluntary partnerships we have entered into with Centro in the West Midlands are already delivering strong passenger growth on some of these routes of up to 10%. We are already working on the next network of services, which we expect to launch in April this year.

Coach travel is the most environmentally friendly form of transport with the lowest carbon emissions of any motorised mode. Our coach business has had another outstanding year, both on core scheduled routes as well as on new products related to supporting events at major venues. Scheduled coach revenue growth has been 6%.

In North America, our Business Transformation project is on track and will deliver significant efficiencies and improved stability of earnings. This will make us the most efficient and competitive North American school bus operation, with a goal to attract those school boards yet to outsource their operations. We remain on course to offer school boards the best value and safest product in the market.

Our Spanish bus and coach operations traded well with passenger growth of 4%. Our acquisition of Continental Auto makes us the number one private operator of public transport services in Spain. Continental Auto's complementary set of geographical routes and business segments, especially commuter buses and urban transport, positions us very well for future growth and further market liberalisation – particularly in urban bus and rail. The acquisition of Continental Auto is the largest the Group has made to date and we are making good progress with the integration and are on track to deliver the benefits and returns we announced at the time of the acquisition.

It is clear that there is an opportunity to create value by developing closer relationships through greater communications with our UK customers. We have started to roll out our masterbrand strategy across all our UK operations enabling our customers to relate to the wide range of services that we offer, leveraging the greater awareness of the National Express brand. We have begun to address a broader range of opportunities to grow our top line including events related activities.

Other sales and marketing initiatives are also starting to show real success and growth. In 2007 we ran a series of marketing campaigns aimed purely at our rail customers. From a database of 150,000 customers we generated incremental profit of around £1 million representing a return on investment of 100%. In 2008 we will broaden this activity to NXEC, National Express East Anglia ("NXEA", formerly 'one' Railway) and coach customers, a combined database of over 2.3 million customers. In November our focus on improving the quality of our services was recognised when we won the business to business category at the UK Customer Service Experience Awards, which identify and recognise industry leaders in customer service. The award recognised the Group's efforts to increase customer satisfaction in every part of the business.

"We believe the addition of National Express East Coast, the UK's premier railway business, to our trains portfolio significantly strengthens our position in the key long distance market."

It is becoming clear that wider recognition of the environmental credentials of public transport over the car and the plane is contributing to the increased use of our services. Businesses, as well as consumers, are becoming more focused on reducing their carbon footprint for travel and we are developing a range of corporate products to encourage this.

With the changes in the Group's portfolio, I would like to thank all our people for their efforts to deliver an excellent set of results. I also welcome those new employees who have recently joined us and thank those who have left the Group during the year. It is down to the efforts and commitment of our people that we are able to further develop the Group and improve our customer offering in the markets where we operate.

**Board changes**
Following a further strengthening of the Board in October when Roger Devlin was appointed as a Non Executive Director, Sue Lyons retired in November after six years service as a Non Executive Director. On behalf of the Board I would like to thank Sue for her invaluable contribution particularly in her role as Chairman of the Safety Committee. In November Adam Walker, Group Finance Director, announced he would be leaving the Group after seven years. Adam was promoted to the Board back in 2003. He has made a significant contribution to the strategic development of the Group and overseen our entry into new markets such as Spain. Adam will be leaving the Group on 26 March and the Board wish him well in his next role. The recruitment process for a successor is well underway.

**Outlook and current trading**
Over the last year, National Express has undertaken significant change to deliver a more customer focused service culture, which has contributed to another year of passenger growth for the Group. Growing awareness of the positive environmental impact of public transport, and population growth within our core markets, continues to support long term growth trends within our operations.

The acquisition of Continental Auto and the award of the East Coast franchise in the final quarter of 2007 reinforced our strong market positions in the Spanish and UK markets. Our diversified portfolio of transport activity provides robust cash flow, market leading margins and significant opportunities for future growth. Despite the current economic backdrop, all operations have started the year well and we have seen no adverse impact on current trading.

Our new dividend policy underlines our commitment to delivering value for shareholders. We remain confident about the Group's prospects for the year ahead.

# Chief Executive's Review

**Making travel simpler**
A year ago, I described National Express as a business in great shape, but with even greater potential.

Our results for the past year confirm that we have begun to realise that potential, for the benefit of all our stakeholders. As we make further progress in implementing our strategy, customers will see the increasing difference it makes when a transport business becomes truly customer centred. Employees will be energised as the business moves emphatically onto the front foot. And investors will see how these changes fundamentally strengthen our ability to create value.

**Our strategy**
Too often, public transport is operationally focused rather than customer led. Passengers are seen in the abstract, rather than as individual consumers who make choices. This gives us an enormous opportunity to stand out in the marketplace and attract more customers by changing their perceptions of public transport. A company that understands and creates strong relationships with its customers will greatly enhance its value. So if we take the trouble to give people a service they want and will pay for, everyone can be a winner.

This ambition could not be more timely. The whole of society is rightly concerned about congestion, atmospheric pollution and, more than ever, global warming. Public transport is increasingly recognised as a crucial part of society's response to these challenges. So our social and commercial missions are wholly aligned. But only if people believe that travelling with us will actually improve their quality of life. Only if we can genuinely make travel simpler.

Our strategy for growing the business remains clear and simple:

- Reorient the Group around a more customer-driven, branded proposition
- Develop new products and services and grow organically
- Acquire businesses in markets where we can add value

We have been doing all these things in the past year, and will continue to do them. Our progress so far has convinced us that we are able to deliver this strategy, that it creates value, and that it gives us an edge over other businesses in our sector. Here's how:

"Our results for the past year confirm that we have begun to realise our potential, for the benefit of all our stakeholders."

**Richard Bowker**
Chief Executive

**One brand**
Customers tell us that getting from A to B has become increasingly complex over the years. We're focused on making it simpler. By branding all of our UK businesses under the National Express name we are making it easier for customers to recognise our services – whichever mode they travel on.

## Reorient the business around a more customer driven, branded proposition

If we are going to make travel simpler, we need to be a more joined-up organisation. We have taken the first step, which is to unite all our UK operations as a single division. Now, for the first time, we are able to think in terms of customers and their end-to-end journey requirements, rather than focusing on the operational requirements of this bus route or that train service.

A single, customer focused team is developing innovative ideas for new projects across all our transport modes. Instead of developing separate schemes for West Midlands bus smart cards, East Coast train smart cards and London's Oyster card, we will now be able to drive them all as a single project. When you're thinking about what customers actually want, working in an integrated way is both more exciting and more profitable.

This clear customer focus is reflected in a more coherent brand identity with clearly defined aims and values. The visible sign of this is the new National Express livery. It began appearing on our Dot2Dot vehicles and East Coast trains in 2007. Through the first half of 2008 it will also start to appear on coaches, buses, and our National Express East Anglia train franchise.

But the brand is not just a new paint job. It tells our customers that we are one business. Our common purpose is to improve the quality of life for all through travel. Our promise is to make travel simpler. We will be embedding our new values in the business, to inspire a change that customers will really notice. To ensure this change is felt across all areas of the business we are investing in training that will help our front line staff focus on our customers. Our 'First Level Leaders' training programme is helping them to lead the culture change that moves us from being operationally focused to living and breathing customer service.

We are putting increasing effort into knowing our customers through research and data capture – to better understand who they are, when and where they want to travel, what they want and don't want. This enables us to market more intelligently.

As we become a more joined-up business with an integrated customer base and brand, we are better placed to join forces with other powerful brands. Partnerships with venues such as the O2 Arena, Twickenham and Wembley Stadium mean people can book combined event and travel tickets. We are currently exploring other partnerships to broaden the offer we can make to customers.

We are also working to link our ticketing systems so that customers can book a single ticket for a journey that may involve several different National Express companies. This will take some time to complete. Last year we brought all our websites together behind a single portal – and the next step will be to introduce an integrated online booking engine. Ultimately, we want our web customers to be able to buy a single e-ticket (or m-ticket on their mobile phone) for their entire journey, which all our ticket systems will recognise.

# Chief Executive's Review continued

**Develop new products and services and grow organically**
In our UK Rail business there's no doubt that the prize of the year was East Coast, the UK's premier railway. There is a great deal we can do to improve its operating performance and offer customers a significantly more enjoyable experience. We have hit the ground running, with almost £50m to invest and a plan to do this fast so we get maximum impact over the life of the contract.

We are refurbishing trains and refining the timetable to make best use of existing resources until 2010, when we can bring in additional refurbished trains to add 25 new services a day. Then in 2012 we can start introducing the brand new Intercity Express trains currently being designed – so there will be exciting developments throughout the contract.

We expect great things from our new partnership with The Football Association and Wembley Stadium. Not just because Wembley is a world-class stadium with capacity for 90,000 people and parking for under 3,000 cars; but more widely because it will help us to raise our profile in the special events market, which is becoming an important part of our business. For example, as coach provider for Glastonbury in 2007, we had coaches leaving at an average of one every 3 minutes on the last day of the festival.

Alsa, our Spanish coach and bus operation, achieved passenger growth of 4% while maintaining our market leading margins. Like for like revenue growth continues to meet our expectations and we are encouraged by the increasing commercial opportunities that are emerging as the Spanish market liberalises.

In North America we had a very good bidding season, winning 14 new school bus contracts. Having sold Stewart Airport in October for US$78.5m we are totally focused on school buses. We are now the number two private operator, carrying a million students to school each day, in a market which is still 70% public sector operated. We are already positioned as a high quality operator with an outstanding offer in customer service and quality. Building on a record of steady 16-17% annual growth, our Business Transformation Programme is beginning to make full use of our scale and technology to offer unbeatable efficiency and value, while developing added-value services that will strongly differentiate us and provide potential new income streams.

As we understand more about people's travel needs, we are able to develop new businesses to satisfy them. Two examples in 2007 were the launches of our dedicated commuter coach services and Dot2Dot – our new airport transfer service.

The traditional downmarket image of coach travel is increasingly out of date. Many of today's coaches compare favourably with aircraft as a place to relax or work. And for sustainability they rate even better than trains. So we are seeking niches where we can attract people who would not normally consider booking a coach ticket.

A model, which has already proved successful in the US, is on-demand transport between airports and individual addresses in town centres. Our new Dot2Dot service, a high-quality, shared ride, linking Heathrow and Gatwick airports with Central London hotels, is designed to offer the convenience of a limo at half the price of a taxi.

Offering simple online booking, Dot2Dot has achieved extremely high customer satisfaction: in our first surveys, 91% said they would recommend it to others. But hotels are just the start, we have already extended the service to London's Canary Wharf, and as part of our joined-up thinking we plan to offer through tickets to Heathrow from East Coast stations, using Dot2Dot from King's Cross.

Another important niche is commuter travel. Last year we began piloting a commuter coach service from Milton Keynes to the Canary Wharf business district. We see coaches as a very viable alternative to rail for commuting: they are cheap and flexible, and allow rapid adjustments in capacity. In 2008 we plan to introduce further new commuter routes.

We are also planning to launch our first premium scheduled service, aimed specifically at business travellers into London. This will be comparable to the Supra premium services that Alsa launched in Spain last year. The new Supra coaches are equipped with leather seats, multi-channel video and audio,

**A clear focus**
We carry more than a million children to school every day. Our focus is on getting them there in safety and comfort.

**Our people**
Our people are at the heart of our business and we remain focused on their training and development. Inspiring our people in turn ensures we provide the best customer service for each of our customers.

laptop power sockets at every seat and, for the first time in Spain, onboard wi-fi. Supra passengers also have their own VIP lounges at a number of coach stations.

**Acquire businesses in markets where we can add value**
For both commuter coaches and Dot2Dot we used small acquisitions to build expertise and market presence more quickly.

To gain momentum in the commuter market we acquired the Kings Ferry Travel Group, which runs the largest and most successful commuter coach operation in London and the South East. And to help establish Dot2Dot we bought London's only comparable operation, Hotelink, which gave us a core business and desks in the airport terminals; we also negotiated the European rights to proven management software used successfully in 30 US cities by GO Airport Shuttle.

In Spain, by contrast, we made a very large acquisition that cements our position as the country's dominant player in coach travel by far. The £459.8m purchase of Continental Auto neatly dovetails with our existing Alsa operation, adding strength in south west and north east Spain to our existing weight in the south east and north west. We now have more than 2,100 coaches and buses in Spain, one of Europe's largest public transport markets. We see great potential for expanding the business, particularly in urban bus networks. And in the longer term there may also be opportunities to build on our UK experience in rail operations.

**The journey continues…**
We have come a long way in the past year, although there is still further to go. Integrating systems and changing cultures cannot be done overnight. But I am encouraged by our people's increasing eagerness to get there. Their enthusiasm for what we are doing, and their initiative in finding more customer centred ways of working, are building ever greater momentum for change. I thank them for what they've achieved so far, and look forward to what we will accomplish together in 2008.

Last year we benefited from favourable market conditions. The economic environment for transport was good, and, in particular, rail saw a boom in demand. This year will be tougher. But our experience convinces us that if we can continue to offer new and exciting ideas, we will go on attracting more customers despite any downturn.

We launched a lot of good ideas last year. This year we will feel the benefit as they gather momentum. We confidently expect to continue growing our business and the National Express brand as customers discover we really are making travel simpler for them.

"As we understand more about people's travel needs, we are able to develop new businesses to satisfy them. Two examples in 2007 were the launches of our dedicated commuter coach services and Dot2Dot – our new airport transfer service."

# Divisional Overview

## Trains

- c2c
- Gatwick Express
- National Express East Anglia
- National Express East Coast

## Buses

- National Express West Midlands
- National Express Coventry
- National Express Dundee
- National Express London
- National Express Midland Metro

## Coaches

- National Express Coaches
- Eurolines
- Airlinks
- National Express Dot2Dot
- Kings Ferry

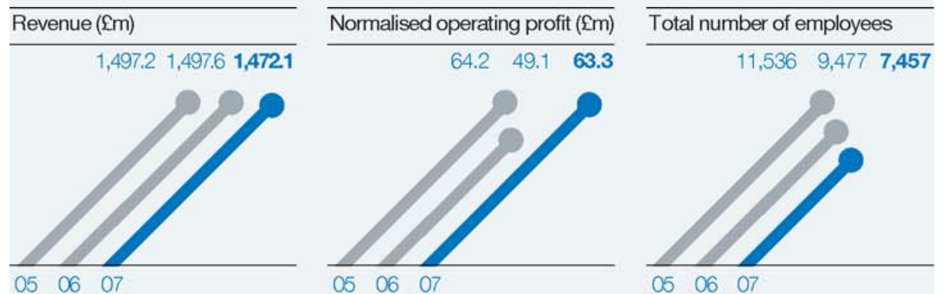
## North America

- Durham School Services
- Stock Transportation

## Spain

- Alsa
- Continental Auto

We operate c2c, Gatwick Express, National Express East Anglia including the Stansted Express, and National Express East Coast. We provide 218 million passenger journeys per year and employ 7,500 people.




We operate over 2,000 buses, providing approximately 390 million passenger journeys and employ 7,250 people in the West Midlands, Dundee and London. We also operate the Midland Metro, the light rail service in the West Midlands.

National Express coaches provide Britain's only scheduled national coach network and serve more than 1,000 destinations, providing approximately 19 million passenger journeys each year. Eurolines offers value for money European travel by coach. The division employs over 2,100 people. National Express Dot2Dot was launched in 2007 operating over 70 vehicles in the South East.

The North American division focuses on student transportation. It operates over 15,000 buses. The division employs over 19,000 people.

We are Spain's leading private operator of coach and bus services. The division provides nearly 144 million passenger journeys per annum and employs over 6,400 people.

# Operating and Financial Review

## Introduction

The Operating and Financial Review ("OFR") of National Express Group PLC describes the main trends and factors underlying the development, performance and strategy of National Express Group PLC during the year ended 31 December 2007, as well as the main trends and factors likely to affect our future development, performance and position.

Throughout the remainder of the Annual Report and Accounts, National Express Group PLC is referred to as "the Company" and the Group, of which it is the ultimate parent company, is referred to as "the Group".

## Group Strategy

The Group's objective is to generate shareholder value over the longer term, which we expect to achieve through three core strategies:

- Reorient the Group around a more customer-driven, branded proposition
- Develop new products and services, and grow organically
- Acquire businesses in markets where we can add value

These three strategies have been explained in more detail in the Chief Executive's Review on pages 10 to 13, together with a review of what has been accomplished in 2007.

## Stakeholder Relationships

The Group has a broad range of stakeholders who are key to the achievement of our business objectives.

Our external stakeholders range from those who award us contracts such as the Department for Transport, local authorities, transport bodies and school boards to our passengers who use our services each day. In addition there are numerous other stakeholders such as non government organisations, trade unions, suppliers and user groups with whom we have a constant dialogue. Our stakeholders are also internal with around 43,000 employees enabling us to deliver our products and services day in day out.

We engage with our stakeholders at a Group, divisional and local business level. During 2006 all of our UK businesses participated in this process mapping out accurately those stakeholders with whom we need to work to deliver our objectives. During 2007 we continued to develop stakeholder plans to support the business.

We communicate with our external stakeholders through a number of channels; open forums such as Meet the Manager sessions, customer magazines and websites. Our internal stakeholders engage with the business through a range of channels including conference calls, management conferences and magazines. As we believe in two way communication, we undertake surveys amongst our stakeholders, primarily customers and employees to gauge their satisfaction with our products and the degree of their engagement with the business.

## Resources

The Group has a range of resources that it uses to deliver its objectives and service its stakeholders.

Our Employees – The Group's most importance resource is its people. We believe there is a strong correlation between employee satisfaction and customer satisfaction, which means that our employees are vital to achieving the Group's objectives.

Our Brand – Market surveys consistently demonstrate that the National Express brand is the most recognised brand amongst the UK transport groups. It is a Superbrand and has received this accolade over a number of years. The strength of our brand has positioned us well to create a masterbrand which we started to roll out across our operations at the end of 2007. We believe focusing on one brand will provide greater clarity for our customers and cost efficiencies as well as focus within the business.

Our Customers – Every year, passengers make almost a billion journeys with us. From this interaction we have databases of customer contacts to whom we believe we could further market our products. We believe the Group has a significant opportunity to market itself, open new sales channels and achieve incremental sales.

Our Reputation – The Group has a strong reputation as a reliable operator across all its divisions. This reputation enables us to bid for contracts safe in the knowledge that we can deliver to meet customer expectations.

Our Expertise – Our reputation is backed up by first class operator knowledge which ensures we deliver a safe, reliable and excellent service. We are constantly reviewing ways to improve our performance.

Our Contracts – Our existing portfolio of contracts, including London Bus contracts, Trains franchises, North American school bus contracts, and in Spain long distance concessions and regional and urban contracts, provides assurance in those divisions over the delivery of shareholder value in the short and medium term.

**Description of the Business**
National Express Group is a leading transport group with operations in the UK, Spain and North America. On the back of the UK Integration process, we now operate three divisions, one for each of these geographies.

The following sections are intended to provide a description of each of our businesses as context for the Operational Review which follows. Narrative describing how the Group manages its operations is contained in the Corporate Governance Report.

**Trains**
Our Trains business operates a range of inter-city, commuter, rural and airport passenger train services under franchise agreements with DfT Rail. Franchises are awarded following a tender process managed by DfT Rail, in which applicants are required to prequalify for the main franchise bid process. Following a successful bid, the franchises generally last for a period of seven years, with the possibility of short term extensions.

Our National Express East Anglia franchise expires in March 2011, but will be extended to March 2014 if certain performance targets are achieved. Our National Express East Coast franchise started in December 2007 and ends in 2015. Our c2c franchise will finish in March 2011 and our Gatwick Express franchise will finish in June 2008. The next franchise tender process will be for the current Southern franchise, which will commence in 2008 with bids submitted in 2009. It is our intention to take part in this bid process.

Revenue is generated from the sale of tickets to passengers, with yield management techniques used to maximise revenue in off peak periods. Increases in certain ticket prices are regulated, with the increase linked to RPI. Other income is generated from areas such as catering services and car park income. In addition a significant amount of Government funding is received in certain franchises in the form of franchise support.

**Buses**
Our Bus operations provide high frequency urban bus services in the West Midlands, London and Dundee.

In the West Midlands and Dundee revenue is generated by the sale of tickets to our passengers. Fare increases are unregulated and we work in partnership with local authorities to grow the business.

In London we operate contracts for Transport for London (“TfL”), which specify frequencies and performance levels. We do not retain any of the revenue from ticket sales in London with all revenue passing to TfL. The contracts normally last for five years, with two year extensions. We are constantly bidding for new contracts and no one contract is material to the business.

The division also operates Midland Metro, the light rail service in the West Midlands, which generates revenue by the sale of tickets to passengers.

**Coaches**
Our Coach business operates a national integrated network of scheduled coach services under the National Express brand. This network operates to more than 1,000 destinations within the UK including all of the major UK airports. Revenue is primarily generated through ticket sales to passengers with yield management systems used to maximise revenue in off peak periods. Fare increases are unregulated. The majority of vehicles used by the business are contracted from third parties who employ the drivers.

There are a number of smaller businesses in this division. Our start-up operation National Express Dot2Dot generates revenue through ticket sales to customers travelling from central London to Heathrow and Gatwick Airports respectively. Eurolines generates revenue through ticket sales to customers travelling between the UK and Europe. National Express Rail Replacement and Airlinks operate coaching services under contracts with Train Operating Companies (TOCs) and coach services at Gatwick Airport respectively.

**North America**
Our North American Division is the second largest operator of private school bus services in the United States and Canada, operating over 15,000 buses. It operates from locations in 27 US states and 2 Canadian provinces.

We completed the disposal of Stewart Airport in October 2007, which enables our North American Division to be totally focused on student transportation. In this business we earn revenue by operating contracts on behalf of school boards to transport children from home to school with additional revenue earned from ad hoc field trip and vehicle charter activity.

The North American student market is highly fragmented. Local school boards operate around 350,000 vehicles in house, with the balance being operated by private companies.

**Spain**
In Spain we trade under the brand names of Alsa and Continental Auto. The combined business is Spain’s leading private operator of long distance and regional coach services and urban bus services.

The coach business operates 28 long distance coach concessions in Spain and international coach routes across Europe. The long distance concessions are granted on an exclusive basis by the national government for each route, with an average duration of 15 years. In addition, the business operates 91 regional coach concessions in Spain awarded by regional governments. In the coach businesses, revenue is principally generated by the sale of tickets to passengers, some of which are subject to regulated price increases.

In addition to its coach businesses, the division operates urban networks in 17 Spanish cities and outside of Spain in Porto and Marrakech and seven commuter concessions. Urban contracts are awarded by city councils and revenue is principally generated by the operation of these contracted services.

**Operational review**
**Group Results**
The Group’s objective is to generate shareholder value over the longer term. In the short term, we monitor the growth in Group profitability to ensure this is being achieved. The Key Performance Indicators (“KPIs”) for profitability are normalised operating profit, normalised profit before tax and normalised diluted earnings per share, which are calculated as per the notes to the accounts.

Operating and Financial Review

Trains

# Winning new contracts

Revenue for the year was £1,472.1 million (2006: £1,497.6 million) with normalised operating profit of £63.3 million (2006: £49.1 million). These results were ahead of expectations and reflect strong passenger growth throughout the year. There were excellent contributions from 'one' Railway, recently renamed National Express East Anglia, and Midland Mainline, reflecting the growth that can be achieved in long distance railways when performance levels are sustained. This is particularly encouraging given that National Express East Coast joined the Group in December 2007.

The reduction in revenue reflects the three franchises that left the Group in November: Central Trains, Midland Mainline and Silverlink. This also impacts the cash outflow from this business in 2007 and 2008.

We saw strong passenger growth of 6%. We believe that growth has been driven by a number of factors, including performance. Our franchises lead the way in the performance league tables with c2c and Gatwick Express at the top of the tables. c2c is the best performing railway in Britain and this continued high performance is attracting good levels of additional off peak business. At NXEA we have improved punctuality from 87.4% to over 90% – its best year for the franchise to date. This has been achieved by implementing joint performance improvement plans with Network Rail and managing their delivery.

During the year we incurred bid costs of £7.5 million (2006: £9.8 million). We were delighted to be awarded the premier East Coast franchise in August and started running the service on 9 December. This new franchise, which runs until 2015, will receive an investment of £44.0 million. We have made an immediate and positive impact in terms of customer service such as introducing free wi-fi internet access for all customers, not just first class and we are making the 100 day joint improvement plan with Network Rail, a top priority. We know from experience elsewhere that improving performance leads to more passengers travelling on our services. Further improvements will be introduced including real time running information accessible by mobile phone; print at home tickets; a website which will enable total journey booking including parking and onward connections in a single visit; and Smartcard ticketing. In addition more and faster services are scheduled from 2010, with the addition of five more trains to the fleet and a further 25 services providing 14,000 extra seats daily.

Another major contributor to our strong revenue performance has been our focus on yield management and pricing strategies. Our industry leading yield management capability at Midland Mainline enabled us to sell otherwise under-utilised capacity and this strategy has enabled us to maximise yield across a wide range of tickets and related services. We have brought all the technology and experience gathered around the Group to the NXEC franchise.

As agreed with the Department for Transport in April last year, Gatwick Express will leave our portfolio in June 2008 prior to the competition for the Southern franchise, which we will enter, being announced later in the year.

Revenue

£1,472.1m

(2006: £1,497.6m)

Normalised operating profit

£63.3m

(2006: £49.1m)

## New look
National Express East Coast and East Anglia now carry our new brand identity.

### Improving our performance
Punctuality at National Express East Anglia rose from 87.4% to almost 90% in 2007, making it the best year of the franchise so far. c2c was the best performing railway in the UK with a record-breaking 94.6% moving annual average.

### The extra mile
Gatwick Express regained its top score of 94% in the National Passenger Survey – the biggest independent survey of train travellers' views – making the rail-air link the country's most popular train company amongst passengers.

### Driving down energy use
National Express East Anglia introduced an energy efficient driver training programme and our c2c trains now use regenerative braking across the entire fleet.

Operating and Financial Review
Buses

# Working in partnership

Revenue
£322.3m
(2006: £300.8m)

Normalised operating profit
£43.5m
(2006: £40.7m)

Revenue for the year was £322.3 million (2006: £300.8 million) and normalised operating profit was £43.5 million (2006: £40.7 million). Profits have increased in our bus division for the first time since 2001 and margins have been maintained at 13.5%.

In order to stimulate growth and encourage customer loyalty and repeat journeys, we did not increase the price of a number of our travelcard products in 2007. We achieved 2% passenger growth in our deregulated services with increases in both concessionary and non concessionary passengers.

We were delighted to sign a ground breaking voluntary partnership with Centro to deliver improved performance and customer satisfaction on six key routes through Birmingham, Walsall and West Bromwich. We have set ourselves demanding targets and, despite only starting the first of the routes in November, we have already seen year on year passenger growth of up to 10% on these routes. These partnership routes provide more frequent services, improved infrastructure, new or refurbished vehicles with the latest CCTV systems and improvements to timetables and employee training. The success has given both the Group and Centro real confidence to develop further ambitious partnership schemes. A new jointly agreed network for Dudley, which covers approximately 40 routes, will be rolled out in April this year and it is intended that this will form the basis of a wider partnership scheme.

Our London operations account for a quarter of our overall bus revenues and we have been pleased to be awarded four new contracts during the period by TfL. In December we introduced five hybrid fuel vehicles into the Travel London fleet to operate on the 129 service between North Greenwich and the Cutty Sark in south east London. These vehicles use up to 40% less fuel. In mid February 2008 we received planning permission for the redevelopment of the Battersea bus depot in London which will see a doubling of capacity at this site.

Travel Dundee performed well in the period. It was awarded the 2007 Scottish Disability and Business Award in November for driver training on disability and its contribution to community work with a range of community groups in the city. This award followed Travel Dundee becoming the first UK based urban bus company to have 100% low-floor easy- access vehicles in 2004.

**Hybrid technology**
Bringing cutting-edge technology to London buses, we introduced five new hybrid buses to the 129 service in North Greenwich last December. Using up to 40% less fuel, the buses are four times cleaner than travelling by car and help minimise our Company's impact on the environment.

**Keeping costs low**
Passenger numbers grew by 2% in 2007, helped in part by an increased emphasis on understanding our consumer. This included measures such as freezing the cost of travelcards and making student and school travel cards available online for the first time.

**Working as one**
Three Premier routes across the West Midlands were developed as a result of a partnership with Centro. With high-back, soft leather seats, tinted windows, air-chill systems and the latest digital CCTV the new vehicles are part of a plan to increase bus patronage.

## National Express West Midlands

10% more passengers on key routes and further plans for growth.

# Operating and Financial Review
## Coaches

# New opportunities

**Reaching our goal**
Our network of coach services now take fans direct to Wembley from around the UK.

Revenue
**£231.0m**
(2006: £207.3m)

Normalised operating profit
**£23.1m**
(2006: £23.7m)

Revenue for the year was £231.0 million (2006: £207.3 million) with a normalised operating profit of £23.1 million (2006: £23.7 million). As expected for a start up business, National Express Dot2Dot incurred losses in 2007 of £4.8 million on revenue of £3.1 million. In the rest of our coaches business, we have grown our top line and increased our margin through segmentation of our product and enhanced yield management.

Coaches experienced an excellent trading year with passenger growth of 3%. This was achieved by the use of yield management, fare innovations and changes in our service offering. We have increased direct sales within the business with internet sales accounting for 35% of all transactions. We believe that greater use of self service ticket kiosks, which are now installed in the majority of our major coach stations, will continue to reduce our costs within the business. Our investment in our retail systems has enabled us to accelerate the roll-out of yield management across the network, with £1 funfares now offered on more than 50 popular routes.

We are continuing to grow our business around special events and venues where public transport is required and travel by private car is discouraged. This year we created a unique network offering customers direct coach services to Wembley Stadium to enable them to attend both sporting and music events. From the start of our association to the end of 2007 we carried 23,000 people to Wembley and expect that figure to grow as we add more routes. We have also developed similar arrangements with other venues such as the Millennium Stadium and Twickenham.

We believe that coach has a very strong role to play in Britain's future transport strategy and are encouraged by the increasing support we are receiving from Government and stakeholders around the country. We are responding to that support by developing and implementing a wide range of innovative products and services. In the summer we trialled a new commuter service operating between Milton Keynes and Canary Wharf in London. The service, which offers a direct and low cost alternative to rail travel, provides free wi-fi, seat back tables, electrical plugs, GPS tracking and leather seats. Customers are texted with up to date information about their services. The trial has gone extremely well and we are now rolling out this concept to other destinations where commuter flows exist.

We extended our knowledge of the commuter coach market through the acquisition of the Kings Ferry Travel Group in November. Kings Ferry is a well established Kent based coach operator providing popular commuter travel services in London and the South of England as well as providing a wide range of contract management services in the bus and coach sector.

During the year we became the first coach company to fit new child friendly areas, with child seat belts. Existing coaches were fitted with eight seats offering height adjustable seat belts for children and isofix fixings for child car seats. All new coaches will have these facilities provided.

The redevelopment and transformation of our main coach hub, Digbeth, in Birmingham is well underway. During the second half of the year we completed a seamless move to a new temporary site near Digbeth. The redevelopment is on schedule to be completed by early 2010.

In November we launched National Express Dot2Dot, a high quality, on demand, shared ride product, targeted primarily at the business to business market with significant capability for the business to consumer market as well. It currently has over 70 vehicles within its fleet. The start up of operations has gone well and customer satisfaction ratings are amongst the highest we have ever seen for any public transport type service.

**First Class transfers**
Connecting central London to Heathrow and Gatwick, Dot2Dot is our new airport transfer service for London. At half the price of a taxi, the service offers a cost-effective alternative for transferring between hotel and airport.

**Commuting by coach**
2007 saw our expansion into the commuter coach market, with the launch of a dedicated Milton Keynes to Canary Wharf service. This was followed by the acquisition of the Kings Ferry Travel Group.

**Safety on board**
National Express coaches now come with child-friendly areas as standard – a first for the coach market. All younger children can be carried in a child seat, and those aged four and above in a booster seat with comfort fit belt.

## Operating and Financial Review
## North America

# Keeping them safe

Revenue

£308.0m

(2006: £283.7m)

Normalised operating profit

£37.7m

(2006: £39.1m)

Revenue in the division for the year was £308.0 million (2006: £283.7 million) and normalised operating profit was £37.7 million (2006: £39.1 million). In local currency, revenue was US$617.5 million (2006: US$524.0 million) and normalised operating profit was US$75.5 million (2006: US$72.3 million). As previously announced, the expiry of a fuel hedge caused an increase in North America fuel costs of $13 million in 2007.

Following the successful sale of Stewart Airport in October, we are now focused on school bus provision. Our school bus operations performed well during the year despite the increasingly competitive landscape. Whilst 2006 had seen our best bidding season, 2007 surpassed this record with $38 million of new business being won and a retention rate of more than 95% of contracts. Following our entry into two new states, Tennessee and South Carolina, the division now operates in 27 states and two Canadian provinces. During the period we acquired three small bolt-on operations which were integrated into the business. We are currently seeing lower levels of business coming out to tender, partly because of the cycle of contracts coming up for expiry and also because the competitive landscape is going through a period of change. Even so, we are well placed to be successful in the bidding opportunities that arise.

Our Business Transformation initiative is focused on changing our business in order to create the highest margin and highest quality school bus business in North America. By fundamentally differentiating ourselves from others and with a focus on quality of service, we aim to compete more effectively, including being uniquely positioned to develop conversion opportunities. Business Transformation is about how to work smarter and more efficiently, how to respond to new competitors and look at creative ways to grow our business. We are also investing in systems and tools which meet the demands of our planned growth. During 2008, we will spend $31 million and expect net benefits to arise in 2009. Full year benefit will commence in 2010. To complement our Business Transformation we are formalising our environmental practices by creating an industry leading environmental strategy.

As with all our businesses, safety is our prime concern and we were delighted to see a further significant improvement in preventable accidents in 2007 from an already low base.

**Growing up**
North America experienced another strong bidding season in 2007 with more than $38 million in new business and a retention rate of over 95%.

**Transforming our business**
Our Business Transformation initiative will allow us to take advantage of our size whilst being flexible enough to offer a quality service that meets the needs of our customers, ensuring we compete in an evolving market place.

**Safety first**
Our newly created safety awards assign points to drivers who exceed safety performance standards. Designed to promote high standards of driving, the key to success lies in safety communication.

## Extending our reach

Following our entry into two new states, we now operate in 27 states and two Canadian provinces.

# Operating and Financial Review
## Spain

# Leading the way

**Driving forward**
2007 has seen us consolidate our position as the number one private transport operator in Spain.

Revenue
**£298.0m**
(2006: £249.3m)

Normalised operating profit
**£50.9m**
(2006: £44.3m)

Revenue was £298.0 million (2006: £249.3 million) and normalised operating profit was £50.9 million (2006: £44.3 million). In local currency revenue was €434.9 million (2006: €365.6 million) and normalised profit was €74.3 million (2006: €65.0 million). 2007 results include a three month contribution from Continental Auto. Trading improved in the second half of 2007 and we achieved a full year margin of 17.1%.

Following the successful acquisition of Continental Auto, we reinforced our position as the number one private transport operator in Spain. We believe that this positions us well to access new market opportunities in Spain as well as driving a more sales and marketing orientated agenda in our existing businesses. Continental Auto has a higher proportion of urban and commuter services which balance the long distance services – the largest part of Alsa. The integration of Continental Auto is proceeding to plan, both in terms of timing and synergies delivered, adjusting and optimising resources. We have already fully integrated our finance, sales and routing systems and implemented safety management and financial control procedures within Continental Auto. We are in the process of consolidating our maintenance facilities and the fleet purchasing process.

During 2007 we negotiated the extension of a number of contracts which now means we do not have any concessions expiring before 2013. Competition pressures exist within the market however and we have responded to the entry of low cost airlines and the development of high speed rail by varying our frequency, adapting our prices and altering our network to provide complementary services.

In addition we secured non regulated work outside the formal concessionary arrangements which we believe arises from having the scale of operations and the expertise to deliver on a timely and consistent basis.

We are developing our product offering in the market. In October we launched the new Supra class incorporating a revised on-board catering offering and wi-fi, being the first transport mode in Spain to incorporate this facility. In addition we launched a new loyalty card Bus Plus which provides benefits to our customers, and e-tickets were rolled out on long distance routes. We are also reviewing our overall distribution costs and are pleased that 15% of all sales for long distance and regional services are now via the internet.

With over 60% of the Spanish transport market represented by bus and coach, we believe there are plenty of opportunities for growth particularly in the urban bus market. We also believe that when future liberalisation of the public transport market in Spain occurs, we are well positioned to bring our experience and market presence to bear.

**Growth through acquisition**
Continental Auto was a key acquisition for the Group in 2007. Spain is one of the fastest growing European public transport markets and we are now in a unique position to participate in this growth.

**Business travel**
The launch of the new Supra class provides a business class of vehicle for travellers in Spain. Incorporating new high-spec vehicles, on-board catering and wi-fi, the coaches are setting the standard for how we develop our UK commuter coach services.

**Bus Plus**
In 2007 we launched the customer loyalty card Bus Plus, providing customer benefits, and e-tickets were rolled out on long distance routes.

# Operating and Financial Review

## Financial Review

### Year at a glance

We have continued our track record of delivering strong financial results. Profit before tax increased by 44.0% to £149.9m (2006: £104.1m), driven by a 14.6% increase in operating profit to £162.3m (2006: £141.6m). Basic earnings per share from continuing operations improved 39.4% to 73.6p (2006: 52.8p).

Our financial key performance indicators are based on normalised results, which we feel reflect the performance of the business more appropriately. Normalised results are defined as the statutory result before the following, as appropriate: profit or loss on the sale of businesses, exceptional profit or loss on the disposal of non-current assets and charges for goodwill impairment, intangible asset amortisation, exceptional items and tax relief thereon as appropriate.

Normalised group operating profit was up by 11.3% to £205.6m (2006: £184.8m), on revenue of £2,615.4m (2006: £2,525.5m) resulting in an increased operating margin of 7.9% (2006: 7.3%). Normalised profit before tax increased by 13.4% to £177.0m (2006: £156.1m), driving a 9.7% increase in normalised diluted earnings per share to 83.9p (2006: 76.5p).

Reflecting this earnings growth and the Board's confidence for its future prospects, the proposed final dividend per share will be increased by 10.0% to 26.40p (2006: 24.0p). This results in a full year dividend per share of 37.96p (2006: 34.75p), an increase of 9.2%.

Net debt increased by £472.4m to £910.8m (2006: £438.4m), with £481.9m of the increase resulting from our acquisition of Continental Auto in Spain.

### Divisional review

Commentary on the divisional results is included in the Operational Review above. Specific financial points to note are included below.

#### Trains

Revenue decreased 2% as a result of franchises leaving the Group. Normalising the result for franchise exits, revenue increased by 11%.

The business margin has improved to 4.3% (2006: 3.3%). The Central Trains, Silverlink and Midland Mainline franchises expired in November 2007, and as part of the DfT re-mapping exercise, Gatwick Express leaves the Group in June 2008. The settlement of working capital balances in respect of trains franchises that have finished will continue to result in operating cash outflows.

#### Coaches

The trading results for the start up business National Express Dot2Dot were in line with the business plan, with revenue of £3.1m resulting in an operating loss of £4.8m. This has been reported as part of the UK Coach results. Consequently on a like for like basis the Coach margins increase to 12.2% (2006: 11.4%).

#### Spain

In local currency, we generated normalised operating profit of €74.3m (2006: €65.0m) on revenue of €434.9m (2006: €365.6m). We are pleased to have maintained our margins above 17%.

The integration of Continental Auto into Alsa is a major project covering the systems for sales, vehicle maintenance and financial reporting. We started this project as soon as the sale completed in October and expect it to be completed by mid-2008. The valuation work on intangibles and key assets will be included in the 30 June 2008 balance sheet in accordance with IFRS 3, "Business Combinations".

### North America

In local currency, North America increased normalised operating profit to US$75.5m (2006: US$72.3m). Revenue has increased by 18% to US$617.5m (2006: US$524.0m).

As reported in last year's results, historic fuel hedges that were in place ended in 2006, which resulted in a US$13m increase in the cost base in 2007. This resulted in a lower margin of 12.2% (2006: 13.8%).

Following the Group's announcement of the planned sale of the operating lease on Stewart International Airport, the assets and related liabilities of the disposal group were separately identified in the 2006 balance sheet, in accordance with IFRS 5, 'Non-current assets held for sale and discontinued operations'. The business did not meet the definition of a discontinued operation, therefore the results, which do not make a significant contribution, are included within continuing operations in 2007 and 2006.

### Fuel

We use fuel swaps to hedge short term movements in the fuel price. These swaps cover a number of different positions including ultra-low sulfur diesel (ULSD) and gasoil in the UK, heating oil in North America and Euro denominated ULSD in Spain. For 2008 and 2009 we have hedged 58% and 31% of our volumes respectively.

### Joint ventures and Associates

The Group has a number of associates and joint ventures in Spain and holds a 40% investment in Inter-Capital and Regional Rail Limited ("ICRRL").

The results of the associates and joint ventures in Spain were a profit of £0.6m (2006: £0.2m) and a loss of £0.2m (2006: £0.2m loss) respectively.

The Group's Eurostar contract with ICRRL was designated an onerous contract in 2006. As a result there is no charge to the income statement in 2007, but in 2006 the total charge was £29.6m, comprising our share of the ICRRL result of £3.9m and a £25.7m exceptional charge for the onerous contract. We have provided for the Eurostar losses to the end of the contract in 2010.

### Finance cost

Net finance costs increased to £29.0m (2006: £24.9m), reflecting the £481.9m increase in net debt following the acquisition of Continental Auto in October 2007.

Included in the net finance cost is a £3.0m (2006: £2.1m) charge to unwind the discounting on provisions, most notably the ICRRL onerous contract. Adjusting for the discounting charge and comparing to normalised operating profit before depreciation and other non-cash items ("EBITDA") of £282.9m (2006: £264.0m), the EBITDA finance cover was 10.9 times (2006: 11.6 times).

### Amortisation of Intangible assets

Amortisation of £27.5m (2006: £27.8m) was charged on the intangible asset that arises from the Group's right to operate its rail franchises £1.1m (2006: £1.6m) and on contracts acquired in Alsa £20.2m (2006: £20.1m), UK Bus £1.1m (2006: £1.6m) and North America £5.1m (2006: £4.5m).

### Exceptional items

Exceptional charges totalled £15.8m, incurred on the Business Transformation program in North America (£8.2m), UK integration program (£4.2m), the Continental Auto integration (£2.6m) and the NXEC franchise mobilisation (£0.8m).

In 2006, exceptional items totalled a net income of £4.8m, comprising a credit of £6.7m in relation to defined benefit pension liabilities and charges of £1.9m in relation to the integration of Alsa.

The £16.2m profit on disposal of non-current assets arises from the sale of the operating lease on Stewart International Airport in October 2007. The £16.9m profit in 2006 resulted from the disposal of a 14% shareholding in Trainline Holdings Limited (£9.4m) and the disposal of a car park in Sheffield (£7.5m).

### Taxation

The total tax charge of £37.6m (2006: £23.6m) on profit before tax of £149.9m (2006: £104.1m) represents an effective rate of 25.1% (2006: 22.7%).

The tax charge on normalised profit of £177.0m (2006: £156.1m) was £48.1m (2006: £39.2m), which represents an effective rate of 27.2% (2006: 25.1%). Reductions in jurisdictional tax rates mean that the expected tax rate on normalised profit before tax decreased by 1.0% to 31.3%. However, the effective tax rate has increased by 2.1% to 27.2% due to the expiry of certain tax efficient financing arrangements.

The total tax charge includes a tax credit on exceptional items of £10.5m (2006: £15.6m) which includes the deferred tax benefit of the Group's non-deductible intangible asset amortisation.

### Discontinued operations

An additional provision of £6.3m was recognised in relation to the Group's Public Transit business which was disposed of in 2005. The Group provided an indemnity to the purchaser at the time of the disposal regarding an industry employment issue in California. The issue is close to resolution and this charge reflects the Directors' best estimate of the Group's liability. The charge of £2.9m on the face of the income statement comprises £6.3m of additional liabilities in relation to the disposed operations, offset by a tax credit of £3.4m.

# Operating and Financial Review

## Financial Review continued

### Cash flow

The Group continues to generate strong cash flow with normalised operating profit of £205.6m (2006: £184.8m) converted into operating cash flow before one-offs of £196.7m (2006: £209.7m). Net cash inflow from operations of £300.6m (2006: £297.1m) is then used to maintain high levels of investment across the Group, particularly in North America where capital expenditure is required for contract wins. The Group's operating cash flow by Division is set out in table 1.

The working capital outflow in UK Bus comprises payments to the defined benefit pension schemes in excess of the income statement charge and the losses associated with the onerous contracts in our London business. The working capital inflow in UK Trains arises from a number of items including working capital phasing and non-cash charges at NXEC incurred in the franchise entry. The working capital outflow in Central functions arises from the reversal of prior year working capital inflows and the settlement of foreign currency swaps.

Net capital expenditure was £103.9m (2006: £87.4m) including £0.2m (2006: £20.7m) of additions purchased under finance leases and £15.4m (2006: £6.8m) of proceeds from disposals.

The net operating cash outflow in respect of TOC franchise entry and exits was £31.9m (2006: £27.7m) comprising cash flows in respect of working capital and property, plant and equipment.

### Net debt

The Group's reconciliation of net debt is set out in table 2. Payments to associates of £8.4m (2006: £8.4m) represent the annual outflow in respect of the ICRRL onerous contract. In 2007 £10.7m was received on the redemption of preference shares following the completion of the Channel Tunnel Rail Link.

Net interest paid of £23.4m (2006: £20.6m) comprises the cash outflow of £22.5m (2006: £19.7m) adjusted for loan fee amortisation of £0.9m (2006: £0.9m). The increase in interest paid follows the acquisition of Continental Auto in October 2007.

As disclosed last year, the 2006 tax payments were reduced by the receipt of tax rebates in respect of prior years.

Acquisitions and disposals in the year increased net debt by £482.1m, principally due to the £481.9m increase resulting from the acquisition of Continental Auto. Three bolt-on acquisitions in North America and the acquisition of the Kings Ferry Travel Group and Hotelink in the UK were funded by the disposal of Stewart Airport in North America.

Movements in foreign currency exchange rates increased net debt by £55.4m principally due to the strengthening of the Euro. The increase in net debt due to exchange is hedged by a corresponding increase in our net investment in Euro denominated assets.

### Table 1: Operating Cash Flow

| | UK Bus £m | UK Coach £m | UK Trains £m | North American Bus £m | Europe £m | Central functions £m | Total £m |
|---|---|---|---|---|---|---|---|
| Normalised operating profit | 43.5 | 23.1 | 63.3 | 37.7 | 50.9 | (12.9) | 205.6 |
| Depreciation | 17.0 | 4.8 | 15.9 | 25.9 | 15.4 | 0.6 | 79.6 |
| Amortisation of leasehold property prepayment | 0.1 | – | – | – | – | – | 0.1 |
| Amortisation of fixed asset grants | (0.1) | – | (0.8) | – | (0.4) | – | (1.3) |
| Profit on disposal | 0.1 | (0.2) | (2.8) | (0.6) | (0.8) | – | (4.3) |
| Share based payments | 0.3 | 0.2 | 0.6 | 0.4 | 0.2 | 1.5 | 3.2 |
| **EBITDA** | **60.9** | **27.9** | **76.2** | **63.4** | **65.3** | **(10.8)** | **282.9** |
| Working capital movement | (9.5) | (0.1) | 43.1 | (3.6) | 1.5 | (13.7) | 17.7 |
| **Net cash inflow from operations** | **51.4** | **27.8** | **119.3** | **59.8** | **66.8** | **(24.5)** | **300.6** |
| Net capital expenditure | (22.3) | (9.6) | (6.1) | (45.1) | (20.3) | (0.5) | (103.9) |
| **Operating cash flow before one-offs** | **29.1** | **18.2** | **113.2** | **14.7** | **46.5** | **(25.0)** | **196.7** |
| UK Train franchise entry and exits | | | | | | | (31.9) |
| **Operating cash flow** | | | | | | | **164.8** |

Operating cash flow is intended to be the cash flow equivalent to normalised operating profit. To reconcile the operating cash flow to the statutory cash flow the following items are included: "Cash generated from operations" plus "Proceeds from disposal of property, plant and equipment" less "Finance lease additions" and "Purchase of property, plant and equipment" as set out in note 38 and the cash flow statement. The non-operating items are then excluded which comprise £8.4m payment to associates and £11.3m payments in relation to other exceptional items.

## Dividend

A final dividend of 26.40p per share will be paid in May 2008, bringing the total dividend for the year to 37.96p. This is a 9.2% increase in total dividends declared compared to 2006 reflecting the 9.7% increase in normalised diluted earnings per share. This dividend is covered 2.2 times (2006: 2.2 times) by normalised profits after tax.

In light of the consistent nature of our rail portfolio for the medium term and based on the Board's confidence in the Group's future prospects, it is proposed to announce a three year commitment on dividend growth of 10% per annum.

## Financial position

The Group looks to adopt efficient financing structures that enable it to use its balance sheet strength to achieve the Group's objectives without putting shareholder value at risk. The Group's balance sheet is set out in table 3.

The Group's capital structure comprises its equity and its net debt. During 2007, the Group issued 792,659 shares to meet obligations under its employee share schemes, for consideration of £5.5m. The increase in the Group's net debt from £438.4m to £910.8m is explained in the Finance Review above. The Group's principal gearing ratio is net debt to EBITDA. At 31 December 2007, based on the reported EBITDA of £282.9 (2006: £264.0m) and net debt of £910.8m (2006: 438.4m) the ratio was 3.2 (2006: 1.7) with the increase driven by the acquisition of Continental Auto.

The Group's treasury objective is to manage the risk for potential loss of shareholder value from certain financial risks. The Group's financial risk management objectives and policies are described in more detail in note 30 to the Annual Report and Accounts.

## Liquidity

At 31 December 2007, the Group had two bank debt facilities: an £800 million revolving credit facility maturing in June 2011 and a €500m term loan facility expiring in April 2008. At 31 December 2007, the headroom under the facilities was £199.4m (2006: £247.8m). The Group has complied with all of its banking covenants in the year. Since year end we have replaced the €500m term loan facility with a €540m term loan facility expiring in February 2009 with a one year extension to February 2010 at the Group's option.

### Table 2: Reconciliation of net debt

| | 2007 £m | 2006 £m |
|---|---|---|
| Operating cash flow | **164.8** | 182.0 |
| Exceptional cash flow | **(11.3)** | (2.0) |
| Exceptional property proceeds | **–** | 13.0 |
| Payments to associates | **(8.4)** | (8.4) |
| Receipt in respect of investments | **10.7** | – |
| Net interest | **(23.4)** | (20.6) |
| Dividends paid to minority interests | **(0.1)** | – |
| Taxation | **(18.8)** | (9.0) |
| **Free cash flow** | **113.5** | 155.0 |
| Share buy back | **–** | (11.6) |
| Financial investments & shares | **5.5** | 15.8 |
| Acquisitions and disposals | **(482.1)** | (16.8) |
| Dividends | **(53.9)** | (49.7) |
| **Net funds flow** | **(417.0)** | 92.7 |
| Foreign exchange | **(55.4)** | 32.3 |
| Funds flow post exchange | **(472.4)** | 125.0 |
| Opening net debt | **(438.4)** | (563.4) |
| **Closing net debt** | **(910.8)** | (438.4) |

### Table 3: Balance sheet

| | 2007 £m | 2006 £m |
|---|---|---|
| Intangible assets | **1,173.9** | 697.6 |
| Property, plant and equipment | **678.7** | 501.9 |
| Other non-current assets | **34.3** | 37.2 |
| Current assets excluding cash | **311.9** | 322.3 |
| Net debt | **(910.8)** | (438.4) |
| Non-current liabilities excluding borrowings | **(186.4)** | (209.7) |
| Current liabilities excluding borrowings | **(660.5)** | (583.1) |
| Disposal group net assets | **–** | 17.7 |
| Net assets | **441.1** | 345.5 |

As explained in note 23 to the Annual Report and Accounts, the Group's net debt includes cash balances totalling £55.2m (2006: £33.5m) which cannot be withdrawn from our TOCs. This is because the franchise agreements with the DfT restrict the withdrawal of cash to ensure a TOC is able to meet its working capital requirements. Cash can only be withdrawn by loan or dividend to the extent that certain financial ratios are complied with.

## Pensions

The Group's principal defined benefit pension schemes are all in the UK.

There are two Bus schemes, the West Midlands Passenger Transport Authority Pension Fund and Tayside Transport Superannuation Fund which have 1,078 and 120 active members respectively. Both schemes have been closed for some years. The National Express Group Staff Pension Plan has 286 active members predominantly from Coaches, and it was closed to new members in June 2002. New employees in Buses and Coaches are offered membership of a defined contribution pension scheme. In the Trains business approximately 6,200 employees are active members of the Railways Pension Scheme ("RPS").

The balance sheet includes provision for the deficits of the defined benefit schemes in the Group. For the RPS, our main obligation is to pay the contributions agreed with the scheme actuary over the life of our train franchise. The IAS 19 deficits have decreased as a result of the strong return on scheme assets in recent years coupled with higher discount rates used to value the scheme's obligations. In the Coach scheme the deficit decreased to £4.9m (2006: £12.7m). In the Bus schemes the deficit has decreased to £5.1m (2006: £17.3m) and the RPS deficit decreased to £18.8m (2006: £21.1m).

# Operating and Financial Review
## Financial Review

### Principal risks and uncertainties
In addition to the opportunities we have to grow and develop our business, the Group faces a range of risks and uncertainties as part of both its day to day operations and its corporate activities. The processes that the Board has established to safeguard both shareholder value and the assets of the Group are described in the Corporate Governance Report.

The narrative below describes those specific risks and uncertainties that the Directors believe could have the most significant impact on the Group's long term value generation. The risks and uncertainties described below are not intended to be an exhaustive list.

### Risks inherent in bidding for contracts
One of the principal methods of increasing shareholder value is winning new contracts. Inherent in bidding for new contracts is a risk that assumptions are made in the bid model that turn out to be undeliverable for any number of reasons. To take a Trains bid as an example, if underlying economic growth falls short of the growth assumed in the bid, the passenger revenue target may not be achievable.

Additionally, when a business is based on winning contracts, there is a requirement for the business to win a minimum number of contracts to retain its existing scale of operations. If that minimum number is not achieved, that division's revenue and profits would be affected.

The business most exposed to this risk is Trains, where a robust process is followed to ensure that all bids are subject to sufficient challenge. In addition, Buses, North America and Spain bid for contracts on a regular basis, but no one contract is material to those businesses.

### Competition
With the exception of North America, our businesses are competing with alternative modes of transportation, primarily the car. Our Coaches, Trains and Spain businesses face competition from a mix of long distance coaches, trains, low-cost airlines and the car. The principal alternative to our Buses business is the car, and with the cost of owning and operating a car at an all time low, it remains imperative to create a more positive customer proposition on our services.

In addition to modal competition, the competitive environment between transport companies remains intense. This is seen both in competition for passengers and when bidding for contracts.

It is important we differentiate ourselves in the marketplace and a number of the initiatives explained in the Chief Executive's statement set out our progress in this area.

### Energy costs
All of our businesses incur energy costs to power their transport operations with Buses, Coaches, Spain and North America exclusively using diesel, and Trains using either gasoil or electricity. All energy prices are subject to significant changes driven by international economic and political factors. In recent years, weather patterns such as mild or cold winters and hurricanes have also had an effect on energy prices.

We seek to limit the effect diesel and gasoil costs have on our year on year profitability through a risk management programme using fuel price swaps. In Trains we have negotiated with Network Rail to reach a new agreement on electricity pricing.

**Political and regulatory changes**
Our businesses are subject to varying degrees of regulation and as such, there is a risk that political and regulatory changes could impact their future prospects. In recent times, the highest profile political and regulatory uncertainty is around the Buses business where the debate around quality partnerships and quality contracts continues through the Local Transport Bill.

To mitigate the risk from political and regulatory changes, the Group looks to service the needs of its stakeholders and lobbies national, regional and local government in addition to passenger, employee and environmental bodies.

**Labour costs**
Our aim to offer high quality services is dependent on recruiting and retaining the right calibre of employees. For each of our businesses, local economic prosperity, employment levels and our image as an employer affect our ability to deliver this aim. Additionally, we incur significant other employee staff costs such as recruitment and training.

Staff costs are the largest single component of the Group's operating costs. We seek to mitigate this risk by securing competitive wage deals that maintain the profitability of our businesses.

**Major incidents**
Safety is an inherent feature of transporting people. We take our safety responsibilities very seriously however there is a risk that any incidents that the Group is involved in, directly or indirectly, could result in injury to our passengers or employees. The potential impact on the Group is wide ranging and includes possible damage to our reputation with passengers, financial loss from claims for damages and our ability to bid successfully for contracts.

To mitigate this risk, the Board operates a Safety and Environment Committee which reviews the Group's safety practices, procedures and record as described in the Corporate Governance Report. For our staff, this translates itself into our culture of operational excellence that seeks to ensure the safety of all our passengers.

The cost of damages claims is managed through the Group's risk management processes. The current policy is to self-insure high frequency claims with the businesses and then provide protection above these types of losses by purchasing insurance cover from a selection of proven and financially strong insurers. A risk remains that the number or size of the self-insured claims could be higher than expected.

**Economic conditions**
Changes in economic conditions have an effect on the ability of our customers to pay for our services. For example, the Trains division's historic growth has been closely correlated to the growth in the overall UK economy.

We look to mitigate this risk by closely monitoring the affordability of our services and varying the cost where appropriate and possible.

**Organisational change**
The number of significant organisational change initiatives in the business at the present time is higher than usual, including UK integration, North America Business Transformation, Continental Auto integration and NXEC franchise start up. As with any organisational change, risks are created.

These risks are being actively managed by the Group leadership team through robust management processes and close monitoring of the businesses where change is occurring.

**Corporate Responsibility**
National Express Group's commitment to corporate responsibility is at the heart of the Group and it is very much integral to the operations that we run. This has been explained in more detail on pages 34 to 35, together with a review of what has been accomplished in 2007.

**Understanding the OFR Statement of Compliance**
The 2007 OFR is intended to meet many of the requirements of the statutory OFR as laid out in the Accounting Standards Board's 'Reporting Statement of Best Practice on the OFR'. This ensures compliance with the legal requirement under the Companies Act to provide a Business Review and is referenced from the Director's Report.

We note that this is the second year that UK companies have been required to produce a Business Review and therefore best practice is still emerging. We will continue to review the narrative disclosure we provide in the Annual Report and Accounts to ensure that the disclosures provided meet the requirements of our stakeholders.

**Cautionary Statement**
The OFR is intended to focus on matters that are relevant to the interests of the shareholders of the Company. The purpose of the OFR is to assist the shareholders of the Company in assessing the strategies adopted by the Company and the potential for those strategies to succeed. It should not be relied on by any other party or for any other purpose.

Where this OFR contains forward-looking statements, these are made by the Directors in good faith based on the information available to them at the time of their approval of this report. Shareholders will understand that these statements should be treated with caution due to the inherent uncertainties underlying any such forward-looking information.

# Operating and Financial Review

## Corporate Responsibility

At National Express Group corporate responsibility is a fundamental part of our business – it's about what we do and how we do it. We know that public transport has a central role to play in improving the quality of people's lives. Our challenge is to effectively communicate the contribution that our services can make to society, in both social and environmental terms.

We report more widely on our corporate responsibility initiatives in our Corporate Responsibility report. In 2007 we were once again included in the Dow Jones Sustainability and the FTSE4Good indices. And in August 2007 we were listed in The Observer newspaper as one of the 20 best firms in the FTSE 350 index, assessed on a range of social, environmental and corporate governance criteria.

**A key part of our communities**
Our business and our brands are an integral part of the fabric of everyday life. Connecting with our communities is key and each part of our business is empowered to do this on a local level.

Much of our community support comes in the shape of initiatives close to the hearts of our people and our customers. In North America we continue our support of the Special Olympics with employees across the division volunteering for events across California, Texas and Illinois. In Spain we signed a €400,000 partnership with UNICEF to support the promotion of breastfeeding in Morocco, a country in which Alsa is a transport provider. Alsa is also the sponsor of the fifth Solidarity and Immigration Mundialito (Little World Cup) which brings together over 700 people from 25 countries with the aim of promoting solidarity through sport. In the UK we became sponsors of The Football Association, providing unique opportunities for our people to engage with the games and players that are such a part of the landscape of life in the UK.

**Working together to create change**
The climate change debate has moved on apace in 2007. Our focus has been on communicating the large net environmental savings to be made from customers using our services instead of car and plane. We launched an online carbon calculator to highlight the carbon savings made by individual journeys and will continue to develop initiatives that promote this message throughout 2008.

We continued our partnership in the Climate Group's 'We're in This Together Campaign', which helps consumers find ways to reduce their carbon footprint. As part of this, in Summer 2007, we ran competitions to win tickets to Live Earth, when our customers told us their pledge to reduce their carbon footprint. As official transport providers to Wembley Stadium we provide services from 57 destinations around the UK to each match, significantly reducing the numbers of car journeys to the stadium. In addition we are a key partner in the Carbonfootyprint.com campaign providing free coach travel to all FA Cup matches from the Third Round onwards, with the aim of reducing the environmental impact of the competition.

**Continuous improvement**
We are also working to reduce our own energy and carbon emissions where we can. In our bus business we started a trial of hybrid buses at Travel London – operating on the 129 route from the Cutty Sark to North Greenwich whilst in Leon, North Central Spain we launched the country's first electric minibus. At National Express East Anglia, through train modifications and the launch of train simulators, which promote energy-efficient driving, we have seen significant drops in energy use. And the entire c2c fleet of trains now uses regenerative braking which has reduced energy use by around 20%. Some of our most ambitious plans for energy reduction come as part of the new National Express East Coast franchise. Over the length of the franchise we plan a 28% reduction in CO2 per passenger kilometre.

We've continued to make improvements at our sites with National Express West Midlands garages reducing their energy use by around 40% and train depots by around 25% in the last three years. We also plan to create a number of green initiatives and invest in onsite renewable energy. As a complement to this in our UK business we switched to "green tariff" electricity so all our site and depot energy in the UK now comes from renewable sources. The contract also provides electricity for the Midland Metro in the West Midlands, resulting in the line becoming the first light rail system in the UK to be effectively emissions free.

**Keeping safety front of mind**
Safety is at the core of our business and we are focused on ensuring that our safety record improves across our operations. 2007 saw two accidents, one involving the tragic loss of three lives. Our thoughts remain with those affected by these incidents. We remain commited to our policy of continuous improvement in safety. In Spain we have invested in driver training with a resulting 15% drop in incidents. Improvements were also recorded in North America, due in part to the second year of the division's safety awards which focus on keeping safety at the forefront of every driver's mind and rewarding drivers who exceed the safety performance standards. In our UK train operations, the rate of signals passed at danger (SPADs) has improved by 16%, and currently stands at its lowest level ever.

**Our business, our people**
The safety and development of our people remains a fundamental part of our success as a business and we ensure that we provide support to them at every level. We continued our 'First Level Leaders' programme which provides managers with the necessary training to help them develop their potential. Engagement with our people is key and we ensure that our communication with each employee is central to everything we do. Our Employee Survey is crucial in gathering their thoughts and views and we ensure that these are not only listened to, but acted on.

We will continue to explore ideas to tackle the issues facing our business and society. Only by listening to our people, our customers and stakeholders can we truly ensure we are making travel simpler.

**Green electricity**
Switching our UK business to a "green tariff" electricity means all our site and depot energy now comes from renewable sources. It also means that Midland Metro, the light rail system in the West Midlands, is effectively emissions free.

**Safety first**
When it comes to safety, driver training is key. We continue to invest in the technology and training programmes to keep our people and passengers protected.

**Encouraging change**
Educating people about the environmental benefits of using public transport is one of our primary roles in reducing the effects of climate change.

# Board of Directors and Company Secretary

1

2

3

4

5

6

7

8

9

10

1 David Ross
Chairman

2 Richard Bowker CBE
Chief Executive

3 Adam Walker
Finance Director

4 Ray O'Toole
Chief Executive UK Division

5 Sir Andrew Foster
Non Executive Director

6 Barry Gibson
Non Executive Director

7 Roger Devlin
Non Executive Director

8 Jorge Cosmen
Non Executive Director

9 Tim Score
Non Executive Director

10 Tony McDonald
Company Secretary

**1 David Ross**
Chairman *ƒ
David Ross joined the Board in February 2001 as a Non Executive Director and became Chairman in May 2004. In 1991 he founded and is currently Non Executive Deputy Chairman of The Carphone Warehouse Group PLC. He is a Non Executive Director of Big Yellow Group PLC and Cosalt PLC and is a Board Member of the Olympic Lottery Distributor. In 2006 he was appointed a Trustee of the National Portrait Gallery and is the main sponsor for Havelock Academy in Grimsby. David is a chartered accountant. Aged 42.

**2 Richard Bowker CBE**
Chief Executive
Richard Bowker was appointed to the Board as Chief Executive in September 2006. He was formerly Chief Executive of Partnerships for Schools ("PfS"), a government body responsible for delivering the Building Schools for the Future Investment Programme. Between December 2001 and September 2004 he was Chairman and Chief Executive of the Strategic Rail Authority. Prior to that he was Group Commercial Director of Virgin Group and Co-chairman of Virgin Rail. Richard is a chartered management accountant and a Non Executive Director of British Waterways. Aged 42.

**3 Adam Walker**
Finance Director
Adam Walker joined the Board in March 2003, as Finance Director. He joined the Group in October 2001 as Corporate Development Director working closely with the Group's operational subsidiaries on developing their financial strategies. Prior to joining the Group he was Director of Corporate Finance at Arthur Andersen and an Associate Director at NatWest Markets. He is a chartered accountant. Aged 40.

**4 Ray O'Toole**
Chief Executive UK Division
Ray O'Toole joined the Board in November 1999 as Chief Operating Officer. From January 2008 Ray became Chief Executive of all our UK operations. He spent the early part of his career in various engineering management positions at Greater Manchester Passenger Transport Executive. He joined National Express from FirstGroup plc, where he was responsible for its operations in Yorkshire and the North West as both Divisional Director and Group Engineering Director. He is a Member of the British Transport Police Authority. Aged 52.

**5 Sir Andrew Foster**
Non Executive Director +*ƒ
Sir Andrew was appointed to the Board in August 2004. He has had an extensive career in the public sector having served as Chief Executive of the Audit Commission for England and Wales between 1992 and 2003. Before this he was Deputy Chief Executive of the NHS and is currently Deputy Chairman of the Royal Bank of Canada Europe Limited, Chairman of the Commonwealth Games Council for England and a Non Executive Director of the Sports Council, Nestor Health Care and PruHealth. Sir Andrew has also recently completed reviews of further education and athletics for the Government. Aged 63.

**6 Barry Gibson**
Non Executive Director *#ƒ
Barry Gibson joined the Board in November 1999 and became the Senior Independent Director in September 2005. He served on the Board at BAA plc as Group Retailing Director. Until October 2001 he was the Group Chief Executive of Littlewoods Organisation plc. He is also a Non Executive Director of William Hill PLC and Homeserve plc. Aged 56.

**7 Roger Devlin**
Non Executive Director +#ƒ
Roger Devlin was appointed to the Board on 1 October 2007. Roger spent 13 years as a Director of Hill Samuel where he was head of Mergers and Acquisitions and Chief Executive of their US investment banking operations. He then moved to Ladbrokes, later Hilton PLC, as Group Corporate Development Director. He left Hilton in 2006 and now chairs three private equity businesses on behalf of Permira and Advent, all active in the leisure and hospitality fields. He is also Senior Independent Director of RPS Group plc, Europe's leading environmental consultancy. Aged 50.

**8 Jorge Cosmen**
Non Executive Director *ƒ
Jorge Cosmen was appointed to the Board in December 2005 at the time of the Alsa transaction. He was Corporate Manager for the Alsa Group from 1995, becoming Chairman in 1999. Between 1986 and 1995 he worked in sales, distribution and banking. He is a Business Administration graduate and has an International MBA from the Instituto de Empresa in Madrid. Aged 39.

**9 Tim Score**
Non Executive Director +#ƒ
Tim Score was appointed to the Board in February 2005. He is Chief Financial Officer at ARM Holdings plc. Before joining ARM he worked as Finance Director of Rebus Group Limited which he joined in 1999. Between 1997 and 1999, he was Group Finance Director of William Baird plc, which he joined from LucasVarity plc. He is a chartered accountant. Aged 47.

**10 Tony McDonald**
Company Secretary
Tony McDonald was appointed Company Secretary in May 2000. Prior to joining the Group he held senior legal positions with the in-house legal teams at Guardian Royal Exchange and BP and in private practice with Slaughter and May. He is a qualified solicitor. Aged 47.

\+ Member of the Audit Committee
* Member of the Nomination Committee
\# Member of the Remuneration Committee
ƒ Member of the Safety and Environment Committee

## DIVISIONAL HEADS

**Ray O'Toole**
Chief Executive UK Division
Ray O'Toole's details are shown opposite.

**Javier Carbajo**
Chief Executive Alsa Group
Javier Carbajo joined the Group in December 2005 when National Express acquired Alsa. A graduate in economics and with an MBA, he has been with Alsa for 28 years during which time he has held management positions in most areas of the business. In 1999 he was appointed Chief Executive of Enatcar following its acquisition by Alsa. In 2003 he was appointed CEO of Alsa Group. Aged 55.

**Brian Stock**
Chief Executive North America
Brian Stock joined the Group in 2002 through the acquisition of Stock Transportation. He has overseen the North American student bus operations since March 2004 and was appointed as Chief Executive of the Group's North American operations in October 2004. Brian has had over 25 years' experience in the bus industry. Prior to joining the Group, Brian was President of Stock Transportation and responsible for guiding the business to become the fifth largest school bus company in North America. Aged 49.

# Directors' Report

The Directors are pleased to present their annual report and the audited financial statements for the year ended 31 December 2007.

**Principal activities**
National Express Group PLC is the holding company of the National Express Group of companies. Its subsidiary companies provide mass passenger transport services in the UK and overseas.

**Business review**
Reviews of the business, likely future developments and details of principal risks and uncertainties as required by Section 234ZZB of the Companies Act 1985 can be found in the following pages and are incorporated into this report by reference:

- Chairman's Statement on pages 7 to 9.
- Chief Executive's Review on pages 10 to 13.
- Operating and Financial Review on pages 14 to 35.
- Principal risks and uncertainties on pages 32 to 33.

**Results and dividends**
The profit on ordinary activities before tax for the year ended 31 December 2007 was £149.9m (2006: £104.1m) and a profit attributable to equity shareholders of £108.9m (2006: £76.5m) was transferred to reserves.

The Directors recommend a final net dividend of 26.4p per share which, together with the interim net dividend of 11.56p per share paid on 28 September 2007, gives a total net dividend for the year of 37.96p per share (2006: 34.75p). If approved by shareholders, the final dividend will be paid on 9 May 2008 to shareholders on the register at 25 April 2008.

**Branches outside the UK**
The Company's subsidiary, National Express Spanish Holdings Limited, established a branch in Spain during the year.

**Directors**
The Directors of the Company who served during the year were:

David Ross
Richard Bowker
Jorge Cosmen
Roger Devlin (appointed 1 October 2007)
Sir Andrew Foster
Barry Gibson
Sue Lyons (resigned 19 December 2007)
Ray O'Toole
Tim Score
Adam Walker (resigned 26 March 2008)

Directors are appointed by ordinary resolution at a general meeting of ordinary shareholders. The Directors have the power to appoint a Director during the year but any person so appointed must be put up for appointment at the next Annual General Meeting. One-third of the Directors, or the number nearest to but not exceeding one-third, must retire from office at each Annual General Meeting. A retiring Director is eligible to stand for re-appointment. Any Director who has held office for three years or more since their last appointment must retire and offer themselves for re-appointment.

In accordance with the above provisions Sir Andrew Foster and Tim Score will retire by rotation at the Annual General Meeting and, being eligible, will offer themselves for re-election. Roger Devlin will stand for election at the 2008 Annual General Meeting following his appointment to the Board on 1 October 2007. Sue Lyons resigned as a Director of the Company on 19 December 2007.

The names and biographies of the current Directors appear on pages 36 and 37. Details of the remuneration of the Directors, their interests in shares of the Company and service contracts are contained in the Directors' Remuneration Report on pages 47 to 53 .

**Directors' interests in contracts**
Except as stated in note 37 on page 102, no contract existed during the year in relation to the Company's business in which any Director was materially interested.

**Directors' Liability Insurance**
The Company maintains Directors' and Officers' Liability Insurance in respect of legal action that might be brought against its Directors. Under the Company's Articles of Association the Company may indemnify its Directors and Officers in accordance with the provisions of Section 309A of the Companies Act 1985. In addition indemnities have been provided by the Company to Ray O'Toole who has been joined as a defendant in proceedings being brought before the Supreme Court of New South Wales. These proceedings relate to a period of time when Ray O'Toole was a Director of Bosnjak Holdings Pty Ltd, which was a subsidiary of the Group. Copies of the Articles of Association and the indemnity for Ray O'Toole are available for inspection at the Company's registered office.

**Employment policies**
The Group strives to meet its business objectives by motivating and encouraging its employees to be responsive to the needs of its customers and continually improve operational performance. The Group is committed to providing equality of opportunity to employees and potential employees. This applies to appropriate training, career development and promotion for all employees, regardless of physical ability, gender, sexual orientation, religion, age or ethnic origin. All UK businesses report diversity data and are responsible for benchmarking against their local population.

Full and fair consideration is given to applications for employment received from disabled persons, according to their skills and capabilities. The services of any existing employee disabled during their period of employment are retained wherever possible.

**Employee involvement**
The Group encourages employee involvement in its affairs. Subsidiary companies produce a range of internal newsletters and circulars which keep employees abreast of developments. In addition, the Group-wide *express* magazine kept employees in touch with the worldwide activities of the Group and reviews of the Group's financial performance appeared in this publication. Senior management within the Group meet regularly to review strategic developments and a Group senior leadership conference was held in 2007. Dialogue takes place regularly with Trade Unions and other employee representatives on a wide range of issues. Employees are able to share in the Group's results through various employee share schemes.

Employee satisfaction is tracked through an annual employee survey. Results from the 2007 survey have been fed back to employees and action plans at local level rolled out. A number of Group-wide initiatives have been established for employees. For example, the "Express Awards" reward outstanding employee activities in and out of the workplace and the "Express Benefits" package gives UK employees competitive discounts with leading retailers.

**Environmental policy**
Details of the Group's environment policy and environmental initiatives are to be found in the Corporate Responsibility Review on pages 34 to 35 and in the separate Corporate Responsibility Report.

**Charitable and political contributions**
Charitable donations made during the year totalled £374,000 (2006: £296,000). It is the Group's policy not to make political donations and accordingly none were made in the year. However the Company did attend and sponsor various political events during the year for which total expenditure was £27,900 (2006: £19,500).

**Creditors' payment policy and practice**
It is the Company's policy to agree terms of payment prior to commencing trade with any supplier and to abide by those terms based on the timely submission of satisfactory invoices.

Trade creditor days of the Company for the year ended 31 December 2007 were 22 days (2006: 18 days) based on the ratio of Company trade creditors at the end of the year to the amounts invoiced during the year by trade creditors.

**Financial instruments**
Details of the use by the Company and its subsidiaries of financial instruments can be found in the Notes to the Consolidated Accounts on pages 90 to 92.

**Major shareholdings**
As at 2 March 2008 the Company had been notified of the following interests in its shares which represent 3% or more of the voting rights in the Company:

| | Ordinary shares | Percentage of share capital | Nature of holding |
|---|---|---|---|
| European Express Enterprises Ltd | 13,503,600 | 8.88 | Direct |
| | 7,587,698 | 4.99 | Indirect |
| Barclays Bank PLC | 6,429,425 | 4.21 | Indirect |
| Barclays Global Investors | 10,748,506 | 6.90 | Indirect |
| Legal & General Group Plc | 6,125,072 | 4.00 | Direct |

These holdings exclude the Directors' holdings which are shown on page 52 of the Directors' Remuneration Report.

**Share capital and rights attaching to the Company's shares**
Under the Company's Articles of Association, any share in the Company may be issued with such rights or restrictions, whether in regard to dividend, voting, return of capital or otherwise as the Company may from time to time by ordinary resolution determine (or, in the absence of any such determination, as the Directors may determine).

At 31 December 2007, the Company's issued share capital consisted of a single class of ordinary shares with a nominal value of 5p. At a general meeting of the Company every member has one vote on a show of hands and on a poll one vote for each share held. The notice of general meeting specifies deadlines for exercising voting rights either by proxy or present in person in relation to resolutions to be passed at a general meeting. Details of the authorised and issued share capital of the Company can be found in note 32 on page 93 and details of shares issued during the year can be found in note 33 on page 93.

# Directors' Report continued

**Share capital (continued)**
No shareholder is, unless the Board decide otherwise, entitled to attend or vote either personally or by proxy at a general meeting or to exercise any other right conferred by being a shareholder if he or she or any person with an interest in shares has been sent a notice under Section 793 of the Companies Act 2006 (which confers upon public companies the power to require information with respect to interests in their voting shares) and he or she or any interested person failed to supply the Company with the information requested within 14 days after delivery of that notice. The Board may also decide that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered. These restrictions end seven days after receipt of the Company of a notice of an approved transfer of the shares or all the information required by the relevant Section 793 notice, whichever is earlier.

The Directors may refuse to register any transfer of any share which is not a fully-paid share, although such discretion may not be exercised in a way which the Financial Services Authority regards as preventing dealings in shares of that class from taking place on an open or proper basis. The Directors may likewise refuse any transfer of a share in favour of more than four persons jointly.

The Company is not aware of any other restrictions on the transfer of ordinary shares in the Company other than:

- certain restrictions that may from time to time be imposed by laws and regulations (for example, insider trading laws); and
- pursuant to the Listing Rules of the Financial Services Authority whereby certain employees of the Company require approval of the Company to deal in the Company's shares.

The Company is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities or voting rights.

Resolutions will be proposed at the 2008 Annual General Meeting to authorise the Directors to exercise all powers to allot shares and approve a limited disapplication of statutory pre-emption rights. Details are set out in the Notice of Meeting accompanying this document.

The Company was granted authority at the Annual General Meeting in 2007 to purchase its own shares up to an aggregate value of 10% of the issued nominal capital. The authority was not used during the year. The authority is renewed annually and approval will be sought at the Annual General Meeting in 2008 for its renewal. Further details are set out in the Notice of Meeting accompanying this document.

As at 2 March 2008 the Company held a total of 1,825,000 ordinary 5p shares (nominal value £91,250) in treasury equal to 1.2% of the issued share capital.

**Share schemes**
The IFG Trust (Jersey) Limited, as Trustee of the National Express Group Employee Benefit Trust, as at 2 March 2008 held 0.28% of the share capital of the Company for employee share schemes. The Trustee may vote the shares held by the Trust at its discretion.

**Annual General Meeting**
The Annual General Meeting will be held on 1 May 2008. Shareholders will be asked to approve five items of special business, details of which are given in the Notice of Meeting accompanying this report.

**Articles of Association**
The Company's Articles of Association may only be amended by a special resolution at a general meeting of shareholders. At the Company's Annual General Meeting to be held in 2008, a resolution will be put to shareholders proposing amendments to the existing Articles of Association, to incorporate changes introduced by the new Companies Act 2006.

**Powers of the Directors**
Subject to its Articles of Association and relevant statutory law and to any direction that may be given by the Company in general meeting by special resolution, the business of the Company shall be managed by the Directors, who may exercise all powers of the Company which are not required to be exercised by the Company in general meeting.

**Change of control agreements**
The Company is party to a number of banking agreements which allow for notification of change of control within five days of becoming aware of the event following which repayment of outstanding commitments is to be made within thirty days.

The Group's UK rail portfolio currently comprises three DfT franchises: National Express East Coast, National Express East Anglia and c2c. Each of the three rail franchise agreements with DfT contains termination rights for the benefit of DfT which would be triggered by a change of control in National Express Group PLC.

The Group's rail franchisees lease their rolling stock. National Express East Coast's rolling stock leases with HSBC Rail (UK) Limited and with Porterbrook Leasing Company Limited both contain termination rights for the benefit of the lessor which would be triggered by a change of control in National Express Group PLC.

All of National Express East Anglia's rolling stock leases with HSBC Rail (UK) Limited and its more significant leases with Porterbrook Leasing Company Limited contain termination rights for the benefit of the lessor which would be triggered by a change of control in National Express Group PLC.

The Group's UK bus business operates routes in London under a framework agreement with TfL. That agreement contains a termination right for the benefit of TfL which would be triggered by a change of control in National Express Group PLC.

The Group's North American business operates school bus services under contracts with school boards. Those contracts invariably contain a change of control clause for the benefit of the board which would be triggered by a change of control in National Express Group PLC. While no one single school bus contract could be considered significant in the context of the Group turnover, the impact on that turnover in the event that each school board exercised its termination right on a change of control would be significant.

**Directors' and employees' service contracts**
Ray O'Toole and Adam Walker have a provision in their service contract which provides that, where the Company initiates a termination other than for cause, within six months of a change of control taking place the Company will exercise its option to make a payment in lieu of notice of an amount equal to salary and benefits that the Director would have received during the notice period. There are no other agreements between the Company and its Directors or employees providing for compensation for loss of office or employment (whether through resignation, purported redundancy or otherwise) that occurs because of a takeover bid.

**Auditors**
Resolutions to appoint Ernst & Young LLP as auditors of the Company and to authorise the Directors to fix their remuneration will be proposed at the 2008 AGM.

**Disclosure of information to auditors**
The Directors confirm that so far as they are aware, there is no relevant audit information of which the Company's auditors are unaware and that each Director has taken all steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

**Going concern**
It should be recognised that any consideration of the foreseeable future involves making a judgement, at a particular point in time, about future events which are inherently uncertain. Nevertheless, at the time of preparation of these accounts and after making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue operating for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.

**Directors' responsibilities for the financial statements**
The Directors are responsible for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards as adopted by the European Union or, in the case of the Company's accounts, UK GAAP.

The Directors are required to prepare financial statements for each financial year that give a true and fair view of the financial position of the Company and of the Group and the financial performance and cash flows of the Group for that period. In preparing those accounts the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- present information and accounting policies in a manner that provides relevant, reliable and comparable information; and
- state that the Company and the Group have complied with applicable accounting standards, subject to any material departures disclosed and explained in the accounts.

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

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

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Information published on the internet is accessible in many countries with different legal requirements. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

**Tony McDonald**
Secretary
28 February 2008

# Corporate Governance Report

### The Board and its principal Committees

Details of the Board and its principal Committees are set out below. The following table sets out the number of meetings of the Board and its Committees during the year and individual attendance by the Board and Committee members at these meetings. All of the Committees are authorised to obtain legal or other professional advice as necessary, to secure the attendance of external advisers at their meetings and to seek information required from any employee of the Company in order to perform their duties. The full terms of reference of the Committees are available on the Company's website at www.nationalexpressgroup.com.

| | The Board of Directors | | Audit Committee | | Remuneration Committee | | Nomination Committee | | Safety and Environment Committee | |
|---|---|---|---|---|---|---|---|---|---|---|
| Name of Director | Attended | Possible | Attended | Possible | Attended | Possible | Attended | Possible | Attended | Possible |
| Richard Bowker *Chief Executive* | 15 | 16 | – | – | – | – | – | – | – | – |
| David Ross *Chairman* | 15 | 16 | – | – | – | – | 2 | 2 | 4 | 4 |
| **Executive Directors** | | | | | | | | | | |
| Ray O'Toole | 16 | 16 | – | – | – | – | – | – | – | – |
| Adam Walker | 15 | 16 | – | – | – | – | – | – | – | – |
| **Non Executive Directors** | | | | | | | | | | |
| Jorge Cosmen | 14 | 16 | – | – | – | – | 2 | 2 | 4 | 4 |
| Roger Devlin[1] | 4 | 4 | 1 | 1 | 1 | 1 | – | – | 1 | 1 |
| Sir Andrew Foster | 15 | 16 | 3 | 4 | – | – | 2 | 2 | 4 | 4 |
| Barry Gibson | 14 | 16 | 4 | 4 | 5 | 5 | – | – | 4 | 4 |
| Sue Lyons[2] | 14 | 16 | – | – | 4 | 5 | 2 | 2 | 4 | 4 |
| Tim Score | 14 | 16 | 4 | 4 | 5 | 5 | – | – | 4 | 4 |

Company Secretary: Tony McDonald (also acts as Secretary to the Board Committees).

1. Appointed to the Board on 1 October 2007.
2. Resigned from the Board on 19 December 2007.

### The Board of Directors

There is a formal schedule of matters reserved for the Board's attention which includes the review and approval of Group strategy and policies, major business acquisitions or disposals, major capital projects, Group budgets, significant changes to accounting policies, capital structure and dividend policy.

### Audit Committee

Members of the Audit Committee are Tim Score (Chairman), Roger Devlin and Sir Andrew Foster. Barry Gibson retired from the Committee on 19 December 2007 and Roger Devlin joined as a new member. The Committee oversees the process for selecting the external auditor, assesses the continuing independence of the external auditor and recommends approval of the audit fee to the Board. It is responsible for ensuring that provision of non audit services does not impair the external auditor's independence or objectivity. It discusses with the external auditor the nature and scope of the audit and any issues or concerns arising from the audit process. The Committee reviews the internal audit programme, considers major findings of the internal audit investigations and reviews management's financial reporting and risk management. The Committee reviews the half-year and annual financial statements and the effectiveness of the Company's internal control and risk management systems.

### Remuneration Committee

Members of the Remuneration Committee are Barry Gibson (Chairman), Roger Devlin and Tim Score. Sue Lyons retired from the Committee on 19 December 2007 and Roger Devlin joined as a new member on that date. The Committee is responsible for determining broad policy for the remuneration of the Executive Directors (including the Chief Executive), the divisional Chief Executives, the Chairman of the Company and the Company Secretary. Within the terms of the agreed policy the Committee will determine the total individual remuneration package of each Executive Director including, where appropriate, bonuses, incentive payments, pension arrangements and share options. The Committee is responsible for selecting, appointing and setting the terms of reference for any remuneration consultants who advise the Committee. The Committee ensures that contractual terms on termination, and any payments made, are fair to the individual and the Company, that failure is not rewarded and the duty to mitigate loss is, where appropriate, fully recognised.

### Nomination Committee

Members of the Nomination Committee are David Ross (Chairman), Sir Andrew Foster, Barry Gibson and Jorge Cosmen. Sue Lyons retired from the Committee on 19 December 2007 and Barry Gibson joined as a new member on that date. The Committee is responsible for identifying and nominating for the approval of the Board, candidates to fill Board vacancies as and when they arise. It will give full consideration to succession planning, and keep under review the leadership needs of the organisation, both executive and non executive. The Committee reviews the time required from a Non Executive Director and uses performance evaluation to assess whether the Non Executive is spending enough time to fulfil their duties.

### Safety and Environment Committee

Members of the Safety and Environment Committee are Jorge Cosmen, Sir Andrew Foster, Barry Gibson, David Ross, Tim Score and Roger Devlin who joined as a new member on 19 December 2007. Sue Lyons retired as Chairman of the Committee on 19 December 2007. The Committee reviews the Group's safety and environment practices, procedures and record.

The Board supports the highest standards of corporate governance and ethical practices within all its operations and continues to review its policies on an ongoing basis. The Board has endorsed a set of principles which establish the framework for how its businesses operate. Key to these is working in an open and honest manner.

**Statement of Compliance with the Combined Code**
In the opinion of the Directors the Company has complied with Section 1 of the Combined Code on Corporate Governance published in 2006 (the "Combined Code") throughout the year apart from provision B.1.6 (notice periods) and provision A.6.1 (performance evaluation of the Board) as follows:

- The notice period of Ray O'Toole, which previously had been 12 months, was increased to 24 months as at 1 September 2006. This period reduced on a daily basis such that on 1 September 2007 the notice period was 12 months once again. This change was approved by the Remuneration Committee on the appointment of a new Chief Executive to the Group to try to ensure continuity of management.
- During the year the Board implemented the recommendations arising from the Board effectiveness review carried out in 2006. The next evaluation of the Board's and Chairman's performance will take place in 2008.

**Applying the principles of good governance**
**The Board of Directors, Chairman and Chief Executive**
The Directors believe it is essential for the Group to be led and controlled by an effective Board that provides entrepreneurial leadership within a framework of sound controls. The Board is responsible for setting the Group's strategic aims, its values and standards and ensuring the necessary financial and human resources are in place to achieve its goals.

The Board consists of the Chairman, three Executive and five Non Executive Directors. A full list of the Directors with details of their biographies and Committee memberships is given on page 37. The offices of Chairman and Chief Executive are held separately and the division of responsibilities between the Chairman and Chief Executive is shown below.

**Main responsibilities of the Chairman include:**

- chairing and managing the business of the Board;
- together with the Chief Executive, leading the Board in developing the strategy of the business and ensuring this is effectively implemented by the executive management team;
- ensuring that there is effective dialogue with investors concerning mutual understanding of objectives;
- in conjunction with the Nomination Committee, taking responsibility for the composition and replenishment of the Board;
- periodically reviewing with the Board its working practices and performance; and
- ensuring there is effective contribution from the Non Executive Directors and a constructive relationship between the Executive and Non Executive Directors.

**Main responsibilities of the Chief Executive include:**

- the development and implementation of management strategy;
- the day-to-day management of the Group;
- managing the executive management team; and
- fostering relationships with key stakeholders.

Barry Gibson is the Senior Independent Director. The Board considers all of the Non Executive Directors to be independent other than Jorge Cosmen, and considered David Ross to be independent prior to his appointment as Chairman. Mr Cosmen is not considered to be independent by the Board due to his close links with the Alsa business and significant interests in the shares of the Company which are held through European Express Enterprises Limited. The Non Executives bring a variety of different experiences and considerable knowledge to assist with Board decisions. Non Executive Directors do not participate in any of the Company's share option or bonus schemes and their service is non pensionable.

The Board meets at least eight times during the year. In 2007 the Board visited businesses in Spain and North America. There is a formal schedule of matters reserved for the Board's decision, the main terms of which are shown on page 42 together with the attendance record of the Directors. During the year the Chairman met on several occasions with the Non Executives without the Executive Directors present to allow informal discussions on a variety of issues.

The Executive Directors are responsible for the day-to-day management of the Group's businesses, implementation of its strategy, policies and budgets and its financial performance. Executive management meetings, involving the Executive Directors and senior management from the divisions are held regularly to discuss current issues.

The Company purchases Directors' and officers' liability insurance for the Company and its subsidiaries, which gives appropriate cover for any legal action brought against its Directors.

**Committees of the Board**
The Board has established a number of Committees with defined terms of reference and receives reports of their proceedings. The principal Committees are the Remuneration Committee, the Nomination Committee, the Audit Committee and the Safety and Environment Committee. The members of each Committee, attendance and main duties are shown on page 42. In addition there is an Executive Committee with authority to approve routine matters of business and a Tax and Treasury Committee which reviews the Group's tax planning, banking facilities and treasury reports.

# Corporate Governance Report continued

### Appointments to the Board

The Nomination Committee leads the process for Board appointments and makes recommendations to the Board. The Committee will prepare a description of the role and requirements for any particular appointment based on its evaluation of the Board as a whole.

The terms and conditions of appointment of the Non Executive Directors are available for inspection at the Company's registered office during normal business hours and at the Annual General Meeting of the Company. The Non Executive Directors disclose to the Board their other significant commitments.

External advisors are normally appointed when recruiting Board members; they use as a basis for their search a description of the role and capabilities required for a particular appointment proposed by the Nomination Committee.

### The work of the Nomination Committee

The members of the Nomination Committee are David Ross (Chairman), Barry Gibson, Sir Andrew Foster and Jorge Cosmen.

Before making a recommendation for an appointment to the Board the Nomination Committee:

- prepares a job specification and a description of the capabilities required for a particular post;
- considers the current composition of the Board and mix of skills and experience; and
- where appropriate, and in particular where a vacancy for a Non Executive Director arises, will use an external search consultancy and/or open advertising.

During the year the Committee:

- considered the appointment of a new Non Executive Director to replace Sue Lyons;
- appointed search consultants for the Non Executive Director's position; and
- interviewed candidates for this position following which Roger Devlin was appointed as a Non Executive Director on 1 October 2007.

### Information and professional development

Reports from the Executive Directors, which include in-depth financial information, are circulated to Board members prior to every Board meeting. Senior management and advisors give presentations to the Board on significant matters during the year.

Under the direction of the Chairman, the Company Secretary is responsible for ensuring Board procedures are followed and applicable rules and regulations are complied with and advises the Board on governance matters. All Directors have access to the advice and services of the Company Secretary and the appointment or removal of the Company Secretary is a matter for the Board as a whole. There is a procedure in place for any Director to take independent professional advice where considered necessary.

On appointment, Directors are offered an appropriate training course and are thereafter encouraged to keep abreast of matters affecting their duties as a Director and to attend training courses relevant to their role. An induction process is in place for new Directors the aims of which are to:

- build an understanding of the nature of the Company, its business and the markets in which it operates;
- establish a link with the Group's employees; and
- build an understanding of the Group's main relationships including stakeholders and customers.

### Performance evaluation

During the year proposals arising from the Board effectiveness review carried out by an external third party were implemented and a review of Richard Bowker's performance after his first full year in the role of Chief Executive was undertaken. The proposals arising from the Board effectiveness review will be reviewed as part of the 2008 evaluation of the Board's performance, its Committees and the Chairman.

### Re-election

In accordance with the Company's Articles of Association all Directors submit themselves for election at the Annual General Meeting following their appointment and thereafter by rotation at least once every three years. Non Executive Directors are appointed for specific terms, subject to re-election. Non Executive Directors will only be put forward for re-election if, following performance evaluation, the Board believes the Director's performance continues to be effective and demonstrates commitment to the role.

### Remuneration and service contracts

The Directors' Remuneration Report including details of remuneration policy and service contracts is set out on pages 47 to 53.

### Accountability and audit

Statements of the respective responsibilities of the Directors and auditors are set out on pages 41 and 54.

## Internal control

### The Board's responsibilities

The Board has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. The Board maintains full control and direction over appropriate strategic, financial, operational and compliance issues and has put in place an organisational structure with formally defined lines of responsibility, delegated authorities and clear operating processes. The systems that the Board has established are designed to safeguard both the shareholders' investment and the assets of the Group, and are described below.

### Key elements of the control framework

*Strategic and financial planning* – an annual budgeting and strategic planning process has been established whereby each division and constituent operating company assesses its competitive position and goals, taking account of the strategic risks faced. This strategy is translated into a financial plan with clear milestones and performance indicators.

*Performance management* – the performance of each division and operating company against its plan is closely monitored by a formal monthly reporting process and by the attendance of the Executive Directors at monthly divisional board meetings.

*Annual fitness check process* – a self assessment review takes place at each operating company to assess the integrity of the balance sheet and to challenge the effective operation of key financial and information systems controls within each material accounting cycle. This process is led by divisional Finance Directors and is closely monitored by group finance and validated by the internal audit function.

*Capital investment* – a clear process is in place for the approval of capital expenditure, which includes detailed appraisal of the benefits of the proposed investment and any associated key risks. Material capital expenditure requires Board approval.

*Health and safety* – health and safety standards and benchmarks have been established in all our businesses and the performance of operating companies in meeting these standards is closely monitored.

*Risk management reporting process* – each division and operating company evaluates its internal control environment and key risks, and the results are reviewed at management level and passed to the Audit Committee before being presented to the Board. This process is reviewed on a regular basis to ensure the validity and relevance of the key risks reported and presented to the Board on a quarterly basis, unless exceptional issues arise. The review covers strategic, financial, compliance and risk management controls. These procedures are mandated and designed to manage the risk in order to ensure that the operations achieve their business objectives.

*Internal audit* – the internal control system is independently monitored and supported by an outsourced internal audit function. The internal audit function reports to management and the Audit Committee on the Group's financial and operational controls, and reviews the extent to which its recommendations have been implemented.

*Board-level reporting on internal control* – during the year the Audit Committee reviews regular reports from the internal audit function, the external auditor, and executive management on matters relating to internal control, financial reporting and risk management. The Audit Committee provides the Board with an independent assessment of the Group's financial position, accounting affairs and control systems. In addition, the Board receives regular reports on how specific risks that are assessed as material to the Group are being managed.

### Review of internal control effectiveness

The system of internal control and risk management, described above, has been in place for the year under review and up to the date of approval of this Annual Report and Accounts. Such a system is designed to manage, rather than to eliminate, the risks inherent in achieving the Group's business objectives, and can therefore provide only reasonable and not absolute assurance against material misstatement or loss. The effectiveness of this system has been regularly reviewed by the Directors in line with the Guidance for Directors in the Combined Code published by the Financial Reporting Council (Turnbull guidance).

## Audit Committee and auditors

### The work of the Audit Committee

Members of the Committee are Tim Score (Chairman), Roger Devlin and Sir Andrew Foster. Barry Gibson retired from the Committee on 19 December 2007. Attendance by the members is shown on page 42.

The Committee meets at least three times a year and met four times in 2007. The agenda reflects the duties delegated to it by its terms of reference, details of which are summarised on page 42. There are a number of standing items considered during the year such as consideration of the internal and external audit reports, review of the annual report and accounts, review of the preliminary and half year announcements, and review of the Corporate Governance Report.

Other items that were considered and discussed during 2007 included a review of the 2007 internal and external audit plans, the transformation project in North America, annual fitness checks within the subsidiaries and the external auditor's performance and fees.

At the invitation of the Committee, and as appropriate to the matters under discussion, meetings may be attended by the Executive Directors and internal and external auditors. Full minutes are kept by the Secretary of the matters considered and decisions taken by the Committee. Outside of the meeting process the Committee Chairman has regular contact with the Executive Directors, other Committee members and the auditors on a variety of topics.

### Review of external auditors

The Audit Committee assesses and reviews on a regular basis the independence of the external auditor. As part of their determination the Audit Committee considers a report by the external auditor on the firm's independence which is required in order to carry out their professional duties and responsibilities as auditor.

# Corporate Governance Report continued

**Policy on auditors providing non audit work**
The Committee has an approved policy on the provision of non audit services. The policy sets the approvals policy for the following types of service:

- services that are considered to have “general pre-approval” by the Audit Committee, by virtue of the approval of the policy;
- services that require “specific pre-approval”, on a case-by-case basis, before any work can commence; and
- services that cannot be supplied by the external auditors (“prohibited services”).

The services that require specific pre-approval are tax, transaction, investigation and valuation, advisory and corporate finance services. The fees for these services are pre-approved up to a level of 25% of the total fees paid to the external auditors. For services exceeding this limit specific pre-approval is required.

In deciding whether or not to grant approval for the provision of specific services by the external auditors, the Audit Committee includes in its consideration the following factors:

(i) whether the external auditing firm is best placed to provide an effective and efficient service, given its familiarity with the Company’s processes, systems and people; and

(ii) the level of non audit fees paid to the external auditors in the year as a proportion of the annual external audit fee.

The majority of non audit work undertaken by the external auditor during the year relates to two items. These were tax advisory and compliance services and financial due diligence services in relation to the acquisition of Continental Auto. These items the Committee believes would be impractical and costly to provide through another party.

**Whistleblowing policy**
A Group “whistleblowing” policy has been issued to all Group companies to ensure a consistent approach across the Group.

**Relations with shareholders**
**Dialogue with institutional shareholders**
The Board maintains regular dialogue with its institutional shareholders and fund managers through a variety of meetings and presentations throughout the year. Presentations are given by the Executive Directors following the full year and half year results to institutional investors, analysts and brokers which the Non Executive Directors may attend. In addition, the Company’s brokers provide confidential feedback to the Company on the views of the major institutions following the half year and final results. A formal review of the opinions of the Company’s major investors on its financial performance and management was undertaken in 2007 and an action plan formulated to address key issues arising from this survey.

During the year written responses are given to correspondence received from shareholders and all shareholders receive copies of the Annual Report and Accounts or the Annual Review and Summary Financial Statement. The Company has introduced an electronic communications facility to enable shareholders to receive documentation such as the Annual Report and Accounts electronically and also to cast their votes by proxy electronically. The Company has also introduced an electronic proxy appointment service for CREST members.

The Company’s website, www.nationalexpressgroup.com, houses wide-ranging information about the Group, including the Annual Report and Accounts, press releases, share price data and links to subsidiary company websites.

**The Annual General Meeting**
The Annual General Meeting provides an opportunity for all shareholders to question the Chairman and Directors on a variety of topics, and information is provided at the meeting on different aspects of the Group’s activities. All of the Company’s Directors are present at the meeting. Voting at the Annual General Meeting on all resolutions is by poll on a one share, one vote basis. The results are available on the Group’s website following the meeting. Notice of the Annual General Meeting and related papers are sent to shareholders at least 20 working days before the meeting.

# Directors' Remuneration Report

This report has been approved by the Board and the Remuneration Committee (the "Committee"). Shareholders will be invited to approve the report at the 2008 Annual General Meeting.

**Remuneration Committee**
**Composition of the Committee**
The members of the Committee who served during the year, all of whom were independent Directors, were:

Barry Gibson *(Chairman)*
Roger Devlin *(appointed to the Committee 19 December 2007)*
Sue Lyons *(resigned 19 December 2007)*
Tim Score

**Role of the Committee**
The key responsibilities of the Committee are to:

- determine the fees of the Chairman;
- determine the remuneration and conditions of employment (including any termination arrangements) of the Executive Directors;
- approve the remuneration and conditions of employment of the Divisional Chief Executives and Company Secretary;
- review the remuneration and conditions of employment of the senior management team; and
- select and appoint any remuneration consultants who advise the Committee.

The full terms of reference of the Committee are available on the Company's website at www.nationalexpressgroup.com

**Advisors to the Committee**
The Committee has appointed independent remuneration consultants, New Bridge Street Consultants LLP (NBSC), to advise on all aspects of senior executive remuneration. NBSC has no other connection with the Group other than in the provision of advice on executive and employee remuneration.

The Chief Executive and Chief Executive UK Division provide guidance to the Committee on remuneration packages for senior executives employed by the Group (but not in respect of their own remuneration).

**Activities of the Committee**
During the year the Committee considered the following items of business:

- Executive Directors' and senior executives' salary levels and 2006 annual bonus awards.
- Annual bonus scheme terms for 2007.
- Review of the Chairman's fees.
- The total shareholder return comparator group used in the Long Term Incentive Plan's performance condition.
- 2007 award levels under the Company's Long Term Incentive Plan and WMT Long Service Option Scheme.
- Testing of performance conditions and vesting of Executive Share Options granted in 2004.
- Long Term Incentive Plan entitlements upon redundancy.

The Committee's recommendations in 2007 were all accepted and implemented by the Board.

**Remuneration of Non Executive Directors**
The fees of the Non Executive Directors are set by the Board as a whole following an annual review. The review takes account of fees paid for similar positions in the market, the time commitment required from the Director (estimated to be 100 days per year for the Chairman and 20 days per year for the other Non Executive Directors) and any additional responsibilities undertaken, such as acting as Chairman to one of the Board Committees or Senior Independent Director. Non Executive Directors are not eligible to receive pension entitlements or bonuses and may not participate in share option schemes. For 2007 the basic fee for acting as a Non Executive Director was £43,000 a year. A fee of £5,000 is paid for chairing a Committee. An additional fee of £5,000 is paid to the Senior Independent Director. The base fee for Non Executive Directors will increase to £44,000 in 2008 and the fee for chairing a Committee will increase to £7,000. The Chairman, David Ross, has made a standing election with his brokers to invest all of his Chaiman's fees in National Express Group PLC shares.

**Remuneration policy for Executive Directors**
Remuneration policy is based on the following broad principles set by the Committee:

- to provide a competitive remuneration package to attract and retain quality individuals;
- to align remuneration to drive the overall objectives of the business;
- to align the interests of management with the interests of shareholders; and
- to provide the foundation for overall reward and remuneration beyond the specific roles falling within the direct remit of the Remuneration Committee.

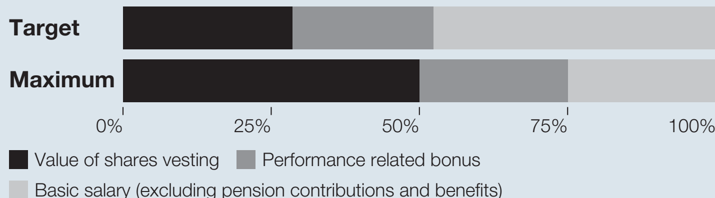
The objective of this policy is aligned with the recommendation of the Combined Code on Directors' remuneration. That is to provide a level of remuneration "to attract, retain and motivate Directors of the quality required to run the Company successfully, but avoid paying more than is necessary for this purpose. A significant proportion of Executive Directors' remuneration should be structured so as to link rewards to corporate and individual performance."

# Directors' Remuneration Report continued

**Remuneration policy for Executive Directors (continued)**
In implementing its policy, the Committee gives full consideration to the principles set out in the Combined Code on Corporate Governance with regard to Directors' remuneration.

Remuneration policy is reviewed on an ongoing basis against the Committee's broad principles and in light of emerging best practice in corporate governance. The Group operates a leadership and development programme which includes an appraisal system for Directors and senior management. The appraisal system uses balanced scorecards to assess performance against financial, customer, operational and people objectives. The results of the annual appraisal system are taken into consideration when setting remuneration levels.

**Performance related versus fixed remuneration (%)**




**Fixed versus variable remuneration**
A substantial proportion of the Executive Directors' pay is performance related. The table opposite shows the balance between fixed and performance related pay at target and maximum performance levels. Maximum performance assumes achievement of maximum bonus and full vesting of shares under the LTIP.

**Elements of remuneration**
Summary of the components of the Executive Directors' remuneration.

| | Objective | Performance period | Policy |
|---|---|---|---|
| Basic salary | To position at a competitive level for similar roles within comparable markets | Annually | Individual pay levels (using comparable mid-market data for guidance) are determined by reference to the individual's performance, experience in post and potential. |
| Performance related bonus | To incentivise delivery of performance objectives | 1 year | Bonus payments are based on the achievement of specified corporate objectives. |
| Pension | To provide competitive benefits in line with market practice and to act as a retention mechanism and reward long service | Ongoing | The policy is to provide market competitive retirement benefits. Only basic salary is pensionable. |
| Long Term Incentive Plan | To drive performance, aid retention and align the interests of Executive Directors with shareholders | 3 years | Half of any award is subject to EPS growth. The remaining half is subject to the relative total shareholder return (TSR) of the Company compared against a bespoke peer group. |
| Other benefits | To provide competitive benefits in line with market practice | Ongoing | Executive Directors receive a fully expensed car, private health and long-term sickness insurance. A cash alternative may be provided according to individual circumstances. |

**(i) Basic salary**
The salary of individual Executive Directors is reviewed at 1 January each year. Account is taken of the performance of the individual concerned, together with any change in responsibilities that may have occurred and the rates for similar roles in a comparator group of companies. The comparator group for the 2007 financial year was made up of two groups of companies. These were a group of transport sector companies with a median market capitalisation of £1,312m and a group of companies from the FTSE Mid 250 drawn from all sectors with a median market capitalisation of £1,451m which reflected that of National Express at the time of completing the review. For 2008 the comparator groups will be based on similar groups of transport/leisure and general sector companies drawn from the FTSE 250.

**(ii) Performance related bonus**
The maximum potential bonus payable to Executive Directors in 2007 was 100% of salary. 70% of the bonus payable was based on financial targets and 30% based on non financial targets. The non financial targets encompass customer, operational excellence and people objectives. No bonus is payable unless the Group's normalised profit budget is achieved. The definition of normalised profit is set out in the Glossary on page 116. Directors receive 50% of that part of the bonus referable to financial targets upon achieving budget and 100% of that part upon achieving a stretch target which, for 2007, was 107% of budget. In terms of actual performance against the targets set for the financial year under review, the stretch financial targets were met in full and, after taking into consideration performance against the non financial targets,bonus payments to Executive Directors were in the range of 95% to 100%. For 2008 bonus payments will be based on a similar structure with the maximum potential bonus opportunity remaining at 100% of salary.

**(iii) Pensions**
Under the terms of their service agreements, Executive Directors are entitled to become members of one of the Group pension schemes or, if preferred, to receive payment of a fixed percentage of salary.

Adam Walker is a member of the National Express Group Staff Pension Plan ("the Plan") which is an HM Revenue & Customs (HMRC) approved defined benefit scheme. The benefits from this Plan are subject to HMRC limits. Spouses' pensions are provided in accordance with the terms of the Plan. Ray O'Toole was a member of this Plan until 7 April 2006 and he now receives a salary supplement of 44% in lieu of pension contributions. Richard Bowker is not a member of a company pension scheme and receives a 25% salary supplement in lieu of pension contributions.

Life assurance of four times' basic annual salary is provided for the Executive Directors.

### (iv) Incentive scheme and share options

#### (a) Long-term incentive arrangements

The National Express Group Long Term Incentive Plan (LTIP) was approved by shareholders at the 2005 Annual General Meeting and operates as the Company's sole type of executive long-term incentive arrangement. The LTIP consists of annual awards of performance and matching shares. Details of the plan are provided below.

#### Performance shares

Executive Directors are eligible to receive a conditional award of shares up to an equivalent of 1 x their annual basic salary. The vesting of the award is conditional on meeting the performance conditions set out below.

#### Matching shares

Executive Directors are also eligible to receive awards of matching shares that are based on a personal investment in National Express Group PLC shares funded either through a personal investment (for example using an annual bonus award) or through pledging of shares already held but not already allocated to the LTIP. The maximum investment/pledge is 30% of gross salary per annum. Matching awards are based on the ratio of 100 shares for every 30 shares purchased. This is a two for one ratio on a gross income tax basis. Matching share awards are also conditional on the performance conditions set out below.

If a participant ceases employment before vesting for a "compassionate" reason (eg redundancy, retirement, death in service, sale of business out of the Company's group) his awards will ordinarily vest. The extent of vesting will be determined by the pro rata application of the performance conditions up to the date of cessation unless the Committee determines that it would be inappropriate to apply a pro rata reduction. Awards lapse on cessation of employment for any other reason.

#### Performance conditions

There are two distinct performance conditions applying to awards made. First, the performance condition attached to one-half of an award (Part "A") is based on the Company's normalised diluted earnings per share ("EPS") growth performance in excess of inflation over a fixed three year period (three financial years commencing with the financial year in which the award is made). The performance condition attached to the other half of an award (Part "B") is based on the Company's TSR performance over the same fixed three year period relative to the TSR performance of a comparator group of 20 transport companies taken predominantly from the FTSE Industrial Transportation and FTSE Travel & Leisure sectors. The companies comprising the comparator group have been chosen on the basis of their comparability to National Express Group PLC (based on their size and scope of business operations). There is no ability to retest either performance condition.

For awards made in 2005, 2006 and 2007 Parts A and B will vest to the extent that the performance conditions set out in the tables below are met:

| Average growth in the Company's normalised diluted EPS* in excess of inflation ("CPI"*) | Percentage of Part A that vests |
|---|---|
| Less than 3% | 0% |
| 3% | 30% |
| 6% | 100% |
| Between 3% and 6% | 30%–100% pro rata |

*Normalised diluted earnings per share and CPI are as defined in the Glossary on page 116.

| Rank of the Company's Total Shareholder Return against a comparator group | Percentage of Part B that vests |
|---|---|
| Below median | 0% |
| Median | 30% |
| 20th percentile | 100% |
| Between median and 20th percentile | 30% and 100% – pro rata |

EPS and TSR were chosen for the LTIP as the most appropriate measures of National Express's long-term performance since EPS remains an important growth measure and driver and TSR improves shareholder alignment and is consistent with Company objectives of providing long-term returns to shareholders.

The following table sets out the percentage of each extant award that would have vested if the performance conditions had been tested as at 31 December 2007 (without making any allowance for pro rata reduction for any period of less than three years).

**Indicative percentage of LTIP awards vesting based on performance to 31 December 2007**

| Year of award | TSR element (max 50%) | EPS element (max 50%) | Total (max 100%) |
|---|---|---|---|
| 2005 | 39.7% | 28.0% | 67.6% |
| 2006 | 33.3% | 0.0% | 33.3% |
| 2007 | 40.5% | 50.0% | 90.5% |

#### (b) Savings Related Share Option Scheme (Sharesave Scheme)

The Company operates an HMRC approved Sharesave Scheme which is open to all UK employees, including the Executive Directors, who have completed at least six months' service at the date of grant. The options are exercisable after three years at a discount of 10% of the market value of the shares at the time of grant.

# Directors' Remuneration Report continued

**Performance criteria**

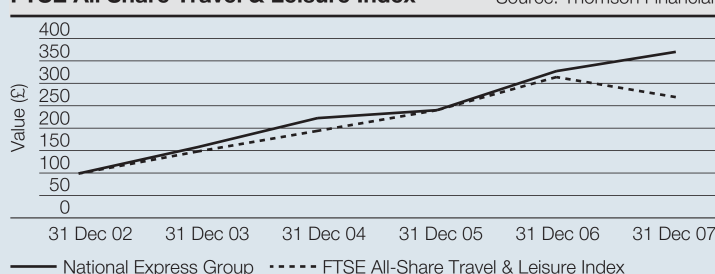
The Committee believes that budgeted profit and/or EPS growth as performance measures for the discretionary bonus scheme and long-term incentives provide a transparent and accessible method of gauging the performance of the Company. The Company calculates performance against these performance measures by reference to the profit or earnings per share figures appearing in the Company's audited accounts, which the Company believes to be the most transparent and objective measure of the Company's profit or EPS. The Committee also monitors the Group's TSR against both the FTSE All Share Travel & Leisure Index as a measure against its peer group and the FTSE 250 Index, representing a broad equity market index of which the Company is a constituent member. TSR has been used by the Company as a second performance measure for awards made to Executive Directors under the LTIP as outlined above.

Prior to making awards in 2008, the Remuneration Committee will undertake a review of the ongoing appropriateness of the range of EPS targets given the recent corporate activity of the Company and the constituents of the TSR peer group.

The following graphs show a comparison of National Express Group PLC total cumulative shareholder return against that achieved by the FTSE All Share Travel & Leisure Index and the FTSE 250 Index. These graphs have been selected because the Company is a constituent of each index and the Committee, therefore, feels that these are the most appropriate indices to represent the Company's relative performance.

**Total shareholder return versus FTSE All Share Travel & Leisure Index**

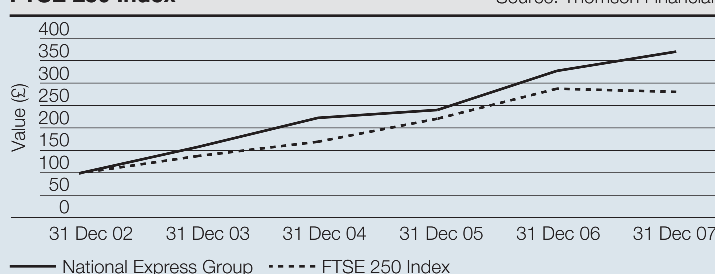
Source: Thomson Financial




Graph 1 looks at the value, by the end of 2007, of £100 invested in National Express Group on 31 December 2002 compared with £100 invested in the FTSE All-Share Travel & Leisure Index. The other points plotted are the values at intervening financial year-ends.

**Total shareholder return versus FTSE 250 Index**

Source: Thomson Financial




Graph 2 looks at the value, by the end of 2007, of £100 invested in National Express Group on 31 December 2002 compared with the value of £100 invested in the FTSE 250 Index. The other points plotted are the values at intervening financial year-ends.

**Directors' service contracts, notice periods and termination payments**

**Executive Directors**

The contract dates and notice periods for the Executive Directors are as follows:

| Director | Contract date | Notice period from the Company | Notice period from the Director |
|---|---|---|---|
| Richard Bowker | 22 May 2006 | 12 months | 12 months |
| Ray O'Toole | 11 September 2003 | To 1 September 2006 – 12 months<br>From 1 September 2006 – 24 months<br>reducing on a daily basis to 12 months<br>by 1 September 2007 | 6 months |
| Adam Walker<br>(resigned as a Director 26 March 2008) | 11 September 2003 | 12 months | 6 months |

It is the Committee's general policy for the notice periods of Executive Directors to be no longer than 12 months. However, the Committee approved a notice period of 24 months for Ray O'Toole on the appointment of a new Chief Executive to try to ensure continuity of management during this time of change. The notice period reduced on a daily basis between 1 September 2006 and 31 August 2007 such that on 1 September 2007 the notice period was once again 12 months.

The service contracts of Richard Bowker and Adam Walker contain a provision, exercisable at the option of the Company, to pay an amount on early termination of employment equal to one year's salary. In the case of Ray O'Toole the early termination payment has fallen from two years at 1 September 2006 to one year's salary at 1 September 2007. The Company will use the payment in lieu of notice provisions when the speed, certainty and protection of restrictive covenants afforded by such clauses are thought to be in the best interests of the Company and the circumstances surrounding the departure of the relevant Director justify their use. The service contracts of Ray O'Toole and Adam Walker have a further provision that, where the Company initiates a termination, other than for cause, within six months of a change of control taking place the Company will exercise its option to make a payment in lieu of notice of an amount equal to the salary and benefits that the Director would have received during the notice period. In any event the Committee's policy is that payments to Directors on termination should reflect the circumstances that prevail at the time, also taking account of the Director's duty to mitigate if appropriate.

Under the terms of their service agreements, Board approval is required before any external appointment may be accepted by an Executive Director.

### Non Executive Directors

The Non Executive Directors do not have service contracts with the Company but are appointed for fixed three-year terms. All Directors are required to stand at least once every three years for re-appointment by shareholders. The appointment dates of the Non Executive Directors are:

Jorge Cosmen – 1 December 2005
Roger Devlin – 1 October 2007
Sir Andrew Foster – 1 August 2004
Barry Gibson – 17 November 1999
David Ross – 1 February 2001
Tim Score – 21 February 2005

### Senior executive remuneration

The Remuneration Committee reviews and notes the salaries of senior executives within the Group. The salaries of this group of employees by band are as follows:

| Salary band £000 | Number of executives 2007 |
|---|---|
| >200–340 | **4** |
| >150–200 | **8** |
| >100–150 | **24** |
| 70–100 | **49** |

### Information subject to audit: Directors' remuneration
### Directors' emoluments

| | Salary/fees £000 | Performance related bonus £000 | Benefits[1] £000 | Benefits in lieu of pension £000 | **Total 2007[2] £000** | Total 2006[2] £000 |
|---|---|---|---|---|---|---|
| **Executive Directors** | | | | | | |
| Richard Bowker (appointed 12 September 2006) | 500 | 475 | 33 | 125 | **1,133** | 359 |
| Ray O'Toole | 375 | 356 | 25 | 165 | **921** | 864 |
| Adam Walker (resigned 26 March 2008) | 360 | 360 | 24 | – | **744** | 663 |
| **Non Executive Directors** | | | | | | |
| David Ross (Chairman) | 185[3] | – | – | – | **185** | 160 |
| Jorge Cosmen | 43 | – | – | – | **43** | 40 |
| Roger Devlin (appointed 1 October 2007) | 11 | – | – | – | **11** | – |
| Sir Andrew Foster | 43 | – | – | – | **43** | 40 |
| Barry Gibson | 53 | – | – | – | **53** | 50 |
| Sue Lyons (resigned 19 December 2007) | 48 | – | – | – | **48** | 45 |
| Tim Score | 48 | – | – | – | **48** | 45 |

1. Benefits in kind include a company car, fuel, life assurance and health insurance.
2. Total remuneration excludes Company pension contributions which are shown below.
3. David Ross has given a standing instruction to his brokers to reinvest his Chairman's fees in National Express Group PLC shares.

### Former Director

Phil White stepped down as Chief Executive of the Company on 11 September 2006. He remained in full time employment with the Group until 31 March 2007. Details of payments to Phil White for the period 1 January 2007 to 31 March 2007 are shown below.

| | Salary/fees £000 | Benefits[1] £000 | Benefits in lieu of pension £000 | **Total 2007 £000** | Total 2006 £000 |
|---|---|---|---|---|---|
| Phil White (resigned as Director 11 September 2006) | 125 | 17 | 62 | **204** | 1,292 |

1. Benefits in kind include a company car, fuel, life assurance and health insurance.

On 31 March 2007 Phil White received, in accordance with his contractual entitlements, the title to his car (value £74,000) and accrued but unused holiday entitlement. From 1 April 2007 to 30 September 2007 Phil White acted as a consultant for the Group for which he received a monthly fee of £25,000. During this period, he assisted the Company in particular, with a piece of ongoing litigation in New South Wales, Australia. On retirement Phil White was entitled to exercise share options granted to him under the 2002 Executive Share Option Plan, subject to the fulfilment of the applicable performance conditions which were met in full. In addition unvested awards held by Phil White under the Long Term Incentive Plan vested subject to the fulfilment of the applicable performance conditions. No part of the awards subject to EPS testing vested and 43.4% of the awards subject to the TSR performance condition vested.

# Directors' Remuneration Report continued

**Pensions**

Pension benefits earned by Directors in the year to 31 December 2007 from both the approved and unapproved plans were:

| | Age | NRA+ | Accrued benefit at 1 January 2007 £000 | Increase in period (net of indexation) £000 | Transfer value of increase in period £000 | **Accrued benefit at 31 December 2007 £000** | Transfer value at 1 January 2007 £000 | **Transfer value at 31 December 2007 £000** | Movement in transfer value during period less Director's contributions £000 |
|---|---|---|---|---|---|---|---|---|---|
| Ray O'Toole* | 52 | 60 | 33.8 | – | – | **35.0** | 461.5 | **490.5** | 29.0 |
| Adam Walker (resigned 26 March 2008) | 40 | 60 | 33.7 | 11.0 | 88.8 | **45.9** | 266.8 | **371.3** | 83.1 |

+Normal Retirement Age.
*Ray O'Toole ceased to accrue pension benefits on 7 April 2006.

**Directors' shareholdings**
**Directors' interests and transactions**
(This table is not subject to audit)

The beneficial and non beneficial interests of the Directors in office as at 31 December 2007 are shown below:

| | **At 31 December 2007** | At 1 January 2007 or on appointment if later | Change from 31 December 2007 to 2 March 2008 |
|---|---|---|---|
| **Executive Directors** | | | |
| Richard Bowker | **7,554** | 2,554 | 11,828 |
| Ray O'Toole | **24,364** | 24,364 | 26,364 |
| Adam Walker (resigned 26 March 2008) | **25,000** | 19,400 | – |
| **Non Executive Directors** | | | |
| Jorge Cosmen | **23,017,253** | 23,017,253 | – |
| Roger Devlin | **–** | – | – |
| Sir Andrew Foster | **–** | – | – |
| Barry Gibson | **3,000** | 3,000 | – |
| David Ross | **3,002,201** | 2,000,000 | 3,003,809 |
| Tim Score | **–** | – | – |

In order to align the interests of the Directors more closely with the shareholders, the Remuneration Committee has also determined that the Executive Directors should build up a share fund equal to at least one year's salary over a period of five years.

**Share Option Awards**

| | Note | At 1 January 2007 | During year: Granted | During year: Exercised | During year: Lapsed | **At 31 December 2007** | Option price | Market price at date of exercise | Date from which exercisable | Expiry date |
|---|---|---|---|---|---|---|---|---|---|---|
| Ray O'Toole | (i ,ii) | 431 | – | – | 431 | **–** | 585.0p | – | 05.07.05 | 05.07.12 |
| | (i, iii) | 92,511 | – | 92,511 | – | **–** | 681.0p | 1263p | 12.05.07 | 12.05.14 |
| Adam Walker | (i, ii) | 187 | – | – | 187 | **–** | 585.0p | – | 05.07.05 | 05.07.12 |
| (resigned 26 March 2008 | (i, iii) | 76,358 | – | 76,358 | – | **–** | 681.0p | 1263p | 12.05.07 | 12.05.14 |

Notes
(i) Options granted under the 2002 National Express Group Executive Share Option Plan Part 2 Unapproved.
(ii) The performance condition is as follows: (a) for awards up to 50% of salary; EPS growth of RPI +4% pa, (b) for awards between 51% of salary and up to 100% of salary; EPS growth of RPI +6% pa, (c) for awards between 101% of salary and up to 150% of salary; EPS growth of RPI + 8% pa, (d) for awards between 151% of salary and up to 200% of salary; EPS growth of RPI + 10% pa. Parts (a) and (b) are initially tested over years 0–3 with a facility to retest over years 0–4 and 0-5. Parts (c) and (d) are not subject to retesting. Straight-line vesting occurs between EPS levels.
(iii) The performance condition is as follows: (a) for awards up to 50% of salary; EPS growth of RPI + 4% pa, (b) for awards between 51% of salary and up to 100% of salary; EPS growth of RPI + 5% pa, (c) for awards between 101% of salary and up to 150% of salary; EPS growth of RPI + 6% pa, (d) for awards between 151% of salary and up to 200% of salary; EPS growth of RPI + 10% pa. Performance is tested over years 0–3. Straight-line vesting occurs between EPS levels. Retesting is not permitted.

**Long Term Incentive Plan (LTIP) Awards**
Performance shares of 1 x salary are awarded to Executive Directors as nil cost options under the Long Term Incentive Plan.
In addition 100 matching shares are awarded for every 30 investment shares pledged or invested by the Director under the share matching element of the LTIP. Further details of the LTIP and the applicable performance conditions are shown on page 49.

| | LTIP Share Awards | At 1 January 2007 | During year Granted | During year Exercised | During year Lapsed | **At 31 December 2007** | Market price on date of award | Market price at date of exercise | Date from which exercisable | Expiry date |
|---|---|---|---|---|---|---|---|---|---|---|
| Richard Bowker | Performance shares | 48,590 | – | – | – | **48,590** | 1032.5p | – | 09.11.09 | 09.05.10 |
| | Matching shares | 8,513 | – | – | – | **8,513** | 1032.5p | – | 09.11.09 | 09.05.10 |
| | Performance shares | – | 37,878 | – | – | **37,878** | 1320.0p | – | 11.04.10 | 11.10.10 |
| | Matching shares | – | 16,666 | – | – | **16,666** | 1320.0p | – | 11.04.10 | 11.10.10 |
| Ray O'Toole | Performance shares | 35,287 | – | – | – | **35,287** | 921.0p | – | 27.06.08 | 27.12.08 |
| | Matching shares | 56,613 | – | – | – | **56,613** | 921.0p | – | 27.06.08 | 27.12.08 |
| | Performance shares | 38,814 | – | – | – | **38,814** | 931.0p | – | 06.04.09 | 06.10.09 |
| | Matching shares | 24,600 | – | – | – | **24,600** | 931.0p | – | 06.04.09 | 06.10.09 |
| | Performance shares | – | 28,409 | – | – | **28,409** | 1320.0p | – | 11.04.10 | 11.10.10 |
| Adam Walker (resigned 26 March 2008) | Performance shares | 32,573 | – | – | – | **32,573** | 921.0p | – | 27.06.08 | 27.12.08 |
| | Matching shares | 32,333 | – | – | – | **32,333** | 921.0p | – | 27.06.08 | 27.12.08 |
| | Performance shares | 34,501 | – | – | – | **34,501** | 931.0p | – | 06.04.09 | 06.10.09 |
| | Matching shares | 32,333 | – | – | – | **32,333** | 931.0p | – | 06.04.09 | 06.10.09 |
| | Performance shares | – | 27,272 | – | – | **27,272** | 1320.0p | – | 11.04.10 | 11.10.10 |
| | Matching shares | – | 18,666 | – | – | **18,666** | 1320.0p | – | 11.04.10 | 11.10.10 |

In respect of the operation of the Long Term Incentive Plan the Company operates the National Express Group Employee Benefit Trust which currently holds 184,019 shares as at 28 February 2008.

The Register of Directors' Interests maintained by the Company contains full details of the Directors' holdings of shares and options over shares in the Company. The aggregate gain between the option price and market price on date of exercise of share options by the Directors during the year was £982,818 (2006: £2,286,881). The mid-market price of the Company's ordinary shares at 31 December 2007 was 1242p (2006: 1130p) and the range during the year ended 31 December 2007 was 1040p to 1320p.

By Order of the Board

**J M B Gibson**
Director and Chairman of the Remuneration Committee
28 February 2008

# Independent Auditors' Report to the Members of National Express Group PLC

We have audited the Group financial statements of National Express Group PLC for the year ended 31 December 2007 which comprise the Group Income Statement, the Group Balance Sheet, the Group Statement of Cash Flows, the Group Statement of Recognised Income and Expense and the related notes 1 to 38. These Group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of National Express Group PLC for the year ended 31 December 2007 and on the information in the Directors' Remuneration Report that is described as having been audited.

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

**Respective responsibilities of directors and auditors**

The Directors' responsibilities for preparing the Annual Report and the Group financial statements in accordance with applicable 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 Group 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 Group financial statements give a true and fair view and whether the Group 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 whether in our opinion the information given in the Directors' Report is consistent with the financial statements. The information given in the Directors' Report includes that specific information presented in the Operating and Financial Review that is cross referred from the Business Review section of the Directors' Report.

In addition we report to you if, in our opinion, 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 2006 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 Group financial statements. The other information comprises only the Chairman's Statement, the Chief Executive's Statement, the Operating and Financial Review, the Corporate Governance Statement, the Statement of Directors' Responsibilities, the unaudited part of the Directors' Remuneration Report and the Directors' Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the group 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 group financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the group financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the group 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 group financial statements.

**Opinion**

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 December 2007 and of its profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the Directors' Report is consistent with the Group financial statements.

**Ernst & Young LLP**
Registered Auditor
London
28 February 2008

# Group Income Statement

## For the year ended 31 December 2007

| | Note | Total before goodwill impairment, intangible amortisation and exceptional items 2007 £m | Goodwill impairment, intangible amortisation and exceptional items 2007 £m | Total 2007 £m | Total before goodwill impairment, intangible amortisation and exceptional items 2006 £m | Goodwill impairment, intangible amortisation and exceptional items 2006 £m | Total 2006 £m |
|---|---|---|---|---|---|---|---|
| **Continuing operations** | | | | | | | |
| Revenue | 4 | **2,615.4** | **–** | **2,615.4** | 2,525.5 | – | 2,525.5 |
| Operating costs before goodwill impairment, intangible amortisation and exceptional items | | **(2,409.8)** | **–** | **(2,409.8)** | (2,340.7) | – | (2,340.7) |
| Goodwill impairment | 5 | **–** | **–** | **–** | – | (20.2) | (20.2) |
| Intangible amortisation | 5 | **–** | **(27.5)** | **(27.5)** | – | (27.8) | (27.8) |
| Exceptional items | 5 | **–** | **(15.8)** | **(15.8)** | – | 4.8 | 4.8 |
| Total operating costs | 6 | **(2,409.8)** | **(43.3)** | **(2,453.1)** | (2,340.7) | (43.2) | (2,383.9) |
| **Group operating profit** | | **205.6** | **(43.3)** | **162.3** | 184.8 | (43.2) | 141.6 |
| Profit on disposal of non-current assets | 5 | **–** | **16.2** | **16.2** | – | 16.9 | 16.9 |
| Profit from operations | | **205.6** | **(27.1)** | **178.5** | 184.8 | (26.3) | 158.5 |
| Share of post tax results from associates and joint ventures accounted for using the equity method | 18 | **0.4** | **–** | **0.4** | (3.8) | (25.7) | (29.5) |
| Finance income | 9 | **17.0** | **–** | **17.0** | 12.4 | – | 12.4 |
| Finance costs | 9 | **(46.0)** | **–** | **(46.0)** | (37.3) | – | (37.3) |
| **Profit before tax** | | **177.0** | **(27.1)** | **149.9** | 156.1 | (52.0) | 104.1 |
| Tax expense | 10 | **(48.1)** | **10.5** | **(37.6)** | (39.2) | 15.6 | (23.6) |
| Profit after tax for the year from continuing operations | | **128.9** | **(16.6)** | **112.3** | 116.9 | (36.4) | 80.5 |
| Loss for the year from discontinued operations | 11 | **–** | **(2.9)** | **(2.9)** | – | (3.2) | (3.2) |
| **Profit for the year** | | **128.9** | **(19.5)** | **109.4** | 116.9 | (39.6) | 77.3 |
| Profit attributable to equity shareholders | | **128.4** | **(19.5)** | **108.9** | 116.1 | (39.6) | 76.5 |
| Profit attributable to minority interests | | **0.5** | **–** | **0.5** | 0.8 | – | 0.8 |
| | | **128.9** | **(19.5)** | **109.4** | 116.9 | (39.6) | 77.3 |
| Earnings per share: | | | | | | | |
| – basic earnings per share | 13 | | | **71.7p** | | | 50.7p |
| – diluted earnings per share | 13 | | | **71.2p** | | | 50.4p |
| Normalised earnings per share: | | | | | | | |
| – basic earnings per share | 13 | **84.5p** | | | 77.0p | | |
| – diluted earnings per share | 13 | **83.9p** | | | 76.5p | | |
| Earnings per share from continuing operations: | | | | | | | |
| – basic earnings per share | 13 | | | **73.6p** | | | 52.8p |
| – diluted earnings per share | 13 | | | **73.1p** | | | 52.5p |
| Dividends per ordinary share: | | | | | | | |
| – interim | 12 | | | **11.56p** | | | 10.75p |
| – final | 12 | | | **26.40p** | | | 24.00p |
| | | | | **37.96p** | | | 34.75p |

Dividends of £54.0m were declared and payable during the year (2006: £50.1m). Dividends of £57.8m were proposed for approval during the year (2006: £52.5m).

# Group Balance Sheet

## At 31 December 2007

| | Note | 2007 £m | 2006 £m |
|---|---|---|---|
| **Non-current assets** | | | |
| Intangible assets | 14 | **1,173.9** | 697.6 |
| Property, plant and equipment | 15 | **678.7** | 501.9 |
| Financial assets – Available for sale | 17 | **7.2** | 13.5 |
| – Derivative financial instruments | 17 | **5.3** | 0.3 |
| Investments accounted for using the equity method | 18 | **11.8** | 8.7 |
| Other receivables | 20 | **10.0** | 4.1 |
| Deferred tax asset | 27 | **–** | 10.6 |
| | | **1,886.9** | 1,236.7 |
| **Current assets** | | | |
| Inventories | 21 | **20.0** | 15.5 |
| Trade and other receivables | 22 | **272.4** | 272.3 |
| Financial assets – Derivative financial instruments | 17 | **10.0** | 8.1 |
| Current tax assets | | **9.5** | 26.4 |
| Cash and cash equivalents | 23 | **157.2** | 143.6 |
| | | **469.1** | 465.9 |
| Disposal group assets classified as held for sale | | **–** | 20.1 |
| **Total assets** | | **2,356.0** | 1,722.7 |
| **Non-current liabilities** | | | |
| Financial liabilities – Borrowings | 28 | **(641.6)** | (538.4) |
| – Derivative financial instruments | 28 | **(5.4)** | (8.3) |
| Deferred tax liability | 27 | **(104.0)** | (84.3) |
| Other non-current liabilities | 25 | **(3.7)** | (3.0) |
| Defined benefit pension liability | 35 | **(29.8)** | (52.8) |
| Provisions | 26 | **(43.5)** | (61.3) |
| | | **(828.0)** | (748.1) |
| **Current liabilities** | | | |
| Trade and other payables | 24 | **(573.3)** | (518.4) |
| Financial liabilities – Borrowings | 28 | **(426.4)** | (43.6) |
| – Derivative financial instruments | 28 | **(17.7)** | (6.4) |
| Current tax liabilities | | **(24.7)** | (40.9) |
| Provisions | 26 | **(44.8)** | (17.4) |
| | | **(1,086.9)** | (626.7) |
| Liabilities directly associated with disposal group assets classified as held for sale | | **–** | (2.4) |
| **Total liabilities** | | **(1,914.9)** | (1,377.2) |
| **Net assets** | | **441.1** | 345.5 |
| **Shareholders' equity** | | | |
| Called up share capital | 32 | **7.7** | 7.7 |
| Share premium account | 33 | **195.3** | 189.8 |
| Capital redemption reserve | 33 | **0.2** | 0.2 |
| Own shares | 33 | **(16.3)** | (16.7) |
| Other reserves | 34 | **30.7** | 7.9 |
| Retained earnings | 33 | **219.6** | 153.3 |
| Total shareholders' equity | | **437.2** | 342.2 |
| Minority interest in equity | 33 | **3.9** | 3.3 |
| **Total equity** | | **441.1** | 345.5 |

**S R Bowker CBE** Chief Executive
**A C Walker** Finance Director
28 February 2008

# Group Statement of Cash Flows

## For the year ended 31 December 2007

| | Note | 2007 £m | 2006 £m |
|---|---|---|---|
| **Cash generated from operations** | 38 | **272.1** | 254.5 |
| Tax paid | | **(18.8)** | (9.0) |
| **Net cash from operating activities** | | **253.3** | 245.5 |
| **Cash flows from investing activities** | | | |
| Payments to acquire businesses, net of cash acquired | 19a) | **(485.0)** | (19.8) |
| Deferred consideration for businesses acquired | | **(1.7)** | (3.0) |
| Purchase of property, plant and equipment | | **(149.7)** | (73.5) |
| Proceeds from disposal of property, plant and equipment | | **22.9** | 24.3 |
| Payments to acquire available for sale investments | | **–** | (4.6) |
| Payments to acquire associates | | **–** | (1.5) |
| Receipts from disposal of available for sale investments | | **10.7** | 13.2 |
| Receipts from disposal of businesses, net of cash disposed | 19b) | **34.3** | – |
| Payments in respect of discontinued operations | 11 | **(1.9)** | – |
| Receipts from disposal of intangible assets | | **–** | 1.5 |
| Interest received | | **17.0** | 12.4 |
| **Net cash used in investing activities** | | **(553.4)** | (51.0) |
| **Cash flows from financing activities** | | | |
| Proceeds from issue of ordinary shares | | **5.5** | 15.8 |
| Purchase of treasury shares | | **–** | (11.6) |
| Interest paid | | **(39.5)** | (32.1) |
| Finance lease principal payments | | **(26.3)** | (21.5) |
| Net loans advanced/(repaid) | | **424.9** | (89.9) |
| Loans receivable repaid | | **–** | 1.0 |
| Dividends paid to minority interests | | **(0.1)** | – |
| Dividends paid to shareholders of the Company | | **(53.9)** | (49.7) |
| **Net cash from/(used in) financing activities** | | **310.6** | (188.0) |
| **Increase in cash and cash equivalents** | | **10.5** | 6.5 |
| Opening cash and cash equivalents | | **143.6** | 140.0 |
| Increase in cash and cash equivalents | | **10.5** | 6.5 |
| Foreign exchange | | **3.1** | (2.9) |
| **Closing cash and cash equivalents** | 23 | **157.2** | 143.6 |

# Group Statement of Recognised Income and Expense

## For the year ended 31 December 2007

| | Note | 2007 £m | 2006 £m |
|---|---|---|---|
| **Income and expense recognised directly in equity** | | | |
| Exchange differences on retranslation of foreign operations | | **83.2** | (55.3) |
| Exchange differences on retranslation of foreign currency borrowings | | **(89.1)** | 46.8 |
| Exchange differences on retranslation of minority interests | | **0.2** | – |
| Actuarial gains on defined benefit pension plans | 35 | **11.7** | 20.6 |
| Gain/(loss) on cash flow hedges taken to equity | | **21.5** | (12.1) |
| | | **27.5** | – |
| **Transfers to the income statement** | | | |
| On cash flow hedges | | **(1.0)** | 1.6 |
| | | **(1.0)** | 1.6 |
| Tax on exchange differences | | **14.3** | (1.3) |
| Tax on share-based payments | | **0.4** | 2.4 |
| Deferred tax on actuarial gains | | **(3.5)** | (6.2) |
| Deferred tax on cash flow hedges | | **(6.1)** | 3.7 |
| Tax on items taken directly to or transferred from equity | | **5.1** | (1.4) |
| Net profit recognised directly in equity | | **31.6** | 0.2 |
| Profit for the financial year | | **108.9** | 76.5 |
| Profit attributable to minority interests | | **0.5** | 0.8 |
| **Total recognised income and expense for the year** | | **141.0** | 77.5 |
| Income and expense attributable to equity shareholders | | **140.3** | 76.7 |
| Income attributable to minority interests | | **0.7** | 0.8 |
| | | **141.0** | 77.5 |

# Notes to the Consolidated Accounts

## For the year ended 31 December 2007

### 1 Corporate information

The consolidated accounts of National Express Group PLC for the year ended 31 December 2007 were authorised for issue in accordance with a resolution of the Directors on 28 February 2008 and the balance sheets were signed on the Board's behalf by S R Bowker and A C Walker. National Express Group PLC is a limited company incorporated in England and Wales whose shares are publicly traded on the London Stock Exchange.

The principal activities of the Group are described in the Operating and Financial Review ("OFR") that accompanies these accounts.

### 2 Accounting policies

#### Statement of compliance

These accounts have been prepared in accordance with International Financial Reporting Standards ("IFRS") and the International Financial Reporting Interpretations Committee's ("IFRIC") interpretations as adopted by the European Union ("EU"), and with those parts of the Companies Act 1985 applicable to companies reporting under IFRS. The Group is required to comply with international accounting requirements under IAS 1 "Presentation of Financial Information" except in extremely rare circumstances where management concludes that compliance would be so misleading that it would conflict with the objective to "present fairly" its accounts. On this basis, the Group has departed from the requirements of IAS 19 "Employee Benefits" and has accounted for its constructive but not legal obligations for the Railways Pension Scheme ("RPS") under the terms of its UK rail franchise agreements. Details of the background and rationale for this departure are provided in note 35, including the impact on the Group's reported financial performance and position of adopting this accounting treatment as required by IAS 1.

#### Basis of preparation

The financial statements have been prepared under the historical cost convention, except for the recognition of derivative financial instruments and available for sale investments detailed below.

As noted above, the Group has taken the extremely rare decision to depart from the requirement of IAS 19 "Employee Benefits" so as to present fairly its financial performance, position and cash flows in respect of its obligation for the RPS. The details of this departure and impact on the Group's accounts are set out in note 35.

A summary of the Group's accounting policies applied in preparing the accounts for the year ended 31 December 2007 is set out below.

The preparation of accounts in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the accounts and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge, actual results ultimately may differ from those estimates.

The key sources of estimation uncertainty that have a significant risk of causing material adjustments to the carrying amounts of assets and liabilities within the next financial year are the measurement and impairment of indefinite life intangible assets (including goodwill) and measurement of defined benefit pension obligations. The measurement of intangible assets other than goodwill on a business combination involves estimation of future cash flows and the selection of a suitable discount rate. The Group determines whether indefinite life intangible assets are impaired on an annual basis and this requires an estimation of the value in use of the cash-generating units to which the intangible assets are allocated. This requires estimation of future cash flows and choosing a suitable discount rate (see note 14). Measurement of defined benefit pension obligations requires estimation of future changes in salaries and inflation, as well as mortality rates, the expected return on assets and the choice of a suitable discount rate (see note 35).

The consolidated accounts are presented in pounds sterling and all values are rounded to the nearest one hundred thousand pounds (£0.1m) except where otherwise indicated.

#### Basis of consolidation

The consolidated accounts comprise the accounts of National Express Group PLC and all its subsidiaries drawn up to 31 December each year. Adjustments are made to bring any dissimilar accounting policies that may exist into line with the Group's accounting policies.

On acquisition of a business, the purchase method of accounting is adopted, and the Group income statement includes the results of subsidiaries and businesses purchased during the year from the date control is assumed. The purchase consideration is allocated to assets and liabilities on the basis of fair value at the date of acquisition. On the sale of a business, the Group income statement includes the results of that business to the date of disposal.

Minority interests represent the portion of profit or loss and net assets in subsidiaries that is not attributable to the parent Company shareholders and is presented separately from parent shareholders' equity in the consolidated balance sheet.

#### Interests in joint ventures

The Group has a number of contractual arrangements with other parties which represent joint ventures which take the form of agreements to share control of other entities.

The Group recognises its interest in the entity's assets and liabilities using the equity method of accounting. The Group balance sheet includes the appropriate share of these joint ventures' net assets and the income statement includes the appropriate share of their results after tax.

Accounts of jointly controlled entities are prepared for the same reporting period as the Group. Adjustments are made in the Group's accounts to eliminate the Group's share of unrealised gains and losses on transactions between the Group and its jointly controlled entities. The Group ceases to use the equity method from the date it no longer has joint control over the entity.

#### Interests in associates

Companies, other than subsidiaries and joint ventures, in which the Group has an investment representing not less than 20% of the voting rights and over which it exerts significant influence are treated as associates. The Group accounts include the appropriate share of these associates' results and net assets based on their latest accounts under the equity method.

# Notes to the Consolidated Accounts continued

**2 Accounting policies (continued)**
**Income statement presentation**
The income statement has been presented in a columnar format to highlight the impact of intangible assets amortisation and exceptional items. This is to enable users of the financial statements to view the normalised results of the Group. Normalised results are defined as the statutory results before the following as appropriate: profit or loss on the sale of businesses, exceptional profit or loss on the sale of non-current assets and charges for goodwill impairment, amortisation of intangible assets, exceptional items and tax relief on qualifying exceptional items.

**Exceptional items**
Exceptional items are material items of income or expenditure which, in the opinion of the Directors, due to their nature and infrequency require separate identification on the face of the income statement to allow a better understanding of the financial performance in the year, in comparison to prior years.

**Revenue recognition**
Rendering of services
Revenue comprises income from road passenger transport, train passenger services, airport operations and related activities in the UK, North America and Europe. Where appropriate, amounts are shown net of rebates and sales tax.

Revenue is recognised by reference to the stage of completion of the customer's travel or services provided under contractual arrangements as a proportion of total services to be provided.

UK Trains revenue includes amounts attributed to the train operating companies ("TOCs"), based principally on agreed models of route usage, by Railway Settlement Plan Limited (which administers the income allocation system within the UK rail industry), in respect of passenger receipts. In addition, franchise agreement receipts from the Department for Transport Rail Division ("DfT Rail") and local Passenger Transport Executives ("PTEs") are treated as revenue. Franchise agreement payments to DfT Rail are recognised in operating costs. UK Coach revenue comprises amounts receivable generated from ticket sales. UK Bus and European Coach & Bus revenue comprises amounts receivable generated from ticket sales and revenue generated from services provided on behalf of local transport authorities, which is recognised as the services are provided. For all the divisions noted above, the relevant share of season ticket or travelcard income is deferred within liabilities and released to the income statement over the life of the relevant season ticket or travelcard. North American Bus revenue from school boards and similar contracts is recognised as the services are provided.

Rental income
Rental income is accounted for on a straight-line basis over the lease term.

Interest income
Revenue is recognised using the effective interest method.

**Government grants**
Government grants relating to property, plant and equipment are included in liabilities as deferred income and are credited to the income statement over the expected useful economic life of the assets concerned. Other grants are credited to the income statement as the related expenditure is expensed.

**Segmental reporting**
Each of the Group's business and geographical segments provides services that are subject to risks and returns that are different from those of the other business segments. Due to the nature of the Group's operations the distinct business segments align directly with geographical segments which are operating in separate economic environments.

The Group's segments comprise: UK Bus; UK Coach; UK Trains; North American Bus; European Coach & Bus; and Central functions. These segments are described in more detail in the OFR accompanying these accounts.

Operations in our North America – Public Transit business was discontinued in 2005.

The net assets of Stewart International Airport were disclosed in "disposal group assets classified as held for sale" and liabilities disclosed in "liabilities directly associated with disposal group assets classified as held for sale" at 31 December 2006 reflecting the sale of this business in 2007.

**Leases**
Leases of property, plant and equipment where substantially all the risks and rewards of ownership of the asset have passed to the Group, are capitalised in the balance sheet as property, plant and equipment. Finance leases are capitalised at the lower of the fair value of the leased property and the present value of the minimum lease payments. The capital element of future obligations under hire purchase contracts and finance leases is included as a liability in the balance sheet. The interest element of rental obligations is charged to the income statement over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding. Property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset or the lease term.

Leases of property, plant and equipment where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Rentals paid under operating leases are charged to the income statement on a straight-line basis over the term of the lease. Incentives received under operating leases and initial direct costs in negotiating the lease are amortised to the income statement on a straight-line basis over the term of lease.

All material arrangements and transactions entered into by the Group are reviewed to check whether they contain elements that meet the accounting definition of a lease, although they may not follow the legal form of a lease.

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

## 2 Accounting policies (continued)

### Current tax and deferred tax

Current tax is provided on taxable profits earned according to the local tax rates applicable where the profits are earned. Income taxes are recognised in the income statement unless it relates to an item accounted for in equity, in which case the tax is recognised directly in equity.

Deferred tax is provided in full in respect of all material temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes, apart from the following exceptions:

- where the temporary difference arises from the initial recognition of goodwill;
- where an asset or liability is recognised in a transaction that is not a business combination and that at the time of the transaction affects neither accounting nor taxable profit or loss; and
- in respect of investment in subsidiaries, associates and joint ventures where the Group is able to control the reversal of the temporary difference and it is probable the temporary difference will not reverse in the foreseeable future.

Deferred tax is measured on a non-discounted basis at tax rates that are expected to apply in the periods in which the temporary differences reverse based on tax rates and laws enacted or substantively enacted at the balance sheet date.

Deferred tax assets are recognised where their recovery is considered more likely than not in that there will be taxable profits from which the future reversal of underlying temporary differences can be deducted. Their carrying amount is reviewed at each balance sheet date on the same basis.

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

### Intangible assets

Intangible assets acquired separately that meet the recognition criteria of IAS 38, “Intangible Assets”, are capitalised at cost and when acquired in a business combination are capitalised at fair value at the date of acquisition. Following initial recognition, finite life assets are amortised on a straight-line basis and indefinite life assets are not amortised. The amortisation expense is taken to the income statement through operating expenses.

The existing finite life intangible assets have a residual value of nil and are amortised over their estimated useful lives as follows:

Customer contracts – over the life of the contract (between 1 and 33 years)
Right to operate TOC franchises – over the life of the franchise (between 1 and 7 years)

Intangible assets with indefinite lives are tested annually for impairment and the useful lives of finite life intangible assets are examined on an annual basis and adjustments, where applicable, are made on a prospective basis. Finite life assets are reviewed for impairment where indicators of impairment exist.

The Group’s indefinite life intangible assets include customer relationships and goodwill. Customer relationship intangible assets are recognised only on contracts where historical experience has shown that these contracts are consistently renewed.

### Goodwill

IFRS 3 “Business Combinations”, has been applied to the accounting for business combinations from 1 January 2004, as permitted by IFRS 1.

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the Group’s interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is stated at historic cost less any accumulated impairment. If an acquisition gives rise to an excess of the acquirer’s interest in the net fair value of the acquiree’s identifiable assets, liabilities and contingent liabilities over cost (previously referred to as negative goodwill), this is credited immediately to the income statement.

In accordance with IFRS 3 “Business Combinations”, goodwill is not amortised. All goodwill is subject to an annual test of impairment and an impairment charge recognised as required.

Fair value accounting adjustments are made in respect of acquisitions. Fair value adjustments based on provisional estimates are amended within one year of the acquisition if required, with a corresponding adjustment to goodwill, in order to refine adjustments to reflect further evidence gained post acquisition.

Where goodwill forms part of a cash-generating unit and all or part of that unit is disposed of, the associated goodwill is included in the carrying amount of the operation when determining the gain or loss on the disposal of the operation.

### Property, plant and equipment

All property, plant and equipment is stated at historic cost less accumulated depreciation and any impairment. Under the transitional arrangements of IFRS 1 the Group has elected to deem the fair value of certain revalued assets to be equivalent to cost.

Land and buildings comprise mainly vehicle depots and garages, and offices. Freehold land is not depreciated. Other property, plant and equipment are depreciated on a straight-line basis over their estimated useful lives as follows:

Freehold buildings – 30 to 50 years
Long leasehold property improvements – 15 to 40 years
Public service vehicles – 8 to 15 years
Plant and equipment, fixtures and fittings – 3 to 15 years

The carrying value of items of property, plant and equipment are reviewed for impairment if events or changes in circumstances indicate that the current carrying value may not be recoverable, and are written down immediately to their recoverable amount. Useful lives and residual values are reviewed annually and adjustments, where applicable, are made on a prospective basis. Repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

# Notes to the Consolidated Accounts continued

**2 Accounting policies (continued)**
An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the derecognition of the asset is included in the income statement in the period of derecognition.

**Impairment of non-current assets**
All non-current assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, except for indefinite life intangible assets and goodwill which are reviewed annually. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount which is the higher of an asset's fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash inflows.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognised in the income statement in expense categories consistent with the function of the impaired asset.

Except for goodwill impairments, a review is made at each reporting date of any previous impairment losses to assess whether they no longer exist or may have decreased. If such indication exists, the asset's recoverable amount is estimated and any previously recognised impairment loss is reversed only if there has been a change in the estimates used to assess the recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased, subject to a limit of the asset's net book value had no previous impairment loss been recognised. Such reversal is recognised in the income statement. Future depreciation or amortisation is then adjusted to allocate the asset's revised carrying amount over its remaining useful economic life. Impairments to goodwill cannot be reversed.

**Financial instruments**
The Group determines the classification of its financial instruments at initial recognition. When financial instruments are recognised initially, they are measured at fair value, including directly attributable transaction costs.

Financial assets held by the Group include certain derivative contracts and investments in entities that are not subsidiaries, associates or joint ventures.

Available for sale financial assets
The Group's investments in entities that are not subsidiaries, associates or joint ventures are classified as available for sale financial assets. After initial recognition these assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or the investment is determined to be impaired, at which time the previously reported cumulative gain or loss is included in the income statement. Where there is no active market for the Group's investments, fair value is determined using valuation techniques including recent commercial transactions and discounted cash flow analyses. In the absence of any other reliable external information, assets are carried at amortised cost.

Derivative financial instruments
The Group uses derivative financial instruments such as foreign currency forward exchange contracts, fuel price swaps and interest rate swaps to hedge its risks associated with foreign currency, fuel price and interest rate fluctuations. Such derivative financial instruments are initially recognised at fair value and subsequently remeasured to fair value for the reported balance sheet. The fair value of foreign currency forward exchange contracts, interest rate and fuel price swaps is calculated by reference to market exchange rates, interest rates and fuel prices at the period end.

The Group's fuel price swaps and interest rate swaps are designated as cash flow hedges. The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity, and the ineffective portion in the income statement. The gains or losses deferred in equity in this way are recycled through the income statement in the same period in which the hedged underlying transaction or firm commitment is recognised in the income statement.

Foreign currency forward currency contracts are used to hedge the Group's net investment in foreign currency denominated operations and to the extent they are designated and effective as net investment hedges are matched in equity against foreign exchange exposure in the related assets and liabilities.

For derivatives that do not qualify for hedge accounting, gains or losses are taken directly to the income statement in the period.

Hedge accounting is discontinued when the hedging instrument expires, is sold, terminated or exercised, or no longer qualifies for hedge accounting.

Trade and other receivables
Trade and other receivables are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. Doubtful debts are provided for when collection of the full amount is no longer probable, whilst bad debts are written off when identified.

Pre-contract costs
Pre-contract costs associated with securing new rail franchises are expensed as incurred up to the point when a franchise is awarded. From this point in time, they are recognised as an asset and are expensed to the income statement over the life of the franchise.
Costs associated with the commencement of all new contracts other than rail franchises are expensed as incurred.

Cash and cash equivalents
Cash and cash equivalents as defined for the cash flow statement comprise cash in hand, cash held at bank with immediate access, other short-term investments and bank deposits with maturities of three months or less from the date of inception and bank overdrafts.
In the consolidated balance sheet cash includes cash and cash equivalents excluding bank overdrafts. Bank overdrafts that have no legal right of set-off against cash and cash equivalents are included within borrowings in current liabilities.

## 2 Accounting policies (continued)

### Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost being the net fair value of the consideration received plus transaction costs that are directly attributable to the issue of the financial asset or liability. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Gains and losses are recognised in the income statement when the assets or liabilities are derecognised or impaired, as well as through the amortisation process.

### Inventories

Inventories are valued at the lower of cost and net realisable value on a FIFO basis, after making due allowance for obsolete or slow moving items.

### Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material using a pre-tax discount rate. The amortisation of the discount is recognised as a finance cost.

### Insurance

The Group's policy is to self-insure high frequency claims within the businesses. To provide protection above these types of losses the Group purchases insurance cover from a selection of proven and financially strong insurers. The insurance provision is based on estimated exposures at the year end principally for claims arising in the UK and North America prior to the year end date, subject to the overall stop loss within the Group's insurance arrangements. The majority of provisions will be utilised within six years, and the provision has been discounted to take account of the expected timing of future cash settlements.

### Pensions and other post-employment benefits

The Group has a number of pension schemes, both of a defined benefit and defined contribution nature. Full details are provided in note 35 including the departure from IAS 19 required for the Group's RPS obligations as outlined in the Statement of Compliance.

The liability in respect of defined benefit schemes comprises the total for each scheme of the present value of the relevant defined benefit obligation at the balance sheet date less the fair value of plan assets. The trustees complete a full actuarial valuation triennially, separately for each plan, but the obligation is updated annually by independent actuaries for financial reporting purposes, using the projected unit credit method. The present value of the obligation is determined by the estimated future cash outflows using interest rates of high quality corporate bonds which have terms to maturity equivalent to the terms of the related liability.

The current service cost and gains and losses on settlements and curtailments are recognised in staff pension costs within operating costs in the income statement. Past service costs are included in operating costs where the benefits have vested, otherwise they are amortised on a straight-line basis over the vesting period. The finance elements of the pension cost, comprising the expected return on assets of funded defined benefit schemes and the interest on pension scheme liabilities, are also included in operating costs. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to the statement of recognised income and expense in the period in which they arise.

Our TOCs participate in the RPS, a defined benefit scheme which covers the whole of the UK Rail industry. This is partitioned into sections and the Group is responsible for the funding of these sections whilst it operates the relevant franchise. In contrast to the pension schemes operated by most businesses, the RPS is a shared cost scheme, which means that costs are formally shared 60% by the employer and 40% by the employee. A liability is recognised in line with other defined benefit schemes in the Group, although this is offset by a franchise adjustment so that the net liability represents the deficit that the Group expects to fund during the franchise term. This represents a departure from IAS 19 so as to present fairly the Group's financial performance, position and cash flow in respect of its obligations for the RPS.

The charges in respect of defined contribution schemes are recognised when they are due. The Group has no legal or constructive obligation to pay further contributions into a defined contribution scheme if the fund has insufficient assets to pay all employees benefits relating to employee service in the current and prior periods.

### Share-based payment

In accordance with the transitional provisions of IFRS 1, IFRS 2, 'Share-based Payment', has been applied only to equity-settled awards granted after 7 November 2002 that were unvested as of 1 January 2005.

The Group awards equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant by an external valuer using a stochastic model. Non-market-based performance-related vesting conditions are not taken into account when estimating the fair value; instead those non-market conditions are taken into account in calculating the current best estimate of the number of shares that will eventually vest and at each balance sheet date before vesting, the cumulative expense is calculated based on that estimate. Market-based performance conditions are taken into account when determining the fair value. The cumulative expense is calculated irrespective of whether or not the market conditions are satisfied, provided that all other performance conditions are met.

### Share capital, share premium and dividends

Where either the Company or employee share trusts purchase the Company's equity share capital, the consideration paid, including any transaction costs, is deducted from total shareholders' equity as Own shares until they are cancelled or reissued. Any consideration subsequently received on sale or re-issue is included in shareholders' equity.

Dividends are recorded as a liability in the period in which the liability to pay shareholders arises.

# Notes to the Consolidated Accounts continued

### 2 Accounting policies (continued)

**Foreign currencies**

The trading results of foreign currency denominated subsidiaries, joint ventures and associates are translated into sterling, the presentation currency of the Group and functional currency of the parent, using average rates of exchange for the year as a reasonable approximation to actual exchange rates at the dates of transactions.

The balance sheets of foreign currency denominated subsidiaries, joint ventures and associates are translated into sterling at the rates of exchange ruling at the year end and exchange differences arising are taken directly to the translation reserve in equity. On disposal of a foreign currency denominated subsidiary, the deferred cumulative amount recognised in the translation reserve (since 1 January 2004 under the transitional rules of IFRS 1) relating to that entity is recognised in the income statement. All other translation differences are taken to the income statement, with the exception of differences on foreign currency borrowings and forward foreign currency contracts which are used to provide a hedge against the Group net investments in foreign enterprises. These are taken directly to equity until the disposal of the net investment, at which time they are recognised in the income statement.

**New standards and interpretations not applied**

The IASB and IFRIC have issued the following standards and interpretations with an effective date after the date of these accounts:

| | | |
|---|---|---|
| **International Accounting Standards (IAS/IFRS)** | | |
| IFRS 2 | Amendment to IFRS 2 – Vesting Conditions and Cancellations | 1 January 2009 |
| IFRS 3 | Business Combinations (revised January 2008) | 1 July 2009 |
| IFRS 8 | Operating Segments | 1 January 2009 |
| IAS 1 | Presentation of Financial Statements (revised September 2007) | 1 January 2009 |
| IAS 23 | Borrowing Costs (revised March 2007) | 1 January 2009 |
| IAS 27 | Consolidated and Separate Financial Statements (revised January 2008) | 1 July 2009 |
| **International Financial Reporting Interpretations Committee (IFRIC)** | | |
| IFRIC 11 | IFRS 2 – Group and Treasury Share Transactions | 1 March 2007 |
| IFRIC 12 | Service Concession Arrangements | 1 January 2008 |
| IFRIC 13 | Customer Loyalty Programmes | 1 July 2008 |
| IFRIC 14 | IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction | 1 January 2008 |

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

### 3 Exchange rates

The most significant exchange rates to UK sterling for the Group are as follows:

| | **2007 Closing rate** | **2007 Average rate** | 2006 Closing rate | 2006 Average rate |
|---|---|---|---|---|
| US dollar | **1.98** | **2.00** | 1.96 | 1.85 |
| Canadian dollar | **1.98** | **2.15** | 2.28 | 2.09 |
| Euro | **1.36** | **1.46** | 1.48 | 1.47 |
| Australian dollar | **2.27** | **2.39** | 2.48 | 2.44 |

If the results for the year to 31 December 2006 had been retranslated at the average exchange rates for the year to 31 December 2007, North America would have achieved normalised operating profit of £36.5m on revenue of £264.5m, compared to normalised operating profit of £39.1m on revenue of £283.7m as reported, and Europe would have achieved a normalised operating profit of £44.5m on revenue of £250.5m, compared to normalised operating profit of £44.3m on revenue of £249.3m as reported.

### 4 Revenue

| | **2007 £m** | 2006 £m |
|---|---|---|
| Rendering of services | **2,607.2** | 2,517.6 |
| Rental income | **8.2** | 7.9 |
| Revenue | **2,615.4** | 2,525.5 |
| Finance income | **17.0** | 12.4 |
| Total revenue from continuing operations | **2,632.4** | 2,537.9 |

During the year, franchise agreement receipts from DfT Rail and PTEs amounted to £340.8m (2006: £377.1m) in UK Trains.

## 5 Segmental analysis

The operating businesses are organised and managed separately according to the nature of the public transport services they provide and the geographical market they operate in. Due to the nature of the services the Group provides, the primary and secondary segments coincide. Commentary on the segments is included in the OFR.

### Analysis by class and geography of business

| | **External revenue 2007 £m** | **Inter-segment sales 2007 £m** | **Segment revenue 2007 £m** | External revenue 2006 £m | Inter-segment sales 2006 £m | Segment revenue 2006 £m |
|---|---|---|---|---|---|---|
| UK Bus | **320.2** | **2.1** | **322.3** | 297.7 | 3.1 | 300.8 |
| UK Trains | **1,472.1** | **–** | **1,472.1** | 1,497.6 | – | 1,497.6 |
| UK Coach | **217.1** | **13.9** | **231.0** | 197.2 | 10.1 | 207.3 |
| Inter-segment sales elimination | **–** | **(16.0)** | **(16.0)** | – | (13.2) | (13.2) |
| UK operations | **2,009.4** | **–** | **2,009.4** | 1,992.5 | – | 1,992.5 |
| North American Bus | **308.0** | **–** | **308.0** | 283.7 | – | 283.7 |
| European Coach & Bus | **298.0** | **–** | **298.0** | 249.3 | – | 249.3 |
| **Total revenue from continuing operations** | **2,615.4** | **–** | **2,615.4** | 2,525.5 | – | 2,525.5 |

Inter-segment sales represent rail replacement services provided to UK Trains by UK Bus and UK Coach. Inter-segment trading is undertaken on standard arm's length commercial terms. Due to the nature of the Group's businesses, the origin and destination of revenue is the same.

| | **Continuing** | | | **Discontinued** | Continuing | | | Discontinued |
|---|---|---|---|---|---|---|---|---|
| | **Normalised operating profit 2007 £m** | **Goodwill impairment, intangible amortisation and exceptional items 2007 £m** | **Segment result 2007 £m** | **Segment result 2007 £m** | Normalised operating profit 2006 £m | Goodwill impairment, intangible amortisation and exceptional items 2006 £m | Segment result 2006 £m | Segment result 2006 £m |
| UK Bus | **43.5** | **(1.2)** | **42.3** | | 40.7 | 2.3 | 43.0 | |
| UK Trains | **63.3** | **(2.9)** | **60.4** | | 49.1 | (20.8) | 28.3 | |
| UK Coach | **23.1** | **(0.3)** | **22.8** | | 23.7 | 1.3 | 25.0 | |
| UK operations | **129.9** | **(4.4)** | **125.5** | | 113.5 | (17.2) | 96.3 | |
| North American Bus | **37.7** | **(13.3)** | **24.4** | | 39.1 | (4.5) | 34.6 | |
| European Coach & Bus | **50.9** | **(22.8)** | **28.1** | | 44.3 | (22.0) | 22.3 | |
| Central functions | **(12.9)** | **(2.8)** | **(15.7)** | | (12.1) | 0.5 | (11.6) | |
| **Result from continuing operations** | **205.6** | **(43.3)** | **162.3** | | 184.8 | (43.2) | 141.6 | |
| Profit on disposal of non-current assets | | | **16.2** | **–** | | | 16.9 | – |
| Profit from operations | | | **178.5** | **–** | | | 158.5 | – |
| Share of post tax results from associates and joint ventures | | | **0.4** | **–** | | | (29.5) | – |
| Loss on sale of discontinued operations | | | **–** | **(2.9)** | | | – | (3.2) |
| Net finance costs | | | **(29.0)** | **–** | | | (24.9) | – |
| Profit/(loss) before tax | | | **149.9** | **(2.9)** | | | 104.1 | (3.2) |
| Tax expense | | | **(37.6)** | **–** | | | (23.6) | – |
| Profit/(loss) for the year | | | **112.3** | **(2.9)** | | | 80.5 | (3.2) |

# Notes to the Consolidated Accounts continued

**5 Segmental analysis (continued)**

Goodwill impairment, intangible asset amortisation and exceptional items can be analysed by class and geography of business as follows:

| | **Intangible asset amortisation 2007 £m** | **Exceptional items 2007 £m** | **Total 2007 £m** |
|---|---|---|---|
| UK Bus | **1.1** | **0.1** | **1.2** |
| UK Trains | **1.1** | **1.8** | **2.9** |
| UK Coach | **–** | **0.3** | **0.3** |
| North American Bus | **5.1** | **8.2** | **13.3** |
| European Coach & Bus | **20.2** | **2.6** | **22.8** |
| Central functions | **–** | **2.8** | **2.8** |
| Total | **27.5** | **15.8** | **43.3** |

| | Goodwill impairment 2006 £m | Intangible asset amortisation 2006 £m | Exceptional items 2006 £m | Total 2006 £m |
|---|---|---|---|---|
| UK Bus | 1.0 | 1.6 | (4.9) | (2.3) |
| UK Trains | 19.2 | 1.6 | – | 20.8 |
| UK Coach | – | – | (1.3) | (1.3) |
| North American Bus | – | 4.5 | – | 4.5 |
| European Coach & Bus | – | 20.1 | 1.9 | 22.0 |
| Central functions | – | – | (0.5) | (0.5) |
| Total | 20.2 | 27.8 | (4.8) | 43.2 |

In the year to 31 December 2007 exceptional costs of £4.2m for UK Integration were incurred in UK Bus, UK Trains, UK Coach and Central functions. Mobilisation costs of £0.8m were incurred in National Express East Coast. Integration costs of £2.6m were incurred in Continental Auto. Business transformation costs of £8.2m were incurred in North America.

In the year to 31 December 2006 exceptional income arose in UK Bus, UK Coach and Central functions for a past service pension credit. Integration costs of £1.9m were incurred in Alsa.

In the year to 31 December 2007 non-operating exceptional items comprise £16.2m of profit on disposal of the trade and business of Stewart International Airport.

In 2006 non-operating exceptional items comprise £7.5m of profit on the disposal of property and £9.4m of profit on disposal of investments, both items relate to the UK Trains division.

Assets, liabilities and capital expenditure can be analysed by class and geography of business as follows:

| | **Assets 2007 £m** | **Liabilities 2007 £m** | **Capital expenditure 2007 £m** | Assets 2006 £m | Liabilities 2006 £m | Capital expenditure 2006 £m |
|---|---|---|---|---|---|---|
| UK Bus | **202.7** | **(104.1)** | **22.4** | 197.4 | (129.4) | 16.6 |
| UK Trains | **212.4** | **(366.6)** | **37.6** | 236.7 | (373.2) | 12.5 |
| UK Coach | **71.4** | **(57.1)** | **13.8** | 47.0 | (47.8) | 6.0 |
| Intercompany elimination | **(2.6)** | **2.6** | **–** | (1.4) | 1.4 | – |
| UK operations | **483.9** | **(525.2)** | **73.8** | 479.7 | (549.0) | 35.1 |
| North American Bus | **498.6** | **(86.2)** | **50.7** | 444.7 | (84.4) | 39.6 |
| European Coach & Bus | **1,199.5** | **(131.8)** | **32.6** | 593.8 | (63.9) | 23.5 |
| Central functions | **9.7** | **(77.6)** | **0.9** | (4.3) | (72.1) | 0.3 |
| Unallocated | **189.2** | **(1,119.0)** | **–** | 202.5 | (619.2) | – |
| Intercompany elimination | **(24.9)** | **24.9** | **–** | (13.8) | 13.8 | – |
| Total continuing operations | **2,356.0** | **(1,914.9)** | **158.0** | 1,702.6 | (1,374.8) | 98.5 |
| Disposal group assets/(liabilities directly associated with disposal group) classified as held for sale | **–** | **–** | **–** | 20.1 | (2.4) | – |
| Total | **2,356.0** | **(1,914.9)** | **158.0** | 1,722.7 | (1,377.2) | 98.5 |

Capital expenditure comprises property, plant and equipment additions as disclosed above and in note 15. In addition there were £nil (2006: £0.3m) of intangible asset additions in UK Trains as disclosed in note 14.

## 5 Segmental analysis (continued)

Unallocated assets and liabilities comprise the following items:

| | **Unallocated assets 2007 £m** | **Unallocated liabilities 2007 £m** | Unallocated assets 2006 £m | Unallocated liabilities 2006 £m |
|---|---|---|---|---|
| Cash and cash equivalents | **157.2** | **–** | 143.6 | – |
| Current tax | **9.5** | **(24.7)** | 26.4 | (40.9) |
| Available for sale investments | **7.2** | **–** | 13.5 | – |
| Derivative financial assets/(liabilities) | **15.3** | **(23.1)** | 8.4 | (14.7) |
| Borrowings, excluding finance leases | **–** | **(966.7)** | – | (478.9) |
| Dividend payable | **–** | **(0.5)** | – | (0.4) |
| Deferred tax | **–** | **(104.0)** | 10.6 | (84.3) |
| Total | **189.2** | **(1,119.0)** | 202.5 | (619.2) |

An operating cash flow and significant non-cash expenditure items by segment are included in the OFR.

## 6 Operating costs

| | | **2007 £m** | 2006 £m |
|---|---|---|---|
| Materials and consumables | | **107.6** | 108.2 |
| Staff costs (including exceptional cost of £5.0m (2006: income of £6.7m)) | | **819.6** | 775.1 |
| Depreciation – Owned assets | | **66.6** | 70.3 |
| – Leased assets | | **13.0** | 11.4 |
| Amortisation of leasehold property prepayment | | **0.1** | 0.6 |
| Amortisation of fixed asset grants | | **(1.3)** | (2.0) |
| Operating lease charges | Rolling stock: capital element | **150.5** | 168.8 |
| | Rolling stock: non-capital element | **61.1** | 68.1 |
| | Public service vehicles | **4.0** | 4.6 |
| | Other | **10.6** | 5.8 |
| | – Plant and equipment | **226.2** | 247.3 |
| | Fixed track access | **330.6** | 309.0 |
| | Other | **79.6** | 74.3 |
| | – Land and buildings | **410.2** | 383.3 |
| Pre-contract bid costs: UK Trains | | **7.5** | 9.8 |
| Foreign exchange differences | | **(0.3)** | – |
| Other charges (including exceptional expense of £10.8m (2006: £1.9m)) | | **776.4** | 731.9 |
| Operating costs before amortisation and impairment | | **2,425.6** | 2,335.9 |
| Goodwill impairment | | **–** | 20.2 |
| Intangible asset amortisation | | **27.5** | 27.8 |
| Total operating costs – continuing operations | | **2,453.1** | 2,383.9 |

The TOCs have fixed track access contracts with Network Rail Infrastructure Limited for access to the railway infrastructure (tracks, stations and depots). The TOCs also have contracts under which rolling stock is leased. The capital element of the rolling stock lease charge is based on the purchase price, capital funded refurbishments and modifications, and the non-capital element of the lease charge includes heavy maintenance charges, risk and charges based on mileage.

An analysis of fees paid to the Group's auditors is provided below:

| | **2007 £m** | 2006 £m |
|---|---|---|
| Fees payable to the Company's auditors for the audit of the consolidated and parent Company accounts | **0.4** | 0.3 |
| Fees payable to the Company's auditors and its associates for other services: | | |
| The audit of the Company's subsidiaries | **1.3** | 0.9 |
| Other services pursuant to legislation | **0.1** | 0.1 |
| Tax services | **0.5** | 0.9 |
| Corporate finance services | **0.2** | – |
| Other services | **–** | – |
| | **2.5** | 2.2 |

Included in the above fees paid to the Group's auditors are £508,000 (2006: £11,000) of fees capitalised with respect to acquisitions. Fees charged to the income statement for other services are £44,000 (2006: £17,000).

# Notes to the Consolidated Accounts continued

## 7 Employee benefit costs
### (a) Staff costs

| | 2007 £m | 2006 £m |
|---|---|---|
| Wages and salaries | **712.5** | 676.6 |
| Social security costs | **76.4** | 72.6 |
| Pension costs (see note 35) | **27.5** | 23.9 |
| Share-based payment (see note 8) | **3.2** | 2.0 |
| | **819.6** | 775.1 |

Included within wages and salaries are exceptional costs of £5.0m (2006: £nil), and included within pension costs is exceptional cost of £nil (2006: income of £6.7m).

The average number of employees, including Executive Directors, during the year was as follows:

| | 2007 | 2006 |
|---|---|---|
| Managerial and administrative | **4,123** | 3,733 |
| Operational | **37,431** | 35,781 |
| | **41,554** | 39,514 |

Included in the above costs are the following costs related to the Group's key management personnel who comprise the Directors of the parent Company.

| | 2007 £m | 2006 £m |
|---|---|---|
| Fees | **0.4** | 0.4 |
| Basic salaries | **1.2** | 1.2 |
| Benefits | **0.4** | 0.3 |
| Performance-related bonuses | **1.2** | 1.2 |
| Post-employment benefits | **0.1** | 0.3 |
| Share-based payment | **0.6** | 0.6 |
| | **3.9** | 4.0 |

Information concerning Directors' emoluments, shareholdings and options is disclosed in the Directors' Remuneration Report.

### (b) Share schemes
Details of options or awards outstanding as at 31 December 2007 under the Group's share schemes as follows:

| | Number of share options 2007 | Number of share options 2006 | Exercise price | Future exercise periods |
|---|---|---|---|---|
| Executive Share Option Plan | **216,925** | 1,060,076 | 398p–1224p | 2008–2014 |
| Long Term Incentive Plan | **1,054,170** | 1,102,793 | nil | 2008–2010 |
| Share Matching Plan | **222,676** | 155,596 | nil | 2008–2010 |
| Deferred Annual Share Bonus Scheme | **237,509** | 166,415 | nil | 2008–2010 |
| WMT Long Service Option Scheme | **177,527** | 325,922 | 398p–1224p | 2008–2017 |
| | **1,908,807** | 2,810,802 | | |

#### (i) Executive Share Option Plan
The Company operates tax approved and unapproved executive share option schemes open to Group employees in senior management positions and Executive Directors. Options granted by this Plan have a maximum term of between seven and ten years. The options vest after three years subject to the satisfaction of certain performance criteria, as disclosed in the Directors' Remuneration Report, based on the achievement of a target growth in earnings per share. If the performance criteria are not met when initially tested, in some instances they may be reassessed during the term of the option. From 2005 executive share option grants have been replaced by awards made under the Long Term Incentive Plan, as described in (ii). There are no cash settlement alternatives.

#### (ii) Long Term Incentive Plan (LTIP)
The LTIP was introduced in 2005 on the recommendation of the Remuneration Committee to replace the annual award under the Executive Share Option Plan to Executive Directors and to certain senior employees. Under the LTIP a Performance Award to acquire a specified number of free shares may be made to the employee or Director. In addition a Matching Award may be made, as described in (iii). Performance conditions are attached to the vesting of Performance and Matching Awards based on either the achievement of target growth in earnings per share or the relative total shareholder return (TSR) of the Company against a comparator group of companies.
If the performance conditions are met Performance and Matching Awards vest on the third anniversary of the grant date and remain exercisable for a period of up to six months following the vesting date. There are no cash settlement alternatives at present.

## 7 Employee benefit costs (continued)

### (b) Share schemes (continued)

### (iii) Share Matching Plan (the Plan)

The Share Matching Plan was introduced in 2005 as part of the new Long Term Incentive Plan arrangements described in (ii). Under the Plan a Matching Award to acquire a specified number of shares for free may be made if the employee pledges a number of shares as investment shares which are then matched by the Company on either a 1:1 or 2:1 basis with the number of shares that could have been purchased with the pre-tax equivalent of the amount invested. The Matching Awards vest on the third anniversary of the grant date and remain exercisable for a period of up to six months following the vesting date. There are no cash settlement alternatives at present.

### (iv) Deferred Annual Share Bonus Plan

The Deferred Annual Share Bonus Plan is a discretionary scheme which forms part of the bonus arrangements for certain senior employees. Under the scheme part of any bonus may be received in cash whilst the remainder is used to make an award of nil cost options which vest three years after the award date. The options must be exercised within three months of vesting. There are no cash settlement alternatives at present.

### (v) West Midlands Travel Ltd (“WMT”) Long Service Option Scheme

The WMT Long Service Option Scheme utilises a fixed amount of shares set aside for this purpose following the acquisition of WMT in 1995 and is open to all WMT employees who have been in service for more than 25 years. The options are exercisable between three and ten years following the grant date. There are no cash settlement alternatives.

### (vi) TWM Share Incentive Plan (the “SIP”)

The TWM SIP exists for the benefit of WMT employees. At the end of the year, 1,540 National Express Group PLC shares were held for the benefit of the Trustee. Dividends on shares held in the SIP forfeited shares account are waived. There are no cash settlement alternatives.

## 8 Share-based payment

The charge in respect of share-based payment transactions included in the Group’s income statement for the year is as follows:

| | **2007 £m** | 2006 £m |
|---|---|---|
| Expense arising from share and share option plans – continuing operations | **3.2** | 2.0 |

During the year ended 31 December 2007, the Group had six share-based payment arrangements, which are described in note 7(b).

For the following disclosure, share options with a nil exercise price have been disclosed separately to avoid distorting the weighted average exercise prices. The number of share options in existence during the year was as follows:

| | **2007** | | 2006 | |
|---|---|---|---|---|
| | **Number of share options** | **Weighted average exercise price p** | Number of share options | Weighted average exercise price p |
| Options without a nil exercise price: | | | | |
| At 1 January | **1,385,998** | **738** | 4,807,708 | 620 |
| Granted during the year | **19,343** | **1,108** | 36,406 | 932 |
| Lapsed during the year | **(62,908)** | **762** | (378,604) | 833 |
| Exercised during the year | **(947,981)** | **713** | (3,079,512) | 544 |
| Outstanding at 31 December[1] | **394,452** | **814** | 1,385,998 | 738 |
| Exercisable at 31 December | **307,795** | **773** | 492,299 | 813 |
| Options with a nil exercise price: | | | | |
| At 1 January | **1,424,804** | **nil** | 716,299 | nil |
| Granted during the year | **497,584** | **nil** | 791,645 | nil |
| Lapsed during the year | **(347,557)** | **nil** | (61,845) | nil |
| Exercised during the year | **(60,476)** | **nil** | (21,295) | nil |
| Outstanding at 31 December | **1,514,355** | **nil** | 1,424,804 | nil |
| Exercisable at 31 December | **–** | **–** | – | – |
| Total outstanding at 31 December | **1,908,807** | | 2,810,802 | |
| Total exercisable at 31 December | **307,795** | | 492,299 | |

(1) Included within this balance are options over 180,920 (2006: 412,896) shares for which no expense has been recognised in accordance with the transitional provisions of IFRS 2 as the options were granted before 7 November 2002 and have not been subsequently modified.

# Notes to the Consolidated Accounts continued

### 8 Share-based payment (continued)

The options outstanding at 31 December 2007 had exercise prices that were between 398p and 1224p (2006: between 398p and 1224p) excluding options with a nil exercise price. The range of exercise prices for options was as follows:

| Exercise price (p) | 2007 | 2006 |
|---|---|---|
| 350–650 | **71,150** | 157,453 |
| 650–950 | **231,059** | 1,110,455 |
| 950–1250 | **92,243** | 118,090 |
| | **394,452** | 1,385,998 |

The options have a weighted average contractual life of three years (2006: four years). Options were exercised regularly throughout the year and the weighted average share price at exercise was 1153p (2006: 911p).

The weighted average fair value of the share options granted during the year was calculated using a stochastic model, with the following assumptions and inputs:

| | Share options without nil exercise price | | Share options with nil exercise price | |
|---|---|---|---|---|
| | 2007 | 2006 | 2007 | 2006 |
| Risk free interest rate | **5.0%–5.2%** | 4.4%–4.7% | **–** | – |
| Expected volatility | **27.0%–27.3%** | 27.0%–27.5% | **19.0%** | 19.0% |
| Peer group volatility | **–** | – | **25.7%–25.9%** | 29.7%–31.2% |
| Expected option life in years | **6 years** | 6 years | **3 years** | 3 years |
| Expected dividend yield | **3.1%** | 3.6%–3.8% | **2.7%–2.8%** | 3.4%–3.5% |
| Weighted average share price | **1071p–1175p** | 937p–940p | **1236p–1295p** | 931p–1033p |
| Weighted average exercise price | **1093p–1153p** | 920p–940p | **0p** | 0p |
| Weighted average fair value of options granted | **215p–262p** | 181p–188p | **684p–1194p** | 369p–934p |

Experience to date has shown that approximately 15% (2006: 15%) of options are exercised early, principally due to redundancies. This has been incorporated into the calculation of the expected option life for the share options without nil exercise price.

Expected volatility in the table above was determined from historic volatility over the last eight years, adjusted for one-off events that were not considered to be reflective of the volatility of the share price going forward. The expected dividend yield represents the dividends declared in the 12 months preceding the date of the grant divided by the average share price in the month preceding the date of the grant.

For share options granted during the year under the LTIP, the TSR targets have been reflected in the calculation of the fair value of the options above.

### 9 Net finance costs

| | 2007 £m | 2006 £m |
|---|---|---|
| Bank interest payable | **(37.9)** | (28.2) |
| Finance lease interest payable | **(5.0)** | (7.0) |
| Other interest payable | **(0.1)** | – |
| Unwind of provision discounting | **(3.0)** | (2.1) |
| **Finance costs** | **(46.0)** | (37.3) |
| Finance income: Bank interest receivable | **17.0** | 12.4 |
| **Net finance costs** | **(29.0)** | (24.9) |
| Of which, from financial instruments: | | |
| Cash and cash equivalents | **17.0** | 12.4 |
| Financial liabilities measured at amortised cost | **(38.4)** | (25.9) |
| Financial liabilities at fair value through profit or loss | **(0.9)** | – |
| Derivatives used for hedging | **0.3** | (2.4) |
| Loan fee amortisation | **(0.9)** | (0.9) |

## 10 Taxation

### (a) Analysis of taxation charge/(credit) in the year

| | 2007 £m | 2006 £m |
|---|---|---|
| Current taxation: | | |
| UK corporation tax – continuing operations | **24.9** | 10.0 |
| Overseas taxation – continuing operations | **11.3** | 8.8 |
| Current income tax charge | **36.2** | 18.8 |
| Amounts overprovided in prior years – UK | **(2.0)** | (4.8) |
| Amounts overprovided in prior years – Overseas | **–** | (0.2) |
| Total current income tax | **34.2** | 13.8 |
| Deferred taxation (see note 27): | | |
| Origination and reversal of temporary differences – continuing operations | **–** | 9.8 |
| Total tax charge | **34.2** | 23.6 |
| The tax charge in the income statement is disclosed as follows: | | |
| Income tax expense on continuing operations | **37.6** | 23.6 |
| Income tax credit on discontinued operations | **(3.4)** | – |
| | **34.2** | 23.6 |
| The tax expense on continuing operations is disclosed as follows: | | |
| Tax charge on profit before goodwill impairment, intangible asset amortisation and exceptional items | **48.1** | 39.2 |
| Tax credit on intangible asset amortisation and exceptional items | **(10.5)** | (15.6) |
| | **37.6** | 23.6 |

### (b) Tax on items charged to equity

| | 2007 £m | 2006 £m |
|---|---|---|
| Current taxation: | | |
| Credit/(charge) on exchange movements offset in reserves | **14.3** | (0.8) |
| Credit on share-based payment | **0.9** | 2.7 |
| | **15.2** | 1.9 |
| Deferred taxation: | | |
| Deferred tax charge on share-based payment | **(0.5)** | (0.3) |
| Deferred tax charge on actuarial gains | **(3.5)** | (6.2) |
| Deferred tax charge on exchange movements on cash flow hedges | **–** | (0.5) |
| Deferred tax (charge)/credit on cash flow hedges | **(6.1)** | 3.7 |
| | **(10.1)** | (3.3) |

### (c) Reconciliation of the total tax charge

| | 2007 £m | 2006 £m |
|---|---|---|
| Profit from continuing operations before income tax | **149.9** | 104.1 |
| (Loss)/profit from discontinued operations before income tax | **(6.3)** | (3.2) |
| Accounting profit before income tax | **143.6** | 100.9 |
| Notional charge at UK corporation tax rate of 30% | **43.1** | 30.3 |
| Non-deductible goodwill impairment and intangible amortisation | **0.8** | 7.2 |
| Utilisation of unrecognised tax losses | **(0.6)** | (0.5) |
| Prior year adjustments within current and deferred tax | **(0.4)** | (8.9) |
| Non-deductible losses from associates | **–** | 1.2 |
| Effect of overseas tax rates | **1.3** | 0.4 |
| Effect of rate reductions | **(0.3)** | – |
| Spanish tax credits | **(4.3)** | (2.3) |
| Non-taxable profit on sale of non-current assets | **(4.2)** | (3.2) |
| Overseas financing deduction | **(1.8)** | (2.1) |
| Non-deductible expenditure | **0.6** | 1.5 |
| Total tax charge reported in the income statement | **34.2** | 23.6 |

# Notes to the Consolidated Accounts continued

### 10 Taxation (continued)
#### (d) Temporary differences associated with Group investments
No deferred tax (2006: £nil) is recognised on the unremitted earnings of subsidiaries, associates and joint ventures, as the Group has determined that these undistributed profits will not be distributed in the near future. The temporary differences associated with investments in subsidiaries, associates and joint ventures, for which deferred tax liability has not been recognised aggregate to £51.1m (2006: £33.8m).

#### (e) Unrecognised tax losses
Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through future taxable profits is probable. Overseas deferred tax assets that the Group has not recognised in the accounts amount to £36.6m (2006: £34.8m), which arise in tax jurisdictions where the Group does not expect to generate future profits. In addition, there are capital losses of £22.3m (2006: £26.4m) which have not been recognised, recoverability of which is dependent on capital gains arising.

#### (f) Deferred tax included in the income statement

| | 2007 £m | 2006 £m |
|---|---|---|
| Accelerated capital allowances | **(3.3)** | 5.0 |
| Short-term temporary differences | **(3.4)** | 1.8 |
| Utilisation/(recognition) of losses | **6.7** | 3.0 |
| | **–** | 9.8 |

Details on the balance sheet position of deferred tax are included in note 27.

### 11 Discontinued operations
The 2007 results include a charge to the income statement in respect of the disposal of the North American Public Transit operation on 1 September 2005. A provision for certain liabilities that remained with the Group on disposal, has been increased due to the settlement of a dispute over working hours. The charge of £2.9m comprises £6.3m of additional liabilities in relation to the disposed operations, offset by a tax credit of £3.4m.

The charge of £3.2m in 2006 represents an increase to the disposal provision relating to the same discontinued operations.

No operations were discontinued in the current or prior years.

| | 2007 £m | 2006 £m |
|---|---|---|
| **Cash flows from operations discontinued in 2005** | | |
| Net cash inflow from operating activities | **–** | – |
| Net cash inflow from investing activities | **(1.9)** | – |
| **Loss per share** | | |
| Basic from discontinued operations | **(1.9p)** | (2.1p) |
| Diluted from discontinued operations | **(1.9p)** | (2.1p) |

### 12 Dividends paid and proposed

| | 2007 £m | 2006 £m |
|---|---|---|
| **Declared and paid during the year** | | |
| Ordinary final dividend for 2006 paid of 24.00p per share (2005: 22.25p per share) | **36.4** | 33.9 |
| Ordinary interim dividend for 2007 paid of 11.56p per share (2006: 10.75p per share) | **17.6** | 16.2 |
| | **54.0** | 50.1 |
| **Proposed for approval (not recognised as a liability at 31 December)** | | |
| Ordinary final dividend for 2007 of 26.40p per share (2006: 24.00p per share) | **40.2** | 36.3 |

### 13 Earnings per share

| | 2007 | 2006 |
|---|---|---|
| Basic earnings per share – continuing operations | **73.6p** | 52.8p |
| Basic loss per share – discontinued operations | **(1.9p)** | (2.1p) |
| Basic earnings/(loss) per share – total | **71.7p** | 50.7p |
| Normalised basic earnings per share – continuing operations | **84.5p** | 77.0p |
| Diluted earnings per share – continuing operations | **73.1p** | 52.5p |
| Diluted loss per share – discontinued operations | **(1.9p)** | (2.1p) |
| Diluted earnings/(loss) per share – total | **71.2p** | 50.4p |
| Normalised diluted earnings per share – continuing operations | **83.9p** | 76.5p |

## 13 Earnings per share (continued)

Basic earnings per share is calculated by dividing the earnings attributable to equity shareholders of £108.9m (2006: £76.5m) by the weighted average number of ordinary shares in issue during the year, excluding those held by employee share ownership trusts and those held as treasury shares which are both treated as cancelled.

For diluted earnings per share, the weighted average number of ordinary shares in issue during the year is adjusted to include the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

The reconciliation of basic and diluted weighted average number of ordinary shares is as follows:

| | **2007** | 2006 |
|---|---|---|
| Basic weighted average shares | **151,914,241** | 150,847,303 |
| Adjustment for dilutive potential ordinary shares | **976,000** | 915,923 |
| Diluted weighted average shares | **152,890,241** | 151,763,226 |

The normalised basic and normalised diluted earnings per share have been calculated in addition to the basic and diluted earnings per shares required by IAS 33 since, in the opinion of the Directors, they reflect the underlying performance of the business's operations more appropriately.

The reconciliation of the earnings and earnings per share to their normalised equivalent is as follows:

| | **2007 £m** | **2007 Basic EPS p** | **2007 Diluted EPS p** | 2006 £m | 2006 Basic EPS p | 2006 Diluted EPS p |
|---|---|---|---|---|---|---|
| Profit/(loss) attributable to equity shareholders | **108.9** | **71.7** | **71.2** | 76.5 | 50.7 | 50.4 |
| Loss from discontinued operations | **2.9** | **1.9** | **1.9** | 3.2 | 2.1 | 2.1 |
| Profit from continuing operations attributable to equity shareholders | **111.8** | **73.6** | **73.1** | 79.7 | 52.8 | 52.5 |
| Goodwill impairment on continuing operations | **–** | **–** | **–** | 20.2 | 13.4 | 13.3 |
| Intangible asset amortisation | **27.5** | **18.1** | **18.0** | 27.8 | 18.5 | 18.3 |
| Exceptional charge for associate onerous contract provision | **–** | **–** | **–** | 25.7 | 17.0 | 16.9 |
| Exceptional items | **15.8** | **10.4** | **10.3** | (4.8) | (3.2) | (3.1) |
| Profit on disposal of non-current assets | **(16.2)** | **(10.7)** | **(10.6)** | (16.9) | (11.2) | (11.1) |
| Tax relief on goodwill and exceptional items | **(10.5)** | **(6.9)** | **(6.9)** | (15.6) | (10.3) | (10.3) |
| Normalised profit attributable to equity shareholders | **128.4** | **84.5** | **83.9** | 116.1 | 77.0 | 76.5 |

## 14 Intangible assets

| | Customer contracts £m | Rail franchise £m | **Finite life assets £m** | Contractual relationships £m | Goodwill £m | **Indefinite life assets £m** | **Total £m** |
|---|---|---|---|---|---|---|---|
| Cost: | | | | | | | |
| At 1 January 2007 | 190.8 | 11.7 | **202.5** | 18.0 | 596.7 | **614.7** | **817.2** |
| Additions through business combinations | 1.9 | – | **1.9** | 6.2 | 420.6 | **426.8** | **428.7** |
| Disposals | (0.6) | (1.8) | **(2.4)** | – | – | **–** | **(2.4)** |
| Foreign exchange | 16.2 | – | **16.2** | 2.4 | 60.3 | **62.7** | **78.9** |
| **At 31 December 2007** | **208.3** | **9.9** | **218.2** | **26.6** | **1,077.6** | **1,104.2** | **1,322.4** |
| Amortisation and impairment: | | | | | | | |
| At 1 January 2007 | 28.5 | 4.3 | **32.8** | – | 86.8 | **86.8** | **119.6** |
| Charge for year | 26.4 | 1.1 | **27.5** | – | – | **–** | **27.5** |
| Disposals | (0.6) | (1.8) | **(2.4)** | – | – | **–** | **(2.4)** |
| Foreign exchange | 3.8 | – | **3.8** | – | – | **–** | **3.8** |
| **At 31 December 2007** | **58.1** | **3.6** | **61.7** | **–** | **86.8** | **86.8** | **148.5** |
| Net book value: | | | | | | | |
| **At 31 December 2007** | **150.2** | **6.3** | **156.5** | **26.6** | **990.8** | **1,017.4** | **1,173.9** |
| At 1 January 2007 | 162.3 | 7.4 | 169.7 | 18.0 | 509.9 | 527.9 | 697.6 |

# Notes to the Consolidated Accounts continued

## 14 Intangible assets (continued)

| | Customer contracts £m | Rail franchise £m | Finite life assets £m | Contractual relationships £m | Goodwill £m | Indefinite life assets £m | Total £m |
|---|---|---|---|---|---|---|---|
| Cost: | | | | | | | |
| At 1 January 2006 | 188.8 | 13.0 | 201.8 | 16.9 | 621.7 | 638.6 | 840.4 |
| Additions through business combinations | 7.3 | – | 7.3 | 3.2 | 9.7 | 12.9 | 20.2 |
| Additions | – | 0.3 | 0.3 | – | – | – | 0.3 |
| Disposals | (1.5) | (1.6) | (3.1) | – | – | – | (3.1) |
| Foreign exchange | (3.8) | – | (3.8) | (2.1) | (34.7) | (36.8) | (40.6) |
| At 31 December 2006 | 190.8 | 11.7 | 202.5 | 18.0 | 596.7 | 614.7 | 817.2 |
| Amortisation and impairment: | | | | | | | |
| At 1 January 2006 | 3.2 | 4.3 | 7.5 | – | 66.6 | 66.6 | 74.1 |
| Charge for year | 26.2 | 1.6 | 27.8 | – | – | – | 27.8 |
| Annual impairment charge for the year – UK Trains | – | – | – | – | 19.2 | 19.2 | 19.2 |
| Impairment charge for the year – Other | – | – | – | – | 1.0 | 1.0 | 1.0 |
| Disposals | – | (1.6) | (1.6) | – | – | – | (1.6) |
| Foreign exchange | (0.9) | – | (0.9) | – | – | – | (0.9) |
| At 31 December 2006 | 28.5 | 4.3 | 32.8 | – | 86.8 | 86.8 | 119.6 |
| Net book value: | | | | | | | |
| At 31 December 2006 | 162.3 | 7.4 | 169.7 | 18.0 | 509.9 | 527.9 | 697.6 |
| At 1 January 2006 | 185.6 | 8.7 | 194.3 | 16.9 | 555.1 | 572.0 | 766.3 |

Due to the proximity of the combination to the year end, the Group has been unable to complete a detailed valuation of the intangible assets acquired with Continental Auto. Accordingly, the surplus of consideration over the provisional fair value of the share of net assets acquired has been allocated to goodwill at 31 December 2007.

Indefinite life intangible assets and goodwill have been allocated to individual cash-generating units for annual impairment testing on the basis of the Group's business operations. The carrying value of indefinite life intangible assets by cash-generating unit is as follows:

| | **2007 Contractual relationships £m** | **2007 Goodwill £m** | **Total £m** | 2006 Contractual relationships £m | 2006 Goodwill £m | 2006 Total £m |
|---|---|---|---|---|---|---|
| UK Bus | **–** | **13.2** | **13.2** | – | 13.2 | 13.2 |
| UK Coach | **–** | **11.9** | **11.9** | – | 5.6 | 5.6 |
| North American Bus | **26.6** | **211.9** | **238.5** | 18.0 | 200.3 | 218.3 |
| European Coach & Bus | **–** | **753.8** | **753.8** | – | 290.8 | 290.8 |
| | **26.6** | **990.8** | **1,017.4** | 18.0 | 509.9 | 527.9 |

The useful economic lives of contractual relationships in North America are deemed to be indefinite where historical experience has shown that these contracts are consistently renewed. The customer contract and rail franchise intangible assets are amortised over the finite duration of the contract or franchise as appropriate. All amortisation charges in the year have been charged to operating costs.

The recoverable amount of indefinite life intangible assets has been determined based on a value in use calculation using cash flow projections based on financial budgets and forecasts approved by senior management covering a three year period. Growth has then been extrapolated forward from the end of the forecasts.

**14 Intangible assets (continued)**

The assumptions used for the cash-generating units, are as follows:

| | Discount rate applied to cash flow projections | | Growth rate used to extrapolate cash flows beyond three year period of management plan | |
|---|---|---|---|---|
| | **2007** | 2006 | **2007** | 2006 |
| UK Bus | **10.4%** | 10.7% | **2.0%** | 2.0% |
| North American Bus | **11.2–12.3%** | 11.7–12.1% | **2.0%** | 2.0% |
| UK Coach | **10.4%** | 10.7% | **2.0%** | 2.0% |
| European Coach & Bus | **11.3%** | 10.7% | **2.0%** | 2.0% |

The discount rates represent the pre-tax risk adjusted weighted average cost of capital appropriate for the cash flow generated.

The calculation of value in use for each cash-generating unit is most sensitive to the assumptions over gross margin, discount rates, price inflation and growth rate.

The Directors consider the assumptions used to be consistent with the historical performance of each unit and to be realistically achievable in light of economic and industry measures and forecasts.

The annual impairment charge in 2006 of £19.2m related to the goodwill arising on the acquisition of Prism Rail PLC, the net book value of this goodwill is £nil (2006: £nil).

The other impairment charge in 2006 of £1.0m related to the goodwill that arose on the remaining share capital acquired of Altram LRT Limited due to ongoing operating losses.

**15 Property, plant and equipment**

| | Freehold land and buildings £m | Long leasehold property improvements £m | Public service vehicles £m | Plant and equipment, fixtures and fittings £m | **Total £m** |
|---|---|---|---|---|---|
| Cost: | | | | | |
| At 1 January 2007 | 55.7 | 3.3 | 503.4 | 166.6 | **729.0** |
| Additions | 4.9 | 0.4 | 103.2 | 49.5 | **158.0** |
| Acquisitions of businesses | 7.5 | 0.5 | 89.0 | 3.0 | **100** |
| Disposals | (0.7) | (0.2) | (30.5) | (53.3) | **(84.7)** |
| Foreign exchange | 2.7 | 0.1 | 19.6 | 1.0 | **23.4** |
| **At 31 December 2007** | **70.1** | **4.1** | **684.7** | **166.8** | **925.7** |
| Depreciation: | | | | | |
| At 1 January 2007 | 5.9 | 0.9 | 128.9 | 91.4 | **227.1** |
| Charge for the year | 1.3 | 0.5 | 54.3 | 23.5 | **79.6** |
| Disposals | (0.2) | (0.2) | (17.2) | (46.4) | **(64.0)** |
| Foreign exchange | – | – | 4.0 | 0.3 | **4.3** |
| **At 31 December 2007** | **7.0** | **1.2** | **170.0** | **68.8** | **247.0** |
| Net book value: | | | | | |
| **At 31 December 2007** | **63.1** | **2.9** | **514.7** | **98.0** | **678.7** |
| At 1 January 2007 | 49.8 | 2.4 | 374.5 | 75.2 | 501.9 |

# Notes to the Consolidated Accounts continued

### 15 Property, plant and equipment (continued)

| | Freehold land and buildings £m | Long leasehold property improvements £m | Public service vehicles £m | Plant and equipment, fixtures and fittings £m | Total £m |
|---|---|---|---|---|---|
| Cost: | | | | | |
| At 1 January 2006 | 54.0 | 15.4 | 471.3 | 179.0 | 719.7 |
| Additions | 3.0 | 0.7 | 74.3 | 20.5 | 98.5 |
| Acquisitions of businesses | – | – | 11.8 | – | 11.8 |
| Disposals | (0.9) | (8.5) | (17.1) | (30.2) | (56.7) |
| Attributable to assets held for sale | – | – | – | (3.5) | (3.5) |
| Reclassifications | 0.6 | (3.7) | 0.8 | 2.3 | – |
| Foreign exchange | (1.0) | (0.6) | (37.7) | (1.5) | (40.8) |
| At 31 December 2006 | 55.7 | 3.3 | 503.4 | 166.6 | 729.0 |
| Depreciation: | | | | | |
| At 1 January 2006 | 4.8 | 2.9 | 107.1 | 90.5 | 205.3 |
| Charge for the year | 1.1 | 0.6 | 50.8 | 29.2 | 81.7 |
| Disposals | (0.4) | (0.7) | (14.5) | (27.4) | (43.0) |
| Attributable to assets held for sale | – | – | – | (0.9) | (0.9) |
| Reclassifications | 0.5 | (1.5) | 0.6 | 0.4 | – |
| Foreign exchange | (0.1) | (0.4) | (15.1) | (0.4) | (16.0) |
| At 31 December 2006 | 5.9 | 0.9 | 128.9 | 91.4 | 227.1 |
| Net book value: | | | | | |
| At 31 December 2006 | 49.8 | 2.4 | 374.5 | 75.2 | 501.9 |
| At 1 January 2006 | 49.2 | 12.5 | 364.2 | 88.5 | 514.4 |

Property, plant and equipment held under finance lease agreements are analysed as follows:

| | **2007 £m** | 2006 £m |
|---|---|---|
| Public service vehicles | | |
| – cost | **165.5** | 179.7 |
| – depreciation | **(64.9)** | (63.7) |
| | **100.6** | 116.0 |
| Plant and equipment | | |
| – cost | **2.4** | 3.0 |
| – depreciation | **(2.0)** | (0.3) |
| | **0.4** | 2.7 |
| Net book value | **101.0** | 118.7 |

Finance leased assets and assets under hire purchase contracts are pledged as security for the related finance lease and hire purchase liabilities.

## 16 Subsidiaries

The companies listed below include all those which principally affect the result and net assets of the Group. A full list of subsidiaries, joint ventures and associates will be annexed to the next Annual Return to Companies House. The principal country of operation in respect of the companies below is the country in which they are incorporated.

National Express Group PLC is the beneficial owner of all the equity share capital, either itself or through subsidiaries, of the companies. The Group's train passenger services in the UK are operated through franchises awarded by DfT Rail, as delegated by the UK Government.

| Incorporated in England and Wales | |
|---|---|
| National Express Limited | Administration and marketing of express coach services in Great Britain |
| Eurolines (UK) Limited | Administration and marketing of express coach services to Europe |
| Airlinks Airport Services Limited | Operation of coach services |
| National Express Rail Replacement Limited | Operation of coach services |
| West Midlands Travel Limited | Operation of bus services |
| Travel London Limited | Operation of bus services |
| Travel London (West) Limited | Operation of bus services |
| Travel London (Middlesex) Limited | Operation of bus services |
| c2c Rail Limited | Operation of train passenger services |
| Central Trains Limited | Operation of train passenger services (ceased trading on 10 November 2007) |
| Gatwick Express Limited | Operation of train passenger services |
| London Eastern Railway Limited (trading as NXEA) | Operation of train passenger services |
| Maintrain Limited | Provision of train maintenance services (ceased trading on 10 November 2007) |
| Midland Main Line Limited | Operation of train passenger services (ceased trading on 10 November 2007) |
| National Express Trains Limited* | Holding company for train operating companies |
| NXEC Trains Limited | Operation of train passenger services (commenced trading on 9 December 2007) |
| Silverlink Train Services Limited | Operation of train passenger services (ceased trading on 10 November 2007) |

| Incorporated in Scotland | |
|---|---|
| Tayside Public Transport Co Limited (trading as Travel Dundee) | Operation of bus services |

| Incorporated in the USA | |
|---|---|
| Durham School Services LP | Operation of school bus services |

| Incorporated in Canada | |
|---|---|
| Stock Transportation Limited | Operation of school bus services |

| Incorporated in Spain | |
|---|---|
| Dabliu Consulting SLU** | Holding company for operating companies |
| Tury Express SA** | Holding company for operating companies |
| General Tecnica Industrial SLU** | Holding company for operating companies |
| Continental Auto SLU | Holding company for operating companies |

*Shares held by the Company. All other shares held by subsidiaries.
**The main holding companies of the Alsa Group.

## 17 Financial assets

| | 2007 £m | 2006 £m |
|---|---|---|
| Available for sale investments – Unlisted ordinary and preference shares | **7.2** | 13.5 |
| Derivative financial instruments – Interest rate swaps | **1.7** | 0.3 |
| Derivative financial instruments – Fuel price swaps | **3.6** | – |
| **Financial assets included in non-current assets** | **12.5** | 13.8 |
| Derivative financial instruments – Interest rate swaps | **1.5** | 1.5 |
| Derivative financial instruments – Fuel price swaps | **8.5** | – |
| Derivative financial instruments – Foreign exchange forward contracts | **–** | 6.6 |
| **Financial assets included in current assets** | **10.0** | 8.1 |

Further information on the Group's use of fuel price swaps, interest rate swaps and foreign exchange forward contracts is included in note 31.

# Notes to the Consolidated Accounts continued

## 17 Financial assets (continued)

**Available for sale investments**

| | 2007 £m | 2006 £m |
|---|---|---|
| Cost or valuation: | | |
| At 1 January | **19.3** | 17.2 |
| Additions | **–** | 5.3 |
| Disposals | **(12.0)** | (3.2) |
| Foreign exchange | **0.7** | – |
| **At 31 December** | **8.0** | 19.3 |
| Accumulated impairment: | | |
| **At 1 January** | **(5.8)** | (5.8) |
| Disposals | **5.0** | – |
| **At 31 December** | **(0.8)** | (5.8) |
| Net carrying amount: | | |
| **At 31 December** | **7.2** | 13.5 |
| At 1 January | **13.5** | 11.4 |

The principal available for sale investments are as follows:

| Name | Country of registration | Class of share | Proportion held % |
|---|---|---|---|
| London & Continental Railways (LCR) | England and Wales | Ordinary shares | 21 |
| Prepayment Cards Limited (PCL) | England and Wales | Ordinary shares | 23.5 |
| Metros Ligeros de Madrid, S.A. (MLM) | Spain | Ordinary shares | 15 |
| Various investments withing Alsa and Continental Auto | Spain | Ordinary shares | 4–16 |

Disposals during the year reflect the receipt of the final preference share dividend from Union Railways (South) Limited, and the subsequent redemption of these preference shares. Disposals during 2006 reflect the sale of the Group's investment in Trainline Holdings Limited.

Additions in 2006 of £5.3m comprised an investment in Metros Ligeros de Madrid, S.A..

Although the Group holds more than 20% of the ordinary shares of LCR, it does not have a presence on the Board and is not in a position to exert significant influence over this investment. Although the Group holds more than 20% of the ordinary shares of PCL, it is not in a position to exert significant influence. The investment is held at nil value and the Group has no obligation to make further investments.

## 18 Investments accounted for using the equity method

Investments accounted for using the equity method are as follows:

| | 2007 £m | 2006 £m |
|---|---|---|
| Joint ventures | **2.1** | 2.2 |
| Associates | **9.7** | 6.5 |
| Total investments accounted for under the equity method | **11.8** | 8.7 |

The Group's share of post tax results from associates and joint ventures accounted for using the equity method is as follows:

| | 2007 £m | 2006 £m |
|---|---|---|
| Share of joint ventures' loss | **(0.2)** | (0.2) |
| Share of associates' profit/(loss) | **0.6** | (3.6) |
| | **0.4** | (3.8) |
| Exceptional charge for associate onerous contract provision | **–** | (25.7) |
| Total share of results from associates and joint ventures | **0.4** | (29.5) |

**(a) Investments in joint ventures**

The Group's interests in joint ventures are as follows:

| Name | Country of registration | Activity | Proportion held % |
|---|---|---|---|
| Ibero – Eurosur SL | Spain | Holding company of Deutsche Touring | 20 |
| Movelia Tecnologias SL | Spain | Travel website | 42 |

## 18 Investments accounted for using the equity method (continued)

### (a) Investments in joint ventures (continued)

The financial information of these joint ventures is summarised below:

| | Ibero | | Movelia | | Total | |
|---|---|---|---|---|---|---|
| Share of joint ventures' balance sheets | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| Non-current assets | **3.2** | 3.0 | **0.5** | 0.5 | **3.7** | 3.5 |
| Current assets | **0.3** | 0.5 | **0.8** | 0.7 | **1.1** | 1.2 |
| Share of gross assets | **3.5** | 3.5 | **1.3** | 1.2 | **4.8** | 4.7 |
| Non-current liabilities | **(2.0)** | (2.0) | **–** | (0.1) | **(2.0)** | (2.1) |
| Current liabilities | **–** | – | **(0.7)** | (0.4) | **(0.7)** | (0.4) |
| Share of gross liabilities | **(2.0)** | (2.0) | **(0.7)** | (0.5) | **(2.7)** | (2.5) |
| Share of net assets | **1.5** | 1.5 | **0.6** | 0.7 | **2.1** | 2.2 |

| | Ibero | | Movelia | | Total | |
|---|---|---|---|---|---|---|
| Share of joint ventures' revenue and loss | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| Revenue | **–** | 0.1 | **0.3** | 0.2 | **0.3** | 0.3 |
| Loss | **(0.1)** | (0.1) | **(0.1)** | (0.1) | **(0.2)** | (0.2) |

The carrying amount of the investment in joint ventures matches the Group's share of the net assets.

### (b) Investments in associates

The Group's carrying amount of the investment in associates is disclosed as follows:

| | Held by Alsa | | Held by Continental Auto | | Total | |
|---|---|---|---|---|---|---|
| | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| Carrying amount of investment | **7.8** | 6.5 | **1.9** | – | **9.7** | 6.5 |

The Group's interests in associates are as follows:

| Name | Country of registration | Proportion held % |
|---|---|---|
| Inter-Capital and Regional Rail Limited | England and Wales | 40 |
| Alsa associates | Spain | 20–50 |
| Continental Auto associates | Spain | 25–35 |

Inter-Capital and Regional Rail Limited ("ICRRL") is contracted to manage the operations of Eurostar UK until 2010. In 2006, an onerous contract provision was recognised in relation to the Group's obligation to fund the losses of ICRRL (see below). As a result, the Group has ceased to recognise the share of results of ICRRL.

The associates of Alsa and Continental Auto are generally involved in the operation of coach and bus services, management of bus stations and similar operations.

The associates' financial information is summarised below:

| | Held by Alsa | | Held by Continental Auto | | Total | |
|---|---|---|---|---|---|---|
| Share of associates' balance sheets | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| Non-current assets | **9.2** | 6.2 | **2.4** | – | **11.6** | 6.2 |
| Current assets | **11.5** | 10.1 | **1.1** | – | **12.6** | 10.1 |
| Share of gross assets | **20.7** | 16.3 | **3.5** | – | **24.2** | 16.3 |
| Non-current liabilities | **(4.0)** | (2.8) | **(0.6)** | – | **(4.6)** | (2.8) |
| Current liabilities | **(8.9)** | (7.0) | **(1.0)** | – | **(9.9)** | (7.0) |
| Share of gross liabilities | **(12.9)** | (9.8) | **(1.6)** | – | **(14.5)** | (9.8) |
| Share of net assets | **7.8** | 6.5 | **1.9** | – | **9.7** | 6.5 |

The Group's net investment in associates is £9.7m (2006: £6.5m) which comprises the Alsa and Continental Auto associates only. The increase in the year represents the Group's acquisition of Continental Auto.

The Group's obligation in respect of ICRRL is included in provisions.

# Notes to the Consolidated Accounts continued

### 18 Investments accounted for using the equity method (continued)
(b) Investments in associates (continued)

| Share of associates' revenue and results | Revenue 2007 £m | Revenue 2006 £m | Profit/(loss) 2007 £m | Profit/(loss) 2006 £m |
|---|---|---|---|---|
| Alsa associates | **13.9** | 7.6 | **0.8** | 0.2 |
| Altram | **–** | 0.4 | **–** | 0.1 |
| Continental Auto associates | **0.5** | – | **(0.2)** | – |
| Total associate results excluding ICRRL | **14.4** | 8.0 | **0.6** | 0.3 |
| Normalised result ICRRL | **–** | 1.9 | **–** | (3.9) |
| Total normalised associates' results | **14.4** | 9.9 | **0.6** | (3.6) |
| Exceptional ICRRL charge | **–** | – | **–** | (25.7) |
| Total associates' results | **14.4** | 9.9 | **0.6** | (29.3) |

An onerous contract provision was recognised in 2006 in relation to the Group's obligation to fund the losses of ICRRL. This resulted in a total income statement charge of £29.6m of which £25.7m was included in exceptional items.

### 19 Business combinations and disposals
(a) Acquisitions
2007 acquisitions
Continental Auto
On 4 October 2007 the Group acquired the entire share capital of Continental Auto S.L.U., a bus and coach operator based in Spain. Consideration of £459.8m was satisfied by cash. Additionally costs of £3.4m have been included in total consideration.

| Net assets at date of acquisition: | Continental Auto book value £m | Continental Auto fair value adjustments £m | Continental Auto fair value total £m |
|---|---|---|---|
| Intangible assets | 92.2 | (92.2) | – |
| Property, plant and equipment | 87.5 | (1.9) | 85.6 |
| Investments accounted for under the equity method | 1.9 | – | 1.9 |
| Inventories | 1.5 | – | 1.5 |
| Trade and other receivables | 17.0 | – | 17.0 |
| Cash and cash equivalents | 4.1 | – | 4.1 |
| Trade and other payables | (16.7) | – | (16.7) |
| Provisions | (1.4) | – | (1.4) |
| Fixed asset grants | (3.0) | – | (3.0) |
| Net financial liabilities | (22.8) | – | (22.8) |
| Current tax | (1.3) | – | (1.3) |
| Deferred tax liability | (11.7) | 0.6 | (11.1) |
| Net assets | 147.3 | (93.5) | 53.8 |
| Less: minority interest | – | – | – |
| Group's share of net assets | 147.3 | (93.5) | 53.8 |
| Goodwill on acquisition | | | 409.4 |
| Total consideration | | | 463.2 |
| Net consideration | | | 459.8 |
| Acquisition costs | | | 3.4 |
| Total consideration | | | 463.2 |
| Less: net cash acquired | | | (4.1) |
| Net cash outflow | | | 459.1 |

In accordance with Group accounting policies, provisional fair value adjustments have been made to the assets and liabilities acquired, mainly in relation to the passenger transportation fleet. Due to the proximity of the combination to the year end the Group has been unable to complete a detailed valuation of the intangible and property, plant and equipment acquired with the business. Accordingly, the surplus of consideration over fair value of the share of net assets acquired has been allocated to goodwill at 31 December 2007. The Group expects to identify intangible assets, including brands, customer relationships and customer contracts, and will complete a property valuation. Independent valuers have been retained by the Group to complete this exercise and the results will be reflected in the Group's next financial statements. The value of goodwill will be adjusted by a corresponding amount for the fair value of intangible assets identified and the difference between the market and book values of the property assets.

From the date of acquisition, Continental Auto has contributed £5.8m to the operating profit of the Group. If the combination had taken place at the beginning of the year, the operating profit for the Group would have been £216.1m and revenue from continuing operations would have been £2,711.4m.

**19 Business combinations and disposals (continued)**
**(a) Acquisitions (continued)**
Other 2007 acquisitions
During the year ended 31 December 2007, in Canada, the Group acquired the entire share capital of school bus operators Dundas (Dundas Bus Service Ltd) on 30 March 2007 and Hogan (Hogan Bus Service Ltd) on 31 May 2007. In the United States, the Group acquired the entire share capital of school bus operators Murphy (Murphy Transportation Inc) on 30 July 2007.

The Group also acquired the entire share capital of Hotelink Limited (now renamed national Express Dot2Dot Limited) on 31 March 2007 and The Kings Ferry Limited on 8 November 2007. These acquired entities operate coach services in the UK.

| | Book value | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Net assets at date of acquisition: | Dundas £m | Hogan £m | Murphy £m | Hotelink £m | Kings Ferry £m | Total £m | Fair value adjustments £m | **Fair value Total £m** |
| Intangible assets | – | – | – | – | – | – | 8.1 | **8.1** |
| Property, plant and equipment | 0.5 | 0.2 | 4.9 | – | 8.5 | 14.1 | 0.3 | **14.4** |
| Inventories | – | – | 0.2 | – | 0.1 | 0.3 | – | **0.3** |
| Trade and other receivables | – | – | 1.5 | 0.2 | 1.2 | 2.9 | – | **2.9** |
| Cash and cash equivalents | – | – | 0.6 | 0.2 | – | 0.8 | – | **0.8** |
| Trade and other payables | – | – | (0.4) | (0.2) | (1.7) | (2.3) | (0.1) | **(2.4)** |
| Financial liabilities – Borrowings | – | – | – | – | (5.0) | (5.0) | – | **(5.0)** |
| Deferred tax liability | – | – | – | – | – | – | (2.4) | **(2.4)** |
| Net assets acquired | 0.5 | 0.2 | 6.8 | 0.2 | 3.1 | 10.8 | 5.9 | **16.7** |
| Goodwill on acquisition | | | | | | | | **11.2** |
| Total consideration | | | | | | | | **27.9** |
| Net consideration | | | | | | | | **27.6** |
| Acquisition costs | | | | | | | | **0.3** |
| Total consideration | | | | | | | | **27.9** |
| Less: deferred consideration | | | | | | | | **(1.1)** |
| Less: acquisition costs accrued | | | | | | | | **(0.1)** |
| Less: net cash acquired | | | | | | | | **(0.8)** |
| Net cash outflow | | | | | | | | **25.9** |

The acquisition balance sheets have been adjusted to reflect fair value adjustments. The adjustments represent:

a) the recognition of customer contracts acquired with Murphy (£1.8m), and customer relationships acquired with Dundas (£1.0m), Hogan (£0.3m) and Murphy (£5.0m) which reflects the expected indefinite renewal of these school bus contracts in North America. The customer contracts are amortised over the life of the contracts, whilst customer relationships are not amortised, but are tested for impairment on an annual basis;

b) an increase in the value of property, plant and equipment at Murphy following a review of the vehicle fleet;

c) an increase in payables of £0.1m at Hotelink; and

d) the deferred tax liability associated on the customer contracts acquired with Murphy (£0.5m), and the customer relationships acquired with Dundas (£0.3m), Hogan (£0.1m) and Murphy (£1.5m).

Consideration was £1.5m for Dundas (including £0.1m deferred consideration), £0.6m for Hogan, £16.3m for Murphy (including £0.1m acquisition costs and £1.0m deferred consideration), £0.9m for Hotelink Limited (including £0.1m acquisition costs), and £8.6m for The Kings Ferry Limited (including £0.1m acquisition costs).

From their respective dates of acquisition Dundas, Hogan, Murphy, Hotelink Limited and The Kings Ferry Limited have contributed £0.3m, £0.1m, £1.4m, a loss of £4.8m and £0.1m respectively to operating profit of the Group. If these combinations had taken place at the beginning of the year the Group operating profit would have been £207.2m, and revenue from continuing operations would have been £2,630.8m.

Included in the goodwill recognised above are certain intangible assets that cannot be separately identified and measured due to their nature. This includes control over the acquired businesses and assembled workforce and increased scale in our North American school bus operations and UK Coach operations. Management believes that goodwill represents value to the Group for which the recognition of a discrete intangible asset is not permitted. The majority of the value was assessed to comprise of synergy benefits expected to be achieved by merging the businesses acquired into the Group’s North American operations.

# Notes to the Consolidated Accounts continued

### 19 Business combinations and disposals (continued)

**(a) Acquisitions (continued)**

2006 acquisitions

During the year ended 31 December 2006, in Canada, the Group acquired the net assets of school bus operators Vine (Vine Bus Lines Ltd) on 7 July 2006, M&O (M&O Bus Lines (Handicab) Limited) on 11 April 2006, and the entire share capital of Deluxe (Palangio Enterprises (1982) Ltd) on 29 September 2006. In the United States, the Group acquired the entire share capital of school bus operators Reliance (Reliance Motor Coach Company Inc.) on 1 June 2006, and Double A (Double A Transportation Inc.) on 15 December 2006. The Group also acquired the net assets of J&R (J&R Bus Co., LLC) on 20 October 2006, a school bus operator in the United States.

| | Book value | | | | | | Fair value | **Fair value** |
|---|---|---|---|---|---|---|---|---|
| **North America**<br>Net assets at date of acquisition: | Reliance<br>£m | J&R<br>£m | Double A<br>£m | Deluxe<br>£m | M&O/Vine<br>£m | Total<br>£m | adjustments<br>£m | **Total**<br>**£m** |
| Intangible assets | – | – | – | – | – | – | 10.5 | **10.5** |
| Property, plant and equipment | 4.4 | 1.1 | 4.0 | 1.4 | 0.5 | 11.4 | 0.4 | **11.8** |
| Trade and other receivables | 0.7 | – | 0.2 | – | – | 0.9 | 0.5 | **1.4** |
| Cash and cash equivalents | 0.2 | – | 0.3 | – | – | 0.5 | – | **0.5** |
| Trade and other payables | (1.5) | – | (0.8) | (0.1) | – | (2.4) | 0.1 | **(2.3)** |
| Deferred tax liability | (1.0) | – | – | – | – | (1.0) | (3.1) | **(4.1)** |
| Net assets acquired | 2.8 | 1.1 | 3.7 | 1.3 | 0.5 | 9.4 | 8.4 | **17.8** |
| Goodwill on acquisition | | | | | | | | **8.7** |
| Total consideration | | | | | | | | **26.5** |
| Net consideration | | | | | | | | **25.4** |
| Acquisition costs | | | | | | | | **1.1** |
| Total consideration | | | | | | | | **26.5** |
| Less: deferred consideration | | | | | | | | **(0.9)** |
| Less: acquisition costs accrued | | | | | | | | **(0.3)** |
| Less: net cash acquired | | | | | | | | **(0.5)** |
| Net cash outflow | | | | | | | | **24.8** |

The acquisition balance sheets have been adjusted to reflect fair value adjustments. The adjustments represent:

a) the recognition of finite life intangible assets of customer contracts acquired with the Reliance business (£4.4m), J&R (£0.4m), Double A (£1.9m) and Deluxe (£0.6m), and of indefinite life intangible assets of customer relationships acquired with J&R (£2.3m) and Deluxe (£0.9m) which reflects the expected indefinite renewal of these school bus contracts in North America. The customer contracts are amortised over the life of the contracts, whilst customer relationships will not be amortised, but will be tested for impairment on an annual basis;

b) an adjustment to the value of property, plant and equipment at J&R and Double A following a review of the vehicle fleet;

c) an increase in working capital of £0.6m to reflect the liabilities excluded from the opening balance sheet at Double A (£0.5m) and Reliance (£0.3m), offset by an increase in insurance provisions of £0.2m at Double A; and

d) deferred tax liability recognised on the customer contracts, customer relationships and property, plant and equipment.

Consideration was £10.8m for Reliance (including £0.1m acquisition costs), £4.6m for J&R (including £0.2m acquisition costs and £0.8m deferred consideration), £7.2m for Double A (including £0.4m acquisition costs), £3.0m for Deluxe (including £0.1m deferred consideration and £0.4m acquisition costs), and £0.9m for M&O and Vine.

From their respective dates of acquisition Reliance, J&R, Double A and the Canadian acquisitions contributed £0.6m, £0.1m, £0.1m and £0.2m respectively to operating profit of the Group during the year ended 31 December 2006. If these combinations had taken place at the beginning of 2006 the Group operating profit for the year ended 31 December 2006 would have been £142.6m, and revenue from continuing operations would have been £2,541.7m.

### 19 Business combinations and disposals (continued)

#### (a) Acquisitions (continued)

On 14 March 2006 the Group acquired the remaining 67% of the share capital of Altram LRT Limited (Altram), a provider of light transport systems, for £0.2m, giving rise to goodwill of a further £1.0m which has been impaired.

| | Final fair value total £m |
|---|---|
| Current assets | **5.9** |
| Current liabilities | **(7.4)** |
| Net liabilities acquired | **(1.5)** |
| Share of liability of associate | **0.7** |
| Goodwill on acquisition | **1.0** |
| Total consideration | **0.2** |
| Net consideration | **–** |
| Acquisition costs | **0.2** |
| Total consideration | **0.2** |
| Less: net cash acquired | **(5.2)** |
| Net cash inflow | **(5.0)** |

Altram contributed a £0.4m loss to operating profit of the Group during the year ended 31 December 2006. If the remaining 67% of share capital had been acquired at the beginning of 2006, the operating profit of the Group for the year ended 31 December 2006 would have been £141.7m and revenue from continuing operations would have been £2,526.3m.

#### (b) Disposals

The trade and business of Stewart International Airport was disposed of on 31 October 2007 for gross proceeds of £36.4m, having been classified as a disposal group held for sale during 2006.

| Net assets disposed of: | £m |
|---|---|
| Property, plant and equipment | **20.0** |
| Inventories | **0.1** |
| Trade and other receivables | **0.5** |
| Trade and other payables | **(2.2)** |
| Interest payables | **(0.3)** |
| Net assets disposed | **18.1** |
| Provision for liabilities arising on disposal | **0.9** |
| Cash flow hedge of disposal proceeds | **(1.0)** |
| Profit on sale of business | **16.2** |
| Net consideration received | **34.2** |
| Total consideration received | **36.4** |
| Less: disposal costs | **2.2** |
| Net consideration received | **34.2** |
| Add: accrued disposal costs | **0.3** |
| Less: deferred consideration receivable | **(0.2)** |
| Net cash inflow | **34.3** |

### 20 Non-current assets – Other receivables

| | 2007 £m | 2006 £m |
|---|---|---|
| Prepayments and accrued income | **4.6** | 2.3 |
| Other receivables | **5.4** | 1.8 |
| | **10.0** | 4.1 |

### 21 Inventories

| | 2007 £m | 2006 £m |
|---|---|---|
| Raw materials and consumables | **20.0** | 15.5 |

The movement on the provision for slow moving and obsolete inventory is immaterial.

# Notes to the Consolidated Accounts continued

### 22 Current assets – Trade and other receivables

| | 2007 £m | 2006 £m |
|---|---|---|
| Trade receivables | **170.3** | 172.9 |
| Less: provision for impairment of receivables | **(6.5)** | (5.6) |
| Trade receivables – net | **163.8** | 167.3 |
| Amounts due from associates and joint ventures | **3.7** | 3.3 |
| Amounts owed by other related parties | **1.0** | 0.6 |
| Other receivables | **42.8** | 51.2 |
| Prepayments and accrued income | **61.1** | 49.9 |
| | **272.4** | 272.3 |

An analysis of the provision for impairment of receivables is provided below:

| | 2007 £m | 2006 £m |
|---|---|---|
| At 1 January | **(5.6)** | (2.6) |
| Provided in the year | **(0.9)** | (3.0) |
| **At 31 December** | **(6.5)** | (5.6) |

Credit risk with respect to trade receivables is low as a large proportion of the Group's trading is with public or quasi-public organisations.

### 23 Cash and cash equivalents

| | 2007 £m | 2006 £m |
|---|---|---|
| Cash at bank and in hand | **68.0** | 43.7 |
| Overnight deposits | **14.6** | 21.6 |
| Other short-term deposits | **74.6** | 78.3 |
| Cash and cash equivalents | **157.2** | 143.6 |

Included in cash and cash equivalents are restricted balances of £55.2m (2006: £33.5m) held by the TOCs due to restrictions included in the franchise agreements.

Cash at bank and in hand earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates. The fair value of cash and cash equivalents is equal to the carrying value.

### 24 Current liabilities – Trade and other payables

| | 2007 £m | 2006 £m |
|---|---|---|
| Trade payables | **218.8** | 187.3 |
| Amounts owed to associates and joint ventures | **1.4** | 1.0 |
| Amounts owed to other related parties | **0.6** | 1.9 |
| Other tax and social security payable | **34.1** | 22.4 |
| Accruals and deferred income | **196.7** | 206.0 |
| Other payables | **121.7** | 99.8 |
| | **573.3** | 518.4 |

Trade payables are non-interest bearing and are normally settled on 30 day terms and other payables are non-interest bearing and have an average term of two months. Included within other payables are deferred fixed asset grants from government or other public bodies of £5.0m (2006: £1.5m).

### 25 Other non-current liabilities

| | 2007 £m | 2006 £m |
|---|---|---|
| Other liabilities | **3.7** | 3.0 |

Other non-current liabilities comprise deferred fixed asset grants of £2.9m (2006: £2.5m) and other liabilities of £0.8m (2006: £0.5m).

## 26 Provisions

| | Insurance claims[a] £m | Eurostar onerous contract provision[b] £m | Other[c] £m | Total £m |
|---|---|---|---|---|
| At 1 January 2007 | 38.5 | 30.6 | 9.6 | 78.7 |
| Charged to income statement | 18.6 | – | 11.7 | 30.3 |
| Utilised in the year | (15.9) | (4.7) | (4.5) | (25.1) |
| Acquired in business combinations | – | – | 1.4 | 1.4 |
| Amortisation of discount | 1.0 | 2.0 | – | 3.0 |
| Exchange difference | (0.1) | – | 0.1 | – |
| **At 31 December 2007** | **42.1** | **27.9** | **18.3** | **88.3** |
| Current 31 December 2007 | 18.1 | 8.4 | 18.3 | 44.8 |
| Non-current 31 December 2007 | 24.0 | 19.5 | – | 43.5 |
| | **42.1** | **27.9** | **18.3** | **88.3** |
| Current 31 December 2006 | 8.1 | 9.3 | – | 17.4 |
| Non-current 31 December 2006 | 30.4 | 21.3 | 9.6 | 61.3 |
| | 38.5 | 30.6 | 9.6 | 78.7 |

a) The insurance claims provision arises from estimated exposures at the year end, the majority of which will be utilised in the next six years, and comprises provisions for existing claims arising in the UK and North America.

b) A provision was recognised in 2006 for the Group's onerous contract for Eurostar with ICRRL. £8.4m was paid to ICRRL during the year, which is offset by a receipt in relation to preference share dividends. The provision will be utilised during the period up to the end of our contract in 2010, with the final payment being made in February 2011.

c) The following items are included within other provisions:

i. An increase in the provision for the expected liabilities in relation to the discontinued North American Public Transit business was recognised in the year, as disclosed in note 11. These liabilities arise as the Group is a party to an industry-wide litigation in respect of working time regulations. A provision has been recognised for the expected value of the settlement, but the total amount of the provisions recognised by the Group is not disclosed as this may prejudice the Group's position in this matter. The whole provision is expected to be paid in 2008.

ii. A provision was recognised in the year for the disposal of Stewart of £0.9m. The balance is expected to be paid in 2008.

iii. All other remaining provisions are expected to be paid within 2008.

When the effect is material, the provisions are discounted to their net present value.

## 27 Deferred tax

| | **2007 £m** | 2006 £m |
|---|---|---|
| Net deferred tax liability brought forward | **(73.7)** | (58.9) |
| Acquisition of subsidiaries | **(13.5)** | (4.1) |
| Charge to income statement | **–** | (9.8) |
| Charge to reserves | **(10.1)** | (3.3) |
| Exchange differences | **(6.7)** | 2.4 |
| **Net deferred tax liability at 31 December** | **(104.0)** | (73.7) |

Based on current capital investment plans, the Group expects to be able to claim capital allowances in excess of depreciation in future years at a similar level to the current year.

The movements in deferred tax liabilities during the period are shown below. Deferred tax liabilities and assets within the same jurisdiction have been offset. In 2007 all jurisdictions are in a liability position for deferred tax. The tables below have been updated to reflect this.

| Deferred tax liabilities | Accelerated tax depreciation £m | Losses carried forward £m | Other £m | **Total £m** |
|---|---|---|---|---|
| At 1 January 2007 | (44.2) | 5.8 | (45.9) | **(84.3)** |
| Transferred from deferred tax assets | (10.0) | 0.1 | 20.5 | **10.6** |
| | (54.2) | 5.9 | (25.4) | **(73.7)** |
| (Charged)/credited to income statement | (3.3) | (3.4) | 6.7 | **–** |
| Charged directly to equity | – | – | (10.1) | **(10.1)** |
| Acquisition of subsidiaries | (2.0) | – | (11.5) | **(13.5)** |
| Exchange differences | (1.1) | 0.1 | (5.7) | **(6.7)** |
| **At 31 December 2007** | **(60.6)** | **2.6** | **(46.0)** | **(104.0)** |

# Notes to the Consolidated Accounts continued

## 27 Deferred tax (continued)

| Deferred tax assets | Accelerated tax depreciation £m | Losses carried forward £m | Other £m | Total £m |
|---|---|---|---|---|
| At 1 January 2006 | (8.4) | – | 31.4 | 23.0 |
| (Charged)/credited to income statement | (1.6) | 0.1 | (7.6) | (9.1) |
| Credited directly to equity | – | – | (3.3) | (3.3) |
| At 31 December 2006 | (10.0) | 0.1 | 20.5 | 10.6 |

| Deferred tax liabilities | Accelerated tax depreciation £m | Losses carried forward £m | Other £m | Total £m |
|---|---|---|---|---|
| At 1 January 2006 | (42.4) | 9.5 | (49.0) | (81.9) |
| (Charged)/credited to income statement | (3.4) | (3.1) | 5.8 | (0.7) |
| Acquisition of subsidiaries | – | – | (4.1) | (4.1) |
| Exchange differences | 1.6 | (0.6) | 1.4 | 2.4 |
| At 31 December 2006 | (44.2) | 5.8 | (45.9) | (84.3) |

## 28 Financial liabilities

| | **2007 £m** | 2006 £m |
|---|---|---|
| **Non-current** | | |
| Bank loans | **562.9** | 458.0 |
| Finance lease obligations | **78.7** | 80.4 |
| Financial liabilities – Interest-bearing loans and borrowings | **641.6** | 538.4 |
| Fuel price swaps | **–** | 2.6 |
| Interest rate swaps | **5.4** | 5.7 |
| Financial liabilities – Derivative financial instruments | **5.4** | 8.3 |
| Non-current financial liabilities | **647.0** | 546.7 |
| **Current** | | |
| Loan notes | **0.8** | 0.8 |
| Bank loans | **403.0** | 20.1 |
| Finance lease obligations | **22.6** | 22.7 |
| Financial liabilities – Interest-bearing loans and borrowings | **426.4** | 43.6 |
| Foreign exchange forward contracts | **14.5** | – |
| Fuel price swaps | **–** | 4.3 |
| Interest rate swaps | **3.2** | 2.1 |
| Financial liabilities – Derivative financial instruments | **17.7** | 6.4 |
| Current financial liabilities | **444.1** | 50.0 |

An analysis of interest-bearing loans and borrowings is provided in note 29. Further information on derivative financial instruments is provided in note 31.

## 29 Interest-bearing loans and borrowings

The effective interest rates on loans and borrowings at the balance sheet date were as follows.

| | Maturity | 2007 £m | Effective interest rate | 2006 £m | Effective interest rate |
|---|---|---|---|---|---|
| Sterling loan notes | On demand | **0.8** | LIBOR + 1.0% | 0.8 | LIBOR + 1.0% |
| **Loan notes** | | **0.8** | | 0.8 | |
| Sterling bank loans | 2012–2015 | **17.5** | LIBOR + 0.2% | – | – |
| Short-term US dollar bank loans | January 2008 | **5.0** | LIBOR + 1.0% | 5.1 | LIBOR + 1.0% |
| US dollar bank loans subject to interest rate hedge | June 2011 | **50.0** | 7.3% | 51.0 | 7.3% |
| US dollar bank loans unhedged | June 2011 | **25.0** | LIBOR + 0.4% | 45.9 | LIBOR + 0.4% |
| Short-term Euro bank loans | 2008 | **27.2** | EURIBOR + 0.5% | 15.0 | EURIBOR + 0.5% |
| Euro bank loans unhedged | April 2008 | **216.8** | EURIBOR + 0.5% | – | – |
| Euro bank loans unhedged | June 2011 | **–** | – | 84.2 | EURIBOR + 0.4% |
| Euro bank loans subject to interest rate hedge | April 2008 | **150.7** | 4.6% | – | – |
| Euro bank loans subject to interest rate hedge | June 2011 | **473.7** | 4.6% | 235.8 | 3.6% |
| Canadian dollar bank loans | June 2011 | **–** | – | 41.1 | LIBOR + 0.4% |
| **Bank loans** | | **965.9** | | 478.1 | |
| US dollar finance leases at fixed rate | 2009–2012 | **18.1** | 3.6% | 21.4 | 3.6% |
| US dollar finance leases at floating rate | 2009–2012 | **21.9** | LIBOR – 0.3% | 25.0 | LIBOR – 0.3% |
| Euro finance leases at floating rate | 2008–2013 | **21.8** | EURIBOR + 0.5% | 6.0 | EURIBOR + 0.5% |
| Sterling finance leases at fixed rate | 2008–2018 | **34.1** | 5.4% | 37.4 | 5.4% |
| Sterling finance leases at floating rate | 2008 | **5.4** | LIBOR + 3.0% | 13.3 | LIBOR + 3.0% |
| **Finance leases** | | **101.3** | | 103.1 | |
| **Total** | | **1,068.0** | | 582.0 | |

The facility expiring on April 2008 was refinanced on 14 February 2008 with a new facility expiring in February 2009, with a one year extension to February 2010 at the Group's option.

Details of the Group's interest rate management strategy and interest rate swaps are included in notes 30 and 31.

The Group is subject to a number of covenants in relation to its borrowing facilities which, if contravened, would result in its loans becoming immediately repayable. These covenants specify maximum net debt to EBITDA and minimum EBITDA to interest.

The following table sets out the carrying amount, by maturity of the Group's financial instruments that are exposed to interest rate risk.

| **As at 31 December 2007** | < 1 year £m | 1–2 years £m | 2–3 years £m | 3–4 years £m | 4–5 years £m | > 5 years £m | **Total £m** |
|---|---|---|---|---|---|---|---|
| **Fixed rate** | | | | | | | |
| Bank loans | (155.7) | – | – | (523.6) | – | – | **(679.3)** |
| Finance leases | (9.5) | (5.7) | (5.3) | (4.6) | (3.3) | (23.8) | **(52.2)** |
| Net interest rate swaps | (1.7) | – | (4.5) | – | 0.8 | – | **(5.4)** |
| **Floating rate** | | | | | | | |
| Cash assets | 157.2 | – | – | – | – | – | **157.2** |
| Loan notes | (0.8) | – | – | – | – | – | **(0.8)** |
| Bank loans | (247.3) | (4.9) | (2.7) | (27.6) | (2.6) | (1.5) | **(286.6)** |
| Finance leases | (13.1) | (9.8) | (6.7) | (5.8) | (4.2) | (9.5) | **(49.1)** |

| As at 31 December 2006 | < 1 year £m | 1–2 years £m | 2–3 years £m | 3–4 years £m | 4–5 years £m | > 5 years £m | **Total £m** |
|---|---|---|---|---|---|---|---|
| **Fixed rate** | | | | | | | |
| Bank loans | – | – | – | – | (286.8) | – | **(286.8)** |
| Finance leases | (8.8) | (9.3) | (6.0) | (7.0) | (4.1) | (23.6) | **(58.8)** |
| Net interest rate swaps | (0.6) | – | – | (5.4) | – | – | **(6.0)** |
| **Floating rate** | | | | | | | |
| Cash assets | 143.6 | – | – | – | – | – | **143.6** |
| Loan notes | (0.8) | – | – | – | – | – | **(0.8)** |
| Bank loans | (20.1) | – | – | – | (171.2) | – | **(191.3)** |
| Finance leases | (13.9) | (9.6) | (4.4) | (3.5) | (1.7) | (11.2) | **(44.3)** |

# Notes to the Consolidated Accounts continued

## 30 Financial risk management objectives and policies

### Financial risk factors and management

The Group's multi-national operations and significant debt financing expose it to a variety of financial risks, the most material of which are the effects of changes in foreign currency exchange rates, interest rates and changes in fuel prices. The Group has in place a risk management programme that seeks to limit the adverse effects of these risks on the financial performance of the Group by using financial instruments including borrowings, forward exchange contracts, fuel price and interest rate swaps.

The Board of Directors have delegated to a sub-committee, the Treasury committee, the responsibility for implementing the risk management policies laid down by the Board. The policies are implemented by the central treasury department that receives regular reports from all the operating companies to enable prompt identification of financial risks so that appropriate actions may be taken. The treasury department has a policy and procedures manual that sets out specific guidelines to manage foreign currency exchange risk, interest rate risk and credit risk including the use of financial instruments.

### Foreign currency

The Group has major operations in the US, Canada, Spain and residual assets in Australia and as a result is exposed to foreign exchange risks on translation of net assets and on earnings denominated in foreign currency. The Group finances overseas investments mainly through the use of foreign currency borrowings to hedge the net asset investment. The Group has also entered into forward exchange contracts to hedge the foreign currency exposure of its overseas subsidiaries. These have the effect of increasing foreign currency denominated debt and reducing sterling debt. The forward exchange contract terms run for periods up to one year. The Group has a policy of hedging between 50% and 100% foreign currency denominated net assets. At 31 December 2007 81% (2006: 78%) of the Group's exposure to US dollar assets were hedged, 71% (2006: 92%) of the exposure to Canadian dollar assets, nil% (2006: 89%) of the exposure to Australian dollar assets and 97% (2006: 94%) of the exposure to Euro assets.

The table below demonstrates the sensitivity of the Group's financial instruments to a reasonably possible change in foreign currency exchange rates, with all other variables held constant. This would affect the Group's profit before tax and translation reserve. The effect on the translation reserve represents the movement in the translated value of the foreign currency denominated loans and forward contracts. These movements would be offset by a corresponding movement in the translated value of the Group's overseas net investments.

| | | **2007** | | 2006 | |
|---|---|---|---|---|---|
| **As at 31 December** | Strengthening/ (weakening) in currency | **Effect on profit before tax £m** | **Effect on translation reserve £m** | Effect on profit before tax £m | Effect on translation reserve £m |
| US dollar | 10% | **–** | **(19.9)** | – | (17.4) |
| Euro | 10% | **–** | **(87.2)** | – | (41.4) |
| Canadian dollar | 10% | **–** | **(8.8)** | – | (9.8) |
| Australian dollar | 10% | **–** | **–** | – | (2.6) |
| US dollar | (10)% | **–** | **19.9** | – | 17.4 |
| Euro | (10)% | **–** | **87.2** | – | 41.4 |
| Canadian dollar | (10)% | **–** | **8.8** | – | 9.8 |
| Australian dollar | (10)% | **–** | **–** | – | 2.6 |

### Interest rate risk

The Group is exposed to interest rate risk on both interest-bearing assets and interest-bearing liabilities. It is the Group's policy to maintain an appropriate balance between fixed and floating interest rates on borrowings in order to provide certainty as to the level of interest expense in the short term and to reduce the year on year impact of interest rate fluctuations over the medium term. Interest on the Group's floating interest rate debt is based on LIBOR or EURIBOR and, to achieve the above objectives, the Group has entered into a series of interest rate swaps that have the effect of converting floating rate debt to fixed rate debt. The net effect of these transactions was that as at 31 December 2007 the Group was hedged against interest rate movements on £731.5m (2006: £345.6m) of gross debt for an average of 3.0 (2006: 2.8) years.

The table below demonstrates the sensitivity of the Group's financial instruments to a reasonably possible change in interest rates, with all other variables held constant, on the Group's profit before tax and on the Group's hedging reserve. The effect on profit before tax arises through movements in interest on floating rate financial instruments. The effect on the hedging reserve represents the movement in the fair value of the Group's interest rate swaps.

The sensitivity analysis covers all floating rate financial instruments, including the interest rate swaps.

### 30 Financial risk management objectives and policies (continued)
#### Interest rate risk (continued)

| As at 31 December | Increase/ (decrease) in basis points | 2007 Effect on profit before tax £m | 2007 Effect on hedging reserve £m | 2006 Effect on profit before tax £m | 2006 Effect on hedging reserve £m |
|---|---|---|---|---|---|
| Sterling | 100 | **1.0** | **–** | 1.2 | – |
| US dollars | 50 | **(0.2)** | **0.6** | (0.3) | 0.6 |
| Euro | 75 | **(1.9)** | **9.5** | (0.7) | 1.9 |
| Sterling | (100) | **(1.0)** | **–** | (1.2) | – |
| US dollars | (50) | **0.2** | **(0.6)** | 0.3 | (0.6) |
| Euro | (75) | **1.9** | **(9.5)** | 0.7 | (1.9) |

### Commodity prices
The Group is exposed to commodity price risk as a result of fuel usage. It is the Group's policy to hedge this exposure in order to provide certainty as to the level of costs in the short-term and to reduce the year on year impact of price fluctuations over the medium term. This is achieved by entering into fuel swaps and purchase contracts which are expected to be highly effective. As at 31 December 2007, the Group had hedged approximately 58% of its 2008 expected usage and 31% of its 2009 expected usage.

The table below demonstrates the sensitivity of the Group's financial instruments to a reasonably possible change in fuel prices, with all other variables held constant, on the Group's profit before tax and on the Group's hedging reserve.

The sensitivity analysis includes all fuel price swaps. The effect on the hedging reserve arises through movements on the fair value of the Group's fuel price swaps.

| As at 31 December | Increase in price | 2007 Effect on profit before tax £m | 2007 Effect on hedging reserve £m | 2006 Effect on profit before tax £m | 2006 Effect on hedging reserve £m |
|---|---|---|---|---|---|
| Sterling denominated ULSD | 20% | **–** | **5.5** | – | 10.5 |
| US dollar denominated gasoil | 20% | **–** | **2.2** | – | 4.2 |
| Euro denominated ULSD | 20% | **–** | **6.2** | – | 5.2 |

### Credit risk
The maximum credit risk exposure of the Group is the gross carrying value of each of its financial assets. This risk is mitigated by a number of factors. The majority of the Group's receivables are public (or quasi-public) bodies, both national (DfT Rail and Network Rail in the UK) and local (school boards in North America, municipal authorities in Spain, Portugal and Morocco, Transport for London and Centro in the UK). The Group does not consider these counterparties to pose a significant credit risk. Outside of this the Group does not consider it has significant concentrations of credit risk. The Group has implemented policies that require appropriate credit checks on potential customers before sales commence.

The counterparties for financial assets other than investments and trade receivables are subject to pre-approval by the Treasury committee and such approval is limited to financial institutions with an A rating or better. The amount of exposure to any individual counterparty is subject to a limit, which is reassessed annually by the Treasury committee.

The only element of the Group's financial assets which are not impaired but are past due are certain trade receivable items. An ageing of the assets which are past due is included below.

| | Carrying amount £m | Of which: neither impaired nor past due £m | Of which: not impaired and past due in the following periods: Less than 30 days £m | Between 30 and 60 days £m | Between 61 and 90 days £m | Over 90 days £m |
|---|---|---|---|---|---|---|
| **Trade receivables at 31 December 2007** | **163.8** | **94.5** | **15.3** | **19.2** | **9.0** | **25.8** |
| Trade receivables at 31 December 2006 | 167.3 | 94.9 | 16.9 | 20.7 | 10.8 | 24.0 |

# Notes to the Consolidated Accounts continued

### 30 Financial risk management objectives and policies (continued)

**Liquidity risk**

The Group actively maintains a mixture of long-term and short-term committed facilities that are designed to ensure the Group has sufficient available funds to meet current and forecast financial requirements as cost effectively as possible. As at 31 December 2007 the Group had committed borrowing facilities of £1,167.5m (2006: £800m) of which £199.4m (2006: £247.8m) were undrawn. The Group's primary loan facilities expire in April 2008 and June 2011 and the lease facilities at various times in line with their terms.

The facility expiring on April 2008 was refinanced on 14 February 2008 with a new facility expiring in February 2009, with a one year extension to February 2010 at the Group's option.

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2007 and 2006 based on the contractual undiscounted payments.

| **Year ended 31 December 2007** | On demand £m | Less than 1 year £m | 1–5 years £m | > 5 years £m | **Total £m** |
|---|---|---|---|---|---|
| Loan notes | 0.8 | – | – | – | **0.8** |
| Bank loans | – | 440.0 | 619.8 | – | **1,059.8** |
| Finance lease obligations | – | 28.0 | 59.5 | 33.2 | **120.7** |
| Interest rate swaps | – | 2.4 | 5.6 | – | **8.0** |
| Foreign exchange forward contracts | – | 14.2 | – | – | **14.2** |
| Trade payables | 218.8 | – | – | – | **218.8** |
| ICRRL onerous contract obligation | – | 8.4 | 24.4 | – | **32.8** |
| | **219.6** | **493.0** | **709.3** | **33.2** | **1,455.1** |

| Year ended 31 December 2006 | On demand £m | Less than 1 year £m | 1–5 years £m | > 5 years £m | **Total £m** |
|---|---|---|---|---|---|
| Loan notes | 0.8 | – | – | – | **0.8** |
| Bank loans | – | 36.2 | 476.7 | – | **512.9** |
| Finance lease obligations | – | 27.3 | 57.0 | 39.7 | **124.0** |
| Interest rate swaps | – | 2.1 | 6.9 | – | **9.0** |
| Fuel price swaps | – | 4.3 | 2.6 | – | **6.9** |
| Trade payables | 187.3 | – | – | – | **187.3** |
| ICRRL onerous contract obligation | – | 9.3 | 32.0 | – | **41.3** |
| | **188.1** | **79.2** | **575.2** | **39.7** | **882.2** |

### 31 Financial instruments (including cash, trade receivables and payables)

**Fair values**

The fair value of foreign exchange forward contracts, fuel price and interest rate swaps has been determined by the third party financial institution with whom the Group holds the instrument, in line with the market value of similar financial instruments.

The fair value of the Group's financial assets and liabilities is equal to the carrying value, except for available for sale investments where there is no active market. In the absence of any other reliable external information, these assets are carried at amortised cost. The Group has no current plans to dispose of these assets.

| Classification of financial instruments **As at 31 December 2007** | Loans and receivables £m | Available for sale assets £m | Derivatives used for hedging £m | Liabilities measured at amortised cost £m | At fair value through profit or loss £m | **Total £m** |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Investments | – | 7.2 | – | – | – | **7.2** |
| Interest rate swaps | – | – | 3.2 | – | – | **3.2** |
| Fuel price swaps | – | – | 12.1 | – | – | **12.1** |
| Cash and cash equivalents | 157.2 | – | – | – | – | **157.2** |
| Trade receivables | 163.8 | – | – | – | – | **163.8** |
| | 321.0 | 7.2 | 15.3 | – | – | **343.5** |
| **Liabilities** | | | | | | |
| Loan notes | – | – | – | (0.8) | – | **(0.8)** |
| Bank loans | – | – | – | (965.9) | – | **(965.9)** |
| Finance lease obligations | – | – | – | (101.3) | – | **(101.3)** |
| Interest rate swaps | – | – | (7.7) | – | (0.9) | **(8.6)** |
| Foreign exchange forward contracts | – | – | (14.5) | – | – | **(14.5)** |
| Trade payables | – | – | – | (218.8) | – | **(218.8)** |
| ICRRL onerous contract obligation | – | – | – | (27.9) | – | **(27.9)** |
| | – | – | (22.2) | (1,314.7) | (0.9) | **(1,337.8)** |

**31 Financial instruments (including cash, trade receivables and payables) (continued)**
**Fair values (continued)**

| Classification of financial instruments<br>As at 31 December 2006 | Loans and receivables £m | Available for sale assets £m | Derivatives used for hedging £m | Liabilities measured at amortised cost £m | At fair value through profit or loss £m | Total £m |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Investments | – | 13.5 | – | – | – | 13.5 |
| Interest rate swaps | – | – | 1.8 | – | – | 1.8 |
| Foreign exchange forward contracts | – | – | 6.6 | – | – | 6.6 |
| Cash and cash equivalents | 143.6 | – | – | – | – | 143.6 |
| Trade receivables | 167.3 | – | – | – | – | 167.3 |
| | 310.9 | 13.5 | 8.4 | – | – | 332.8 |
| **Liabilities** | | | | | | |
| Loan notes | – | – | – | (0.8) | – | (0.8) |
| Bank loans | – | – | – | (478.1) | – | (478.1) |
| Finance lease obligations | – | – | – | (103.1) | – | (103.1) |
| Fuel price swaps | – | – | (6.9) | – | – | (6.9) |
| Interest rate swaps | – | – | (7.8) | – | – | (7.8) |
| Trade payables | – | – | – | (187.3) | – | (187.3) |
| ICRRL onerous contract obligation | – | – | – | (30.6) | – | (30,6) |
| | – | – | (14.7) | (799.9) | – | (814.6) |

The financial liabilities at fair value through profit or loss are held for trading. There is no difference between the fair value and the amount that would be required to settle the liability.

Other receivables and other payables are to be settled in cash in the currency they are held in.

In accordance with IAS 39, "Financial Instruments: Recognition and Measurement", the Group has reviewed all contracts for embedded derivatives that are required to be separately accounted for. No embedded derivatives have been identified.

**Hedging activities**
The movement on derivative financial instruments is detailed below:

| | Interest rate swaps £m | Foreign currency forward contracts £m | Fuel swaps £m | Total £m |
|---|---|---|---|---|
| Net (liability)/asset at 1 January 2007 | (6.0) | 6.6 | (6.9) | (6.3) |
| Cash settlements | (0.2) | – | (0.8) | (1.0) |
| Revaluation through income statement | (0.9) | – | – | (0.9) |
| Revaluation through SORIE | 1.6 | 0.4 | 19.5 | 21.5 |
| Exchange differences | 0.1 | (21.5) | 0.3 | (21.1) |
| **Net (liability)/asset at 31 December 2007** | **(5.4)** | **(14.5)** | **12.1** | **(7.8)** |

| | Interest rate swaps £m | Foreign currency forward contracts £m | Fuel swaps £m | Total £m |
|---|---|---|---|---|
| Net (liability)/asset at 1 January 2006 | (12.4) | (9.3) | 7.3 | (14.4) |
| Cash settlements | 2.4 | – | (0.8) | 1.6 |
| Revaluation through SORIE | 1.4 | (0.4) | (13.1) | (12.1) |
| Exchange differences | 2.6 | 16.3 | (0.3) | 18.6 |
| Net (liability)/asset at 31 December 2006 | **(6.0)** | **6.6** | **(6.9)** | **(6.3)** |

The movement on the hedging reserve is detailed below:

| | **2007 £m** | 2006 £m |
|---|---|---|
| At 1 January | **(9.0)** | (2.2) |
| Transferred to income statement – operating costs | **(0.7)** | (0.8) |
| Transferred to income statement – net finance costs | **(0.3)** | 2.4 |
| Revaluation, net of tax | **15.4** | (8.4) |
| **At 31 December** | **5.4** | (9.0) |

# Notes to the Consolidated Accounts continued

**31 Financial instruments (including cash, trade receivables and payables) (continued)**

**Interest hedges**

The Group has a number of interest rate swaps in place to hedge the cash flow risk in relation to interest rates. These instruments are summarised below:

a) A cash flow hedge with a total principal of US$100m that was entered into in September 2000 fixed at 6.8545% until September 2010.

b) A cash flow hedge with a principal of €150m that was entered into in December 2006 fixed at 3.77% until December 2008.

c) A cash flow hedge with a principal of €300m that was entered into in November 2007 fixed at 4.26% until August 2010.

d) A cash flow hedge with a principal of €150m that was entered into in December 2007 fixed at 4.24% until March 2010.

e) A cash flow hedge with a principal of €250m that was entered into in November 2007 fixed at 4.27% until May 2012.

f) An interest rate swap of US$100m that was entered into in September 2000 fixed at 6.9% and a separate US$100m interest rate swap that has the effect of fixing the accrued loss on the first swap. These instruments do not qualify for hedge accounting. The net effect on the income statement is immaterial.

The conditions of all swaps remaining in place at 31 December 2007 coincide with the material conditions of the underlying loans. The underlying cash flows are expected to take place periodically from 2008 to 2012 and will affect profit or loss over the same period of time.

The benchmark rate for floating rate financial liabilities is the relevant interbank borrowing rate.

During the year £0.2m (2006: £2.4m) has been transferred from the hedging reserve to the income statement in respect of interest rate swaps, no ineffectiveness was recognised in the income statement.

**Hedge of net investments in foreign entities**

Included in bank loans are borrowings of US$150.0m (£75.6m) (2006: US$190.0m (£96.9m)), CAN$nil (£nil) (2006: CAN$96.0m (£41.1m)) and €1,145.0m (£841.6m) (2006: €475.0m (£320.0m)) which have been designated as a hedge of net investments in the foreign currency denominated net assets of the Group and are being used to reduce the exposure to foreign exchange risk. In addition the Group has synthetic debt in the form of foreign currency forward contracts in place split between US$283.8m (£143.0m) (2006: US$185.0m (£94.4m)), CAN$192.1m (£97.1m) (2006: CAN$150.0m (£65.7m)), AUD$nil (£nil) (2006: AUD$72.0m (£29.0m)) and €160.0m (£117.6m) (2006: €200.5m (£135.1m)) to complete the post-tax hedge of the net investment in foreign entities. The portion of the gain or loss on the foreign currency forward contracts that is determined to be an effective hedge is recognised directly in equity and, to this extent, offsets any gains or losses on translation of the net investments in the subsidiaries. No ineffectiveness has been recognised in the income statement.

**Fuel price hedges**

The Group has a number of fuel price swaps in place to hedge the different types of fuel used in each division. Ultra low sulphur diesel and gasoil as used in the UK Bus, UK Coach, UK Trains and European Coach & Bus divisions are hedged by swaps in the same type of fuel. Diesel used in the North American division is hedged by heating oil swaps. The timing of the swap cash flows will match the underlying fuel purchases during 2008 and 2009.

During the year £0.8m (2006: £0.8m) has been transferred from the hedging reserve, of which a £4.3m debit (2006: £6.7m) was recognised in the hedging reserve at 1 January 2007 and the remainder was generated during the year due to the movement in market fuel prices.

Fuel price swaps can be analysed as follows:

| | **31 December 2007 £m** | 31 December 2006 £m | **31 December 2007 Volume million litres** | 31 December 2006 Volume million litres |
|---|---|---|---|---|
| Sterling denominated fuel swaps – UK Bus, UK Coach and UK Trains | **4.7** | (1.6) | **57.0** | 131.5 |
| US dollar denominated fuel swaps – North American Bus | **1.5** | (1.5) | **23.3** | 45.4 |
| Euro denominated fuel swaps – European Coach & Bus | **2.3** | (1.2) | **48.8** | 44.4 |
| Fuel price swaps included in current assets/(liabilities) | **8.5** | (4.3) | **129.1** | 221.3 |
| Sterling denominated fuel swaps – UK Bus, UK Coach and UK Trains | **1.7** | (0.7) | **24.0** | 72.0 |
| US dollar denominated fuel swaps – North American Bus | **0.4** | (0.9) | **11.4** | 34.6 |
| Euro denominated fuel swaps – European Coach & Bus | **1.5** | (1.0) | **34.5** | 58.8 |
| Fuel price swaps included in non-current assets/(liabilities) | **3.6** | (2.6) | **69.9** | 165.4 |
| **Total fuel price swaps** | **12.1** | (6.9) | **199.0** | 386.7 |

**Interest swap at fair value through profit or loss**

The Group has entered into a series of one year basis swaps, where the company pays six month EURIBOR less a margin and receives one month EURIBOR. These swaps were entered into in November 2007 and expire in November 2008. The Group did not seek to obtain hedge accounting for these instruments. The fair value at 31 December 2007 was a liability of £0.9m.

## 32 Called-up share capital

| | 2007 £m | 2006 £m |
|---|---|---|
| At 31 December: | | |
| Authorised: | | |
| 200,000,000 (2006: 200,000,000) ordinary shares of 5p each | **10.0** | 10.0 |
| Issued called-up and fully paid: | | |
| 154,627,671 (2006: 153,835,012) ordinary shares of 5p each | **7.7** | 7.7 |

| Movement in ordinary shares during the year: | £m | Number of shares |
|---|---|---|
| At 1 January 2006 | 7.5 | 150,920,310 |
| Exercise of share options | 0.2 | 2,914,702 |
| At 1 January 2007 | 7.7 | 153,835,012 |
| Exercise of share options | – | 792,659 |
| **At 31 December 2007** | **7.7** | **154,627,671** |

The total number of share options exercised in the year was 1,008,457 (2006: 3,100,807) of which 792,659 (2006: 2,914,702) exercises were satisfied by newly issued shares and 215,798 (2006: 186,105) exercises were satisfied by transferring shares from the National Express Employee Benefit Trust.

## 33 Share capital and reserves

| | Share capital £m | Share premium £m | Capital redemption reserve £m | Own shares £m | Other reserves (note 34) £m | Retained earnings £m | Total £m | Minority interests £m | Total equity £m |
|---|---|---|---|---|---|---|---|---|---|
| At 1 January 2007 | 7.7 | 189.8 | 0.2 | (16.7) | 7.9 | 153.3 | 342.2 | 3.3 | 345.5 |
| Shares issued | – | 5.5 | – | – | – | – | 5.5 | – | 5.5 |
| Own shares released to satisfy employee share schemes | – | – | – | 0.4 | – | (0.4) | – | – | – |
| Total recognised income and expense | – | – | – | – | 22.8 | 117.5 | 140.3 | 0.7 | 141.0 |
| Share-based payments | – | – | – | – | – | 3.2 | 3.2 | – | 3.2 |
| Dividends | – | – | – | – | – | (54.0) | (54.0) | – | (54.0) |
| Dividends paid to minority interest | – | – | – | – | – | – | – | (0.1) | (0.1) |
| **At 31 December 2007** | **7.7** | **195.3** | **0.2** | **(16.3)** | **30.7** | **219.6** | **437.2** | **3.9** | **441.1** |

| | Share capital £m | Share premium £m | Capital redemption reserve £m | Own shares £m | Other reserves (note 34) £m | Retained earnings £m | Total £m | Minority interests £m | Total equity £m |
|---|---|---|---|---|---|---|---|---|---|
| At 1 January 2006 | 7.5 | 174.2 | 0.2 | (5.1) | 24.5 | 108.1 | 309.4 | 2.9 | 312.3 |
| Shares issued | 0.2 | 15.6 | – | – | – | – | 15.8 | – | 15.8 |
| Shares purchased | – | – | – | (11.6) | – | – | (11.6) | – | (11.6) |
| Total recognised income and expense | – | – | – | – | (16.6) | 93.3 | 76.7 | 0.8 | 77.5 |
| Share-based payments | – | – | – | – | – | 2.0 | 2.0 | – | 2.0 |
| Dividends | – | – | – | – | – | (50.1) | (50.1) | – | (50.1) |
| Dividends paid to minority interest | – | – | – | – | – | – | – | (0.4) | (0.4) |
| At 31 December 2006 | 7.7 | 189.8 | 0.2 | (16.7) | 7.9 | 153.3 | 342.2 | 3.3 | 345.5 |

Own shares comprise treasury shares and shares held in the Employee Benefit Trust.

Treasury shares include 1,825,000 (2006: 1,825,000) ordinary shares in the Company. During the year, the Group repurchased no (2006: 1,425,000) shares for consideration of £nil (2006: £11.6m). No additional (2006: 1,425,000) shares have been retained as treasury shares within equity for future issue under the Group's share schemes or cancellation. No shares were cancelled during the year (2006: nil). The market value of these shares at 31 December 2007 was £22.7m (2006: £20.6m).

Own shares include 447,554 (2006: 663,352) ordinary shares in the Company that have been purchased by the Trustees of the National Express Employee Benefit Trust (the "Trust"). During the year, the Trust purchased no (2006: nil) shares and 215,798 (2006: 186,105) shares were used to satisfy options granted under a number of the Company's share schemes. The value of shares within the Trust has been recognised as an investment in treasury shares. The market value of these shares at 31 December 2007 was £5.6m (2006: £7.5m). The dividends payable on these shares have been waived.

The Group's definition and management of capital is included in the OFR.

# Notes to the Consolidated Accounts continued

## 34 Other reserves

| | Merger reserve £m | Hedging reserve £m | Translation reserve £m | Total £m |
|---|---|---|---|---|
| At 1 January 2007 | 15.4 | (9.0) | 1.5 | 7.9 |
| Hedge movements, net of tax | – | 14.4 | – | 14.4 |
| Exchange differences, net of tax | – | – | 8.4 | 8.4 |
| **At 31 December 2007** | **15.4** | **5.4** | **9.9** | **30.7** |

| | Merger reserve £m | Hedging reserve £m | Translation reserve £m | Total £m |
|---|---|---|---|---|
| At 1 January 2006 | 15.4 | (2.2) | 11.3 | 24.5 |
| Hedge movements, net of tax | – | (6.8) | – | (6.8) |
| Exchange differences, net of tax | – | – | (9.8) | (9.8) |
| At 31 December 2006 | 15.4 | (9.0) | 1.5 | 7.9 |

The nature and purpose of the other reserves are as follows:

- The merger reserve includes the premium on shares issued to satisfy the purchase of Prism Rail PLC in 2000. The reserve is not distributable.
- The hedging reserve records the movements on designated hedging items, offset by any movements recognised directly in equity on underlying hedged items.
- The translation reserve records exchange differences arising from the translation of the accounts of foreign currency denominated subsidiaries offset by the movements on loans and derivatives used to hedge the net investment in foreign subsidiaries.

## 35 Pensions and other post-employment benefits

### (a) Summary of pension benefits and assumptions

The UK Bus and UK Coach divisions operate both funded defined benefit schemes and a defined contribution scheme. The majority of employees of the UK Trains companies are members of the appropriate shared-cost section of the Railways Pension Scheme (“RPS”), a funded defined benefit scheme. The assets of all schemes are held separately from those of the Group. Contributions to the schemes are determined by independent professionally qualified actuaries.

Subsidiaries in North America contribute to a number of defined contribution plans. The Group also provides certain additional unfunded post-employment benefits to employees in North America and Spain, which are disclosed in section c) in the Other category.

The total pension cost for the year was £27.5m (2006: £23.9m), of which £3.2m (2006: £3.4m) relates to the defined contribution schemes.

The defined benefit pension liability included in the balance sheet is as follows:

| | **2007 £m** | 2006 £m |
|---|---|---|
| UK Bus | **(5.1)** | (17.3) |
| UK Coach | **(4.9)** | (12.7) |
| UK Trains | **(18.8)** | (21.1) |
| Other | **(1.0)** | (1.7) |
| Total | **(29.8)** | (52.8) |

The valuations conducted for financial reporting purposes are based on the triennial actuarial valuations. A summary of the latest triennial actuarial valuations, and assumptions made, is as follows. Triennial valuations of the Travel West Midlands and UK Coach schemes have taken place during the year, however the results have not yet been finalised.

| | UK Bus | | UK Coach | UK Train |
|---|---|---|---|---|
| Date of actuarial valuation | Tayside 31 March 2005 | Travel West Midlands 31 March 2004 | 5 April 2004 | 31 December 2004 |
| Actuarial method used | Projected unit | Attained age* | Projected unit | Projected unit |
| Rate of investment returns per annum | 6.0% | 5.6%–6.6% | 5.2%–6.0% | 4.8%–6.8% |
| Increase in earnings per annum | 4.3% | 4.3% | 4.7% | 4.3% |
| Scheme assets taken at market value | £34.9m | £300.7m | £25.3m | £638.9m |
| Funding level | 89% | 88% | 65% | 86%–95% |

*Amounts included in the income statement, statement of recognised income and expense and the balance sheet are calculated using the projected unit method.

The range of funding levels for UK Trains reflects the range of funding levels in the various sections of the RPS. The plans do not provide medical benefits.

## 35 Pensions and other post-employment benefits (continued)

### (a) Summary of pension benefits and assumptions (continued)

The most recent triennial valuations are then updated by independent professionally qualified actuaries for financial reporting purposes, in accordance with IAS 19. The main actuarial assumptions underlying the IAS 19 valuations are:

| | 2007 | | | 2006 | | |
|---|---|---|---|---|---|---|
| | **UK Bus** | **UK Coach** | **UK Trains** | UK Bus | UK Coach | UK Trains |
| Rate of increase in salaries | **4.3%** | **4.3%** | **4.8%** | 4.0% | 4.0% | 4.5% |
| Rate of increase of pensions | **3.3%** | **3.3%** | **3.3%** | 3.0% | 3.0% | 3.0% |
| Discount rate | **5.8%** | **5.8%** | **5.8%** | 5.1% | 5.1% | 5.1% |
| Inflation assumption | **3.3%** | **3.3%** | **3.3%** | 3.0% | 3.0% | 3.0% |
| Expected rates of return on scheme assets | | | | | | |
| Equities | **8.0%** | **8.0%** | **8.0%** | 7.9% | 7.9% | 7.9% |
| Bonds | **5.8%** | **5.8%** | **5.8%** | 5.1% | 5.1% | 5.1% |
| Properties | **6.3%** | **6.3%** | **6.3%** | 6.2% | 6.2% | 6.2% |
| Other | **4.8%** | **4.8%** | **4.8%** | 4.3% | 4.3% | 4.3% |
| Post-retirement mortality in years: | | | | | | |
| Current pensioners at 65 – male | **19.4** | **21.9** | **17.8** | 17.8 | 21.3 | 17.8 |
| Current pensioners at 65 – female | **22.2** | **24.8** | **20.1** | 20.7 | 24.2 | 20.1 |
| Future pensioners at 65 – male | **20.3** | **23.0** | **18.8** | 19.4 | 23.1 | 18.8 |
| Future pensioners at 65 – female | **23.1** | **25.8** | **21.3** | 22.4 | 25.9 | 21.3 |

The demographic assumptions reflect those included in the most recent triennial valuation. For the RPS, mortality assumptions are based on the recent experience of the scheme with an allowance for future improvements in mortality.

Scheme assets are stated at their market values at the respective balance sheet dates. The expected rate of return on scheme assets is determined based on market returns on each category of scheme assets.

### (b) Accounting for the Railways Pension Scheme

The majority of employees of the UK Train companies are members of the appropriate section of the RPS, a funded defined benefit scheme. The RPS is a shared cost scheme, which means that costs are formally shared 60% employer and 40% employee. To date, the Group has experienced nine changes of UK Train franchise ownership where the current owner has funded the scheme during the franchise term and the pension deficit at franchise exit has transferred to the new owner, without cash settlement. However, although the Group's past experience has proven otherwise, our legal advisors have opined that in certain situations, the liability for the deficit on the relevant sections of the RPS could theoretically crystallise for funding by an individual TOC at the end of the franchise. By entering into the franchise contract, the TOC becomes the designated employer for the term of the contract and under the rules of the RPS must fund its share of the pension liability in accordance with the schedule of contributions agreed with the Scheme trustees and actuaries and for which there is no funding cap set out in the franchise contract.

To comply with IAS 19, the Group is required to account for its legal obligation under the formal terms of the RPS and its constructive obligation that arises under the terms of each franchise agreement.

In determining the appropriate accounting policy for the RPS to ensure that the Group's accounts present fairly its financial position, financial performance and cash flows, management has consulted with TOC industry peers and has concluded that the Group's constructive but not its legal RPS defined benefit obligations should be accounted for in accordance with IAS 19. This accounting policy, which in all other respects is consistent with that set out in this note for the Group's other defined benefit schemes, means that the Group's accounts reflect that element of the deficits anticipated to be settled by the Group during the franchise term and will prevent gains arising on transfer of the existing RPS deficits to a new owner at franchise exit.

In calculating the Group's constructive obligations in respect of the RPS, the Group has calculated the total pension deficits in each of the RPS sections in accordance with IAS 19 and the assumptions set out above. These deficits are reduced by a "franchise adjustment" which is that portion of the deficit projected to exist at the end of the franchise and for which the Group will not be required to fund. The franchise adjustment, which has been calculated by the Group's actuaries, is offset against the present value of the RPS liabilities so as to fairly present the financial performance, position and cash flows of the Group's obligations.

The franchise adjustment decreased from £44.4m at 31 December 2006 to £2.3m at 31 December 2007. The decrease is caused by interest on the franchise adjustment of £2.1m offset by net actuarial movements of £29.4m and by £14.8m relating to the franchise exits. In the prior year, the franchise adjustment decreased by £26.6m from £71.0m at 1 January 2006 to £44.4m at 31 December 2006. The decrease was caused by interest on the franchise adjustment of £2.5m offset by net actuarial movements in scheme liabilities of £6.7m and by £22.4m relating to franchise exits.

# Notes to the Consolidated Accounts continued

### 35 Pensions and other post-employment benefits (continued)

#### (b) Accounting for the Railways Pension Scheme (continued)

If the Group had accounted for its legal obligation in respect of the RPS instead of the constructive obligation, the following adjustments would have been made to the financial information:

| | 2007 £m | 2006 £m |
|---|---|---|
| **Balance sheet** | | |
| Defined benefit pension deficit | **(2.3)** | (44.4) |
| Deferred tax asset | **–** | 13.6 |
| Intangible asset | **3.0** | 3.3 |
| **Net increase/(reduction) in net assets** | **0.7** | (27.5) |
| **Statement of recognised income and expense** | | |
| Actuarial gains | **29.4** | 6.7 |
| Tax on actuarial gains and losses | **(9.8)** | (0.3) |
| **Net increase in actuarial gains** | **19.6** | 6.4 |
| **Income statement** | | |
| Interest on franchise adjustment | **(2.1)** | (2.5) |
| Curtailment gain on franchise exit | **14.8** | 22.4 |
| Intangible asset amortisation | **(0.3)** | 0.2 |
| Deferred tax charge | **(3.8)** | (6.2) |
| **Net increase in income** | **8.6** | 13.9 |

#### (c) Financial results for pension benefits

The amounts charged to the Group income statement and Group statement of recognised income and expense for the years ended 31 December 2007 and 2006 are set out in the following tables. The restriction on surplus arises on the Tayside UK Bus scheme.

Year ended 31 December 2007

| Group income statement | UK Bus 2007 £m | UK Coach 2007 £m | UK Trains 2007 £m | Other 2007 £m | Total 2007 £m |
|---|---|---|---|---|---|
| Amounts charged to normalised operating profit: | | | | | |
| Current service cost | **(5.1)** | **(1.5)** | **(30.2)** | **(0.3)** | **(37.1)** |
| Past service credit | **0.7** | **–** | **–** | **–** | **0.7** |
| Expected return on pension scheme assets | **25.2** | **2.6** | **31.9** | **–** | **59.7** |
| Interest on pension liabilities | **(21.1)** | **(2.7)** | **(25.9)** | **–** | **(49.7)** |
| Interest on franchise adjustment | **–** | **–** | **2.1** | **–** | **2.1** |
| Total charge to income statement | **(0.3)** | **(1.6)** | **(22.1)** | **(0.3)** | **(24.3)** |
| Actual return on plan assets | **20.0** | **2.0** | **35.1** | **–** | **57.1** |

| Group statement of recognised income and expense | UK Bus 2007 £m | UK Coach 2007 £m | UK Trains 2007 £m | Other 2007 £m | Total 2007 £m |
|---|---|---|---|---|---|
| Actual return less expected return on pension scheme assets | **(5.2)** | **(0.6)** | **3.2** | **–** | **(2.6)** |
| Other actuarial gains and losses | **12.6** | **7.5** | **(2.6)** | **–** | **17.5** |
| Adjustment for unrecognised surplus | **(3.2)** | **–** | **–** | **–** | **(3.2)** |
| Actuarial gain | **4.2** | **6.9** | **0.6** | **–** | **11.7** |

Year ended 31 December 2006

| Group income statement | UK Bus 2006 £m | UK Coach 2006 £m | UK Trains 2006 £m | Other 2006 £m | Total 2006 £m |
|---|---|---|---|---|---|
| Amounts charged to normalised operating profit: | | | | | |
| Current service cost | (6.1) | (1.7) | (32.6) | (0.2) | (40.6) |
| Expected return on pension scheme assets | 24.4 | 2.3 | 30.8 | – | 57.5 |
| Interest on pension liabilities | (20.0) | (2.5) | (24.1) | – | (46.6) |
| Interest on franchise adjustment | – | – | 2.5 | – | 2.5 |
| Charge to normalised operating profit | (1.7) | (1.9) | (23.4) | (0.2) | (27.2) |
| Past service credit (within exceptional items) | 4.9 | 1.8 | – | – | 6.7 |
| Total charge to income statement | 3.2 | (0.1) | (23.4) | (0.2) | (20.5) |
| Actual return on plan assets | 31.9 | 2.3 | 63.4 | – | 97.6 |

## 35 Pensions and other post-employment benefits (continued)
### (c) Financial results for pension benefits (continued)

| Group statement of recognised income and expense | UK Bus 2006 £m | UK Coach 2006 £m | UK Trains 2006 £m | Other 2006 £m | Total 2006 £m |
|---|---|---|---|---|---|
| Actual return less expected return on pension scheme assets | 7.5 | – | 32.6 | – | 40.1 |
| Other actuarial gains and losses | 3.0 | (0.5) | (20.5) | – | (18.0) |
| Adjustment for unrecognised surplus | (1.5) | – | – | – | (1.5) |
| Actuarial gain/(loss) | 9.0 | (0.5) | 12.1 | – | 20.6 |

The amounts recognised in the balance sheet at 31 December are:

As at 31 December 2007

| | **UK Bus 2007 £m** | **UK Coach 2007 £m** | **UK Trains 2007 £m** | **Other 2007 £m** | **Total 2007 £m** |
|---|---|---|---|---|---|
| Equities | **228.0** | **21.4** | **510.0** | **–** | **759.4** |
| Bonds | **175.0** | **21.9** | **62.4** | **–** | **259.3** |
| Property | **4.0** | **–** | **47.4** | **–** | **51.4** |
| Other | **5.0** | **0.4** | **0.5** | **–** | **5.9** |
| Fair value of scheme assets | **412.0** | **43.7** | **620.3** | **–** | **1,076.0** |
| Present value of scheme liabilities | **(412.4)** | **(48.6)** | **(655.4)** | **(1.0)** | **(1,117.4)** |
| Franchise adjustment | **–** | **–** | **2.3** | **–** | **2.3** |
| Defined benefit obligation | **(412.4)** | **(48.6)** | **(653.1)** | **(1.0)** | **(1,115.1)** |
| Restriction on surplus | **(4.7)** | **–** | **–** | **–** | **(4.7)** |
| Members' share of deficit | **–** | **–** | **14.0** | **–** | **14.0** |
| Defined benefit pension deficit | **(5.1)** | **(4.9)** | **(18.8)** | **(1.0)** | **(29.8)** |

As at 31 December 2006

| | UK Bus 2006 £m | UK Coach 2006 £m | UK Trains 2006 £m | Other 2006 £m | Total 2006 £m |
|---|---|---|---|---|---|
| Equities | 228.9 | 19.6 | 593.3 | – | 841.8 |
| Bonds | 169.1 | 20.0 | 78.4 | – | 267.5 |
| Property | 4.0 | – | 70.9 | – | 74.9 |
| Other | 4.0 | 0.3 | 0.8 | – | 5.1 |
| Fair value of scheme assets | 406.0 | 39.9 | 743.4 | – | 1,189.3 |
| Present value of scheme liabilities | (421.8) | (52.6) | (852.6) | (1.7) | (1,328.7) |
| Franchise adjustment | – | – | 44.4 | – | 44.4 |
| Defined benefit obligation | (421.8) | (52.6) | (808.2) | (1.7) | (1,284.3) |
| Restriction on surplus | (1.5) | – | – | – | (1.5) |
| Members' share of deficit | – | – | 43.7 | – | 43.7 |
| Defined benefit pension deficit | (17.3) | (12.7) | (21.1) | (1.7) | (52.8) |

The movement in the present value of the defined benefit obligation in the year is as stated below. For UK Trains, the RPS is a shared cost scheme, which means that costs are formally shared 60% employer and 40% employee.

# Notes to the Consolidated Accounts continued

### 35 Pensions and other post-employment benefits (continued)
### (c) Financial results for pension benefits (continued)

The Group's defined benefit obligation comprises £1,114.1m (2006: £1,282.6m) arising from plans that are wholly or partly funded and £1.0m (2006: £1.7m) from unfunded plans.

| | UK Bus £m | UK Coach £m | UK Trains £m | Other £m | **Total £m** |
|---|---|---|---|---|---|
| Defined benefit obligation at 1 January 2007 | (421.8) | (52.6) | (808.2) | (1.7) | **(1,284.3)** |
| Current service cost | (5.1) | (1.5) | (30.2) | (0.3) | **(37.1)** |
| Past service credit | 0.7 | – | – | – | **0.7** |
| Franchise entry | – | – | (277.6) | – | **(277.6)** |
| Franchise exit | – | – | 419.3 | – | **419.3** |
| Curtailment | – | – | 55.9 | – | **55.9** |
| Benefits paid | 23.7 | 1.1 | 21.5 | 1.0 | **47.3** |
| Contributions by employees | (1.4) | (0.4) | (13.7) | – | **(15.5)** |
| Finance charge | (21.1) | (2.7) | (25.9) | – | **(49.7)** |
| Interest on franchise adjustment | – | – | 2.1 | – | **2.1** |
| Members' share of movement on liabilities | – | – | 6.3 | – | **6.3** |
| Actuarial gain/(loss) recognised in statement of recognised income and expense | 12.6 | 7.5 | (2.6) | – | **17.5** |
| **Defined benefit obligation at 31 December 2007** | (412.4) | (48.6) | (653.1) | (1.0) | **(1,115.1)** |

| | UK Bus £m | UK Coach £m | UK Trains £m | Other £m | Total £m |
|---|---|---|---|---|---|
| Defined benefit obligation at 1 January 2006 | (423.6) | (50.6) | (900.7) | (1.9) | (1,376.8) |
| Current service cost | (6.1) | (1.7) | (32.6) | (0.2) | (40.6) |
| Past service credit | 4.9 | 1.8 | – | – | 6.7 |
| Franchise extension | – | – | (0.3) | – | (0.3) |
| Franchise exit | – | – | 176.2 | – | 176.2 |
| Benefits paid | 21.4 | 1.4 | 22.4 | 0.2 | 45.4 |
| Contributions by employees | (1.4) | (0.5) | (14.9) | – | (16.8) |
| Finance charge | (20.0) | (2.5) | (24.1) | – | (46.6) |
| Interest on franchise adjustment | – | – | 2.5 | – | 2.5 |
| Members' share of movement on liabilities | – | – | (16.2) | – | (16.2) |
| Exchange differences | – | – | – | 0.2 | 0.2 |
| Actuarial gain/(loss) recognised in statement of recognised income and expense | 3.0 | (0.5) | (20.5) | – | (18.0) |
| Defined benefit obligation at 31 December 2006 | (421.8) | (52.6) | (808.2) | (1.7) | (1,284.3) |

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

| | UK Bus £m | UK Coach £m | UK Trains £m | **Total £m** |
|---|---|---|---|---|
| Fair value of scheme assets at 1 January 2007 | 406.0 | 39.9 | 743.4 | **1,189.3** |
| Expected return on plan assets | 25.2 | 2.6 | 31.9 | **59.7** |
| Franchise entry | – | – | 277.6 | **277.6** |
| Franchise exit | – | – | (419.3) | **(419.3)** |
| Curtailment | – | – | (55.9) | **(55.9)** |
| Cash contributions – Employer | 8.3 | 2.5 | 23.8 | **34.6** |
| Cash contributions – Employee | 1.4 | 0.4 | 13.7 | **15.5** |
| Benefits paid | (23.7) | (1.1) | (21.5) | **(46.3)** |
| Members' share of return on assets | – | – | 23.4 | **23.4** |
| Actuarial gain/(loss) recognised in statement of recognised income and expense | (5.2) | (0.6) | 3.2 | **(2.6)** |
| **Fair value of scheme assets at 31 December 2007** | 412.0 | 43.7 | 620.3 | **1,076.0** |

| | UK Bus £m | UK Coach £m | UK Trains £m | Total £m |
|---|---|---|---|---|
| Fair value of scheme assets at 1 January 2006 | 385.8 | 35.7 | 796.4 | 1,217.9 |
| Expected return on plan assets | 24.4 | 2.3 | 30.8 | 57.5 |
| Franchise exit | – | – | (176.2) | (176.2) |
| Cash contributions – Employer | 8.3 | 2.8 | 24.7 | 35.8 |
| Cash contributions – Employee | 1.4 | 0.5 | 14.9 | 16.8 |
| Benefits paid | (21.4) | (1.4) | (22.4) | (45.2) |
| Members' share of return on assets | – | – | 42.6 | 42.6 |
| Actuarial gain recognised in statement of recognised income and expense | 7.5 | – | 32.6 | 40.1 |
| Fair value of scheme assets at 31 December 2006 | 406.0 | 39.9 | 743.4 | 1,189.3 |

The Group expects to contribute £31.7m to its defined benefit pension plans in 2008.

### 35 Pensions and other post-employment benefits)
### (c) Financial results for pension benefits (continued)

| History of experience gains and losses: | **2007 £m** | 2006 £m | 2005 £m | 2004 £m |
|---|---|---|---|---|
| **UK Bus** | | | | |
| Fair value of scheme assets | **412.0** | 406.0 | 385.8 | 338.0 |
| Present value of defined benefit obligation | **(412.4)** | (421.8) | (423.6) | (374.2) |
| Restriction on surplus to be recognised | **(4.7)** | (1.5) | – | – |
| Deficit in the scheme | **(5.1)** | (17.3) | (37.8) | (36.2) |
| Experience adjustments arising on liabilities | **(4.6)** | (3.0) | (3.3) | 24.9 |
| Experience adjustments arising on assets | **(5.2)** | 7.5 | 35.3 | 9.8 |
| **UK Coach** | | | | |
| Fair value of scheme assets | **43.7** | 39.9 | 35.7 | 28.7 |
| Present value of defined benefit obligation | **(48.6)** | (52.6) | (50.6) | (39.7) |
| Deficit in the scheme | **(4.9)** | (12.7) | (14.9) | (11.0) |
| Experience adjustments arising on liabilities | **(2.2)** | (1.6) | – | (0.4) |
| Experience adjustments arising on assets | **(0.6)** | – | 2.5 | 1.7 |
| **UK Trains** | | | | |
| Fair value of scheme assets | **620.3** | 743.4 | 796.4 | 634.4 |
| Present value of defined benefit obligation | **(653.1)** | (808.2) | (900.7) | (709.3) |
| Members' share of deficit | **14.0** | 43.7 | 70.1 | 57.0 |
| Deficit in the scheme | **(18.8)** | (21.1) | (34.2) | (17.9) |
| Experience adjustments arising on liabilities | **(5.3)** | (25.5) | (53.8) | (13.0) |
| Experience adjustments arising on assets | **3.2** | 32.6 | 54.4 | 10.9 |
| **Other** | | | | |
| Fair value of scheme assets | **–** | – | – | – |
| Present value of defined benefit obligation | **(1.0)** | (1.7) | (1.9) | (0.6) |

The cumulative amount of actuarial gains and losses recognised in the statement of recognised income and expense since 1 January 2004 is £2.0m loss (2006: £13.7m loss). The Directors are unable to determine how much of the pension scheme deficit recognised on transition to IFRSs and taken directly to equity of £51.9m is attributable to actuarial gains and losses since inception of those pension schemes. Consequently the Directors are unable to determine the amount of actuarial gains and losses that would have been recognised in the statement of recognised income and expense before 1 January 2004.

### 36 Commitments and contingencies
### Operating lease commitments

The Group's total operating lease commitments are as follows:

| | | **2007 £m** | 2006 £m |
|---|---|---|---|
| Future minimum rentals payable under non-cancellable operating leases: | | | |
| Within one year: | Land and buildings | **364.8** | 394.1 |
| | Plant and equipment | **198.3** | 215.8 |
| | | **563.1** | 609.9 |
| After one year but not more than five years: | Land and buildings | **1,031.4** | 609.8 |
| | Plant and equipment | **563.6** | 433.1 |
| | | **1,595.0** | 1,042.9 |
| More than five years: | Land and buildings | **13.5** | 15.7 |
| | Plant and equipment | **121.6** | 1.2 |
| | | **135.1** | 16.9 |
| | | **2,293.2** | 1,669.7 |

# Notes to the Consolidated Accounts continued

### 36 Commitments and contingencies (continued)

The majority of the Group's commitments arise in the UK Trains division. Trains division companies have contracts with Network Rail Infrastructure Limited for access to the railway infrastructure (tracks, stations and depots). They also have contracts under which rolling stock is leased. The TOC's obligations to fulfil these commitments exist only as part of their franchise agreement. The table below reflects the commitments up to the current franchise end dates unless an extension or new franchise agreement has been signed. The commitments are based on charges advised by the Rail Regulator for the period starting on 1 April 2004. Commitments for future minimum rental payments under these contracts are shown below:

| | | Land and buildings | | Plant and equipment | |
|---|---|---|---|---|---|
| UK Trains division commitments: | | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| Future minimum rentals payable under non-cancellable operating leases: | | | | | |
| Within one year: | Fixed track access | **302.9** | 329.2 | **–** | – |
| | Rolling stock | **–** | – | **191.9** | 209.0 |
| | Other | **50.3** | 55.4 | **1.8** | 2.2 |
| | | **353.2** | 384.6 | **193.7** | 211.2 |
| After one year but not more than five years: | Fixed track access | **866.5** | 479.4 | **–** | – |
| | Rolling stock | **–** | – | **551.6** | 419.7 |
| | Other | **139.2** | 105.7 | **3.9** | 5.5 |
| | | **1,005.7** | 585.1 | **555.5** | 425.2 |
| More than five years: | Fixed track access | **–** | – | **–** | – |
| | Rolling stock | **–** | – | **120.8** | – |
| | Other | **–** | 0.1 | **0.7** | 1.2 |
| | | **–** | 0.1 | **121.5** | 1.2 |
| | | **1,358.9** | 969.8 | **870.7** | 637.6 |

Fixed track access agreements have an average remaining life of 4.2 years (2006: 3.6 years), other land and buildings have an average duration of 3.6 years (2006: 3.9 years). Rolling stock agreements have an average life of 5.1 years (2006: 4.0 years) and other plant and equipment 4.8 years (2006: 5.1 years).

Outside of the UK Trains division the Group has entered into operating leases on certain properties, public service vehicles and various items of plant and equipment. Commitments for future minimum rental payments under cancellable operating leases are shown below:

| | Land and buildings | | Public service vehicles | | Other | |
|---|---|---|---|---|---|---|
| Other divisions' commitments: | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| Within one year | **11.6** | 9.5 | **3.6** | 3.7 | **1.1** | 0.9 |
| After one year but not more than five years | **25.7** | 24.7 | **6.5** | 5.7 | **1.6** | 2.2 |
| More than five years | **13.5** | 15.6 | **0.1** | – | **–** | – |
| | **50.8** | 49.8 | **10.2** | 9.4 | **2.6** | 3.1 |

The average remaining life of operating lease commitments in the "Other Divisions" is 7.6 years (2006: 8.8 years) for land and buildings, 2.8 years (2006: 2.7 years) for public service vehicles and 2.9 years (2006: 2.5 years) for other plant and equipment.

### Operating lease agreements where the Group is the lessor

The Group receives rent on properties as follows:

| | **2007 £m** | 2006 £m |
|---|---|---|
| Future minimum rentals receivable under non-cancellable operating leases: | | |
| Within one year | **2.5** | 4.9 |
| After one year but not more than five years | **9.1** | 9.9 |
| More than five years | **2.8** | – |
| | **14.4** | 14.8 |

The leases have an average unexpired duration of 5.7 years (2006: 3.8 years).

## 36 Commitments and contingencies (continued)

### Finance lease commitments

The Group has finance leases for public service vehicles and various items of plant and equipment. These leases have terms of renewal but no purchase options and escalation clauses. Renewals are at the option of the specific entity that holds the lease.

| | 2007 | | 2006 | |
|---|---|---|---|---|
| | **Minimum payments £m** | **Present value of payments £m** | Minimum payments £m | Present value of payments £m |
| Within one year | **28.0** | **22.6** | 27.3 | 22.7 |
| After one year but not more than five years | **59.5** | **45.4** | 57.0 | 45.6 |
| More than five years | **33.2** | **33.3** | 39.7 | 34.8 |
| Total minimum lease payments | **120.7** | **101.3** | 124.0 | 103.1 |
| Less future financing charges | **(19.4)** | **–** | (20.9) | – |
| Present value of minimum lease payments | **101.3** | **101.3** | 103.1 | 103.1 |

### Capital commitments

| | **2007 £m** | 2006 £m |
|---|---|---|
| Contracted | **34.2** | 25.4 |

The Group is committed to vehicle purchases and various land and buildings improvements.

### Contingent liabilities

#### Bonds and letters of credit

In the ordinary course of business, the Group is required to issue counter-indemnities in support of its operations. As at 31 December 2007, there were UK Train performance bonds of £78.3m (2006: £46.9m) and UK Train season ticket bonds of £79.4m (2006: £85.3m). The Group has other performance bonds which include the £15.5m (2006: £15.0m) performance bond in respect of Inter-Capital and Regional Rail Limited, performance bonds in respect of businesses in the US of £63.4m (2006: £49.2m) and the rest of Europe of £19.7m (2006: £31.8m). Letters of credit have been issued to support insurance retentions of £74.8m (2006: £82.1m).

#### Claims

The Directors' Report discloses that Ray O'Toole is a defendant in proceedings being brought before the Supreme Court of New South Wales. These proceedings relate to a period of time when Ray O'Toole was a director of Bosnjak Holdings Pty Ltd, which was a subsidiary of the Group. The Company is also a defendant to these proceedings. The Directors believe no liabilities will arise from these proceedings and therefore no provision has been made at 31 December 2007.

## 37 Related party transactions

| | Amount of transactions | | Amounts due from related parties | | Amounts due to related parties | |
|---|---|---|---|---|---|---|
| | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m | **2007 £m** | 2006 £m |
| **Associates** | | | | | | |
| ICRRL | **8.4** | 8.4 | **–** | – | **–** | – |
| Alsa associates | **0.8** | 0.3 | **1.8** | 2.4 | **(1.0)** | (0.9) |
| Continental Auto associates | **0.3** | – | **0.2** | – | **(0.2)** | – |
| **Joint ventures** | | | | | | |
| Alsa joint ventures | **0.6** | 0.2 | **1.7** | 0.9 | **(0.2)** | (0.1) |
| **Trade investments** | | | | | | |
| Alsa trade investments | **1.4** | 0.8 | **0.7** | 0.1 | **(0.1)** | (0.9) |
| Continental Auto trade investments | **0.1** | – | **–** | – | **–** | – |
| **Property transactions** | | | | | | |
| Stock | **0.3** | 0.3 | **–** | – | **–** | – |
| Alsa | **3.7** | 3.5 | **0.3** | 0.5 | **(0.5)** | (0.7) |
| Durham | **0.3** | 0.3 | **–** | – | **–** | (0.3) |
| Total associates and joint ventures | **10.1** | 8.9 | **3.7** | 3.3 | **(1.4)** | (1.0) |
| Total other related parties | **5.8** | 4.9 | **1.0** | 0.6 | **(0.6)** | (1.9) |
| Total | **15.9** | 13.8 | **4.7** | 3.9 | **(2.0)** | (2.9) |

Amounts due to ICRRL of £8.4m are included in provisions as disclosed in note 26.

# Notes to the Consolidated Accounts continued

### 37 Related party transactions (continued)

**Property transactions**

Brian Stock was appointed as Chief Executive of the Group's North American operations in October 2004. Stock Transportation Limited, a school bus operator in North America, was acquired in July 2002. As part of the Sale and Purchase Agreement, the Group entered into leases for eight properties at market rents and on standard terms and conditions. The rental payments of £0.3m (2006: £0.3m) are made to Stock Properties Limited and Stock Realty Limited, of which Brian Stock is a related party.

A number of Alsa companies have leased properties from companies related to the Cosmen family. Jorge Cosmen is a Non Executive Director of the Group. These leases were in place before the Group's acquisition of Alsa and are for appropriate market rates.

**Compensation of key management personnel of the Group**

| | **2007 £m** | 2006 £m |
|---|---|---|
| Total compensation paid to key management personnel (as disclosed in note 7) | **3.9** | 4.0 |

Directors' interests in employee share plans are disclosed in the Report on Directors' Remuneration.

### 38 Cash flow statement

The net cash inflows from operating activities include outflows of £11.3m (2006: £2.0m) from continuing operations which are related to exceptional costs.

**(a) Reconciliation of Group profit before tax to cash generated from operations**

| Total Operations | **2007 £m** | 2006 £m |
|---|---|---|
| **Net cash inflow from operating activities** | | |
| Profit before tax | **149.9** | 104.1 |
| Net finance costs | **29.0** | 24.9 |
| Profit on disposal of non-current assets | **(16.2)** | (16.9) |
| Share of post tax results under the equity method | **(0.4)** | 29.5 |
| Depreciation of property, plant and equipment | **79.6** | 81.7 |
| Amortisation of leasehold property prepayment | **0.1** | 0.6 |
| Goodwill impairment | **–** | 20.2 |
| Intangible asset amortisation | **27.5** | 27.8 |
| Amortisation of property, plant and equipment grants | **(1.3)** | (2.0) |
| Profit on disposal of non-current assets (in operating profit) | **(4.3)** | (3.1) |
| Share-based payments | **3.2** | 2.0 |
| (Increase)/decrease in inventories | **(2.1)** | 2.9 |
| Decrease in receivables | **17.7** | 27.3 |
| Increase/(decrease) in payables | **5.9** | (21.1) |
| Decrease in provisions | **(16.5)** | (23.4) |
| Cash generated from operations | **272.1** | 254.5 |

**(b) Analysis of changes in net debt**

Net debt at 31 December 2007 comprises cash and cash equivalents of £157.2m (2006: £143.6m) as disclosed in note 23, current interest bearing loans and borrowings of £426.4m (2006: £43.6m) and non-current interest bearing loans and borrowings of £641.6m (2006: £538.4m) as disclosed in note 28.

| | At 1 January 2007 £m | Cash flow £m | Acquisitions/ disposals £m | Exchange differences £m | Other movements £m | **At 31 December 2007 £m** |
|---|---|---|---|---|---|---|
| Cash | 43.7 | 22.4 | – | 1.9 | – | **68.0** |
| Overnight deposits | 21.6 | (7.0) | – | - | – | **14.6** |
| Other short-term deposits | 78.3 | (4.9) | – | 1.2 | – | **74.6** |
| Cash and cash equivalents | 143.6 | 10.5 | – | 3.1 | – | **157.2** |
| Borrowings: | | | | | | |
| Loan notes | (0.8) | – | – | – | – | **(0.8)** |
| Bank loans | (478.1) | (424.9) | (4.4) | (57.6) | (0.9) | **(965.9)** |
| Finance lease obligations | (103.1) | 26.3 | (23.4) | (0.9) | (0.2) | **(101.3)** |
| | (582.0) | (398.6) | (27.8) | (58.5) | (1.1) | **(1,068.0)** |
| Net debt | (438.4) | (388.1) | (27.8) | (55.4) | (1.1) | **(910.8)** |

Short-term deposits included within liquid resources relate to term deposits repayable within three months. Changes in cash and cash equivalents arising from acquisitions and disposals in the year are disclosed separately on the face of the cash flow statement.

Other non cash movements in net debt represent finance lease additions of £0.2m (2006: £20.7m) and £0.9m (2006: £0.9m) amortisation of loan arrangement fees.

## 38 Cash flow statement (continued)
### (b) Analysis of changes in net debt (continued)

| | At 1 January 2006 £m | Cash flow £m | Acquisitions/ disposals £m | Exchange differences £m | Other movements £m | At 31 December 2006 £m |
|---|---|---|---|---|---|---|
| Cash | 53.2 | (8.1) | – | (1.4) | – | 43.7 |
| Overnight deposits | 24.5 | (2.9) | – | - | – | 21.6 |
| Other short-term deposits | 67.8 | 12.0 | – | (1.5) | – | 78.3 |
| Bank overdrafts | (5.5) | 5.5 | – | - | – | – |
| Cash and cash equivalents | 140.0 | 6.5 | – | (2.9) | – | 143.6 |
| Other debt receivable | 1.0 | (1.0) | – | - | – | – |
| Borrowings: | | | | | | |
| Loan notes | (0.8) | – | – | – | – | (0.8) |
| Bank loans | (594.5) | 89.9 | (2.6) | 30.0 | (0.9) | (478.1) |
| Finance lease obligations | (109.1) | 21.5 | – | 5.2 | (20.7) | (103.1) |
| | (704.4) | 111.4 | (2.6) | 35.2 | (21.6) | (582.0) |
| Net debt | (563.4) | 116.9 | (2.6) | 32.3 | (21.6) | (438.4) |

### (c) Reconciliation of net cash flow to movement in net debt

| | **2007 £m** | 2006 £m |
|---|---|---|
| Increase in cash and cash equivalents in the year | **10.5** | 6.5 |
| Cash (inflow)/outflow from movement in debt and finance leases | **(398.6)** | 110.4 |
| Change in net debt resulting from cash flows | **(388.1)** | 116.9 |
| Change in net debt resulting from acquisitions and disposals | **(27.8)** | (2.6) |
| Change in net debt resulting from non-cash movements | **(56.5)** | 10.7 |
| Movement in net debt in the year | **(472.4)** | 125.0 |
| Opening net debt | **(438.4)** | (563.4) |
| Net debt | **(910.8)** | (438.4) |

# Independent Auditors' Report to the Members of National Express Group PLC

We have audited the parent company financial statements of National Express Group PLC for the year ended 31 December 2007 which comprise the Company Balance Sheet and the related notes 1 to 19. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Group financial statements of National Express Group PLC for the year ended 31 December 2007.

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

**Respective responsibilities of Directors and auditors**

The Directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the parent company financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

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

We report to you our opinion as to whether the parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the parent company Directors' Report is consistent with the financial statements. The information given in the Directors' Report includes that specific information presented in the Operating and Financial Review that is cross referred from the Business Review section of the directors' report.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the Chairman's Statement, the Chief Executive's Statement, the Operating and Financial Review, the Corporate Governance Statement, the Statement of Directors' Responsibilities, the unaudited part of the Directors' Remuneration Report and the Directors' Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

**Basis of audit opinion**

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

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

**Opinion**

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2007;
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the parent company financial statements.

**Ernst & Young LLP**
Registered Auditor
London
28 February 2008

# Company Balance Sheet

## At 31 December 2007

| | Note | 2007 £m | 2006 £m |
|---|---|---|---|
| **Fixed assets** | | | |
| Tangible assets | 4 | **0.9** | 1.0 |
| Financial assets – Investments | 5 | **873.0** | 880.0 |
| | | **873.9** | 881.0 |
| **Current assets** | | | |
| Debtors | 7 | **1,385.0** | 903.1 |
| Financial assets – Derivative financial instruments | 6 | **3.2** | 8.4 |
| Cash at bank and in hand | 8 | **11.1** | 20.7 |
| | | **1,399.3** | 932.2 |
| Creditors: amounts falling due within one year | 9 | **(1,245.0)** | (799.7) |
| Financial liabilities – Derivative financial instruments | 6 | **(17.7)** | (2.1) |
| **Net current assets** | | **136.6** | 130.4 |
| **Total assets less current liabilities** | | **1,010.5** | 1,011.4 |
| Creditors: amounts falling due after more than one year | 10 | **(548.6)** | (458.0) |
| Financial liabilities – Derivative financial instruments | 6 | **(5.4)** | (5.7) |
| Provisions for liabilities and charges | 11 | **(31.1)** | (31.5) |
| **Net assets** | | **425.4** | 516.2 |
| **Shareholders' equity** | | | |
| Called-up share capital | 14 | **7.7** | 7.7 |
| Share premium account | 15 | **195.3** | 189.8 |
| Capital redemption reserve | 15 | **0.2** | 0.2 |
| Own shares | 15 | **(16.3)** | (16.7) |
| Hedging reserve | 15 | **(3.0)** | (4.1) |
| Profit and loss account | 15 | **241.5** | 339.3 |
| **Shareholders' funds** | | **425.4** | 516.2 |

**S R Bowker CBE** Chief Executive
**A C Walker** Finance Director
28 February 2008

# Notes to the Company Accounts

## For the year ended 31 December 2007

### 1 Accounting policies

**Basis of preparation**

The separate accounts of the parent Company are presented as required by the Companies Act 1985. The accounts have been prepared under the historic cost convention, except for the recognition of derivative financial instruments and available for sale investments detailed below, and in accordance with applicable accounting standards in the United Kingdom.

In applying these policies management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the accounts and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

No profit and loss account is presented by the Company as permitted by Section 230 of the Companies Act 1985.

**Leases**

Leases of tangible fixed assets where substantially all the risks and rewards of ownership of the asset have passed to the Company, are classified as finance leases and are capitalised in the balance sheet as plant and equipment. Finance leases are capitalised at the fair value of the present value of the minimum lease payments. The capital element of future obligations under hire purchase contracts and finance leases is included as a liability in the balance sheet. The interest element of rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding. Assets acquired under finance leases are depreciated over the shorter of the useful life of the asset and the lease term.

Leases of assets where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Rentals paid under operating leases are charged to the profit and loss account on a straight-line basis over the term of the lease. Incentives received under operating leases and initial direct costs in negotiating the lease are amortised to the profit and loss account on a straight-line basis over the term of the lease, or to the first review if shorter.

**Tangible fixed assets**

Tangible fixed assets are stated at historic cost less accumulated depreciation and any impairment. Tangible fixed assets are depreciated on a straight-line basis over their estimated useful lives as follows:

Plant and equipment – 3 to 5 years

The carrying value of fixed assets are reviewed for impairment if events or changes in circumstances indicate that the current carrying value may not be recoverable, and are written down immediately to their recoverable amount. Repairs and maintenance are charged to the profit and loss account during the financial period in which they are incurred.

**Investments in subsidiaries**

Investments are held at historic cost less any provision for impairment.

**Available for sale investments**

Available for sale financial assets are non-derivative financial assets that are designated as such, or that are not classified as a loan or receivable, held to maturity or at fair value through profit or loss. After initial recognition these assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or the investment is determined to be impaired, at which time the previously reported cumulative gain or loss is included in the income statement.

**Interest bearing loans and borrowings**

Loans and borrowings are initially recognised at the fair value of the consideration received, net of issue costs. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Hedge accounting is adopted where derivatives such as fixed to floating interest rate swaps are held as fair value hedges against fixed interest rate borrowings. Under fair value hedge accounting, fixed interest rate borrowings are revalued at each balance sheet date by the change in fair value attributable to the interest rate being hedged.

**Provisions**

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Company expects a provision to be reimbursed the reimbursement is recognised as a separate asset but only when reimbursement is virtually certain.

**Pensions**

The Company participates in both the National Express Group multi-employer funded defined benefit scheme and a defined contribution scheme. The Company is unable to identify its share of the underlying assets and liabilities of the multi-employer scheme on a consistent and reasonable basis, and therefore has accounted for the scheme as if it were a defined contribution scheme under the requirements of FRS 17, “Retirement Benefits”.

## 1 Accounting policies (continued)

### Share-based payment

In accordance with the transition provisions, FRS 20 has been applied to all grants after 7 November 2002 that were unvested as of 1 January 2005.

The Company awards equity-settled share-based payment to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant by an external valuer using a stochastic model. Non-market-based performance-related vesting conditions are not taken into account when estimating the fair value; instead those non-market conditions are taken into account in calculating the current best estimate of the number of shares that will eventually vest and at each balance sheet date before vesting. The cumulative expense is calculated based on that estimate. Market-based performance conditions are taken into account when determining the fair value and at each balance sheet date before vesting, the cumulative expense is calculated irrespective of whether or not the market conditions are satisfied, provided that all other performance conditions are met.

### Deferred tax

Deferred tax is recognised in respect of all material timing differences that have originated, but not reversed, by the balance sheet date. Deferred tax is measured on a non-discounted basis at tax rates that are expected to apply in the periods in which the timing differences reverse based on tax rates and laws enacted or substantively enacted at the balance sheet date. Deferred tax assets are recognised where their recovery is considered more likely than not in that there will be suitable taxable profits from which the future reversal of underlying timing differences can be deducted.

### Foreign currencies

Foreign currency assets and liabilities are translated into sterling at the rates of exchange ruling at the year end. Foreign currency transactions arising during the year are translated into sterling at the rate of exchange ruling on the date of the transaction. Any exchange differences so arising are dealt with through the profit and loss account.

### Derivative financial instruments

The Company uses derivative financial instruments such as foreign currency contracts and interest rate swaps to hedge its risks associated with foreign currency and interest rate fluctuations. Such derivative financial instruments are initially recognised at fair value and subsequently remeasured to fair value for the reported balance sheet. The fair value of forward exchange contracts and interest rate swaps is calculated by reference to market exchange rates and interest rates at the period end.

In relation to cash flow hedges which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity, and the ineffective portion in the profit and loss account. The gains or losses deferred in equity in this way are recycled through the profit and loss account in the same period in which the hedged underlying transaction or firm commitment is recognised in the profit and loss account.

For derivatives that do not qualify for hedge accounting, including the foreign currency contracts, gains or losses are taken directly to the profit and loss account in the period.

Hedge accounting is discontinued when the hedging instrument expires, is sold, terminated or exercised, or no longer qualifies for hedge accounting.

## 2 Exchange rates

The most significant exchange rates to the pound for the Company are as follows:

| | **2007 Closing rate** | **2007 Average rate** | 2006 Closing rate | 2006 Average rate |
|---|---|---|---|---|
| US dollar | **1.98** | **2.00** | 1.96 | 1.85 |
| Canadian dollar | **1.98** | **2.15** | 2.28 | 2.09 |
| Euro | **1.36** | **1.46** | 1.48 | 1.47 |
| Australian dollar | **2.27** | **2.39** | 2.48 | 2.44 |

## 3 Directors' emoluments

Detailed information concerning Directors' emoluments, shareholdings and options is shown in the Directors' Remuneration Report.

# Notes to the Company Accounts continued

### 4 Tangible fixed assets

| | Plant and equipment £m |
|---|---|
| Cost: | |
| At 1 January 2007 | 3.4 |
| Additions | 0.9 |
| Disposals | (1.2) |
| **At 31 December 2007** | **3.1** |
| Depreciation: | |
| At 1 January 2007 | 2.4 |
| Charge for the year | 0.5 |
| Disposals | (0.7) |
| **At 31 December 2007** | **2.2** |
| Net book value: | |
| **At 31 December 2007** | **0.9** |
| At 31 December 2006 | 1.0 |

Tangible fixed assets held under finance lease agreements are analysed as follows:

| | **2007 £m** | 2006 £m |
|---|---|---|
| Plant and equipment | | |
| – cost | **0.2** | 0.2 |
| – depreciation | **(0.2)** | (0.1) |
| | **–** | 0.1 |

Leased assets and assets under hire purchase contracts are pledged as security for the related finance lease and hire purchase liabilities.

### 5 Financial assets: Investments

| | Investments in subsidiaries £m | Available for sale investments £m | Total £m |
|---|---|---|---|
| Cost or valuation: | | | |
| At 1 January 2007 | 1,271.9 | 12.8 | 1,284.7 |
| Disposals | – | (12.0) | (12.0) |
| **At 31 December 2007** | **1,271.9** | **0.8** | **1,272.7** |
| Provisions: | | | |
| At 1 January 2007 | (398.9) | (5.8) | (404.7) |
| Disposals | – | 5.0 | 5.0 |
| **At 31 December 2007** | **(398.9)** | **(0.8)** | **(399.7)** |
| Net carrying amount: | | | |
| **At 31 December 2007** | **873.0** | **–** | **873.0** |
| At 31 December 2006 | 873.0 | 7.0 | 880.0 |

Disposals during the year reflect the receipt of the final preference share dividend from Union Railways (South) Limited, and the subsequent redemption of these preference shares.

The information provided below is given for the Company's principal subsidiaries. A full list of subsidiaries and investments will be annexed to the next Annual Return to Companies House. The principal country of operation in respect of the companies below is the country in which they are incorporated.

National Express Group PLC is the beneficial owner of all the equity share capital, either itself or through subsidiary undertakings, of the companies, unless indicated otherwise. The Group's train passenger services in the UK are operated through franchises awarded by DfT Rail, as delegated by the UK Government.

**5 Financial assets: Investments (continued)**
The following holdings are 100% held directly by the Company:

| Incorporated in England and Wales | |
|---|---|
| National Express Holdings Limited | Holding company for UK Coach operating companies |
| National Express Group Holdings Limited | Holding company for US operating companies |
| National Express Overseas Limited | Holding company for discontinued Australian business |
| National Express Trains Limited | Holding company for UK Train operating companies |
| National Express Transport Holdings Limited | Holding company for UK Bus and Canadian operating companies |
| National Express European Holdings Limited | Holding company for Spanish operating companies |
| **Incorporated in Guernsey** | |
| National Express Guernsey Limited | Insurance captive |

Other investments include:

| Name | Country of registration | Class of share | Proportion held % |
|---|---|---|---|
| Inter-Capital and Regional Rail Limited (ICRRL) | England and Wales | Ordinary shares | 40 |
| London & Continental Railways Limited | England and Wales | Ordinary shares | 21 |
| Prepayment Cards Limited | England and Wales | Ordinary shares | 23.5 |

**6 Derivatives**

| | **2007 £m** | 2006 £m |
|---|---|---|
| Interest rate swaps | **1.7** | 0.3 |
| **Financial assets due over one year** | **1.7** | 0.3 |
| Interest rate swaps | **1.5** | 1.5 |
| Foreign exchange forward contracts | **–** | 6.6 |
| **Financial assets due under one year** | **1.5** | 8.1 |
| Interest rate swaps | **(5.4)** | (5.7) |
| **Financial liabilities due over one year** | **(5.4)** | (5.7) |
| Interest rate swaps | **(3.2)** | (2.1) |
| Foreign exchange forward contracts | **(14.5)** | – |
| **Financial liabilities due under one year** | **(17.7)** | (2.1) |

Full details of the Group's financial risk management objectives and policies can be found in note 30 of the Group accounts. As the holding company for the Group, the Company faces similar risks over foreign currency and interest rate movements.

**7 Debtors**

| | **2007 £m** | 2006 £m |
|---|---|---|
| Trade debtors | **0.9** | 0.3 |
| Amounts owed by subsidiary undertakings | **1,368.4** | 874.9 |
| Corporation tax recoverable | **11.8** | 18.6 |
| Deferred tax asset (see note 12) | **0.9** | 3.0 |
| Other debtors | **1.7** | 5.5 |
| Prepayments and accrued income | **1.3** | 0.8 |
| | **1,385.0** | 903.1 |

Included within prepayments is £0.5m (2006: £0.6m) which is recoverable after more than one year.

**8 Cash at bank and in hand**

| | **2007 £m** | 2006 £m |
|---|---|---|
| Other short-term deposits | **8.1** | 19.0 |
| Cash at bank | **3.0** | 1.7 |
| | **11.1** | 20.7 |

Cash at bank and in hand earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Company, and earn interest at the respective short-term deposit rates. The fair value of cash equals the carrying value.

# Notes to the Company Accounts continued

## 9 Creditors: amounts falling due within one year

| | 2007 £m | 2006 £m |
|---|---|---|
| Bank overdraft | **37.7** | 9.2 |
| Bank loans | **367.5** | – |
| Trade creditors | **1.9** | 2.3 |
| Amounts owed to subsidiary undertakings | **819.6** | 777.5 |
| Accruals and deferred income | **9.0** | 4.7 |
| Other creditors | **9.3** | 6.0 |
| | **1,245.0** | 799.7 |

Trade creditors are non-interest bearing and are normally settled on 30 day terms and other creditors are non-interest bearing and have an average term of six months.

## 10 Creditors: amounts falling due after more than one year

| | 2007 £m | 2006 £m |
|---|---|---|
| Bank loans | **548.6** | 458.0 |

## 11 Provisions for liabilities and charges

| | Insurance claims[a] £m | Eurostar onerous contract[b] £m | Exceptional redundancy provision[c] £m | Total £m |
|---|---|---|---|---|
| At 1 January 2007 | 0.9 | 30.6 | – | 31.5 |
| Provided in the year | 1.2 | – | 1.5 | 2.7 |
| Released in the year | (0.3) | – | – | (0.3) |
| Amortisation of discount | – | 2.0 | – | 2.0 |
| Utilised in the year | (0.1) | (4.7) | – | (4.8) |
| **At 31 December 2007** | **1.7** | **27.9** | **1.5** | **31.1** |

(a) The insurance claims provision arises from estimated exposures at the year end, the majority of which will be utilised in the next six years and comprise provisions for existing claims arising in the UK and North America.

(b) A provision was recognised in 2006 for the Company's onerous contract for Eurostar with ICRRL. £8.4m was paid to ICRRL during the year, which is offset by a receipt in relation to preference share dividends. The provision will be utilised during the period up to the end of our contract in 2010, with the final payment being made in February 2011.

(c) This provision stems from the reorganisation of the Group's operations in the UK, which is expected to be settled during 2008.

## 12 Deferred tax

The major components of the provision for deferred taxation are as follows:

| | 2007 £m | 2006 £m |
|---|---|---|
| Accelerated capital allowances | **–** | 0.1 |
| Other timing differences | **0.9** | 2.9 |
| **Net deferred tax asset at 31 December** | **0.9** | 3.0 |

The reconciliation of deferred tax balances is as follows:

| | £m |
|---|---|
| Deferred tax asset at 1 January 2007 | 3.0 |
| Charged to profit and loss | (1.5) |
| Credited to equity in relation to cash flow hedges | (0.6) |
| **Deferred tax asset at 31 December 2007** | **0.9** |

### Timing differences associated with Group investments

No deferred tax (2006: £nil) is recognised on the unremitted earnings of subsidiaries and associates, as no dividends have been accrued as receivable, and no binding agreement to distribute the past earnings in future has been entered into by the subsidiaries.

### 13 Interest-bearing loans and borrowings

The effective interest rates at the balance sheet date were as follows:

| | Maturity | **2007 £m** | Effective interest rate | 2006 £m | Effective interest rate |
|---|---|---|---|---|---|
| **Current** | | | | | |
| Bank overdraft | On demand | **37.7** | BASE + 1.0% | 9.2 | BASE + 1.0% |
| Euro bank loans unhedged | April 2008 | **216.8** | EURIBOR + 0.5% | – | – |
| Euro bank loans subject to interest hedge | April 2008 | **150.7** | 4.17% | – | – |
| **Bank loans** | | **367.5** | | – | |
| **Total current** | | **405.2** | | 9.2 | |
| **Non-current** | | | | | |
| US dollar bank loans subject to interest rate hedge | June 2011 | **50.0** | 9.5% | 51.0 | 7.3% |
| US dollar bank loans unhedged | June 2011 | **25.0** | LIBOR + 0.4% | 45.9 | LIBOR + 0.4% |
| Euro bank loans subject to interest rate hedge | June 2011 | **473.6** | 4.17% | 235.8 | 3.6% |
| Euro bank loans unhedged | June 2011 | – | – | 84.2 | EURIBOR + 0.4% |
| Canadian dollar bank loans | June 2011 | – | – | 41.1 | LIBOR + 0.4% |
| **Bank loans** | | **548.6** | | 458.0 | |
| **Total non-current** | | **548.6** | | 458.0 | |

The facility expiring on April 2008 was refinanced on 14 February 2008 with a new facility expiring in February 2009, with a one year extension to February 2010 at the Group's option.

Details of the Company's interest rate management strategy and interest rate swaps are included in note 30 and note 31 of the Group accounts.

### 14 Called-up share capital

| | **2007 £m** | 2006 £m |
|---|---|---|
| At 31 December : | | |
| Authorised: | | |
| 200,000,000 (2006: 200,000,000) ordinary shares of 5p each | **10.0** | 10.0 |
| Issued called-up and fully paid: | | |
| 154,627,671 (2006: 153,835,012) ordinary shares of 5p each | **7.7** | 7.7 |

| Movement in ordinary shares during the year | £m | Number of shares |
|---|---|---|
| At 1 January 2006 | 7.5 | 150,920,310 |
| Exercise of share options | 0.2 | 2,914,702 |
| At 1 January 2007 | 7.7 | 153,835,012 |
| Exercise of share options | – | 792,659 |
| **At 31 December 2007** | **7.7** | **154,627,671** |

The total number of share options exercised in the year by employees of the Group was 1,008,457 (2006: 3,100,807) of which 792,659 (2006: 2,914,702) exercises were satisfied by newly issued shares and 215,798 (2006: 186,105) exercises were satisfied by transferring shares from the National Express Employee Benefit Trust.

# Notes to the Company Accounts continued

### 15 Shareholders' funds and statement of changes in shareholders' equity

| | Share capital £m | Share premium £m | Capital redemption reserve £m | Own shares £m | Hedging reserve £m | Profit and loss account £m | Total £m |
|---|---|---|---|---|---|---|---|
| At 1 January 2007 | 7.7 | 189.8 | 0.2 | (16.7) | (4.1) | 339.3 | 516.2 |
| Shares issued | – | 5.5 | – | – | – | – | 5.5 |
| Shares utilised | – | – | – | 0.4 | – | (0.4) | – |
| Share-based payments | – | – | – | – | – | 1.5 | 1.5 |
| Tax on share-based payments credited to reserves | – | – | – | – | – | 0.9 | 0.9 |
| Hedge movements | – | – | – | – | 1.1 | – | 1.1 |
| Dividends | – | – | – | – | – | (54.0) | (54.0) |
| Loss for the year | – | – | – | – | – | (45.8) | (45.8) |
| **At 31 December 2007** | **7.7** | **195.3** | **0.2** | **(16.3)** | **(3.0)** | **241.5** | **425.4** |

Own shares comprise treasury shares and shares held in the Employee Benefit Trust.

Treasury shares include 1,825,000 (2006: 1,825,000) ordinary shares in the Company. During the year, the Group repurchased no (2006: 1,425,000) shares for nil consideration (2006: £11.6m). No additional (2006: 1,425,000) shares have been retained as treasury shares within equity for future issue under the Group's share schemes or cancellation. No shares were cancelled during the year (2006: nil). The market value of these shares at 31 December 2007 was £22.7m (2006: £20.6m).

Own shares include 447,554 (2006: 663,352) ordinary shares in the Company that have been purchased by the Trustees of the National Express Employee Benefit Trust (the "Trust"). During the year, the Trust purchased no (2006: nil) shares and 215,798 (2006: 186,105) shares were used to satisfy options granted under a number of the Company's share schemes. The market value of these shares at 31 December 2007 was £5.6m (2006: £7.5m). The dividends payable on these shares have been waived.

### 16 Retirement benefits

The Company participates in both the National Express Group Staff Pension Fund (a multi-employer funded defined benefit scheme) and the WM Pension Scheme (a defined contribution scheme). The Company is unable to identify its share of the underlying assets and liabilities of the multi-employer scheme on a consistent and reasonable basis, and therefore has accounted for the scheme as if it were a defined contribution scheme under the requirements of FRS 17, "Retirement Benefits". Contributions to this scheme are determined by independent professionally qualified actuaries. The details of the latest actuarial valuation are detailed in note 35 to the Group accounts.

The pension charge for the year amounted to £0.8m (2006: £1.1m).

### 17 Share-based payment

During the year ended 31 December 2007, the Company had the following share-based payment arrangements, which are described in note 7(b) to the Group accounts.

For the following disclosure, share options with a nil exercise price have been disclosed separately to avoid distorting the weighted average exercise prices. The number of share options in existence during the year was as follows:

| | **2007** | | 2006 | |
|---|---|---|---|---|
| | **Number of share options** | **Weighted average exercise price (p)** | Number of share options | Weighted average exercise price (p) |
| Options without a nil exercise price: | | | | |
| At 1 January | **493,123** | **689** | 1,759,870 | 574 |
| Granted during the year | **–** | **–** | – | – |
| Lapsed during the year | **(4,867)** | **630** | (24,304) | 985 |
| Group transfers during the year | **15,715** | **710** | – | – |
| Exercised during the year | **(451,840)** | **682** | (1,242,443) | 511 |
| Outstanding at 31 December[1] | **52,131** | **759** | 493,123 | 689 |
| Exercisable at 31 December | **52,131** | **759** | 38,679 | 782 |
| Options with a nil exercise price: | | | | |
| At 1 January | **930,791** | **nil** | 462,337 | nil |
| Granted during the year | **247,102** | **nil** | 472,790 | nil |
| Lapsed during the year | **(242,411)** | **nil** | (2,243) | nil |
| Group transfers during the year | **(82,016)** | **nil** | – | nil |
| Exercised during the year | **(37,626)** | **nil** | (2,093) | nil |
| Outstanding at 31 December | **815,840** | **nil** | 930,791 | nil |
| Exercisable at 31 December | **–** | | – | |
| Total outstanding at 31 December | **867,971** | | 1,423,914 | |
| Total exercisable at 31 December | **52,131** | | 38,679 | |

1 Included within this balance are options over nil (2006: 35,487) shares for which no expense has been recognised in accordance with the transitional provisions of FRS 20, as the options were granted before 7 November 2002 and have not been subsequently modified.

### 17 Share-based payment continued

The options outstanding at 31 December 2007 had exercise prices that were between 398p and 862.5p (2006: between 398p and 862.5p) excluding options with a nil exercise price. The range of exercise prices for options was as follows:

| Exercise price (p) | 2007 | 2006 |
|---|---|---|
| 350–650 | **3,191** | 8,679 |
| 650–950 | **48,940** | 484,444 |
| 950–1250 | **–** | – |
| | **52,131** | 493,123 |

The options have a weighted average contractual life of two years (2006: four years). Options were exercised throughout the year and the weighted average share price at exercise was 1144p (2006: 919p).

The weighted average fair value of the remaining share options granted during the year was calculated using a stochastic model, with the following assumptions and inputs:

| | Share options with nil exercise price | |
|---|---|---|
| | 2007 | 2006 |
| Risk free interest rate | **–** | – |
| Expected volatility | **19.0%** | 19.0% |
| Peer group volatility | **25.7%–25.9%** | 29.7%–31.2% |
| Expected option life in years | **3 years** | 3 years |
| Expected dividend yield | **2.7%–2.8%** | 3.4%-3.5% |
| Weighted average share price | **1236p–1295p** | 931p–1033p |
| Weighted average exercise price | **0p** | 0p |
| Weighted average fair value of options granted | **684p–1194p** | 369p–934p |

Experience to date has shown that approximately 15% (2006: 15%) of options are exercised early, principally due to redundancies. This has been incorporated into the calculation of the expected option life for the share options without nil exercise price.

Expected volatility in the table above was determined from historic volatility over the last eight years, adjusted for one-off events that were not considered to be reflective of the volatility of the share price going forward. The expected dividend yield represents the dividends declared in the 12 months preceding the date of the grant divided by the average share price in the month preceding the date of the grant.

For share options granted during the year under the LTIP, the TSR targets have been reflected in the calculation of the fair value of the options above.

### 18 Commitments and contingencies

#### Operating lease commitments

The Company has entered into operating leases on certain properties. Annual commitments under non-cancellable operating leases are as follows:

| | Land and buildings | |
|---|---|---|
| | 2007 £m | 2006 £m |
| Operating leases which expire: | | |
| Within two to five years | **0.6** | 0.6 |
| Over five years | **0.5** | – |

#### Contingent liabilities

(a) Guarantees

The Company has guaranteed credit facilities totalling £76.4m (2006: £101.6m) of certain subsidiaries.

(b) Bonds and letters of credit

In the ordinary course of business, the Company is required to issue counter-indemnities in support of its subsidiaries' operations. As at 31 December 2007, there were UK Train performance bonds of £78.3m (2006: £46.9m) and UK Train season ticket bonds of £79.4m (2006: £85.3m). The Company has other performance bonds which include the £15.5m (2006: £15.0m) performance bond in respect of Inter-Capital and Regional Rail Limited and performance bonds in respect of businesses in the United States of America of £63.4m (2006: £49.2m). Letters of credit have been issued to support insurance retentions of £74.8m (2006: £82.1m).

(c) Claims

The Directors' Report discloses that Ray O'Toole is a defendant in proceedings being brought before the Supreme Court of New South Wales. These proceedings relate to a period of time when Ray O'Toole was director of Bosnjak Holdings Pty Ltd, which was a subsidiary of the Group. The Company is also a defendant to these proceedings. The Directors believe no liabilities will arise from these proceedings and therefore no provision has been made at 31 December 2007.

### 19 Related party transactions

The Company has taken advantage of the exemption in paragraph 3c of FRS 8, 'Related party disclosures' from disclosing transactions with related parties that are part of the National Express Group or investees of the Group.

# Five year summary

| Year ended 31 December | IFRS<br>2007<br>£m | IFRS<br>2006<br>£m | IFRS<br>2005<br>£m | IFRS<br>2004<br>£m | UK GAAP<br>2003<br>£m |
|---|---|---|---|---|---|
| Revenue | **2,615.4** | 2,525.5 | 2,216.0 | 2,354.5 | 2,565.7 |
| Normalised * operating profit | **205.6** | 184.8 | 155.5 | 143.3 | 128.9 |
| Group operating profit | **162.3** | 141.6 | 109.5 | 99.9 | 83.2 |
| Profit before tax | **149.9** | 104.1 | 89.3 | 77.9 | 54.1 |
| **Statistics** | | | | | |
| Basic earnings/(loss) per share | **71.7p** | 50.7p | (2.0p) | 45.7p | 31.9p |
| Normalised* diluted earnings per share | **83.9p** | 76.5p | 76.3p | 69.3p | 50.1p |
| Dividends per share | **37.96p** | 34.75p | 32.25p | 30.0p | 26.0p |
| Net assets | **441.1** | 345.5 | 312.3 | 266.8 | 264.2 |
| **Net (debt)/funds** | | | | | |
| Cash at bank and in hand | **157.2** | 143.6 | 145.5 | 147.2 | 97.0 |
| Other debt receivable | **–** | – | 1.0 | 1.0 | – |
| Loan notes | **(0.8)** | (0.8) | (0.8) | (7.5) | (8.4) |
| Bank and other loans | **(965.9)** | (478.1) | (594.5) | (215.5) | (324.4) |
| Bank overdrafts | **–** | – | (5.5) | – | (0.2) |
| Finance lease obligations | **(101.3)** | (103.1) | (109.1) | (61.8) | (53.1) |
| | **(910.8)** | (438.4) | (563.4) | (136.6) | (289.1) |

*Normalised results are defined as the statutory results before the following as appropriate: profit or loss on sale of businesses, exceptional profit or loss on sale of non-current assets and charges for goodwill impairment, intangible amortisation, property, plant and equipment impairments, exceptional items and tax relief on qualifying exceptional items.

# Shareholder information

**Shareholder electronic communications**
By registering for electronic communications you can help us to conserve environmental resources by reducing print, paper and postage costs. Log on to www.shareview.co.uk if you would like to:

- register your e-mail so that future shareholder information, including the annual report and accounts, are sent to you electronically;
- check the balance of your shareholding;
- set up a dividend mandate online;
- change your registered postal address or your dividend mandate details; or
- submit your vote online prior to a general meeting.

To sign up for the first time you should click on "Register" and follow the simple instructions – you will need your shareholder reference number from your share certificate or dividend voucher or any other correspondence sent to you by Equiniti Limited (formerly Lloyds TSB Registrars).

**Dividends paid direct to your bank account**
Having dividends paid direct to your bank account has the following advantages:

- avoids the risk of cheques being lost and incurring a replacement fee;
- saves you time in presenting the cheque for payment; and
- the dividend is credited to your account on the payment date.

The tax voucher is sent to your registered address at the same time as the dividend is credited to your account. To set up a new dividend mandate please log on to www.shareview.co.uk or contact the Registrar, Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA. Shareholder helpline number: 0871 384 2152*.

**Share dealing service**
A telephone and internet share dealing service, which provides a simple way to buy and sell shares, is available through our Registrars, Equiniti. For further information log on to www.shareview.co.uk/dealing or telephone 0871 384 2020*.

*Calls to these numbers are charged at 8p per minute from a BT landline. Other telephony providers' costs may vary.

**Company website**
The company website at www.nationalexpressgroup.com has information about the Group, press releases, share price data and copies of the half year and annual report and accounts.

**Sharegift**
ShareGift is an independent charity share donation scheme administered by the Orr Mackintosh Foundation (registered charity number 1052686). Those shareholders who hold only a small number of shares, the value of which make it uneconomic to sell them, can donate the shares to ShareGift who will sell them and donate the proceeds to a wide range of charities. Further information about ShareGift can be obtained from its website at www.sharegift.org and a ShareGift transfer form can be downloaded from www.nationalexpressgroup.com.

**Unclaimed assets register**
The Company participates in the Unclaimed Assets Register ("UAR") which provides a search facility for shareholdings and other financial assets that may have been forgotten. For further information contact UAR, 6th Floor, Cardinal Place, 80 Victoria Street, London SW1E 5JL Tel: 0870 241 1713 or visit www.uar.co.uk.

**Analysis of ordinary shareholdings at 2 March 2008**

| | Number of accounts | Per cent of total number of accounts | Number of shares '000 | Per cent of ordinary capital |
|---|---|---|---|---|
| **By size of holding** | | | | |
| 1 – 500 | 7,556 | 56 | 1,305 | 1 |
| 501 – 1,000 | 1,872 | 14 | 1,420 | 1 |
| 1,001 – 5,000 | 2,730 | 21 | 6,187 | 4 |
| 5,001 – 50,000 | 1,065 | 8 | 11,722 | 8 |
| 50,001 – 1,000,000 | 190 | 1 | 46,866 | 30 |
| Over 1,000,000 | 29 | – | 87,132 | 56 |
| | 13,442 | 100 | 154,632 | 100 |
| **By investor type** | | | | |
| Individuals | 12,124 | 90 | 15,214 | 10 |
| Institutional Investors | 1,204 | 9 | 122,517 | 79 |
| Other Corporate Investors | 114 | 1 | 16,901 | 11 |
| | 13,442 | 100 | 154,632 | 100 |

# Dividends and Financial Calendar

| | |
|---|---|
| Final dividend ex dividend date | 23 April 2008 |
| Final dividend record date | 25 April 2008 |
| Annual General Meeting | 1 May 2008 |
| Final dividend payment date | 9 May 2008 |
| Half year results announced | July 2008 |
| Interim dividend ex dividend date | September 2008 |
| Interim dividend record date | September 2008 |
| Interim dividend payment date | September 2008 |

# Corporate Information

**Secretary and registered office**
**A J McDonald**
National Express Group PLC
7 Triton Square
London NW1 3HG
Tel: +44 (0) 8450 130130
Fax: +44 (0)20 7506 4320
e-mail: info@natex.co.uk.com
www.nationalexpressgroup.com

**Registered number**
2590560

**Auditors**
**Ernst & Young LLP**
1 More London Place
London
SE1 2AF

**Registrar**
**Equiniti Limited**
Aspect House
Spencer Road
Lancing
West Sussex
BN99 6DA
Shareholder helpline: 0871 384 2152*

* Calls to this number are charged at 8p per minute from a BT landline. Other telephone providers' costs may vary.

**Principal bankers**
**HSBC Bank plc**
8 Canada Square
London
E14 5HQ

**Royal Bank of Scotland**
135 Bishopsgate
London
EC2M 3UR

**Corporate solicitors**
**Ashurst**
Broadwalk House
5 Appold Street
London
EC2A 2HA

**Financial advisors**
**Merrill Lynch International Limited**
Merrill Lynch Financial Centre
2 King Edward Street
London
EC1A 1HQ

**Stockbrokers**
**Merrill Lynch International Limited**
Merrill Lynch Financial Centre
2 King Edward Street
London
EC1A 1HQ

**Morgan Stanley**
20 and 25 Cabot Square
Canary Wharf
London
E14 4QW

# Glossary

| Term | Definition |
|---|---|
| **AGM** | Annual General Meeting |
| **Combined Code** | The Combined Code on Corporate Governance published by the Financial Reporting Council |
| **CPI** | Consumer Price Index |
| **CR** | Corporate Responsibility |
| **The Company** | National Express Group PLC |
| **DfT** | Department for Transport |
| **DNA** | The name for our leadership development strategy |
| **EBT** | Employee Benefit Trust |
| **EBITDA** | Normalised operating profit before depreciation and other non-cash items excluding discontinued operations |
| **EPS** | Earnings Per Share – The profit for the year attributable to shareholders, divided by the weighted average number of shares in issue, excluding those held by the Employee Benefit Trust and shares held in treasury which are treated as cancelled. |
| **EU** | European Union |
| **The Group** | The Company and its subsidiaries |
| **IFRIC** | International Financial Reporting Interpretations Committee |
| **IFRS** | International Financial Reporting Standards |
| **KPI** | Key Performance Indicator |
| **LTIP** | Long Term Incentive Plan |
| **NXEA** | National Express East Anglia |
| **NXEC** | National Express East Coast |
| **Normalised diluted earnings** | Earnings per share and excluding the profit or loss on sale of businesses, exceptional profit or loss on the disposal of non current assets and charges for goodwill impairment, intangible asset amortization, exceptional items and tax relief on qualifying exceptional terms |
| **Normalised profit** (For the purposes of Directors' Remuneration) | Profit before tax, goodwill impairment, intangible amortization and exceptional items |
| **OFR** | Operating and Financial Review |
| **RPS** | Railway Pension Scheme |
| **SPAD** | Signal Passed at Danger |
| **TfL** | Transport for London |
| **TOC** | Train Operating Company |
| **TSR** | Total Shareholder Return – the growth in value of a shareholding over a specified period assuming that dividends are reinvested to purchase additional shares |
| **UK GAAP** | UK Generally Accepted Accounting Principles |

This Annual Report and Accounts is printed on Revive 50:50 silk and Revive 50:50 uncoated, both papers are produced from 50% recovered waste and 50% virgin fibre. Both the paper mill and printer involved in the production support the growth of responsible forest management and are both accredited to ISO14001 which specifies a process for continuous environmental improvement and both are FSC certified. If you have finished reading this report and no longer wish to retain it, please pass it on to other interested readers or dispose of it in your recycled paper waste.

Thank you.

This annual report is available at www.nationalexpressgroup.com

Designed and produced by Radley Yeldar (London)

Printed by Cousins

National Express Group PLC
7 Triton Square
London NW1 3HG
Tel: +44 (0) 8450 130130
Fax: +44 (0) 20 7506 4320
e-mail: info@nationalexpress.com
www.nationalexpressgroup.com