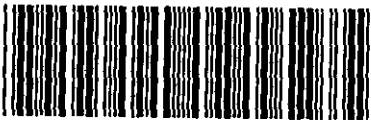


SC157176

FIRST GROUP PLC

WEDNESDAY THURSDAY			
	SC9W2RKM		
	SCT	26/07/2007	803
	COMPANIES HOUSE		
	SCT	04/07/2007	521
	COMPANIES HOUSE		
	SCT	15/06/2007	1600
	COMPANIES HOUSE		

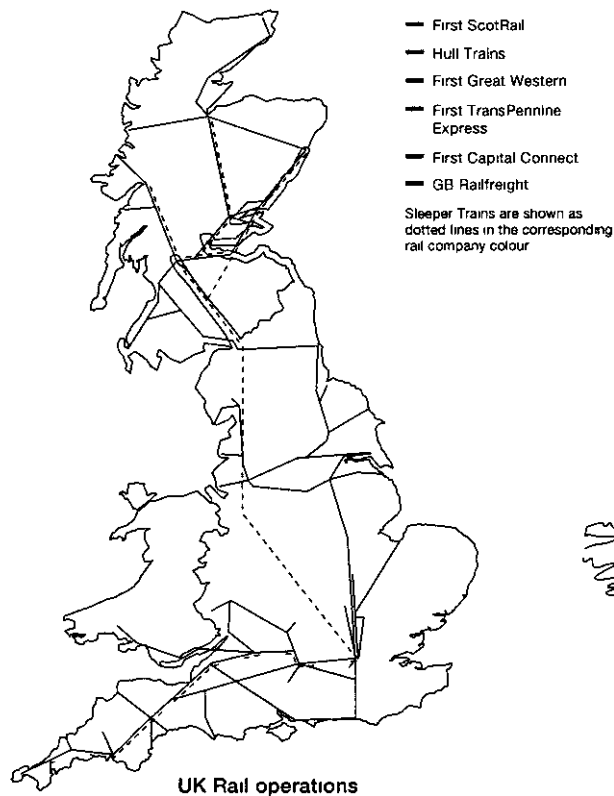
This has been a year of excellent progress across the Group, building on our position as the leading transport provider.

Our focus is on delivering safe, high quality and reliable services throughout our business. The safety of our passengers and employees is our highest priority and we strive to lead the industry in this area and achieve the highest possible standards across the Group.

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Group overview

We are the leader in safe, innovative, reliable, sustainable transport services – global in scale and local in approach.

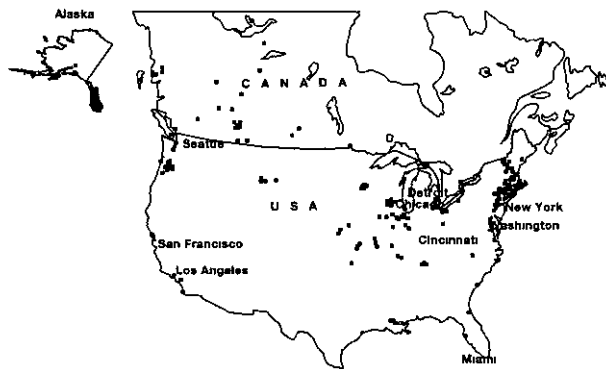


UK Rail. We are the UK's largest rail operator running nearly a quarter of the UK passenger rail network and carrying some 260 million passengers a year.

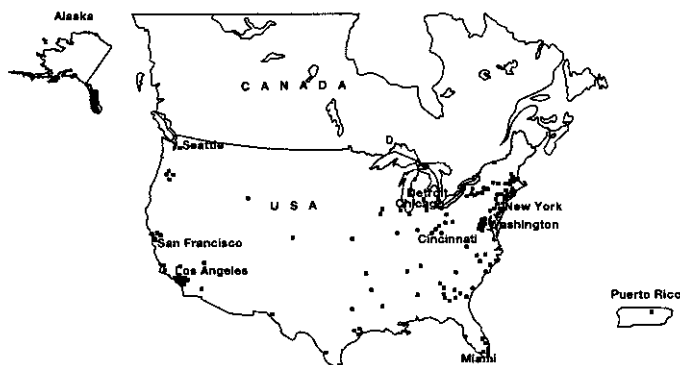
We have a strong, balanced portfolio and we are the only operator to run every type of overground rail service in the UK, from high speed intercity trains and overnight sleepers to local branch lines, regional and commuter services and open access, light rail and freight operations. We operate four passenger rail franchises: First Capital Connect, First Great Western, First ScotRail and First TransPennine Express. We also operate Hull Trains, a non-franchised open access operator. We also provide freight services through GB Railfreight and operate the Croydon Tramlink network which carries over 24 million passengers per annum. We have a strong track record of innovation and investment delivering improved services, such as new rolling stock and customer facilities across our rail operations.

UK Bus. We are the UK's largest bus operator, running more than one in five of all local bus services.

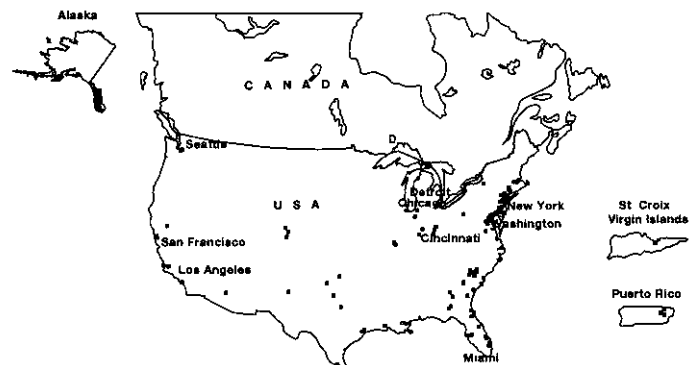
Our fleet of nearly 9,000 buses carries 2.9 million passengers every day in over 40 major towns and cities. The majority of our operations are in urban areas where the bus is the most effective means of tackling traffic congestion. We continue to develop and promote effective partnerships and we are working with local authorities and other stakeholders to provide punctual and reliable services for passengers through Punctuality Improvement Partnerships, bus priority and other traffic management schemes.



First Student



First Transit



First Services

North America: Headquartered in Cincinnati, Ohio, our three divisions have operations across the US and Canada.

First Student

We are the second largest provider of student transportation in North America with a fleet of approximately 22,000 yellow school buses, operating every day across the US and Canada. We are dedicated to providing the safest and most efficient student transportation service in North America. Our ethos is 'A safer and better way to the school day'.

First Transit

We are one of the largest private sector providers of transit management and contracting, managing public transport systems on behalf of transit authorities in cities such as Los Angeles, Houston and Denver. We are also one of the largest providers of

airport shuttle bus services in the US, serving airports in cities such as Baltimore, Philadelphia and Miami. We also manage call centres, paratransit operations and other light transit activities.

First Services

Our Services division is the largest private sector provider of vehicle maintenance and support services in the US. We provide fleet maintenance for private and public sector customers such as the Federal Government, cities and fire and police departments. We also provide a range of services including vehicle maintenance, logistics support and facilities management to public and private sector clients including the US Navy and US Air Force.

Financial highlights

22.4%

increase in revenue to
£3,708.8m

£108.8m

UK Rail operating profit up 36.7%

9.1%

increase in adjusted basic
earnings per share to 33.7p

£103.0m

UK Bus operating profit up 4.7%

10.0%

increase in dividend per share
to 15.5p

\$130.5m

North America operating profit
up 8.6%

	2007	2006
Revenue (£m)	3,708.8	3,030.9
Adjusted operating profit ¹ (£m)	259.2	229.7
Operating profit (£m)	203.6	210.7
Adjusted profit before taxation ¹ (£m)	195.8	176.4
Profit before taxation (£m)	140.2	157.4
Adjusted basic EPS ¹ (pence)	33.7	30.9
Basic EPS (pence)	23.1	27.4
Adjusted EBITDA ² (£m)	398.9	351.7
Adjusted EBITDA interest cover ³	6.3x	6.6x
Net debt (£m)	(516.2)	(704.4)
Share price at year end (pence)	665	425

¹ Before intangible asset amortisation, non-recurring bid costs, other non-recurring items and (loss)/profit on disposal of fixed assets

² Adjusted operating profit as defined above plus depreciation

³ Adjusted EBITDA divided by the net of finance costs and investment income

Chairman's statement

The Board's commitment to increase dividends by 10% for a further three years reflects our confidence in the Group's strong cash generation and prospects for further growth.

I am delighted to report a very successful year for the Group delivering on our clear strategy to profitably grow in our core markets and create further value for shareholders. Our focus is on delivering safe, high quality and reliable services throughout our business. The safety of our passengers and employees is our highest priority and we strive to lead the industry in this area and achieve the highest possible standards across the Group.

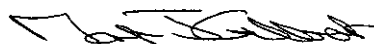
This has been a year of excellent progress across our business. We achieved a record set of results with revenue increased to £3,708.8m (2006: £3,030.9m) and adjusted profit before tax (before intangible asset amortisation, non-recurring bid costs, other non-recurring items and loss on disposal of fixed assets) increased to £195.8m (2006: £176.4m). Profit before tax was £140.2m (2006: £157.4m) reflecting higher one-off costs primarily as a result of non-recurring rail franchise mobilisation costs and lower property results. I am very pleased that the Group has delivered this strong performance despite the additional fuel cost increase during the year which impacted Group operating profit by £37.1m. EBITDA (Group operating profit* plus depreciation) increased to a record £398.9m (2006: £351.7m) and cash generation has been excellent. Adjusted basic earnings per share increased by 9.1% to 33.7p (2006: 30.9p). The Board has proposed a final dividend, subject to approval by shareholders, of 10.5p making a full year payment of 15.5p, an increase of 10%. The dividend is covered 2.2 times, before intangible asset amortisation, non-recurring bid costs, other non-recurring items and loss on disposal of fixed assets. It will be paid on 24 August 2007 to shareholders on the register on 20 July 2007. The Board's commitment to increase dividends by 10% for the foreseeable future, at least for a further three years, reflects our confidence in the Group's strong cash generation and prospects for further growth.

On 9 February 2007 we were delighted to announce the proposed acquisition of Laidlaw International, Inc. the leading provider of school and intercity bus transportation and a supplier of public transit services in North America. Following the approval for this transaction from both our shareholders and Laidlaw stockholders on 20 April 2007 we now only await the necessary antitrust regulatory approvals in the US and Canada for completion. We believe this transformational acquisition will significantly enhance shareholder value and underpins future growth. The integration of Laidlaw with FirstGroup gives us a unique opportunity to become the leading operator in the large, fragmented North American transport market and leverage value through scale. We have an excellent track record of successfully acquiring and integrating businesses and we are excited by the opportunities this acquisition will bring to increase the service offering to customers.

We recognise that our staff are our greatest asset. On behalf of the Board I would like to take this opportunity

to thank all of our staff for their continued hard work and commitment in delivering another excellent year for the Group. I would also like to welcome new employees who have joined our businesses in the UK and North America during the period.

I am very pleased with the progress achieved by the Group this year building on our position as a leading transport provider. We are delivering on our clear strategy to create shareholder value by sustainable growth in our core businesses and exploring opportunities to develop in new markets. We have made a significant investment in our business to ensure that we offer the highest level of service to our customers and we remain committed to increasing the dividend by 10% per annum for the foreseeable future. This is an exciting time for the Group as we consolidate our position in the highly attractive North American market and continue to deliver improved operating performance and revenue growth in our UK businesses. The Board is optimistic about the opportunities for the business and looks forward to the future with confidence.

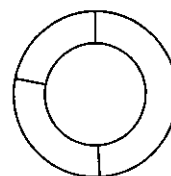


Martin Gilbert
Chairman

*Operating profit referred to throughout this document refers to operating profit before intangible asset amortisation, non-recurring bid costs, other non-recurring items and (loss)/profit on disposal of fixed assets.

Chief Executive's review

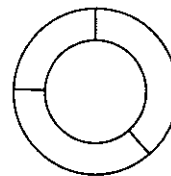
All of our businesses have delivered a very strong performance. Our strategy is focused on delivering high quality services for customers and value for shareholders.



Revenue

□ UK Rail	£1,824.1m
□ UK Bus	£1,073.7m
□ North America	£802.9m

Excluding other revenue of £8.1m



Operating profit

□ UK Rail	£108.8m
□ UK Bus	£103.0m
□ North America	£68.2m

Excluding central items of £20.8m

Overview

Safety

The safety and security of our passengers and staff is fundamental to everything that we do. We continually seek to improve the safety culture throughout our business and apply a 'zero tolerance' approach to unsafe acts and practices. Over the past few years we have made great strides in improving our working practices and procedures and in monitoring our performance in this area. We are never complacent and continually strive to meet the highest possible standards of safety for our passengers and staff. For example, our Injury Prevention Programme (IPP) is not only innovative but unprecedented in our industry. I am pleased to report that IPP has been rolled out across all of our operations and is designed to engage all our staff and encourage good safety practices to embed the safety culture in all of our operations.

Results

I am delighted with the excellent performance of the Group which has delivered a record year of growth. Group revenue increased by 22.4% to £3,708.8m (2006: £3,030.9m). Adjusted operating profit was £259.2m (2006: £229.7m). This strong performance is all the more notable as we have faced strong headwinds during the year, primarily the significant rise in fuel costs. In these results operating profit was impacted by £37.1m by additional fuel costs. Foreign exchange translation on North American results reduced sterling earnings year on year by £3.8m – the average rate for 2006/07 was \$1.89 compared to \$1.79 for 2005/06. Profit before tax was £140.2m (2006: £157.4m) reflecting higher one-off costs

primarily as a result of non-recurring rail franchise mobilisation costs and lower property results. Strong cash generation is a feature of this business and I am pleased to report that the Group generated record EBITDA (adjusted operating profit plus depreciation) of £398.9m (2006: £351.7m) an increase of 13.4%, enabling us to continue to invest in the business as well as increasing the dividend by 10% for the third consecutive year.

UK Rail

The UK Rail division operates passenger and freight services in the UK. We have a strong, balanced portfolio of intercity, regional and commuter franchises. Passenger rail franchises consist of First Great Western, First Capital Connect, First TransPennine Express and First ScotRail. We also operate Hull Trains, a non-franchised open access intercity passenger train operator, and we provide rail freight services through GB Railfreight. We are the UK's largest rail operator carrying almost 260 million passengers per annum.

Results

Our successful rail division has delivered its best ever year of growth. We are committed to the long-term development of railways in the UK and are investing to deliver improved services for passengers. We are the only operator to run every type of overground rail service in the UK, from high speed intercity trains and overnight sleepers to local branch lines, regional and commuter services and open access, light rail and freight operations. We will continue to build on our reputation of investment, innovation and customer service.

As we improve our services to give people a real alternative to using cars and other transport modes, bus and rail passenger numbers continue to increase with strong volume growth in both our UK Bus division and across our UK Rail division

A year into the franchise First Capital Connect is working on a range of initiatives to increase capacity across the network. We have started a programme to refresh our Class 319 trains, part of our £30m investment in the train fleet

Discounted tickets such as First Great Western's 'firstminute fares' have been a big success. More than 100,000 are available each week and 2.2 million have been sold in just nine months, saving customers £28m compared with the equivalent 'walk up' fares

Revenue in the Group's rail division increased by 56.6% to £1,824.1m (2006: £1,164.9m) and operating profit increased by 36.7% to £108.8m (2006: £79.6m) reflecting a full year contribution from the new and enlarged rail franchises together with strong volume growth across our network. Across all of our rail operations we have experienced good growth in passenger volumes

First Great Western

At First Great Western we are working hard to ensure that we deliver our franchise plans and we are investing £200m to improve the services we offer our customers. Since we commenced operation of the new enlarged franchise (combining First Great Western, First Great Western Link and Wessex Trains) we have integrated three diverse railway businesses into one operation. First Great Western operates more high speed trains into London than any other operator and provides train services for 1.5 million passengers each week.

During the past 12 months we have consolidated depots, introduced a new management structure and common systems, brought together 4,400 staff, introduced new amalgamated timetables, commenced a substantial fleet refurbishment programme and started the many major improvements which we committed to as part of our franchise. Despite our best efforts to ensure a seamless transition we faced some operational challenges principally as a result of changing the rolling stock maintenance depot and the introduction of a new consolidated timetable. We made great efforts to swiftly rectify those issues, the majority of which we have now

overcome. The new timetables which will be introduced in May and December this year will further improve services.

As part of our £145m investment to completely overhaul the High Speed Train (HST) fleet, we have commenced the installation of new more reliable, environmentally friendly engines. We have already fitted 42 new engines which have improved operating performance, doubled reliability, cut CO₂ emissions by 64% and smoke emissions by 42%. The remainder of these new engines will be in place by the end of this year. We are also making good progress on our fleet refurbishment programme. A new stylish and contemporary interior for the HSTs will offer a step change in quality for rail passengers and provide an additional 3 million seats for passengers per annum. The first of these new designed carriages are now in service and we are on track to complete the refurbishment of more than 405 carriages by the end of the financial year. We are also spending £4m on an interior refresh of our fleet of regional trains. The new platform at Bristol Parkway opened in May 2007 and will ease congestion of trains into and departing from the station and reduce delays for passengers travelling to London, Wales, Birmingham and the South West. We are working with Network Rail to upgrade the majority of the Reading to London relief line to 90mph by mid-2008 creating greater capacity, reliability and improved journey times for commuters in the Thames Valley. We have progressed our plans to deliver a range of improvements across the franchise area including the installation of automatic ticket gates at Exeter St Davids, Plymouth and Swindon, reducing both ticket fraud and crime on the railways. We have also invested in station

First Capital Connect has invested £1m to provide 24 Police Community Support Officers and five British Transport Police Officers for the network and has started to introduce gatelines at stations to further improve security for customers and employees

First Great Western and Network Rail are investing £1 billion across the franchise in the next two years. Our investment will improve punctuality and reliability and provide customers with an additional 3 million seats a year

Our £145m 'Refresh' programme of the First Great Western HST fleet will improve reliability, deliver punctuality benefits and enhance our customers' journeys. New engines for the entire HST fleet will reduce fuel consumption by 15% and carbon dioxide emissions by 64%.

improvements such as the installation of more than 120 additional ticket vending machines, increased car parking at stations, refurbished facilities and waiting areas at a number of stations across our network. We have simplified our fares structure and now offer more than 100,000 significantly discounted tickets each week for advance purchases and off peak travel. For example, 'firstminute fares' enables our customers to save up to 80% on regular fares when booking early. This has been very popular and already more than 2.2 million tickets have been sold saving customers a total of £28m compared to the equivalent 'walk up' fare. First Great Western faces major challenges from ageing infrastructure and the effect this has on performance. We are working closely with Network Rail, the infrastructure provider, to tackle the deep rooted performance issues on the network and overcome the recurring infrastructure problems on our main line. A number of initiatives have been designed to improve performance and we are committed to working in partnership to deliver improved infrastructure and services across our network.

First Capital Connect
First Capital Connect, which operates across London and the South East, had an equally busy first 12 months of operation and made an overall improvement in operational performance. PPM, the industry measurement of punctuality and reliability, improved to over 88% and we were particularly pleased to achieve the highest ever recorded PPM of over 95% on the Great Northern part of the network. We are investing £55m, the majority in the first three years of the franchise term, to improve the service we

offer our customers. During the year we commenced the refurbishment of waiting rooms and facilities at a number of our stations across the network. In addition we embarked on a programme to refresh the interiors of our Class 319 fleet. Eight units have already been completed and we will continue to roll this out to the remaining units in due course. In December last year we announced a further investment of £2m, over and above our franchise commitment, to improve the interiors of the trains that operate on the Great Northern route. This additional work, which will improve on board comfort for passengers, commenced in March 2007 and will be completed by the end of the year. During this period we also brought the engineering of our fleet in house which delivered greater service quality and cost efficiency. In April 2007 we

£145m HST investment

At First TransPennine Express we have invested £250m in new trains, improved station facilities and delivered a more punctual and reliable service. Customer satisfaction has increased and we were awarded four titles at the HSBC Rail Business Awards 2006, including 'Rail Business of the Year'.

Overall customer satisfaction with First ScotRail has reached its highest ever level at 88%, according to a survey by Passenger Focus. Punctuality and reliability are improving across the network and First ScotRail has reduced delays by 39% since the start of the franchise in October 2004.

Our successful and innovative freight business GB Railfreight has won £45m in new contracts with customers including Royal Mail, Metronet, Serco Rail operations and Drax Power and added to its fleet with a £28m investment programme.

of additional staff to carry out further ticket checks and the installation of automatic ticket gates at a number of stations across the network including Blackfriars, City Thameslink and Stevenage. Further automatic ticket gates will be installed at key stations across the network in the coming months. We have also invested over £1m to provide additional Police Community Support Officers and British Transport Police to serve our network. These initiatives are proven to improve security, reduce ticketless travel and lessen vandalism.

First ScotRail

We are proud to operate Scotland's train services through our First ScotRail operation. Since we took over the franchise in October 2004 we have established a successful record of delivering improved services for passengers together with a strong focus on operating performance and service quality. We have reduced operator delays, for which we are responsible, by some 39%, over and above our franchise commitment of 2% per annum. Performance has continued to improve over the year and we are now regularly running services at more than 90% punctuality. We were pleased to record the highest PPM performance in seven years for the last period. In addition customer satisfaction has been recorded at its highest level and outperformed the average for regional train operators. During the year we continued to invest in fleet reliability and passenger comfort and also provided additional services to meet demand such as increased late night services on 18 routes out of Glasgow Central on Fridays. Increased security and revenue protection is a key priority and we have installed automatic

welcomed the announcement by the Department for Transport that the remaining 12 Class 319 trains will be transferred to First Capital Connect from Southern Railway. These trains will provide up to 8,000 extra seats per day during the peak periods and help to ease crowding on our very busy Thameslink route. In addition improvements to be introduced in the May timetable will also increase capacity at peak times, providing more seats for customers in the morning and evening peak with additional services and an increased number of carriages on some of our busy routes. One of our key priorities is to improve security on the network and reduce ticket fraud through improved revenue protection. We have provided customers with improved ticketing facilities and have already reduced revenue leakage through the introduction

First Great Western is introducing new and improved catering services including a redesigned buffet and an extended at seat service. Every year First Great Western customers consume nearly 1 million litres of tea and coffee, 400,000 litres of mineral water and over 1 million sandwiches.

Hull Trains introduced an additional weekday service between Hull and London Kings Cross taking its total number of weekday services to seven in each direction. Over 2 million passengers have now used Hull Trains services.

First TransPennine Express has introduced an entire fleet of new trains. This, combined with our focus on performance and customer service, has led to passenger satisfaction reaching a record high.

ticket gates at stations including Aberdeen, Ayr, Dundee and Stirling. Security is further enhanced by the installation of CCTV on almost the entire First ScotRail fleet and we are continuing our investment programme to roll out CCTV, customer information systems, induction loops and help points at stations across the country. Over the last year a number of investments have been made to improve the level and availability of facilities at stations in Scotland. In February 2007, an extension to Haymarket Depot in Edinburgh was opened. This extension of two maintenance facilities will assist in further improving the reliability of the Class 170 and Class 158 fleets, by providing the opportunity for more trains to be maintained more quickly.

First TransPennine Express

First TransPennine Express had another successful year with excellent operational performance coupled with strong revenue and volume growth reflecting the high demand for its services in the region. Passenger journeys increased by 7.3% to 18.5 million during the year. Our focus on performance has ensured that PPM is consistently over 90% and overall customer satisfaction has exceeded the national average for all train operators. Since we commenced operation of the franchise two years ago we have introduced an entire fleet of brand new 100mph Siemens trains which have a range of new, high quality features such as improved seating, air conditioning, on board security cameras and easier access for all passengers. We continued our station investment programme during the year and spent £2m refurbishing waiting areas and customer and staff facilities. We secured

additional funding from the Department for Transport to provide accessibility improvements such as automatic doors, disabled facilities and ticket counters at stations across our network. During the year we successfully managed the integration of the Manchester Airport to Blackpool routes which we took over in June 2006. We have demonstrated our competence in delivering the process both smoothly and cost efficiently. From December 2007 we will further extend our TransPennine network to operate the Manchester Airport to Glasgow and Edinburgh services. We are very proud of our achievements at First TransPennine Express and were delighted that our efforts were recognised by the industry when we were awarded an unprecedented four national awards, including 'Rail Business of the Year' at the HSBC Rail Business Awards 2006.

Hull Trains

Hull Trains, our non franchised, open access intercity train company operating between London Kings Cross and Hull, performed well during the year with strong passenger volume growth which increased by 30%. In December we were pleased to be awarded an additional train path by the Office of Rail Regulation bringing our number of weekday services to seven in each direction. This clear response to passenger demand ensures that we can offer our customers a greater choice and level of service. Our focus on operational performance has ensured that we are once again ranked as the most reliable long distance operator on the East Coast Mainline with performance figures that exceed the industry average for long distance operators.

On 9 February 2007 FirstGroup announced the \$3.6 billion proposed acquisition of Laidlaw International, Inc. the leading operator of school buses, the provider of Greyhound bus services and a supplier of public transit services in North America

At First Student over 6,500 drivers have now been trained in the Smith System Advanced Driving module, which focuses on 'five keys to safe driving'

All our North American operating companies now participate in the Automotive Service Excellence (ASE) programme for training and testing technicians

GB Railfreight

We are pleased with the progress of GB Railfreight (GBRf), our innovative and demand responsive freight company. GBRf enjoyed another successful year winning further contracts worth some £45m to provide rail freight services around the UK for customers such as Drax Power, EDF Energy, Mendip Rail and Serco. In addition, we were pleased that Royal Mail extended a contract for GBRf to move mail by rail, demonstrating the success of the operation and the service provided. In August 2006 we successfully commenced a significant contract to transport infrastructure materials for Metronet as part of the renewal programme on the London Underground. In March 2007 we were pleased to run the first freight train transporting coal between the Port of Tyne directly into Drax Power Station in North Yorkshire. We have invested in a number of freight locomotives and wagons in order to support the new contracts and the ongoing development of the business. GBRf has delivered further growth and contract wins through the development of its innovative and customer focused business model and we are optimistic about the future prospects for this business.

New franchises

This has been a busy year for the Group as we commenced operation of our two franchises First Great Western and First Capital Connect and integrated the new areas with existing operations. We are committed to a long term future in the UK's railways and are delighted to be shortlisted for three further franchises: East Midlands, New Cross Country and InterCity East Coast. We have an impressive and unrivalled track record of integrating

services and delivering on large investment programmes. Our bid team is highly experienced and committed to delivering plans that meet the needs of passengers by bringing new investment and improved services that are cost efficient.

North America

In North America the Group is currently the second largest provider of student transportation with approximately 22,000 yellow school buses operating every day across the US and Canada. We operate a transit contracting and management business in North America and we have a services division providing fleet maintenance and ancillary services to public and private sector clients.

Our North American business has delivered solid and consistent returns for shareholders since we entered the market in 1999. During that time we have generated \$1,335.8m of EBITDA. This division is cash generative after self-financing maintenance capital expenditure, organic growth within existing contracts and the acquisition of small in-fill businesses.

Our successful growth in North America confirms our view that this is a highly attractive market which offers significant growth opportunities for our business. We have built up significant experience and expertise in this marketplace and believe that it offers opportunities to deliver further attractive earnings growth and value for shareholders.

First Transit is the industry leader in specialised transportation management services with more than 20 paratransit management contracts nationwide. Our call centres handle over 4.6 million transportation calls every year.

First Student carries over 1 million students to and from school every day. From Alaska to Florida and from Massachusetts to California, the primary focus and mission of our drivers and technicians is to transport students in safety.

The proposed acquisition of Laidlaw will create a strong platform to secure long-term growth in our North American business. On completion, the deal will create North America's leading transport services company operating over 60,000 yellow school buses.

4.6m

calls handled every year

Results

I am pleased with the performance of our North American division which delivered margin improvement during the year. Revenue from our three businesses was £802.9m or \$1,522.4m (2006: £826.3m or \$1,476.0m). Revenue in these results is £45.8m lower than the prior year due to foreign exchange movements. Operating profit increased to £68.2m or \$130.5m (2006: £67.1m or \$120.2m) despite absorbing additional fuel costs of \$11.2m or £5.9m.

First Student

We have had a successful year within our school bus business despite continued fuel cost pressure. US Dollar revenue increased by 5.4% and operating profit rose by 14.7%. During the year we have worked hard to mitigate the impact of cost pressures through the contract renewal cycle and have won or renewed business on terms which reflect the increased costs that we face. Margin enhancement has been a priority for us this year and through contract bidding, tight management of controllable costs and a strong focus on productivity we have improved margins to 10.9% (2006: 10.0%). We enjoyed a good bidding season with contract retention, which is a key feature of this business, at over 95%. We continued to grow our share of this large, fragmented market through a mixture of new contract wins, organic growth and in-fill acquisitions. During the year we expanded into Sedona, Arizona and we won a significant contract in Savannah, Georgia. In addition we completed five take-in acquisitions in New Jersey, Connecticut, New York and Illinois that either complement our existing operations or enable us to enter new markets.

We were pleased to retain almost 100% of our business in Canada which remains an attractive market for First Student in which we aim to grow further.

Looking forward we had a successful bidding season and continue to focus on profitable growth and margin enhancement. Our strategy is to continue to improve our product offering and closely manage our cost base in order to offer a compelling service to our customers, parents and students. This year sees the further rollout of new technology such as GPS and Zonar equipment which provides us with detailed and accurate information which will enable us to schedule services and labour more efficiently as well as provide our customers with real-time information about services.

First Transit

First Transit had a successful year with US Dollar revenue increased by 1.7% and operating profit by 15.6%. Our strategy to improve the margin and implement a significant cost control and efficiencies programme throughout the division has delivered good results with margin increased to 4.9% (2006: 4.3%).

During the year we continued to grow the business with the award of new business including paratransit contracts in California and Ohio. We also continued to grow our share of the outsourced call centre market with a new contract in Oregon. This is in line with our strategy to further penetrate the faster growing light transit markets in North America. We now operate ten call centres in cities such as Chicago, Denver, Hartford, New York and Portland.

First Student successfully retained over 95% of its contracts which came up for renewal during the year. First Student has more than doubled in size since we entered the North American market in 1999 by winning new business, organic growth and in-fill acquisitions.

Thousands of First Student's buses utilise the latest, state-of-the-art safety and security advances, including GPS and Zonar, a hand-held computerised inspection tool used by school bus drivers prior to and following every bus trip. We continue to invest in the latest technology to ensure the safety of the students we carry.

Our First Vehicle Services location in Fort Wayne, Indiana was named most efficient fleet at the 'Best Fleets in North America' awards. Fort Wayne operates a 1,400-vehicle fleet with a 99% average overall vehicle availability and has reduced maintenance costs by 15% over the last decade.

At First Student our driver turnover has reduced by 3.5% this year. Our management has been working hard to identify ways to improve driver retention, including an increased emphasis on communication to ensure good information flow and enable employees to raise any concerns.

We were also awarded new transit management business through contracts won in Iowa, Ohio, Texas and Virginia. We were pleased to win the contract to operate more than 170 buses in El Paso, Texas and renew a contract in Minnesota for an additional five years. The private shuttle bus market is an area of growth for First Transit and during the year we acquired Cognisa. This in-fill acquisition further strengthened our presence in the US private shuttle bus market with 19 customer contracts located across seven states. First Transit is one of the leading providers of shuttle bus services with contracts to serve airports in cities such as Cincinnati, Houston, Miami, Philadelphia, Portland and Las Vegas. I am pleased with the progress made at First Transit this year. This business, which requires little or no capital expenditure, has improved its

margin and continues to deliver returns. We continue to grow our expertise in this market and develop potential for future profitable growth.

First Services

This year First Services, which provides a range of outsourced vehicle maintenance, operations and support services in the private and public sectors, renewed a significant contract within the large, federal market. US Dollar revenue was, as anticipated, down by 1.9% reflecting the renewal, at a lower margin, of a substantial contract to provide land-based support services to the US Navy. This important contract with revenues of over \$450m over the term was re-awarded to First Services for ten years in July. Our strategy is to achieve organic growth within the existing contract through the provision of additional add-on services. We also won new business in the large federal market through the award of a contract to provide support services to the Defense Logistics Agency in San Joaquin, California. We expanded our fleet maintenance business with new business wins for the City of Newport, Rhode Island and Ocean Township, New Jersey and with customers such as Eastman Chemical, Allegheny Power and Motiva Shell. Looking ahead our focus is to achieve organic growth within the large federal contracts and continue to use our expertise and strong track record of customer service to grow in these areas.

Proposed acquisition of Laidlaw International, Inc
On 9 February 2007 the Group announced the proposed acquisition of Laidlaw International, Inc, the leading

This year First Vehicle Services introduced an online quarterly customer service survey. Over 90% of our customers are either 'satisfied' or 'very satisfied' with the service that is delivered.

First Student has worked very hard to progress its safety culture and safety performance. This year we achieved significant reductions in employee injuries, collisions and passenger injuries.

First Transit's acquisition of Cognisa more than doubled our shuttle bus business, adding a further 19 customer contracts located in seven states across the US.

First, Sheffield City Council and South Yorkshire Passenger Transport Executive signed 'The Sheffield Bus Agreement', a Voluntary Quality Partnership Agreement that will lead to a range of significant measures, including £16.9m of funding, that will benefit millions of First customers in Sheffield each year.

operator of school and intercity bus transportation and a supplier of public transit services in North America for a consideration of \$3.6 billion. We have received approval from both FirstGroup and Laidlaw shareholders, and the acquisition now remains conditional on the receipt of necessary antitrust approvals in the US and Canada. We are working with the relevant antitrust authorities to provide the necessary information, including the Department of Justice to comply with their second request process.

This is a transformational deal with considerable prospects for value creation. This is a unique opportunity to establish the leading position in the North American transportation market and generate significant value and returns for shareholders. In bringing together FirstGroup America and Laidlaw, we believe we can create a stronger, more robust business in a highly fragmented market. We aim to leverage value through scale and grow earnings through improved operating efficiencies and extraction of substantial synergies. This acquisition will provide a strong platform for us to improve our offering to customers by bringing further operational and cost efficiencies, economies of scale and a greater range of services. Since the announcement we have made good progress on a number of plans for the integration of the businesses.

Laidlaw International, Inc. has some 62,500 employees and operates three main business segments in the US and Canada.

Laidlaw Education Services, which operates approximately 40,000 yellow school buses in 37 states in the US and six provinces in Canada.

Greyhound is the only national provider of scheduled intercity bus transportation services in the US and Canada. Greyhound provides scheduled passenger services to approximately 2,400 destinations throughout the US and Canada, carrying approximately 24 million passengers annually. We consider Greyhound to be an attractive business with exciting growth prospects and have committed to carry out a strategic review of the business.

Laidlaw Transit Services provides municipal public transportation services in North America, specialising in paratransit and fixed route contract services in approximately 23 states in the US.

UK Bus

The Group is the largest bus operator in the UK with a fleet of nearly 9,000 buses and a market share of approximately 23%. We carry over 2.9 million passengers every day.

Results

I am pleased to report another year of strong trading performance from our UK Bus division. Revenue increased to £1,073.7m (2006: £1,031.2m) as a result of revenue and passenger growth initiatives and increased journeys including concessions and pricing. Operating profit was £103.0m (2006: £98.4m). This is a particularly notable achievement as operating profit was adversely impacted by £28.2m as a result of increased fuel costs.

We have been working hard to improve connectivity with many airports across the UK and Ireland and have introduced York Aircoach, a new service between York railway station and Leeds Bradford International Airport

We are the first major bus operator in the UK to publish our punctuality and reliability data. This is part of our mission to meet customers' travel needs by providing a quality service in the local area that is sustainable, profitable, and of which we are proud

Our UK Bus division was named winner in the 'Skills for Life' category at the Business in the Community 2006 awards. This year 1,100 bus drivers received vocational qualifications. 20% of our bus drivers are now qualified with more planned for this year

We introduced the 'UK Bus Engineering Apprentice Awards' in recognition of the hard work and dedication of our engineering talent from across the UK. This annual event acknowledges successful completion of apprenticeships and recognises individual achievement

We continue to deliver improvements in operational performance and efficiency within the business. Targeting improvements in quality, allied to initiatives to tightly control our costs, continues to underpin our strategy of margin enhancement. Depot and route optimisation, a focus on headway management together with revenue and passenger growth initiatives, contributed to a turnaround in profitability and service quality of operations. We are also implementing a programme to target a consistent level of fleet cleanliness and appearance. I am pleased to report that the significant investment in our maintenance and engineering functions in recent years, and the implementation of initiatives to improve engineering efficiency and planning and to standardise our processes, has continued to reduce our lost mileage this year.

In London we have focused on operational performance and cost efficiencies and are pleased to report that our overall punctuality and reliability has improved again this year. Our operations in the West of London are currently top of the Transport for London (TfL) league tables. In preparation for the western extension of the Congestion Charge, TfL increased the frequency of a number of our services to provide additional passenger capacity.

We welcome the Government's commitment to buses and its recognition that buses are a crucial part of our transport system, set out in 'Putting Passengers First'. We believe that the industry has demonstrated that the most effective way to deliver better services to passengers is through voluntary partnership agreements. Working in partnership with local authorities to deliver improved bus services for

passengers continues to deliver encouraging results in our business. Passenger numbers are increasing throughout our operations, supported by growing numbers of concessionary fares passengers benefiting from the Government's introduction of a new scheme in April 2006. We are seeing particularly strong growth in passenger numbers where, working in partnership with local authorities, we are delivering measures to improve the punctuality and reliability of our services.

We are pleased to report the commitment of local authorities across the UK to delivering improved bus services for passengers through partnerships. In November we signed a 'Stability and Growth Pact' with Glasgow City Council and Strathclyde Partnership for Transport. The pact will bring major improvements to Glasgow's bus services including an annual Route Development Plan, a Joint Performance Improvement Plan to make significant improvements in punctuality and reliability and sustained growth in bus passenger numbers with a commitment for reasonable fares. The pact builds on the city's award-winning £30m Streamline Partnership between First and Glasgow City Council, Strathclyde Passenger Transport and the Scottish Executive last year.

At the start of May 2007 we signed 'The Sheffield Bus Agreement', a Voluntary Quality Partnership (VQP) Agreement with Sheffield City Council and South Yorkshire Passenger Transport Authority. We believe that this agreement is the most comprehensive VQP ever agreed. The agreement will give customers a more stable network and improve the reliability of bus services by delivering

ftir is now in its second year and a new scheme started in Leeds in January. We are delighted by the reaction of our customers, our employees and our stakeholders. A recent independent customer survey in York showed a satisfaction rating of 87%.

Three years after the initial group of 36 Polish bus drivers were deployed to Bath and Bristol, our European Union recruitment programme has delivered over 1,200 staff to our UK Bus division with a retention rate of over 90%.

We have invested more than £40m in our bus operations in Manchester to support passenger growth. By working with local authorities we are delivering more punctual and reliable services for our customers.

significant financial investment and improvements to the city's bus infrastructure. Over the next two years we will invest £10m in new vehicles, extra CCTV cameras on buses and training programmes for staff. The Transport Executive and the City Council have invested £4.4m during the year and have agreed to invest £2.5m in the coming year which will be used to fund infrastructure improvements.

We are working in partnership with the four Unitary Authorities in the Greater Bristol area to deliver improved bus services in the region. The authorities have submitted final plans to the Department for Transport for ten 'Showcase' routes as part of the Greater Bristol Bus Network. The network will see a major investment of some £49m in new infrastructure, including bus lanes, road widening, improved bus stops, enhanced traffic controls and Real Time Passenger Information as well as some £20m in new buses. This demonstrates the strong working relationship which delivered the first Showcase route in Bristol, now operating very successfully, and a second Showcase route due for completion later this year.

All of our operating companies are working on plans to improve the punctuality of our bus services on a route by route basis. We are the first of the major operators to publish punctuality and reliability data by operating company and are working with local authorities in all of our operating areas to develop Punctuality Improvement Partnerships (PIPs). We developed our first PIP with Greater Manchester Passenger Transport Executive and now have a number of PIPs in progress to deliver improved

bus services for passengers. We continue to address issues within our direct control, for example, by introducing new timetables to improve the punctuality of our services. The PIP process has highlighted that, in order to achieve improvements in service performance in some cases, highway alterations and other infrastructure works are required. Some of these are already being addressed by our partners.

In January this year we started our second ftir service in Leeds. ftir was first launched in York in May last year and uses state of the art articulated tram like vehicles. We have seen passenger growth of 28% on the York ftir service and continue to be encouraged by positive feedback from our customers, local authorities from across the UK and from wider stakeholders. Independent customer research showed an 87% satisfaction rating amongst passengers using the ftir service. We continue to develop plans for further ftir services and our scheme in Swansea will start next year.

We are pleased with the continued development of Aircoach, which operates express coaches between Dublin city centre and the airport and contracted services for airport car parks. The company continued to perform well during the year and significant passenger growth at Dublin Airport has benefited both our scheduled and our contracted car park services. We are using the Aircoach model to introduce new services in the UK and recently launched York Aircoach, a frequent, express, direct coach service between York rail station and Leeds Bradford International Airport.

This year we introduced biodiesel to all of our UK Bus operating companies and started a programme to support fuel efficiency improvements. All of our new buses have Euro IV engines further reducing fuel consumption and carbon dioxide and other harmful emissions.

The key to having a trained, motivated and customer focused workforce is making sure we recruit and retain the right staff. Through improved recruitment processes and a comprehensive learning and development programme driver turnover in our UK Bus division is at a record low.

First and the Transport and General Workers' Union signed the first national agreement on life long learning that will encourage and support a culture of learning and continued personal development throughout the UK Bus division.

This year Hull Trains became the latest of our companies to achieve the prestigious Investors in People standard. We are committed to continuously improving our performance by investing in our people.

We welcome the Government's announcement encouraging local initiatives in support of improved school transport services. We pioneered the introduction of American style yellow school buses into the UK and one of our first pilot schemes in West Yorkshire was the precursor to Metro's MyBus initiative, which has successfully reduced congestion at the school gates by giving parents a high quality alternative to using their cars for the school run.

Capital expenditure was focused in areas with potential for high passenger growth. Towns and cities including Aberdeen, Bradford, Bristol, Glasgow, Leeds and Manchester were among those who benefited from our £57m spend on new low floor, easy access buses this year.

We were delighted that our commitment to investing in our people at all levels was recognised at the Business in the Community Awards 2006. The 'Rentokil Initial Skills for Life' award, supported by the Department for Education and Skills and in association with Investors in People, recognised our joint strategy, with the Transport & General Workers' Union, to improve recruitment, retention and motivation. Our learning and development initiatives, together with improvements to our recruitment and training programmes and our European recruitment programme, has reduced driver turnover to an all time low.

Europe

We continue to invest in European bidding activity. We have submitted bids for Connexion in the Netherlands and also, with our partner DSB, for the Øresund rail

franchise which links Denmark and Sweden. While North America remains our primary market for growth and international expansion we continue to explore opportunities in new markets. We recently made a modest investment in Germany of 130 buses in the Rhein Neckar region. This small entry into Germany enables us to build a greater understanding of the market as it continues to liberalise.

Group outlook

All of our businesses have delivered a very strong performance. Our UK Rail division continues to go from strength to strength. This year we commenced operation of two new enlarged franchises. We have made significant investment across all of our rail businesses to deliver improvements in rolling stock, capacity and services for passengers. Demand for our services continues to accelerate with passenger and income growth across all of our rail operations. We are delighted to pre-qualify for a further three franchises: East Midlands, New Cross Country and InterCity East Coast and await the outcome later this year. I am pleased with the strong trading result from our UK Bus division despite absorbing additional fuel costs of £28.2m. We have delivered improved operating performance and volume growth. Increased passenger journeys, together with our initiatives to grow revenue and bear down on costs, have resulted in a strong performance. We continue to promote a partnership approach to delivering a comprehensive and sustainable bus network in the towns and cities where we operate and have seen encouraging growth as a result. Our North American business has enjoyed high contract retention.

Our Injury Prevention Programme is innovative, unprecedented in our industry and designed to engage all our staff in safety and embed a safety culture in all of our operations. This year lost time injuries have been reduced by 31%.

FirstGroup won the award for 'Continuing Environmental Excellence' at the Network Rail Environment Awards 2006, for innovative environmental initiatives introduced throughout the Group over the years, which demonstrated a proactive approach in all areas of environmental management, including our stations and supply chain.

We are one of the Major Supporters of Scotland's bid for the 2014 Commonwealth Games. A First ScotRail train, specially wrapped in the Commonwealth Games Bid livery, will travel the length and breadth of Scotland in the months leading up to the final decision on the 2014 Host City.

and margin improvement. We are seeing the positive impact of our strategy to mitigate fuel cost pressures through the contract renewal process. The Board is pleased with the consistent returns generated from this business since we entered the market in 1999 and remains confident that North America offers further exciting growth prospects for the Group.

Our strategy is focused on delivering value for shareholders from further growth within our core businesses and exploring opportunities to develop in new markets. For the third year running we have increased the dividend by 10% reflecting the Board's confidence in the Group's future prospects and ability to continue to generate strong cash flows. We are committed to this level of annual dividend growth for the foreseeable future, at least for the next three years. I am pleased to report that trading in the new financial year has started well and is in line with our expectations.

Corporate Social Responsibility (CSR)

CSR is at the core of our business. We believe that in order to deliver sustainable growth CSR must be embedded in the vision and values of a business. Our aim is to transform the way people travel and how they feel about public transport. Our management of key issues such as safety, environment, our relationships with customers and our employees is at the heart of our strategy and key to achieving our vision.

This year we reviewed the content of our Code of Business Ethics and Group Equal Opportunities Policy as part of

our ongoing efforts to implement best practice in these areas. After consultation with independent CSR auditors, corporate governance professionals and our shareholders we decided to incorporate all of our existing policies into one Group CSR Policy.

Safety is our highest priority. We are continuously developing and improving our processes to ensure that a 'Safety First' culture is embedded throughout the Group. We strive to ensure that our services are as safe as possible for our passengers and our staff. Over the last year we have worked very hard to improve our safety culture and performance. We have accomplished significant improvements including significant reductions in employee injuries, collisions and passenger injuries.

As the UK's leading public transport operator we have a unique opportunity to improve the environment by helping to reduce traffic congestion, carbon dioxide emissions and air pollution. We are working hard to reduce the environmental impacts of our operations.

FirstGroup was presented with the gold award for our environmental submission in the Transport, Freight and Highways category at the 2006 Green Apple Awards.

This year, as part of our ongoing efforts to implement best practice in these areas, we produced an updated Group CSR Policy. After consultation with independent CSR auditors, corporate governance professionals and shareholder groups we included among other things, specific reference to Freedom of Association through a secret ballot which employees tell us is important to them.

We have pioneered and rolled out safety standards over and above the requirements of the safety regulators. Our Injury Prevention Programme (IPP), which has been rolled out throughout the Group, is innovative and designed to engage all our staff in safety. The aim of IPP is to ensure that action is taken to report any matters of safety and to resolve them promptly in order to prevent any harm from occurring to anyone. Lost time injuries across the Group have reduced by 31% this year. However, we are never complacent and strive to ensure that we continuously improve our performance in this critical area.

Our people are often the first point of contact between our customers and our business and are central to our success. Their commitment, dedication and effort are crucial if we are to meet our customers' expectations and ensure that we are the leader in safe, innovative, reliable, sustainable transport services. We want to be the employer of choice in our industry, offering our staff opportunities to develop and grow to reach their full potential. We continue to invest in the training and development of our employees across the Group. We have ongoing programmes for employees working towards recognised training in the form of vocational qualifications. In UK Bus our successful partnership with the Transport and General Workers' Union to expand our workplace learning provision continues and we are sponsoring the Business in the Community 'Skills for Life' award this year to encourage other employers to follow our lead. In North America all of our technicians can now participate in the Automotive Service Excellence Programme designed to train and test technicians. First Student continues to

promote the 'Smith System of Defensive Driving' to further improve our safety performance and to further reduce the possibility of incidents likely to lead to passenger or employee injuries or collisions.

We continue to receive recognition for improving our environmental performance. At the Green Apple Awards we were presented with a gold award in the Transport, Freight and Highways category. We also received the 'Continuing Environmental Excellence Award' at the Network Rail Environment Awards 2006 and were runners up in the National Business Awards for Scotland 2006 in the 'Scottish Power Environmental Awareness Awards'. We are pleased that our commitment to integrating corporate social responsibility into our business and to managing, measuring and reporting our key social and environmental impacts resulted in an improved score in the Business in the Community Corporate Responsibility Index 2006. We also participate in the FTSE4Good Index and the Dow Jones Sustainability Index.

Our CSR Policy, together with our Corporate Social Responsibility Report, which gives further details of our activities and progress during the year, can be found at www.firstgroup.com



Moir Lockhead
Chief Executive

Finance Director's review
2006/07 was a year of significant achievements in terms of the results with Group revenue exceeding £3.7 billion and adjusted operating profit exceeding £250 million for the first time.

Overview

2006/07 was a year of significant achievements in terms of the results with Group revenue exceeding £3.7 billion and adjusted operating profit exceeding £250 million for the first time. Our UK Rail and North American businesses have reported record earnings and adjusted basic EPS and EBITDA are the highest we have ever achieved, up 9.1% and 13.4% respectively on last year.

The Group is now the UK's largest passenger rail operator. At the start of the year we added First Capital Connect and the enlarged First Great Western to our portfolio of rail franchises. Passenger revenue growth across all Train Operating Companies (TOCs) has been very strong and profits have grown by more than a third. UK Rail generated over 40% of Group profits.

In February 2007 we announced the acquisition of Laidlaw subject to shareholder approval and antitrust clearances. When completed, in excess of 50% of the Group's revenue and adjusted operating profit will come from North America. The prospects for value creation are considerable. In addition to the significant synergies to be achieved by combining our current North American operations with Laidlaw, we will have the scale and expertise to become our customers' first choice for safety and service quality.

The net pension deficit has been eliminated and we now have a net surplus when measured on an IAS 19 basis. This has mainly been achieved through additional cash payments into the schemes during the year, further recovery in equity markets and by limiting future increases in pension costs.

One-off costs of £21.3m for rolling stock refurbishment, redundancy and other mobilisation costs were incurred on the start-up of the two new rail franchises. These costs relate entirely to the mobilisation and will not be repeated in 2007/08.

We have continued to invest heavily in new buses during the year in both UK and North America. In addition we have invested £110.0m in our UK Rail franchises to improve capacity, performance and customer service. This significant investment is likely to be repeated in 2007/08 but thereafter will fall to maintenance requirements only.

Results

Revenue was £3,708.8m (2006: £3,030.9m), an increase of 22.4%. Adjusted operating profit was £259.2m (2006: £229.7m), an increase of 12.8%. Adjusted operating profits were higher at each division and margin improvements were made both in North America and UK Bus, despite an additional £37.1m of fuel costs year on year.

Finance Director's review continued

Divisional results	Year to 31 March 2007			Year to 31 March 2006		
	Revenue £m	Adjusted operating profit ¹ £m	Operating margin ¹ %	Revenue £m	Adjusted operating profit ¹ £m	Operating margin ¹ %
UK Bus	1,073.7	103.0	9.6	1,031.2	98.4	9.5
UK Rail	1,824.1	108.8	6.0	1,164.9	79.6	6.8
North America	802.9	68.2	8.5	826.3	67.1	8.1
Other ²	8.1	(20.8)	–	8.5	(15.4)	–
Total Group	3,708.8	259.2	7.0	3,030.9	229.7	7.6

¹ Before intangible asset amortisation, non recurring bid costs, other non recurring items and (loss)/profit on disposal of fixed assets

² Tram operations, central management, Group information technology and other items

Throughout the Finance Director's review operating profit, operating margin and EBITDA are defined as being before intangible asset amortisation, non recurring bid costs, other non recurring items and (loss)/profit on disposal of fixed assets

UK Bus revenue was £1,073.7m (2006: £1,031.2m), an increase of 4.1% or an increase of 6.0% when adjusted for last year's additional days. Operating profit was £103.0m (2006: £98.4m), an increase of 4.7%. Results were driven by strong volume growth, with passenger volumes outside of London increasing by over 2%. A focus on improving operational performance and initiatives to tightly manage controllable costs led to a margin improvement of 0.1% despite £28.2m of additional fuel costs year on year. The new English concessionary schemes for OAPs that commenced at the beginning of the year stimulated most of the growth in passenger numbers. However, better operational performance also contributed to passenger growth. During the year a number of bus operating leases were restructured as finance leases. This has resulted in a decrease in the charge for the financing element of leases and an increase in the depreciation charge, both of which go through the 'operating cost' line and an increase in the charge for finance lease interest which goes through the 'finance cost' line.

UK Rail had an exceptional year with strong revenue growth across all TOCs combined with the two new franchises. Revenue was £1,824.1m (2006: £1,164.9m), an increase of 56.6%. Operating profit was £108.8m (2006: £79.6m), an increase of 36.7%. Whilst favourable economic growth contributed to these results, so too did the considerable investment that we are making to improve services. Both First TransPennine Express and First ScotRail are delivering significantly better punctuality and record customer satisfaction ratings. Both First Capital Connect and First Great Western are investing in significant fleet upgrades that will enhance performance, capacity and customer satisfaction. We have been shortlisted for three further franchises (InterCity East Coast, New Cross Country and East Midlands) and await the outcome of all three.

North American revenue was £802.9m (2006: £826.3m). Although lower in Sterling, at constant exchange rates, this result represents an increase of 3.1%. Operating profit was £68.2m (2006: £67.1m). In US Dollar terms this represents an increase of 8.6%. Overall the North American US Dollar margin improved by 0.5% to 8.6% despite higher fuel costs. All three operating divisions enjoyed strong contract retention over the course of 2006/07. Earnings growth was particularly strong in Student and Transit Services. Profits and margins fell due to the retendering of a significant contract.

Central costs were higher than last year reflecting the growth in the business as well as an unusually high level of corporate activity.

Property

Property losses of £3.7m (2006: profits of £14.0m) were incurred during the year. There were no significant properties disposed of during the year and the loss incurred was largely due to abortive costs in relation to the Aberdeen depot relocation.

Intangible asset amortisation

The intangible asset amortisation charge was £10.3m (2006: £4.5m). This increase is mostly explained by higher pension intangible charges on the new First Capital Connect and First Great Western franchises.

Non recurring bid costs and other non recurring items. Bid costs of £19.3m (2006: £28.5m) were incurred during the year. Of this amount UK Rail bids for South Western, New Cross Country and InterCity East Coast franchises accounted for £14.5m. Non rail bid costs of £4.8m (2006: £2.4m) were incurred principally on European bid activities.

UK Rail transition costs of £21.3m (2006: £nil) were incurred in mobilising the First Capital Connect and First Great Western franchises including subsequent obligations to refurbish trains on both franchises. These costs will not recur in 2007/08.

Finance costs

The net finance cost was £63.4m (2006: £53.3m) with the increase of £10.1m explained by higher lease finance debt, higher bank debt and higher US interest rates. The net finance cost is covered 6.3 times (2006: 6.6 times) by earnings before interest, taxation, depreciation and amortisation (EBITDA).

Taxation

The taxation charge on profit before intangible amortisation, non-recurring bid costs and other non-recurring items was £51.1m (2006: £45.3m) representing an effective rate of 26.1% (2006: 25.7%). Tax relief on US intangible amortisation, non-recurring bid costs and other non-recurring items reduced the tax charge to £38.1m (2006: £40.0m) representing a rate of 27.2% (2006: 25.4%).

The actual cash effect of taxation to the Group was a charge of £5.5m (2006: a credit of £3.3m). The UK cash cost of taxation was low due to increased pension payments and by favourable UK tax settlements achieved during the year. It is anticipated that the tax to be paid for

2007/08 will remain low. The Group pays a minimal amount of tax on its profits in the US due to tax losses carried forward and we believe that the level of the cash tax in the US will remain low for the medium term.

Dividends

The final dividend of 10.5p (2006: 9.55p) per ordinary share together with the interim dividend of 5.0p (2006: 4.55p) per ordinary share, gives a full year dividend of 15.5p (2006: 14.1p), an increase of 10.0%. In accordance with IFRS the final dividend has not been provided for in the 2007 balance sheet. The final dividend will be paid on 24 August 2007 to shareholders on the register of members at the close of business on 20 July 2007.

EPS

Adjusted basic EPS, before intangible asset amortisation, non-recurring bid costs, other non-recurring items and (loss)/profit on disposal of fixed assets, was 33.7p (2006: 30.9p), an increase of 9.1%. Basic EPS was 23.1p (2006: 27.4p).

EBITDA

The Group's businesses continue to generate strong operating profits which are converted into cash. EBITDA for the year was £398.9m (2006: £351.7m) up 13.4%. EBITDA from North American operations was up 4.0% in US Dollar terms. EBITDA by division is set out below.

	Year to 31 March 2007			Year to 31 March 2006		
	Revenue £m	EBITDA £m	EBITDA %	Revenue £m	EBITDA £m	EBITDA %
UK Bus	1,073.7	173.6	16.2	1,031.2	157.3	15.3
UK Rail	1,824.1	122.4	6.7	1,164.9	84.9	7.3
North America	802.9	119.2	14.8	826.3	122.0	14.8
Other	8.1	(16.3)	–	8.5	(12.5)	–
Total Group	3,708.8	398.9	10.8	3,030.9	351.7	11.6

Finance Director's review continued

Cash flow

Cash generated by operations increased to £367.9m from £300.7m last year as a result of improved profitability, better management of working capital and cash inflows in connection with the commencement of the First Capital Connect franchise. The working capital inflow of £5.5m (2006 outflow of £27.1m) was mainly due to positive working capital movements on the new rail franchises partly offset by additional cash pension contributions.

Capital expenditure and acquisitions

Capital expenditure, as set out in note 15, was £321.6m (2006 £209.1m). Capital expenditure was predominantly in North American operations of £48.1m (2006 £65.6m), UK Bus operations of £141.9m (2006 £102.4m) including £84.0m of lease restructuring, UK Rail £110.0m (2006 £16.9m) and UK Bus properties of £19.8m (2006 £15.4m).

The acquisitions made in 2006/07 were five small yellow school bus operations in North America and one Transit shuttle bus operation. The total consideration for all acquisitions made during the year was £17.9m and provisional goodwill arising on all acquisitions amounted to £9.1m.

Funding and risk management

At the year end, total bank borrowing facilities amounted to £596m of which £520m is committed. Of these committed facilities, £318.7m were utilised at 31 March 2007 leaving committed headroom of £201.3m.

The maturity profile of committed banking facilities is regularly reviewed and well in advance of their expiry such facilities are extended or replaced.

At 31 March 2007 the Group's average debt maturity was 6.4 years (2006 7.8 years).

As the Group is a net borrower, it minimises cash and bank deposits, which arise principally in the Rail companies. The Group can only withdraw cash and bank deposits from the Rail companies on a permanent basis to the lower of retained profits or the amount determined by prescribed liquidity ratios.

The Group does not enter into speculative financial transactions and uses financial instruments for certain risk management purposes only.

Interest rate risk

With regard to net interest rate risk, the Group reduces exposure by using a combination of fixed rate debt and interest rate derivatives to achieve an overall hedged position over the medium term of between 75% to 100%.

Commodity price risk

In the UK the cost of fuel increased from \$38 per barrel in 2005/06 to \$67 per barrel in 2006/07, an overall cost increase of £28.2m in UK Bus and £3.0m in UK Rail. Looking ahead, we now have 100% coverage of our UK requirements for 2007/08 (total annual usage 2.7 million barrels) at an average rate of \$67 per barrel. In North America (total annual usage 0.7 million barrels) for 2007/08 we have 27% coverage on crude oil price risk at an average price of \$55 per barrel (2006/07 average of \$53 per barrel).

Foreign currency risk

Group policies on currency risk affecting cash flow and profits are maintained to minimise exposures to the Group by using a combination of hedge positions and derivative instruments where appropriate.

With regard to balance sheet translation risk, the Group hedges part of its exposure to the impact of exchange rate movements on translation of foreign currency net assets by holding currency swaps and net borrowings in foreign currencies. At 31 March 2007 33% (2006 34%) of foreign currency net assets were hedged.

Analysis of net debt	Fixed £m	Variable £m	Total £m
Cash	–	59 1	59 1
Share placement proceeds deposited ¹	–	212 5	212 5
Rail ring fenced cash and deposits	–	139 6	139 6
Sterling bond (2013 6 875%) ²	(296 3)	–	(296 3)
Bond (2019 6 125%) ³	(221 1)	–	(221 1)
Sterling bank loans and overdrafts	–	(264 4)	(264 4)
US Dollar bank and other loans and overdrafts	(0 3)	(0 9)	(1 2)
Canadian Dollar bank and other loans and overdrafts	(2 2)	(35 1)	(37 3)
Euro bank loans and overdrafts	–	(9 4)	(9 4)
HP and finance leases	(3 7)	(78 2)	(81 9)
Loan notes	(8 7)	(7 1)	(15 8)
Interest rate swaps, net	(57 0)	57 0	–
Total	(589 3)	73 1	(516 2)

¹ Net proceeds of £216 9m less £4 4m of acquisition costs not related to the equity placement

² Excludes accrued interest

³ Stated excluding accrued interest and adjusted for currency and coupon swaps

Net debt

Net debt decreased over the year by £188 2m. This reduction is mainly explained by the share placement in February 2007, associated with the planned acquisition of Laidlaw, which raised £216 9m net of expenses.

The Group's net debt at 31 March 2007 was £516 2m and was comprised as above.

Balance sheet and net assets

Net assets increased by £275 4m over the year reflecting the net outcome of the share placing of £211 0m (net proceeds of £216 9m less £5 9m of additional anticipated costs relating to equity placing), retained earnings (after the payment of £57 1m of dividends) for the year of £34 6m, actuarial gains on defined benefit pension arrangements (net of tax) of £81 9m, an increase in the hedging reserve of £24 8m and a net movement in own shares held of £9 2m. These positive movements were partly offset by a reduction in the translation reserve of £85 5m.

Shares in issue

In 2006/07 3 3m treasury shares were used to either satisfy the exercise of Save As You Earn (SAYE) options on the maturity of the 2003 SAYE scheme or were transferred to the Employee Benefit Trust to satisfy the exercise of Executive Share Options and Deferred Bonus Shares. In February 2007 39 5m shares were placed at 559p per share, a discount of 1p on the market rate at the time. As at 31 March 2007 there were 434 0m (2006 392 0m) shares in issue, excluding treasury shares and 3 3m shares (2006 6 6m shares) were held as treasury shares at year end.

The weighted average number of shares in issue for the purpose of EPS calculations (excluding own shares held in trust for employees and treasury shares) was 397 9m (2006 392 6m).

Foreign exchange

The results of the North American businesses have been translated at an average rate of £1 \$1 89 (2006 £1 \$1 79). The period end rate was £1 \$1 96 (2006 £1 \$1 74).

Pensions

The combined rail schemes and UK Bus occupational scheme are still in deficit but these were more than offset by the surplus across the Local Government Bus Schemes. The cash payments in 2007/08 into all the schemes are unaffected by these changes.

The aggregate pensions deficit of £132m at the start of the year is now an aggregate surplus of £24m as at 31 March 2007 as measured on an IAS 19 basis.

The movement in the pension position had three main elements being the additional cash contributions being paid into the UK Bus and UK Rail schemes, the continued recovery of equities and certain measures that limit pension cost increases going forward.



Dean Finch
Finance Director

Board of Directors

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From left to right
 Martin Gilbert Moir Lockhead, Dean Finch,
 David Leeder, Sidney Bame

Martin Gilbert LLd MA LLB CA

Chairman,
 Chairman of the Nomination Committee³
 A Chartered Accountant, he is one of the founders and
 Chief Executive of Aberdeen Asset Management PLC
 He was appointed to the Board of FirstGroup plc in 1995
 He is Chairman of Chaucer Holdings PLC and a director
 of a number of investment trusts. He is a Non Executive
 Director of Primary Health Properties PLC. Age 51

Moir Lockhead OBE

Deputy Chairman and Chief Executive,
 Chairman of the Safety Committee^{3,4,5}
 Chief Executive and Deputy Chairman since the Group's
 formation in 1995. Originally a mechanical engineer he
 joined Grampian Transport in 1985 as General Manager
 and went on to lead the successful employee buy out of
 GRT Bus Group PLC. In 1996 he was awarded the OBE
 for services to the bus industry and he is a past President
 of the Confederation of Passenger Transport. Age 62

Dean Finch BSc MBA ACA

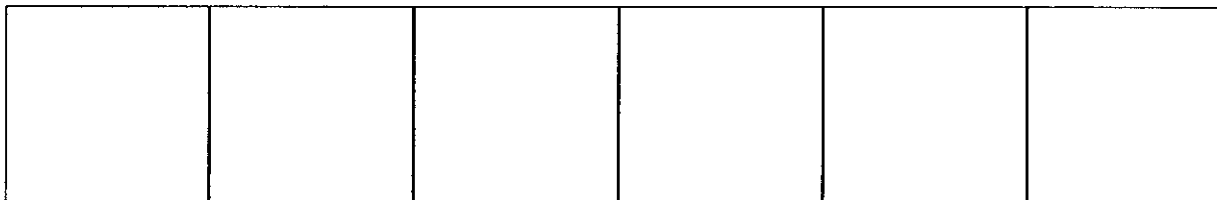
Finance Director^{4,5}
 Appointed to the Board as Commercial Director in
 February 2004 and subsequently appointed Finance
 Director later that year. He is also responsible for all of the
 Group's rail activities including refranchising. He joined
 the Company in 1999 as Commercial Director of the Rail
 Division and was subsequently appointed Managing
 Director of the Rail Division in August 2001. He qualified
 as a Chartered Accountant with KPMG where he worked
 for 12 years specialising in Corporate Transaction Support
 Services including working for the Office of Passenger
 Rail Franchising on the privatisation of train operating
 companies. Age 40

David Leeder BSc FILT

Director of International Development and Marketing^{4,5}
 Appointed to the Board in May 2004. He joined the Group
 in 2001 as Managing Director UK Bus and assumed his
 present role as Director of International Development and
 Marketing in 2005. He has held various senior posts in the
 transport industry including Chief Executive of Travel West
 Midlands and subsequently Group Marketing Director of
 National Express Group plc. He is Vice Chair of the
 Commission for Integrated Transport. A Fellow of the
 Chartered Institute of Logistics and Transport, he is also
 a past President of the Confederation of Passenger
 Transport. Age 41

Sidney Bame LLB

Commercial Director,
 Company Secretary^{4,5}
 Appointed to the Board in August 2005 as Commercial
 Director and subsequently Company Secretary. He
 joined the Group from Paul & Williamsons, solicitors
 in Aberdeen, where he was a senior partner and Head
 of Corporate acting for a number of listed and private
 companies. He had a long association with the Group in
 an advisory capacity going back to the original employee
 buy out of GRT Bus Group PLC. In his current role he has
 responsibility for a range of commercial activities across
 the Group. Age 56



From left to right
David Dunn, James Forbes John Sievwright
David Begg, Audrey Baxter Martyn Williams

David Dunn CA

Senior Independent Non Executive Director,
Chairman of the Audit Committee^{1,2,3}
Appointed to the Board as a Non Executive Director in
December 1999. He is a Chartered Accountant and is
Non Executive Chairman of Brammer plc. He is also
a Non Executive Director of Croda International plc
Age 62

James Forbes CBE MSc BSc CEng MIEE

Non Executive Director,
Chairman of the Remuneration Committee^{1,2,3}
Appointed to the Board in April 2000, he is the former
Chief Executive of Scottish and Southern Energy plc.
His career began with the South of Scotland Electricity
Board and he has since held various senior posts in the
electricity industry. Age 60

John Sievwright MA CA

Non Executive Director^{1,2,3}
Appointed to the Board in May 2002, he is a Senior Vice
President and Chief Operating Officer of Global Markets
and Investment Banking for Merrill Lynch & Co. A
Chartered Accountant, he has held various senior
management positions in banking in London, New York,
Dublin and Japan. He is a member of the North American
Board of the Michael Smurfit Business School, Dublin
Age 52

David Begg DSc BA

Non Executive Director^{1,2,3}
Appointed to the Board as Non Executive Director in
August 2005. He is Chairman of Tube Lines Limited and
Northern Way Transport Compact. He is an adviser to
Greater Manchester Passenger Transport Executive
and is publisher of Transport Times. Until 2005 he was
Chairman of the Commission for Integrated Transport and
a Non Executive Director of the Strategic Rail Authority
Age 50

Audrey Baxter DBA LLD DipAcc BA

Non Executive Director^{1,2,3}
Appointed to the Board as Non Executive Director in
August 2006. She is Chief Executive of Baxters Food
Group. She has held a number of non executive positions
and was formerly a member of the Scottish Business
Forum and the Scottish Economic Council. Age 46

Martyn Williams

Non Executive Employee Director
Appointed to the Board as Employee Director in January
2003, he is currently serving a second term as Employee
Director. He is employed as a customer services
supervisor in Swansea and has worked for the Group
for 29 years. Age 52

¹ Member of the Audit Committee
² Member of the Remuneration Committee
³ Member of the Nomination Committee
⁴ Member of the Safety Committee
⁵ Member of the Executive Committee

Corporate governance

The Company applies all of the main and supporting principles of good governance set out in section 1 of the Combined Code on Corporate Governance published by the Financial Reporting Council in July 2003 (the 'Code'). The way in which it applies those principles is set out below. Except as described in paragraph 1.1 (b) below, the Company complies with all of the provisions of section 1 of the Code.

1 The Board and its principal committees

Details of the Board, its members and its principal committees are set out below.

1.1 The Board

(a) Board structure and responsibilities

The Board currently consists of the Chairman, four Executive Directors and six Non Executive Directors. The Board meets at least eight times each year and is responsible for setting and reviewing the Company's strategy and objectives, reviewing the financial and operational performance of each of the Group's business units, agreeing and reviewing progress against the Group's annual budgets and setting and reviewing on a regular basis its longer term business plans. It also has a schedule of matters specifically reserved to it including approval of the annual and interim financial statements, financing arrangements, material capital commitments, business acquisitions and disposals, relationships with regulatory authorities and operating and accounting policies.

During the year, the Board met eight times and all members of the Board attended all meetings held whilst they were Directors except for Audrey Baxter who was absent from one of these meetings.

The Board also held a number of separate strategy meetings.

(b) Board balance and independence

The independence of the Non Executive Directors has been reviewed against the definition of independence in the Code. David Begg, David Dunn, Jim Forbes, John Sievwright and Audrey Baxter are considered to be independent within this definition. As Martyn Williams is an employee of one of the Group's subsidiaries, he cannot be considered to be independent. However, the Board feels very strongly that it is extremely beneficial for its employees to be represented on the Board in this way so that important employee related issues can be raised at the highest level and a two way communication process between the management of the Company and its employees is maintained.

Therefore, the Company complies with the Code provision that at least one half of the Board, excluding the Chairman, is made up of Non Executive Directors who are considered by the Board to be independent. The Directors are satisfied that the current Board possesses the breadth of business, financial and international experience necessary to manage effectively an organisation of the size and complexity of the Group.

(c) Roles of the Chairman and Chief Executive

The Chairman

The Chairman of the Board is Martin Gilbert. He has a written statement of responsibilities which has been approved by the Board.

The Chairman is responsible for

- leadership of the Board, ensuring its effectiveness on all aspects of its role and setting its agenda, taking into account the issues relevant to the Group and the concerns of all Board members,
- ensuring, with the Chief Executive and Company Secretary, the provision of accurate, timely and clear information to the Board,
- ensuring effective communication with shareholders and that the Board develops an understanding of the views of major investors,
- managing the Board, ensuring that sufficient time is allowed for the discussion of complex or contentious issues,
- ensuring a regular evaluation of the performance of the Board as a whole, its Committees and individual Directors,
- taking the lead in identifying and meeting the development needs of individual Directors and the Board as a whole, with a view to enhancing the overall effectiveness of the team,
- facilitating the effective contribution of Non Executive Directors and ensuring constructive relations between Executive and Non Executive Directors,
- ensuring, with the Chief Executive and Company Secretary, that new Directors receive a comprehensive induction programme to ensure their early contribution to the Board, and
- encouraging active engagement by all members of the Board.

The Board is of the opinion, reinforced by the performance evaluation review, that Martin Gilbert's significant and in depth knowledge and experience of the Group's business, combined with his external business experience enables

him to provide effective leadership of the Board and to continue to make a positive contribution to the Group's ongoing business

The Chairman's other significant business commitments, which remain unchanged from last year, are described in his biography on page 22. The Board performance evaluation process confirmed that the other Board members are satisfied that Martin Gilbert has the necessary time available to devote to the proper performance of his duties as Chairman.

The Chief Executive

The Chief Executive is Moir Lockhead. The Chief Executive also has a written statement of responsibilities which has been approved by the Board.

The Chief Executive is responsible for

- running the day to day business of the Group, within the authorities delegated to him by the Board,
- ensuring implementation across the Group of the policies and strategy set by the Board for the Group,
- day to day management of the executive and senior management team,
- leading the development of senior management within the Group with the aim of assisting the training and development of suitable individuals for future Director roles,
- ensuring that the Chairman is kept apprised in a timely manner of the issues facing the Group and of any important events and developments, and
- leading the development of the Group's future strategy including identifying and assessing opportunities for the growth of its business and reviewing the performance of its existing businesses.

(d) Senior Independent Non Executive Director

David Dunn, who chairs the Audit Committee, is the Senior Independent Non Executive Director. He is available to shareholders if they have concerns that contact through the normal channels of Chairman, Chief Executive or Finance Director has failed to resolve or for which such contact is inappropriate.

(e) Information and professional development of Board members

The Board receives detailed papers on the business to be conducted at each meeting well in advance and individual Board members have direct access to senior executives should they wish to receive additional information on any of the items for discussion. The head of each operating

division attends Board meetings on a regular basis to ensure that the Board is properly informed about the performance of and current issues facing that division. Management give presentations on current issues facing the business. A number of Board meetings each year are held on site at operating locations in the UK and US allowing the Directors to visit the Group's operations and to discuss key issues with local operational management and stakeholders.

All Directors have access to the advice and services of the Company Secretary and, if necessary, can seek independent professional advice at the Company's expense in the furtherance of their duties. The Company Secretary is responsible for advising the Board on corporate governance matters and for ensuring compliance with Board procedures.

Directors receive induction on appointment to the Board, which is tailored to their individual needs. This includes meetings with senior management and relevant external advisers. In addition, information is provided on their responsibilities and obligations under law, regulation and best practice guidelines. The induction process is supported during the year by the programme of business presentations and operational visits described above.

The Board also receives updates, as required, on changes to the law and the regulatory regimes affecting the Group.

(f) Performance evaluation

During the course of the year, the Board undertook an evaluation of its performance. The Chairman led the process, assisted by the Company Secretary. The objectives of this exercise were to ensure that the Board, its Committees and each individual Director continued to act effectively and to fulfil the duties and responsibilities expected of them, and also to identify any additional training requirements. A tailored questionnaire was developed, which each Director completed. The responses were analysed and discussed at a meeting of the Board. The Senior Independent Non Executive Director led a process of evaluation of the performance of the Chairman. No significant issues were raised in the course of the evaluation process.

(g) Re election of Directors

As required by the Company's Articles of Association, Directors offer themselves for re election at least once every three years. Any Director appointed during the year is required to seek re appointment by shareholders at the next Annual General Meeting. The biographical details of all the Directors, including those seeking re election at the 2007 Annual General Meeting, are set out on pages 22 to 23.

Corporate governance continued

(h) Appointment of Non Executive Directors

Non Executive Directors are appointed by the Board for an initial term of three years, subject to re-appointment by shareholders. They have letters of appointment, which are available on request for inspection.

(i) Directors' and Officers' liability insurance

The Company maintained Directors' and Officers' liability insurance cover throughout the year as permitted by section 310 of the Companies Act 1985. The cover was renewed on 1 April 2007.

2 Committees of the Board

In addition to the Audit, Remuneration and Nomination Committees, the terms of reference for which are published on the Company's website and details of which are set out below, the Board has also delegated certain matters to Committees. The principal such Committees are

2.1 Executive Safety Committee ('ESC')

The ESC is chaired by the Chief Executive and meets on a monthly basis. It comprises the Executive Directors, other senior managers and safety officers. The ESC reviews the Group's safety performance and practices, develops safety policies and procedures and follows up on outstanding issues. During the year, a number of meetings were attended by independent safety experts and senior representatives of relevant industry bodies, including the Health & Safety Executive.

2.2 Executive Management Board ('EMB')

The EMB, which comprises the Executive Directors and certain senior business managers, is chaired by the Chief Executive. It acts as a general operating management committee and meets on a monthly basis to review outstanding issues and to consider the Group's operational and financial performance.

2.3 Executive Committee

The Executive Committee comprises the Executive Directors and meets on an ad hoc basis to consider matters which arise in the ordinary course of the Group's operations. It is chaired by the Chief Executive and has specific delegated powers within prescribed limits to deal with matters arising in the ordinary course of business which need to be considered before the next scheduled Board meeting.

2.4 Nomination Committee and appointments to the Board

The Nomination Committee is chaired by the Chairman and includes David Begg, David Dunn, Jim Forbes, John Sievwright, Audrey Baxter and Moir Lockhead. Martyn Williams attends meetings of the Committee at the invitation of the Chairman of the Committee to represent

the Group's employees. The Committee meets as required to discuss appointments to the Board of both Executive and Non Executive Directors. Its recommendations are then put to the full Board for consideration. External search consultants are used to assist the process, where appropriate.

During the year the Committee did not hold any meetings.

The Employee Director is elected by the Employee Directors' forum, which comprises the Employee Directors and representatives of each of the Company's UK subsidiaries, and serves a maximum of two three year terms.

The Company's policy is to permit Executive Directors to accept a limited number of outside non executive directorships, recognising that this is an effective way to broaden their knowledge and expertise. However, no such appointment can be taken up without prior Board approval. The Company's policy on fees relating to such outside directorships is set out on page 33 of the Directors' Remuneration Report.

2.5 Remuneration Committee

The Remuneration Committee, under the chairmanship of Jim Forbes, met four times during the year and all members of the Committee attended all of its meetings held whilst they were Directors except for John Sievwright and Audrey Baxter who were each absent from one of these meetings. Details of the membership of the Remuneration Committee are set out in the Directors' Remuneration Report on pages 31 to 37, together with a statement of the Group's remuneration strategy and policy. Full details of Directors' remuneration appear on page 34.

2.6 Audit Committee

The Audit Committee is chaired by David Dunn and includes David Begg, Jim Forbes, John Sievwright and Audrey Baxter. It met three times during the year and all members attended each of those meetings whilst they were Directors except for Audrey Baxter who was absent from two of these meetings and John Sievwright who was absent from one of these meetings. The Group Director of Internal Audit attended each of those meetings and the Company's external auditors also attended two of those meetings. Executive Directors and other senior managers attended where requested and as appropriate.

The Board considers that each member of the Committee has sufficient and recent financial experience to enable the Committee to discharge its functions effectively.

Under its remit, the Committee keeps under review the effectiveness of the Company's financial reporting and

internal control policies and procedures for the identification, assessment and reporting of risk. It also keeps under review the nature, scope and results of the audits conducted by the internal audit department and the external auditors, the consistency of accounting policies and reporting across the Group and it reviews the half year and full year financial statements before they are presented to the Board.

The Committee considers the Group's compliance with the Code and its related guidance and oversees the objectivity and effectiveness of internal audit. The work of the internal audit department is focused on areas of priority as identified by risk analysis and in accordance with an annual audit plan approved by the Committee and the Board. Reports are sent to senior executives of the Group and subsidiary units and there is a follow up process to ensure that actions to resolve identified control weaknesses are implemented. The Group Director of Internal Audit has the right of direct access to the Chairman of the Audit Committee.

The Committee is responsible for making recommendations to the Board in respect of the appointment or re-appointment of the Group's external auditors and, subject to the approval of shareholders, recommends to the Board the audit fee to be paid to the external auditors. The Committee is also charged with monitoring the independence of the external auditors and the objectivity and effectiveness of the external audit process. The objectivity and independence of the external auditors is considered on a regular basis, with particular regard to the level of non-audit fees. The majority of non-audit work is put out to tender, with the exception of due diligence work on acquisitions or potential acquisitions in both the UK and overseas, where the current auditors' knowledge of the Company's business processes and controls means that they are best placed to undertake this work cost effectively on the Company's behalf. The majority of the non-audit work undertaken by the auditors during the year was associated with acquisition related due diligence. Details of the audit and non-audit fees, including a breakdown of the non-audit fee, are set out in note 6 to the financial statements. The external auditors have direct access to the Committee to raise any matters that may concern them.

The Committee reviews with management a detailed analysis of the Group's financial information prior to completion and announcement of the half year and full year results and receives a report from the external auditors on the audit process. If necessary, the external auditors also meet separately with the Committee and/or the Chairman, Chief Executive and Finance Director. The Annual Report and Financial Statements and interim results go through a detailed verification and due diligence process involving external advisers.

The Committee may request the Executive Directors and any other officers of the Group to attend its meetings but none has the right of attendance. Committee meetings may be requested by the external or internal auditors if they consider it necessary.

The business considered and discussed by the Committee during the year included the reports of the external auditors on the half year and full year results, the 2007/08 Group Internal Audit Plan and budget, papers concerning any regular and special audits and an executive summary of each internal audit report, risk analysis assessments and a review of the implications of changes in accounting standards and the application and implementation of International Financial Reporting Standards.

3 Financial reporting

The Directors have a commitment to best practice in the Group's external financial reporting in order to present a balanced and comprehensible assessment of the Group's financial position and prospects to its shareholders, employees, customers, suppliers and other third parties. This commitment encompasses all published information including but not limited to the year end and interim financial statements, regulatory news announcements and other public information. A statement of the Directors' responsibility for preparing the financial statements may be found on page 41.

4 Internal controls

The Board has established procedures to meet the requirements of the Code and its related guidance on internal controls. These procedures, which are subject to regular review, provide an ongoing process for identifying, evaluating and managing any significant risks faced by the Group.

4.1 Responsibility

The Board has overall responsibility for the system of internal control and assessing risk. The responsibility for establishing detailed control and risk management procedures within each subsidiary lies with the Executive Directors and subsidiary unit managing directors. A sound system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

4.2 Control environment

The Board is committed to business integrity, high ethical and moral values and professionalism in all its activities, principles with which all managers and employees are required to comply. The Group has a Code of Business Ethics, which is part of the Group's Corporate Social

Corporate governance continued

Responsibility Policy and applies to all of its subsidiary undertakings, a copy of which is available on the Company's website

The Group has a defined divisional organisational structure with lines of authority and delegated responsibility which allows the Board to plan, execute, control and monitor the business in a manner consistent with the Group's objectives. The day to day business management is delegated to the Executive Directors and subsidiary unit managing directors under the overall direction of the Chief Executive. As noted above, the Board reserves to itself a number of specific items, which ensures that it retains control over key business decisions and significant transactions in terms of size, type or risk. A number of the Group's key functions, including treasury, taxation, insurance, corporate finance, legal, corporate communications and procurement are dealt with centrally. Each of these functions is monitored by an Executive Director.

4.3 Monitoring

The Group adopts a financial reporting and information system which complies with generally accepted accounting practice. The Group Finance Manual, circulated by the Group Finance function to all subsidiaries, details the Group accounting policies and procedures with which subsidiaries must comply. These are also available on the Group's intranet. Budgets are prepared by subsidiary company management and are subject to review by both Group management and the Executive Directors. Monthly forecasts are completed during the year and compared against actions required. Each subsidiary unit prepares a monthly report of operating performance, with a commentary on variances against budget, forecasts and prior year. Similar reports are prepared at a Group level. Key performance indicators, both financial and operational, are monitored on a weekly basis. In addition, business units participate in strategic reviews which include consideration of long term financial projections and the evaluation of business alternatives.

A process of annual self assessment and hierarchical reporting provides for a documented and auditable trail of accountability from the subsidiary units to senior management to the Executive Directors.

A Control Assurance Questionnaire is completed by each operating entity on an annual basis confirming that

management have reviewed the effectiveness of the systems of internal controls during the year. Both from this process and as a result of planned reviews of operating units by Internal Audit staff, invariably a number of minor control weaknesses are identified. These weaknesses are discussed with management and actions are agreed to address any weaknesses identified. Follow up visits to the operating entity then ensure that the additional controls have been put in place and are working effectively. No such weaknesses have resulted in any material losses, contingencies or uncertainties that would require disclosure in the Group's Annual Report.

4.4 Risks and uncertainties

There are a number of potential risks and uncertainties that could have an impact on the Group's long term performance.

Competitive pressures

Our businesses compete in the areas of pricing and service and face competition from a number of sources.

In UK Bus, our main competitor is the car as the cost of driving a car is generally perceived as less expensive than bus travel, especially if there is more than one person in the car. In order to make bus travel a viable alternative to the car we seek to work with local authorities to introduce bus priority measures and effect infrastructure changes that promote bus patronage.

The main competitor to our UK Rail businesses is again the car and to a lesser extent, long distance coach operators and budget airlines. To mitigate the risk from these pressures, the Group works with local and national bodies to ensure that services are provided that meet or exceed the requirements of our stakeholders.

In North America our businesses cover a wide geographic spread competing with several large companies and a substantial number of smaller, locally owned or government owned operators. Our competitors in the yellow school bus business can also include school districts since most school districts operate their own yellow school buses. Similarly, while the majority of our Transit and Services business streams are operated by private entities, including several large companies, our Transit and Services businesses also compete with many municipalities. In North America our businesses compete on service, quality and price.

Legislation and regulation

Our businesses are subject to numerous laws regulating safety procedures, equipment specifications, employment requirements, environmental procedures, insurance coverage and other operating issues and considerations. These laws and regulations are constantly subject to change. The costs associated with complying with the adoption of new legislation, regulations or other laws could adversely impact the results of our operations.

To mitigate the risk of legislative or regulatory changes the Group regularly lobbies both governmental and transport bodies.

Labour costs

Labour costs represent the largest component of the Group's operating costs. Labour shortages, or low unemployment rates, could hinder the Group's ability to recruit and retain qualified employees leading to a higher than expected increase in the cost of recruitment, training and other staff costs.

To mitigate this risk, the Group seeks to structure our recruitment and retention strategies to attract and retain the right people.

Fuel costs

Fuel costs constitute a significant proportion of our cost base. Fuel prices and supplies are influenced significantly by international, political and economic circumstances as well as natural disasters. If a fuel supply shortage were to arise from a national strike or world supply difficulties, a disruption to oil imports or refining capacity due to a natural disaster or otherwise, higher fuel prices could impact on the Group's operating results.

To mitigate the risk of rising fuel costs the Group regularly enters into forward contracts to buy fuel at fixed prices. In addition the Group seeks to limit the impact of unexpected fuel price increases through efficiency and pricing measures.

Insurance costs

Insurance reserves are made for estimates of losses that we will ultimately incur on accidents or incidents that have been reported but not paid and accidents or incidents that have been incurred but not reported. These reserves are based on actuarial valuations that are regularly prepared by independent actuaries. The actuarial valuations consider a number of factors, including historical claim payment patterns and changes in case reserves, the assumed rate of increase in medical treatment costs and property damage repairs and ultimate compensation. Historical experience and recent trends are the most significant factors in the determination of these reserves.

Given the magnitude of the claims involved and the length of time until the ultimate cost is known the use of any estimation technique is inherently uncertain.

The Group seeks to mitigate the risk of rising insurance costs by promoting a culture of safety in everything that we do, through the ESC that is headed up by the Chief Executive.

Terrorism

Terrorist acts and public concerns about potential attacks could adversely affect demand for our services. The Group has a Head of Security who is responsible for improved security awareness, implementation of good practice and development of a passenger and employee security structure.

Economy

The level of economic activity affects the number of bus and train journeys taken by passengers in the UK. Any changes in economic activity may impact on passenger numbers and hence our UK operations. The potential impact of this is reduced on certain rail franchises due to the existence of revenue share arrangements. In most UK Bus operating companies, the Group has the ability to modify services by giving 45 days' notice of such modifications.

Risk Assessment

The Board has established an ongoing process for identifying, evaluating and managing the significant risks faced by the Group. As an integral part of planning and review, management from each business area and major projects identify their risks, the probability of the risks occurring, the impact on the business should the risks occur and the actions taken to manage the risks. The risks are assessed on a regular basis and could be associated with a variety of internal and external sources including regulatory requirements, disruption to information systems, industrial relations issues, control breakdowns and social, ethical and environmental issues.

4.5 Whistleblowing

The Group has established procedures whereby employees of the Group may, in confidence, raise concerns relating to matters of potential fraud or other improprieties. These procedures also cover other issues affecting employees including health and safety issues. The confidential hotline covers all businesses across the Group and each country in which it operates. The Committee is confident that these 'whistleblowing' arrangements are satisfactory and will enable the proportionate and independent investigation of such matters and appropriate follow up action to be taken.

Corporate governance continued

4.6 Review of effectiveness of financial controls

The Directors confirm that they have reviewed the effectiveness of the system of internal control for the year under review and to the date of approval of the Annual Report and Financial Statements through the monitoring process described above. In addition, the Directors confirm that they have conducted a specific annual review of the effectiveness of the Group's internal audit function.

4.7 Treasury operations

The Board has set a policy for the management of those risks and this is set out in more detail in note 25 to the financial statements. A Group Treasury Policy has been formulated and adopted to ensure compliance with best practice and to control and monitor effectively the risks attendant upon treasury and banking operations.

4.8 Auditors

Deloitte & Touche LLP have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

5 Relations with shareholders

The Group recognises the importance of regular communication with all of its shareholders. The full Annual Report and Financial Statements are made available to all shareholders and an Interim Report is published and sent to shareholders at the half year. These reports are intended to provide shareholders and other interested parties with a clear and balanced understanding of the Group's operational performance, its financial results and prospects.

All investors are kept informed of key business activities, decisions, appointments etc. via regulatory news and press releases and the Group's website. There is also regular dialogue with institutional shareholders throughout the year and general presentations are made by the Chief Executive and Finance Director following the announcement of the full and half year results. Other Directors, including Non-Executive Directors, attend meetings with major shareholders if requested.

Regular reports on investor relations activity and feedback from investors are submitted to the Board and senior management. The Non-Executive Directors have also had informal contact with major shareholders regarding the Group during the year and they expect that informal dialogue to continue.

6 Annual General Meeting

All shareholders have the opportunity to put questions to the Directors at the Company's Annual General Meeting, at which a report is made on the highlights of the key business developments during the year under review. The Chairmen of each of the Nomination, Remuneration and Audit Committees attend the Annual General Meeting to answer specific questions from shareholders. All Directors who then held office were present at the 2006 Annual General Meeting.

Notice of the Annual General Meeting is circulated to all shareholders at least 20 working days prior to the meeting. Separate resolutions are proposed at the Annual General Meeting on each substantially separate issue. Proxy votes are counted on all resolutions and, where votes are taken on a show of hands, the proxy results are subsequently announced to the meeting.

Directors' remuneration report

This report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002 (the 'Regulations'). It also meets the requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the main supporting principles of the Combined Code on Corporate Governance published by the Financial Reporting Council in July 2003 (the 'Code') relating to Directors' remuneration. The Company complies with all of the provisions of the Code. A resolution to approve this report will be proposed at the Company's Annual General Meeting to be held on 12 July 2007.

The Regulations require the Company's auditors to report to the Company's shareholders on the 'auditable' part of the Directors' Remuneration Report and to state whether in their opinion that part of the report has been properly prepared in accordance with the Companies Act 1985 (as amended by the Regulations). This report has therefore been divided into separate sections for audited and unaudited information.

Unaudited information

Remuneration Committee

The Remuneration Committee is chaired by Jim Forbes. The other current members of the Committee are David Begg, David Dunn, John Sievwright and Audrey Baxter. The Board considers each of the members of the Committee to be independent in accordance with the Code. None of the members of the Committee has any personal financial interest (other than as a shareholder) in the matters to be decided, conflict of interest arising from cross directorships or any involvement in the day to day running of the business.

The remit of the Committee was adopted in March 2004 in the light of the recent revisions to the Code and its terms of reference are available on request and are also published on the Company's website. These terms of reference will be kept under review to take into account any changes to the Code and corporate governance practice. The principal purpose of the Committee is to consider matters related to the remuneration of the Executive Directors and senior management below Board level.

The Committee met four times during the year and all members attended each meeting held whilst they were Directors except for John Sievwright and Audrey Baxter who were each absent from one of these meetings.

In determining the Executive Directors' remuneration for the year, the Committee considered publicly available information, including the remuneration packages of those

holding equivalent posts at the Company's peers within the transport industry and other companies of comparable market capitalisation. The Committee also consults with the Chief Executive although no Director participates in discussions concerning his own remuneration.

Remuneration policy

Aim

The aim of the Committee is to design remuneration packages for the Company's Executives which attract, retain and motivate the high calibre individuals necessary to maintain the Group's position as a leader in the public transportation industry. In implementing its policy, the Committee has given full consideration to the Principles of Good Governance of the Code with regard to Directors' remuneration.

Structure of remuneration packages

There are currently four main elements to the executive remuneration package:

- basic salary and benefits in kind,
- annual cash and deferred share bonus (both paid under the Executive Annual Bonus Plan),
- share options, and
- pension provision.

The Committee considers the remuneration package as a whole, balancing each of the individual elements to ensure that overall, the remuneration received by each Executive Director is competitive but not excessive, contains an appropriate balance between fixed and variable (performance related) remuneration and that each Executive Director has sufficient long term incentive to ensure that his interests are aligned with those of shareholders. A high proportion of each Director's potential remuneration is performance related.

The remuneration of the Executive Directors is made up of the following components:

Basic salary and benefits in kind

The basic salary and benefits in kind for each Executive Director are determined by the Committee for each financial year and when an individual changes position or responsibility. In determining appropriate levels, the Committee considers the Group as a whole and also the packages received by similar individuals at the Company's peers in the public transport sector and other companies of comparable market capitalisation. Details of the salaries and benefits in kind received by each of the Executive Directors in the year are shown on page 34.

Directors' remuneration report continued

Executive Annual Bonus Plan

The Group operates a discretionary performance related bonus plan for its senior management under which payment of bonuses is linked to achievement of budgeted annual Group operating profit targets and personal objectives (including safety targets). Where an Executive Director is also directly responsible for one or more operating division(s), payment of a proportion of the bonus is also linked to the profitability of those divisions. The Committee considers and agrees the Group and divisional objectives for all Executive Directors and the personal objectives for the Chief Executive. The Chief Executive, in consultation with the Committee, agrees the personal objectives for the other Executive Directors.

Each year, the Board sets challenging budget targets for the Group as a whole and for each business unit within the Group. The Committee's policy continues to be that bonuses will be payable for Group performance against budget of between 90% and 110% although the level of bonus payable is heavily skewed towards performance in excess of 100% of budget. 70% of any bonus payable is dependent upon Group performance and the balance upon the achievement of safety objectives (up to 20%) and personal objectives (up to 10%).

Bonus payments comprise a mixture of cash and deferred share awards. Share awards for the year under review were deferred for five years and will lapse if the relevant individual leaves the Group during the deferral period for any reason other than redundancy, retirement or ill health. The Committee considers it is appropriate for a proportion of the annual bonus to be taken in the form of deferred shares as this acts as a retention mechanism and also aligns that Executives' longer term interests with those of the Company's shareholders.

As the award of any bonus is already dependent on the achievement of stringent targets, the Committee considers that it is not appropriate to attach further performance conditions on vesting of the deferred share element of any bonus other than that the relevant Executive remains employed by the Group and has not tendered his resignation at the end of the deferral period.

The level of bonus payable to Executive Directors in the year to 31 March 2007 was 110% of basic salary in the case of the Chief Executive and 100% of basic salary in the case of the other Executive Directors. Each of the Chief Executive and the other Executive Directors would receive half of their bonus in cash and the remaining half in the form of deferred shares.

For all Executive Directors, up to 50% of any bonus award will be payable in shares. The deferral period for these shares is five years in order to provide long term lock in and to further align the Directors' interests with those of shareholders. The same deferred period also applies to senior management within the Group. The bonus arrangements will be kept under review by the Committee for future years to ensure that they remain appropriate.

Share Option Schemes

Executive Share Option Scheme

The Company operated an Executive Share Option Scheme ('ESOS') up to June 2004 for Executive Directors and other senior management.

The performance period in respect of awards granted under the ESOS in 2004 expired on 31 March 2007. The earnings per share ('EPS') performance target was exceeded. Additionally, the total shareholder return ('TSR') condition was fulfilled as the Company ranked first relative to the original TSR comparator group which comprised Associated British Ports Holdings PLC, Arva plc, BAA plc, The Go Ahead Group plc, The Mersey Docks & Harbour Company, TBI plc, National Express Group plc, Exel plc, Tibbett & Britten (now part of Exel plc), Avis Europe plc, Stagecoach Group plc, British Airways plc, Peninsular & Oriental Steam Navigation Company and easyJet plc.

Accordingly the awards granted under the ESOS in 2004 will vest on 10 June 2007.

Save As You Earn ('SAYE') Scheme

The Company operated an SAYE Scheme for eligible employees during the year under review under which options may be granted on an annual basis at a discount of up to 20% of market value. As with the previous scheme the Executive Directors are eligible to participate in the current scheme.

Buy As You Earn ('BAYE') Scheme

The Company operates a Share Incentive Plan under the title 'Buy As You Earn'. The scheme, which is open to all UK employees of the Group enables employees (including the Executive Directors) to purchase partnership shares from their gross income (before income tax and National Insurance deductions). The Company provides two matching shares for every three partnership shares, subject to a maximum Company contribution of shares to the value of £20 a month. The shares are held in trust for up to five years, in which case, no income tax or National Insurance will be payable. The matching shares will be forfeited if the corresponding partnership shares are removed from trust within three years from award.

Special Share Award

On 22 August 2006 the Company declared a special bonus of deferred nil cost options over 200,000 ordinary shares in the capital of the Company in favour of Dean Finch.

These options will vest on 31 March 2011 but only to the extent that certain performance criteria are satisfied based on targets relating to the profitability of First Greater Western Limited and the EPS growth of the Company over a five year performance period which commenced on 1 April 2006.

Retirement benefits

Executive Directors are members of a number of defined benefit Group pension schemes. Their dependants are eligible for dependants' pensions and the payment of a lump sum in the event of death in service. Further details are set out on page 35.

Service contracts

It is the Company's policy to restrict notice periods for Executive Directors to a maximum of 12 months. In line with this policy, all of the Executive Directors have service contracts with an undefined term but which provide for a notice period of 12 months.

The contracts contain a provision, exercisable at the discretion of the Company, to pay an amount in lieu

of notice on early termination of the contract. Such payments are limited to basic salary plus certain benefits but would not include entitlement to bonus or share options. There are no contractual provisions governing payment of compensation on early termination of the contracts. If it becomes necessary to consider early termination of a service contract, the Company will have regard to all the circumstances of the case, including mitigation, when determining any compensation to be paid. Details of the Executive Directors' contracts are set out below.

	Date of service contract
Moir Lockhead	5 March 2001
Dean Finch	26 February 2004
David Leeder	3 September 2001
Sidney Barrie	31 August 2005

Where Board approval is given for an Executive Director to accept an outside non executive directorship, unless the appointment is in connection with Group business, the individual Director is entitled to retain any fees received.

Non Executive Directors

All Non Executive Directors have a letter of appointment and their fees are determined by the Board based on surveys of fees paid to Non Executive Directors of comparable companies. These letters of appointment are available for inspection at the Company's registered office during normal business hours and will be made available at the Annual General Meeting.

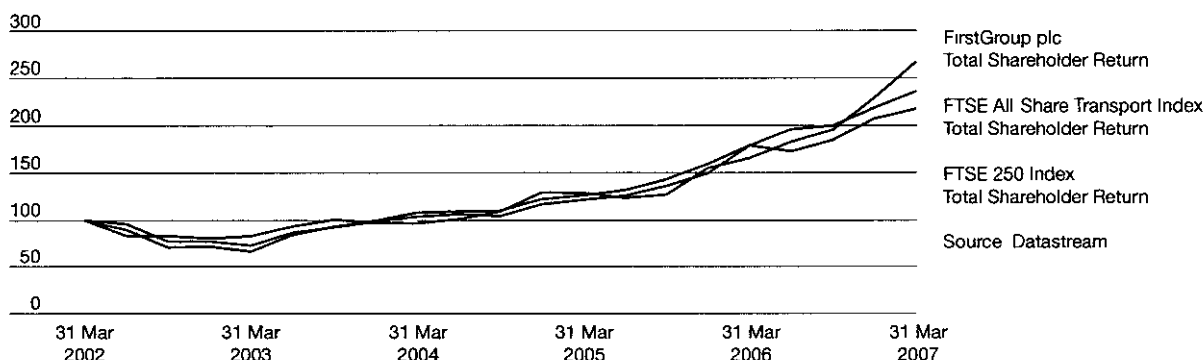
Non Executive Directors cannot participate in any of the Company's share option schemes and, other than the Group Employee Director, are not eligible to join a Company pension scheme. Each of the Non Executive Directors (other than David Dunn, who, with effect from January 2006 elected to receive all of his fees in cash and Audrey Baxter, who receives all of her fees in the form of shares in the Company) has elected to receive 40% of his fees in the form of shares in the Company (in the case of Martyn Williams, with effect from January 2006) in order to ensure that their interests are more closely aligned to those of the Company's shareholders. The shares are purchased on a monthly basis in the market. The appointment of each of the Non Executive Directors is subject to early termination without compensation if he/she is not re-appointed at a meeting of shareholders where he/she is up for re-election.

Directors' remuneration report continued

Total shareholder return

The following graph shows, for the last five financial years of the Company, the total shareholder return on a holding of shares in the Company as against that of a hypothetical holding of shares made up of shares of the same kinds and number as those by reference to which the FTSE 250 Index and the FTSE All Share Transport Index are calculated

Total shareholder return index



This graph is included to meet the relevant legislative requirements and is not directly relevant to the performance criteria used for the Company's Executive Share Option Scheme. Nonetheless, the indices used were selected as the Company believes that they are the most appropriate and representative indices against which to measure the Company's performance for this purpose.

Audited information

Directors' remuneration

Details of the Directors' remuneration for the year ended 31 March 2007 are set out on the following pages

Emoluments and compensation

The total salaries, fees and benefits paid to, or receivable by, each person who served as a Director of the Company at any time during the year for the period of such directorship are shown in the table below. These include any and all payments for services as a Director of the Company, its subsidiaries or otherwise in connection with the management of the Group.

	Salary 2007 £000	Cash bonus 2007 £000	Benefits in kind 2007 ¹ £000	Fees 2007 £000	Total 2007 £000	Total 2006 £000
Executive Directors						
Moir Lockhead	461	254	30	–	745	723
Dean Finch	308	165	20	–	493	468
David Leeder	282	141	19	–	442	411
Sidney Barne	231	115	11	–	357	233
Non Executive Directors						
Martin Gilbert	–	–	–	132	132	114
David Begg	–	–	–	38	38	25
David Dunn	–	–	–	43	43	39
Jim Forbes	–	–	–	43	43	39
John Sievwright	–	–	–	38	38	36
Audrey Baxter ²	–	–	–	25	25	–
Martyn Williams	–	–	–	28	28	20
Total	1,282	675	80	347	2,384	2,108

¹ The Directors received the following non cash benefits in the year: Moir Lockhead: £24,000 company car, £5,000 private fuel and £1,000 medical insurance for himself and spouse; Dean Finch: £14,000 company car, £5,000 private fuel and £1,000 medical insurance for himself and family; David Leeder: £13,000 company car, £5,000 private fuel and £1,000 medical insurance for himself; Sidney Barne: £10,000 car allowance, £1,000 medical insurance for himself and spouse.

² Appointed 1 August 2006

Retirement benefits

Details of the retirement benefits for each of the Directors are set out in the table below

	Moir Lockhead	Dean Finch	David Leeder	Sidney Barne
	1	2	2	2
Scheme				
Normal retirement age	65 ³	60	60	60
Directors' contributions during the year (£)	29,088	12,489	13,575	16,290
Decrease/increase in accrued pensions during the year (net of inflation) (£ pa)	(3,576)	2,805	2,369	2,557
Increase in accrued pension during the year (£ pa)	6,739	3,675	3,053	2,765
Accrued pension as at 31 March 2007 (£ pa)	225,212	19,005	14,933	4,525
Transfer value of increase in accrued pension (net of inflation) during the year (£)	(67,048)	21,057	17,901	41,476
Transfer value of accrued pension at 31 March 2006 (£)	4,066,745	106,475	83,087	27,114
Transfer value of accrued pension at 31 March 2007 (£)	4,192,178	142,698	112,839	73,377
Increase in transfer value over the year, net of Director's contributions (£ pa)	96,344	23,734	16,177	29,973

¹ Aberdeen City Council No 2 Pension Fund

² FirstGroup Flexible Benefits Scheme

³ Normal retirement age under relevant scheme is 65 but benefits can be taken without reduction at 60 so transfer values for the purpose of this table have been calculated assuming immediate retirement
Guaranteed Minimum Pensions have been ignored for the purpose of the transfer value calculations

The Group does not have one pension scheme but instead operates a number of different schemes. All of the schemes in which the Executive Directors participate are defined benefit schemes and are not limited in membership to Executive Directors.

Directors' remuneration report continued

Directors' share options

The outstanding share options under the ESOS, deferred share bonus and SAYE Scheme granted to each of the serving Directors are set out in the table below. No price was paid for the award of any option. There have been no changes to the terms and conditions of any option awarded to Directors.

			At beginning of year or date of appointment (number of shares)	Granted during the year (number of shares)	Exercised during the year (number of shares)	Lapsed/ waived during the year (number of shares)	At end of year (number of shares)	Exercise price (pence)	Date from which exercisable	Expiry date
Directors	Scheme									
Moir Lockhead	ESOS	2001	130,985	–	–	–	130,985	346.5	15.8.04	15.8.11
		2002	173,784	–	–	–	173,784	269	21.6.05	21.6.12
		2003	166,958	–	–	–	166,958	287	18.11.06	18.11.13
		2004	193,277	–	–	–	193,277	275.08	10.6.07	10.6.14
	Deferred share bonus ¹	2003	28,559 ²	–	28,559	–	–	nil	1.4.06	1.4.07
		2004	34,062	–	–	–	34,062	nil	1.4.07	1.4.08
		2005	36,787	–	–	–	36,787	nil	1.4.08	1.4.09
		2006	–	61,567	–	–	61,567	nil	1.4.11	1.4.12
Sidney Barrie	SAYE	2005/06	678	–	–	–	678	325	1.5.09	31.10.09
	Deferred share bonus ¹	2006	–	18,657	–	–	18,657	nil	1.4.11	1.4.12
Dean Finch	ESOS	2001	18,470 ²	–	18,470	–	–	346.5	15.8.04	15.8.11
		2002	24,535 ²	–	24,535	–	–	269	21.6.05	21.6.12
		2003	58,930 ³	–	58,930	–	–	287	18.11.06	18.11.13
		2004	90,883	–	–	–	90,883	275.08	10.6.07	10.6.14
	Deferred share bonus ¹	2003	13,720 ⁴	–	13,720	–	–	nil	1.4.06	1.4.07
		2004	27,029	–	–	–	27,029	nil	1.4.07	1.4.08
		2005	38,344	–	–	–	38,344	nil	1.4.08	1.4.09
		2006	–	37,313	–	–	37,313	nil	1.4.11	1.4.12
	Special share award	2006	–	200,000	–	–	200,000	nil	31.3.11	30.3.12
	David Leeder	ESOS	2002	26,914	–	–	–	26,914	269	21.6.05
2003			64,643	–	–	–	64,643	287	18.11.06	18.11.13
2004			90,883	–	–	–	90,883	275.08	10.6.07	10.6.14
Deferred share bonus ¹		2003	7,163 ⁴	–	7,163	–	–	nil	1.4.06	1.4.07
		2004	19,941	–	–	–	19,941	nil	1.4.07	1.4.08
		2005	29,311	–	–	–	29,311	nil	1.4.08	1.4.09
		2006	–	31,872	–	–	31,872	nil	1.4.11	1.4.12
SAYE		2005/06	678	–	–	–	678	325	1.5.09	31.10.09
Martyn Williams	SAYE	2003/04	636	–	–	–	636	232	1.2.07	31.8.07
		2004/05	567	–	–	–	567	267	1.2.08	31.8.08
		2005/06	345	–	–	–	345	325	1.5.09	31.10.09
		2006/07	–	340	–	–	340	444	1.2.10	31.8.10

¹ The figures shown represent the number of nil cost options which were granted under the deferred share element of the Executive Annual Bonus Plan in respect of the 2002/03, 2003/04, 2004/05 and 2005/06 financial years. The cash values of the 2006/07 award are Moir Lockhead: £254,000, Sidney Barne: £115,000, Dean Finch: £165,000 and David Leeder: £141,000. These awards will take the form of nil cost options over shares which will, subject to satisfaction of the requirements of the plan, vest on 1 April 2012. The number of shares under option will depend on the market price of shares at the close of business on 16 May 2007.

² Exercised on 9 August 2006. The closing price on the date of exercise was 449.25p.

³ Exercised on 20 November 2006. The closing price on the date of exercise was 554.5p.

⁴ Exercised on 7 June 2006. The closing price on the date of exercise was 401.50p.

Market price of FirstGroup plc shares

The market price of FirstGroup plc shares at 31 March 2007 was 665p and the range during the year was 381p to 668p

This report was approved by the Board of Directors, on the recommendation of the Remuneration Committee, on 10 May 2007 and signed on its behalf by

A handwritten signature in black ink, appearing to read 'James Forbes', written in a cursive style.

James Forbes
Chairman of the Remuneration Committee
15 May 2007

Directors' report

The Directors have pleasure in submitting their Annual Report and Financial Statements for the year ended 31 March 2007

Principal activities

The principal activity of the Group is the provision of passenger transport services

Review of the business

Reviews of the business and principal events and likely future developments are given in the Chairman's statement, Chief Executive's review and in the Finance Director's review set out on pages 2 to 21. Our review of the principal risks and uncertainties of the business is set out on pages 28 to 29

Results and dividends

The results for the year are set out in the consolidated income statement on page 42. The Directors recommend payment of a final dividend of £45.6m (10.5p per share), which, with the interim dividend of £19.6m (5.0p per share) paid on 7 February 2007, gives a total dividend of £65.2m (15.5p per share) for the year. The proposed final dividend, if approved, will be paid on 24 August 2007 to shareholders on the register at the close of business on 20 July 2007.

Share capital

Details of changes in share capital, including purchases by the Company of its own shares, are set out in note 28 to the consolidated financial statements. Authority for the Company to make market purchases of up to 39,875,000 of its own shares was renewed at the 2006 Annual General Meeting. This authority remains in place until the 2007 Annual General Meeting, when it is intended to seek a further renewal. Further to the authority given at the 2006 Annual General Meeting, the Company did not purchase any of its own shares.

Directors

The Directors of the Company who served during the year were Martin Gilbert, Moir Lockhead, Sidney Barrie, Audrey Baxter (appointed 1 August 2006), David Begg, David Dunn, Dean Finch, Jim Forbes, David Leeder, John Sievwright and Martyn Williams. Biographical details of all the serving Directors are set out on pages 22 to 23.

In accordance with the Company's Articles of Association, Moir Lockhead, John Sievwright, Dean Finch and David Leeder will retire by rotation at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election. Audrey Baxter, who was

appointed since the last Annual General Meeting will retire at the forthcoming Annual General Meeting and, being eligible, offer herself for election. Details of the fees and remuneration of the Directors and their service contracts or terms of appointment are set out in the Directors' Remuneration Report on pages 31 to 37.

Directors' interests

The Directors who held office at the end of the year had the following interests in the ordinary shares of the Company:

	Ordinary 5p shares			
	At beginning of year or subsequent appointment		At end of year	
	Beneficial	Non beneficial	Beneficial	Non beneficial
Sidney Barrie	20,000	–	20,000	–
Audrey Baxter	–	–	3,619	–
David Begg	2,645	–	5,603	–
David Dunn	24,837	–	24,837	–
Dean Finch	8,334	–	16,411	–
Jim Forbes	18,113	–	21,467	–
Martin Gilbert	74,959	–	85,328	–
David Leeder	10,636	–	15,260	–
Moir Lockhead	1,157,604	470,690	1,174,412	470,690
John Sievwright	25,332	–	28,288	–
Martyn Williams	2,138	–	3,422	–

Details of the Directors' share options are set out in the Directors' Remuneration Report on pages 31 to 37. Moir Lockhead also holds nominal non-beneficial interests in a number of the Company's subsidiary undertakings.

Between 1 April 2007 and 15 May 2007, the following changes occurred to Directors' interests:

On 24 April 2007, David Leeder acquired 22 shares pursuant to the Company's Buy As You Earn Scheme. On 25 April 2007, Martin Gilbert acquired 719 shares, Jim Forbes acquired 216 shares, each of David Begg and John Sievwright acquired 190 shares, Martyn Williams acquired 83 shares and Audrey Baxter acquired 388 shares under the standing arrangements whereby they have elected to receive 40% (except for Audrey Baxter who has elected to receive 100%) of their monthly fees in the form of shares in the Company.

No Director is materially interested in any significant contract or agreement with the Group, other than their service contracts.

Significant interests

At 15 May 2007, the Company had been advised of the following holders of 3% or more of its issued share capital for the purpose of section 198 of the Companies Act 1985

Institution	Ordinary 5p shares	%
Ameriprise Financial, Inc	35,070,076	8.06
JP Morgan Chase & Co	20,273,058	4.66
Lloyds TSB Group plc	18,452,730	4.24
Aviva plc	15,831,999	3.64
Legal & General plc	14,763,688	3.39

Employees

The Group is committed to employee involvement and uses a variety of methods to inform, consult and involve its employees in the business. These include subsidiary company newsletters and circulars and also First Edition, a Group wide newsletter, which is sent to all employees across the Group on a biannual basis. Senior managers within each division meet regularly to discuss current issues and employees are encouraged to discuss any issues with management at any time. Each division also operates a confidential hotline which staff can use to report health and safety, employment related and other issues concerning them.

The Group also has a regular dialogue with employees and representatives from Trades Unions. Each operating company has either an elected Company Council or, more typically, an Employee Director on its board. This principle extends to the plc Board where one of the Employee Directors is elected by his or her peers to represent employees across the Group.

Each division has its own information and consultation arrangements and levels of employee involvement in the business differ. However, in the UK, the Group has worked with Trades Unions to set up a number of joint schemes, including workplace learning, credit unions, new national policies on assaults, drugs and alcohol, the restructuring of Group pension schemes and a joint committee to review staff uniform procedures.

The Group is committed to wide employee share ownership. During the year, employees continued to have the opportunity to participate in the Group's Save As You Earn and Buy As You Earn schemes, details of which are set out in note 35 to the financial statements.

The Group is committed to equality of opportunity in all its employment practices, policies and procedures. To this

end, within the framework of the law, we are committed wherever practicable to achieving and maintaining a workforce which broadly reflects the local catchment area within which we operate. We aim to ensure that no employee or potential employee will receive less favourable treatment due to their race, colour, nationality, ethnic origin, religion, sex, gender reassignment, sexual orientation, religion, marital status, trade union membership, age or disability.

Corporate Social Responsibility

The system of internal control described on pages 27 to 30 covers significant risks associated with social, environmental and health and safety issues. The Group publishes a separate Corporate Social Responsibility Report covering these matters, which will be available on our website at www.firstgroup.com.

Charitable and political contributions

The Group made various donations to UK charities totalling approximately £100,000 during the year (2006 £170,000). No payments were made for political purposes.

Creditors

It is the Group's policy to abide by the payment terms agreed with suppliers wherever it is satisfied that the supplier has provided goods and services in accordance with agreed terms and conditions. A number of significant purchases including fuel, tyres and commitments under hire purchase contracts, finance leases and operating leases are paid by direct debit. At 31 March 2007, the Group had the equivalent of 31 days' (2006 28 days') purchases outstanding, based on the ratio of Group trade creditors at the end of the year to the amounts invoiced during the year by trade creditors. The Company does not have any trade creditors in its balance sheet.

Audit information

In the case of each of the persons who are Directors of the Company at the date when this report was approved

- so far as each of the Directors is aware, there is no relevant audit information (as defined in the Companies Act 1985) of which the Company's auditors are unaware, and
- each of the Directors has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information (as defined) and to establish that the Company's auditors are aware of that information.

Directors' report continued

Annual General Meeting

The Annual General Meeting will be held at the Aberdeen Exhibition and Conference Centre, Bridge of Don, Aberdeen, Scotland AB23 8BL on Thursday 12 July 2007 at 11.00 am. The Notice of Meeting is contained in a separate letter from the Chairman accompanying this Annual Report.

Going concern

Whilst any consideration of future matters involves making a judgement, at a particular point in time, about future events which are inherently uncertain, after making enquiries, the Directors have formed the judgement, at the time of approving these financial statements, that

there is a reasonable expectation that the Company and the Group have adequate resources to continue operating for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing these financial statements.

By order of the Board



Sidney Barne
Company Secretary
15 May 2007

395 King Street
Aberdeen
AB24 5RP

Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the accounts. The Directors are required to prepare accounts for the Group in accordance with International Financial Reporting Standards ('IFRS') and have chosen to prepare Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice ('UK GAAP')

In the case of UK GAAP accounts, the Directors are required to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether applicable accounting standards have been followed, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

In the case of IFRS accounts, International Accounting Standard 1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting

Standards Board's 'Framework for the preparation and presentation of financial statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs. Directors are also required to

- properly select and apply accounting policies,
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance, and
- prepare the accounts on a going concern basis unless, having assessed the ability of the Company to continue as a going concern, management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a Directors' report and Directors' Remuneration Report which comply with the requirements of the Companies Act 1985

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions

Consolidated income statement

Year ended 31 March 2007

	Notes	Before amortisation charges, non recurring bid costs and other non recurring items 2007 £m	Amortisation charges, non recurring bid costs and other non recurring items 2007 £m	Total 2007 £m	Before amortisation charges and non recurring bid costs 2006 £m	Amortisation charges and non recurring bid costs 2006 £m	Total 2006 £m
Revenue							
Continuing operations	3	3,708 8	–	3,708 8	3,030 9	–	3,030 9
Operating costs before (loss)/profit on disposal of fixed assets							
Continuing operations		(3,449 6)	(51 9)	(3,501 5)	(2,801 2)	(33 0)	(2,834 2)
Operating profit before (loss)/profit on disposal of fixed assets							
Continuing operations		259 2	(51 9)	207 3	229 7	(33 0)	196 7
Operating profit before amortisation charges, non recurring bid costs and other non recurring items		259 2	–	259 2	229 7	–	229 7
Amortisation charges	14	–	(10 3)	(10 3)	–	(4 5)	(4 5)
Non recurring bid costs	5	–	(19 3)	(19 3)	–	(28 5)	(28 5)
Other non recurring items	5	–	(22 3)	(22 3)	–	–	–
Operating profit before (loss)/profit on disposal of fixed assets		259 2	(51 9)	207 3	229 7	(33 0)	196 7
(Loss)/profit on disposal of fixed assets		–	(3 7)	(3 7)	–	14 0	14 0
Operating profit	6	259 2	(55 6)	203 6	229 7	(19 0)	210 7
Investment income	3, 8	9 4	–	9 4	8 5	–	8 5
Finance costs	9	(72 8)	–	(72 8)	(61 8)	–	(61 8)
Profit before tax		195 8	(55 6)	140 2	176 4	(19 0)	157 4
Tax	10	(51 1)	13 0	(38 1)	(45 3)	5 3	(40 0)
Profit for the period from continuing operations		144 7	(42 6)	102 1	131 1	(13 7)	117 4
Attributable to							
Equity holders of the parent		134 1	(42 4)	91 7	121 5	(14 0)	107 5
Minority interests		10 6	(0 2)	10 4	9 6	0 3	9 9
		144 7	(42 6)	102 1	131 1	(13 7)	117 4
Basic earnings per share	11			23 1p			27 4p
Diluted earnings per share	11			22 8p			27 1p

Dividends of £57 1m (2006 £52 0m) were paid during the year. Dividends of £45 6m (2006 £37 4m) were proposed for approval in respect of the year.

Consolidated statement of recognised income and expense

Year ended 31 March 2007

	2007 £m	2006 £m
Derivative hedging instrument movements	22.8	(43.2)
Deferred tax on derivative hedging instrument movements	2.0	8.1
Exchange differences on translation of foreign operations	(85.5)	49.6
Actuarial gains on defined benefit pension schemes	116.9	36.7
Deferred tax on actuarial gains on defined benefit pension schemes	(35.0)	(11.0)
Net income recognised directly in equity	21.2	40.2
Profit for the period	102.1	117.4
Total recognised income and expense for the period	123.3	157.6
Attributable to		
Equity holders of the parent	112.9	147.7
Minority interests	10.4	9.9
	123.3	157.6

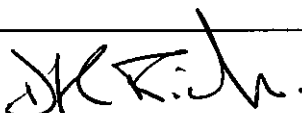
Consolidated balance sheet

As at 31 March 2007

	Notes	2007 £m	2006 £m
Non current assets			
Goodwill	13	468 8	503 1
Other intangible assets	14	60 8	30 0
Property, plant and equipment	15	1,059 7	926 5
Financial assets – derivative financial instruments	25	27 7	8 5
		1,617 0	1,468 1
Current assets			
Inventories	17	64 6	54 2
Trade and other receivables	18	377 3	373 1
Financial assets – cash and cash equivalents	21	411 2	174 4
– derivative financial instruments	25	8 3	14 1
		861 4	615 8
Non current assets classified as held for sale	19	7 5	6 6
Retirement benefit surplus	36	57 1	–
Total assets		2,543 0	2,090 5
Current liabilities			
Trade and other payables	20	695 1	545 1
Tax liabilities		49 7	47 8
Financial liabilities – bank overdrafts and loans	22	1 8	30 9
– bonds	22	23 1	23 1
– loan notes	24	5 2	2 8
– obligations under finance leases	23	11 5	2 3
– derivative financial instruments	25	5 0	1 8
		791 4	653 8
Net current assets/(liabilities)		70 0	(38 0)
Non current liabilities			
Financial liabilities – bank loans	22	310 5	268 8
– bonds	22	539 3	553 2
– loan notes	24	10 6	17 7
– obligations under finance leases	23	70 4	10 1
– derivative financial instruments	25	4 3	0 8
Retirement benefit obligation	36	33 3	132 0
Deferred tax liabilities	26	142 7	84 6
Long term provisions	27	33 2	37 6
		1,144 3	1,104 8
Total liabilities		1,935 7	1,758 6
Net assets		607 3	331 9
Equity			
Share capital	28	21 9	19 9
Share premium account	29	447 8	238 8
Hedging reserves	29	26 7	1 9
Other reserves	29	4 6	4 6
Own shares	29	(17 4)	(26 6)
Translation reserves	30	(57 8)	27 7
Retained earnings	29	170 4	52 9
Equity attributable to equity holders of the parent		596 2	319 2
Minority interests		11 1	12 7
Total equity		607 3	331 9

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Consolidated cash flow statement

Year ended 31 March 2007

	Note	2007 £m	2006 £m
Net cash from operating activities	32	295.5	235.0
Investing activities			
Interest received		9.4	5.9
Proceeds of disposal of property, plant and equipment		18.3	27.3
Purchases of property, plant and equipment		(251.2)	(196.2)
Grants received		29.1	–
Acquisition of businesses		(17.9)	(12.4)
Net cash used in investing activities		(212.3)	(175.4)
Financing activities			
Repurchase of ordinary share capital		–	(23.0)
Shares purchased by Employee Benefit Trust		–	(1.4)
Monies received on exercise of options		2.8	8.4
Dividends paid		(57.1)	(52.0)
Dividends paid to minority shareholders		(11.3)	(7.2)
Repayment of obligations under finance leases		(14.4)	(11.8)
Repayment of loan notes		(4.8)	(0.5)
Payment of new bank facility issue costs		–	(1.0)
Proceeds on issue of shares		216.9	–
New bank loans raised		22.4	55.7
Net cash from financing activities		154.5	(32.8)
Net increase in cash and cash equivalents before foreign exchange movements		237.7	26.8
Cash and cash equivalents at beginning of year		169.9	145.9
Effect of foreign exchange rate changes		2.7	(2.8)
Cash and cash equivalents at end of year		410.3	169.9
Cash and cash equivalents for cash flow statement purposes comprises		2007 £m	2006 £m
Cash and cash equivalents per balance sheet		411.2	174.4
Overdrafts		(0.9)	(4.5)
		410.3	169.9

Note to the consolidated cash flow statement – reconciliation of net cash flows to movement in net debt

Year ended 31 March 2007

	2007 £m	2006 £m
Increase in cash and cash equivalents in year before foreign exchange movements	237.7	26.8
Increase in debt and finance lease financing	(3.2)	(43.4)
Inception of new finance leases	(84.0)	–
Lease and hire purchase contracts acquired with business/franchise	–	(0.7)
Fees on issue of new loan facility	–	1.0
Other non-cash movements in relation to financial instruments	(0.8)	(1.9)
Foreign exchange differences	38.5	(23.1)
Movement in net debt in year	188.2	(41.3)
Net debt at beginning of year	(704.4)	(663.1)
Net debt at end of year	(516.2)	(704.4)

Notes to the consolidated financial statements

1 General information

FirstGroup plc is a company incorporated in the United Kingdom under the Companies Act 1985. The address of the registered office is 395 King Street, Aberdeen AB24 5RP. The nature of the Group's operations and its principal activities are set out in the Chief Executive's review on pages 3 to 16.

These financial statements are presented in pounds sterling because that is the currency of the primary economic environment in which the Group operates. Foreign operations are included in accordance with the accounting policies set out in note 2.

The parent Company financial statements and notes thereto are shown separately under UK GAAP on pages 83 to 90.

2 Significant accounting policies

Basis of accounting

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) adopted for use in the European Union and therefore comply with Article 4 of the EU IAS Regulation.

The financial statements have been prepared on the historical cost basis, except for the revaluation of certain financial instruments. The principal accounting policies adopted are set out below.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 March each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

Minority interests in the net assets of the consolidated subsidiaries are identified separately from the Group's equity interest therein. Minority interests consist of those interests at the date of the original business combination and the minority's share of the changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 *Business combinations* are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 *Non-current assets held for sale and discontinued operations*, which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisitions is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in the income statement.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

2 Significant accounting policies continued

Non current assets held for sale

Non current assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell

Non current assets are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Goodwill

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

Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash generating units. Cash generating units to which goodwill has been allocated are tested for impairment annually, or more frequently where there is an indication that the unit may be impaired. If the recoverable amount of the cash generating unit is less than the carrying amount of the unit, the impairment loss is allocated to the unit and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

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

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

Revenue recognition

Revenue principally comprises revenue from train passenger and freight services, road passenger transport, and certain management and maintenance services in the UK and North America. Where appropriate, amounts are shown net of rebates and sales taxes.

Revenue in UK Rail includes franchise agreement receipts from the Department for Transport (DfT) and Transport Scotland. Payments to the DfT for amounts due under the terms of a franchise are included in operating costs. Revenue also includes amounts attributable to the train operating companies ('TOCs'), predominantly based on models of route usage, by the Railway Settlement Plan in respect of passenger receipts. Where season tickets are issued in excess of one week's duration, the attributable share of income is deferred within creditors and is recognised in the income statement over the period covered by the season ticket.

UK Bus revenue principally comprises amounts receivable from ticket sales and concessionary fare schemes. Concessionary amounts are recognised in the period in which the service is provided based on a predetermined formula as agreed with the relevant local authority. Other Bus, including North America, and services revenue from contracts with government bodies and similar organisations are recognised as the services are provided.

Interest income is recognised on an accruals basis.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases and the rental charges are charged against income on a straight line basis over the life of the lease.

Notes to the consolidated financial statements continued

2 Significant accounting policies continued

Assets held under hire purchase contracts and finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs (see below).

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

Foreign currencies

The individual financial statements of each Group company are presented in the currency of the primary economic environment in which it operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group company are expressed in pounds sterling, which is the functional currency of the company, and the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual companies, transactions in currencies other than pounds sterling are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in profit or loss for the period. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognised directly in equity.

In order to hedge its exposure to certain foreign exchange risks, the Group holds currency swaps and net foreign borrowings in foreign currencies (see below for details of the Group's policies in respect of derivative financial instruments and foreign exchange risks).

On consolidation, the assets and liabilities of the Group's overseas operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used. Exchange differences arising from the average or spot exchange rates used and the period end rate, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in the income statement in the period in which they are incurred.

Operating profit

Operating profit is stated after charging intangible asset amortisation, non-recurring bid costs and other non-recurring items but before investment income and borrowing costs.

Non-recurring items

Non-recurring items are material items of income or expenditure which due to their size, 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.

2 Significant accounting policies continued

Retirement benefit costs

The Group operates or participates in a number of pension schemes, which include both defined benefit schemes and defined contribution schemes

Payments to defined contribution retirement benefit schemes are charged as an expense as they fall due. There is no legal or constructive obligation to pay 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.

For defined benefit schemes, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside the income statement and presented in the statement of recognised income and expense.

Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost, and as reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to past service cost, plus the present value of available refunds and reductions in future contributions to the scheme.

Various train operating companies in the UK Rail business participate in the Railways Pension Scheme, which is an industry wide defined benefit scheme. The Group is obligated to fund the relevant section of the scheme over the period for which the franchise is held. The full liability is recognised on the balance sheet, which is then reduced by a franchise adjustment so that the net liability reflects the Group's obligations to fund the scheme over the franchise term.

Taxation

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

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

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

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

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

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

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

Notes to the consolidated financial statements continued

2 Significant accounting policies continued

Property, plant and equipment

Properties for provision of services or administrative purposes are carried at cost, less any recognised impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Fixtures and equipment are stated at cost less accumulated depreciation and any recognised impairment loss.

Depreciation is charged so as to write off the cost of assets, other than freehold land, the land element of long leasehold properties or on assets in the course of construction, over their estimated useful lives, using the straight line method, on the following bases:

Freehold buildings	50 years straight line
Long leasehold buildings	50 years straight line
Short leasehold properties	period of lease
Passenger carrying vehicles	7 to 15 years straight line
Other plant and equipment	3 to 25 years straight line

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, over the term of the relevant lease.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

Government grants

Government grants relating to property, plant and equipment are treated as deferred income and released to the income statement over the expected useful lives of the assets concerned.

Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash generating unit to which the asset belongs. An intangible asset with an indefinite useful life is tested for impairment annually and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. 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 for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset or cash generating unit is estimated to be less than its carrying amount, the carrying amount of the asset (cash generating unit) is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately except in the case of goodwill, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Financial instruments

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

2 Significant accounting policies continued

Financial assets

The Group measures financial assets on initial recognition at fair value, and determines the classification of such assets at initial recognition and on any subsequent reclassification event

Where there is no active market for a financial asset, fair value is determined using valuation techniques including recent commercial transactions and discounted cash flows. Otherwise financial assets are carried at amortised cost

Financial assets are classified into one of four primary categories

Fair value through the income statement

This covers any financial asset designated on initial recognition to be measured at fair value with fair value changes to go through the income statement, and financial assets acquired principally for the purpose of trading in the short term

Held to maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified here when the Group has the intention and ability to hold to maturity. These financial assets are held at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when the investments are derecognised or impaired as well as through amortisation

Loans and receivables

Non-derivative financial assets with fixed or determinable payments that are not quoted in an active market have not been designated as either fair value through the income statement or Available For Sale. Such assets are carried at amortised cost. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired as well as through amortisation

The most significant financial assets under this category are trade receivables and bank deposits

Trade receivables are measured at fair value, i.e. original invoice amount, less an allowance for uncollectable amounts. Appropriate allowances for estimated irrecoverable amounts are recognised in the income statement when there is objective evidence that the asset is impaired

Bank deposits are included within 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. All are carried on the balance sheet at cost. Cash and cash equivalents includes ring-fenced cash. Under the terms of the Rail franchise agreements, cash can only be distributed by the train operating companies up to the lower of the amount of retained profits or the amount determined by prescribed liquidity ratios. The ring-fenced cash represents that which is not available for distribution or the amount required to satisfy the contractual liquidity ratio at the balance sheet date

Available for sale financial assets

Available for sale financial assets are non-derivative financial assets that are designated as such, or that are not classified in any of the other categories. 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

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received net of direct issue costs

Notes to the consolidated financial statements continued

2 Significant accounting policies continued

Financial liabilities

Bank borrowings

Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs

Sterling bonds and loan notes

These are measured either on an amortised cost basis or at fair value, if adopted

Trade payables

Trade payables are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest rate method

Derivative financial instruments and hedge accounting

The Group uses derivative financial instruments to hedge interest rate risks, foreign currency risks and fuel price risks. Use of such financial instruments is governed by policies and delegated authorities approved by the Board. The Group does not use derivative financial instruments for speculative purposes

The main derivative financial instruments used by the Group are interest rate swaps and collars, fuel swaps and collars, and cross currency interest rate swaps and currency forwards. Such instruments are initially recognised at fair value and subsequently re-measured to fair value at the reported balance sheet date. The fair values are calculated by reference to market exchange rates, interest rates and fuel prices at the period end, and supported by counterparty confirmations. The interest rate swaps are designated as cash flow hedges for interest rate risk on certain floating rate debt, and fair value hedges for fair value risk relating to the LIBOR element of a fixed rate financial liability. The fuel swaps and collars are designated as cash flow hedges of fuel price risks or otherwise used as economic hedges of such risks. The cross currency swaps are designated as hedges of the foreign exchange risk relating to part of the Group's net investment in US Dollar assets. The currency forwards are designated as a cash flow hedge of foreign exchange risk relating to US Dollar denominated fuel purchases in the UK.

Changes in the fair value of derivative financial instruments that do not qualify for hedge accounting as cash flow hedges or foreign currency hedges of a foreign net investment are recognised in the income statement as they arise.

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

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not carried at fair value with unrealised gains or losses reported in the income statement.

Provisions

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

Insurance

The Group's policy is to self-insure high frequency, low value claims within the businesses. To provide protection above these types of losses, cover is obtained through third-party insurance policies. Provision is made under IAS 37 for the estimated cost of settling uninsured claims for incidents occurring prior to balance sheet date.

Share based payments

The Group issues equity settled share based payments to certain employees. Equity settled share based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity settled share based payments is expensed on a straight line basis over the vesting period, based on the Group's estimate of shares that will eventually vest and is adjusted for the effects of non-market based vesting conditions.

2 Significant accounting policies continued

Fair value is measured by use of a Black Scholes model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders.

New standards and interpretations not applied

The International Accounting Standards Board and the International Financial Reporting Interpretations Committee (IFRIC) have issued the following standards and interpretations with effective dates starting after 1 April 2006.

International Accounting Standard (IAS)/International Financial Reporting Standard (IFRS)

IFRS 7 Financial Instruments: Disclosures	1 January 2007
IAS 1 Amendment – Presentation of Financial Statements: Capital Disclosures	1 January 2007
IFRS 8 Operating Segments	1 January 2009
IAS 23 Borrowing Costs (revised March 2007)	1 January 2009

IFRIC

IFRIC 8 Scope of IFRS 2	1 May 2006
IFRIC 9 Reassessment of Embedded Derivatives	1 June 2006
IFRIC 10 <i>Interim Financial Reporting and Impairment</i>	1 November 2006
IFRIC 11 Group and Treasury Share Transactions	1 March 2007
IFRIC 12 Service Concession Arrangements	1 January 2008

Under IFRS 7 the Group will have to disclose additional information about its financial instruments, their significance and the nature and extent of risks that they give rise to. More specifically, the Group will need to disclose the fair values of its financial instruments and its risk exposure in greater detail. The Directors do not anticipate that the adoption of any of the above standards or interpretations will have a material impact on the Group's Accounts in the period of initial application.

Critical accounting judgements and key sources of estimation uncertainty

In the process of applying the Group's accounting policies which are described above, management has made the following judgements and estimates that have the most significant effect on the amounts recognised in the financial statements:

Impairment of intangible assets (including goodwill)

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which the goodwill has been allocated. The value in use requires the entity to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value. The carrying amount of goodwill at the balance sheet date was £468.8m (2006: £503.1m) as set out in note 13 and the carrying amount of other intangible assets at balance sheet date was £60.8m (2006: £30.0m) as set out in note 14.

Defined benefit pension arrangements

Measurement of defined benefit pension obligations requires estimation of a suitable discount rate, the expected return on scheme assets, expected rate of future salary and pension increases along with assumptions about mortality rates. The most significant of these assumptions is the discount rate. A 0.1% movement in the discount rate applied would impact operating profit and the balance sheet deficit by approximately £1.0m and £23.0m respectively. The net pension surplus as at the balance sheet date was £23.8m (2006: net deficit of £132.0m) as set out in note 36.

Self insurance

Provision is made for all known incidents for which there is self insurance using management's best estimate of the likely settlement of these incidents. The estimated settlement is reviewed on a regular basis with independent actuarial advice and the amount provided is adjusted as required. The Group's total insurance reserves as at the balance sheet date was £70.9m (2006: £80.7m) as set out in note 27.

Notes to the consolidated financial statements continued

	2007 £m	2006 £m
3 Revenue		
Services rendered	3,708.8	3,030.9
Investment income (note 8)	9.4	8.5
Total revenue (as defined in IAS 18)	3,718.2	3,039.4

Revenue by business segment is set out in note 4 below

4 Business and geographical segments

Business segments

For management purposes, the Group is currently organised into three operating divisions – UK Bus, UK Rail and North America. These divisions are the basis on which the Group reports its primary segment information. The principal activities of these divisions are set out in the Chief Executive's review.

Segment information about these businesses is set out below.

The segment results for the year to 31 March 2007 are as follows:

	UK Bus 2007 £m	UK Rail 2007 £m	North America 2007 £m	Group items 2007 £m	Total 2007 £m
Revenue	1,073.7	1,824.1	802.9	8.1	3,708.8
Segment results ¹	103.0	108.8	68.2	(20.8)	259.2
Amortisation of intangible assets	–	(8.2)	(2.1)	–	(10.3)
Non recurring bid costs (note 5)	–	(14.5)	–	(4.8)	(19.3)
Other non recurring items (note 5)	–	(21.3)	(1.0)	–	(22.3)
Loss on disposal of fixed assets	(3.7)	–	–	–	(3.7)
Operating profit	99.3	64.8	65.1	(25.6)	203.6
Investment income					9.4
Finance costs					(72.8)
Profit before tax					140.2
Tax					(38.1)
Profit for the year					102.1
Other information					
	UK Bus 2007 £m	UK Rail 2007 £m	North America 2007 £m	Group items 2007 £m	Total 2007 £m
Capital additions	161.7	145.3	69.3	1.8	378.1
Depreciation and amortisation	70.7	21.8	53.0	4.5	150.0
Balance sheet					
	UK Bus 2007 £m	UK Rail 2007 £m	North America 2007 £m	Group items 2007 £m	Total 2007 £m
Total assets	856.2	496.1	1,084.2	106.5	2,543.0
Total liabilities	627.5	422.0	586.0	300.2	1,935.7

¹Before amortisation of intangible assets, non recurring bid costs, other non recurring items and (loss)/profit on disposal of fixed assets.

4 Business and geographical segments continued

The segment results for the year to 31 March 2006 are as follows

	UK Bus 2006 £m	UK Rail 2006 £m	North America 2006 £m	Group items 2006 £m	Total 2006 £m
Revenue	1,031.2	1,164.9	826.3	8.5	3,030.9
Segment results ¹	98.4	79.6	67.1	(15.4)	229.7
Amortisation of intangible assets	–	(2.9)	(1.6)	–	(4.5)
Non-recurring bid costs (note 5)	–	(26.1)	–	(2.4)	(28.5)
Profit on disposal of fixed assets	14.0	–	–	–	14.0
Operating profit	112.4	50.6	65.5	(17.8)	210.7
Investment income					8.5
Finance costs					(61.8)
Profit before tax					157.4
Tax					(40.0)
Profit for the year					117.4

¹Before amortisation of intangible assets, non-recurring bid costs, other non-recurring items and (loss)/profit on disposal of fixed assets

	UK Bus 2006 £m	UK Rail 2006 £m	North America 2006 £m	Group items 2006 £m	Total 2006 £m
Other information					
Capital additions	118.7	16.9	82.2	9.9	227.7
Depreciation and amortisation	58.9	8.2	56.5	2.9	126.5

	UK Bus 2006 £m	UK Rail 2006 £m	North America 2006 £m	Group items 2006 £m	Total 2006 £m
Balance sheet					
Total assets	740.1	332.8	946.6	71.0	2,090.5
Total liabilities	567.4	277.0	423.2	491.0	1,758.6

Geographical segments

The Group's operations are located in the United Kingdom and North America. The following table provides an analysis of the Group's revenue by geographical market

	2007 £m	2006 £m
United Kingdom	2,905.9	2,204.6
North America	802.9	826.3
	3,708.8	3,030.9

Notes to the consolidated financial statements continued

4 Business and geographical segments continued

The following is an analysis of the carrying amount of segment assets, and additions to property, plant and equipment and intangible assets, analysed by the geographical area in which the assets are located

	Carrying amount of segment assets		Additions to property plant and equipment and intangible assets	
	2007 £m	2006 £m	2007 £m	2006 £m
United Kingdom	1,458.8	1,143.9	308.8	145.5
North America	1,084.2	946.6	69.3	82.2
	2,543.0	2,090.5	378.1	227.7

Other non cash items, included within Group items, include the following charges

	2007 £m	2006 £m
Share based payments	3.2	3.2
Loss on disposal of plant and equipment	1.9	1.4
	5.1	4.6

5 Non recurring bid costs and other non recurring items

Non recurring bid costs of £19.3m (2006 £28.5m) were incurred during the year and included £14.5m bidding for the South West Trains, Cross Country and InterCity East Coast franchises. Costs of £4.8m (2006 £2.4m) were incurred on non rail bids.

UK Rail transition costs of £21.3m (2006 £nil) were incurred on the mobilisation of the First Capital Connect and First Great Western franchises and subsequent train refurbishment obligations relating to both franchises. In addition £1.0m or \$2.2m (2006 £nil) was charged in North America to provide for onerous contracts.

The tax benefit as a result of this expenditure was a credit of £12.5m (2006 credit of £8.6m).

6 Operating profit

Operating profit has been arrived at after charging

	2007 £m	2006 £m
Depreciation of property, plant and equipment (note 15)	139.7	122.0
Amortisation of intangible assets (note 14)	10.3	4.5
Cost of inventories recognised as an expense	370.0	358.2
Staff costs (note 7)	1,486.4	1,376.1
Auditors' remuneration for audit services (see page 57)	0.8	0.7

6 Operating profit continued

Amounts payable to Deloitte & Touche LLP and their associates by the Company and its subsidiary undertakings in respect of audit and non audit services are shown below

	2007 £m	2006 £m
Fees payable to the Company's auditors for the audit of the Company's annual accounts	0.1	0.1
Fees payable to the Company's auditors and their associates for other services to the Group		
– The audit of the Company's subsidiaries pursuant to legislation	0.7	0.6
Total audit fees	0.8	0.7
– International Financial Reporting convergence assistance	–	0.1
– Tax services	0.1	–
– Due diligence	0.5	0.1
Total non audit fees	0.6	0.2

In addition to the above, there are other fees deferred in the balance sheet in respect of acquisition advice from Deloitte & Touche LLP of £2.6m (2006: £nil)

A description of the work of the Audit Committee is set out in the corporate governance statement on pages 26 to 27 and includes an explanation of how auditor objectivity and independence is safeguarded when non audit services are provided by the auditors

7 Staff costs

The average monthly number of employees (including Executive Directors) was

	2007 No	2006 No
Operational	69,874	66,535
Administrative	4,359	4,212
	74,233	70,747

Their aggregate remuneration (including Executive Directors) comprised

	2007 £m	2006 £m
Wages and salaries	1,359.2	1,264.6
Social security costs	101.6	92.8
Other pension costs (note 36)	25.6	18.7
	1,486.4	1,376.1

Disclosures on Directors' remuneration, share options, long term incentive schemes and pension entitlements required by the Companies Act 1985 and those specified for audit by the Financial Services Authority are contained in the tables/notes within the Directors' Remuneration Report on pages 31 to 37 and form part of these audited financial statements

	2007 £m	2006 £m
8 Investment income		
Interest income	9.4	8.5

Notes to the consolidated financial statements continued

	2007 £m	2006 £m
9 Finance costs		
Bond and bank borrowings	59.8	53.1
Loan notes	1.4	1.8
Finance charges payable in respect of finance leases	4.7	0.8
Total borrowing costs	65.9	55.7
Notional interest on long term provisions	6.9	6.1
	72.8	61.8

There was no interest capitalised into qualifying assets in either the year ended 31 March 2006 or 31 March 2007

	2007 £m	2006 £m
10 Tax on profit on ordinary activities		
Current tax	5.5	(3.3)
Deferred tax (note 26)	32.6	43.3
	38.1	40.0

Corporation tax is calculated at 30% (2006 30%) of the estimated assessable profit for the year

Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions

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

	2007 £m	2007 %	2006 £m	2006 %
Profit before tax	140.2	100.0	157.4	100.0
Tax at the UK corporation tax rate of 30%	42.1	30.0	47.2	30.0
Tax effect of expenses that are not deductible in determining taxable profit	1.1	0.8	0.9	0.6
Income not subject to tax	(3.2)	(2.3)	(0.5)	(0.3)
Effect of tax rates of subsidiaries operating in other jurisdictions	3.0	2.2	4.6	2.9
Adjustments to tax in respect of prior years	(4.9)	(3.5)	(12.2)	(7.8)
Tax expense and effective tax rate for the year	38.1	27.2	40.0	25.4

In addition to the amount charged to the income statement, tax relating to share based payments, actuarial gains and cash flow and net investment hedges, amounting to £28.9m (2006 £0.8m) has been charged directly to equity

11 Earnings per share (EPS)

Basic EPS is calculated by dividing the profit attributable to equity shareholders of £91.7m (2006 £107.5m) by the weighted average number of ordinary shares of 397.9m (2006 392.6m)

Diluted EPS is calculated by dividing the profit attributable to equity shareholders of £91.7m (2006 £107.5m) by the weighted average number of ordinary shares of 402.0m (2006 396.5m). The difference in the number of shares between the basic calculation and the diluted calculation represents the weighted average number of potentially dilutive ordinary shares.

A reconciliation of the number of shares used in the basic and diluted measures is set out below

	2007 No m	2006 No m
Weighted average number of shares used in basic calculation	397.9	392.6
SAYE share options	2.5	3.0
Executive share options	1.6	0.9
	402.0	396.5

11 Earnings per share (EPS) continued

The adjusted basic EPS and adjusted cash EPS are intended to demonstrate recurring elements of the results of the Group before amortisation of intangible assets, non recurring bid costs, other non recurring items and loss/profit on disposal of fixed assets. A reconciliation of the earnings used in the bases is set out below.

	2007		2006	
	£m	Earnings per share (p)	£m	Earnings per share (p)
Profit for basic EPS calculation	91.7	23.1	107.5	27.4
Amortisation of intangible assets ¹	10.1	2.5	4.3	1.1
Non recurring bid costs	19.3	4.9	28.5	7.2
Other non recurring items	22.3	5.6	–	–
Loss/(profit) on disposal of fixed assets ²	3.7	0.9	(13.5)	(3.4)
Taxation effect of adjustments	(13.0)	(3.3)	(5.3)	(1.4)
Profit for adjusted basic EPS calculation	134.1	33.7	121.5	30.9
Depreciation ³	138.8	34.9	121.6	31.0
Profit for adjusted cash EPS calculation ⁴	272.9	68.6	243.1	61.9

¹Amortisation charge of £10.3m per note 14 less £0.2m (2006: £4.5m less £0.2m) attributable to equity minority interests.

²Loss on disposal of fixed assets of £3.7m less £nil (2006: profit of £14.0m less £0.5m) attributable to equity minority interests.

³Depreciation charge of £139.7m (2006: £122.0m) per note 15 less £0.9m (2006: £0.4m) attributable to equity minority interests.

⁴Excludes working capital movements.

	2007 £m	2006 £m
12 Dividends		
Amounts recognised as distributions to equity holders in the period		
Final dividend for the year ended 31 March 2006 of 9.55p (2005: 8.69p) per share	37.5	34.1
Interim dividend for the year ended 31 March 2007 of 5.0p (2006: 4.55p) per share	19.6	17.9
	57.1	52.0
Proposed final dividend for the year ended 31 March 2007 of 10.5p (2006: 9.55p) per share	45.6	37.5

The proposed final dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements.

	2007 £m	2006 £m
13 Goodwill		
Cost		
At 1 April	503.1	465.8
Additions	9.1	10.3
Exchange rate differences	(43.4)	27.0
At 31 March	468.8	503.1
Accumulated impairment losses		
At 31 March	–	–
Carrying amount		
At 31 March	468.8	503.1

Notes to the consolidated financial statements continued

13 Goodwill continued

Details of acquisitions in the year are shown in note 31. During the year, goodwill was reviewed for impairment in accordance with IAS 36. For the purposes of this impairment review goodwill has been valued on the basis of discounted future cash flows arising in each relevant cash generating unit. The Group prepares cash flow forecasts derived from the most recent five year plan for the next four years and extrapolates cash flows for the following six years based on estimated growth rates of 2.5% for the United Kingdom and 3.0% for North America. A discount rate of 10.0% was used in arriving at the value in use for each of the cash generating units. The calculation of value in use for each cash generating unit is most sensitive to the principal assumptions of discount rate, growth rates and margins achievable. The Directors consider the assumptions to be reasonable based on historic performance of each cash generating unit and are realistic in light of economic and industry forecasts.

The goodwill is split as follows

	2007 £m	2006 £m
Carrying amount		
UK Bus	87.4	87.4
UK Rail	19.8	19.8
First Student	255.3	281.0
First Transit	54.7	57.3
First Services	51.6	57.6
	468.8	503.1

The reduction in the carrying value of goodwill is mainly as a result of foreign exchange movements, as the balance sheet rate was \$1.96/£1 at 31 March 2007 compared with \$1.74/£1 at 31 March 2006, net of additions made during the year.

14 Other intangible assets	Contracts acquired £m	Franchise agreements £m	Total £m
Cost			
At 1 April 2006	15.7	21.0	36.7
Additions	7.1	35.3	42.4
Exchange rate differences	(1.6)	–	(1.6)
At 31 March 2007	21.2	56.3	77.5
Amortisation			
At 1 April 2006	2.2	4.5	6.7
Charge for year	2.1	8.2	10.3
Exchange rate differences	(0.3)	–	(0.3)
At 31 March 2007	4.0	12.7	16.7
Carrying amount			
At 31 March 2007	17.2	43.6	60.8

14 Other intangible assets continued	Contracts acquired £m	Franchise agreements £m	Total £m
Cost			
At 1 April 2005	10.6	21.0	31.6
Additions	4.3	–	4.3
Exchange rate differences	0.8	–	0.8
At 31 March 2006	15.7	21.0	36.7
Amortisation			
At 1 April 2005	0.6	1.6	2.2
Charge for year	1.6	2.9	4.5
Exchange rate differences	–	–	–
At 31 March 2006	2.2	4.5	6.7
Carrying amount			
At 31 March 2006	13.5	16.5	30.0

Contracts acquired through the purchases of businesses and subsidiary undertakings are amortised on a straight line basis over their useful lives which is, on average, nine years

The rail franchise agreement intangible asset represents the part of the economic benefit derived from the rail franchise agreement that is realised as a result of recognising our share of the rail pension deficit and is amortised on a straight line basis over the term of the franchise. The largest elements of the franchise intangible relates to the ScotRail franchise (carrying amount £11.0m (2006 £13.4m)) and the First Great Western franchise (carrying amount £22.9m (2006 £nil)) which are being amortised on a straight line basis over the term of each respective franchise

15 Property, plant and equipment	Land and buildings £m	Passenger carrying vehicle fleet £m	Other plant and equipment £m	Total £m
Cost				
At 1 April 2006	157.0	1,331.9	203.7	1,692.6
Subsidiary undertakings and businesses acquired	–	5.0	–	5.0
Additions	28.6	178.8	114.2	321.6
Disposals	(5.1)	(43.1)	(22.8)	(71.0)
Reclassifications	4.1	–	(4.1)	–
Reclassified as held for sale	–	(24.5)	–	(24.5)
Exchange rate differences	(2.9)	(58.2)	(5.0)	(66.1)
At 31 March 2007	181.7	1,389.9	286.0	1,857.6
Accumulated depreciation and impairment				
At 1 April 2006	22.1	621.1	122.9	766.1
Charge for year	5.2	107.7	26.8	139.7
Disposals	(0.9)	(38.7)	(19.8)	(59.4)
Reclassified as held for sale	–	(18.1)	–	(18.1)
Exchange rate differences	(0.8)	(26.5)	(3.1)	(30.4)
At 31 March 2007	25.6	645.5	126.8	797.9
Carrying amount				
At 31 March 2007	156.1	744.4	159.2	1,059.7

Notes to the consolidated financial statements continued

	Land and buildings £m	Passenger carrying vehicle fleet £m	Other plant and equipment £m	Total £m
15 Property, plant and equipment continued				
Cost				
At 1 April 2005	149 1	1,228 7	161 4	1,539 2
Subsidiary undertakings and businesses acquired	–	4 0	–	4 0
Additions	16 2	155 5	37 4	209 1
Disposals	(5 1)	(64 2)	(2 9)	(72 2)
Reclassifications	(5 1)	–	5 1	–
Reclassified as held for sale	–	(27 3)	–	(27 3)
Exchange rate differences	1 9	35 2	2 7	39 8
At 31 March 2006	157 0	1,331 9	203 7	1,692 6
Accumulated depreciation and impairment				
At 1 April 2005	23 7	581 2	99 3	704 2
Charge for year	3 6	99 0	19 4	122 0
Disposals	(0 6)	(52 1)	(2 3)	(55 0)
Reclassifications	(5 1)	–	5 1	–
Reclassified as held for sale	–	(21 5)	–	(21 5)
Exchange rate differences	0 5	14 5	1 4	16 4
At 31 March 2006	22 1	621 1	122 9	766 1
Carrying amount				
At 31 March 2006	134 9	710 8	80 8	926 5

The carrying amount of the Group's passenger carrying vehicle fleet includes an amount of £103 0m (2006 £44 4m) in respect of assets held under finance leases

At 31 March 2007 the Group had entered into contractual commitments amounting to £224 0m (2006 £65 3m), principally representing buses ordered in the United Kingdom and commitments under the First Great Western and First Capital Connect franchises

16 Subsidiaries

A list of the significant investments in subsidiaries, including the name, country of incorporation, proportion of ownership interest is given in note 4 to the Company's separate financial statements on page 86

	2007 £m	2006 £m
17 Inventories		
Spare parts and consumables	48 1	41 7
Property development work in progress	16 5	12 5
	64 6	54 2

In the view of the Directors there is no material difference between the balance sheet value of inventories and their replacement cost. There was no material write down of inventories during the current or prior year. The provision for stock obsolescence at the balance sheet date was £4 3m (2006 £4 4m)

18 Trade and other receivables	2007 £m	2006 £m
Amounts due within one year		
Trade debtors	262.7	279.3
Other debtors	61.8	38.8
Other prepayments and accrued income	52.8	55.0
	377.3	373.1

The Directors consider that the carrying amount of trade and other receivables approximates to their fair value

Credit risk

The Group's principal financial assets are short term bank balances and cash, derivative financial instruments and short term trade and other receivables, which represent the Group's maximum exposure to credit risk in relation to financial assets

The Group's credit risk is primarily attributable to its short term trade receivables. The amounts presented in the balance sheet are net of allowances for doubtful receivables, estimated by the Group's management based on prior experience and their assessment of the current economic environment. The provision for doubtful receivables at the balance sheet date was £2.3m (2006: £2.1m)

The credit risk on short term cash assets and derivative financial instruments is limited because the counterparties are banks with strong credit ratings assigned by international credit rating agencies

The Group has no significant concentration of credit risk, with exposure spread over a large number of counterparties and customers

19 Non current assets classified as held for sale

Non current assets held for sale comprise North American yellow school buses which are surplus to requirement and are being actively marketed on the Internet. Gains or losses arising on the disposal of such assets are included in arriving at operating profit in the income statement. The Group expects to sell such yellow school buses within 12 months of them going onto the 'for sale' list

20 Trade and other payables	2007 £m	2006 £m
Amounts falling due within one year		
Trade creditors	194.5	129.7
Other creditors	104.7	106.5
Accruals and deferred income	346.4	294.9
Season ticket deferred income	49.5	14.0
	695.1	545.1

The Directors consider that the carrying amount of trade payables approximates to their fair value

Notes to the consolidated financial statements continued

	2007 £m	2006 £m
21 Cash and cash equivalents		
Cash and cash equivalents	411.2	174.4

The fair value of cash and cash equivalents matches the carrying value

Cash and cash equivalents includes ring fenced cash of £139.6m (2006: £119.5m). Under the terms of the Rail franchise agreements, cash can only be distributed by the train operating companies up to the lower of amount of retained profits or the amount determined by prescribed liquidity ratios. The ring fenced cash represents that which is not available for distribution or the amount required to satisfy the liquidity ratio at the balance sheet date.

	2007 £m	2006 £m
22 Financial liabilities – borrowings		
Current financial liabilities		
Short term bank loans	0.9	26.4
Bank overdrafts	0.9	4.5
	1.8	30.9
Finance leases (note 23)	11.5	2.3
Loan notes (note 24)	5.2	2.8
Bond 6 875% (repayable 2013) – accrued interest	20.1	20.1
Bond 6 125% (repayable 2019) – accrued interest	3.0	3.0
	23.1	23.1
Total current financial liabilities	41.6	59.1
Non current financial liabilities		
Syndicated unsecured bank loans	308.2	264.9
Other loans	2.3	3.9
	310.5	268.8
Finance leases (note 23)	70.4	10.1
Loan notes (note 24)	10.6	17.7
Bond 6 875% (repayable 2013)	296.3	295.9
Bond 6 125% (repayable 2019)	243.0	257.3
	539.3	553.2
Total non current financial liabilities	930.8	849.8
Total financial liabilities	972.4	908.9
Gross borrowings repayment profile		
Within one year or on demand	41.6	59.1
Between one and two years	24.5	21.1
Between two and five years	351.1	271.7
Over five years	555.2	557.0
	972.4	908.9

The non current bond repayable in 2013 is measured on an amortised cost basis and had a par value of £300.0m. Interest on the 2013 bond is payable annually in April. The non current bond repayable in 2019 is measured on an amortised cost basis, adjusted for certain fair value movements on the bond that are fully and effectively hedged by swaps. The 2019 bond had a par value of £250.0m. Interest on the 2019 bond is payable annually in January.

22 Financial liabilities – borrowings continued

Effective interest rates

The effective interest rates at the balance sheet dates were as follows

	2007	2006
Bank overdraft	LIBOR + 1%	LIBOR + 1%
Bank borrowings	LIBOR + 0.225% to 0.35%	LIBOR + 0.225% to 0.35%
Bond 2013	7.10%	7.10%
Bond 2019	6.18%	6.18%
Finance leases	LIBOR up to average fixed of 6.85%	LIBOR + 0.50% up to average fixed of 7.00%
Loan notes	LIBOR – 0.50% up to total fixed of 11.00%	LIBOR – 0.50% up to total fixed of 11.00%

Carrying value of gross borrowings by currency	2007 £m	2006 £m
Sterling	923.3	853.5
Euros	9.4	9.9
US Dollar	1.2	5.0
Canadian Dollar	38.5	40.5
	972.4	908.9

Maturity of non current financial liabilities	2007					2006				
	Debt £m	Finance leases £m	Loan notes £m	Bonds £m	Total £m	Debt £m	Finance leases £m	Loan notes £m	Bonds £m	Total £m
Due in more than one year but not more than two years	1.0	12.9	10.6	–	24.5	1.2	2.2	17.7	–	21.1
Due in more than two years but not more than five years	309.4	41.7	–	–	351.1	267.1	4.6	–	–	271.7
Due in more than five years	0.1	15.8	–	539.3	555.2	0.5	3.3	–	553.2	557.0
Total	310.5	70.4	10.6	539.3	930.8	268.8	10.1	17.7	553.2	849.8

Borrowing facilities

The Group had £201.3m (2006 £211.0m) undrawn committed borrowing facilities as at 31 March 2007. Total bank borrowing facilities at 31 March 2007 stood at £596.0m (2006 £597.0m) of which £520.0m (2006 £527.4m) was committed and £76.0m (2006 £69.6m) was uncommitted.

23 Finance leases

The Group had the following obligations under finance leases as at the balance sheet dates

	2007 £m	2006 £m
Due in less than one year	11.5	2.3
Due in more than one year but not more than two years	12.9	2.2
Due in more than two years but not more than five years	41.7	4.6
Due in more than five years	15.8	3.3
Total	81.9	12.4

The lease obligations are denominated in Sterling and Canadian Dollars. The Sterling fixed rate leases of £2.5m (2006 £2.9m) have an average remaining life of six years and an effective borrowing rate of 6.85% (2006 7.00%). The Canadian Dollar fixed rate leases of £1.2m (2006 £1.9m) have an average remaining life of two years and an effective borrowing rate of 6.70% (2006 6.75%). The Group considers there to be no material difference between the fair value of the finance leases and the carrying amount in the balance sheet.

Notes to the consolidated financial statements continued

24 Loan notes

The Group had the following loan notes issued as at the balance sheet dates

	2007 £m	2006 £m
Due in less than one year	5.2	2.8
Due in more than one year but not more than two years	10.6	17.7
Total	15.8	20.5

The loan notes have been classified by reference to the earliest date on which the loan note holder can request redemption. Loan notes of £14.9m (2006: £19.7m) are supported by unsecured bank guarantees.

The loan notes have an effective borrowing rate of 8.20% (2006: 7.55%) and an average remaining term of 10 years (2006: 11 years) assuming that holders do not request redemption. The fair value of the loan notes has been determined to be £20.7m (2006: £27.0m). This has been calculated by discounting future cash flows that will arise under the loan notes.

25 Derivative financial instruments	2007 £m	2006 £m
Non-current assets		
Cross currency swaps (net investment hedge)	24.9	–
Coupon swaps (fair value hedge)	–	8.1
Interest rate collars (cash flow hedge)	–	0.4
Fuel derivatives (cash flow hedge)	2.8	–
	27.7	8.5
Current assets		
Cross currency swaps (net investment hedge)	2.9	–
Coupon swaps (fair value hedge)	1.2	3.3
Fuel derivatives (cash flow hedge)	4.2	10.8
	8.3	14.1
Total assets	36.0	22.6
Current liabilities		
Interest rate swaps (cash flow hedge)	0.3	0.9
Cross currency swaps (net investment hedge)	–	0.9
Fuel derivatives (cash flow hedge)	1.4	–
Currency forwards (cash flow hedge)	3.3	–
	5.0	1.8
Non-current liabilities		
Interest rate swaps (cash flow hedge)	–	0.4
Cross currency swaps (net investment hedge)	–	0.4
Coupon swaps (fair value hedge)	4.1	–
Interest rate collars (cash flow hedge)	0.2	–
	4.3	0.8
Total liabilities	9.3	2.6

During the year £1.5m was debited to the hedging reserve in respect of cash flow hedges (2006: £2.0m credit). In addition £4.5m was recycled from the hedging reserve and credited to the income statement in respect of cash flow hedges (2006: £27.1m credit).

Financial risks and management

In addition to certain pension risks, the most material financial risks faced by the Group are the effects of changes in foreign exchange rates, interest rates and fuel prices. The Group manages these risks within the context of a set of formal treasury policies established by the Board. Certain risk management responsibilities are formally delegated by the Board, principally to a sub-committee of the Board and to the Group Finance Director.

25 Derivative financial instruments continued

Foreign currency

The Group's principal operations outside the UK are in the US and Canada, with the US being the most significant. The Group is exposed to foreign exchange risk in retranslating net assets and earnings in US Dollars and Canadian Dollars to Sterling for reporting purposes. The Group's objective is to hedge at a minimum of 30% for US Dollar net assets and 75% for other currencies. As at 31 March 2007 there was a net investment hedge of 33% (2006 34%) of US net assets which were hedged with currency swaps and US Dollar debt. The currency swaps expire in March 2011. Any exchange gain or loss realised in cash on the swaps at expiry would remain in equity. Retranslation risk on US Dollar earnings are substantially hedged through natural offset by US Dollar denominated costs, principally UK fuel costs and Dollar interest costs. With the exception of UK fuel, transactional currency exposures are minimal. Currency forward contracts from April 2007 to March 2008 have been entered into as a cash flow hedge of US Dollar denominated fuel costs in the UK.

Interest rate risk

The Group has interest bearing cash and debt and therefore is exposed to the effects of changes to interest rates. The Group's policy objective is to maintain fixed interest rates at a minimum average of 75% of on balance sheet net debt over the medium term, so that volatility is substantially reduced year on year. The main floating rate benchmarks are UK LIBOR and US Dollar LIBOR. The Group achieves the policy objective through fixed rate debt and cash flow hedge financial instruments, being interest rate swaps and collars. The interest rate swaps expire in the year ending 31 March 2008, with no material impact anticipated either to the cash flow or income statement. The US interest rate collars expire in March 2009 and carry a floor of 3.6% and a ceiling of 5.75%. They provide a partial economic hedge each year up to March 2009 on US Dollar LIBOR risk over this period. They are not anticipated to have a material impact on either cash flow or income statement over this period as long as the LIBOR rate remains within the collar range. At 31 March 2007, 81% (2006 85%) of net debt was fixed with an average duration of 3.4 years (2006 4.1 years). It is Board policy to hedge 100% of interest rate risk in finance leases.

Fair value changes in the £250m Sterling bond relating to the LIBOR element is hedged with coupon swaps. These swaps match the fair value movements of the bond in the income statement and have the same term as the bond. Interest income is received in January and payments made in March and September each year.

Commodity price risk – fuel prices

The Group purchases diesel fuel on a floating price basis in its UK Bus, UK Rail, US and Canadian bus operations and therefore is exposed to changes in diesel prices, of which the most significant element is crude oil price risk. The Group's policy objective is to maintain a significant degree of fixed price protection in the short term, so that the businesses have time to prepare and adjust for prices after the current hedge period expires. The Group uses a range of cash flow hedge financial instruments to achieve significant fixed price certainty, mainly swaps and collars. During the year to 31 March 2007, the Group hedged 100% of crude price risk in the UK and 76% of crude price risk in the US.

The Group also entered into swaps for periods from April 2007 to March 2011 with the majority of these swaps relating to the year to 31 March 2008. The swaps give rise to monthly cash flow exchanges with counterparties to offset the underlying settlement of floating price costs, except where they have a deferred start date. Gains or losses on fuel derivatives are recycled from equity to the income statement on qualifying hedges to achieve fixed rate fuel costs.

Credit risk

The maximum credit risk exposure of the Group is the gross carrying value of the financial assets as disclosed above, and trade receivables as disclosed in note 18. Most of trade receivables are with public or quasi public bodies, principally the UK DfT, Network Rail, Transport for London, UK city councils, School Bus Boards and city councils in North America. The Group does not consider these counterparties to be a significant risk.

Financial instrument counterparties are subject to pre approval by the Board and it is Board policy to require institutions to have a credit rating of at least 'A' from an international rating agency.

Liquidity risk

The Group maintains committed bank facilities with core banks to provide prudent levels of borrowing headroom. At 31 March 2007, the total amount of committed facilities stood at £520m (2006 £527m). It is Group policy to maintain a minimum of £100m of committed borrowing headroom, to support financial flexibility. At 31 March 2007, committed borrowing headroom stood at £201.3m (2006 £211.0m) under the Group's £520m syndicated bank facility. This bank facility expires in March 2010.

Notes to the consolidated financial statements continued

25 Derivative financial instruments continued

The Group has an average debt duration at 31 March 2007 of 6.4 years (2006 7.8 years), principally provided by its two Sterling bonds, expiring in 2013 and 2019

26 Deferred tax

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

(Assets)/liabilities	Accelerated tax depreciation £m	Other temporary differences £m	Tax losses £m	Total £m
At 1 April 2005	134.3	(53.1)	(40.5)	40.7
Charge/(credit) to income	32.9	32.0	(21.6)	43.3
Charge to equity	–	2.6	–	2.6
Acquisition of subsidiary	–	(3.6)	–	(3.6)
Exchange differences	4.9	(0.3)	(3.0)	1.6
At 31 March 2006	172.1	(22.4)	(65.1)	84.6
Charge to income (note 10)	4.0	20.7	7.9	32.6
Charge to equity	–	30.4	–	30.4
Exchange differences	(11.0)	(1.1)	7.2	(4.9)
At 31 March 2007	165.1	27.6	(50.0)	142.7

At the balance sheet date, the aggregate amount of temporary differences associated with undistributed earnings of subsidiaries for which deferred tax liabilities have not been recognised was £177m (2006 £148m). No liability has been recognised in respect of these differences because the Group is in a position to control the timing of the reversal of the temporary difference and it is probable that such differences will not reverse in the foreseeable future.

It has been announced that the UK corporation tax rate is to reduce from 30% to 28% on 1 April 2008 and that Industrial Buildings Allowances will be abolished. These changes in tax law are not expected to be enacted until during the year ended 31 March 2009 and are expected to affect the carrying value of deferred tax at 31 March 2009. The effect of the reduction in the UK Corporation tax rate will be to reduce the deferred tax liability on UK temporary differences at 31 March 2009. The deferred tax liability on UK property will increase at 31 March 2009 because there will be a reduction in the tax base of property that would have qualified for Industrial Buildings Allowances prior to abolition.

No deferred tax asset has been recognised in respect of £10m (2006 £10m) of capital losses.

27 Provisions	Insurance claims ¹ £m	Pensions £m	Total £m
At 1 April 2006	30.7	6.9	37.6
Provided in the year	32.4	–	32.4
Utilised in the year	(39.2)	(0.6)	(39.8)
Notional interest	6.9	–	6.9
Exchange rate differences	(3.9)	–	(3.9)
At 31 March 2007	26.9	6.3	33.2

¹Insurance claims accruals due within one year at 31 March 2007 amounted to £44.0m (2006 £50.0m) and are included in 'accruals and deferred income' within note 20. The amount included within provisions above represents the estimate of amounts due after more than one year.

The insurance claims provision arises from estimated exposures for incidents occurring prior to balance sheet date. It is anticipated that the majority of such claims will be settled within the next six years.

The pension provision relates to certain unfunded obligations that arose on the acquisition of certain UK Bus companies. It is anticipated that this will be utilised over several decades.

	2007 £m	2006 £m
28 Called up share capital		
Authorised		
600 0m ordinary shares of 5p each ¹	30 0	30 0
Allotted, called up and fully paid		
438 3m (2006 398 8m) ordinary shares of 5p each	21 9	19 9
	No m	£m
At 1 April 2006	398 8	19 9
Equity share placing	39 5	2 0
At 31 March 2007	438 3	21 9

¹Subsequent to year end the authorised share capital was increased to 4 600m shares of 5p each or £230 0m

In February 2007 the Group issued 39 5m shares for gross proceeds of £221 4m 3,334,407 (2006 6,630,500) shares were being held as treasury shares at 31 March 2007

The Company has one class of ordinary shares which carry no right to fixed income

	Hedging reserve £m	Share premium account £m	Own shares £m	Retained earnings £m
29 Statement of changes in equity				
At 1 April 2005	37 0	238 8	(18 9)	(25 3)
Retained profit for the financial year	–	–	–	107 5
Dividends paid	–	–	–	(52 0)
Movement in EBT, QUEST and treasury shares during the year	–	–	(7 7)	(8 3)
Current tax on share based payments	–	–	–	1 8
Actuarial gains on defined benefit pension schemes	–	–	–	36 7
Deferred tax on actuarial gains on defined benefit pension schemes	–	–	–	(11 0)
Derivative hedging instrument movements	(43 2)	–	–	–
Deferred tax on derivative hedging instrument movements	8 1	–	–	–
Share based payments provision	–	–	–	3 2
Deferred tax on share based payments	–	–	–	0 3
At 31 March 2006	1 9	238 8	(26 6)	52 9
Retained profit for the financial year	–	–	–	91 7
Dividends paid	–	–	–	(57 1)
Premium arising on issue of equity shares	–	219 4	–	–
Expenses on issue of equity shares	–	(10 4)	–	–
Movement in EBT, QUEST and treasury shares during the year	–	–	9 2	(6 3)
Current tax on share based payments	–	–	–	1 5
Actuarial gains on defined benefit pension schemes	–	–	–	116 9
Deferred tax on actuarial gains on defined benefit pension schemes	–	–	–	(35 0)
Derivative hedging instrument movements	22 8	–	–	–
Deferred tax on derivative hedging instrument movements	2 0	–	–	–
Share based payments provision	–	–	–	3 2
Deferred tax on share based payments	–	–	–	2 6
At 31 March 2007	26 7	447 8	(17 4)	170 4

- the hedging reserve records the movement on designated hedging items
- the share premium account represents the premium on shares issued since 1999. The reserve is non distributable
- the own shares reserve represents the cost of shares in FirstGroup plc purchased in the market and either held as treasury shares or held in trust to satisfy the exercise of share options (see page 70)

Notes to the consolidated financial statements continued

29 Statement of changes in equity continued

Own shares

The number of own shares held by the Group at the end of the year was 4,318,925 (2006 6,759,709) FirstGroup plc ordinary shares of 5p each. Of these, 951,998 (2006 49,742) were held by the FirstGroup plc Employee Benefit Trust, 32,520 (2006 79,467) by the FirstGroup plc Qualifying Employee Share Ownership Trust and 3,334,407 (2006 6,630,500) were held as treasury shares. Both trusts and treasury shares have waived the rights to dividend income from the FirstGroup plc shares. The market value of the shares at 31 March 2007 was £28.7m (2006 £28.7m).

	Capital redemption reserve £m	Capital reserve £m	Total other reserves £m
At 31 March 2007 and 31 March 2006	1.9	2.7	4.6

There have been no movements on the capital redemption reserve or capital reserve during the year ended 31 March 2007.

- the capital redemption reserve represents the cumulative par value of all shares bought back and cancelled. The reserve is not distributable.
- the capital reserve arose on acquisitions in 2000. The reserve is not distributable.

30 Translation reserves

	£m
At 1 April 2005	(14.2)
Reclassify to hedging reserve on financial instrument recognition	(7.7)
Movement for the financial year	49.6
At 31 March 2006	27.7
Movement for the financial year	(85.5)
At 31 March 2007	(57.8)

- the translation reserve records exchange differences arising from the translation of the accounts of foreign currency denominated subsidiaries offset by movements on loans used to hedge the net investment in foreign subsidiaries.

	2007 £m	2006 £m
31 Acquisition of businesses and subsidiary undertakings		
Provisional fair values of net assets acquired		
Tangible assets	5.0	4.0
Intangible assets	7.1	4.3
Other current assets	0.1	–
Other creditors	(3.4)	(6.2)
	8.8	2.1
Goodwill (note 13)	9.1	10.3
	17.9	12.4
Satisfied by cash paid and payable	17.9	12.4

There was no material difference between the book value and the provisional fair values of the net assets acquired and there were no adjustments required in respect of accounting policy alignments. The intangible assets calculation is provisional and will be finalised during 2007/08.

The businesses and subsidiary undertakings acquired during the year contributed £5.1m (2006 £0.7m) to the Group's net operating cash flows. There were no other cash flow movements from the businesses acquired during the year or the previous year.

31 Acquisition of businesses and subsidiary undertakings continued

If the acquisition of the businesses and undertakings acquired during the year had been completed on the first day of the financial year, Group revenues from these acquisitions for the period would have been £22.0m (2006: £10.1m) and the Group operating profit from these acquisitions attributable to equity holders of the parent would have been £3.3m (2006: £1.6m)

The businesses acquired during the year contributed £10.3m to Group revenue and £2.5m to Group operating profit from date of acquisition to 31 March 2007

Due to the overall magnitude and similar profile of the acquisitions made during the year and the preceding year, the Directors have decided not to disclose the total cost and components of each individual combination separately

The goodwill represents the management relationships acquired and the reputation of the existing business

The businesses and subsidiary undertakings acquired during the year and dates of acquisition were

Business acquired	Date acquired	% Voting equity instruments acquired
Ladd Bus, Inc	30 June 2006	100
TNT Bus Services, Inc	27 July 2006	100
Earl D Stires Bus Company, Inc	28 July 2006	100
School Transportation Service, Inc	2 October 2006	100
Stout's Bus Service, Inc	1 November 2006	100
Cognisa Transportation, Inc	31 December 2006	100

32 Notes to the consolidated cash flow statement	2007 £m	2006 £m
Operating profit before (loss)/profit on disposal of fixed assets	207.3	196.7
Adjustments for		
Depreciation charges	139.7	122.0
Amortisation of intangible assets	10.3	4.5
Share based payments	3.2	3.2
Loss on disposal of plant and equipment	1.9	1.4
Operating cash flows before working capital	362.4	327.8
Increase in inventories	(8.8)	(9.6)
(Increase)/decrease in receivables	(25.8)	3.9
Increase/(decrease) in payables	40.1	(21.4)
Cash generated by operations	367.9	300.7
Corporation tax paid	(5.5)	(3.5)
Interest paid	(62.3)	(61.3)
Interest element of finance lease payments	(4.6)	(0.9)
Net cash from operating activities	295.5	235.0

Notes to the consolidated financial statements continued

33 Contingent liabilities

To support subsidiary undertakings in their normal course of business, the Company and certain subsidiaries have indemnified certain banks and insurance companies who have issued performance bonds for £264.1m (2006: £225.9m) and letters of credit for £123.6m (2006: £138.6m). The performance bonds relate to the North American businesses of £132.0m (2006: £135.7m) and the UK Rail franchise operations of £132.1m (2006: £90.2m). The letters of credit relate substantially to insurance arrangements in the UK and North America.

The Company has provided unsecured loan facilities of £103m (2006: £103m) to First Greater Western Limited, a £46m (2006: £46m) unsecured loan facility to First Capital Connect Limited, a £3.2m (2006: £3.2m) unsecured loan facility to First/Keolis TransPennine Limited, and a £13.6m (2006: £13.6m) unsecured loan facility to First ScotRail Limited. Under these facilities, £10m (2006: £nil) was drawn at 31 March 2007 by First Greater Western Limited. These facilities represent contingent liabilities of the Company in relation to these subsidiaries, but they do not represent contingent liabilities of the Group.

The Company is party to certain unsecured guarantees granted to banks for overdraft and cash management facilities provided to itself and subsidiary undertakings. The Company has given certain unsecured guarantees for the liabilities of its subsidiary undertakings arising under certain loan notes, hire purchase contracts, finance leases, operating leases, supply contracts and certain pension scheme arrangements. It also provides unsecured cross guarantees to certain subsidiary undertakings as required by VAT legislation. UK Bus subsidiaries have provided unsecured guarantees on a joint and several basis to the Trustees of the UK Bus Occupational Pension Scheme.

Certain of the Company's subsidiaries have issued unsecured guarantees to the Company's Sterling bondholders. These unsecured guarantees rank *pari passu* with unsecured guarantees provided by those subsidiaries to lenders participating in the Group's £520m (2006: £520m) syndicated unsecured bank facility.

34 Operating lease arrangements	2007 £m	2006 £m
Minimum lease payments made under operating leases recognised in the income statement for the year		
Plant and machinery	8.0	25.1
Track and station access	540.1	279.2
Hire of rolling stock	152.3	106.3
Other assets	20.1	19.9
	720.5	430.5

At the balance sheet dates, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2007 £m	2006 £m
Within one year	777.4	349.1
In the second to fifth years inclusive	2,727.9	1,307.6
After five years	402.4	252.8
	3,907.7	1,909.5

35 Share based payments

Equity settled share option plans

(a) Save as you earn (SAYE)

The Group operates an Inland Revenue approved savings related share option scheme. Grants were made in December 2002, December 2003, December 2004, April 2006 and December 2006. The scheme is based on eligible employees being granted options and their agreement to opening a sharesave account with a nominated savings carrier and to save weekly or monthly over a specified period. Sharesave accounts are held with Lloyds TSB. The right to exercise the option is at the employee's discretion at the end of the period previously chosen for a period of six months.

	SAYE 2002 Options No	SAYE 2003 Options No	SAYE 2004 Options No	SAYE April 2006 Options No	SAYE Dec 2006 Options No
Outstanding at the beginning of the year	343,812	1,193,778	2,469,178	–	–
Awarded during the year	–	–	–	1,996,187	2,478,422
Exercised during the year	(193,336)	(1,054,698)	(16,601)	(2,142)	–
Lapsed during the year	(150,476)	(36,134)	(156,790)	(112,252)	(22,934)
Outstanding at the end of the year	–	102,946	2,295,787	1,881,793	2,455,488
Exercisable at the end of the year	–	102,946	–	–	–
Weighted average exercise price (pence)	192.0	232.0	267.0	325.0	444.0
Weighted average share price at date of exercise (pence)	426.5	598.4	562.3	611.6	N/A

(b) Executive share option scheme (ESOS)

Options are exercisable between three and ten years of the date of grant provided that the pre-determined performance criteria are met.

	ESOS 2001 Options No	ESOS 2002 Options No	ESOS 2003 Options No	ESOS 2004 Options No
Outstanding at the beginning of the year	398,333	1,085,682	1,195,874	1,340,791
Forfeited during the year	–	–	(58,128)	(64,660)
Exercised during the year	(88,816)	(641,562)	(490,083)	–
Outstanding at the end of the year	309,517	444,120	647,663	1,276,131
Exercisable at the end of the year	309,517	444,120	647,663	–
Weighted average exercise price (pence)	346.5	269.0	287.0	275.1
Weighted average share price at date of exercise (pence)	467.9	466.2	562.0	N/A

(c) Deferred bonus shares (DBS)

	DBS 2003 Options No	DBS 2004 Options No	DBS 2005 Options No	DBS 2006 Options No
Outstanding at the beginning of the year	245,628	267,883	346,537	–
Granted during the year	–	–	–	714,576
Forfeited during the year	(182)	(2,077)	(28,039)	(45,301)
Exercised during the year	(245,446)	–	–	–
Outstanding at the end of the year	–	265,806	318,498	669,275
Exercisable at the end of the year	–	–	–	–
Weighted average exercise price (pence)	Nil	Nil	Nil	Nil
Weighted average share price at date of exercise (pence)	489.2	N/A	N/A	N/A

Notes to the consolidated financial statements continued

35 Share based payments continued

The fair values of the options granted during 2006/07 and 2005/06 were measured using a Black Scholes model. The inputs into the Black Scholes model were as follows:

	2007	2006
Weighted average share price (pence)		
DBS	402.0	326.0
SAYE April 2006	406.2	–
Dean Finch options	402.0	–
SAYE December 2006	555.0	–
Weighted average exercise price (pence)		
DBS	–	–
SAYE April 2006	325.0	–
Dean Finch options	–	–
SAYE December 2006	444.0	–
Expected volatility – all options	35%	35%
Expected life		
– Dean Finch options	5 years	–
– SAYE schemes	3 years	–
– Deferred share bonus plans	5 years	3 years
Risk free rate of interest		
– DBS	4.4%	4.99%
– SAYE April 2006	4.4%	–
– SAYE December 2006	5.0%	–
– Dean Finch options	4.4%	–
Expected dividend yield		
– DBS	4.5%	4.5%
– SAYE April 2006	4.5%	–
– SAYE December 2006	3.5%	–
– Dean Finch options	4.5%	–

Expected volatility was determined by calculating the historical volatility of the Group's share price over the previous five years. The expected life used in the model has been adjusted based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

Allowances have been made for the SAYE schemes for the fact that, amongst a group of recipients some are expected to leave before an entitlement vests. The accounting charge is then adjusted over the vesting period to take account of actual forfeitures, so although the total charge is unaffected by the pre-vesting forfeiture assumption, the timing of the recognition of the expense will be sensitive to it. Fair values for the SAYE include a 10% pre-vesting leaver assumption whereas the Executive and deferred share plans exclude any allowance for pre-vesting forfeitures.

The Group used the inputs noted above to measure the fair value of the new share options.

(d) Buy As You Earn (BAYE) scheme

BAYE enables eligible employees to purchase shares from their gross income. The Company provides two matching shares for every three shares bought by employees, subject to a maximum Company contribution of shares to the value of £20 per employee per month. If the shares are held in trust for five years or more, no income tax and national insurance will be payable. The matching shares will be forfeited if the corresponding partnership shares are removed from trust within three years of award.

At 31 March 2007 there were 6,609 (2006: 4,576) participants in the BAYE scheme who have cumulatively purchased 2,264,621 (2006: 1,781,489) shares with the Company contributing 679,416 (2006: 553,009) matching shares on a cumulative basis.

The Group recognised total expenses of £3.2m (2006: £3.2m) related to equity-settled share-based payment transactions.

35 Share based payments continued

(e) LTIP

Options still unexercised under the LTIP are as follows

	2007 No	2006 No	Award price (p)
Date of award			
3 July 2000	95,370	145,452	236 0

	2007 No	2006 No	Award price (p)
(f) Dean Finch options			
Awarded during the year	200,000	–	nil

The options have vesting conditions based on Group EPS targets being achieved and profit targets on the First Great Western franchise being achieved or exceeded

36 Retirement benefit schemes

Defined contribution schemes

The Group operates defined contribution retirement benefit schemes for all qualifying employees. The assets of the schemes are held separately from those of the Group in funds under the control of trustees. Where there are employees who leave the schemes prior to vesting fully in the contributions, the contributions payable by the Group are reduced by the amount of forfeited contributions.

The total cost charged to income of £3.1m (2006: £2.8m) represents contributions payable to these schemes by the Group at rates specified in the rules of the plans.

Defined benefit schemes

The Group operates or participates in a number of pension schemes which cover the majority of UK employees and certain North American employees. These are principally defined benefit schemes under which benefits provided are based on employees' number of years of service and either career average or final salary. The scope of benefits varies between schemes. The assets of the schemes are held in separately administered trusts which are managed independently of the Group's finances by investment managers appointed by the schemes' trustees.

The various defined benefit schemes include five UK Bus Division schemes where the subsidiary undertaking is a participating employer in a scheme operated by a local authority. These schemes are subject to relevant local government regulations. First Greater Western Limited, First Capital Connect Limited, First ScotRail Limited, GB Rail and TransPennine Express have sections in the Railways Pension Scheme (RPS), which is an industry wide arrangement. Under the terms of the RPS, any fund deficit or surplus is shared by the employer (60%) and the employees (40%).

At their last triennial valuations, the defined benefit schemes had funding levels between 76.0% and 99.6% (2006: 69.0% and 99.6%). The market value of the assets at 31 March 2007 for all defined benefit schemes totalled £2,507m (2006: £1,993m).

Contributions are paid to all defined benefit schemes in accordance with rates recommended by the schemes' actuaries. The valuations are made using the Projected Unit Credit Method.

The valuation assumptions used for accounting purposes have been made uniform to Group standards, as appropriate, when each scheme is actuarially valued.

	2007 %	2006 %	2005 %
Key assumptions used			
Discount rate	5.45	5.0	5.5
Expected return on scheme assets	7.5	7.3	7.6
Expected rate of salary increases	4.3	4.1	4.1
Inflation	2.8	2.6	2.6
Future pension increases	2.8	2.6	2.6

Notes to the consolidated financial statements continued

36 Retirement benefit schemes continued

Amounts recognised in income in respect of these defined benefit schemes are as follows

	2007 £m	2006 £m	2005 £m
Current service cost	75.2	53.4	46.1
Interest cost	102.0	89.0	80.0
Expected return on scheme assets	(140.5)	(107.6)	(87.9)
Interest on franchise adjustment	(1.0)	(2.3)	(1.5)
Past service cost	(13.2)	(16.6)	–
	22.5	15.9	36.7

Actuarial gains and losses have been reported in the statement of recognised income and expense

The actual return on scheme assets was £191.1m (2006 £348.0m)

The amount included in the balance sheet arising from the Group's obligations in respect of its defined benefit pension schemes is as follows

	2007 £m	2006 £m	2005 £m
Fair value of schemes' assets	2,506.7	1,992.6	1,578.4
Present value of defined benefit obligations	(2,488.5)	(2,193.8)	(1,881.8)
Rail franchise adjustment (60%)	2.2	38.3	41.7
Irrecoverable surplus	(6.8)	–	–
Adjustment for employee share of RPS deficits (40%)	10.2	30.9	40.6
Surplus/(deficits) in schemes	23.8	(132.0)	(221.1)
This amount is presented in the balance sheet as follows			
Non-current assets	57.1	–	–
Non-current liabilities	(33.3)	(132.0)	(221.1)
	23.8	(132.0)	(221.1)

Movements in the present value of defined benefit obligations (DBO) were as follows

	2007 £m	2006 £m	2005 £m
At 1 April	2,193.8	1,881.8	1,415.8
Cessation of rail franchises	(332.9)	–	–
New rail franchises	594.8	–	294.2
Group service cost	75.2	53.4	46.1
Group past service cost	(13.2)	(16.6)	–
Group interest cost	102.0	89.0	80.0
Employee share of change in DBO (not attributable to franchise adjustment)	53.5	73.6	45.0
Actuarial (gain)/loss	(133.6)	145.8	38.4
Benefit payments	(47.8)	(35.0)	(36.9)
Currency (gain)/loss	(3.3)	1.8	(0.8)
At 31 March	2,488.5	2,193.8	1,881.8

36 Retirement benefit schemes continued

Movements in the fair value of scheme assets were as follows

	2007 £m	2006 £m	2005 £m
At 1 April	1,992 6	1,578 4	1,137 0
Cessation of rail franchises	(289 5)	–	–
New rail franchises	524 0	–	246 6
Expected return on assets	140 5	107 6	87 9
Company contributions	95 3	68 3	54 8
Employee contributions	41 0	32 9	26 2
Employee share of return on assets	37 6	50 5	15 6
Gain on assets	15 8	188 7	47 6
Benefits paid from schemes	(47 8)	(35 0)	(36 9)
Currency (loss)/gain	(2 8)	1 2	(0 4)
At 31 March	2,506 7	1,992 6	1,578 4

Movements in the franchise adjustment were as follows

	2007 £m	2006 £m	2005 £m
At 1 April	63 9	69 2	31 9
Cessation of rail franchises	(43 4)	–	–
New rail franchises	11 7	–	16 3
Interest on franchise adjustment	1 0	2 3	1 5
Employee share of change in DBO (attributable to franchise adjustment)	(11 4)	(2 0)	8 3
Actuarial (loss)/gain on franchise adjustment	(18 1)	(5 6)	11 2
At 31 March	3 7	63 9	69 2

The analysis of the scheme assets and the expected rate of return at the balance sheet dates were as follows

	Expected return 2007 %	Fair value of assets 2007 £m	Expected return 2006 %	Fair value of assets 2006 £m	Expected return 2005 %	Fair value of assets 2005 £m
Equity instruments	8 45	1,756 9	8 35	1,444 8	8 8	1,094 4
Debt instruments	4 8	362 0	4 3	317 6	4 7	282 4
Property	6 3	256 2	6 3	135 9	6 8	121 8
Other assets	4 0	131 6	3 6	94 3	3 6	79 8
		2,506 7		1,992 6		1,578 4

The expected rates of return on assets at 31 March 2007, 31 March 2006 and 31 March 2005 were determined by looking at the individual asset classes and applying a model developed by Aon, an independent firm of Actuaries

Notes to the consolidated financial statements continued

36 Retirement benefit schemes continued

The history of experience adjustments is as follows

	2007 £m	2006 £m	2005 £m
Fair value of schemes' assets	2,506.7	1,992.6	1,578.4
Present value of defined benefit obligations	(2,488.5)	(2,193.8)	(1,881.8)
Rail franchise adjustment (60%)	2.2	38.3	41.7
Irrecoverable surplus	(6.8)	–	–
Adjustment for employee share of RPS deficits (40%)	10.2	30.9	40.6
Surplus/(deficits) in the schemes	23.8	(132.0)	(221.1)
Experience gain on scheme assets			
Amount (£m)	15.8	188.7	47.6
Percentage of scheme assets (%)	0.6	10.8	3.4
Experience gain on scheme liabilities			
Amount (£m)	12.4	13.6	15.5
Percentage of scheme liabilities (%)	0.5	0.7	0.8
Experience gain on scheme liabilities after franchise adjustment			
Amount (£m)	14.2	8.0	26.7
Percentage of scheme liabilities (%)	0.6	0.4	1.4

The estimated amounts of contributions expected to be paid to the schemes during the financial year to 31 March 2008 is £74.1m (year to 31 March 2007 £78.1m)

Accounting for UK Rail pension arrangements

The Group recognises its share of Train Operating Companies' deficits that the Group expects to fund over the term of the respective franchises. This is accounted for by way of a franchise adjustment.

Had the Group accounted for UK Rail pensions as if the respective franchises had an indefinite duration, the impact on the financial statements would have been as follows

	2007 £m	2006 £m	2005 £m
Balance sheet			
Pension deficit	(2.2)	(38.3)	(41.7)
Intangible assets	(43.6)	(16.5)	(19.4)
Deferred taxation	13.7	16.4	18.3
Impact on net assets	(32.1)	(38.4)	(42.8)
Income statement			
Unwinding of discount on franchise adjustment	(1.0)	(2.3)	(1.5)
Intangible asset amortisation	8.2	2.9	1.6
Deferred taxation	(2.2)	(0.2)	–
Impact on profit for the period from continuing operations	5.0	0.4	0.1
Statement of recognised income and expense			
Actuarial losses/(gains) on franchise adjustment	18.1	5.6	(11.2)

37 Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note

Remuneration of key management personnel

The remuneration of the Directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS 24 *Related Party Disclosures*. Further information about the remuneration of individual Directors is provided in the Directors' Remuneration Report on pages 31 to 37

	Year to 31 March 2007 £m	Year to 31 March 2006 £m
Basic salaries	1.3	1.2
Performance related bonuses	0.7	0.6
Benefits in kind	0.1	0.1
Fees	0.3	0.3
Pension contributions	0.2	0.2
Share based payment	0.5	0.4
	3.1	2.8

Independent auditors' report to the members of FirstGroup plc

We have audited the Group financial statements of FirstGroup plc for the year ended 31 March 2007 which comprise the Consolidated income statement, Consolidated statement of total recognised income and expense, Consolidated balance sheet, Consolidated cash flow statement and the related notes 1 to 37. These Group 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 individual Company financial statements of FirstGroup plc for the year ended 31 March 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 Group financial statements in accordance with applicable 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 and the part of the Directors' Remuneration Report described as having been audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We report to you whether in our opinion the information given in the Directors' report is consistent with the Group financial statements. 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 2003 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 statement on internal control covers all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report for the above year as described in the contents section and consider whether it is consistent with the Group financial statements. 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 further information outside the Annual Report.

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 and the part of the Directors' Remuneration Report described as having been audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the 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 and the part of the Directors' Remuneration Report described as having been audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Group financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

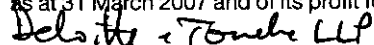
In our opinion

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 March 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,
- the part of the Directors' Remuneration Report described as having been audited has been properly prepared in accordance with the Companies Act 1985, and
- the information given in the Directors' report is consistent with the Group financial statements

Separate opinion in relation to IFRS

As explained in note 2 of the Group financial statements, the Group, in addition to complying with its legal obligation to comply with IFRSs as adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board

In our opinion the financial statements give a true and fair view, in accordance with IFRSs, of the state of the Group's affairs as at 31 March 2007 and of its profit for the year then ended



Deloitte & Touche LLP

Chartered Accountants and Registered Auditors

London

United Kingdom

15 May 2007

Group financial summary

	IFRS			UK GAAP	
	2007 £m	2006 £m	2005 £m	2004 £m	2003 £m
Consolidated income statement					
Group turnover	3,708.8	3,030.9	2,693.4	2,479.0	2,291.0
Operating profit before amortisation charges, non recurring bid costs and other non recurring items	259.2	229.7	214.8	204.1	216.1
Amortisation charges	(10.3)	(4.5)	(2.2)	(25.9)	(25.8)
Non recurring bid costs	(19.3)	(28.5)	(11.9)	(6.7)	(3.4)
Other non recurring items	(22.3)	–	–	(6.8)	(7.2)
Operating profit before (loss)/profit on disposal of fixed assets	207.3	196.7	200.7	164.7	179.7
Operating profit	203.6	210.7	204.0	184.3	189.7
Net finance charge	(63.4)	(53.3)	(48.3)	(42.8)	(56.3)
Exceptional interest charge	–	–	–	(18.7)	–
Profit before taxation	140.2	157.4	155.7	122.8	133.4
Taxation	(38.1)	(40.0)	(41.1)	(30.6)	(35.8)
Profit after taxation	102.1	117.4	114.6	92.2	97.6
EBITDA	398.9	351.7	322.4	307.1	315.3
Earnings per share					
	pence	pence	pence	pence	pence
Adjusted basic	33.7	30.9	28.9	27.3	26.8
Basic	23.1	27.4	27.1	22.3	23.4
Adjusted cash	68.6	61.9	55.8	52.4	50.6
Consolidated balance sheet					
	£m	£m	£m	£m	£m
Fixed assets	1,681.6	1,474.7	1,335.4	1,258.8	1,272.5
Net current assets/(liabilities)	70.0	(38.0)	(58.1)	(92.9)	(115.5)
Creditors' amounts due after more than one year	(968.4)	(982.6)	(977.4)	(682.8)	(630.9)
Provision for liabilities and charges	(175.9)	(122.2)	(75.4)	(128.1)	(124.0)
Equity minority interests	(11.1)	(12.7)	(10.6)	(2.1)	(1.1)
Equity shareholders' funds	596.2	319.2	213.9	352.9	401.0
Share data					
Number of shares in issue (excluding treasury shares and shares in trusts)	million	million	million	million	million
At year end	434.0	392.0	393.6	403.0	413.4
Average	397.9	392.6	399.2	410.0	416.7
Share price	pence	pence	pence	pence	pence
At year end	665	425	343	268	240
High	668	426	379	306	339
Low	381	311	256	219	200
Market capitalisation	£m	£m	£m	£m	£m
At year end	2,886	1,665	1,369	1,078	992

The amounts disclosed for 2004 and earlier periods are stated on the basis of UK GAAP because it is not practicable to restate amounts for periods prior to the date of transition to IFRSs

Company balance sheet

At 31 March 2007

	Notes	2007 £m	2006 restated ¹ £m
Fixed assets			
Investments	4	1,693 3	1,690 1
Current assets			
Financial assets – cash and cash equivalents		213 1	–
– derivative financial instruments	5	35 0	16 5
Debtors	6	973 1	895 6
		1,221 2	912 1
Creditors amounts falling due within one year	7	(699 7)	(666 5)
Financial liabilities – derivative financial instruments	5	(5 0)	(1 8)
– current bond liability		(23 1)	(23 1)
		(727 8)	(691 4)
Net current assets		493 4	220 7
Total assets less current liabilities		2,186 7	1,910 8
Creditors amounts falling due after more than one year	7	(847 6)	(823 4)
Financial liabilities – derivative financial instruments	5	(4 3)	(0 8)
Provisions for liabilities and charges		–	(0 1)
		1,334 8	1,086 5
Financed by			
Capital and reserves			
Called up share capital	8	21 9	19 9
Share premium account	9	447 8	238 8
Other reserves	9	262 1	261 5
Own shares	9	(17 4)	(26 6)
Profit and loss account	9	620 4	592 9
Equity shareholders' funds		1,334 8	1,086 5

¹ Restated on adoption of UITF 44 (see note 1)

Notes to the Company financial statements

1 Significant accounting policies

Basis of accounting

The following accounting policies have been used consistently throughout the year and the preceding year in accordance with UK GAAP with the exception of the adoption of UITF 44

Cash flow statement

The Company has taken the advantage of the exemption under FRS 1 (revised) not to disclose a cash flow statement

Investments

Fixed asset investments in subsidiaries and associates are shown at cost less provision for impairment

For investments in subsidiaries acquired for consideration, including the issue of shares qualifying for merger relief, cost is measured by reference to the nominal value only of the shares issued. Any premium is ignored

Foreign currencies

Transactions in currencies other than Sterling are recorded at the rate of exchange on the date of the transaction. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing at the relevant balance sheet date. Exchange differences arising on the settlement of monetary items, and on the retranslation of non-monetary items at each balance sheet date are included in the profit or loss for the accounting period

Taxation

The charge for taxation is based on the profit or loss for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Provision is made for deferred tax on all timing differences except those arising from the revaluation of fixed assets for which there is no binding agreement to sell on property gains if it is anticipated that rollover relief will be available and on the undistributed profits of overseas subsidiaries, associates and joint ventures. Deferred tax is calculated at the rates at which it is estimated the tax will arise. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. The deferred tax provision is not discounted to net present value

Financial instruments

From 1 April 2005 derivative financial instruments are initially recorded at fair value and then for reporting purposes are remeasured to fair value at each subsequent balance sheet date

Derivative financial instruments and hedge accounting

The Company uses derivative financial instruments to hedge interest rate risks, foreign currency risks and fuel price risks. Use of such financial instruments is governed by policies and delegated authorities approved by the Board. The Company does not use derivative financial instruments for speculative purposes

The main derivative financial instruments used by the Company are interest rate swaps and collars, fuel swaps and collars, and cross currency interest rate swaps. Such instruments are initially recognised at fair value and subsequently remeasured to fair value at the reported balance sheet date. The fair values are calculated by reference to market exchange rates, interest rates and fuel prices at the period end, and supported by counterparty confirmations

Changes in the fair value of derivative financial instruments that do not qualify for hedge accounting as cash flow hedges or foreign currency hedges of a foreign net investment are recognised in the profit or loss as they arise

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

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not carried at fair value with unrealised gains or losses reported in the income statement

Related party transactions

As permitted under FRS 8, *Related party transactions*, the Company has taken advantage of the exemption not to disclose transactions between Group companies

1 Significant accounting policies continued

Debt

Debt is initially stated at the amount of the net proceeds after the deduction of issue costs. The carrying amount is increased by the amortisation of debt issuance fees in respect of the accounting period and reduced by repayments made in the period.

Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

Change in accounting policy

The Company has adopted the requirements of UITF 44 *FRS 20 Group and Treasury Share Transactions* as the Company awards share options to employees working in different entities across the Group. The impact of this change in accounting policy is that both investments and retained profits are £6.1m higher at 31 March 2006 than previously stated.

2 Profit for the year

As permitted by section 230 of the Companies Act 1985 the Company has elected not to present its own profit and loss account for the year. FirstGroup plc reported a profit for the financial year ended 31 March 2007 of £85.4m (2006: profit of £15.5m).

The auditors' remuneration for audit services to the Company was £0.1m (2006: £0.1m).

The Company had no employees in the current or preceding financial year.

3 Dividends

Amounts recognised as distributions to equity holders in the year

	2007 £m	2006 £m
Final dividend for the year ended 31 March 2006 of 9.55p (2005: 8.69p) per share	37.5	34.1
Interim dividend for the year ended 31 March 2007 of 5.0p (2006: 4.55p) per share	19.6	17.9
	57.1	52.0
Proposed final dividend for the year ended 31 March 2007 of 10.5p (2006: 9.55p) per share	45.6	37.5

The proposed final dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements.

	Unlisted subsidiary undertakings £m	Other investments £m	Total £m
4 Fixed asset investments			
Cost			
At 31 March 2006 as previously stated	1,689.4	8.1	1,697.5
Prior year adjustment on adoption of UITF 44	6.1	–	6.1
At 31 March 2006 as restated	1,695.5	8.1	1,703.6
Additions	3.2	–	3.2
At 31 March 2007	1,698.7	8.1	1,706.8
Provisions			
At 1 April 2006 and 31 March 2007	(5.4)	(8.1)	(13.5)
Net book value			
At 31 March 2007	1,693.3	–	1,693.3
At 31 March 2006	1,690.1	–	1,690.1

Notes to the Company financial statements continued

4 Fixed asset investments continued

Subsidiary undertakings

The principal subsidiary undertakings of FirstGroup plc at the end of the year were

UK local bus and coach operators

CentreWest London Buses Limited
First Aberdeen Limited+
First Beeline Buses Limited
First Bristol Limited
First Capital East Limited
First Capital North Limited
First Somerset & Avon Limited
First Cymru Buses Limited
First Eastern Counties Buses Limited
First Edinburgh Limited+
First Essex Buses Limited
First Glasgow (No 1) Limited+
First Glasgow (No 2) Limited+
First Hampshire and Dorset Limited
First Manchester Limited

First Midland Red Buses Limited
First PMT Limited
First South Yorkshire Limited
First Wessex Limited
First West Yorkshire Limited
First Devon & Cornwall Limited
First York Limited
Leicester CityBus Limited (94%)
Northampton Transport Limited

North America school bus operators

First Student, Inc†
FirstBus Canada Limited‡
FirstGroup America, Inc†
FirstGroup USA, Inc†
Cardinal Transportation Group, Inc†
Cardinal Coach Lines Limited‡ (60%)

Transit contracting and fleet maintenance

First Transit, Inc†
SKE Support Services, Inc†

Rail companies

First Capital Connect Limited
First Greater Western Limited
FirstInfo Limited
First/Keolis TransPennine Limited (55%)
Hull Trains Company Limited (80%)
GB Railfreight Limited
First ScotRail Limited

All subsidiary undertakings are wholly owned at the end of the year except where percentage of ownership is shown above
All these companies above are incorporated in Great Britain and registered in England and Wales except those marked + which are registered in Scotland, those marked † which are incorporated in the United States of America and those marked ‡ which are registered in Canada

All shares held in subsidiary undertakings are ordinary shares, with the exception of Leicester CityBus Limited where the Group owns 100% of its redeemable cumulative preference shares, as well as 94% of its ordinary shares

All of these subsidiary undertakings are owned via intermediate holding companies

Advantage has been taken of section 231(5) of the Companies Act 1985 to list only those undertakings as are required to be mentioned in that provision, as an exhaustive list would involve a statement of excessive length

Other investments

The interest in other investments at the end of the year is a 6% interest in the ordinary share capital of Prepayment Cards Limited, which is incorporated in Great Britain and registered in England and Wales

5 Derivative financial instruments	2007 £m	2006 £m
Non current assets		
Cross currency swaps (net investment hedge)	24.9	–
Coupon swaps (fair value hedge)	–	8.1
Interest rate collars (cash flow hedge)	–	0.4
Fuel derivatives (cash flow hedge)	2.8	–
	27.7	8.5
Current assets		
Cross currency swaps (net investment hedge)	2.9	–
Coupon swaps (fair value hedge)	1.2	3.3
Fuel derivatives (cash flow hedge)	3.2	4.7
	7.3	8.0
Total assets	35.0	16.5
Current liabilities		
Interest rate swaps (cash flow hedge)	0.3	0.9
Cross currency swaps (net investment hedge)	–	0.9
Fuel derivatives (cash flow hedge)	1.4	–
Currency forwards (cash flow hedge)	3.3	–
	5.0	1.8
Non current liabilities		
Interest rate swaps (cash flow hedge)	–	0.4
Cross currency swaps (net investment hedge)	–	0.4
Interest rate collars (cash flow hedge)	0.2	–
Coupon swaps (fair value hedge)	4.1	–
	4.3	0.8
Total liabilities	9.3	2.6

The Company has taken advantage of the exemption under FRS 25 for parent company accounts

The disclosures are included within the Group accounts

6 Debtors	2007 £m	2006 £m
Amounts due within one year		
Amounts due from subsidiary undertakings	972.6	895.6
Deferred tax asset	0.5	–
	973.1	895.6
7 Creditors	2007 £m	2006 £m
Amounts due within one year		
Bank loans and overdrafts	161.2	175.7
Loan notes	5.2	1.3
Corporation tax	2.3	3.5
Other creditors	0.8	0.3
Amounts due to subsidiary undertakings	526.1	478.5
Accruals and deferred income	4.1	7.2
	699.7	666.5

Notes to the Company financial statements continued

7 Creditors continued	2007 £m	2006 £m
Amounts falling due after more than one year		
Bank loans		
– Due in more than two years but not more than five years	308.3	264.9
Loan notes		
– Due in more than one year but not more than two years	–	5.3
£300.0m Sterling bond – 6.875% 2013	296.3	295.9
£250.0m bond – 6.125% 2019	243.0	257.3
	847.6	823.4

Borrowing facilities

The maturity profile of the Company's undrawn committed borrowing facilities is as follows

Facilities maturing	2007 £m	2006 £m
More than two years	201.0	202.6

8 Called up share capital	2007 £m	2006 £m
Authorised		
600.0m ordinary shares of 5p each ¹	30.0	30.0
Allotted, called up and fully paid		
Ordinary shares of 5p each	21.9	19.9

¹ Subsequent to year end the authorised share capital was increased to 4,600m shares of 5p each or £230.0m

The Company had 438.3m (2006 398.8m) shares in issue at 31 March 2007 including 3,334,407 (2006 6,630,500) shares held as treasury shares at this date. During the year 39.5m shares were allotted with a nominal value of £2.0m for a gross consideration of £221m.

9 Reserves	Share premium account £m	Own shares £m	Profit and loss account £m
At 31 March 2006 as previously stated	238.8	(26.6)	586.8
Prior year adjustment on adoption of UITF 44	–	–	6.1
At 31 March 2006 as restated	238.8	(26.6)	592.9
Retained profit for the year	–	–	85.4
Dividends paid	–	–	(57.1)
Share based provision	–	–	3.2
Premium arising on issue of equity shares	219.4	–	–
Expenses on issue of equity shares	(10.4)	–	–
Movement in EBT, QUEST and treasury shares during the year	–	9.2	(6.3)
Foreign exchange differences	–	–	2.3
At 31 March 2007	447.8	(17.4)	620.4

Own shares

The number of own shares held by the Group at the end of the year was 4,318,925 (2006 6,759,709) FirstGroup plc ordinary shares of 5p each. Of these, 951,998 (2006 49,742) were held by the FirstGroup plc Employee Benefit Trust, 32,520 (2006 79,467) by the FirstGroup plc Qualifying Employee Share Ownership Trust and 3,334,407 (2006 6,630,500) were held as treasury shares. Both trusts and treasury shares have waived the rights to dividend income from the FirstGroup plc shares. The market value of the shares at 31 March 2007 was £28.7m (2006 £28.7m).

9 Reserves continued	Hedging reserve £m	Capital redemption reserve £m	Capital reserve £m	Merger reserve £m	Total other reserves £m
At 1 April 2006	(0.6)	1.9	93.8	166.4	261.5
Derivative hedging instrument movement	0.6	–	–	–	0.6
At 31 March 2007	–	1.9	93.8	166.4	262.1

10 Reconciliation of movement in equity shareholders' funds	2007 £m	2006 restated £m
Profit for the financial year	85.4	15.5
Dividends	(57.1)	(52.0)
	28.3	(36.5)
Share based provision	3.2	3.2
Issue of equity shares	211.0	–
Movement in EBT, QUEST and treasury shares during the year	2.9	(16.1)
Derivative hedging instrument movement	0.6	30.9
Foreign exchange differences	2.3	(1.2)
Net addition to/(reduction in) equity shareholders' funds	248.3	(19.7)
Equity shareholders' funds at beginning of year (as previously reported)	1,086.5	1,103.3
Prior year adjustment	–	2.9
Equity shareholders' funds at beginning of year (restated)	1,086.5	1,106.2
Equity shareholders' funds at end of year	1,334.8	1,086.5

11 Contingent liabilities

To support subsidiary undertakings in their normal course of business, the Company and certain subsidiaries have indemnified certain banks and insurance companies who have issued performance bonds for £264.1m (2006 £225.9m) and letters of credit for £123.6m (2006 £138.6m). The performance bonds relate to the North American businesses of £132.0m (2006 £135.7m) and the UK Rail franchise operations of £132.1m (2006 £90.2m). The letters of credit relate substantially to insurance arrangements in the UK and North America.

The Company has provided unsecured loan facilities of £103m (2006 £103m) to First Greater Western Limited, a £46m (2006 £46m) unsecured loan facility to First Capital Connect Limited, a £3.2m (2006 £3.2m) unsecured loan facility to First/Keolis TransPennine Limited, and a £13.6m (2006 £13.6m) unsecured loan facility to First ScotRail Limited. Under these facilities, £10m (2006 £nil) was drawn at 31 March 2007 by First Greater Western Limited.

The Company is party to certain unsecured guarantees granted to banks for overdraft and cash management facilities provided to itself and subsidiary undertakings. The Company has given certain unsecured guarantees for the liabilities of its subsidiary undertakings arising under certain loan notes, hire purchase contracts, finance leases, operating leases, supply contracts and certain pension scheme arrangements. It also provides unsecured cross guarantees to certain subsidiary undertakings as required by VAT legislation. UK Bus subsidiaries have provided unsecured guarantees on a joint and several basis to the Trustees of the UK Bus Occupational Pension Scheme.

Certain of the Company's subsidiaries have issued unsecured guarantees to the Company's Sterling bondholders. These unsecured guarantees rank pari passu with unsecured guarantees provided by those subsidiaries to lenders participating in the Group's £520m (2006 £520m) syndicated unsecured bank facility.

Independent auditors' report to the members of FirstGroup plc

We have audited the individual Company financial statements of FirstGroup plc for the year ended 31 March 2007 which comprise balance sheet and the related notes 1 to 11. These parent company financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the Group financial statements of FirstGroup plc for the year ended 31 March 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, the Directors' Remuneration Report and the parent company financial statements in accordance with applicable law and United Kingdom 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 have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the Directors' Report is consistent with the parent company financial statements. 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 the other information contained in the Annual Report as described in the contents section and consider whether it is consistent with the audited parent company financial statements. 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 further information outside the Annual Report.

Basis of audit opinion

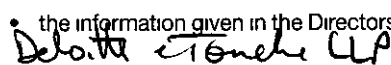
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent company financial statements. It also includes an assessment 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 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.

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 March 2007,
- the parent company financial statements 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.



Deloitte & Touche LLP

Chartered Accountants and Registered Auditors

London

United Kingdom

15 May 2007

Shareholder information

Shareholder enquires

The Company's share register is maintained on our behalf by Lloyds TSB Registrars, who are responsible for making dividend payments and updating the register, including details of changes to shareholders' addresses and purchases and sales of the Company's shares. If you have any questions about your shareholding in the Company or need to notify any changes to your personal details you should contact Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA
Telephone 0870 600 3973

Employees with queries about shares held in the Company's employee share schemes should contact Lloyds TSB Registrars at the same address or by telephoning 0870 241 3938

Duplicate shareholder accounts

If you receive more than one copy of Company mailings this may indicate that more than one account is held in your name on the Register. This happens when the registration details of separate transactions differ slightly. If you believe more than one account exists in your name you may contact the Registrars to request that the accounts are combined. There is no charge for this service.

Direct dividend payments

If you would like your dividend to be paid directly into your bank or building society account, you should contact the Registrars or complete the dividend mandate attached to your dividend cheque. Mandating your dividends has a number of advantages. Firstly, the dividend will go into your account on the payment date – there is no chance of it being delayed in the post and you do not have to wait for a cheque to clear. Secondly, the payment method is more secure than receiving a cheque through the post. Thirdly, you still receive tax information about the dividend, which is sent direct to you at your registered address.

Online information

The Registrars also provide an online service enabling you to access details of your shareholding. To view your details and a range of general information about holding shares, visit www.shareview.co.uk

FirstGroup policy on discounts for shareholders

Shareholders are reminded that it is not Group policy to offer travel or other discounts to shareholders, as they may be used only by a small number of individuals. The Group would rather maximise dividends, which are of benefit to all shareholders.

Unsolicited mail

As the Company's share register is, by law, open to public inspection, shareholders may receive unsolicited mail from organisations that use it as a mailing list. To limit the amount of unsolicited mail you receive, write to the Mailing Preference Society, FREEPOST 22, London W1E 7EZ or register online at www.mpsonline.org.uk

Shareholder profile

At 30 April 2007	Number of holders	%	Shares held	%
By category				
Individuals	40,940	95.1	50,287,933	11.5
Banks and nominees	1,995	4.5	374,619,736	85.5
Insurance and assurance	2	–	10,300	–
Other companies	231	0.4	13,353,781	3.0
Other institutions	3	–	7,048	–
	43,171	100.0	438,278,798	100.0
By size of holding				
1-1,000	33,421	77.4	8,440,454	1.9
1,001-5,000	7,450	17.3	16,374,349	3.7
5,001-10,000	1,176	2.7	8,164,944	1.9
10,001-100,000	805	1.9	22,791,185	5.2
Over 100,000	319	0.7	382,507,866	87.3
	43,171	100.0	438,278,798	100.0

Financial calendar

Annual General Meeting	12 July 2007
Shares trade ex dividend	18 July 2007
Record date for final dividend*	20 July 2007
Final dividend payment	24 August 2007
Interim results announced	November 2007
Interim dividend paid	February 2008
Preliminary announcement of full year results	May 2008

*Shareholders recorded on the register at this date will receive the final dividend

Designed by Pauffley

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