Significant Accounting Policies

Applicable to the Consolidated Financial Statements for the year ended 31 December 2005

Basis of preparation

From 1 January 2005, the Group is required to prepare Consolidated Financial Statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union. The Group previously prepared Consolidated Financial Statements in accordance with UK GAAP until 31 December 2004.

Details with respect to the Group's transition from UK GAAP to IFRS, including accounting policies used, reconciliations and descriptions of the effect of the transition on the Group's net income, equity and cash flows are provided in Notes 45 and 46.

The basis of accounting and format of presentation is subject to change following any further interpretative guidance that may be issued by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC") from time to time. The European Commission has not yet endorsed all of the recent amendments to the Standards or recent Interpretations. In particular, the amendments contained in IAS 21 (revised), The Effects of Changes in Foreign Exchange Rates recently approved by the IASB has not been applied pending endorsement by the European Commission (see below).

Additionally, IFRS is being applied in the United Kingdom and in a large number of countries simultaneously for the first time. Furthermore, due to a number of new and revised standards included within the body of standards that comprise IFRS, there is not yet a significant body of established practice on which to draw in forming options regarding interpretation and application. Accordingly, practice is continuing to evolve.

The Consolidated Financial Statements have been prepared on the historical cost basis, except for the revaluation of certain financial instruments, and have been prepared in accordance with the accounting policies set out below.

These policies have been consistently applied to all the periods presented except for those relating to the classification and measurement of financial instruments. The Group has made use of the exemption under IFRS 1, First Time Adoption of International Financial Reporting Standards, to only apply IAS 32, Financial Instruments: Disclosure and Presentation, and IAS 39, Financial Instruments: Recognition and Measurement, with effect from 1 January 2005. The policies applied to the Consolidated Financial Statements for 2004 and 2005 are disclosed separately below.

The impact of the implementation of IAS 32 and IAS 39 on equity as at 1 January 2005 is provided in Note 47.

The Group has also elected to early adopt IAS 19 (Amendment), Employee Benefits. This amendment introduces the option for actuarial gains and losses on retirement benefit obligations to be recognised in full in the statement of recognised income and expense in the period in which they occur. The Group has applied this option in the Consolidated Financial Statements for both the year ended 31 December 2005 and the comparative period.

Standards, interpretations and amendments to published standards that are not yet effective

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2006 or later periods but which the Group has not early adopted, as follows:

IAS 21 (Amendment), The Effects of Changes in Foreign Exchange Rates (effective from 1 January 2006)

The revised IAS 21 includes additional guidance explaining that the net investment definition includes loans between sister companies. The amended IAS 21 also permits intercompany items denominated in any currency to be part of a net investment in a foreign operation. Previously such loans had to be denominated in the currency of a party to the transaction. The Group has not been able to early adopt this amendment, as the amended standard had not been endorsed by the European Commission prior to the approval of the 2005 Consolidated Financial Statements. Had the revisions to IAS 21 been applied, most of the foreign exchange on net debt recognised in the income statement for the years ended 31 December 2005 and 31 December 2004, would have instead been recognised in the statement of recognised income and expense.

IAS 39 (Amendment), Cash Flow Hedge Accounting of Forecast Intra-group Transactions (effective from 1 January 2006)

The amendment allows the foreign currency risk of a highly probable forecast intra-group transaction to qualify as a hedged item in the Consolidated Financial Statements, provided that:
(a) the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction; and
(b) the foreign currency risk will affect consolidated profit or loss.
This amendment is not relevant to the Group's operations, as the Group does not have any intra-group transactions that would qualify as a hedged item in the Consolidated Financial Statements as of 31 December 2005 and 31 December 2004.

IAS 39 (Amendment), The Fair Value Option (effective from 1 January 2006)

This amendment changes the definition of financial instruments classified at fair value through profit or loss and restricts the ability to designate financial instruments as part of this category. The Group believes that this amendment should not have a significant impact on the classification of the Group's financial instruments.

IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts (effective from 1 January 2006)

This amendment requires issued financial guarantees, other than those previously asserted by the entity to be insurance contracts, to be initially recognised at their fair value and subsequently measured at the higher of: (a) the unamortised balance of the related fees received and deferred; and (b) the expenditure required to settle the commitment at the balance sheet date. Management considered this amendment to IAS 39 and concluded that it is not relevant to the Group.

IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective from 1 January 2007)

IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and disclosure requirements in IAS 32, Financial Instruments:

Disclosure and Presentation. It is applicable to all entities that report under IFRS. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Group assessed the impact of IFRS 7 and the amendment to IAS 1 and concluded that the main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1. The Group will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

IFRIC 4, Determining whether an Arrangement contains a Lease (effective from 1 January 2006)
IFRIC 4 requires the determination of whether an arrangement is or contains a lease to be based on the substance of the arrangement. It requires an assessment of whether: (a) fulfilment of the arrangement is dependent on the use of a specific asset or assets (the asset); and (b) the arrangement conveys a right to use the asset. Management is currently assessing the impact of IFRIC 4 on the Group's operations, but does not expect this to affect how the Group currently classifies its leasing arrangements.

IFRIC 8, Scope of IFRS 2 (effective from 1 May 2006)
IFRIC 8 is not relevant to the Group's operations as the only share-based payments issued by the Group are in relation to employee services which are already accounted for in accordance with IFRS 2.

Other
The following standards and interpretations have also been issued, but all are deemed not relevant to the Group's operations:

a) IFRS 1 (Amendment), First-time Adoption of International Financial Reporting Standards (effective from 1 January 2006).

b) IFRS 6, Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006).

c) IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from 1 January 2006).

d) IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment (effective from 1 December 2005).

e) IFRIC 7, Financial Reporting in Hyperinflationary Countries (effective from 1 March 2006).

Functional currency
The Company's functional currency is sterling. As a significant proportion of the Group's revenues, costs, assets and funding arise in euro, the Consolidated Financial Statements of the Group are presented in euro. The Parent Company's Financial Statements are presented in sterling.

Basis of consolidation
The Consolidated Financial Statements comprise a consolidation of the accounts of the Company and its subsidiary undertakings.

The accounting reference dates of certain of the Group's subsidiary undertakings and its associated undertaking are governed by local requirements and are not coterminous with the Group's 31 December year end. For those companies with non-coterminous year ends, management accounts for the relevant period to 31 December have been consolidated. The main subsidiary undertakings with such non-coterminous year ends are Avis Location de Voitures sas and Avis Autonoleggio SpA. In the opinion of the Directors, the expense of providing additional coterminous statutory accounts, together with consequential delay in producing the Consolidated Financial Statements, would outweigh any benefit to the shareholders.

Subsidiary undertakings
Subsidiary undertakings are those entities in which the Group has, directly or indirectly, an interest of more than half of the voting rights or otherwise has the power to exercise control over the operations, are consolidated. Subsidiaries are consolidated from the date that control is transferred to the Group and are no longer consolidated from the date that control ceases. All inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated upon consolidation.

Joint ventures
Interests in jointly controlled entities (including joint ventures) are recognised using the equity method. Unrealised gains and losses on transactions between the Group and its joint ventures are eliminated to the extent of the Group's interest in the joint ventures. The Group's investment in joint ventures includes goodwill on acquisition. The Group's share of profit from joint ventures represents the Group's share of the joint venture's profit after tax. If the Group's share of losses in a joint venture equals or exceeds its investment in the joint venture, the Group does not recognise further losses unless it has incurred obligations or made payments on behalf of the joint venture.

Associate undertaking
Investments in the associate undertaking are accounted for using the equity method. This is an undertaking over which the Group has significant influence but not control, generally accompanied by a share of between 20% and 50% of the voting rights. The Group's share of profit from the associate represents the Group's share of the associate's profit after tax.

Underlying measures
In addition to the reported profit and earnings per share, the Group also discloses underlying performance measures, including underlying profit and underlying earnings per share. The Group believes that these underlying performance measures provide additional useful information on underlying trends to shareholders. The term "underlying" is not defined under IFRS, and may therefore not be comparable with similarly titled profit measurements reported by other companies. It is not intended to be a substitute for, or superior to, IFRS measures of profit.

Underlying measures are calculated based on reported profit before exceptional items, certain re-measurement items and adjustments to reflect the realised gains and losses on foreign exchange forward contracts and accrued interest cash flows on any financial instruments (economic hedge adjustments).

Exceptional items
Exceptional items are material non-recurring items that derive from events or transactions that fall within the ordinary activities of the Group, and which individually or, if of a similar type, in aggregate, are separately disclosed by virtue of their size or incidence.

Significant Accounting Policies *continued*

Applicable to the Consolidated Financial Statements for the year ended 31 December 2005

Certain re-measurement items
Items that represent the certain re-measurement of underlying assets or liabilities (for example due to interest rate or exchange rate changes) are presented as certain re-measurement items. Events which may give rise to the classification of these certain re-measurement items include the following:

a) Recognised fair value gains and losses on derivatives in accordance with the financial instruments and hedge accounting policy below.

b) Exchange gains and losses arising upon the translation of foreign currency borrowings at the closing rate.

c) Actuarial gains and losses arising on defined benefit retirement benefit schemes.

Economic hedge adjustments
Under IAS 39, the Group applies hedge accounting to hedge relationships (primarily forward exchange contracts, cross currency interest rate swaps, interest rate swaps and forward exchange contracts) where it is permissible and practicable to do so. Due to the nature of its economic hedging relationships, in a number of circumstances the Group is unable to apply hedge accounting to these derivatives. The Group continues, however, to enter into these arrangements as they provide certainty of the exchange rates applying to the foreign currency transactions entered into by the Group and the interest rate on the Group's debt. These arrangements result in fixed and determined cash flows. The Group believes that these arrangements remain effective economic and commercial hedges, and therefore adjustment is made to reported profit measures such that underlying profit reflects full application of hedge accounting.

Segment reporting
The Group's primary reporting format is business segments and its secondary format is geographical segments. A business segment is a component of the Group that is engaged in providing a group of related products and services, and is subject to risks and returns that are different from those other business segments. A geographical segment is a component of the Group that operates within a particular economic environment and this is subject to risks and returns that are different from those of components operating in other economic environments.

Revenue
Revenue includes vehicle rental income, fees from the provision of services incidental to vehicle rental, and fees receivable from licensees, net of discounts and excluding inter-company sales, value added and sales taxes.

When the outcome of a transaction involving the rendering of services can be estimated reliably, revenue associated with the transaction is recognised by reference to the stage of completion of the transaction at the balance sheet date. The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

a) the amount of revenue can be measured reliably;

b) it is probable that the economic benefits associated with the transaction will flow to the Group;

c) the stage of completion of the transaction at the balance sheet date can be measured reliably; and

d) the cost incurred for the transaction and the costs to complete the transaction can be measured reliably.

Cost of sales
Cost of sales includes selling, revenue related costs (e.g. commissions and credit card fees) and vehicle costs. Contributions to vehicle costs from suppliers are credited over the holding period of the related vehicles. Any such contributions dependent on performance criteria are recognised in the income statement only to the extent that it is considered probable that the criteria will be met.

Finance costs
Finance costs are recognised as an expense in the period in which they are incurred.

Share-based payments
Share-based payments are exclusively made in connection with employee stock option plans ("ESOPs").

IFRS 2, Share-Based Payment, is not applied to shares, share options or other equity instruments that were granted before or on 7 November 2002 and which had not vested at 1 January 2005. Equity-settled ESOPs granted after that date are accounted for in accordance with IFRS 2, such that the fair value of the employee service received in exchange for the grant of the option is recognised in the income statement over the related performance period. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example profitability growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the Group revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates in the income statement, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium when the options are exercised.

Goodwill
Business combinations are accounted for by applying the purchase method. The excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities, recognised in accordance with IFRS 3, Business Combinations, constitutes goodwill, and is recognised as an asset. Where this excess is negative, it is recognised immediately in the income statement. Goodwill on acquisition of subsidiaries is included in "Goodwill". Goodwill on acquisition of associates and joint ventures is included in "Investments accounted for using equity method".

After initial recognition, goodwill is measured at cost less any accumulated impairment losses, until disposal or termination of the previously acquired business (including planned disposal or termination where there are indications that the value of the goodwill has been permanently impaired), when the profit or loss

on disposal or termination will be calculated after charging the book amount, at current exchange rates, of any such goodwill through the income statement. Goodwill is tested for impairment at least annually, and whenever there are indications that goodwill may have become impaired. Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or group of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

Goodwill arising on acquisitions before 1 January 2004, the date of transition to International Financial Reporting Standards, has been retained at the previous UK GAAP amounts, subject to being tested for impairment at that date. The Group's policy up to and including 28 February 1998 was to eliminate goodwill arising upon acquisitions to reserves. Under IFRS 1 and IFRS 3, such goodwill will remain eliminated against reserves and is not included in determining any subsequent profit or loss on disposal.

Other intangible assets

Other intangible assets are valued at cost less any accumulated amortisation and any accumulated impairment losses. Costs that are directly associated with identifiable and unique software products controlled by the Group and which have probable economic benefits exceeding the cost beyond one year, are recognised as intangible assets. Computer software programmes are amortised on a straight-line basis over periods varying between two and five years.

Vehicles

Vehicles are initially measured at cost. This cost comprises its purchase price (including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates), plus any costs directly attributable to bringing the vehicle to the location and condition necessary for it to be capable of operating. After initial recognition, the vehicle is carried at its cost less any accumulated depreciation and any accumulated impairment losses. Straight-line depreciation is based on initial cost, after consideration of their expected holding periods and estimates of residual values. Where the carrying amount of a vehicle is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Recoverable amount is the higher of fair value less costs to sell and value in use.

Other property, plant and equipment

Other property, plant and equipment is initially measured at cost. This cost comprises its purchase price (including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates), plus any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating. If applicable, initial estimates of the cost of dismantling and removing the item and restoring the site are also included in the cost of the item.

After initial recognition, the fixed assets are carried at cost less any accumulated depreciation and any accumulated impairment losses. The depreciable amount of the item is allocated according to the straight-line method over its useful economic life. The main useful lives are as follows:

a) Buildings:	40 to 50 years;
b) Plant and equipment:	3 to 15 years;
c) IT equipment:	2 to 7 years;
d) Leased assets:	depending on the length of the lease.

Where the carrying amount of a fixed asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Recoverable amount is the higher of fair value less costs to sell and value in use and is determined for an individual asset.

Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases.

Operating leases for which the Group is the lessor

Rental income is recognised on a straight-line basis over the lease term. Unless the vehicles themselves are held under operating leases for which the Group is the lessee, vehicles leased out under operating leases are included in vehicles in the balance sheet. They are depreciated over their expected useful lives.

Operating leases for which the Group is the lessee

Lease payments under operating leases are recognised as expenses in the income statement on a straight-line basis over the lease term.

Vehicles subject to manufacturer re-purchase agreements

Vehicles subject to manufacturer re-purchase agreements are not recognised as non-current assets since these arrangements are accounted for as operating leases (lessee accounting). The difference between the initial payment and the final re-purchase price (the obligation of the manufacturer) is considered as a deferred charge and is classified as prepaid vehicle operating lease charges within trade and other receivables. At inception of the arrangement, a separate re-purchase agreement receivable is also recognised within trade and other receivables for the final re-purchase price.

Finance leases for which the Group is the lessee

Leases of vehicles (including vehicles subject to manufacturer re-purchase arrangements), other property, plant and equipment, where the Group has substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased property or the present value of the minimum lease payments. Each lease payment is allocated between the liability and the finance charge so as to achieve a constant rate of return on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in interest-bearing liabilities. The interest element of the finance cost is charged to the income statement over the lease period. The leased assets are depreciated over their expected useful lives on a basis consistent with similar owned vehicles or other property, plant and equipment. If there is no reasonable certainty that ownership will be acquired by the end of the lease term, the asset is depreciated over the shorter of the lease term and its useful life.

Significant Accounting Policies *continued*

Applicable to the Consolidated Financial Statements for the year ended 31 December 2005

Non-current assets held for sale
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 met when the sale is highly probable, the asset is available for immediate sale in its present condition, management are committed to the asset disposal, and disposal is expected to be completed within 12 months. Non-current assets classified as held for sale cease to be depreciated and are measured at the lower of carrying amount and fair value less selling costs.

Inventories
Inventories are measured at the lower of cost and net realisable value. The cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their location and condition at the balance sheet date. Items are valued using the first in, first out method. When inventories are used, the carrying amount of those inventories are recognised as an expense in the period in which the related revenue is recognised. Provision for write-downs to net realisable value and losses of inventories are recognised as an expense in the period in which the write-down or loss occurs. Reversals are recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

Trade and other receivables
Trade and other receivables are measured at amortised cost using the effective interest method as reduced by appropriate allowances for estimated irrecoverable amounts.

Cash and cash equivalents
Cash comprises cash in hand, demand deposits and bank overdrafts. Cash equivalents include short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

Trade and other payables
Trade and other payables are measured at amortised cost using the effective interest method.

Provisions
A provision is recognised when there is a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision is recognised.

Uninsured losses are recognised when the underlying event occurs. Accruals are made for uninsured losses notified and provisions are made for claims incurred but not reported at each year end. Recoveries of amounts claimed from insurers to settle expenses incurred are recognised when it is virtually certain that reimbursement will be received.

Provisions are measured at the value of the expenditures expected to be required to settle the obligation.

Retirement benefit obligations
The Group operates various defined benefit and defined contribution retirement benefit plans. Most of these plans are funded schemes, that is they are financed through a pension fund or an external insurance policy. The minimum funding level of these schemes is defined by national rules.

Payments to defined contribution retirement benefit plans are charged as an expense as they fall due.

The Group's commitments under defined benefit retirement benefit plans, and the related costs, are valued 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 in the statement of recognised income and expense. Past service cost is recognised immediately to the extent that the benefits have 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 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 any refunds and reductions in future contributions to the plan. The current service costs and gains and losses on settlements and curtailments are included in operating expenses in the income statement.

Taxation
The current tax 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 substantially enacted at the balance sheet date.

Current tax for current and prior periods, to the extent unpaid, are recognised as a liability. If the amount already paid in respect of current and prior periods exceeds the amount due for those periods, the excess is recognised as a current asset. The benefit relating to a tax loss that can be carried back to recover current tax of a previous period is recognised as a current asset.

Deferred tax is provided in full using the balance sheet liability method, on temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the corresponding tax bases for taxation purposes. Deferred taxes are not calculated on the following temporary differences: (i) the initial recognition of goodwill and (ii) the initial recognition of assets and liabilities that affect neither accounting nor taxable profit. The amount of deferred tax provided is based on the expected basis of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the unused tax losses and credits can be utilised. Deferred tax assets previously recognised are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax is charged or credited to 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.

Foreign currency translation

The Group consolidation is prepared in sterling. Income statements of foreign operations are translated into sterling at the weighted average exchange rates for the period and balance sheets are translated into sterling at the exchange rate ruling on the balance sheet date. Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as local currency assets and liabilities of the foreign entity and are translated at the closing rate.

Foreign currency transactions are accounted for at the exchange rate prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Exchange movements arising from the re-translation at closing rates of the opening balance sheets and results of subsidiaries, joint ventures and associates are taken to the translation reserve. Other exchange movements are taken to the income statement.

Where the Group hedges net investments in foreign operations, the gains and losses relating to the effective portion of the hedging instrument is recognised in the translation reserve in equity. The gain or loss relating to any ineffective portion is recognised in the income statement. Gains and losses accumulated in equity are included in the income statement when the foreign operation is disposed of.

The Group's results are presented in euro. The consolidated assets and liabilities at each balance sheet date are translated into euro at the closing rate at that balance sheet date. The consolidated income and expenses are translated into euro at the average monthly exchange rates. All resulting exchange differences are taken to the translation reserve.

Equity

Where the Company (or its subsidiaries) re-acquires its own equity instruments, those instruments are deducted from equity as treasury shares. Where such equity instruments are subsequently sold, any consideration received is recognised in equity.

Dividend distribution

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

Financial instruments and hedge accounting

From 1 January 2004 to 31 December 2004 financial instruments used as hedges in the financing and financial risk management of the Group were accounted for as follows:

a) Forward foreign exchange contracts which hedged currency assets and liabilities were recognised in the financial statements together with the assets and liabilities they hedged. The contract rate was used for translation. Foreign exchange contracts which hedged future sales and purchases were not recognised in the Consolidated Financial Statements until the transaction they hedged was itself recognised. If a foreign exchange contract ceased to be a hedge, then any gain or loss was taken to the income statement.

b) Options on cross currency or interest rate swaps were used either to hedge borrowings or as a means of entering into a swap (as a hedge) at a pre-determined target rate: premiums paid or received for such options were accounted for over the life of the relevant transaction, or, if immaterial and no transaction took place, were recognised in the income statement upon exercise or at maturity of the option contract.

c) Cross currency swaps were included in the Consolidated Financial Statements at the rate of exchange ruling on the balance sheet date. Exchange differences arising were dealt with in accordance with the accounting policy on foreign currencies. Interest paid or received on cross currency swaps was recorded on an accruals basis. Apart from inclusion at the ruling rate of exchange, cross currency swaps were not revalued to fair value at the balance sheet date.

d) Interest arising upon interest rate swaps, caps and collars was taken to the income statement on an accruals basis. None of these instruments were revalued to fair value at the balance sheet date. Premiums paid on caps and collars were recognised on an accruals basis.

From 1 January 2005, in accordance with IAS 39, financial instruments are recorded initially at fair value. Subsequent measurement depends upon the designation of the instrument, as follows:

a) Investments (other than interests in joint ventures, associates and fixed deposits) and short-term investments (other than fixed deposits) are normally designated as available for sale.

b) Fixed deposits, comprising principally funds held with banks and other financial institutions, and short-term borrowings and overdrafts are classified as loans and receivables and are held at amortised cost.

c) Derivatives, comprising interest rate swaps, foreign exchange contracts, cross currency interest rate swaps, options and embedded derivatives, are classified as derivative financial instruments.

d) Long-term loans are generally held at amortised cost.

The fair values of derivative financial instruments are determined on the basis of market forward interest, exchange rates, and option valuation techniques at the balance sheet date. Changes in fair value of derivative financial instruments that do not qualify for hedge accounting are recognised in the income statement as they arise.

Cash flow hedges

Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cash flows are recognised directly in equity and any ineffective portion is recognised immediately in the income statement. If the cash flow hedge is a firm commitment or the forecasted transaction results in the recognition of an asset or a liability, then, at the time the asset or liability is recognised, the associated gains or losses on the derivative that had previously been recognised in equity are included in the initial measurement of the asset or liability. For

Significant Accounting Policies *continued*

Applicable to the Consolidated Financial Statements for the year ended 31 December 2005

hedges that do not result in the recognition of an asset or a liability, amounts deferred in equity are recognised in the income statement in the same period in which the hedged item affects net profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Fair value hedges

For an effective hedge of an exposure to changes in the fair value of a hedged item, the hedged item is adjusted for changes in fair value attributable to the risk being hedged with a corresponding entry in the income statement. Gains or losses from re-measuring the derivative, or for non-derivatives, the foreign currency component of its carrying amount, are also recognised in the income statement.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used, is amortised to the income statement over the period to maturity.

Embedded derivatives

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 the host contracts, and the host contracts are not carried at fair value with unrealised gains or losses reported in the income statement.

The impact of this change in accounting policy is detailed in Note 47.

Critical accounting policies and judgements

The preparation of the Consolidated Financial Statements requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and disclosure of contingencies at the date of the Consolidated Financial Statements. If in the future such estimates and assumptions, which are based on management's best judgement at the date of the Consolidated Financial Statements, deviate from the actual circumstances, the original estimates and assumptions will be modified, as appropriate, in the period in which the circumstances change. The following policies are considered to be of greater complexity and/or particularly subject to the exercise of judgement:

Goodwill

As required by IAS 36, Impairment of Assets, the Group regularly monitors the carrying value of its assets, including goodwill. Impairment reviews compare the carrying values to the present value of future cash flows that are derived from the relevant asset or cash-generating unit. These reviews therefore depend on management estimates and judgements, in particular in relation to the forecasting of future cash flows and the discount rate applied to the cash flows (see Note 10).

Exceptional items

Exceptional items are those that, by virtue of their size or incidence, should be separately disclosed in the income statement. The determination of which items should be separately disclosed as operating exceptional items requires judgement.

Fleet

Given the nature of the Group's business, the main asset in the balance sheet is the vehicle fleet. The majority of fleet is held under manufacturer re-purchase arrangements, which guarantee a disposal value at the end of the holding period. However, a proportion of fleet has no such contractual protection and therefore the value at the end of the rental life will depend on the market for those vehicles at the time of disposal. Judgement is therefore required in the estimation of disposal value.

Post-employment benefits

Application of IAS 19, Employee Benefits, requires the exercise of judgement in relation to setting the assumptions used by the actuaries in assessing the financial position of each scheme. The Group determines the assumptions to be adopted in discussion with its actuaries, and believes these assumptions to be in line with UK generally accepted practice, but the application of different assumptions could have a significant effect on the amounts reflected in the income statement and balance sheet in respect of post-employment benefits. In particular, the defined benefit obligation for funded schemes is forecast to vary by approximately €4 million for each 0.1% movement in either the applied discount rate or inflation rate. Similarly, the defined benefit obligation for unfunded schemes is forecast to vary by approximately €0.8 million for each 0.1% movement in either the discount rate or inflation rate.

Provisions

The Group continues to carry balance sheet provisions in a number of areas against exposures that arise in the normal course of trading. These provisions cover areas such as uninsured losses, termination and reorganisation activities and property dilapidation reserves. Judgement is involved in assessing the exposures in these areas and hence in setting the level of the required provision.