

building on our strengths



RAC plc is a unique support services company delivering a comprehensive range of motoring services to consumers and businesses through our strong and trusted RAC, BSM and Lex brands.



Front cover picture, left to right
Jonathan Glenn Customer Service
Manager, Lex Vehicle Leasing
Paul Oakley Patrol of the Year,
RAC Roadside Services
Shona Sinclair Driving instructor, BSM

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2004 highlights

Revenue growth from continuing operations up 8%

- RAC Consumer Services up 6%

- Business Services up 8%.

Profits from continuing operations (excluding Paccar) up 12% to £71.2 million.

Full year dividend up 6.2% to 25.8p.

Profit before goodwill amortisation, exceptional items and tax up 2% to £88.6 million.

Earnings per share on this basis up 2% to 55.7p.

Debt reduced to £139.8 million.

Major strategic step in financial services.

Record number of service awards.

delivering inspirational service

We are a customer service business with a philosophy to create an environment in which our colleagues feel motivated and supported to deliver service excellence, and our customers feel inspired to maintain and develop their relationships with us.

From Good to Great

Our aim is to make RAC a Great company by making it a great place to work, delivering inspirational service and rapid organic growth.

To assess our progress we look at three complementary measures



*Continuing operations

#Before goodwill amortisation, exceptional items and tax

*Continuing operations (excluding Paccar)

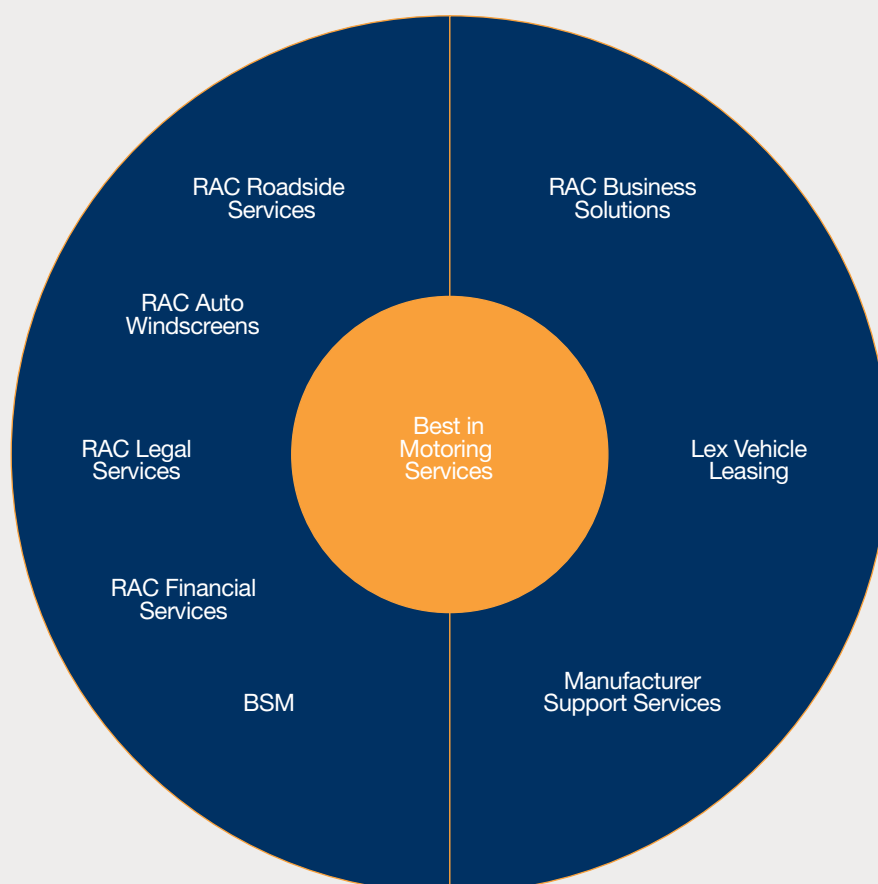
serving the consumer and business markets

Consumer Services Trading profit*

2004 – £47.5 million#
2003 – £51.3 million

Business Services Trading profit*

2004 – £54.7 million
2003 – £53.0 million

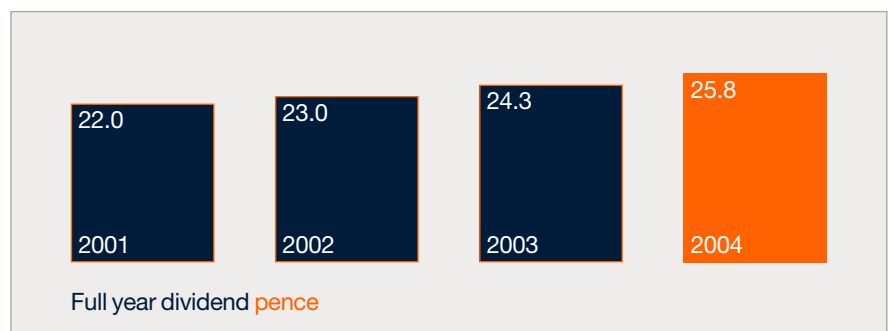
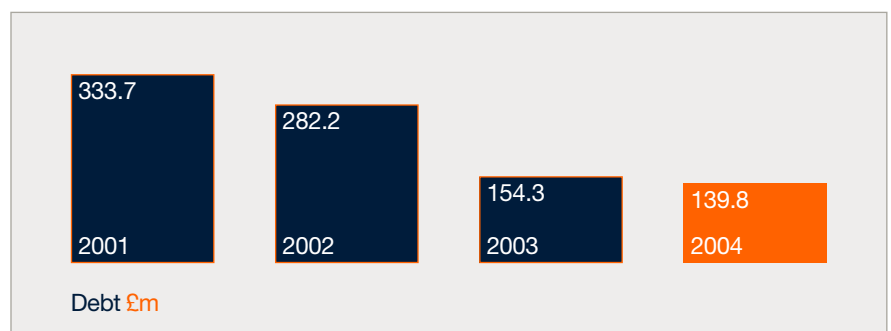
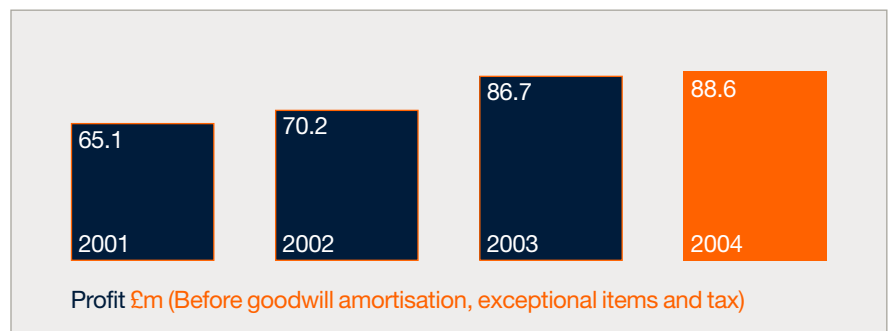


*Continuing operations

#After charging £6.4 million of restructuring and Insurance Mediation Directive implementation costs

A strong performance from our continuing businesses, with profits (excluding the Paccar contribution) up 12% in 2004.

This emphasises our success in delivering against our strategy of building sustainable organic growth.



consumer services



Roadside Our patrol team serve over 7 million members across the UK – including individual members and those receiving cover through corporate fleets, insurers and vehicle manufacturers. This year we were awarded No1 in customer satisfaction in the annual JD Power Study*, the 'Best in Vehicle Recovery' in the 2004 Fleet Excellence Awards, and at the National Customer Service Awards picked up the 'Best use of technology in customer service'.



RAC Auto Windscreens Our expert fitters repair and replace over 750,000 pieces of glass every year, and serve individual motorists, fleet vehicles and the insurance markets. With over 820 fitters, across 154 sites, we operate 24 hours a day, 365 days a year.



RAC Legal Services We have been providing legal advice for motorists for over 90 years. Our straight forward and clear approach to dealing with personal injury and legal expenses insurance has seen our customer base increase in the last year to 2.3 million legal expenses policies, and our personal injury claims work increase to over 21,000.



RAC Financial Services We offer customers personal insurance products covering motor, home and travel, as well as a range of motor and personal loans. We have a track record in achieving high levels of insurance renewals with our customers – reflecting the success of our approach based on choice, value for money and excellence in customer service.



BSM We are the UK's largest driver training company, with over 3,100 instructors across the UK. In 2004, we delivered driver tuition and training to over 157,000 people, from learner drivers to those requiring refresher or advanced driving skills for personal or business use. BSM also accredit a network of Rider Training Schools across the country, providing training to motorcyclists.



Vehicle Inspections RAC provides vehicle examinations for individual motorists, fleets, vehicle manufacturers, finance companies, and dealerships. In 2004, our Inspectors carried out over 350,000 vehicle inspections; providing peace of mind and potentially money saving advice to customers.

*RAC was ranked the top roadside rescue and recovery company in the J.D. Power and Associates 2004 UK Roadside Assistance StudySM. Study based on responses from 23,641 owners and drivers of 51 and 02 registered vehicles who required roadside assistance. www.jdpower.com

business services



Customer contact centres RAC Business Solutions delivers a seamless service to business customers who want an organisation to manage their customer service and customer care operations. Our customers include vehicle manufacturers, fleet operators, and insurance companies.



Claims management and accident services RAC Business Solutions works extensively with insurers and fleet operators on all aspects of the claims handling event – from first notification of an accident and vehicle damage or loss, through to managing the entire repair and settling the claim.



Vehicle supply, parts and maintenance We have a wealth of knowledge and expertise in providing vehicle solutions to the fleet market through Lex Vehicle Leasing, and to the commercial vehicle market through Lex Vehicle Leasing and Lex Transfleet.



Fleet management and support Through Lex Vehicle Leasing, and Lex Transfleet we provide a full range of vehicle management, maintenance and incident support for companies and individuals who want to achieve stress-free motoring. We also provide, through RAC Software Solutions, vehicle and asset management software for public and private sector organisations.



Supply chain solutions Lex Auto Logistics, and Lex Multipart Defence provide a broad range of innovative services from forecasting and procurement to physical logistics solutions for parts and components; delivering value and customer service to private and public sector organisations.



Vehicle marketing and distribution Hyundai Car UK is the sole importer of Hyundai cars into the UK. With a national dealership network of 165, we provide national marketing support, vehicle finance, and parts supply for Hyundai Cars in the UK. Lex Commercials, our commercial vehicle dealer group, sells, maintains and supplies parts for new and used trucks, trailers, vans and specialist equipment.

our sector expertise

Across RAC plc we combine our knowledge and expertise to provide services to organisations in the public and private sectors. It is a fundamental part of our product offer that we approach each new prospect with a tailored service to meet their individual needs.

We have identified five target sectors, where we have existing relationships, and which represent significant areas for growth. Contracts within these sectors can involve long lead times from the identification of a prospect through to pre-qualification, tendering, award and full implementation.



Defence Responsible for over £1 billion of MoD contracts, Lex Defence is one of the largest suppliers of vehicles, fleet management, and logistics support services to the UK defence market. In addition to managing over 14,000 vehicles on behalf of the MoD, Lex Defence provides logistics support solutions, from spares for the Challenger 2 Tank, to a warehouse and distribution management service for the Rapier weapon system.



Motor and Vehicle Manufacturers Our capabilities extend to contact centre and customer care services, mystery shopping, centralised service bookings, lead qualification, breakdown assistance for commercial and motor vehicles, and inspection services and warranties. Over 40% of all new cars sold carry RAC breakdown cover and we have recently integrated contract hire services to Ford.



Airside Airlines, airports and ground handling companies are increasingly aware of the need to concentrate on core capabilities. From 2003, Lex Transfleet Airside Solutions has been working with British Airways on one of the largest contracts of its kind, delivering maintenance and fleet management for British Airways' fleet of ground support equipment. This 10-year contract covers over 7,000 vehicles from aircraft tugs and baggage trailers, to crew buses and passenger coaches, and includes operations at Heathrow, Gatwick, Manchester and Birmingham airports.



Utilities Services For every company within the utilities sector, regulatory and commercial pressures create a constant need to reduce costs and optimise efficiency, while maintaining service quality. RAC Utilities Services has extensive experience in this specialist sector and a wide range of skills from total fleet management through to effective asset management.



Insurance Services Providing customer contact centres for leading insurance and financial services companies, including Lloyds TSB, NFU Mutual, and Norwich Union, we design our services to bring efficiency gains to our clients, and deliver high levels of satisfaction for their customers. We work extensively with insurers and fleet operators on all aspects of the claims handling event – from the first notification of an accident or vehicle damage or loss, through to managing the repair and settling the claim.

inspiring our colleagues

Core to our business success is the service we deliver to our customers. We have a fundamental belief in the role that our colleagues play in delivering inspirational service. With the support of our colleagues, we base our actions and build our culture, around a set of five key values:

Pioneering

Pace & Ambition

Integrity

Hungry to Learn

Together we make a difference

We invest in learning and development programmes designed to support our colleagues in delivering inspirational service, and build our overall understanding of colleague satisfaction through an annual company-wide survey.

In 2004, our overall colleague satisfaction increased by 2% to 73%, and almost 10,000 colleagues responded to the survey. Our monthly 'People P&L' which looks at colleague turnover, stability, absence and satisfaction, gives further information on progress and ensures that our colleagues and the environment in which they work is high on the agenda across the company.

supporting the community



13 pupils at King James School in Knaresborough, receiving their award from RAC Patrol, Andy Hardcastle.

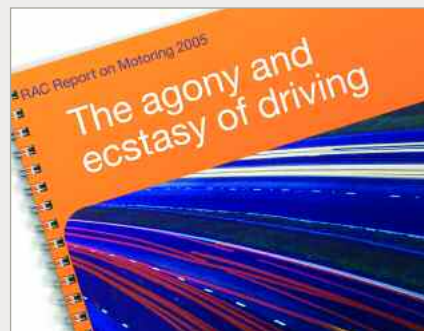
We recognise our corporate social responsibility in a number of ways: through the donations we and our colleagues make to charities, through the promotion of road safety to schools across the United Kingdom, and through our adoption of environmentally aware processes. We also play a role in helping shape the policy debate around motoring and are proud to represent the views of our members, and Britain's motorists in general, both through our annual Report on Motoring, and contributing to comment on the transport issues of the day.

Charities RAC plc supports colleagues through matching funds raised by them to a maximum of £250 per individual or £500 per team. We believe that our colleagues are motivated to raise funds for initiatives close to them and therefore do not have a chosen charity for the company. The range of charities benefiting from our fundraising include Macmillan Cancer Relief, British Heart Foundation through to transport related charities including BEN – the Motor and Allied Trades Benevolent Fund – and Motability, which provides adapted vehicles for people with disabilities.

Road safety Every year we work with schools across the UK to involve children in suggesting ways to improve safety measures on their route to school. This programme, called Grass Routes, involves 11-14 year olds, the most vulnerable group on the roads. Over 3,000 Grass Routes resource packs, which are endorsed by the Department for Transport and the Department for Education and Skills are used in secondary schools as part of the national curriculum.

Environment We have minimum standards for both health and safety and environmental management in each business, supported by training and site-specific policies and procedures. We also track our performance through an annual environmental report which covers areas from accident reporting to managing our environmental standards. This is published on our website www.racplc.co.uk

Voice of the motorist The RAC brand is synonymous with motoring. We support motorists from their first experience behind the wheel and throughout their motoring lives. As such, we have a wealth of experience and knowledge which we constantly grow and enhance. Each year, we produce our Report on Motoring, now in its 16th year, to put the spotlight on a topical issue. In 2005 we are looking at the frustration and liberation drivers experience on today's busy roads. We use our findings to inform ongoing debate with our members, the media and with government.



Our 16th annual Report on Motoring looks at the agony and ecstasy of driving today.

building on our strengths

2004 has been a good year for RAC plc. The following pages highlight a number of our key successes. These include: our Roadside Assistance and Fleet Excellence awards; our strategic step in financial services; the successful integration of our new Ford contract; the growth of BSM; our expanding business to business services; and our investment in future skills for our British Airways contract.



Number 1 for customer satisfaction

This year we were voted No.1 for customer satisfaction in the annual JD Power Study, 'Best in Vehicle Recovery' at the Fleet Excellence Awards, and also picked up the 'Best use of technology in customer service' award at the National Customer Service awards. These achievements recognise the outstanding service delivered 24 hours a day by our front line patrols and dedicated customer service and support teams. For membership information call 08000 722822.

Financial services

In September we made a major commitment to our financial services business through our agreement to buy the renewal rights to AXA Direct's 270,000 motor and home insurance policies. Our agreement included regaining ownership of our brand, RAC Insure, and created tremendous potential to grow our financial services business by offering members and non-members alike products offering value, choice and great service. For information on our financial services, call 0800 0154435.



Fleet management

Lex Vehicle Leasing successfully integrated our contract with Ford, which is worth £1 billion over the next 7 years. Our total managed fleet now exceeds 123,600 vehicles.

Building on our vision to be a world-class business, we were also pleased to receive a number of service awards in 2004 – including: Best Leasing and Best Fleet Management company at the Fleet Excellence Awards. For more information on our fleet management services go to www.lvl.co.uk





Driver training

In June 2004 we celebrated the addition of our 3,000th driving Instructor. As the UK's largest driving school, BSM utilises simulators and on-line tools to help prepare drivers for their test. We deliver training and tuition annually to over 157,000 drivers from those taking the wheel for the first time to those needing refresher courses or advanced skills for business or pleasure. For more information go to www.bsm.co.uk

Training future skills

In August, we launched the first apprentice programme of its kind to support the work we do for British Airways managing their 7,000 strong airside vehicles. The scheme is a first for us and the industry, and represents our commitment to the ongoing development of skills to benefit our customers and our colleagues. Pictured are Aaron Lusher, apprentice and Daniel Wicks, de-icer technician and mentor.





Solutions for business

We deliver a growing range of services to business. During the year, RAC Business Solutions launched a new service where we provide information on drivers' licence status using the DVLA's database, to help companies more effectively manage the corporate risks of running their fleet vehicles. For more information on our services go to www.rac.co.uk/business

building on our strengths

Our goal is to be regarded by our customers as providing the 'best in motoring services' and we will achieve this through delivering inspirational service to them.



Peter Smith **Chairman**



Andrew Harrison **Chief Executive**

We have strong brands in RAC, Lex and BSM. Our strategy is to deliver growth by leveraging their strength and our customer base. During 2004, we undertook extensive research on the RAC brand, and were pleased when it confirmed that our customers find us one of the most trustworthy brands in the UK, and rated us excellent for service. The internal research was confirmed by external awards, with our success as Number 1 in customer satisfaction in the annual JD Power study and a near clean sweep for all our brands in the annual Fleet Excellence awards.

Our most important strategic step in 2004 was the restoration, in the autumn, of full ownership of our Financial Services business, through buying out our joint venture with AXA and the associated acquisition of renewal rights to AXA Direct's motor and home insurance policyholders. With a highly trusted brand we are ambitious in financial services.

For a number of years, the company has anticipated the cessation of our parts distribution relationship with Paccar, the worldwide truck manufacturer. A disengagement was agreed in November 2004, although it will be late 2005 before this is completed. This will mark the conclusion of a highly cash generative trading relationship.

The continuing RAC businesses have been growing rapidly and it is encouraging that in 2004 the profits in these continuing businesses, excluding the contribution from Paccar, grew by 12% to £71.2 million (2003 – £63.6 million). In 2004 the profit contribution from our Paccar contract reduced to £17.4 million (2003 – £25.6 million).

Revenue growth from continuing operations was strong, up 8% to £1,509.1 million (2003 – £1,401.5 million). Total revenues increased by 1% to £1,539.4 million (2003 – £1,526.2 million) reflecting the disposal of our mechanical handling businesses.

Profit before goodwill amortisation, exceptional items and taxation grew by 2% to £88.6 million (2003 – £86.7 million). This reflected the £8.2 million reduction in the Paccar contribution as well as restructuring charges of £4.4 million relating to the integration of the AXA Direct business and other business efficiency improvements, and costs of £2.0 million in relation to the implementation of the Insurance Mediation Directive. Earnings per share on this basis increased by 2% to 55.7p (2003 – 54.4p).

After exceptional items, primarily associated with business disposals

and VAT repayments from prior periods, profit before tax was £77.7 million (2003 – £25.7 million) and earnings per share calculated in accordance with FRS 14 were 45.8p (2003 – 8.3p).

The company continued to generate cash, despite investing £31 million in the AXA transaction and injecting capital into Lex Vehicle Leasing to support the Ford Financial transaction. Net debt fell by £14.5 million to £139.8 million (2003 – £154.3 million).

The Board proposes a final year dividend of 15.6p to bring the total dividend for the year to 25.8p, an increase of 6.2% on 2003 (24.3p).

Operating highlights

Consumer Services RAC Consumer Services made progress in 2004, with total revenues of £374.8 million, up 6% (2003 – £353.1 million). Underlying profits after adjusting for restructuring charges associated with the integration of AXA and other business efficiency improvements, and the costs of implementing the Insurance Mediation Directive, increased by 5%.

Total revenues in our Motoring Services businesses were up 29% with strong performances from Financial Services, Legal Services and BSM. Our Roadside

business grew revenue by 3%, although membership growth was constrained by process issues which affected customer payment collection and call centre service and had an impact on membership renewals. We have made good progress in resolving these issues and anticipate a return to membership growth in 2005.

We took a major step in our financial services strategy through acquiring the renewal rights to AXA Direct's 270,000 motor and home insurance policyholders, and regaining control of the RAC Financial Services brand, previously jointly owned with AXA. Costs of £1.9 million were incurred during the year in integrating the business. This acquisition should increase our motor, home and personal insurance book to approximately 450,000 policies by the end of 2005.

To further accelerate our Roadside, Financial and Legal Services businesses, we will be spending an additional £5 million on marketing for 2005, funded by business efficiency improvements.

RAC Auto Windscreens has experienced challenging trading conditions, reflected in pressure on margins and the loss of some insurance customers who elected to change to single source supplier agreements. Nevertheless the business has stabilised and there have been encouraging signs of success in our sales activities, most notably at the end of 2004 with Co-operative Insurance Services, where we have become the preferred supplier for all its automotive glazing repair and replacement work.

We prepared for the introduction of the Insurance Mediation Directive, which came into force in January 2005, and brings parts of the company, including our Roadside business, under Financial Services Authority regulation for the first time. The costs associated with this for 2004 were £2.0 million, and a similar figure will be incurred in 2005 as a continuing operating cost. We also embarked on a business efficiency improvement programme at the end of 2004, which incurred one off costs of £2.5 million.

Nick Hughes has been appointed as Managing Director of RAC Consumer Services with effect from 1 May 2005. Nick joins RAC from American Express where he has been European Head of Marketing for the last three years. His previous experience includes McKinsey & Co and South African Breweries.

Jon Walden has resumed his role as Managing Director of Lex Vehicle Leasing.

Business Services Our Business Services operations performed well in 2004, with revenues from continuing operations up 8% to £1,131.8 million (2003 – £1,045.1 million) and profits, after absorbing the Paccar reduction, increasing by 3% to £54.7 million (2003 – £53.0 million).

We continued to increase the services we sell into the business to business market – in particular, the work we carry out in claims handling for the insurance market, and services to motor manufacturers, including an agreement to manage service bookings for a major UK motor manufacturer. RAC Business Solutions grew revenues by 6% to £169.8 million (2003 – £160.8 million) and increased profits by 271% from £1.4 million in 2003 to £5.3 million.

Lex Vehicle Leasing, our joint venture with HBOS, had another good year, with an increase in fleet size of 21% to 123,600 vehicles (2003 – 102,300 vehicles). The successful integration of the Ford Financial contract announced at the end of 2003 and good organic fleet growth, resulted in a 17% improvement in revenues to £241.8 million (2003 – £207.2 million) with profits up 16% at £22.7 million (2003 – £19.6 million).

Within Manufacturing Support Services, Hyundai increased its sales by 16%, significantly outperforming the new car market as a whole. We remain the preferred bidder, in partnership with Amey, for the Ministry of Defence's 15 year, £500 million C Vehicle contract – anticipated to be awarded in early 2005.

This year we also completed the exiting of our mechanical handling business through the disposal of Lex Komatsu South, Lex Havelange in Belgium and Lex Manutention in France. We also negotiated the management buy-out of Isuzu Truck and disposed of Multipart Universal.

Our people Core to our business success is the service we deliver to our customers, and we have a strong belief in the role that our colleagues play in achieving service excellence. In 2004 we were pleased to receive further recognition of the positive steps we are taking towards our aim of delivering inspirational service – internally, we achieved an increase in overall colleague satisfaction, and externally received a record number of customer service awards across our consumer and business services. We are grateful to all our colleagues who have delivered outstanding service to our customers throughout the year.

Public policy RAC has been synonymous with motoring for over a century and continues to provide comment on the key issues of the day – from congestion and road safety, to driving standards and transport investment. In conjunction with our partners at the RAC Foundation, we engage at all levels of government and through the media to promote the interests of motorists.

Our annual 'Report on Motoring' is now in its 16th year. Our 2005 report looks at the various agonies and ecstasies of motoring today. The report investigates the major factors impacting negatively on the motorist, focusing particularly on those representing the biggest challenges to policy makers looking to make our roads safer. By focusing on these major road safety factors, the RAC Report on Motoring supports the current legislative agenda which aims to reduce the 38,000 deaths and serious injuries that are suffered on our roads every year, and so make them a safer and more enjoyable place to be.

Outlook Over the past three years our continuing operating profits, excluding the discontinuing Paccar income, have grown by 12% pa. In 2004 we delivered good revenue growth in both Consumer and Business Services driven by the strength of our brands, our customer base, and improvements in customer service. We have started the new financial year well and remain confident in our future prospects.

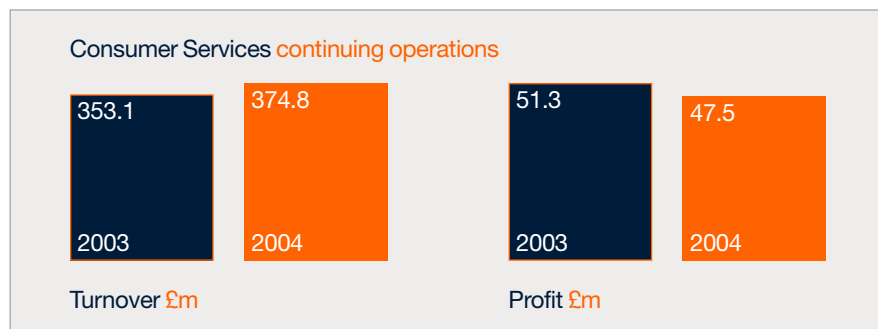


Peter Smith
Chairman



Andrew Harrison
Chief Executive

revenues increased by 6%



The RAC brand is one of the most trusted in the UK. We give peace of mind to millions of customers through our 24 hour roadside and replacement windscreen services, our range of motor, legal and home insurance products and advice on personal injury claims. In BSM we are the market leader in driving tuition, providing training to 157,000 pupils each year, from beginners starting on our unique simulators to experienced drivers requiring advanced skills for personal or business use.

Consumer Services Consumer Services has grown steadily in recent years and now contributes over half the company's operating profit.

Roadside 2004 saw us deliver our best service standards ever at the roadside, with customers voting our breakdown business No.1 for customer satisfaction in the JD Power annual customer study, and No.1 breakdown provider in the Fleet Service awards. This success comes on the back of investment made over the last few years in state of the art equipment and diagnostic tools for our patrol force and customer service teams.



Voted number 1 for customer satisfaction in the annual JD Power and Associates UK Roadside Assistance StudySM.

Revenue grew in 2004 by 3% to £205.4 million (2003 – £198.7 million); membership remained static at 2.2 million members after a number of years of strong growth. Following the implementation of new customer management systems late in 2003, we encountered difficulties with call handling times in our contact centres and some issues with collecting cash from customers whose bank or credit card details had changed since we last took payment. We worked hard to minimise the impact on our customers, and saw progressive improvement in these issues as the year progressed. There was a resulting dip in our high renewal rate, from 83% in 2003 to 80% in 2004 as a whole, but it is encouraging to note that the rate for December was back above 82% and that this has been maintained in January.



We now have over 3,100 driving instructors at BSM providing training to over 157,000 pupils a year.

Motoring Services

Financial Services With strong brand recognition, high renewal rates and access to our Roadside membership base, developing RAC Financial Services is one of our biggest strategic opportunities. In 2004 we took a major step towards exploiting this strategy through acquiring the renewal rights to AXA Direct's 270,000 motor and home insurance policyholders, and regaining ownership of the RAC Financial Services brand, previously jointly owned with AXA. These initiatives should increase our motor, home and personal insurance policy book to approximately 450,000 by the end of 2005.

Integration costs for this acquisition were £1.9 million in 2004, and we expect the acquisition to be earnings enhancing (before goodwill amortisation) in 2005, and substantially so beyond that. Revenues grew by 59% to £13.8 million, (2003 – £8.7 million), including organic growth of 16%.

Legal Services We provide legal expense insurance and assistance in personal injury claims for both members and non-members. Our customers trust us to pursue their claims honestly and professionally, and insurers know that we will not pursue frivolous claims. We have

been growing our in-house legal practice strongly and now employ 45 lawyers as well as a panel of 24 firms of solicitors around the UK. Personal injury claims handled increased by 10% to 21,400 (2003 – 19,400) and the number of legal expense policies sold grew by 14% to 2.4 million, (2003 – 2.1 million) with total revenues growing by 46% to £15.0 million (2003 – £10.3 million).

BSM The UK's largest driving school, BSM, welcomed its 3000th instructor in June this year and provided tuition to 157,000 new and experienced drivers. BSM utilises the latest techniques – such as on-line training tools and driving simulators – to give those new to driving the best start and those looking for additional skills the right support and access to advanced training. The dynamics of the market remain attractive, with the young driver population growing, tests getting progressively harder and the demand for further tuition beyond the test (which can enable young drivers to obtain favourable insurance rates) increasing. Revenues grew by 10% to £34.9 million (2003 – £31.8 million).

RAC Auto Windscreens Auto Windscreens experienced challenging trading conditions, reflected in a reduction in margins, when a number of insurers opted for a single source of supply in 2003 and Auto Windscreens was unsuccessful in the tenders. The new management team took action to

reduce costs and are introducing new, more flexible, working conditions into the business. Towards the end of the year there were encouraging signs of success in our sales activities, most notably with Co-operative Insurance Services where we have become the preferred supplier for all its automotive glass repair and replacement work.

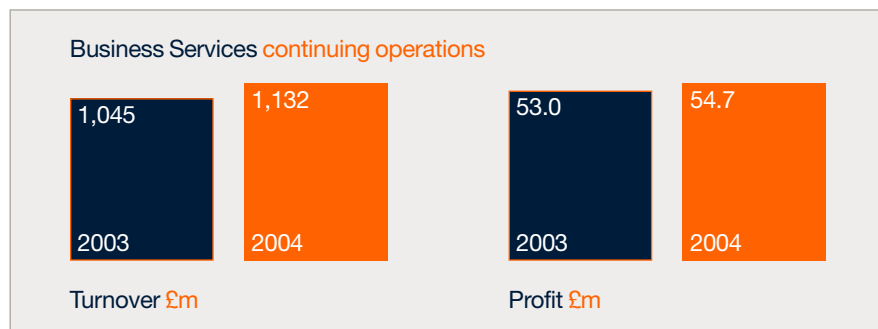
Sales in 2004 were down by 2% at £95.2 million (2003 – £96.9 million). The business continues to make an attractive return on sales, to cover its cost of capital, and to be cash generative.

Whilst 2004 was a mixed year for RAC Consumer Services, we nonetheless saw revenue growth and underlying profit momentum, and a vitally important strategic move into financial services. The major priorities for 2005 are to stimulate growth in our Roadside membership base and, through a £5 million increase in marketing expenditure, maximise the opportunity presented by our Financial and Legal Services businesses. Success in these areas will help us move towards our goal of 20% of members buying more than one service, from the 13% level seen in 2004.

Major strategic step in financial services through the acquisition of renewal rights to AXA Direct's 270,000 motor and home insurance policyholders.



revenues increased by 8%



Overview We have strong business to business credentials through our Lex and RAC brands, and provide extensive vehicle and customer services including roadside assistance, motor claims handling, contact centres, fleet management, vehicle finance, supply chain management and vehicle distribution and sales. Our customers include the Ministry of Defence, British Airways, Norwich Union, Ford and Audi. We provide support and service around the clock, 365 days a year.

As a Company our individual businesses work together to provide services across a number of sectors. In particular, we have identified five key areas: motor and vehicle manufacturers, defence, insurance, utilities, and airside operations, where customers benefit from our knowledge and expertise to bring operational and efficiency benefits. The opportunities within these sectors are considerable and we estimate that our current order book has a revenue value of approximately £2 billion. Our sales to these sectors increased by 10% to £303 million in 2004.



Lex Vehicle Leasing
fleet increases to
123,600 vehicles.

Our Business Services' operations performed well in 2004, with revenues from continuing activities up 8% to £1,131.8 million (2003 – £1,045.1 million) and profits, after absorbing the anticipated reduction in Paccar contribution, increasing by 3% to £54.7 million (2003 – £53.0 million). We strengthened the range of RAC's services sold into the business to business market. In particular, the work we carry out in claims handling for the insurance market, and services to motor manufacturers, including an agreement to manage service bookings for a major UK motor manufacturer, have helped RAC Business Solutions grow revenues by 6%, and profit by 271%.



Record new car sales in Hyundai, topping 37,000 vehicles.

Lex Vehicle Leasing Lex Vehicle Leasing, our joint venture with HBOS, had another excellent year. Our half share of profits grew 16% to £22.7 million, (2003 – £19.6 million), on revenue up 17% to £241.8 million (2003 – £207.2 million). Organic sales growth accounted for 4% of the increase, and the new business with Ford Financial the remaining 13%.

The company increased its fleet size by 21% to 123,600 vehicles (2003 – 102,300 vehicles), reflecting both the successful integration of the Ford Financial outsourcing contract and organic sales growth, with particularly good performances with large fleet customers. Profit growth was further aided by good cost control and the continued delivery of benefits from the company's Six Sigma quality programme which is now being adopted elsewhere in RAC. The used car market was better than expected throughout the year, resulting in lower than anticipated disposal losses.

The business' market-leading service reputation was confirmed by the award, for the sixth year out of seven, of 'UK's Best Contract Hire Company' by Fleet Week and Fleet Management, and additionally being named 'UK Leasing Specialist of the year' by the Institute of Transport Management.

RAC Business Solutions Revenues grew by 6% to £169.8 million (2003 – £160.8 million), and profits increased by 271% to £5.2 million (2003 – £1.4 million).

During 2004 we were successful with both existing and new customers, strengthening our relationships with motor manufacturers, fleet operators and insurance companies. We renewed important contracts with Motability, for roadside assistance and vehicle inspection, and Norwich Union, for claims handling.

We broadened the range of products we offer to our customers, helped by the successful implementation of new claims handling and customer management systems, and now have a comprehensive range of services, including outsourcing of customer and dealer contact centres, vehicle inspections, automotive technical support and third party care for insurers.

Our new products include service booking solutions for both motor manufacturers and fleet operators, automated vehicle licence checking, and a new accident management service for fleets and insurers, at our operation in France.

Manufacturing Support Services

Included in this division are: Lex Defence; Hyundai, our car importership; Lex Auto Logistics, our supply chain management business; Lex Commercial, our truck dealership group and Lex Transfleet, our commercial vehicle contract hire, rental and fleet management business, (jointly owned with Lombard – part of the Royal Bank of Scotland Group).

We are the preferred bidder, in partnership with Amey, for the Ministry of Defence C Vehicle contract to supply and maintain construction vehicles, plant equipment and rough terrain mechanical handling equipment operated by the British armed forces world-wide. We anticipate the contract will be awarded in the Spring of 2005, with full implementation by April 2006. This will extend our long standing relationship with the Ministry of Defence, our biggest vehicle services client.

Hyundai had an excellent year with strong growth in sales, outperforming a buoyant new car market. The model range continued to strengthen, with the award winning Getz and highly regarded Coupe supported by the successful launch of the Tucson, Hyundai's mid-range 4x4. Registrations were up 17% to 37,600, and market share increased to 1.5% (2003 – 1.3%).

Lex Auto Logistics concluded negotiations with Paccar for the cessation of our Leyland parts distribution activities, which will now revert to Paccar towards the end of 2005. As a result of the negotiation, Lex Auto Logistics will continue to benefit from the contract until September 2005, but additionally will receive an exceptional profit of £18.0 million, with £4.5 million reported in 2004 and the remaining £13.5 million in 2005. Management have initiated a restructuring plan to minimise the effect of the lost contribution from the contract, including a move to smaller premises planned for early 2006.

Lex Commercial had a good year with revenues up by 3% to £162.8 million (2003 – £158.6 million) aided by strong demand for new vans and trucks. During 2004, Lex Commercial signed additional franchises for Foden and Isuzu trucks, acquired a further DAF/LDV outlet and a specialist commercial workshop. This business continues to support a number of group companies in the delivery of complex bids.

During the year we completed the exit from our mechanical handling businesses, through the disposal of Lex Komatsu South, Lex Havelange in Belgium, and Lex Manutention in France. We also negotiated the management buy-out of Isuzu Truck and disposed of Multipart Universal.

The Chairman and Chief Executive's statement describes the overall revenue and profit performance of the company during the year.

Segmental analysis The segmental analysis of turnover, profit and loss and net assets, showing continuing and discontinued activities, before goodwill amortisation, exceptional items and tax is detailed in note 1 to the accounts. A summary of the segmental profit analysis is shown in the table at the foot of this page.

The RAC Consumer Services result is after:

- £1.9 million of integration costs relating to the buy out of AXA's interest in RAC Financial Services and the acquisition of the renewal rights of AXA Direct.
- £2.0 million of costs in relation to preparation for regulation under the Insurance Mediation Directive, which are expected to continue through 2005.

- £2.5 million of restructuring costs relating primarily to the outsourcing of IT support and the reshaping of our car inspections activities.

Lex Vehicle Leasing's result included a first-time contribution from the contract to supply vehicles for Ford Financial, which began in 2004.

The contribution to Manufacturer Support Services profits of the Leyland parts distribution activity, which will transfer to Paccar in September 2005, has been disclosed in a separate line to give clarity. A receipt of £4.5 million in 2004 has been treated separately as an exceptional item.

Profit from continuing operations before goodwill, exceptional items and tax fell by £0.6 million to £88.6 million, but excluding the non-recurring costs referred to above, it grew by £3.8 million (4.3%). Profit before tax for the year was £77.7 million (2003 – £25.7 million). The large increase reflects operating exceptional income in 2004 compared with operating exceptional charges in

the prior year as described on page 25. Additionally the comparative period had a significantly higher level of exceptional charges from asset disposals and impairments principally relating to our divestment of mechanical handling businesses. Whilst the last disposals were completed in the first half of 2004, the material impairments were taken in 2003.

Interest Average net non-contract hire debt in 2004 was virtually unchanged on the 2003 level as a result of the investments referred to in the Cash flow and debt section on page 26. The company's exposure to interest rate rises was limited by outstanding interest rate swaps which had been established in previous years. Overall, the interest charge fell by £0.5 million to £8.9 million, giving a reduced interest rate of 6.9%. The falling average rate reflects a number of factors including reduced average margins and commitment fees paid to lenders and the maintenance of slightly lower levels of cash and investments (held mainly in the insurance related businesses for regulatory reasons).

Segmental profit analysis	Continuing Operations 2004 £m	Discontinued Operations 2004 £m	Total 2004 £m	Continuing Operations 2003 £m	Discontinued Operations 2003 £m	Total 2003 £m
RAC Consumer Services	47.5	–	47.5	51.3	–	51.3
RAC Business Solutions	5.2	–	5.2	1.4	–	1.4
Lex Vehicle Leasing	22.7	–	22.7	19.6	–	19.6
Lex Industrial Solutions	–	0.1	0.1	–	(2.4)	(2.4)
– Leyland parts distribution and related activities	17.4	–	17.4	25.6	–	25.6
– All other activities	9.4	(0.1)	9.3	6.4	(0.1)	6.3
Manufacturer Support Services	26.8	(0.1)	26.7	32.0	(0.1)	31.9
Other	(4.7)	–	(4.7)	(5.7)	–	(5.7)
Profit before interest, goodwill amortisation, exceptionals and taxation	97.5	–	97.5	98.6	(2.5)	96.1
Interest	(8.9)	–	(8.9)	(9.4)	–	(9.4)
Profit before goodwill amortisation, exceptionals and taxation	88.6	–	88.6	89.2	(2.5)	86.7

Exceptional items	2004 £m
Operating exceptional items (including VAT interest income):	
Leyland transfer fee (first receipt)	4.5
VAT recovery:	
– principal amount	3.0
– interest income (credited to net interest payable and similar charges)	3.3
	10.8
Non-operating exceptional items:	
Manufacturer Support Services and Lex Industrial Solutions:	
– loss on disposal	(5.7)
– goodwill previously written off to reserves	(9.4)
Total loss on disposal of discontinued operations	(15.1)
Profit on sale of fixed assets	1.2
	(13.9)
Net exceptional items	(3.1)

Goodwill amortisation Goodwill amortisation totalled £7.8 million (2003 – £5.6 million). The £2.2 million increase relates to the part-year amortisation of goodwill on the acquisition of insurance assets from AXA (£1.5 million) and on our share of the Lex Vehicle Leasing contract with Ford Financial (£0.7 million).

Exceptional items The company recorded a net exceptional loss (operating, non-operating and VAT interest income) of £3.1 million.

There were operating exceptional credits, including VAT interest income, of £10.8 million (2003 – charge of £30.2 million). These were made up of the £4.5 million first payment on transfer of the Leyland parts distribution contract, and £6.3 million of VAT and interest recovered as a result of claims in relation to past VAT payments. These items are disclosed separately in order to present a more accurate view of the company's underlying trading performance.

In addition to the operating exceptional credits, there were exceptional losses of £13.9 million. The most significant items were a £9.4 million write off of goodwill which had previously been charged to reserves in relation to disposal of the mechanical handling businesses, and £5.7 million loss on disposal of those remaining mechanical handling businesses together with two Manufacturer Support Services businesses, Isuzu Truck and Multipart Universal. These losses have been partially offset by £1.2 million profit on fixed asset disposals.

The net loss on the disposal and closure of these operations reduced the current year tax charge by £2.5 million.

Group tax rate The underlying group tax rate was 28% (2003 – 28%).

Earnings per share Earnings per share on an FRS14 basis were 45.8 p (2003 – 8.3p) after exceptional items and goodwill amortisation. The rise in profits before goodwill amortisation and

exceptional items has resulted in a modest increase in earnings per share on this basis to 55.7 p (2003 – 54.4p), up 2% on last year.

Dividends The proposed final dividend of 15.6p per share would bring the total dividend for the year to 25.8p (2003 – 24.3p). The increase of 6.2% on last year (2003 – 5.7% increase) underlines our confidence in the prospects for growth in both profits and cash generation, as does our intention to effect a modest £20 million share buyback programme, announced in December. Dividend cover on profit before goodwill amortisation and exceptional items, after tax is 2.2 times (2003 – 2.2 times)

Shareholders funds Shareholders funds have increased by £28.5 million to £427.7 million. The key factors were the retained profit for the year of £23.0 million and the add back of £9.4 million of goodwill on disposals previously written off to reserves. This increase is partially offset by a £7.7 million increase in own shares held in relation to share option schemes.

Capital expenditure Gross capital expenditure was £70.9 million (2003 – £89.7 million), a reduction of £18.8 million compared with the high levels of 2003. This reflects the change in structure of the company following the disposal of the last mechanical handling businesses (which were capital intensive), and the large systems investments which took place in 2003. Our total net capital expenditure, including disposals, fell by £15.8 million to £25.5 million. The level of gross capital expenditure and disposals is affected by BSM driver training vehicles which we retain for approximately six months before selling them back to the manufacturer.

Cash flow and debt Net cash inflow from operating activities was £110.0 million (2003 – £117.9 million). We invested £25.5 million net (2003 – £41.3 million) in capital expenditure and £30.8 million in acquiring insurance assets from AXA. The disposal of the last mechanical handling businesses generated £10.6 million, excluding disposal expenses. Additionally, the financing of the Ford Financial transaction in Lex Vehicle Leasing was funded through a small capital injection of £7.5 million and the foregoing of our first half dividend from that joint venture, which would have been £6.5 million.

Despite the investment activity described above, total net debt decreased by £14.5 million to £139.8 million.

The financial ratios of the company have remained strong with interest cover at 11.0 times (2003 – 10.2 times) and a net debt to EBITDA ratio of 1.1 times (2003 – 1.3 times).

Pensions In common with many other companies, our pension fund continued to be in deficit. Under FRS17 the total deficit at the end of the year, net of deferred tax, was estimated at £148 million (2003 – £123 million). To begin to address this shortfall additional

contributions of over £5 million were made in 2004 and are ongoing. In addition a number of changes have been made to reduce the normal annual cost of the scheme by approximately £5 million. An improvement of £62 million in the market value of fund assets to £529 million (2003 – £467 million) was insufficient to offset the increase of £98 million in the valuation of pension liabilities to £740 million (2003 – £642 million) primarily caused by falling bond yields, an increase in our future inflation assumptions, and better estimates of actuarial experience.

Unlike many defined benefit schemes, the trustees of the company pension scheme are entitled to set the contribution rate required from the company. As set out in Note 33, an actuarial valuation took place on 5 April 2004. In the light of this valuation, it was agreed by the trustees that no change in contribution rates would be demanded for 2005, but it was noted that actuarial assumptions regarding life expectancy are under review by the pensions industry and that conclusions may start to be drawn during 2005. The trustees and company management have therefore agreed that a further review of company pensions provision will be undertaken during the course of 2005.

Risks The company's financial risk policy identifies risks and sets out a control framework for managing exposures. This policy is approved by the Board and covers financial risks as follows:

Liquidity risks Committed facilities are maintained at levels which are in excess of current funding requirements. In addition the availability of facilities over the next five years is managed in accordance with policies which link the required minimum level of committed lines to planned needs. Compliance with the policies is monitored regularly throughout the year.

The businesses are able to access liquidity through overdraft accounts which, as they are subject to netting arrangements, ensure that short-term cash balances are directly offset against overdrafts.

Interest rate risks Board policies dictate a range for the amount of debt upon which interest rates must be fixed. The policies cover the next five years, and ensure that interest rate exposure management is linked to the interest cover covenants contained within our various funding agreements.

A key part of the activities of our joint venture contract hire companies is the management of funding. Substantially all of the interest rate exposures of these companies are managed through term borrowings or the use of derivatives. The companies aim to eliminate their exposures rather than seek to make any gain from the future movement in interest rates.

Exchange rate risks The company has very limited currency denominated transactions. Where transaction exposures do arise they are largely hedged. Similarly as the company's overseas activities are small there are few translation exposures. Currently no translation exposures are hedged. Should exposures increase beyond a specified de minimis current policies dictate that appropriate hedging will be initiated.

International Financial Reporting Standards (IFRS) RAC plc will report 2005 interim and full year results under IFRS, including comparative information for 2004. We will also communicate the 2004 results restated for IFRS, and the opening balance sheet, to shareholders and the wider financial community in the first half of 2005. We consider ourselves to be well prepared for these changes.

The following new accounting standards will have most effect on RAC:

Share-based payments (IFRS 2) Share option awards are not currently charged to earnings, on the basis that such awards have been granted either at the market value of the underlying share or under an approved SAYE scheme. Under IFRS the fair value of the option grant will be measured and charged to earnings over the vesting period.

Goodwill amortisation and Intangibles (IFRS 3 and IAS 36 & 38) Current policy is either to amortise goodwill over its estimated useful life, or to perform an annual review for impairment. Under IFRS we will cease to amortise goodwill, but will continue with the annual impairment reviews. At the same time, a wider range of intangible assets will be recognised than under UK GAAP for acquisitions occurring after 1 January 2004, and these will continue to be amortised. The acquisition of renewal rights in relation to the AXA Direct business undertaken in 2004 will be treated accordingly.

Pensions (IAS 19) Under IAS 19, in addition to the service cost for pensions, which is charged to payroll costs (and is broadly comparable to SSAP 24) there will be a financing charge on the scheme deficit which will appear within net financing charges. Also, under IFRS, pension scheme assets and liabilities will be carried on the balance sheet at fair value. Actuarial gains and losses will be recognised immediately in the statement of recognised income and expenditure.

Leases (IAS 16, 17 & 18) IFRS require depreciation to be charged on a straight line basis, rather than on the actuarial after tax (AAT) basis used in Lex Vehicle Leasing. IFRS also require changes in the basis for maintenance cost accounting which will affect both Lex Vehicle Leasing and Lex Transfleet. These changes have no pre-tax cash impact on our contract-

hire businesses, and no impact on profits over the life of an individual lease. However, they will tend to change the profile of profits during the life of the vehicle lease, and in a growing business will have the effect of deferring profit recognition in comparison with our current UK GAAP treatment.

Legal revenue recognition (IAS 18) Under IFRS, revenue in our legal practice will be recognised based on an assessment of the proportion of the case which has been completed, rather than on the current basis of payments received. Given that payments are typically made only on case completion, this will have the effect of bringing forward revenue recognition.

The first three areas will affect RAC in common with many UK public companies. The final two (leases and legal revenue recognition) are more specific to RAC and, taken together, are not expected to be material to RAC's operating profitability.

Insurance Mediation Directive Parts of RAC plc, particularly the Consumer business, have become regulated by the FSA under the General Insurance Regulation provisions with effect from 14 January 2005. The Regulation covers, amongst other things, the conduct of business, risk assessment procedures and capital adequacy considerations in respect of the company's roadside breakdown, motor insurance and other general insurance activities.

Directors and management



Peter Smith BSc, FCA Aged 58, Chairman. Appointed to the Board on 1 January 2003 as non-executive Deputy Chairman and became Chairman on 30 April 2003. He was UK Senior Partner of PricewaterhouseCoopers until July 2000 and a member of its Global Management Board.

He is a non-executive director of N M Rothschild & Sons Ltd and of The Equitable Life Assurance Society. In 2004, he relinquished his non-executive directorship in Safeway plc and was appointed as a non-executive director and Chairman of Savills plc, the international property services group; he was also appointed as a non-executive director of Templeton Emerging Markets Investment Trust.

He is a member of the Finance and General Purposes Committee of the CBI and sits on the Harvard Business School's Global Corporate Governance Advisory Council. (Nom*)



Peter Long CIMA Aged 52, non-executive director. Appointed as a non-executive director in February 2001. He is Chief Executive of First Choice Holidays plc and was formerly Chief Executive of Sunworld Ltd having previously been Finance Director then Chief Executive of the tour operating division of International Leisure Group. He is a non-executive director of Rentokil Initial plc. (Aud*, Nom and Rem)



John Warren BSc, FCA Aged 51, non-executive director. Appointed as a non-executive director in September 2003. He is the Group Finance Director of WH Smith plc and his previous appointments include Group Finance Director of United Biscuits Holdings plc and a non-executive directorship of Rexam plc. (Aud, Nom and Rem)



John Poulter MA Aged 62, non-executive director. Appointed to the Board in April 2002. He is Chairman of Spectris plc, an international instrumentation and controls business, which he joined in 1988 after an earlier career with Cambridge Instruments and BTR plc. He was Chief Executive for ten years prior to becoming non-executive Chairman in 2001. He is a non-executive director of Kidde plc, Smaller Companies Value Trust plc and The London Metal Exchange. (Aud, Nom and Rem*)



Dianne Thompson BA, FCIM Aged 54, non-executive director. Appointed as a non-executive director in February 2002. She is currently Chief Executive of Camelot Group plc. Her previous appointments include Marketing Director for the Signet Group, Director of Marketing for Woolworths and Managing Director of Sandvik Saws and Tools. (Aud, Nom and Rem)



Andrew Harrison BA, MBA Aged 47, Chief Executive. Appointed to the Board as Chief Executive in 1996. He was previously a director of Courtaulds Textiles plc, responsible for its International Fabrics and Home Furnishings businesses, having worked for the Courtaulds group since 1986. He is a non-executive director of Emap plc, where he is the Chairman of the Audit Committee. (Nom)



Peter Harris BA, FCA Aged 53, Group Managing Director, Manufacturer Support Services. Appointed to the Board on joining Lex Service PLC as Finance Director in 1994 he currently leads the businesses which provide outsourced business services to vehicle manufacturers and fleet operators. These businesses include Lex Auto Logistics, Lex Transfleet, Lex Commercials, Hyundai Car (UK), Lex Defence and RAC Software Solutions. He is a non-executive and senior independent director of Wembley plc and Chairman of Coworth-Flexlands School Ltd.



Debbie Hewitt MBA, FIPD Aged 41, Group Managing Director, RAC Roadside Services. Joined the Company in 1987 and held various personnel and operational positions in Lex Retail prior to her appointment as Human Resources Director in December 1997. She was appointed to the Board in January 2000 and from May 2004 became Group Managing Director of RAC Roadside Services, which provides vehicle breakdown and recovery assistance to motorists. She is a non-executive director, and Chairman of the Remuneration Committee, of De Vere Group plc.



Richard Pennycook BSc, FCA Aged 40, Group Finance Director. Appointed to the Board in August 2003 as Group Finance Director. His previous appointments include Group Finance Director of JD Wetherspoon, Laura Ashley, Welcome Break and HP Bulmer. He is a non-executive director of jibeanos and was a non-executive director of Richer Sounds plc until 17 February 2004.



Jon Walden FCA Aged 51, Managing Director, Lex Vehicle Leasing. Having previously held a number of senior management positions within the Company he rejoined in May 1999 and was appointed to the Board in January 2000 as Managing Director of Lex Vehicle Leasing. From September 2004 he was responsible for leadership of the RAC Consumer Services business. His previous appointments within the Company included Deputy Chief Executive of Volvo Concessionaires, overseeing the Company's acquisition of Hyundai Car in the UK, and Managing Director of both Lex Vehicle Leasing and Lex Retail. He is a non-executive director of Morgan Sindall PLC.

Executive Board

Andrew Harrison *Chief Executive, RAC plc*
Simon Carter *Group Quality and Systems Director, RAC plc*
Peter Harris *Group MD, Manufacturer Support Services*
Debbie Hewitt *Group MD, RAC Roadside Services*
Jill Nealon *Group Human Resources Director, RAC plc*
Richard Pennycook *Group Finance Director, RAC plc*
Jon Walden *Managing Director, Lex Vehicle Leasing*
Duncan Wilkes *Group MD, RAC Business Solutions*

Secretary

Pamela Coles

Notes

Committee membership
 (Aud) – Member of the Audit Committee
 (Nom) – Member of the Nominations Committee
 (Rem) – Member of the Remuneration Committee
 *Committee Chairman

Directors' report

The directors of RAC plc submit their report and the audited financial statements for the financial year ended 31 December 2004.

Principal activities The principal activity of the Company is to provide a range of motoring and vehicle services to individual and business customers.

Business review and future developments The directors' report should be read in conjunction with the operating and financial reviews on pages 20 to 27 and the Chairman and Chief Executive's joint statement on pages 18 and 19 which together include information about the Company, its subsidiaries and associated companies including the financial performance during the year and likely future developments.

Acquisitions/Disposals In September 2004 the Group announced its agreement with AXA to buy out AXA's interest in RAC Financial Services, which was established in 2002, and to acquire the renewal rights of AXA Direct - AXA's personal lines direct insurance business which provides motor and home cover.

During 2004 the Group disposed of Lex Manutention S.A., Lex Havelange S.A. and the net assets of Lex Komatsu Forklift (South) Limited, thus completing its divestment of the mechanical handling businesses, and the net assets of both Multipart Universal and Isuzu Truck (UK) Limited.

Details of these acquisitions and disposals are contained in the financial review on pages 24 and 25, and in notes 28 and 29 on pages 68 and 69.

Dividends The directors recommend a final dividend of 15.6p per share (2003 – 14.6p) which, with the interim dividend already paid, will provide total dividends for the year of 25.8p per share, an increase of 6.2% on the 24.3p paid in respect of last year. Payment of the recommended final dividend, if approved at the Annual General Meeting, will be made on 5 May 2005 to shareholders registered at the close of business on 8 April 2005.

Share capital Details of the Company's authorised and issued share capital at 31 December 2004, of shares issued during the year and of options granted under the Company's employee share schemes, are detailed in notes 6 and 23 to the financial statements on pages 55, 56 and 66.

Purchase by the Company of its own shares The authority given at last year's Annual General Meeting for the Company to purchase in the market up to 11.8

million of its own shares, representing approximately 10% of the share capital in issue on 31 December 2003, expires at the close of the 2005 Annual General Meeting. No shares have been purchased pursuant to this authority. The directors are seeking to renew this authority (i.e. for the Company to purchase in the market up to 11.84 million of its own shares, representing approximately 10% of the share capital in issue on 31 December 2004) at the forthcoming Annual General Meeting. The Board announced in December 2004 that it has approved a share buy-back programme to purchase up to £20 million of shares for treasury, if the market conditions are deemed appropriate. Beyond that, the Board has no present intention to make market purchases but would like to retain the flexibility to do so.

Purchases will be made only if the directors deem them to be in the best interests of shareholders generally. The authority sought by this resolution will expire at the conclusion of the Annual General Meeting to be held in 2006 or, if earlier, 14 July 2006. The directors intend to seek renewal of this authority at each Annual General Meeting.

Authority to allot shares A resolution will be proposed at the forthcoming Annual General Meeting to give the Board authority to allot unissued shares up to an aggregate nominal value of £9,500,000 which represents approximately one third of the issued share capital of the Company. If approved, the authority will expire at the conclusion of the Annual General Meeting to be held in 2006 or, if earlier, 14 July 2006.

A resolution will also be proposed seeking shareholders' approval for renewal of the authority given at last year's Annual General Meeting to enable the directors, to a limited extent, to issue ordinary shares for cash without first offering such shares to existing shareholders in proportion to their holdings. The authority being sought is for a maximum nominal value of £1,480,000 being approximately 5% of the issued share capital of the Company. If approved, the authority will expire at the conclusion of the Annual General Meeting to be held in 2006 or, if earlier, 14 July 2006. It is not currently the intention of the directors to issue for cash any part of the unissued share capital for purposes other than upon the exercise of options granted under the Company's employee share schemes.

Substantial shareholders Details of shareholders who have notified the Company that they have an interest in 3% or more of the Company's issued share capital are set out on page 80.

Fixed assets The Group's tangible fixed assets are included in the financial statements at cost less accumulated depreciation. The properties are employed in the business and many of them were acquired when market values were significantly lower than at present. The directors consider that a surplus over book value exists but have not quantified the excess.

Going concern The directors consider that the Company, and therefore the Group as a whole, has adequate resources to continue its operational activities for the foreseeable future. The directors therefore continue to adopt the going concern basis in preparing the financial statements.

Directors The names and biographical details of the current directors, all of whom held office throughout the whole of 2004, are given on pages 28 and 29. There were no resignations from, or appointments to, the Board during the year.

In accordance with the Company's articles of association, Peter Harris, Andrew Harrison and Dianne Thompson will retire by rotation at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election. Peter Harris and Andrew Harrison are executive directors and their service contracts are terminable upon one year's notice from the Company. Dianne Thompson is a non-executive director and does not have a service contract.

Details of directors' interests in the Company's ordinary shares are set out in the Remuneration Report on pages 35 to 41.

A table showing each Director's record of attendance at meetings held during 2004 is shown in the Corporate Governance section on page 34.

Employee relations **Employee involvement** The Company believes that, to achieve excellent customer service, its employees should be well informed about the Company's plans and performance and have the opportunity to discuss their performance regularly with their managers. The Company is therefore committed to providing all its employees with information on a regular basis and to encouraging their participation in schemes where they will benefit from the Company's progress and profitability.

Employees receive information about the Company in several different forms. There are publications such as the annual report and accounts, the interim report and 'Juice', a magazine which is sent to all employees at least twice a year.

Individual businesses also produce their own in-house newspapers. The Company's intranet provides details on all businesses in the Group, copies of the latest press releases and vacancies across the Company as well as access to a bespoke on-line learning resource.

Open communication and feedback operates throughout all parts of the Group. In 2004, employees were engaged regularly in large scale briefings from their business managing directors and Executive Board members. Views and opinions were also collected in the annual colleague satisfaction survey, which was completed by 86% of employees in 2004, and we act positively to address the issues that they raise.

The Board is committed to acting with integrity towards each of our stakeholder groups and has an established 'Safety Net' policy which enables all of our colleagues to raise their concerns in confidence, and without fear of reprisals. This policy, which is part of our integrity commitment, can be viewed on the website (www.racplc.co.uk).

Employees are encouraged to become involved in the performance of the Company through a variety of share schemes. The principal schemes are the Long Service Share Award Scheme (under which employees receive ordinary shares according to their length of service), the Sharesave Scheme and the Executive Share Option Scheme.

Employment of disabled persons It is the Company's policy to ensure that disabled persons are treated fairly and consistently in terms of recruitment, training, career development and promotion and that their employment opportunities should be based on a realistic assessment of their aptitudes and abilities. Wherever possible the Company will continue the employment of employees who become disabled during the course of their employment with the Company through re-training, acquisition of special aids and equipment or the provision of suitable alternative employment.

Pensions information The pensions department provides the Company's UK employees with guidance on pension matters during their employment. The department also counsels and assists employees in preparation for retirement.

Community relations Environment The directors regard the protection of the environment as an essential part of the Company's corporate responsibilities.

Within the context of the Group's Environmental Policy, individual companies undertake their own initiatives to address their business specific impacts.

Known environmental risks are closely monitored by the operating companies, Group-wide assessments of environmental risks are frequently undertaken and significant environmental issues are regularly discussed by the Board.

The Group's Environmental Policy, environmental management systems, objectives and targets are reviewed periodically to ensure that they continue to address significant environmental aspects and to achieve continued improvement in the Group's environmental performance.

The Group's annual environmental report, including a policy statement, is available on the website (www.racplc.co.uk).

Health and safety Andrew Harrison, Chief Executive, is the director responsible for health and safety, reinforcing the message that health and safety issues are a high priority for the Group; Group-wide assessments of health and safety risks are periodically undertaken, reported to and discussed by the Board. A copy of the health and safety policy statement is available on the website (www.racplc.co.uk).

In accordance with guidance provided by the Health and Safety Commission, the Board formally recognises its collective responsibility for, and individual directors each accept their individual roles in, providing leadership across the Group.

As part of the Group's commitment to reducing accidents at work, accident statistics across the Group are analysed. This enhances the visibility of areas where improvements can be targeted and is supported by regular status reports on health and safety incidents to the Board.

Charitable donations and contributions for political purposes During the year the Company made charitable donations amounting to £100,000 (2003 – £124,000). This was distributed to a range of charities, the largest donation being a long-term commitment to the Motor and Allied Trades Benevolent Fund, 'BEN'. Included in the 2004 total are donations made by the Company to match the charitable fund-raising activities of our own employees.

There were no contributions for political purposes either in the current or prior year and the Company has no intention of changing its policy of not making donations to political parties.

At the 2003 Annual General Meeting, shareholders agreed to grant the

Company a limited authority to make certain payments which might inadvertently breach the provisions of the Political Parties, Elections and Referendums Act 2000 (the 'Act') in an aggregate amount not exceeding £100,000 in any year. The authority will expire at the conclusion of the Annual General Meeting to be held in 2007 or, if earlier, 29 April 2007 and the Board will not use that authority to make any political donations as that expression would have been understood before the Act became law.

Policy on the payment of suppliers Due to the diverse range of the services offered by the Company's operating businesses, the Company does not follow any uniform code or standard on payment practice. The operating businesses are responsible for agreeing the terms and conditions under which business transactions are conducted with their suppliers. It is Company policy that payments to suppliers are made in accordance with these terms, provided that the supplier is also complying with all relevant terms and conditions.

The amount due to trade creditors at the end of the financial year for the Company represents 38 days (2003 – 33 days) of purchases received from those creditors.

Annual General Meeting The Annual General Meeting will be held at 12:00 noon on Thursday, 14 April 2005 at The Montcalm Hotel, Great Cumberland Place, London W1.

By way of special business, approval is being sought from shareholders for the adoption of new Articles of Association and also for an increase in the Company's authorised share capital. For shareholders, a separate Notice of Meeting document, which includes an explanation of all of the proposed resolutions, will be mailed with this annual report.

Auditors A resolution to re-appoint KPMG Audit Plc as auditors and to authorise the directors to determine their remuneration will be proposed at the forthcoming Annual General Meeting.

The Board's opinion is that re-election and fees of the auditors are inter-related issues and should therefore be dealt with by a single resolution.

The report of the directors has been approved by the Board and signed on its behalf by

Pamela Coles
Secretary
16 February 2005

The Company is committed to high standards of corporate governance and supports the principles of governance set out in the revised Combined Code on Corporate Governance issued in July 2003 (the 'Combined Code'). This report contains the Company's statement on how it has applied the principles set out in the Combined Code, together with its statement of compliance with the Code provisions. These statements are made following a review which has been carried out in relation to the Board's practices. The Company's auditors have reviewed our compliance with those provisions of the Combined Code specified for their review.

Compliance with the Combined Code

The Board is pleased to confirm that throughout the year it has applied the principles of good governance contained in Section 1 of the Combined Code.

With the exceptions as set out below the Company was in compliance throughout the year with the provisions of the Combined Code:

- Provision A.3.2 of the Code stipulates that at least half of the Board should be comprised of non-executive directors. The Board believes that, with four wholly-independent directors and a non-executive Chairman, its membership currently includes a sufficient number of non-executive directors to ensure that an effective balance of views is in place. All of the directors were appointed before the revised Code came into force.
- Reference is made in the Remuneration Report on pages 35 to 41 to the inclusion of fluctuating emoluments within the calculation of pensionable pay (provision B.1.1 by reference to paragraph 6 of Schedule A) although any new executive directors joining after 1 April 2000 will have their pensionable salary calculated by reference to basic salary only. It has been decided, at this time, not to seek to withdraw the benefit from those executive directors to whom the inclusion of fluctuating emoluments in pensionable pay calculations is a contractual entitlement. However, this matter will continue to be kept under review.

The Board There is a clear division of authority and responsibility at the most senior level within the Company through the separation of the roles of Chairman and Chief Executive, and a written schedule setting out their respective responsibilities has been agreed by the Board.

In broad terms, the Chairman is responsible for the leadership and effective running of the Board and ensuring that appropriate strategies, plans and budgets are presented for consideration by the directors, arrangements for Board succession are regularly reviewed, and that all directors, both executive and non-executive, are consulted to enable them to play their full part in the Company's activities.

The Chief Executive is responsible for the executive management of the Group and for the implementation of the strategies, policies and plans approved by the Board.

The Board recognises its responsibility to identify and determine price sensitive information and for ensuring that such information is disseminated in an appropriate manner.

The Board normally meets on nine days during the year (including a two-day strategy meeting held in October). It has a schedule of matters specifically reserved to it, some of which are delegated to Board committees, and these include the approval of the interim and annual results, dividend policy, circulars to shareholders and listing particulars, matters relating to share capital, the approval of the annual budget and all major capital projects, investments and commitments.

The Board currently comprises the Chairman, five executive directors and four non-executive directors. All of the four non-executive directors are considered by the Board to be independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgement. The senior independent director is Peter Long.

Brief biographical details of the current directors of the Company are set out on pages 28 and 29. The non-executive directors are from varied business and other backgrounds and all directors have the benefit of induction visits and briefings following their appointment to the Board. The Company keeps the directors informed about the Company's business and regulatory matters by written briefings and presentations by senior management. The non-executive directors' experience allows them to exercise independent judgement on the Board and their views carry substantial weight in Board decisions. They contribute to the Company's overall strategy, business planning and policy

formulation, in addition to monitoring its performance and its executive management. The non-executive directors are given the opportunity to have meetings together, either with or without the Chairman present, and have so met within the past 12 months.

The non-executive directors are appointed for three years; re-appointment is not automatic, and each non-executive director's position is subject to review prior to the expiry of their term of office. In accordance with the Company's articles of association one third of the Board are required to retire by rotation each year provided that each director shall retire at least once every three years. Directors appointed during the year are required to seek re-election at the first Annual General Meeting following their appointment. There is an agreed procedure for directors to take independent professional advice in the furtherance of their duties, if necessary, at the Company's expense. Directors have access to the advice of the Company Secretary. The removal of the Company Secretary is a matter for the Board as a whole.

An evaluation review of board effectiveness was carried out in 2004 using an independent facilitator, and the outputs and the recommendations from that review are being implemented.

The membership of the Board committees is provided on pages 28 and 29.

The Chairman The Board is mindful of the need to ensure that the Chairman has enough time available to devote to the job. Peter Smith's other significant commitments are described in his brief biography shown on page 28, together with the changes to those commitments that took place during the year; these changes had no material impact upon the amount of time that he was able to devote to his Chairmanship of RAC plc during 2004.

The Executive Board As shown on page 29, the Executive Board comprises the Chief Executive, four business Managing Directors, the Group Finance Director, the Group Quality and Systems Director, and the Group Human Resources Director.

It is collectively responsible for the operational performance of the Company, developing strategy, leading management development and agreeing company-wide operational policies. It meets on a regular basis, usually monthly.

The Nominations Committee The Nominations Committee is established under written terms of reference and comprises the Chairman, the Chief Executive and the four non-executive directors. It is chaired by Peter Smith and meets at least once a year, and at such other times as is required.

It keeps the balance of Board membership under review and makes recommendations to the Board on the appointment of new directors.

The Remuneration Committee The Remuneration Committee is operated under clearly defined terms of reference, is comprised exclusively of independent non-executive directors. This Committee is chaired by John Poulter and its role is described in the Remuneration Report on pages 35 to 41.

The report includes a statement of the Board's policy on the remuneration of executive directors and details of the remuneration of each director. Further details are also set out in note 7 to the financial statements on page 56.

The Audit Committee The Audit Committee comprises all of the non-executive directors and was chaired by Peter Long throughout 2004. The Audit Committee normally meets four times per year and has an agenda linked to events in the Company's financial calendar. Other directors have a right of attendance and other members of management may attend by invitation. The Committee is established with written terms of reference, which include the following main responsibilities:

- monitoring the integrity of the Company's financial statements;
- reviewing the internal control and risk management systems;
- monitoring and reviewing the internal audit function;
- making recommendations to the Board in relation to the appointment of the external auditor and approving the remuneration and terms of engagement of the external auditor following appointment by the shareholders in general meeting;
- monitoring and reviewing the external auditor's independence, objectivity and effectiveness;

- monitoring policy on the engagement of the external auditor for the supply of non-audit services; and
- monitoring the effectiveness of the 'Safety Net' policy in encouraging employees to raise concerns about possible improprieties where ever they may arise.

Audit independence The Audit Committee and Board put great emphasis on the objectivity of our auditors KPMG Audit Plc in their reporting to shareholders.

The annual appointment of auditors by the shareholders at the Annual General Meeting is a fundamental safeguard but, beyond this, controls have been in place for some years to ensure the independence of the auditors.

The KPMG audit director and senior manager are present at Audit Committee meetings to ensure full communication.

The overall performance of the auditors is reviewed annually by the Audit Committee based on their own assessment of the auditors' performance and assisted by management feedback. Feedback is also provided to independent reviewers appointed by KPMG Audit Plc for review on a periodic basis. This activity forms part of KPMG Audit Plc's own system of quality control. The Audit Committee has regular meetings with the auditors, without executive management being present.

The scope of the year's audit is discussed in advance by the Audit Committee. Rotation of the audit director's responsibilities within KPMG Audit Plc is included within the Audit Committee's annual review and is also required by their profession's ethical standards. The audit director responsible for the engagement has held his role for two years. There is also rotation of personnel within the audit teams.

Assignments with KPMG Audit Plc and its associates are, and have been, subject to controls by management that have been agreed by the Audit Committee so that audit independence is not compromised. In summary the procedures are:

- Audit related services: As auditors this is the main area of work of KPMG Audit Plc and its associates. It includes formalities relating to shareholder circulars, regulatory reports and work in respect of acquisitions and disposals.

- Tax consulting: In cases where they are best suited, the Company uses KPMG and its associates, but also uses other tax consultancies. Significant pieces of tax work are evaluated competitively.
- General and systems consulting: All significant consulting projects are put out to competitive bids. KPMG is only allowed to tender when Group management and KPMG are satisfied that the nature of the work presents no potential threat to the independence of the audit team. Of the general and systems consulting work that has taken place in the Group in recent years, KPMG and its associates has had only a small part.

In accordance with the policies set by the Audit Committee, the Group Finance Director must approve and authorise all non-audit work carried out by KPMG Audit Plc and its associates anywhere in the Group in excess of a predetermined financial threshold. A part of this process is to determine that other potential providers of the services have been adequately considered. The Audit Committee also receives and reviews regular reports on the non-audit work that is carried out by the auditors under that authority.

Remuneration for non-audit work undertaken in 2004, and sanctioned by the Committee, is shown in note 4 to the Accounts; further assurance services included advice on IFRS, half-year review, business disposals and completion accounts; tax advice was for work undertaken in respect of VAT repayment claims for earlier years.

Taken together these controls and procedures provide the Audit Committee with adequate confidence in the independence of KPMG Audit Plc in its reporting on the audit of the Group.

Internal control The directors are responsible for establishing and maintaining the systems of internal control and risk management throughout the Group and the joint venture companies and for reviewing their effectiveness. The systems are designed to manage risks that may impede the achievement of the Group's business objectives rather than to eliminate these risks. The internal control system can therefore provide only reasonable, not absolute, assurance against material misstatement or loss.

There is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group and this has been in place, across the Group and the joint venture companies, during the year under review and up to the date of approval of this report. That process is regularly reviewed by the Board and accords with the Combined Code and related guidance (the Turnbull guidance on Internal Control).

The processes used by the Board to review the effectiveness of the systems of internal control, including financial, operational and compliance controls and risk management systems, for the period included the following:

- a control environment which includes an organisation structure with clearly defined levels of responsibility and authority in addition to documented controls and procedures appropriate to the specific area;
- financial reporting procedures which require the Board to approve the annual budget, review monthly trading results, balance sheets and cash flows against plan, and receive explanations from management on significant variances;
- a risk management process in which senior managers around the Group confirm the nature and extent of the significant risks facing their businesses and the likelihood of their materialising and the controls in place to manage such risks;
- regular reporting to the Board on risk management, including health, safety and environmental risks and risk transfer, and the internal control

environment, and from a number of functions, including Treasury and Tax; and

- formal statements prepared by the Chief Executive and by the managing directors of each operating division and company, in which they acknowledge their responsibility for the internal control and risk management systems in their businesses and confirm that they have reviewed the effectiveness of those systems.

Procedures for monthly reporting on internal control issues enable management to identify any control problems and to ensure that prompt and effective remedial action is taken.

The Group's control systems and processes are subject to risk focused internal audit which plays an important role in providing independent assurance to management and the Audit Committee on key control processes.

The Audit Committee reviews internal audit plans and reports, together with external audit plans and management letters.

The scope of the work, authority and resources of internal audit are reviewed by the Audit Committee, which also conducts a self-appraisal exercise to monitor its own effectiveness, annually.

Board meeting and committee attendance in 2004 The table below shows the record of each Director's attendance at the Board Meetings held during the year, and also at the principal committees of which they were members:

All of the Directors attended the Company's Annual General Meeting held on 29 April 2004.

Shareholder relations The Company is committed to ongoing communications across its shareholder base, whether institutional investors, private or employee shareholders.

Regular feedback is obtained of the views and opinions of major shareholders, and these are communicated to the Board as a whole. On 14 May 2004, the Company hosted an Investor Day for institutional investors and analysts at which presentations were given to enable them to enhance their understanding of the Group's key business areas.

The Company's website (www.racplc.co.uk) provides both corporate and customer information and is updated on a regular basis.

The chairmen of the Audit, Nominations and Remuneration Committees are available at Annual General Meetings to take any relevant questions. The proxy votes cast at general meetings are made available to all shareholders and are announced at the meeting. The Company proposes a separate resolution on each substantially separate issue and does not bundle resolutions together inappropriately.

Shareholders have been asked to vote on the Remuneration Report since the Annual General Meeting held in 2001 and the Board will be asking shareholders to approve the Remuneration Report at the forthcoming Annual General Meeting.

Name of director	Board	Nominations Committee	Remuneration Committee	Audit Committee
Andrew Harrison	9/9	3/3	–	–
Peter Harris	9/9	–	–	–
Debbie Hewitt	9/9	–	–	–
Peter Long	8/9	3/3	9/9	4/4
Richard Pennycook	9/9	–	–	–
John Poulter	9/9	3/3	9/9	4/4
Peter Smith	9/9	3/3	–	–
Dianne Thompson	9/9	1/3	8/9	3/4
Jon Walden	9/9	–	–	–
John Warren	9/9	3/3	9/9	4/4

The Remuneration Committee's composition, responsibilities and operation comply with Section 1(B) of the revised Combined Code on Corporate Governance issued in July 2003.

This report covers the remuneration policy for directors and includes specific disclosures relating to directors' emoluments and for their shares and other interests. Although the Board considers itself ultimately responsible for both the framework and the cost of executive remuneration, it has delegated prime responsibility for executive remuneration to the Remuneration Committee.

The Remuneration Committee is a committee of the Board consisting exclusively of independent non-executive directors ('the Committee') and its membership throughout 2004 was as follows:

John Poulter (Chairman)
Peter Long
Dianne Thompson
John Warren

The Committee is established under written terms of reference. It is responsible for determining executive directors' remuneration, which is reviewed annually. It also reviews proposals in respect of other senior managers immediately below Board level, based on broadly the same structure. The Committee determines targets for performance related share schemes operated by the Company and oversees any major changes in employee benefit structures throughout the Group.

In carrying out its responsibility the Committee takes advice from a leading independent remuneration consultancy, New Bridge Street Consultants LLP, in respect of the design and implementation of its employee share schemes, and the market levels of remuneration in comparable companies. In 2003 the Committee formally engaged New Bridge Street Consultants LLP to advise it on remuneration matters. The Committee uses Mercer, the pensions specialist, for the provision of advice on pensions. Mercer is also the pension scheme's actuary and supplies the Company with specialist advice on healthcare arrangements but, apart from the foregoing, the Committee's advisers provide no other services to the Company.

The Committee consults with the Chief Executive about proposals relating to the remuneration of executive directors, other than himself, and the Group Human

Resources Director attends its meetings. In setting remuneration packages for executive directors it also has regard to senior managers' pay and employment conditions elsewhere in the Group.

In 2004 the Committee met nine times and, apart from the one occasion on which one director was absent, these meetings were attended by all of the members. The Committee's formal Terms of Reference are available on request from the Company Secretary.

The disclosure information set out below relating to directors' emoluments, pension entitlements, interests in shares and options over shares, is included within the scope of the audit.

Remuneration policy The Company's remuneration policy is to ensure that executive directors' remuneration properly reflects their duties and responsibilities and is sufficient to attract, retain, motivate and reward high calibre senior management collectively capable of delivering the goals of the Company. Furthermore, the objective is to ensure that incentive schemes are in line with best practice and generate alignment with the interests of our shareholders.

Anticipated total earnings, including bonus and incentive awards, are compared to payments made by organisations of similar size and complexity. The policy for setting remuneration levels is for fixed remuneration to be set by reference to the median and to reflect individual experience and performance. For exceptional performance, the Committee believes that the remuneration package should deliver upper quartile levels of total remuneration. In order to achieve this policy, variable pay makes up a significant proportion of executive directors' remuneration packages. Variable pay comprises an annual bonus scheme and an annual grant share option scheme, under which rewards to executive directors are linked to the achievement of demanding financial performance targets. Performance criteria for both schemes incorporate sliding scales of reward meaning that executive directors are incentivised to perform at the highest level.

The main components of executive directors' remuneration are basic salary, a performance related annual bonus scheme, longer term incentives, pension provision and benefits. The details of these arrangements for the year to 31 December 2004 are set out in the remainder of this report.

There were no departures during the year from the remuneration policies stated herein and this report will be presented to shareholders for their approval at the forthcoming Annual General Meeting.

Salary Salaries reflect the executive directors' experience and responsibility. Salary levels are reviewed annually by reference to external market data and a comparator group of UK listed companies in the Support Services, Vehicle Distributors and Transport sectors.

The policy is to set basic salary levels by reference to the median, or to the relevant quartile of the comparator group for appropriate performance, and total remuneration at the upper quartile of the comparator group.

The Committee's next annual review of executive directors' salaries will take place in April 2005.

Bonus Bonuses for executive directors are performance related and based on a formula recommended by and discussed with independent consultants and approved by the Committee. The bonus structure is reviewed annually to ensure that it reflects the priorities of the business.

The 2004 bonus scheme provided for a maximum bonus entitlement of 50% of basic salary for all executive directors and other members of the Executive Board of management with 'on-target' bonus levels of 35% of basic salary for Peter Harris and Jon Walden, and 30% of basic salary for the other executive directors.

Measurement was by reference to targeted levels of profitability as well as non-financial performance criteria. The major part of the 'above-target' bonus could only be earned upon the achievement of stretching levels of financial performance. The bonus arrangements for Peter Harris, Debbie Hewitt and Jon Walden included measures linked to financial, growth and other key objectives within Manufacturer Support Services, RAC Roadside and Lex Vehicle Leasing respectively.

In recognition of his additional responsibility for the RAC Consumer business, Jon Walden earned a one-off discretionary bonus payment of £23,000 for the achievement of specific financial and non-financial performance objectives for that business.

Remuneration report

The percentages of base salary payable to the executive directors as bonus (excluding the one-off discretionary bonus referred to in the previous paragraph) was as follows:

	2004	2003
Andrew Harrison	39.2%	40.5%
Peter Harris	45.0%	46.1%
Debbie Hewitt	35.5%	40.5%
Richard Pennycook	39.2%	40.5%
Jon Walden	42.5%	42.5%

The Committee has established that the 2005 bonus scheme will again have a maximum entitlement of 50% of basic salary and that the 'on-target' bonus levels and the performance measures will be broadly similar to the arrangements for the 2004 bonus scheme.

Long term incentive arrangements

The Company's senior managers and executives participate in the RAC plc Executive Share Option Scheme (2001) (the 'Scheme'), which contains both Inland Revenue approved and unapproved sections. Options are granted annually, with grant levels determined by seniority, an individual's potential and their past performance. The Committee oversees the operation of the Company's formal appraisal system in determining the employees' performance for option grants.

The most senior employees may be granted options over shares worth up to a maximum of three times salary. Grants of share options over lower multiples of salary are made to other executives. Options have a seven year life and are normally exercisable no earlier than three years from the date of grant to the extent that the performance targets have been met.

The most senior executives, who will generally receive the higher option grants, will have more stretching targets attached to a significant proportion of their option grants. Performance targets attached to options granted in 2004 require normalised EPS growth of RPI plus 3%, 4% and 5% per annum for option grants over shares worth up to one, two or three times an individual's rate of salary respectively.

There will be no re-testing if the initial performance conditions should fail to be met. It is anticipated that options to be granted in 2005 will have similar performance targets to those granted in 2004, and again there will be no re-testing.

The Committee will verify whether the performance conditions have been satisfied. Although the Scheme Rules do provide for re-testing of the performance conditions on no more than two occasions, the Committee's policy is that, for all share options granted in 2004 or later, the performance targets will not be re-tested in this way.

An EPS basis was chosen for setting the performance conditions as this is an appropriate way of aligning the interests of senior executives with shareholders and requires a sustained, significant and demanding improvement in the Company's earnings' performance (and the exercise of an option already requires an improvement in share price performance since the time of its grant in order to merit it being exercised).

Options held under the Scheme by the executive directors who were in office during the year are set out in the table on page 39.

Pension arrangements The Company operates a final salary pension scheme and the policy and arrangements for executive directors are set out in detail on pages 40 and 41.

Service agreements for executive directors All executive directors have one year rolling contracts and no service contract of any executive director contains provisions for pre-determined compensation on termination which would exceed one year's salary and benefits in kind.

When calculating any termination payments, the Committee will take into account a variety of factors including age, years of service and the individual director's performance and obligation to mitigate his/her own loss, for example by obtaining new employment.

Policy on external directorships The Company recognises that its executive directors may be invited to become non-executive directors of other companies and that this additional experience may benefit both the Company and the development of individual directors.

Executive directors are therefore permitted to accept one non-executive appointment each, provided it is not with a competing company, is not likely to lead to any conflict of interest, does not interfere with the abilities of the individual to perform his or her function as an executive director of the Company and can be demonstrated to have benefits for the development of the individual or the Company.

The fees payable to an executive director by another company, for service as a non-executive director of that company, are retained by the individual director.

The fees receivable by executive directors in respect of their non-executive directorships in other companies during 2004 were as follows:

	2004	2003
Andrew Harrison	£42,000	£40,500
Peter Harris	£31,956	£31,500
Debbie Hewitt	£34,875	£30,000
Richard Pennycook	Nil	Nil
Jon Walden	£25,000	£25,000

Non-executive directors Remuneration of the Company's non-executive directors is determined by the Board itself, upon receipt of advice from external consultants, but the non-executive directors take no part in the decisions reached.

Non-executive directors do not participate in any of the incentive schemes. Each non-executive director has a letter of appointment for a fixed period of three years. The terms of appointment do not contain any express contractual provisions requiring a notice period or the right to receive any compensation in the event of early termination.

The non-executive directors' fees are reviewed periodically and at 1 January 2005 fees were payable at the rate of £30,000 per annum to each non-executive director (2004: £30,000). An additional amount of £5,000 per annum is paid for chairmanship of the Board's Remuneration Committee or Audit Committee (2004: £5,000 for each chairmanship).

Chairman Peter Smith was appointed to the Board initially as non-executive Deputy Chairman on 1 January 2003 at a fixed rate of £150,000 per annum, and became Chairman at the conclusion of the 2003 Annual General Meeting held on 30 April 2003. His appointment is for a fixed period of three years from 1 January 2003 and is terminable upon three months' notice by the Company or six months' notice by him; in the event of early termination of the appointment there is no right to receive any compensation from the Company.

Share option schemes Prior to 1998, options were granted under successive executive share schemes and a small number of options which were outstanding under the Executive Share Option Scheme (1994) (the '1994 Scheme') were exercised during 2004.

Directors' emoluments The emoluments of the directors during the year ended 31 December 2004 are shown in the following table:

Name of director	Date of Contract	Fees and salary £	Bonus £	Other benefits ⁵ £	Additional pension supplement ⁶ £	Total 2004 £	Total 2003 £
Peter Smith Chairman	1 Jan 2003	150,000	–	–	–	150,000	150,000
Executive directors							
Andrew Harrison Chief Executive	2 Sep 1996	472,200	185,102	23,205	–	680,507	646,088
Peter Harris	18 Aug 1995	256,200	115,290	18,694	–	390,184	372,383
Debbie Hewitt	19 Jun 1995	215,925	76,653	17,500	–	310,078	280,814
Richard Pennycook	4 Aug 2003	261,250	102,410	26,659	32,000	422,319	164,430
Jon Walden	26 May 1999	264,975	135,947	21,117	49,117	471,156	423,490
Non-executive directors							
Peter Long ¹	21 Feb 2001	35,000	–	–	–	35,000	31,343
John Poulter ²	24 Apr 2002	35,000	–	–	–	35,000	29,667
Dianne Thompson ³	1 Feb 2002	30,000	–	–	–	30,000	28,010
John Warren	1 Sep 2003	30,000	–	–	–	30,000	9,333
Former directors ⁴		–	–	–	–	–	192,424
Totals		1,750,550	615,402	107,175	81,117	2,554,244	2,327,982

Notes:

1 On 18 February 2004 Peter Long's appointment was extended for a further period of 3 years to 20 February 2007.

2 On 15 February 2005 John Poulter's appointment was extended for a further period of 3 years to 23 April 2008.

3 On 14 December 2004 Dianne Thompson's appointment was extended for a further period of 3 years to 31 January 2008.

4 Former directors who served in 2003 – Paul Hewitt (to 31 March) and Sir Trevor Chinn (to 30 April).

5 Each executive director is provided with a company car, fuel, medical insurance and (apart from Debbie Hewitt and Richard Pennycook) life insurance. A cash adjustment is made if the company car provided has a lower or a higher value than an individual's entitlement and included within 'Other benefits' are cash supplements of £3,900 each paid to Andrew Harrison, Peter Harris and Debbie Hewitt, £2,352 paid to Jon Walden and a cash deduction of £77 for Richard Pennycook.

6 Jon Walden and Richard Pennycook received additional payments to supplement their pension funds as they do not participate in the FURBS arrangements referred to in the Pensions disclosure table on page 40.

A long term incentive plan ('LTIP') was introduced in 1998 and the most recent award of shares granted under that plan took place in 2000, and vested in 2003. The Committee does not intend to grant any further LTIP awards for the foreseeable future.

In 2001, an executive share option scheme (the '2001 Scheme') was adopted to replace the LTIP. The Committee's policy for granting options under the 2001 Scheme is explained in the section entitled 'Long term incentive arrangements' on page 36.

The Company also operates a Sharesave Scheme, and details of the directors' options outstanding under that, and the other share option schemes, are shown in the table on page 39.

Executive Share Option Scheme (1994)

Awards under the 1994 Scheme were conditional upon achievement of positive total shareholder return against the weighted average total shareholder return for motor distributor companies. The performance condition attached to those options unexercised at the start of 2004 had already been achieved and all outstanding options were exercised during the year.

Executive Share Option Scheme (2001)

For all options granted in 2001, the following performance conditions applied:

- for grants of options over shares worth up to one times an individual's rate of salary, earnings per share (EPS) for the financial year end 2003 must have been at least 42p;

- for the balance of options over shares worth above one times an individual's rate of salary but not more than two times an individual's rate of salary, EPS for the financial year end 2003 must have exceeded 44p;
- for the balance of options over shares worth above two times an individual's rate of salary, EPS for the financial year end 2003 must have exceeded 45p.

If these targets had not been attained in full in respect of the financial year ending 2003, the performance conditions would have been re-tested using the 2004 or 2005 EPS results, with the EPS targets of 42p, 44p and 45p inflated by RPI plus 3%, 4% or 5% per annum for option grants over shares worth up to one, two or three times an individual's rate of salary respectively. To the extent that these targets had not been satisfied after five years, the options would have lapsed.

Remuneration report

Directors' interests in shares The directors' beneficial interests in ordinary shares of the Company at the end of the year were as follows:

Name of director	Beneficial interests in ordinary shares	
	As at 1 January 2004	As at 31 December 2004
Andrew Harrison	103,870	84,771
Peter Harris	79,200	79,250
Debbie Hewitt	66,423	47,324
Peter Long	5,000	5,000
Richard Pennycook	–	–
John Poulter	5,000	5,000
Peter Smith	12,000	12,000
Dianne Thompson	–	–
Jon Walden	5,000	5,000
John Warren	1,646	1,646

Notes:

- 1 There were no changes in the interests of directors in shares, or options over shares, between 1 January 2005 and 15 February 2005.
- 2 The executive directors are technically interested in all of the ordinary shares held by the trustees of the 2001 ESOS Trust as potential beneficiaries of the trust, along with all other employees of the Company and its subsidiaries. The trust held 3,778,268 ordinary shares at 31 December 2004 (2003 – 2,727,500 shares).
- 3 As beneficiaries under the Employee Benefit Trust, the directors are deemed to be interested in the shares held by the trust to fulfil entitlements under the Long Term Incentive Plan. The trust held 124,685 ordinary shares at 31 December 2004 (2003 – 124,685 shares).

For all options granted in 2002 and subsequent years, the performance targets require normalised EPS growth of RPI plus 3%, 4% and 5% per annum for option grants over shares worth up to one, two or three times an individual's rate of salary respectively.

If the targets for options granted in 2002 are not attained in full in respect of the financial year ended 2004 then the performance conditions may be re-tested using the 2005 or 2006 EPS results, with the EPS targets inflated by RPI plus 3%, 4% or 5% per annum for option grants over shares worth up to one, two or three times an individual's rate of salary respectively. To the extent that these targets are not satisfied after five years, the options will lapse. The performance conditions for options granted in 2003 are also capable of being re-tested on a similar basis to those granted in 2002, but at the end of the 2006 or 2007 financial years.

For options granted in 2004 and beyond, no re-testing of the performance conditions will take place in the event that the EPS targets are not attained in full by the third anniversary of the grant date, and if not so attained the options accordingly would lapse.

Sharesave Scheme Under the terms of the Sharesave Scheme, the Board may offer options to purchase ordinary shares in the Company to those eligible employees, including executive directors, who enter into an Inland Revenue approved Save-As-You-Earn ('SAYE') savings contract. All employees in the United Kingdom are eligible to participate in the Sharesave Scheme.

The price at which options may be offered is up to a maximum discount of 20% of the market value of a share on the relevant invitation date. The options may normally be exercised during the period of six months after the completion of the SAYE contract, whether three or five years after entering the Sharesave Scheme.

In 2004, options were granted under the Sharesave Scheme at a price of 524p per share to all eligible applicants, including the executive directors. The non-executive directors are excluded from participation in this scheme.

Directors' share ownership guidelines

In order to align further the interests of the executives with those of shareholders, the Committee has introduced a shareholding guideline for the Executive Directors and members of the Executive Board. The executives are expected to build up and maintain a personal shareholding of RAC plc ordinary shares equal to once times annual salary. It is expected that the shareholding will be achieved through the retention of shares acquired through the Company's Executive Share Option Scheme and be achieved within five years of adoption of the guidelines, or of the executive's appointment date if later.

Directors' interests in share options Details of options held at 31 December 2004 under the Company's Sharesave and Executive Share Option Schemes are shown in the table below.

Name of director	Options held at 1 January 2004	Options granted during the year	Options exercised during the year	Options held at 31 December 2004	Option exercise price per share	Earliest normal exercise date	Expiry date	Market price on date of exercise	Gain on exercise of share options ¹
Andrew Harrison									
Sharesave	901	–	901	–	430p	01.11.04	01.05.05	640p	£1,892
	800	–	–	800	461p	01.11.06	01.05.07	–	–
	–	719	–	719	524p	01.11.07	01.05.08	–	–
Executive (1994)	113,378	–	113,378	–	441p	02.09.00	02.09.04	683p	£274,375
Executive (2001)	193,632	–	–	193,632	581p	21.06.04	21.06.08	–	–
	233,918	–	–	233,918	513p	07.03.05	07.03.09	–	–
	355,794	–	–	355,794	371p	11.03.06	11.03.10	–	–
	–	194,283	–	194,283	693p	11.03.07	11.03.11	–	–
Peter Harris									
Sharesave	1,569	–	–	1,569	430p	01.11.06	01.05.07	–	–
	800	–	–	800	461p	01.11.06	01.05.07	–	–
	–	359	–	359	524p	01.11.07	01.05.08	–	–
Executive (2001)	113,598	–	–	113,598	581p	21.06.04	21.06.08	–	–
	131,579	–	–	131,579	513p	07.03.05	07.03.09	–	–
	194,070	–	–	194,070	371p	11.03.06	11.03.10	–	–
	–	105,972	–	105,972	693p	11.03.07	11.03.11	–	–
Debbie Hewitt									
Sharesave	901	–	901	–	430p	01.11.04	01.05.05	640p	£1,892
	800	–	–	800	461p	01.11.06	01.05.07	–	–
	–	719	–	719	524p	01.11.07	01.05.08	–	–
Executive (2001)	77,451	–	–	77,451	581p	21.06.04	21.06.08	–	–
	96,491	–	–	96,491	513p	07.03.05	07.03.09	–	–
	149,595	–	–	149,595	371p	11.03.06	11.03.10	–	–
	–	81,687	–	81,687	693p	11.03.07	11.03.11	–	–
Richard Pennycook									
Sharesave	1,375	–	–	1,375	461p	01.11.08	01.05.09	–	–
Executive (2001)	93,282	–	–	93,282	559p	04.08.06	04.08.10	–	–
	–	108,225	–	108,225	693p	11.03.07	11.03.11	–	–
Jon Walden									
Sharesave	1,375	–	–	1,375	461p	01.11.08	01.05.09	–	–
	–	1,248	–	1,248	524p	01.11.09	01.05.10	–	–
Executive (2001)	111,015	–	–	111,015	581p	21.06.04	21.06.08	–	–
	131,579	–	–	131,579	513p	07.03.05	07.03.09	–	–
	198,111	–	–	198,111	371p	11.03.06	11.03.10	–	–
	–	108,180	–	108,180	693p	11.03.07	11.03.11	–	–

Notes:

1 Aggregate gains (nominal and realised) made following the exercise of share options by directors during 2004 were £278,159 (2003 – £105,216).

No consideration was payable to the Company by a participant for the grant of options under any of the employee share option schemes.

Remuneration report

Pensions The Company operates an Executive section within the RAC (2003) Pension Scheme providing a pension on a final salary basis with a normal retirement date of age 60. The method by which pensionable pay is calculated is dependent on the date the director joined the scheme.

The maximum permitted pensionable salary for any director who joined the Company after 1 June 1989 is equal to the Inland Revenue imposed 'Earnings Cap' (the Cap) which is £102,000 for the 2004/05 tax year. In addition, for all directors earning in excess of £100,000, final pensionable pay must be averaged over a minimum three year period in accordance with statutory regulations.

The Committee has previously reviewed the inclusion of fluctuating emoluments, such as bonus payments, within the calculation of pensionable pay. As a

result, any director who joined the Executive section of the scheme after 1 April 2000 has their pensionable salary calculated on their basic salary only, excluding bonus payments and any other fluctuating emoluments.

From 1 July 2003 directors who are members of the Executive section have the choice of contributing at a higher level for a higher accrual rate, or to contribute at a lower level for a lower accrual rate. The level of contribution is dependent upon the date that membership of the Executive section began.

For directors who joined before 1 April 2000 a choice is available of contributing 4% of pensionable salary for a one-fortieth accrual, or 12% for a one-thirtieth accrual. Of the directors who are members of the Executive section, Andrew Harrison and Jon Walden have both elected the higher contribution and

accrual rate. Debbie Hewitt also elected the higher contribution rate up to 30 September 2004. From 1 October 2004 Debbie Hewitt elected to reduce her contribution and receive the lower accrual rate for future service.

For directors who joined the Executive section after 1 April 2000 a 6% contribution is required for a one-fortieth accrual, or directors can contribute 14% of pensionable salary for a one-thirtieth accrual. Richard Pennycook is in the Executive section on these terms and has elected the higher contribution and accrual rate level of benefit.

For members of the former non-contributory section, an employee contribution of 4% was introduced from 1 July 2003 in order that members may maintain the accrual rate for future service at the level of one-sixtieth of pensionable pay. Alternatively, members

Directors' pension disclosure The pension entitlements earned by each individual director during the year, calculated on a prescribed basis are set out in the table below.

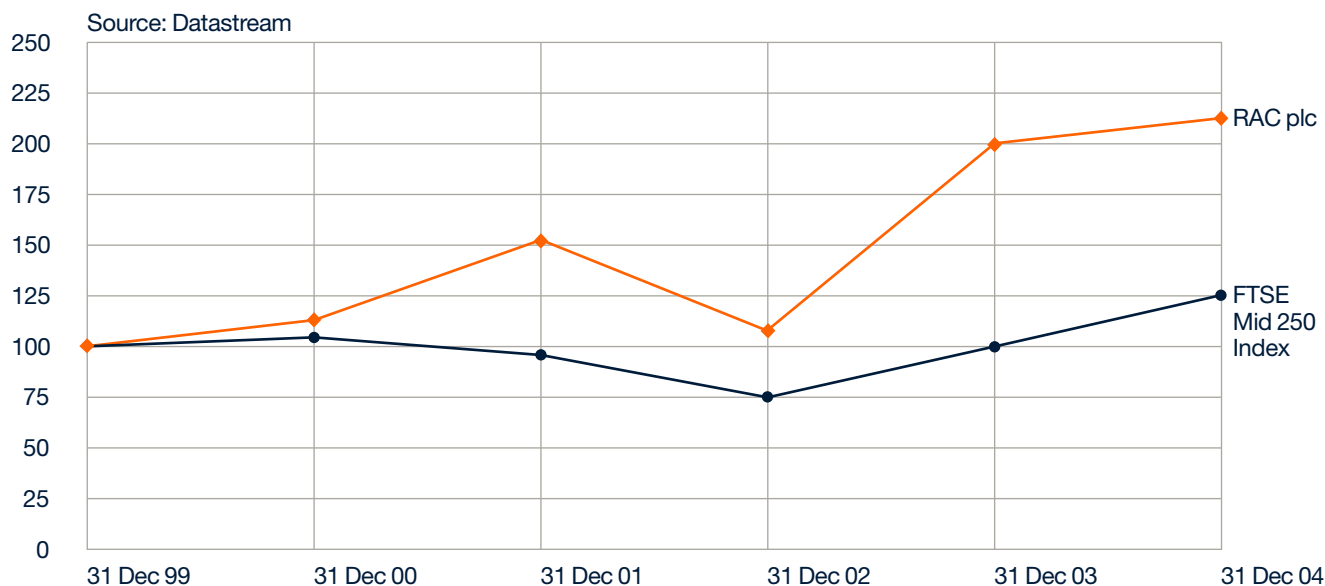
Name of director	Gross increase in accrued pension during the year £ p.a.	Increase in accrued pension net of inflation £ p.a.	Total accrued pension at the year end £ p.a.	Value of net increase in accrual over the year ⁶ £	Total change in value during the year ⁷ £	Value of accrued pension at 31 December 2004 £	Value of accrued pension at 31 December 2003 £	Company contribution to FURBS during the year ³ £
Andrew Harrison	4,133	3,383	28,329	22,674	53,776	291,616	225,690	166,651
Peter Harris	15,029	13,087	77,680	121,792	183,223	722,924	539,701	91,667
Debbie Hewitt	24,016	21,625	101,159	122,639	188,186	691,171	472,448	–
Richard Pennycook	3,441	3,399	4,797	11,505	12,913	36,243	9,155	–
Jon Walden	3,858	3,389	18,983	30,051	52,840	236,377	171,387	–

Notes:

- The pension entitlement shown is that which would be paid annually at normal retirement age based on service to 31 December 2004.
- The transfer value has been calculated in accordance with Version 8.1 of Guidance Note GN11 issued by the actuarial profession.
- The contributions shown represent Company contributions to the Funded Unapproved Retirement Benefits Schemes (FURBS) for Andrew Harrison and Peter Harris.
- Members of the scheme have the option to pay Additional Voluntary Contributions. Neither the contributions nor the resulting benefits are included in the above table.
- None of the non-executive directors participates in the Company pension arrangements.
- The value of net increase represents the incremental value to the director of his or her service during the year, calculated on the assumption service terminated at the year-end. It is based on the increase in accrued pension net of inflation after deducting the director's contribution.
- The total change in value includes the effect of fluctuations in the transfer value due to factors beyond the control of the Company and directors, such as stock market movements. It is calculated after deducting the director's contribution.
- Accruing occupational pension rights are a liability of the scheme and represent value that may be received by the individual at a later date. For this reason, the transfer values are not comparable with direct cash remuneration and cannot be meaningfully added to it.
- The aggregate Company contribution to FURBS during the year was £258,318 (2003 – £271,067).
- Jon Walden has a separate pension entitlement in respect of a previous period of employment with the Company from 1 October 1982 to 31 October 1997. The deferred pension as at 31 December 2004 amounted to £81,644 per annum. This pension is re-valued each year in line with statutory requirements.
- For Debbie Hewitt, the 'Value of accrued pension at 31 December 2003' has been restated as £472,448 (was £519,748) to reflect the value of her non-contributory section benefits which are based on a Normal Retirement Age of 65 rather than 60.

Share price performance The performance of the Company's ordinary shares compared with the FTSE Mid 250 Index for the five year period ended 31 December 2004 is shown in the graph below.

Total shareholder return: Value £



This graph looks at the value, by the end of 2004, of £100 invested in RAC plc on 31 December 1999 compared with the value of £100 invested in the FTSE Mid 250 Index on the same date. The other points plotted are the values at intervening financial year-ends.

That Index was chosen as the Board believes that it gives shareholders a reasonable comparison with the total shareholder return – i.e. including the re-investment of all dividend payments – of an equity investment in companies in the same stock market category (by size of market capitalisation) as the Company was throughout that five year period.

of this section can remain on a 'non-contributory' basis and accept a reduced accrual rate of one-eightieth of pensionable pay for future service. Pensionable pay in this section is defined in the scheme Rules as basic salary averaged over one year plus the average of any bonus payments in the 36 months before the date of leaving. Other benefits in kind are excluded from the pensionable pay calculation.

Peter Harris is a member of the former non-contributory final salary section of the RAC (2003) Pension Scheme and has elected the reduced accrual rate of one-eightieth of pensionable salary for future service from 1 July 2003.

To compensate for the effect of the Cap, Andrew Harrison and Peter Harris are also members of a supplementary pension arrangement known as a 'Funded Unapproved Retirement Benefit Scheme' (FURBS). This enables benefits to be provided on total earnings above the Cap, excluding the value of any benefits in kind.

Richard Pennycook and Jon Walden are also subject to the Cap and each receive a salary supplement calculated on their basic salary above the Cap. Richard Pennycook receives a supplement of 20%, and Jon Walden a supplement of 30%, of their basic salaries above the Cap. The supplements are not included in the calculation of salary reviews, bonus payments, share options, or any other salary related benefit.

There were no excess retirement benefits paid to serving directors, or past directors, during the year (2003 – £ nil).

The Finance Act 2004 makes major changes to the taxation and regulation of occupational pension schemes, and to the benefits which occupational pension schemes may provide. This together with the Pensions Act 2004 phase changes in progressively over the course of 2005 and 2006. RAC plc is actively considering their implications for the provision of pensions to all of its employees and directors.

Details of share price in 2004 The middle market price of an ordinary share at 31 December 2004 was 635p and the range during the year was 602.5p (low) to 730p (high).

This remuneration report complies with the requirements of The Directors' Remuneration Report Regulations 2002 (the 'Regulations') and KPMG Audit Plc have audited the table on page 37 and the sections contained within pages 38 to 41 as required by the Regulations. The report has been approved by the Board and signed on its behalf by

John Poulter
Chairman of the Remuneration Committee
16 February 2005

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and Group and of the profit or loss for that period. In preparing those 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, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Independent auditors' report to the members of RAC plc

We have audited the financial statements on pages 44 to 78. We have also audited 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 are responsible for preparing the Annual Report and the directors' remuneration report. As described on page 42 this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom law and Accounting Standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our

opinion, the directors' report is not consistent with the financial statements, if 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 or the Listing Rules regarding directors' remuneration and transactions with the Group is not disclosed.

We review whether the corporate governance statement on pages 32 to 34 reflects the Company's compliance with the nine provisions of the 2003 FRC Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement and the unaudited part of the directors' remuneration report, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the directors' remuneration report to be audited. It also includes an

assessment of the significant estimates and judgements made by the directors in the preparation of the 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 financial statements and the part of the directors' remuneration report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the directors' remuneration report to be audited.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2004 and of the profit of the Group for the year then ended; and
- the financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
8 Salisbury Square, London, EC4Y 8BB
16 February 2005

Statement of accounting policies

Principal accounting policies

The accounts have been prepared under the historical cost accounting convention, and comply with applicable UK accounting standards and with the requirements of the Companies Act 1985 except as set out under 'Goodwill' below.

FRS 17 Retirement benefits

The Group is following the transitional arrangements under which additional disclosure on retirement benefits is required in the notes to the accounts for the year ended 31 December 2004 (see note 33).

UITF 38 Accounting for ESOPs & UITF 17 Employee share schemes

Following the publication of Tech 64/04 on 21 December 2004, there is further guidance on implementing UITF 38 and the revised UITF 17. As a consequence, the investment in own shares is now shown as a deduction within the profit and loss reserve, instead of being shown as a separate deduction from shareholders' funds as in the past. As permitted by UITF 17 the Group does not apply the requirements to its Inland Revenue approved Save-As-You-Earn scheme.

Consolidation

The Group accounts include the accounts of the Company and its subsidiary undertakings made up to 31 December 2004. Unless otherwise stated, the acquisition method of accounting has been adopted. Under this method, the results of subsidiary undertakings acquired or disposed of in the year are included in the consolidated profit and loss account from the date of acquisition or up to the date of disposal. Intra-group sales and profits are eliminated fully on consolidation.

An associate is an undertaking in which the group has a long-term interest, usually less than 50% of the equity voting rights, and over which it exercises significant influence. The Group's share of the profits less losses of associates is included in the consolidated profit and loss account and its interest in their net assets is included in investments in the consolidated balance sheet.

A joint venture is an undertaking in which the Group has a long-term interest over which it exercises joint control. The Group's share of the profits less losses of joint ventures is included in the consolidated profit and loss account and its interest in their net assets is included in investments in the consolidated balance sheet.

In relation to the associated undertakings and joint ventures, the amounts included in the consolidated accounts are taken from the latest accounts of the undertakings (details are set out on pages 61 and 78).

Under section 230(4) of the Companies Act 1985 the Company is exempt from the requirement to present its own profit and loss account.

Turnover

Turnover is based on the invoiced value of goods and services. It excludes sales between Group undertakings, VAT and similar sales-based taxes.

RAC roadside membership subscriptions are apportioned on a time basis over the period to which they relate. The unrecognised proportion of subscription income is held within creditors as deferred income.

Tangible fixed assets

Tangible fixed assets are stated at historical cost less accumulated depreciation.

Depreciation

Depreciation is provided to write down tangible fixed assets to their estimated residual values as follows:

Land and buildings

The cost of each freehold, long and short leasehold building is depreciated on a straight line basis over its estimated useful life. The estimated remaining useful life of the buildings averages 23 years. Long leases are defined as those having 50 or more years unexpired at the balance sheet date. Freehold land is not depreciated.

Vehicles, plant and machinery and assets held on contract hire

The cost of vehicles is depreciated to estimated residual value on a straight line basis at annual rates between 20% and 33%. Plant and machinery is depreciated on a straight line basis at annual rates between 7% and 20%.

Fixtures, fittings, tools and equipment

The cost of fixtures, fittings, tools and equipment is depreciated on a straight line basis at annual rates between 10% and 20%. Computer equipment is depreciated on a straight line basis at annual rates between 10% and 33%.

Stocks

Stocks are valued at the lower of cost and net realisable value. Cost is arrived at principally on the average and 'first in, first out' (FIFO) basis. Provisions are made against obsolete and surplus stocks.

Vehicles held on consignment from manufacturers are included in the balance sheet where it is considered that the Group enjoys the benefits and carries the risk of ownership. Vehicles included in stocks which are subject to repurchase agreements are included at the agreed repurchase price or net realisable value whichever is lower. In both of these cases the associated liability is included in creditors.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

There is a Group payment arrangement in place between RAC plc and the Inland Revenue such that all UK corporation tax payments and receipts within the RAC plc Group (excluding joint ventures and associates) are made or received by RAC plc. Accordingly, RAC plc charges or credits all UK corporation tax balances to its intercompany account with subsidiaries as they arise.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date.

A deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is not discounted.

Pension costs

The expected cost of providing pensions and other post-retirement benefits is charged to the profit and loss account so as to spread the cost over the expected remaining service lives of current employees. Variations from regular costs are spread over the expected remaining service lives of current eligible employees. The pension cost is assessed in accordance with the advice of qualified actuaries, using the projected unit method.

Goodwill

Purchased goodwill arising on consolidation in respect of acquisitions before 1 January 1998, when FRS 10 Goodwill and intangible assets was adopted, was written off to reserves in the year of acquisition. When a subsequent disposal occurs, any related goodwill previously written off to reserves is written back through the profit and loss account as part of the profit or loss on disposal.

Purchased goodwill arising on consolidation in respect of acquisitions since 1 January 1998 is capitalised. In most cases, positive goodwill is amortised to nil by equal annual instalments over its estimated useful life of 20 years. The goodwill arising on the acquisition of AXA's interest in RAC Financial Services and the renewal rights of AXA Direct is amortised on a reducing balance rate of approximately 25% per annum based on the anticipated renewal rate. On the subsequent disposal or termination of a business acquired since 1 January 1998, the profit or loss on disposal or termination is calculated after charging the unamortised amount of any related goodwill.

Goodwill relating to the acquisition of RAC Holdings Limited amounting to £404.6 million has been capitalised. The directors consider that this goodwill has an indefinite life due to the durability of the business as demonstrated over more than 100 years and accordingly it is not amortised but is subject to annual review for impairment. This is not in accordance with Schedule 4 to the Companies Act 1985 which requires that all goodwill be amortised. The directors consider that this would fail to give a true and fair view of the profit for the year and that the economic measure of performance in any period is properly made by reference only to any impairment that may have arisen. It is not practicable to quantify the effect on the accounts of this departure. Any impairment charge is included within operating profits.

Foreign currencies

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction or, if hedged forward, at the rate of exchange under the related forward exchange contract.

Monetary assets and liabilities in foreign currencies are translated into sterling at the financial year end rates.

The results of overseas subsidiary undertakings, associates and joint ventures are translated into sterling at average rates for the period except for material exceptional items which are translated at the rate on the date of the transaction. The adjustment to financial year end rates is taken to reserves.

Differences on exchange arising from the translation of the net assets of subsidiary undertakings and foreign currency debt financing those assets are taken to reserves and are reported in the statement of total consolidated recognised gains and losses. Other exchange differences are taken to the profit and loss account.

Derivatives and other financial instruments

Short term debtors and creditors as defined in FRS 13 Derivatives and other financial instruments have been excluded from the disclosures in note 36, save those relating to currency risk.

Derivative financial instruments used to hedge interest rate and foreign currency exposures are accounted for as they are settled. Any gains or losses on these instruments are reported in the profit and loss account.

Operating leases

Operating lease rentals are charged to the profit and loss account on a straight line basis over the life of the lease.

Assets held for use in operating leases are recorded as fixed assets and are depreciated over their useful lives to their estimated residual value.

With the exception of Lex Vehicle Leasing (Holdings) Limited income from operating leases is credited to the profit and loss account on a straight line basis over the life of the contract.

Lex Vehicle Leasing (Holdings) Limited, a joint venture, credits net income on operating leases, after charging interest, depreciation, maintenance and other costs, to the profit and loss account to give a constant rate of return on the operating lease asset over the period of the contract.

Finance leases

Leases which confer rights and obligations similar to those attaching to owned assets are defined as finance leases. The present value of future minimum lease payments of assets

acquired under finance leases is included in fixed assets and in creditors as an obligation to pay future rentals. Depreciation is provided at the same rates as for owned assets.

Rentals payable under finance leases are apportioned between the finance charge and the outstanding obligation so as to produce a constant rate of charge on the remaining balance.

Cash and liquid resources

Cash, for the purpose of the cash flow statement, comprises cash in hand and deposits repayable on demand, less overdrafts payable on demand.

Liquid resources are current asset investments which may be disposed of without curtailing or disrupting the business and are either readily convertible into known amounts of cash at or close to their carrying values or traded in an active market.

Pre-contract costs

Pre-contract costs are written off as incurred, except that directly attributable costs are capitalised as an asset when it is virtually certain that the contract will be obtained and when the contract is expected to result in future net cash inflows with a present value no less than all amounts recognised as an asset.

Consolidated profit and loss account

for the financial year ended 31 December 2004

Total turnover

Less share of joint ventures

Less share of associates

Group turnover

Cost of sales

Gross profit

Distribution and selling expenses

Operating exceptional items

Amortisation of goodwill

Other administrative expenses

Total administrative expenses

Group operating profit/(loss)

Share of joint ventures' operating profit/(loss)

Share of associates' operating profit

Total operating profit/(loss): Group and share of joint ventures and associates

Net loss on sale or closure of businesses

Net profit on sale of fixed assets

Total non-operating exceptional items

Net interest payable and similar charges

Profit/(loss) on ordinary activities before taxation

Group taxation

Share of joint ventures' taxation

Share of associates' taxation

Taxation on profit on ordinary activities

Profit on ordinary activities after taxation

Equity minority interests

Profit for the financial year

Equity dividends – paid and proposed

Retained profit/(loss) for the financial year

Profit for the financial year

Earnings per ordinary share

Earnings per ordinary share (diluted)

Profit before goodwill amortisation, exceptionals and taxation for the financial year

Earnings per ordinary share on this basis after taxation and minority interests

Earnings per ordinary share on this basis after taxation and minority interests (diluted)

Dividends per ordinary share – paid and proposed

There is no difference between the Group's profit at historical cost and the profit for the financial year reported above in either year.

Included within continuing operations in 2004 is turnover of £3.7 million, cost of sales of £0.7 million, distribution and selling expenses of £1.5 million, goodwill amortisation of £1.5 million and other administrative expenses of £2.4 million relating to acquisitions. Integration costs of £1.9 million, relating to acquisitions is included within other administrative expenses of £2.4 million. Further details of acquisitions are shown in note 28.

An analysis of profit before goodwill amortisation, exceptionals and taxation for the financial year is shown in note 1.

2004						2003				
Notes	Continuing operations			Discontinued operations	Total	Continuing operations			Discontinued operations	Total
	Before goodwill amortisation and exceptional items £m	Goodwill amortisation and exceptional items £m	Total £m	£m	£m	Before goodwill amortisation and exceptional items £m	Goodwill amortisation and exceptional items £m	Total £m	£m	£m
1	1,509.1	–	1,509.1	30.3	1,539.4	1,401.5	–	1,401.5	124.7	1,526.2
1	(334.6)	–	(334.6)	(7.7)	(342.3)	(286.2)	–	(286.2)	(17.0)	(303.2)
1	(7.8)	–	(7.8)	–	(7.8)	(7.3)	–	(7.3)	–	(7.3)
1	1,166.7	–	1,166.7	22.6	1,189.3	1,108.0	–	1,108.0	107.7	1,215.7
	(776.3)	–	(776.3)	(19.6)	(795.9)	(739.1)	–	(739.1)	(94.6)	(833.7)
	390.4	–	390.4	3.0	393.4	368.9	–	368.9	13.1	382.0
	(193.1)	–	(193.1)	(1.3)	(194.4)	(176.9)	–	(176.9)	(6.3)	(183.2)
1	–	7.5	7.5	–	7.5	–	–	–	(30.2)	(30.2)
1	–	(7.1)	(7.1)	–	(7.1)	–	(5.6)	(5.6)	–	(5.6)
	(131.3)	–	(131.3)	(1.9)	(133.2)	(120.9)	–	(120.9)	(8.8)	(129.7)
	(131.3)	0.4	(130.9)	(1.9)	(132.8)	(120.9)	(5.6)	(126.5)	(39.0)	(165.5)
	66.0	0.4	66.4	(0.2)	66.2	71.1	(5.6)	65.5	(32.2)	33.3
	27.3	(0.7)	26.6	0.2	26.8	24.1	–	24.1	(0.5)	23.6
	4.2	–	4.2	–	4.2	3.4	–	3.4	–	3.4
	97.5	(0.3)	97.2	–	97.2	98.6	(5.6)	93.0	(32.7)	60.3
2	–	–	–	(15.1)	(15.1)	–	–	–	(26.0)	(26.0)
	–	1.2	1.2	–	1.2	–	0.8	0.8	–	0.8
	–	1.2	1.2	(15.1)	(13.9)	–	0.8	0.8	(26.0)	(25.2)
3	(8.9)	3.3	(5.6)	–	(5.6)	(9.4)	–	(9.4)	–	(9.4)
4	88.6	4.2	92.8	(15.1)	77.7	89.2	(4.8)	84.4	(58.7)	25.7
					(15.3)					(8.6)
					(8.6)					(6.6)
					(1.3)					(1.0)
8					(25.2)					(16.2)
					52.5					9.5
					–					–
					52.5					9.5
9					(29.5)					(28.0)
24					23.0					(18.5)
					£52.5m					£9.5m
10					45.8p					8.3p
10					44.7p					8.2p
					£88.6m					£86.7m
1					55.7p					54.4p
10					54.3p					53.8p
9					25.8p					24.3p

Consolidated balance sheet

at 31 December 2004

	Notes	2004 £m	2003 £m
Fixed assets			
Intangible assets	11	533.7	500.7
Tangible assets	12	161.3	177.2
Fixed asset investments			
Investments in joint ventures		668.8	572.8
– share of gross assets		(602.2)	(523.6)
– share of gross liabilities		66.6	49.2
Investments in associates	13	5.8	5.9
		72.4	55.1
		767.4	733.0
Current assets			
Stocks	15	189.5	176.3
Debtors			
– due within one year	16	153.3	154.9
– due after one year	16	45.7	44.8
		199.0	199.7
Investments	30	6.7	20.8
Cash at bank and in hand	17	35.5	21.4
		430.7	418.2
Creditors: amounts falling due within one year			
Bank and other loans	18	42.4	96.4
Other creditors	18	497.2	459.3
		539.6	555.7
Net current liabilities		(108.9)	(137.5)
Total assets less current liabilities		658.5	595.5
Creditors: amounts falling due after more than one year			
Bank and other loans	19	138.3	97.4
Other creditors	19	66.9	75.0
		205.2	172.4
Provisions for liabilities and charges	22	25.4	23.9
Net assets		427.9	399.2
Capital and reserves			
Called up share capital	23	29.7	29.5
Share premium account	24	136.3	133.4
Own shares held reserve	24	–	(14.0)
Capital redemption reserve	24	1.0	1.0
Profit and loss account	24	260.7	249.3
Equity shareholders' funds		427.7	399.2
Equity minority interest	24	0.2	–
		427.9	399.2

The accounts on pages 44 to 78 were approved by the board of directors on 16 February 2005 and were signed on its behalf by:

Andrew Harrison
Richard Pennycook
Directors

Company balance sheet

at 31 December 2004

	Notes	2004 £m	2003 £m
Fixed assets			
Tangible assets	12	15.2	16.0
Fixed asset investments			
Investments in subsidiaries	14	629.3	633.8
Investments in joint ventures	14	85.1	77.6
		714.4	711.4
		729.6	727.4
Current assets			
Debtors			
– due within one year	16	159.2	150.3
– due after one year	16	9.2	7.8
		168.4	158.1
Cash at bank and in hand		0.5	0.5
		168.9	158.6
Creditors: amounts falling due within one year			
Bank and other loans	18	50.0	93.4
Other creditors	18	232.0	364.4
		282.0	457.8
Net current liabilities		(113.1)	(299.2)
Total assets less current liabilities		616.5	428.2
Creditors: amounts falling due after more than one year			
Bank and other loans	19	138.3	97.4
Other creditors	19	43.0	40.8
		181.3	138.2
Provisions for liabilities and charges	22	3.8	3.5
Net assets		431.4	286.5
Capital and reserves			
Called up share capital	23,25	29.7	29.5
Share premium account	25	136.3	133.4
Own shares held reserve	25	–	(14.0)
Capital redemption reserve	25	1.0	1.0
Merger reserve	25	–	24.9
Other reserve	25	19.8	19.8
Profit and loss account	25	244.6	91.9
Equity shareholders' funds		431.4	286.5

The accounts on pages 44 to 78 were approved by the board of directors on 16 February 2005 and were signed on its behalf by:

Andrew Harrison
Richard Pennycook
Directors

Consolidated cash flow statement

for the financial year ended 31 December 2004

	Notes	2004 £m	2003 £m
Net cash inflow from operating activities	26	110.0	117.9
Dividends received from joint ventures and associates		12.0	15.2
Returns on investments and servicing of finance			
Interest received		5.0	2.5
Interest paid		(11.8)	(18.9)
Net cash outflow from returns on investments and servicing of finance		(6.8)	(16.4)
Taxation		(19.8)	(13.6)
Capital expenditure and financial investment			
Tangible fixed assets acquired	27	(70.2)	(89.1)
Tangible fixed assets sold	27	45.4	48.4
Capital injection into joint venture	27	(7.5)	–
Net cash outflow from capital expenditure and financial investment	27	(32.3)	(40.7)
Acquisitions and disposals			
Subsidiary undertakings and businesses acquired	28	(30.8)	(0.3)
Subsidiary undertakings and businesses disposed	29	15.7	90.3
Net cash (outflow)/inflow from acquisitions and disposals		(15.1)	90.0
Equity dividends paid		(28.4)	(26.9)
Net cash inflow before use of liquid resources and financing		19.6	125.5
Management of liquid resources			
Increase in liquid resources and current investments		(0.9)	(2.9)
Financing			
Issue of ordinary share capital		3.1	3.2
Purchase of own shares for Executive Share Option Scheme		(9.6)	–
Sale or transfer of own shares from Executive Share Option Scheme		1.9	–
Increase/(decrease) in debt and finance leases		8.3	(145.0)
Net cash inflow/(outflow) from financing		3.7	(141.8)
Increase/(decrease) in cash in the year		22.4	(19.2)
Reconciliation of net cash flow to movement in debt			
Increase/(decrease) in cash in the year	30	22.4	(19.2)
Increase in liquid resources and current investments	30	0.9	2.9
(Increase)/decrease in debt and finance leases	30	(8.3)	145.0
Change in net debt resulting from cash flows	30	15.0	128.7
New finance leases	30	(0.7)	(0.6)
Exchange movements	30	0.2	(0.2)
Movement in net debt in the year		14.5	127.9
Opening net debt	30	(154.3)	(282.2)
Closing net debt	30	(139.8)	(154.3)

Statement of total consolidated recognised gains and losses

for the financial year ended 31 December 2004

	2004 £m	2003 £m
Profit for the financial year	52.5	9.5
Currency translation gains on foreign currency net investments	0.7	0.9
Total consolidated recognised gains relating to the financial year	53.2	10.4

Reconciliation of movements in shareholders' funds

for the financial year ended 31 December 2004

	2004 £m	2003 £m
Profit for the financial year	52.5	9.5
Equity dividends	(29.5)	(28.0)
Retained profit/(loss) for the financial year	23.0	(18.5)
Goodwill previously written off to reserves now charged to profit for the financial year	9.4	9.8
Issue of ordinary share capital	3.1	3.2
Net (increase)/decrease in own shares held	(7.7)	1.7
Currency translation gains on foreign currency net investments	0.7	0.9
Net movement in shareholders' funds	28.5	(2.9)
Opening shareholders' funds	399.2	402.1
Closing shareholders' funds	427.7	399.2

A reconciliation of movements in shareholders' funds for the Company is provided in note 25.

Notes to the accounts

for the financial year ended 31 December 2004

1 Segmental analysis

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 (restated) £m	Discontinued operations 2003 (restated) £m	Total 2003 (restated) £m
Turnover						
RAC Consumer Services	374.8	–	374.8	353.1	–	353.1
RAC Business Solutions	169.8	–	169.8	160.8	–	160.8
Lex Vehicle Leasing	241.8	–	241.8	207.2	–	207.2
Lex Industrial Solutions	–	21.2	21.2	–	95.6	95.6
Leyland parts distribution and related activities	39.6	–	39.6	63.7	–	63.7
All other activities	680.6	9.1	689.7	613.4	29.1	642.5
Manufacturer Support Services	720.2	9.1	729.3	677.1	29.1	706.2
Other	2.5	–	2.5	3.3	–	3.3
Total of subsidiary undertakings, joint ventures and associates	1,509.1	30.3	1,539.4	1,401.5	124.7	1,526.2
Less Group share of joint ventures' turnover						
RAC Consumer Services	(0.7)	–	(0.7)	(0.7)	–	(0.7)
Lex Vehicle Leasing	(241.8)	–	(241.8)	(207.2)	–	(207.2)
Lex Industrial Solutions	–	(7.7)	(7.7)	–	(17.0)	(17.0)
Manufacturer Support Services	(92.1)	–	(92.1)	(78.3)	–	(78.3)
	(334.6)	(7.7)	(342.3)	(286.2)	(17.0)	(303.2)
Less Group share of associates' turnover						
Manufacturer Support Services	(7.8)	–	(7.8)	(7.3)	–	(7.3)
Group turnover	1,166.7	22.6	1,189.3	1,108.0	107.7	1,215.7

Turnover by origin and turnover by destination do not differ materially.

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 (restated) £m	Discontinued operations 2003 (restated) £m	Total 2003 (restated) £m
Profit/(loss)						
RAC Consumer Services	47.5	–	47.5	51.3	–	51.3
RAC Business Solutions	5.2	–	5.2	1.4	–	1.4
Lex Vehicle Leasing	22.7	–	22.7	19.6	–	19.6
Lex Industrial Solutions	–	0.1	0.1	–	(2.4)	(2.4)
Leyland parts distribution and related activities	17.4	–	17.4	25.6	–	25.6
All other activities	9.4	(0.1)	9.3	6.4	(0.1)	6.3
Manufacturer Support Services	26.8	(0.1)	26.7	32.0	(0.1)	31.9
Other	0.2	–	0.2	0.5	–	0.5
Total of subsidiary undertakings, joint ventures and associates	102.4	–	102.4	104.8	(2.5)	102.3
Unallocated Group overheads	(4.9)	–	(4.9)	(6.2)	–	(6.2)
Profit before interest, goodwill amortisation, exceptionals and taxation	97.5	–	97.5	98.6	(2.5)	96.1
Net interest payable and similar charges	(8.9)	–	(8.9)	(9.4)	–	(9.4)
Profit before goodwill amortisation, exceptionals and taxation	88.6	–	88.6	89.2	(2.5)	86.7
Goodwill amortisation (including share of joint ventures)	(7.8)	–	(7.8)	(5.6)	–	(5.6)
Operating exceptional items	7.5	–	7.5	–	(30.2)	(30.2)
Exceptional interest income on VAT refund	3.3	–	3.3	–	–	–
Non-operating exceptional items – Corporate activities	1.2	(15.1)	(13.9)	0.8	(26.0)	(25.2)
Profit/(loss) on ordinary activities before taxation	92.8	(15.1)	77.7	84.4	(58.7)	25.7
Total of subsidiary undertakings, joint ventures and associates						
Subsidiary undertakings	75.1	(0.2)	74.9	80.8	(2.0)	78.8
Joint ventures	23.2	0.2	23.4	20.7	(0.5)	20.2
Associates	4.1	–	4.1	3.3	–	3.3
Profit/(loss)	102.4	–	102.4	104.8	(2.5)	102.3

Share of joint ventures' and associates' operating profit is stated after central overhead allocations.

1 Segmental analysis (continued)

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 £m	Discontinued operations 2003 £m	Total 2003 £m
Analysis of goodwill amortisation by segment						
RAC Consumer Services	(6.8)	–	(6.8)	(5.3)	–	(5.3)
RAC Business Solutions	(0.3)	–	(0.3)	(0.3)	–	(0.3)
	(7.1)	–	(7.1)	(5.6)	–	(5.6)
Share of joint ventures' goodwill amortisation						
Lex Vehicle Leasing	(0.7)	–	(0.7)	–	–	–
Goodwill amortisation	(7.8)	–	(7.8)	(5.6)	–	(5.6)

Analysis of operating exceptional items by segment

Lex Industrial Solutions						
Impairment of assets held for resale	–	–	–	–	(30.2)	(30.2)
Manufacturer Support Services						
Leyland parts distribution transfer	4.5	–	4.5	–	–	–
Corporate activities						
VAT refund	3.0	–	3.0	–	–	–
Operating exceptional items	7.5	–	7.5	–	(30.2)	(30.2)

Manufacturer Support Services

In consideration for the transfer of the Leyland parts distribution contract, an initial amount of £4.5 million has been received. A further £13.5 million is receivable on 30 September 2005.

Corporate activities

Following a change in the interpretation of VAT regulations, previous over-payments of £3.0 million net of fees, and related interest of £3.3 million, have been recovered.

The operating exceptional items, including the related interest of £3.3 million, increased the current year tax charge by £3.2 million (2003 – £nil).

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 (restated) £m	Discontinued operations 2003 (restated) £m	Total 2003 (restated) £m
Net assets/(liabilities)						
RAC Consumer Services	500.8	–	500.8	465.1	–	465.1
RAC Business Solutions	(13.6)	–	(13.6)	(8.3)	–	(8.3)
Lex Vehicle Leasing	56.7	–	56.7	40.1	–	40.1
Lex Industrial Solutions	–	–	–	–	16.1	16.1
Manufacturer Support Services	86.8	–	86.8	90.2	9.2	99.4
Other	12.9	–	12.9	25.2	–	25.2
Total of subsidiary undertakings, joint ventures and associates	643.6	–	643.6	612.3	25.3	637.6
Corporate net liabilities			(75.9)			(84.1)
Net debt including obligations under finance leases			(139.8)			(154.3)
Net assets			427.9			399.2
Total of subsidiary undertakings, joint ventures and associates						
Subsidiary undertakings	571.2	–	571.2	557.7	24.8	582.5
Joint ventures	66.6	–	66.6	48.7	0.5	49.2
Associates	5.8	–	5.8	5.9	–	5.9
Net assets	643.6	–	643.6	612.3	25.3	637.6

The segmental analysis above has been restated to reflect the current operating structure of the Group following the exit from Mechanical Handling.

The Group's operations are conducted almost wholly in the United Kingdom.

Notes to the accounts

for the financial year ended 31 December 2004

2 Net loss on sale or closure of businesses

	Loss before goodwill £m	Goodwill previously written off to reserves £m	2004 £m	2003 £m
Discontinued operations				
Loss on disposal of Mechanical Handling businesses	(1.8)	(9.4)	(11.2)	(23.5)
Loss on disposal of Manufacturer Support Services businesses	(3.9)	–	(3.9)	–
Loss on closure of Managed Services division in Lex Industrial Solutions	–	–	–	(2.5)
Net loss on sale or closure of businesses	(5.7)	(9.4)	(15.1)	(26.0)

The net loss on the sale or closure of businesses reduced the current year tax charge by £2.5 million (2003 – £8.1 million).

3 Net interest payable and similar charges

	2004 £m	2003 £m
Continuing operations		
Interest payable on bank loans and overdrafts	(3.6)	(4.3)
Interest payable on loans falling due within five years	(6.7)	(2.8)
Interest payable on loans falling due after more than five years	–	(3.1)
Stock financing charges	(0.2)	(0.2)
Finance charges in respect of finance leases and similar hire purchase agreements	(0.1)	(1.2)
Interest payable and similar charges	(10.6)	(11.6)
Interest receivable and similar income	5.0	2.2
Net interest payable and similar charges	(5.6)	(9.4)

Interest arising on Mechanical Handling businesses of £0.6 million (2003 – £4.2 million) is included in the discontinued element of cost of sales.

4 Profit on ordinary activities before taxation

The profit on ordinary activities before taxation is stated after charging:

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 £m	Discontinued operations 2003 £m	Total 2003 £m
Depreciation	28.7	3.5	32.2	24.7	52.5	77.2
Net profit on sale of tangible fixed assets	(1.6)	–	(1.6)	–	(0.4)	(0.4)
Amortisation of goodwill	7.1	–	7.1	5.6	–	5.6
Auditors' remuneration						
– audit services	0.5	–	0.5	0.6	0.1	0.7
– further assurance services	0.4	0.1	0.5	0.1	0.1	0.2
– tax services	1.0	–	1.0	0.3	–	0.3
– other services	–	–	–	0.4	–	0.4
	1.9	0.1	2.0	1.4	0.2	1.6
Operating lease rentals						
– land and buildings	11.7	0.1	11.8	11.8	0.7	12.5
– other	13.7	0.1	13.8	12.0	2.3	14.3

Included in auditors' remuneration is an amount of £0.1 million for audit fees (2003 – £0.1 million) and £0.1 million for non-audit fees (2003 – £0.5 million) in respect of RAC plc.

Excluded from the analysis above are operating lease rentals of £89.8 million (2003 – £91.8 million) incurred by Lex Defence Management Limited, a wholly owned subsidiary, to certain joint ventures of the Group. Lex Defence Management acts solely as an intermediary between these joint ventures and certain customers.

5 Employees

The aggregate payroll costs of employees (including directors) were:

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 £m	Discontinued operations 2003 £m	Total 2003 £m
Wages and salaries	223.8	4.3	228.1	213.1	21.3	234.4
Social security costs	22.9	1.2	24.1	21.1	4.3	25.4
Other pension costs (note 33)	21.6	0.2	21.8	19.3	1.4	20.7
	268.3	5.7	274.0	253.5	27.0	280.5

The average number of employees in the Company and its subsidiary undertakings (including executive directors) was:

	Continuing operations 2004 Number of employees	Discontinued operations 2004 Number of employees	Total 2004	Continuing operations 2003 Number of employees	Discontinued operations 2003 Number of employees	Total 2003
RAC Consumer Services	4,980	–	4,980	4,699	–	4,699
RAC Business Solutions	2,448	–	2,448	2,503	–	2,503
Lex Industrial Solutions	–	139	139	–	903	903
Manufacturer Support Services	1,587	68	1,655	1,608	102	1,710
Other	162	–	162	158	–	158
	9,177	207	9,384	8,968	1,005	9,973

Certain employees of UK joint ventures and associates have contracts of employment with RAC plc, but the costs are borne by the relevant businesses.

6 Share option schemes

The Company had three principal share option schemes in operation during the year.

Executive Share Option Scheme (1994)

The Executive Share Option Scheme (1994) was adopted on 27 April 1994. The exercise of options will normally be conditional upon the achievement of a specified performance target to be determined by the Company's Remuneration Committee. Options over 113,378 shares were exercised during 2004 and there are no longer any outstanding options that could be exercised under this Scheme.

Executive Share Option Scheme (2001)

The Executive Share Option Scheme (2001) was adopted on 26 April 2001. Options will normally be exercisable only upon the achievement of performance criteria determined at the time of option grant by the Company's Remuneration Committee.

The following options to acquire ordinary shares were outstanding at 31 December 2004:

Period during which options are exercisable	Price per share	Number of shares under option
Executive Share Option Scheme (2001)		
21 June 2004 to 20 June 2008	581p	903,577
7 March 2005 to 6 March 2009	513p	1,435,072
17 May 2005 to 16 May 2009	522p	26,819
11 March 2006 to 10 March 2010	371p	2,467,661
4 August 2006 to 3 August 2010	559p	165,680
11 March 2007 to 10 March 2011	693p	1,605,155
22 September 2007 to 21 September 2011	670p	69,400
		6,673,364

Options over a total of 113,378 ordinary shares granted under the 1994 scheme were exercised during the year for which a total consideration of £499,997 was received by the Company.

Notes to the accounts

for the financial year ended 31 December 2004

6 Share option schemes (continued)

Sharesave Scheme

Under the terms of the Sharesave Scheme, introduced in 1997, the Board may offer options to purchase ordinary shares in the Company to those employees who enter into an Inland Revenue approved Save-As-You-Earn (SAYE) savings contract for a period of either 3 or 5 years. The price at which options may be offered is up to a maximum discount of 20% of the market value of a share on the relevant invitation date, but also not less than the nominal value per share. The options may normally be exercised during the period of six months after the completion of the SAYE contract.

Outstanding options granted under the Sharesave Scheme at 31 December 2004 are as follows:

Date of grant	Number of shares under option outstanding	Date from which normally exercisable	Expiry date	Option price
31 March 2000	670,866	1 May 2005 ²	1 November 2005 ²	259p
7 September 2001	32,411	1 November 2004 ¹	1 May 2005 ¹	430p
7 September 2001	535,704	1 November 2006 ²	1 May 2007 ²	430p
10 September 2003	786,248	1 November 2006 ¹	1 May 2007 ¹	461p
10 September 2003	640,279	1 November 2008 ²	1 May 2009 ²	461p
9 September 2004	743,614	1 November 2007 ¹	1 May 2008 ¹	524p
9 September 2004	436,751	1 November 2009 ²	1 May 2010 ²	524p

1 Three year contract

2 Five year contract

7 Emoluments of directors of RAC plc

	2004 £000	2003 £000
The emoluments of the directors were as follows:		
Salary payments and fees (including benefits in kind)	1,939	1,796
Performance-related bonus	615	532
	2,554	2,328

Details of emoluments, share options, long term incentive schemes and directors' pension entitlements form part of the Remuneration Report on pages 35 to 41.

8 Taxation on profit on ordinary activities

Analysis of charge in year

	2004 £m	2003 £m
Current tax		
United Kingdom corporation tax at 30% (2003 – 30%)		
– subsidiaries	21.3	17.8
– share of joint ventures'	5.8	5.1
– share of associates'	1.3	1.0
	28.4	23.9
(Over)/under provision in respect of previous years		
– subsidiaries	(4.2)	(3.0)
– share of joint ventures'	0.6	0.5
	(3.6)	(2.5)
Total current tax	24.8	21.4
Deferred tax		
Origination and reversal of timing differences		
– subsidiaries	(1.2)	(5.1)
– share of joint ventures'	2.7	1.0
	1.5	(4.1)
Over provision in respect of previous years		
– subsidiaries	(0.6)	(1.1)
– share of joint ventures'	(0.5)	–
	(1.1)	(1.1)
Total deferred tax	0.4	(5.2)
Taxation on profit on ordinary activities	25.2	16.2

8 Taxation on profit on ordinary activities (continued)

Factors affecting the current tax charge for the year

The current tax assessed for the year is higher than the standard rate of corporation tax in the UK (30%). The differences between the standard rate of corporation tax in the UK and the current tax charge for the Group are explained below:

	2004 £m	2003 £m
Profit on ordinary activities before taxation	77.7	25.7
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2003 – 30%)	23.3	7.7
Effects of		
Expenses not deductible for tax purposes (primarily goodwill amortisation and impairment of asset values)	6.8	16.2
Depreciation (less than)/in excess of capital allowances	(1.4)	4.1
Utilisation of capital gains tax losses	–	(4.4)
Foreign (profits)/losses for which no tax relief is available	(0.3)	0.3
Adjustments to tax charge in respect of previous years	(3.6)	(2.5)
Total current tax	24.8	21.4

Factors that may affect future tax charges

There are no factors expected to significantly affect the tax charge in the future.

9 Equity dividends

	2004 £m	2003 £m
The dividends for the year are:		
Ordinary dividends		
Interim paid of 10.2p per share (2003 – 9.7p)	12.0	11.5
Final proposed of 15.6p per share (2003 – 14.6p)	18.5	17.2
Dividends waived	(1.0)	(0.7)
Equity dividends	29.5	28.0

During the year Lex Employee Benefit Trustees Limited and Mourant & Co. Trustees Limited, which own shares in relation to the Long Term Incentive Plan and Executive Share Option Scheme respectively, waived their right to dividends of £1.0 million (2003 – £0.7 million). Both have also waived their right to future dividend payments.

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for the financial year ended 31 December 2004

10 Earnings per ordinary share

	2004 £m	2004 Undiluted pence	2004 Diluted pence
Profit for the financial year / earnings per ordinary share	52.5	45.8	44.7
Operating exceptional items	(7.5)		
Exceptional interest income on VAT refund	(3.3)		
Amortisation of goodwill	7.8		
Net loss on sale or closure of businesses	15.1		
Profit on sale of fixed assets	(1.2)		
Taxation impact of reconciling items	0.4		
Adjustment for exceptional items / earnings per ordinary share	11.3	9.9	9.6
Profit before goodwill amortisation and exceptionals / earnings per ordinary share	63.8	55.7	54.3
Taxation on profit before goodwill amortisation and exceptionals	24.8		
Profit before goodwill amortisation, exceptionals and taxation	88.6		
Weighted average number of shares (less any own shares held) in issue		114.6m	114.6m
Share options outstanding adjustment		–	3.0m
		114.6m	117.6m

	2003 £m	2003 Undiluted pence	2003 Diluted pence
Profit for the financial year / earnings per ordinary share	9.5	8.3	8.2
Operating exceptional items	30.2		
Amortisation of goodwill	5.6		
Net loss on sale or closure of businesses	26.0		
Profit on sale of fixed assets	(0.8)		
Taxation impact of reconciling items	(8.1)		
Adjustment for exceptional items / earnings per ordinary share	52.9	46.1	45.6
Profit before goodwill amortisation and exceptionals / earnings per ordinary share	62.4	54.4	53.8
Taxation on profit before goodwill amortisation and exceptionals	24.3		
Profit before goodwill amortisation, exceptionals and taxation	86.7		
Weighted average number of shares (less any own shares held) in issue		114.7m	114.7m
Share options outstanding adjustment		–	1.3m
		114.7m	116.0m

Earnings per share are also shown by reference to earnings before goodwill amortisation and exceptionals because the directors consider this gives a useful representation of underlying performance.

11 Intangible fixed assets

Group	Goodwill £m
Cost or valuation	
1 January 2004	552.0
Provisional goodwill arising on acquisition (see note 28)	40.3
Arising on disposals	(5.8)
31 December 2004	586.5
Amortisation	
1 January 2004	51.3
Arising on disposals	(5.6)
Charge for the year	7.1
31 December 2004	52.8
Net book value at 31 December 2004	533.7
Net book value at 1 January 2004	500.7

12 Tangible fixed assets

Group	Land and buildings £m	Assets held for contract hire £m	Vehicles, plant, fixtures and fittings £m	Total £m
Cost				
1 January 2004	74.3	73.3	128.0	275.6
Exchange adjustment	–	(3.1)	–	(3.1)
Additions	3.7	1.7	65.5	70.9
Disposals	(0.6)	(7.7)	(75.4)	(83.7)
Disposed businesses	(4.5)	(64.2)	(2.6)	(71.3)
31 December 2004	72.9	–	115.5	188.4
Depreciation				
1 January 2004	13.6	63.3	21.5	98.4
Exchange adjustment	–	(2.5)	–	(2.5)
Charge for the year	3.3	3.3	25.6	32.2
Disposals	(0.3)	(6.1)	(33.5)	(39.9)
Disposed businesses	(1.4)	(58.0)	(1.7)	(61.1)
31 December 2004	15.2	–	11.9	27.1
Net book value at 31 December 2004	57.7	–	103.6	161.3
Net book value at 1 January 2004	60.7	10.0	106.5	177.2

Included in the fixed assets of the Group are assets held under finance leases with a net book value of £0.9 million (2003 – £1.9 million). The amount of depreciation on assets held under finance leases for the year was £1.2 million (2003 – £6.1 million).

The total value of land and buildings not depreciated during the year amounted to £7.7 million (2003 – £7.9 million).

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12 Tangible fixed assets (continued)

RAC plc	Land and buildings £m	Vehicles, plant, fixtures and fittings £m	Total £m
Cost			
1 January 2004	22.8	3.9	26.7
Additions	0.4	0.2	0.6
Disposals	(0.5)	–	(0.5)
31 December 2004	22.7	4.1	26.8
Depreciation			
1 January 2004	7.7	3.0	10.7
Charge for the year	0.7	0.3	1.0
Disposals	(0.1)	–	(0.1)
31 December 2004	8.3	3.3	11.6
Net book value at 31 December 2004	14.4	0.8	15.2
Net book value at 1 January 2004	15.1	0.9	16.0

Land and buildings at 31 December 2004 are stated at cost, net of accumulated depreciation as set out below:

Group	Freehold £m	Long leasehold £m	Short leasehold £m	Total £m
Cost	58.4	6.8	7.7	72.9
Accumulated depreciation	(7.7)	(2.1)	(5.4)	(15.2)
Net book value	50.7	4.7	2.3	57.7

RAC plc	Freehold £m	Long leasehold £m	Short leasehold £m	Total £m
Cost	13.1	4.1	5.5	22.7
Accumulated depreciation	(2.7)	(0.9)	(4.7)	(8.3)
Net book value	10.4	3.2	0.8	14.4

Land and buildings at 31 December 2003 are stated at cost, net of accumulated depreciation as set out below:

Group	Freehold £m	Long leasehold £m	Short leasehold £m	Total £m
Cost	62.4	5.2	6.7	74.3
Accumulated depreciation	(7.4)	(2.0)	(4.2)	(13.6)
Net book value	55.0	3.2	2.5	60.7

RAC plc	Freehold £m	Long leasehold £m	Short leasehold £m	Total £m
Cost	13.3	4.2	5.3	22.8
Accumulated depreciation	(2.5)	(0.8)	(4.4)	(7.7)
Net book value	10.8	3.4	0.9	15.1

13 Fixed asset investments: Group

The movements in the year in the Group's investments were as follows:

	Joint ventures £m	Associates £m	Total £m
Share of net assets			
1 January 2004	49.2	5.9	55.1
Share of profit on ordinary activities after taxation	19.1	2.9	22.0
Dividends	(9.2)	(3.0)	(12.2)
Capital injection	7.5	–	7.5
31 December 2004	66.6	5.8	72.4

Included within the Group's retained profit is a retained loss of £16.4 million (2003 – retained loss of £26.2 million) relating to the Group's share of profit or loss retained by the joint ventures and associates. The capital injection related to Lex Vehicle Leasing.

The following information is provided in respect of the Group's share of joint ventures and associates.

	Lex Vehicle Leasing 2004 £m	Other joint ventures 2004 £m	Associates 2004 £m	Total 2004 £m
Profit and loss account				
Turnover	241.8	100.5	7.8	350.1
Profit before exceptional items and taxation	24.0	2.8	4.2	31.0
Exceptional items	0.8	0.1	–	0.9
Profit on ordinary activities before taxation	24.8	2.9	4.2	31.9
Taxation	(7.7)	(0.9)	(1.3)	(9.9)
Profit on ordinary activities after taxation	17.1	2.0	2.9	22.0
Balance sheet				
Fixed assets	544.5	70.4	–	614.9
Current assets	38.7	15.2	94.8	148.7
Liabilities due in less than one year	(251.0)	(41.4)	(44.7)	(337.1)
Liabilities due in more than one year	(275.5)	(34.3)	(44.3)	(354.1)

	Lex Vehicle Leasing 2003 £m	Other joint ventures 2003 £m	Associates 2003 £m	Total 2003 £m
Profit and loss account				
Turnover	207.2	96.0	7.3	310.5
Profit before exceptional items and taxation	21.4	2.2	3.4	27.0
Exceptional items	–	(2.5)	–	(2.5)
Profit/(loss) on ordinary activities before taxation	21.4	(0.3)	3.4	24.5
Taxation	(6.7)	0.1	(1.0)	(7.6)
Profit/(loss) on ordinary activities after taxation	14.7	(0.2)	2.4	16.9
Balance sheet				
Fixed assets	454.5	73.4	–	527.9
Current assets	18.6	26.3	96.8	141.7
Liabilities due in less than one year	(262.0)	(51.3)	(47.3)	(360.6)
Liabilities due in more than one year	(171.0)	(39.3)	(43.6)	(253.9)

Details of joint ventures and associates are shown on page 78.

Neither the Company nor any of its subsidiaries had guaranteed the borrowings of the joint ventures or any of the associates.

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13 Fixed asset investments: Group (continued)

Services provided by RAC plc to its joint ventures and associates

Internal audit, legal and property services are provided by RAC plc to its joint ventures and associates. The costs involved in respect of these services was £0.5 million (2003 – £0.4 million).

Transactions with joint ventures and associates

Hyundai Car Finance Limited

Sales of £359.7 million (2003 – £302.8 million) were made by the Group to third parties which were financed by Hyundai Car Finance, an associate. The balance due from Hyundai Car Finance at 31 December 2004 was £1.3 million (2003 – £1.7 million).

Lex Defence (Whitefleet) Limited

Net purchases of £36.1 million (2003 – £42.0 million) were made by the Group from Lex Defence (Whitefleet), a joint venture. The balance due from Lex Defence (Whitefleet) at 31 December 2004 was £0.1 million (2003 – £2.0 million due to Lex Defence (Whitefleet)).

Lex Transfleet Limited

Net sales of £4.3 million (2003 – £3.1 million) were made by the Group to Lex Transfleet, a joint venture. The balance due from Lex Transfleet at 31 December 2004 was £5.6 million (2003 – £3.6 million).

Lex Vehicle Leasing (Holdings) Limited

Net purchases of £46.7 million (2003 – £44.0 million) were made by the Group from Lex Vehicle Leasing, a joint venture. The balance due from Lex Vehicle Leasing at 31 December 2004 was £0.7 million (2003 – £2.1 million).

RAC Trafficmaster Telematics Limited

Net purchases of £0.2 million (2003 – £0.3 million) were made by the Group from RAC Trafficmaster Telematics, a joint venture. The balance due from RAC Trafficmaster Telematics at 31 December 2004 was £0.7 million (2003 – £0.5 million).

Operating lease agreements with joint ventures and associates

The Group has operating lease agreements with Lex Vehicle Leasing, a joint venture. The amount paid by the Group in the year was £52.1 million (2003 – £51.2 million).

14 Fixed asset investments: RAC plc

	Subsidiary undertakings £m	Joint ventures £m	Total £m
Cost			
1 January 2004	724.4	77.6	802.0
Capital injection	–	7.5	7.5
Disposals	(9.0)	–	(9.0)
31 December 2004	715.4	85.1	800.5
Provisions			
1 January 2004	90.6	–	90.6
Reversal of impairment	(4.3)	–	(4.3)
Disposals	(0.2)	–	(0.2)
31 December 2004	86.1	–	86.1
Net book value at 31 December 2004	629.3	85.1	714.4
Net book value at 1 January 2004	633.8	77.6	711.4

Details of the Company's principal subsidiary undertakings and the Company's effective holdings in the principal joint ventures and associates are set out on page 78.

15 Stocks

	2004 £m	Group 2003 £m
Finished goods		
Vehicles	129.6	118.8
Vehicle repurchase commitments	21.5	14.4
Vehicle parts	36.8	41.5
	187.9	174.7
Work in progress	0.3	0.3
Raw materials and consumables	1.3	1.3
Total stocks	189.5	176.3

Vehicle consignment stock

Vehicle consignment stock amounting to £0.5 million (2003 – £0.3 million) has been reflected in stock in the balance sheet together with an associated creditor. This consignment stock has been acquired under agreements with finance companies at an interest rate of 2% over finance house rates.

In addition, the Group held consignment stock with a cost of £3.9 million (2003 – £4.9 million) in respect of which the benefits and risks of holding the stock had not been passed to the Group. This stock was held under agreements providing interest free periods of up to 100 days.

Vehicle repurchase commitments

Vehicle repurchase commitments amounting to £21.5 million (2003 – £14.4 million) have been reflected in stock in the balance sheet together with an associated creditor. This stock represents contractual obligations to repurchase certain vehicles previously sold as part of normal trading activities.

16 Debtors

	2004 £m	Group 2003 £m	2004 £m	RAC plc 2003 £m
Amounts falling due within one year				
Trade debtors	85.2	105.1	–	0.3
Amounts owed by subsidiary undertakings	–	–	148.1	139.7
Amounts owed by joint ventures and associates	8.7	8.8	6.0	3.7
Corporation tax	–	–	–	2.6
Amounts owed on disposal of business	0.3	–	–	–
Other debtors	23.2	15.9	4.5	3.5
Prepayments and accrued income	35.9	25.1	0.6	0.5
	153.3	154.9	159.2	150.3
Amounts falling due after one year				
Deferred taxation (note 21)	–	–	9.2	7.8
Amounts owed on disposal of business	2.0	–	–	–
Other debtors	43.7	44.8	–	–
	45.7	44.8	9.2	7.8
Total debtors	199.0	199.7	168.4	158.1

17 Cash at bank and in hand

Included within cash in the consolidated balance sheet is an amount of £31.8 million (2003 – £16.8 million) which is not readily available for use by the Group. Of this amount £24.6 million (2003 – £7.7 million) is held to comply with regulatory requirements applicable to insurance businesses.

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18 Creditors: amounts falling due within one year

	Notes	2004 £m	Group 2003 £m	2004 £m	RAC plc 2003 £m
Bank and other loans					
Bank overdrafts		6.3	29.8	13.9	29.4
Unsecured loan notes	(a)	2.5	3.3	2.5	3.3
Guaranteed loan notes	(b)	13.6	17.4	13.6	17.4
Other loans	(c)	20.0	45.9	20.0	43.3
		42.4	96.4	50.0	93.4
Other creditors					
Trade creditors		101.7	92.0	1.0	0.6
Vehicle consignment stock creditor		0.5	0.3	–	–
Vehicle repurchase commitments		21.5	14.4	–	–
Vehicle consignment deposits received		14.3	16.9	–	–
Amounts owed to subsidiary undertakings		–	–	188.7	335.7
Amounts owed to joint ventures and associates		0.3	2.9	–	–
Corporation tax		16.6	19.3	16.6	–
Other taxation including social security		29.9	27.9	0.3	0.3
Other creditors		50.4	55.9	2.7	5.4
Amounts due on purchase of business		7.5	–	–	–
Obligations under finance leases and similar hire purchase agreements (see note 20)		1.0	2.3	–	–
Accruals and deferred income		235.6	210.6	4.8	5.6
Proposed dividend for equity shareholders		17.9	16.8	17.9	16.8
		497.2	459.3	232.0	364.4
Total creditors: amounts falling due within one year		539.6	555.7	282.0	457.8

Notes:

- (a) These loan notes bear interest at a rate 0.75% below LIBOR. A resolution was passed in December 2003 to extend the maturity date of the loan notes to July 2010. The notes may be redeemed in May and November each year up until their maturity.
- (b) £13.6 million of notes bearing interest at 2% below LIBOR were outstanding (2003 – £17.4 million) and may be redeemed as per the unsecured loan notes detailed in (a) above. Redemption of any of the guaranteed loan notes will increase RAC's available facilities by an equal amount.
- (c) £20.0 million of bank loans outstanding at 31 December 2004 were at short term rates linked to interbank rates. The 2003 figures included a \$70 million US private placement at a fixed dollar interest rate of 7.73% per annum which matured in December 2004. The loan had been swapped into floating rate sterling.

19 Creditors: amounts falling due after more than one year

	Notes	2004 £m	Group 2003 £m	2004 £m	RAC plc 2003 £m
Bank and other loans					
US private placement	(a)	52.3	52.3	52.3	52.3
Bank loans	(b)	86.0	45.1	86.0	45.1
		138.3	97.4	138.3	97.4
The loans are repayable as follows:					
– between one and two years	(c)	–	30.0	–	30.0
– between two and five years		108.3	15.1	108.3	15.1
– after five years		30.0	52.3	30.0	52.3
		138.3	97.4	138.3	97.4
Other creditors					
Pensions and post-retirement medical benefits		43.6	40.8	43.0	40.8
Deferred income		23.0	33.8	–	–
Obligations under finance leases and similar hire purchase agreements (see note 20)		0.3	0.4	–	–
		66.9	75.0	43.0	40.8
Total creditors: amounts falling due after more than one year		205.2	172.4	181.3	138.2

Notes:

- (a) The \$75 million US private placement matures in May 2009 and bears interest at a fixed dollar interest rate of 7.64% per annum. The loan has been swapped into floating rate sterling and at 31 December 2004 the floating rate was 7.03%.
- (b) Bank loans are in euros and sterling at rates linked to interbank rates.
- (c) Loan maturities are classified according to committed facility expiry dates.

20 Creditors: obligations under finance leases

	2004 £m	Group 2003 £m
Obligations under finance leases are repayable as follows:		
– between one and two years	0.3	0.4
– within one year	1.0	2.3
Total obligations under finance leases	1.3	2.7

21 Deferred taxation

	2004 £m	Group 2003 £m	2004 £m	RAC plc 2003 £m
Accelerated capital allowances	(8.4)	(7.9)	(1.8)	(1.8)
Other timing differences	(0.5)	(2.8)	11.0	9.6
Deferred taxation (liability)/asset	(8.9)	(10.7)	9.2	7.8

The movements in the year in the Group provision for deferred taxation are shown in note 22.

The movement in the year in the deferred taxation asset in RAC plc was as follows:

	RAC plc £m
1 January 2004	7.8
Credit to profit and loss account	1.4
31 December 2004	9.2

22 Provisions for liabilities and charges

Group	Property costs £m	Deferred taxation £m	Vehicle £m	Other £m	Total £m
1 January 2004	5.5	10.7	4.5	3.2	23.9
Created	0.8	–	6.1	–	6.9
(Credit)/charge to profit and loss account	–	(1.2)	–	0.3	(0.9)
Over provision in respect of previous years	–	(0.6)	–	–	(0.6)
Utilised	(1.0)	–	(2.3)	(0.6)	(3.9)
31 December 2004	5.3	8.9	8.3	2.9	25.4

RAC plc	Property costs £m
1 January 2004	3.5
Created	0.8
Utilised	(0.5)
31 December 2004	3.8

The property costs provision relates to dilapidations and rent on onerous lease agreements in respect of vacant properties. Amounts will be paid out on these onerous leases until 2014 and on dilapidations over periods up to 25 years.

Vehicle provisions relate to free servicing and RAC membership and are expected to be utilised by 2007.

Other provisions relate to self-insured permanent health arrangements and unfunded pension obligations for employees subject to the earnings cap. These provisions will be utilised over the remaining lives of those individuals involved.

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23 Share capital

	Shares	2004 £m	Shares	2003 £m
Authorised				
Ordinary shares of 25p each	156,940,000	39.2	156,940,000	39.2
Allotted, called up and fully paid				
Ordinary shares of 25p each	118,798,024	29.7	118,077,790	29.5

113,378 ordinary shares were allotted during the year following the exercise of options granted under the Executive Share Option Scheme (1994), and the total consideration received for those shares was £499,997.

606,856 ordinary shares were allotted during the year following the exercise of options granted under the Sharesave Scheme, and the total consideration received for those shares was £2,556,550.

Further details of the share option schemes in operation during the year can be found in note 6.

24 Share premium account, reserves and minority interests: Group

	Share premium account £m	Own shares held reserve £m	Capital redemption reserve £m	Profit and loss account £m	Minority interests £m
1 January 2004	133.4	(14.0)	1.0	249.3	–
Retained profit for the financial year	–	–	–	23.0	–
Goodwill previously written off now charged to profit for the financial year	–	–	–	9.4	–
Premium on issue of ordinary shares	2.9	–	–	–	–
Transfer of own shares held reserve	–	14.0	–	(14.0)	–
Net increase in own shares held	–	–	–	(7.7)	–
Increase in minority interest arising from acquisition of 15% of Isuzu Truck (UK) Limited	–	–	–	–	0.2
Exchange variations	–	–	–	0.7	–
31 December 2004	136.3	–	1.0	260.7	0.2

The cumulative amount of goodwill written off to reserves resulting from acquisitions before 1 January 1998, net of goodwill attributable to subsidiary undertakings or businesses disposed, amounted to £114.7 million (2003 – £124.1 million). Goodwill arising from acquisitions since 1 January 1998 has been capitalised.

Included within the profit and loss account are own shares held which represents the cost of funding the purchase by Trustees of the Company's own shares in respect of the Long Term Incentive Plan and the Executive Share Option Scheme (2001) ('the Scheme'). 3,902,953 (2003 – 2,852,185) ordinary shares with a nominal value of 25p each have been purchased in total on the open market at a cost of £21.7 million (2003 – £14.0 million). Further details are included within the Remuneration Report.

25 Capital and reserves: RAC plc

	Share capital £m	Share premium account £m	Own shares held reserve £m	Capital redemption reserve £m	Merger reserve £m	Other reserve £m	Profit and loss account £m	Total £m
1 January 2004	29.5	133.4	(14.0)	1.0	24.9	19.8	91.9	286.5
Retained profit for the financial year before equity dividends	–	–	–	–	–	–	179.1	179.1
Equity dividends	–	–	–	–	–	–	(29.5)	(29.5)
Issue of ordinary shares	0.2	2.9	–	–	–	–	–	3.1
Transfer of own shares held reserve	–	–	14.0	–	–	–	(14.0)	–
Net increase in own shares held	–	–	–	–	–	–	(7.7)	(7.7)
Realisation of merger reserve	–	–	–	–	(24.9)	–	24.9	–
Exchange variations	–	–	–	–	–	–	(0.1)	(0.1)
31 December 2004	29.7	136.3	–	1.0	–	19.8	244.6	431.4

The retained profit for the financial year before equity dividends of the Company was £179.1 million (2003 – £33.5 million).

The merger reserve was realised during the year following the liquidation of a number of subsidiaries acquired as part of the acquisition of the Sears Motor Group Limited in 1987. At that time, the premium on the shares allotted in part settlement of the acquisition was credited to the merger reserve.

The other reserve arose in 2002 on the assignment of certain trademarks to RAC Brand Management, a subsidiary undertaking, at market value.

26 Reconciliation of operating profit/(loss) to net cash inflow from operating activities

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 £m	Discontinued operations 2003 £m	Total 2003 £m
Operating profit/(loss)	66.4	(0.2)	66.2	65.5	(32.2)	33.3
Interest on contract hire businesses	–	0.6	0.6	–	4.2	4.2
Depreciation and goodwill amortisation	35.8	3.5	39.3	30.3	52.5	82.8
(Profit)/loss on disposal of tangible fixed assets	(1.3)	–	(1.3)	0.8	(0.4)	0.4
(Increase)/decrease in stocks	(22.7)	1.0	(21.7)	1.9	2.5	4.4
(Increase)/decrease in debtors	(10.8)	1.1	(9.7)	(16.1)	18.7	2.6
Increase/(decrease) in creditors and provisions	38.7	(2.1)	36.6	5.2	(15.0)	(9.8)
Net cash inflow from operating activities in the year	106.1	3.9	110.0	87.6	30.3	117.9

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27 Capital expenditure and financial investment

	Continuing operations 2004 £m	Discontinued operations 2004 £m	Total 2004 £m	Continuing operations 2003 £m	Discontinued operations 2003 £m	Total 2003 £m
Tangible fixed assets acquired	(68.4)	(1.8)	(70.2)	(69.8)	(19.3)	(89.1)
Tangible fixed assets sold	43.6	1.8	45.4	43.3	5.1	48.4
Capital injection into joint venture	(7.5)	–	(7.5)	–	–	–
Net cash outflow from capital expenditure and financial investment	(32.3)	–	(32.3)	(26.5)	(14.2)	(40.7)

28 Subsidiary undertakings and businesses acquired

RAC Consumer Services

On 17 September 2004 the Group acquired AXA's interest in RAC Financial Services and the renewal rights of AXA Direct insurance contracts. Total consideration, including deferred consideration and acquisition expenses, is expected to be £40.1 million. This has been capitalised as goodwill in the Group balance sheet. The deferred consideration is linked to the number of successful conversions from the renewal rights acquired. The potential range of deferred consideration payable is £nil up to a maximum of £13.4 million. The deferred consideration estimated to be payable is £7.5 million.

Manufacturer Support Services

Prior to the disposal of the net assets of Isuzu Truck (UK) the Group entered into an agreement to acquire the remaining minority interest in Isuzu Truck (UK) Limited for consideration of £nil. The value of the minority acquired was £(0.2) million. The goodwill arising was capitalised and immediately written off to the loss on disposal of the business (see note 29).

	RAC Consumer Services £m	Manufacturer Support Services £m	2004 £m	2003 £m
Reconciliation to goodwill arising on acquisition				
Consideration	37.2	–	37.2	0.3
Acquisition expenses	2.9	–	2.9	–
Net assets acquired	–	–	–	(0.2)
Minority interest acquired	–	0.2	0.2	–
Goodwill arising on acquisition	40.1	0.2	40.3	0.1

Reconciliation to net cash outflow from subsidiary undertakings and businesses acquired

Consideration	(37.2)	(0.3)
Deferred consideration payable	7.5	–
Acquisition expenses paid at the year end	(1.1)	–
Net cash outflow from subsidiary undertakings and businesses acquired	(30.8)	(0.3)

29 Subsidiary undertakings and businesses disposed

Mechanical Handling

On 13 January 2004 the Group disposed of Lex Havelange SA for consideration, including net debt divested, of £1.0 million. On 1 April 2004 the Group disposed of the net assets of Lex Komatsu Forklift (South) Limited for consideration, net of cash divested, of £7.6 million. Of this consideration, £2.3 million is receivable in three annual instalments (2005 – £0.3 million, 2006 – £1.0 million, 2007 – £1.0 million) commencing on the first anniversary of completion. On 17 June 2004 the Group disposed of Lex Manutention SA for consideration, including net debt divested, of £6.5 million. The total exceptional loss on these disposals was £11.2 million, after writing back goodwill from reserves of £9.4 million.

Manufacturer Support Services

On 8 March 2004 the Group disposed of the net assets of Isuzu Truck (UK) Limited for consideration of £3.4 million. On 27 September 2004 the Group disposed on the net assets of Multipart Universal, a division of Lex Multipart Limited, for consideration of £3.1 million. The total exceptional loss on these disposals was £3.9 million.

	Mechanical Handling £m	Manufacturer Support Services £m	2004 £m	2003 £m
Analysis of net assets disposed				
Tangible fixed assets	8.2	2.0	10.2	98.4
Stocks	1.3	7.2	8.5	1.9
Debtors	9.6	3.0	12.6	–
Cash at bank and in hand	3.0	–	3.0	–
Total assets	22.1	12.2	34.3	100.3
Bank and other loans	(5.2)	–	(5.2)	–
Creditors	(6.5)	(3.5)	(10.0)	(0.7)
Total liabilities	(11.7)	(3.5)	(15.2)	(0.7)
Net assets disposed	10.4	8.7	19.1	99.6
Reconciliation to exceptional loss on disposal				
Total proceeds	12.9	6.5	19.4	94.6
Net assets disposed	(10.4)	(8.7)	(19.1)	(99.6)
Disposal expenses incurred	(4.3)	(1.5)	(5.8)	(8.7)
Goodwill previously capitalised written off	–	(0.2)	(0.2)	–
Goodwill previously written off to reserves	(9.4)	–	(9.4)	(9.8)
Exceptional loss on disposal	(11.2)	(3.9)	(15.1)	(23.5)
Reconciliation to net cash inflow from subsidiary undertakings and businesses disposed				
Total proceeds			19.4	94.6
Cash at bank and in hand divested			(3.0)	–
Bank and other loans divested			5.2	–
Deferred consideration receivable			(2.3)	–
Disposal expenses paid at the year end			(2.9)	(3.7)
Disposal expenses paid in respect of previously disposed businesses			(0.7)	(0.6)
Net cash inflow from subsidiary undertakings and businesses disposed			15.7	90.3

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30 Analysis of net debt

	2004 £m	Cash flow £m	New finance leases £m	Exchange movements £m	2003 £m
Investments	6.7	(14.1)			20.8
Ring fenced cash and short term deposits	31.8	15.0			16.8
Increase in liquid resources and current investments		0.9			
Cash	3.7	(0.9)			4.6
Cash at bank and in hand	35.5				21.4
Overdrafts	(6.3)	23.3		0.2	(29.8)
Increase in cash in the year		22.4			
Other debt due within one year	(36.1)	30.5			(66.6)
Bank and other loans due within one year	(42.4)				(96.4)
Bank and other loans due after one year	(138.3)	(40.9)			(97.4)
Obligations under finance leases	(1.3)	2.1	(0.7)		(2.7)
Increase in debt and finance leases		(8.3)			
Net debt	(139.8)	15.0	(0.7)	0.2	(154.3)

Investments are not readily available for use by the Group.

31 Capital commitments

	2004 £m	Group 2003 £m
Capital expenditure contracted for but not provided		
Contract hire businesses	–	1.8
Non contract hire businesses	0.3	3.7
	0.3	5.5

The Group's share of joint venture and associated undertakings capital commitments was £34.0 million (2003 – £35.2 million).

32 Operating lease commitments

	Land and buildings 2004 £m	Other 2004 £m	Total 2004 £m	Land and buildings 2003 £m	Other 2003 £m	Total 2003 £m
Group						
Annual lease commitment on leases expiring						
– within one year	0.8	2.1	2.9	0.8	1.9	2.7
– from two to five years	6.0	9.4	15.4	4.1	11.6	15.7
– after five years	4.4	–	4.4	8.0	–	8.0
	11.2	11.5	22.7	12.9	13.5	26.4
RAC plc						
Annual lease commitment on leases expiring						
– within one year	0.1	0.1	0.2	0.1	0.1	0.2
– from two to five years	2.1	0.2	2.3	0.2	0.2	0.4
– after five years	0.4	–	0.4	2.9	–	2.9
	2.6	0.3	2.9	3.2	0.3	3.5

Excluded from the analysis above are operating lease commitments of £52.5 million (2003 – £53.5 million) between Lex Defence Management Limited, a wholly owned subsidiary, and certain joint ventures of the Group. Lex Defence Management acts solely as an intermediary between these joint ventures and certain customers.

33 Pension schemes

The Group has continued to account for pensions in accordance with SSAP24 Accounting for pension costs, see (a) and (b) below. The relevant transitional disclosures under FRS17 Retirement benefits, are shown in section (c).

The Group operates both defined benefit and defined contribution schemes for eligible UK employees. The assets of these schemes are held independently from those of RAC plc, its subsidiaries and joint venture undertakings.

RAC plc's pension costs are charged to the profit and loss account so as to spread them systematically over employees' working lives with the Group.

(a) RAC (2003) Pension Scheme

The RAC (2003) Pension Scheme (the 'Scheme') is a funded defined benefit scheme and was formerly called the Lex Service Pension Scheme. It was renamed on 11 February 2003 following the transfer on 1 January 2002 of the assets and liabilities of the RAC Pension Scheme into the assets and liabilities of the Lex Service Pension Scheme.

The most recent actuarial valuation was carried out as at 5 April 2004 by an independent qualified actuary using the projected unit method on an ongoing basis.

The principal assumptions applied in the valuation calculations were:

Pre-retirement interest	6.9% p.a.
Post-retirement interest	5.7% p.a.
Increases in pensionable salaries	4.0% p.a.
Price inflation	2.5% p.a.

In addition, the valuation included an allowance for discretionary increases in payment of 1.67% p.a. relating to service before 6 April 1997 for former Lex Service Pension Scheme members and an allowance of 2.5% p.a. for former members of the RAC Pension Scheme. An allowance of 2.5% p.a. is also made for guaranteed pension increases relating to service after 5 April 1997 (pensions relating to service after 5 April 1997 are guaranteed to increase in line with RPI up to a maximum of 5% p.a.).

At the date of the valuation, the discounted value of the assets of the Scheme was £492.5 million, which was sufficient to cover 79% of the benefits which had accrued to members, allowing for future expected increases in earnings.

The cost of providing pension benefits for the future has increased. This is primarily because people are living longer, typically drawing a pension for twice as long as they did in the 1960s, which requires a proportionate increase in funding. In addition, tax changes and lower anticipated investment returns are also increasing the cost of funding the Scheme. To maintain the Scheme, the Group has shared the increase in costs with employees, who during 2003 were offered the choice of reduced future benefit levels or increased employee contribution rates from 1 July 2003. The Group has also increased its contributions into the pension fund.

For determining pension cost, the shortfall of the market value of assets over liabilities is spread throughout the expected remaining service lives of employees currently in the Scheme.

The total pension cost, including administration costs, of the merged Scheme was £23.5 million (2003 – £21.8 million) of which £3.2 million (2003 – £2.6 million) was attributable to joint venture undertakings.

A net prepayment of £3.0 million (2003 – £3.0 million) is included in the balance sheet.

(b) Other schemes

The Group operates a number of smaller defined benefits and defined contribution schemes.

The aggregate total pension cost of these schemes was £1.5 million (2003 – £1.5 million).

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33 Pension schemes (continued)

(c) FRS 17 Retirement benefits

The major financial assumptions used to calculate scheme liabilities under FRS 17 are:

	2004	2003	2002
Discount rate	5.4%	5.5%	5.6%
Inflation rate	2.6%	2.5%	2.2%
Increase to deferred benefits during deferment	2.6%	2.5%	2.2%
Increase to pensions in payment	2.6%	2.5%	2.2%
Salary increases	4.1%	4.0%	3.7%

On full compliance with FRS 17, on the basis of the above assumptions, the amounts that would have been charged to operating profit, finance income and consolidated statement of total recognised gains and losses for the year ended 31 December 2004 are set out below:

	2004 £m	Group 2003 £m
Operating profit		
Current service cost	(17.2)	(20.4)
Past service cost	—	—
Total charge to operating profit	(17.2)	(20.4)

Finance income

Expected return on pension scheme assets	32.5	24.4
Interest on pension scheme plan liabilities	(35.6)	(32.5)
Net charge to finance income	(3.1)	(8.1)

Consolidated statement of total recognised gains and losses

Actual return less expected return on post employment plan assets	18.7	51.0
Experience (losses) and gains arising on the plan liabilities	(32.2)	6.3
Changes in assumptions underlying the present value of the plan liabilities	(25.6)	(41.9)
Actuarial (loss)/gain recognisable in the consolidated statement of total recognised gains and losses	(39.1)	15.4

Movement in deficit in year

Deficit in scheme at 1 January	(175.6)	(184.8)
Movements in year		
— current service cost	(17.2)	(20.4)
— past service cost	—	—
— contributions	24.0	22.3
— net charge to finance income	(3.1)	(8.1)
— actuarial (loss)/gain	(39.1)	15.4
Deficit in scheme at the end of the year	(211.0)	(175.6)

	2004 £m	Group 2003 £m	2002 £m
History of experience gains and losses			
Difference between the expected and actual return on plan assets			
— amount £ million	18.7	51.0	(104.6)
— percentage of scheme assets	4%	11%	(27%)
Experience (losses)/gains on plan liabilities			
— amount £ million	(32.2)	6.3	(16.8)
— percentage of the present value of scheme liabilities	(4%)	1%	(3%)
Total amount recognised in consolidated statement of total recognised gains and losses			
— amount £ million	(39.1)	15.4	(115.6)
— percentage of the present value of scheme liabilities	(5%)	2%	(20%)

33 Pension schemes (continued)

(c) FRS 17 Retirement benefits (continued)

The assets and liabilities in the schemes and the expected rate of return were:

	Long-term rate of return expected 2004	2004 £m	Long-term rate of return expected 2003	2003 £m	Long-term rate of return expected 2002	2002 £m
Equities	7.30%	365.0	7.50%	340.2	6.72%	270.8
Bonds	4.89%	157.3	5.08%	121.8	5.03%	111.0
Other	4.75%	6.3	4.00%	4.5	4.00%	7.4
Total market value of assets		528.6		466.5		389.2
Present value of liabilities in the schemes		(739.6)		(642.1)		(574.0)
Deficit in the schemes		(211.0)		(175.6)		(184.8)
Related deferred tax asset		63.3		52.7		55.5
Net pension liability		(147.7)		(122.9)		(129.3)

	2004 £m	2003 £m	2002 £m
Net assets			
Net assets excluding net SSAP 24 pension asset	425.8	397.1	400.5
Net pension liability	(147.7)	(122.9)	(129.3)
Net assets including net pension liability	278.1	274.2	271.2

	2004 £m	2003 £m	2002 £m
Reserves – Profit and loss account			
Profit and loss account excluding net SSAP 24 pension asset	258.6	247.2	255.5
Net pension liability	(147.7)	(122.9)	(129.3)
Profit and loss account including net pension liability	110.9	124.3	126.2

34 Post-retirement medical benefits

The Company provides medical benefits on a discretionary basis for certain pensioners and their dependants in the United Kingdom. In addition, certain employees may also become eligible for this benefit on retirement. The number of pensioners entitled to this benefit at 31 December 2004 was 175 (2003 – 184).

The Company's obligation for these benefits was assessed in 2004 by independent qualified actuaries using the projected unit credit method, which disclosed a liability of £4.4 million (2003 – £4.8 million). The future health care cost trend rates were 7.5% for two years, falling to 4.1% per annum thereafter. The discount rate used to determine the liability and cost was 5.75% per annum.

The liability recognised under SSAP 24 was £3.9 million (2003 – £3.9 million). The total cost of providing these benefits in 2004 was £0.3 million (2003 – £0.3 million).

35 Contingent liabilities

Cross guarantees

The Company and certain of its subsidiary undertakings have given cross guarantees in respect of joint bank accounts. The Company has also given other guarantees in respect of certain bank overdrafts of, and loans to, subsidiary undertakings. The Company's contingent liabilities in respect of these items amounted to £0.1 million at 31 December 2004 (2003 – £10.5 million). The consolidated balance sheet includes all of the overdrafts and loans.

End of life vehicles Directive

In September 2000, the European Parliament passed Directive 2000/53/EC on end of life vehicles. As part of this Directive, vehicle manufacturers and professional vehicle importers would be responsible for a significant part of the end of life costs of collecting, disposing and recycling new cars put on the road from 1 July 2002, and from 1 January 2007, for cars put on the road before 2002. There are a number of uncertainties surrounding the exact form and implementation of the legislation in the UK regarding vehicles registered prior to 1 July 2002.

Although industry estimates have been made, the Directors consider that they believe there is still insufficient information available to them to allow the assessment of the form or value of any obligations that may fall to the Group.

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36 Financial instruments

(a) Objective for holding or issuing financial instruments

The principal financial instruments held or issued by the Group are as follows:

- cash;
- debt, including loan notes and finance lease obligations;
- forward foreign exchange contracts;
- interest rate and currency swaps; and
- certain debtors and creditors that meet the definition of a financial instrument as set out in FRS13.

The Group's main objectives for holding cash are to meet day to day working capital and investment needs and to comply with regulatory requirements; forward foreign exchange contracts are held for hedging purposes as are interest rate and currency swaps.

The debtors, creditors and provisions arise directly as part of the Group's operations.

The main risks which the holding and issuing of financial instruments seek to control are liquidity risk, interest rate risk and exchange rate risk.

An explanation of the Board's objectives, policies and strategies for holding and issuing financial instruments is set out in the financial review on page 26.

(b) Liquidity

The maturity of all financial liabilities classified according to facility renewal dates is shown in the following table:

	Debt other than finance leases 2004 £m	Debt other than finance leases 2003 £m	Finance lease obligations 2004 £m	Finance lease obligations 2003 £m	Total 2004 £m	Total 2003 £m
Financial liabilities maturing						
– in one year or less or on demand	42.4	96.4	1.0	2.3	43.4	98.7
– in more than one year but not more than two years	–	30.0	0.3	0.4	0.3	30.4
– in more than two years but not more than five years	108.3	15.1	–	–	108.3	15.1
– in more than five years	30.0	52.3	–	–	30.0	52.3
	180.7	193.8	1.3	2.7	182.0	196.5

Undrawn borrowing facilities are available to the Group with the maturities set out in the following table:

	2004 £m	2003 £m
Undrawn borrowing facilities expiring		
– in one year or less	–	5.6
– in more than one year but not more than two years	–	79.6
– in more than two years	100.6	42.2
	100.6	127.4

The conditions precedent to the availability of these facilities are all satisfied at the balance sheet date.

36 Financial instruments (continued)

(c) Interest rate risk profile on financial assets

The interest rate profile of the financial assets of the Group was:

	Financial assets on which no interest is received 2004 £m	Floating rate financial assets 2004 £m	Fixed rate financial assets 2004 £m	Total financial assets 2004 £m	Fixed rate financial assets Weighted average interest rate 2004 %	Fixed rate financial assets Weighted average period for which rate is fixed 2004 months
Currency						
Sterling	0.2	33.7	5.0	38.9	6.0	27
Euro zone	1.0	4.7	4.2	9.9	3.6	19
Other	0.6	0.1	–	0.7	–	–
	1.8	38.5	9.2	49.5	4.9	24

	2003 £m	2003 £m	2003 £m	2003 £m	2003 %	2003 months
Currency						
Sterling	0.3	31.4	4.9	36.6	7.8	24
Euro zone	2.2	8.2	–	10.4	–	–
Other	–	0.1	–	0.1	–	–
	2.5	39.7	4.9	47.1	7.8	24

The interest free financial assets of £1.8 million have no set maturity dates and are immediately available to the Group.

Financial assets include cash, short and medium term investments and certain other debtors.

(d) Interest rate risk profile on financial liabilities

The interest rate profile of the financial liabilities of the Group was:

	Floating rate financial liabilities 2004 £m	Fixed rate financial liabilities 2004 £m	Total financial liabilities 2004 £m	Fixed rate financial liabilities Weighted average interest rate 2004 %	Fixed rate financial liabilities Weighted average period for which rate is fixed 2004 months
Currency					
Sterling	120.6	61.3	181.9	5.6	18
Euro zone	0.1	–	0.1	–	–
	120.7	61.3	182.0	5.6	18

	2003 £m	2003 £m	2003 £m	2003 %	2003 months
Currency					
Sterling	86.2	82.7	168.9	5.6	19
Euro zone	2.7	24.9	27.6	4.4	23
	88.9	107.6	196.5	5.3	20

The floating rate financial liabilities comprise overdrafts and other loans bearing interest rates that are linked to interbank rates.

There were no financial liabilities on which no interest was paid in either year.

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36 Financial instruments (continued)

(e) Currency risk

The analysis below shows the net monetary assets and liabilities of the Group that are not denominated in their functional currency and therefore give rise to exchange gains and losses in the profit and loss account. The amounts shown take into account the effect of foreign currency adjustments.

	Sterling 2004 £m	Sterling 2003 £m
Net foreign currency monetary assets		
US Dollar	0.1	–
Euro zone	2.7	2.1
Other	0.6	–
	3.4	2.1

(f) Fair values

The table below sets out the fair values and estimated book values of the Group's financial instruments:

	Book value 2004 £m	Fair value 2004 £m	Book value 2003 £m	Fair value 2003 £m
Primary financial instruments				
Debtors due within one year	1.5	1.5	–	–
Debtors due after more than one year	5.8	5.7	4.9	5.1
Cash at bank and in hand	35.5	35.5	21.4	21.4
Current asset investments	6.7	6.8	20.8	20.8
Bank and other loans	(180.7)	(180.7)	(193.8)	(190.4)
Other creditors falling due within one year	(1.0)	(1.0)	(2.3)	(2.4)
Other creditors due after more than one year	(0.3)	(0.3)	(0.4)	(0.4)
Derivative financial instruments				
Forward foreign exchange instruments to hedge currency exposure	–	(0.4)	–	(1.1)
Interest rate swaps	–	(0.7)	–	(2.1)
Currency swaps	–	(11.9)	–	(9.7)

As required by FRS 13 Derivatives and other financial instruments, pension and related benefits have been excluded from this analysis.

Fair values have been calculated using standard net present valuation methods and mark to market valuations provided by third parties.

36 Financial instruments (continued)

(g) Hedging

Hedging gains and losses on hedging instruments are not recognised until the underlying assets or liabilities are realised. The movement in unrecognised gains and losses on hedges is shown in the following table:

	Gains 2004 £m	Losses 2004 £m	Net gains/ (losses) 2004 £m
1 January 2004	0.1	(13.0)	(12.9)
Arising in previous years and recognised during the year	(0.1)	2.6	2.5
Arising before 1 January 2004 and not recognised during the year	–	(10.4)	(10.4)
Arising during the year and not recognised during the year	0.3	(2.9)	(2.6)
31 December 2004	0.3	(13.3)	(13.0)
Expected to be recognised			
– in one year or less	0.3	(3.9)	(3.6)
– in later years	–	(9.4)	(9.4)
	0.3	(13.3)	(13.0)

	Gains 2003 £m	Losses 2003 £m	Net gains/ (losses) 2003 £m
1 January 2003	5.4	(8.0)	(2.6)
Arising in previous years and recognised during the year	(0.1)	1.2	1.1
Arising before 1 January 2003 and not recognised during the year	5.3	(6.8)	(1.5)
Arising during the year and not recognised during the year	(5.2)	(6.2)	(11.4)
31 December 2003	0.1	(13.0)	(12.9)
Expected to be recognised			
– in one year or less	0.1	(4.2)	(4.1)
– in later years	–	(8.8)	(8.8)
	0.1	(13.0)	(12.9)

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37 Principal subsidiary undertakings, joint ventures and associates

The principal subsidiary undertakings, joint ventures and associates as at 31 December 2004 were:

Company	Principal activity by segment	RAC Group effective holding in ordinary share capital
RAC Motoring Services ¹	RAC Consumer Services, RAC Business Solutions, Other	100%
RAC Auto Windscreens Limited ¹	RAC Consumer Services	100%
RAC Software Solutions Limited	RAC Business Solutions	100%
<i>Lex Vehicle Leasing (Holdings) Limited²</i>	Lex Vehicle Leasing	50%
<i>Lex Transfleet Limited³</i>	Manufacturer Support Services	50%
<i>Lex Multipart Limited⁴</i>	Manufacturer Support Services	100%
<i>Hyundai Car (UK) Limited⁵</i>	Manufacturer Support Services	100%
<i>Hyundai Car Finance Limited⁵</i>	Manufacturer Support Services	49.99%
<i>Lex Commercials Limited</i>	Manufacturer Support Services	100%

Notes:

All shares are held directly by RAC plc unless otherwise stated below.

1 RAC Group shares in RAC Motoring Services and RAC Auto Windscreens Limited are held through a number of intermediate holding companies.

2 The remaining shares are held by Halifax Vehicle Leasing (1998) Limited.

3 The remaining shares are held by Lombard North Central PLC.

4 Lex Multipart Limited is a wholly owned subsidiary of Multipart (Holdings) Limited.

5 Hyundai Car (UK) Limited is a wholly owned subsidiary of Morgan Brown Limited, incorporated in the Isle of Man. Hyundai Car Finance Limited is a subsidiary of United Dominions Trust Limited, which holds 50.01% of the shares. The remaining 49.99% of the shares are held by Hyundai Financial Holdings (UK) Limited which is a wholly owned subsidiary of RAC plc.

All the above companies were incorporated in either England or Scotland.

Companies shown above in italics are associates or joint ventures, and all of the other companies above are subsidiary undertakings.

All companies had a 31 December 2004 year end (with the exception of Lex Transfleet which had a 26 December 2004 year end and which uses 4, 4, 5 week reporting periods rather than monthly calendar periods).

A full list of all the Group's subsidiary undertakings, joint ventures and associates will be filed with the Company's next annual return.

Five year record

	2004 £m	2003 £m	2002 £m	2001 £m	2000 £m
Group turnover	1,189	1,216	1,217	1,175	1,221
Profit before goodwill amortisation, disposal losses, exceptionals and taxation	88.6	86.7	70.2	65.1	54.6
Profit/(loss) on ordinary activities before taxation	77.7	25.7	23.1	62.3	(17.5)
Profit/(loss) on ordinary activities after taxation and minority interests	52.5	9.5	9.7	45.5	(11.0)
Shareholders' funds	428	399	402	412	390
Return on average shareholders' funds (see note below)	12.0%	11.7%	9.1%	8.7%	7.2%
Earnings per ordinary share on profit before goodwill amortisation and exceptional items (see note 10)	55.7p	54.4p	43.9p	41.9p	35.6p
Dividends per ordinary share	25.8p	24.3p	23.0p	22.0p	21.0p

Return on average shareholders' funds is computed as profit after tax for the financial year, after deducting minority interests, before goodwill amortisation, disposal losses net of tax and exceptional items net of tax, expressed as a percentage of the total of average shareholders' funds and goodwill previously written off to reserves.

Shareholder information

Analysis of shareholders of RAC plc

At 31 December 2004 there were 118,798,024 ordinary shares in issue held by 7,839 shareholders (2003 – 7,689 shareholders).

	Number of accounts	Number of ordinary shares	% of shares
Type of shareholder			
Individuals	6,873	5,174,212	4.36
Corporate bodies	966	113,623,812	95.64
	7,839	118,798,024	100.00
Level of shareholding			
1 – 999	6,230	1,737,998	1.46
1,000 – 4,999	1,135	2,138,648	1.80
5,000 – 99,999	349	8,166,530	6.87
100,000 – 249,999	60	9,283,616	7.82
250,000 – 999,999	43	19,919,397	16.77
1,000,000 and over	22	77,551,835	65.28
	7,839	118,798,024	100.00

Substantial shareholders

The following are the only interests of 3% or more in the Company's ordinary share capital at 15 February 2005 of which the Company has been notified:

	Number of ordinary shares	% of ordinary share capital
Barclays PLC	12,997,939	10.99
Legal & General Group plc	3,731,901	3.16
Mourant & Co. Trustees Limited	3,550,000	3.00
Sanford C Bernstein & Co Inc	4,184,168	3.61
Schroders plc	26,262,531	22.11
Silchester International Investors Limited	9,082,377	7.68

Capital gains tax

The market value of the Company's ordinary shares of 25p at 31 March 1982, unadjusted for the 1:10 rights issue in 1983 and the 1:6 rights issue in 1995, was 107.5p.

Financial calendar

Annual General Meeting Thursday 14 April 2005 at 12:00 noon at The Montcalm Hotel, Great Cumberland Place, London W1.

Final ordinary dividend To be paid on 5 May 2005 to shareholders on the register at the close of business on 8 April 2005.

Half year results to 30 June 2005 To be announced on 27 July 2005.

Interim ordinary dividend To be paid on 2 September 2005 to shareholders on the register at the close of business on 5 August 2005.

Other shareholder information

Low-cost share dealing services

Information on a range of low-cost share dealing services is available from the Company Secretary's office on 01628 843817.

Secretary, registered office and company registration particulars

Pamela Coles, RAC plc, 17 Connaught Place, London W2 2EL. Incorporated in England No. 229121.

Shareholder information

For further information about RAC plc, please contact: Investor Relations, RAC plc, RAC House, Boston Drive, Bourne End, Bucks SL8 5YS. Tel: 01628 843823 Fax: 01628 810632 Internet: www.racplc.co.uk E-mail: racplc@rac.co.uk

Registrars & transfer agents

For queries about dividend payments, changes of address or other matters concerning your shareholding, please contact our Registrars: Computershare Investor Services PLC, P.O.Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH.

Tel: 0870 702 0000 Fax: 0870 703 6101. You can also check your shareholding on the following website: www.computershare.com

RAC plc

Motoring services to consumers and businesses

RAC plc
RAC House
Boston Drive
Bourne End
Bucks SL8 5YS
Tel: 01628 843 888
www.racplc.co.uk

RAC Roadside Services

RAC Roadside Services
RAC House
1 Forest Road
Feltham
Middlesex TW13 7RR
Tel: 08000 722 822
www.rac.co.uk

RAC Consumer Services

RAC Auto Windscreens
Britannia House
Storforth Lane
Chesterfield
Derbyshire S40 2UZ
Tel: 0800 919 700
www.racautowindcreens.co.uk

RAC Legal Services
RAC House
Great Park Road
Bradley Stoke
Bristol BS32 4QN
Tel: 08705 533 533
www.rac.co.uk

RAC Financial Services
RAC House
1 Forest Road
Feltham
Middlesex TW13 7RR
Tel: 08000 154 435
www.rac.co.uk

BSM
Suite 3 Merchants Granary
15-17 Cheapside
Wakefield
West Yorkshire WF1 2SD
Tel: 08457 276 276
www.bsm.co.uk

RAC Business Solutions

RAC Business Solutions
Thomas Street
Stretford
Manchester M32 0XH
Tel: 08000 156 638
www.racbusiness.co.uk

RAC Business Solutions
RAC House
1 Forest Road
Feltham
Middlesex TW13 7RR
Tel: 020 8917 2500
www.rac.co.uk/business

Lex Vehicle Leasing

Lex Vehicle Leasing
Globe House
Parkway
Globe Park
Marlow
Bucks SL7 1LY
Tel: 08457 697 381
www.lvl.co.uk

Manufacturer Support Services

Lex Auto Logistics
Pilling Lane
Chorley
Lancs PR7 3EL
Tel: 01257 265 531
www.lexautologistics.com

Hyundai Car (UK)
St John's Court
Easton Street
High Wycombe
Bucks HP11 1JX
Tel: 0800 981 981
www.hyundai-car.co.uk

Lex Transfleet
Lex House
Torwood Close
Westwood Business Park
Coventry CV4 8HX
Tel: 0845 650 2225
www.lextransfleet.co.uk

Lex Defence
13 The Courtyard
Roman Way
Coleshill
Birmingham B46 1HQ
Tel: 01675 430033
www.lexdefence.co.uk

Lex Commercials
St John's Court
Easton Street
High Wycombe
Bucks HP11 1JX
Tel: 01494 428 790
www.lexcommercials.co.uk

RAC Software Solutions
Unit 4 Thornbury Office Park
Midland Way
Thornbury
Bristol BS35 2BS
Tel: 01454 874 002
www.racsoftwaresolutions.co.uk

RAC plc
RAC House
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Bourne End
Bucks SL8 5YS

Tel: (01628) 843888
Fax: (01628) 810613
www.racplc.co.uk
e-mail: racplc@rac.co.uk