

Virgin Rail Group Limited

Directors' report and financial statements

31 March 1997

Registered number 3282548



Directors' report and financial statements

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Directors' report

The directors present their annual report and the audited financial statements for the period from incorporation on 18 November 1996 to 31 March 1997.

Principal activities

The group's principal activity during the period was the operation of passenger rail services in England, Scotland and Wales. The group operates these services under the terms of two franchise agreements between Virgin Rail Group Limited and the director of Passenger Rail Franchising. The agreements expire during the year ending March 2012.

Results for the period

The profit and loss account reflects the results of the two train operating subsidiaries, CrossCountry Trains Limited and West Coast Trains Limited since their acquisition on 5 January 1997 and 9 March 1997 respectively. A loss for the period of £10,159,000 has been taken to reserves, which is after an exceptional charge of £12,383,000 in respect of voluntary severance schemes and staff restructuring.

Business review and future prospects

	Period to 31 March 1997 £000
Turnover	45,912
Operating (loss) before interest and taxation	(10,387)
Interest (net)	228
Loss on ordinary activities before taxation	(10,159)
Tax on loss on ordinary activities	-
Retained loss	(10,159)

The future outlook for Virgin Rail Group Limited is optimistic, with a number of new and exciting initiatives already underway or planned for the short to medium term.

A dedicated reservation centre (Virgin TrainLine) has already been implemented and has been fully operational since 1 May 1997, enabling customers to book in advance of travel and reserve a seat. A new product strategy has been developed which will be progressively introduced during summer 1998 onwards.

Arrangements are well advanced for new customer care teams already in place at London Euston and Manchester Piccadilly to be introduced at other stations. A major programme of station investment is planned to include provision of Virgin lounges, and Virgin Information Points giving passengers access to "real time" information.

Current reliability is in excess of 99% and punctuality is at a level which is in excess of the comparable period last year. The group is putting in place the actions necessary to secure the improvements in performance required by its franchise commitments.

The Group has a major refurbishment programme underway on its existing fleet, a quarter of the rolling stock fleet already having been refurbished. The Group is also committed under its Franchise Plans to replace these with a new fleet and plans to introduce 55 ultra modern active tilting trains on the West Coast Mainline in 2001, alongside a revamped diesel service on CrossCountry routes. These new trains, combined with planned infrastructure improvements, should result in significantly shorter journey times and increased frequency of services.

An agreement in principle with Railtrack has been reached, designed to provide additional capacity and speed benefits, which is currently with the Rail Regulator for approval.

Directors' report *(continued)*

Proposed dividend

The directors do not recommend the payment of a dividend.

Significant changes in fixed assets

The only significant changes in fixed assets arose on the acquisition of the two passenger rail franchises.

Directors and directors' interests

The directors who held office during the period were as follows:

	Date appointed	Date resigned
Stephen Murphy (Chairman)	18 November 1996	
William Whitehorn	18 November 1996	
Richard Branson	18 November 1996	9 March 1997
Brian Barrett	9 March 1997	
Pierre Dupont	9 March 1997	
Jeremy Ferris	9 March 1997	
Manjit Dale*	9 March 1997	23 May 1997

Since the period end there have been the following changes in directors:

	Date appointed
Randl Shure*	23 May 1997
Alan Tomlin	10 June 1997
Chris Tibbits	10 June 1997
Ivor Warburton	10 June 1997

* Having resigned on 23 May 1997, Manjit Dale was appointed as an alternative director to Randl Shure.

Richard Branson was appointed president of the company on 9 March 1997.

At the end of the period the following directors held interests in options over non-voting ordinary shares of 10p each in the company:

	Options
Stephen Murphy	303,945
William Whitehorn	303,945
Brian Barrett	303,945
Alan Tomlin	101,315

All of the above options were granted on 20 March 1997 with an exercise price of £1.20 per share. Each individual has the opportunity to exercise options once in any year from three years since they were granted, or on the date of a listing on the London Stock Exchange (see note 21) if earlier, until the options' expiry seven years after they were granted. No specific performance criteria apply to the exercising of options.

Otherwise none of the directors had any interest in the share capital of the company either during the period or at the end of the period.

Directors' report (continued)

Employees

The group is a non-discriminatory employer operating an Equal Opportunities Policy which aims to guard against unfair discrimination, harassment, victimisation and bullying. The group is committed to ensuring that all individuals are treated fairly, with respect and are valued irrespective of disability, race, gender, health, social class, sexual preference, marital status, nationality, religion, employment status, age or membership or non-membership of a trade union.

The group uses the consultative procedures agreed with its staff and elected representatives with a view to ensuring that its people are aware of the financial and economic factors which affect the group's performance and prospects.

The group's policy, where possible, is to continue to employ those who may become disabled in service, together with ensuring our recruitment practice does not discriminate against disabled people. Training is adjusted to cater for an individual disability and the disabled share the same conditions of service as other staff in relation to career development and promotion.

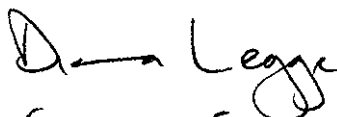
Political and charitable contributions

The group made no donations to charities or to political parties.

Auditors

In accordance with Section 385 of the Companies Act 1985, a resolution for the appointment of KPMG as auditors of the company is to be proposed at the forthcoming Annual General Meeting.

By order of the board


COMPANY SECRETARY

29 January 1998

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year or period 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;
- 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 the group and to 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.

The directors, having prepared the financial statements, note that the auditors are required by the Companies Act 1985 to take whatever steps and undertake whatever inspections they consider to be appropriate for the purposes of enabling them to give their audit report.



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London EC4Y 8BB

Report of the auditors to the members of Virgin Rail Group Limited

We have audited the financial statements on pages 6 to 32.

Respective responsibilities of directors and auditors

As described on page 4 the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of 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. 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 are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and the group as at 31 March 1997 and of the loss of the group for the period then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG
Chartered Accountants
Registered Auditors

29 January 1998

Consolidated profit and loss account

for the period from 18 November 1996 to 31 March 1997

		Period 18 November 1996 to 31 March 1997		
	Note	Before exceptional items £000	Exceptional item (note 9) £000	Total £000
Turnover	2	45,912	-	45,912
Other operating income	3	36,614	-	36,614
Train operating expenditure	4	(66,853)	-	(66,853)
Staff costs	5	(8,642)	(12,383)	(21,025)
Depreciation	6	(13)	-	(13)
Other operating charges		(5,022)	-	(5,022)
Operating profit/(loss)		1,996	(12,383)	(10,387)
Other interest receivable and similar income	9			467
Interest payable and similar charges	10			(239)
Loss on ordinary activities before taxation	6			(10,159)
Tax on loss on ordinary activities	11			-
Retained loss on ordinary activities after taxation for the period	22			(10,159)

There were no gains or losses other than the loss for the period.

There were no differences between the profit and loss account shown above and that prepared on a historical cost basis. The whole of the results relate to acquisitions and continuing operations.

Consolidated balance sheet
 at 31 March 1997

	Note	31 March 1997 £000
Fixed assets		
Tangible assets	12	286
Intangible assets - negative goodwill	13	(14,089)
Current assets		
Stocks	15	2,618
Debtors	16	74,748
Cash at bank and in hand	17	84,395
Creditors: amounts falling due within one year	18	161,761 (75,076)
Net current assets		
Due within one year		55,885
Debtors due after more than one year		30,800
Total net current assets		86,685
Total assets less current liabilities		72,882
Creditors: amounts falling due after more than one year	19	(25,051)
Provisions for liabilities and charges	20	(22,940)
Net assets		24,891
Capital and reserves		
Called up share capital	21	3,500
Share premium account	22	31,550
Profit and loss account	22	(10,159)
Equity shareholders' funds		24,891

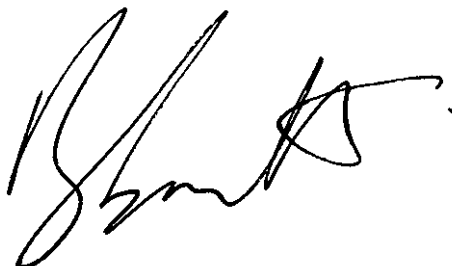
These financial statements were approved by the board of directors on 29TH JANUARY 1998 and were signed on its behalf by:

Company balance sheet

at 31 March 1997

	Note	31 March 1997 £000
Fixed assets		
Tangible assets	12	3
Investments	14	4,197
		<hr/>
		4,200
Current assets		
Debtors	16	30,227
Cash at bank and in hand		30,062
		<hr/>
		60,289
Creditors: amounts falling due within one year	18	(5,048)
		<hr/>
Net current assets		55,241
		<hr/>
Total assets less current liabilities		59,441
		<hr/>
Creditors: amounts falling due after more than one year	19	(25,000)
		<hr/>
Net assets		34,441
		<hr/>
Capital and reserves		
Called up share capital	21	3,500
Share premium reserve	22	31,550
Profit and loss account	22	(609)
		<hr/>
Equity shareholders' funds		34,441
		<hr/>

These financial statements were approved by the board of directors on 29th JANUARY 1998 and were signed on its behalf by:

Reconciliations of movements in shareholders' funds
for the period from 18 November 1996 to 31 March 1997

	Period 18 November 1996 to 31 March 1997	
	Group £000	Company £000
Loss for the financial period	(10,159)	(609)
New share capital subscribed	3,500	3,500
Share premium arising on new share capital	31,550	31,550
Net addition to shareholders' funds	24,891	34,441
Opening shareholders' funds	-	-
Closing shareholders' funds	24,891	34,441

Consolidated cash flow statement

for the period from 18 November 1996 to 31 March 1997

	<i>Note</i>	Period to 31 March 1997 £000
Net cash inflow from operating activities	26	25,606
Return on investments and servicing of finance	27	119
Capital expenditure and financial investment	27	27
Acquisitions and disposals	27	(1,407)
Management of liquid resources	27	(30,000)
Net cash outflow before financing		(5,655)
Financing	27	60,050
Increase in cash	28	54,395

Notes

(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the group's financial statements.

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules.

Basis of consolidation

The group accounts consolidate the accounts of Virgin Rail Group Limited and all of its subsidiary undertakings. These accounts are made up to 31 March 1997.

The consolidated accounts are based on accounts of subsidiary undertakings, all of which are coterminous with those of the parent company, and on the accounts of the parent company.

The acquisition method of accounting has been adopted. Under this method, the results of subsidiary and associated undertakings acquired in the period are included in the consolidated profit and loss account from the date of acquisition. Goodwill has been determined by subtracting the fair value of net assets acquired from the cash consideration and associated costs of acquisition in respect of each acquisition. The resulting negative goodwill is reduced by the extent of any impairment of the fair values of net assets acquired.

Negative goodwill up to the fair values of non-monetary assets acquired is amortised to the profit and loss account in the periods in which the non-monetary assets are recovered, whether through depreciation, amortisation or sale, but not exceeding the franchise period associated with each acquisition.

The amount of the loss for the financial period dealt with in the financial statements of Virgin Rail Group Limited is disclosed in note 22 to these financial statements. The company has taken advantage of Section 230(4) of the Companies Act 1985 and has not presented its own profit and loss account.

Turnover

Turnover represents the net amount receivable, excluding VAT, for services and goods supplied to external customers.

Passenger revenue represents principally amounts attributed to the group by the Railway Settlement Plan. Income is attributed based on models of certain aspects of passenger behaviour and to a lesser extent from allocations agreed for specific revenue flows. The attributed share of season ticket income is deferred within creditors and released to the profit and loss account over the life of the relevant season ticket.

Fixed assets and depreciation

Depreciation is provided on a straight line basis over the estimated useful economic lives of the assets commences from the date on which the assets are brought into use. The lives used for the major categories of assets are:

Freehold buildings	-	30-40 years
Computer equipment	-	3 years
Plant	-	20 years

Notes (continued)

Accounting policies (continued)

Leases

Where the group enters into a lease which entails taking substantially all the risks and rewards of ownership of an asset, the lease is treated as a 'finance lease'. The asset is recorded in the balance sheet as a tangible fixed asset and is depreciated over its estimated useful life or the term of the lease, whichever is shorter. Future instalments under such leases, net of finance charges, are included within creditors. Rentals payable are apportioned between the finance element, which is charged to the profit and loss account, and the capital element which reduces the outstanding obligation for future instalments.

All other leases are accounted for as 'operating leases' and the rental charges are charged to the profit and loss account on a straight line basis over the life of the lease. Specified rolling stock maintenance is included within the non-capital element of the rolling stock operating lease payments.

Government grants

Revenue based government grants are credited to the profit and loss account so as to match them with the expenditure towards which they are intended to contribute.

Stocks

Stocks are stated at the lower of cost and net realisable value. Raw materials include amounts incurred in respect of the rights to utilise stocks of replaceable spares.

Pensions and other post-retirement benefits

The group companies participate in sections of a pension scheme which provides benefits on a defined benefit basis. The assets of the scheme are held separately from those of the group in an independently administered fund. Contributions to the scheme are charged to the profit and loss account so as to spread the cost of pensions over employees' working lives within the group.

Details of the pension scheme are provided in note 25.

Deferred taxation

Deferred tax, using the liability method, is provided at the rates of corporation tax which are expected to apply when the additional tax is estimated to be payable, except those which it is considered will continue for the foreseeable future.

Notes (continued)

Accounting policies (continued)

2 Turnover

Turnover originates in the United Kingdom.

The directors consider that the whole of the activities of the group constitute a single class of business.

Turnover comprises:

	Period to 31 March 1997 £000
Passenger revenue and catering income	42,963
Other trading income	2,949
	<hr/> 45,912 <hr/>

Other trading income consists principally of the provision of light maintenance services and station facilities to other train operators, the hire of train crew and rolling stock.

3 Other operating income

Other operating income comprises:

	Period to 31 March 1997 £000
Revenue grant	36,506
Property income	108
	<hr/> 36,614 <hr/>

Notes (continued)

4 Train operating expenditure

Train operating expenditure comprises:

Period to
31 March
1997
£000

Raw materials and consumables	4,347
Hire of train crew and rolling stock, station, track and depot access charges and vehicle maintenance	62,506
	<hr/> 66,853 <hr/>

5 Staff numbers and costs

Staff numbers and costs comprise:

Period to
31 March
1997
£000

Wages and salaries	7,495
Social security costs	619
Other pension costs	196
Other staff costs	12,715
	<hr/> 21,025 <hr/>

The average number of persons employed by the group during the period were:

Average number
of employees
during the period

Management	507
Other staff	3,672
	<hr/> 4,179 <hr/>

Notes (continued)

6 Loss on ordinary activities before taxation

	Period to 31 March 1997 £000
<i>Loss on ordinary activities before taxation is stated after charging/(crediting)</i>	
Auditors' remuneration:	
Audit - group	100
- parent	25
Other services	50
Depreciation	13
Hire of plant and machinery - rentals payable under operating leases	14,078
Other operating leases	731
Hire of plant and machinery - finance charges under finance leases	2
Rental income received on properties	(108)

The cost of acquiring the franchises (see note 14) includes fees payable to the auditors of £365,000.

7 Remuneration of directors

	Period to 31 March 1997 £000
Aggregate emoluments of directors	2
Number of directors eligible for shares under a long term incentive scheme	3

Directors interests in the ordinary share capital of the company and options granted during the period are disclosed in the Director's report.

None of the non-executive directors received fees during the period. Certain of the shareholders and other related parties received fees totalling £4,728 for providing the services of non-executive directors.

Notes (continued)

8 Exceptional items

The following exceptional item has been included in arriving at operating loss.

	Period to 31 March 1997 £000
Staff costs:	
Costs of voluntary severance schemes and staff restructuring	12,383
	<u>12,383</u>

9 Other interest receivable and similar income

	Period to 31 March 1997 £000
Bank interest	178
Other interest	289
	<u>467</u>

10 Interest payable and similar charges

	Period to 31 March 1997 £000
Amounts payable on other loans	239
	<u>239</u>

11 Taxation

No taxation is payable in respect of the period due to the availability of tax losses within the group.

Notes (continued)

12 Tangible fixed assets

	Plant and equipment £000
Group	
<i>Cost</i>	
Acquisition of subsidiaries	326
Additions	3
Disposals	(30)
	<hr/>
At 31 March 1997	299
	<hr/>
<i>Depreciation</i>	
Charge for period	13
	<hr/>
At 31 March 1997	13
	<hr/>
<i>Net book value</i>	
At 31 March 1997	286
	<hr/> <hr/>

Included in the net book value of plant and equipment is £4,000 in respect of assets held under hire purchase and finance leases. Depreciation charged in the period amounted to £nil.

	Plant and equipment £000	Total £000
Company		
<i>Cost</i>		
Additions	3	3
	<hr/>	<hr/>
At 31 March 1997	3	3
	<hr/>	<hr/>
<i>Net book value</i>		
At 31 March 1997	3	3
	<hr/> <hr/>	<hr/> <hr/>

Notes (continued)

13 Negative goodwill

	£000
Negative goodwill on acquisition of:	
- CrossCountry Trains Limited	(4,105)
- Intercity West Coast Limited	(10,082)
	<hr/>
Gross negative goodwill at 31 March 1997	(14,187)
Provision for amortisation of negative goodwill	
- provided during the period	98
	<hr/>
Provision for amortisation of negative goodwill at 31 March 1997	98
Net book value of negative goodwill at 31 March 1997	(14,089)
	<hr/> <hr/>

14 Fixed asset investments - company

	Cost of shares in subsidiaries £000
Company	
Additions at cost	4,197
	<hr/> <hr/>
At 31 March 1997	4,197
	<hr/> <hr/>

On 5 January 1997 the company acquired all of the £1 Ordinary shares of CrossCountry Trains Limited, a company registered in England and Wales operating passenger rail services, pursuant to a 15 year franchise agreement granted by the Office of Passenger Rail Franchising ("OPRAF") for a cash consideration of £1,004,971. Acquisition costs incurred in the period to 31 March 1997 totalled £139,681. The estimated fair value of the net assets acquired was £5,250,000 (see table below). The resulting negative goodwill of £4,105,000 has been recognised under intangible assets.

Notes (continued)

14 Fixed asset investments - company (continued)

Acquisition of CrossCountry Trains Limited

	Book value £000	Fair value adjustments £000	Fair value to the group £000
Fixed assets			
Tangible	104	-	104
Current assets			
Stock	113	-	113
Debtors	22,381	7,300	29,681
Cash	1,884	-	1,884
Total assets	24,482	7,300	31,782
Liabilities			
Deferred season ticket	(298)	-	(298)
Trade creditors	(22,049)	-	(22,049)
Other creditors	(1,260)	-	(1,260)
Other tax and social security creditor	(735)	-	(735)
Deferred tax	-	(2,190)	(2,190)
Total liabilities	(24,342)	(2,190)	(26,532)
Net assets	140	5,110	5,250
Negative goodwill arising on acquisition			(4,105)
			1,145
Discharged by:			
Cash consideration			1,005
Costs associated with the acquisition			140
			1,145

Fair value adjustments represent a pension fund surplus at acquisition (see note 25) and the related deferred tax liability.

Notes (continued)

14 Fixed asset investments - company (continued)

The results of the subsidiary are included in these financial statements under the acquisition method.

Included in the group loss for the period is a net loss after tax of £935,000 relating to the period since acquisition. CrossCountry Trains Limited made a net loss after tax of £3,452,000 for the period from when it commenced trading on 12 November 1995 to 31 March 1996. CrossCountry Trains Limited made a profit of £7,843,000 from 1 April 1996 to the date of acquisition.

On 9 March 1997 the company acquired all of the £1 Ordinary shares of Intercity West Coast Limited, a company registered in England and Wales operating passenger rail services, pursuant to a 15 year franchise agreement granted by OPRAF for a cash consideration of £2,617,001. Acquisition costs incurred at 31 March 1997 totalled £435,173. The estimated fair value of the net assets acquired was £13,134,000 (see table below). The resulting negative goodwill of £10,082,000 has been recognised under intangible assets. The company changed its name on 10 March 1997 to West Coast Trains Limited.

Notes (continued)

14 Fixed asset investments (continued)

Acquisition of West Coast Trains Limited

	Book value	Fair value adjustments	Fair value to the group
	£000	£000	£000
Fixed assets			
Tangible	222	-	222
Current assets			
Stock	2,742	-	2,742
Debtors	34,045	23,500	57,545
Cash	3,097	-	3,097
Total assets	40,106	23,500	63,606
Liabilities			
Bank loans and overdrafts	(6,388)	-	(6,388)
Deferred season tickets	(1,313)	-	(1,313)
Trade creditors	(27,347)	-	(27,347)
Other creditors	(3,431)	-	(3,431)
Accruals	(140)	-	(140)
Other tax and social security	(3,111)	-	(3,111)
Finance leases due in less than one year	(41)	-	(41)
Finance leases due in more than one year	(51)	-	(51)
Deferred tax	-	(7,050)	(7,050)
Provisions	-	(1,600)	(1,600)
Total liabilities	(41,822)	(8,650)	(50,472)
Net (liabilities)/assets	(1,716)	14,850	13,134
Negative goodwill arising on acquisition			(10,082)
			3,052
Discharged by:			
Cash consideration			2,617
Costs associated with acquisition			435
			3,052

The principal fair value adjustments represents a pension fund surplus at acquisition (see note 25) and the related deferred tax liability.

Notes (continued)

14 Fixed asset investments (continued)

The results of the subsidiary are included in these financial statements under the acquisition method.

Included in the group net loss after tax for the period is a net loss after tax of £9,778,000 relating to the period since acquisition. West Coast Trains Limited made a profit of £5,860,000 for the period from when it commenced trading on 30 April 1995 to 31 March 1996. West Coast Trains Limited made a loss of £1,403,000 from 1 April 1996 to the date of acquisition.

15 Stocks

	Group 31 March 1997 £000
Raw materials and consumables	2,618

16 Debtors

	Group 31 March 1997 £000	Company 31 March 1997 £000
Amounts falling due within one year		
Trade debtors	27,826	-
Amounts owed by subsidiary undertakings	-	118
Other debtors	13,458	109
Prepayments and accrued income	2,664	-
	<hr/> 43,948	<hr/> 227
Amounts falling due after more than one year		
Prepayments and accrued income	30,800	-
Amounts owed by subsidiary undertakings	-	30,000
	<hr/> 74,748	<hr/> 30,227

Prepayments falling due after more than one year represent the pension surpluses recognised as fair value adjustments on the acquisition of West Coast Trains Limited and CrossCountry Trains Limited (see note 14 and 25).

Amounts owed after more than one year by subsidiary undertakings to Virgin Rail Group Limited represent subordinated loans of £21 million to West Coast Trains Limited and £9 million to CrossCountry Trains Limited made according to the terms of the Franchise Agreements for the length of the franchise terms.

17 Cash at bank and in hand

At 31 March 1997, the balance of £84,395,000 included £30 million held on deposit. This is required as security for the performance bonds (see note 24).

Notes (continued)

18 Creditors: amounts falling due within one year

	Group 31 March 1997 £000	Company 31 March 1997 £000
Obligations under finance leases	41	-
Trade creditors	59,028	94
Other taxes and social security costs	3,509	-
Other creditors	5,013	45
Deferred consideration payable to franchise vendors	4,197	4,197
	<hr/>	<hr/>
	71,788	4,336
Accruals and other deferred income	1,800	712
Deferred season ticket income	1,488	-
	<hr/>	<hr/>
	75,076	5,048
	<hr/> <hr/>	<hr/> <hr/>

19 Creditors: amounts falling due after more than one year

	Group 31 March 1997 £000	Company 31 March 1997 £000
Other loans	25,000	25,000
Obligations under finance leases	51	-
	<hr/>	<hr/>
	25,051	25,000
	<hr/> <hr/>	<hr/> <hr/>

Under the terms of a loan instrument dated 7 March 1997, the company issued £25,000,000 of unsecured loan stock. Interest of 15% per annum is payable in arrears on 30 September 1997 for the period from 7 March 1997 to 30 September 1997 and thereafter quarterly. The company may redeem all or any part of the stock at any time up to 7 March 2003, at which date all outstanding loan stock shall be redeemed.

Notes (continued)

19 Creditors: amounts falling due after more than one year (continued)

The maturity of obligations under finance leases and hire purchase contracts, net of finance charges, is as follows:

	Group 31 March 1997 £000
Within one year	41
In the second to fifth years	51
Over five years	-
	<hr/> 92 <hr/>

20 Provisions for liabilities and charges

	Group deferred tax £000	Group Other provisions £000	Group Total £000
Arising on acquisition of subsidiaries	9,240	1,600	10,840
Provided during period	-	12,100	12,100
	<hr/> 9,240	<hr/> 13,700	<hr/> 22,940 <hr/>
At end of period	<hr/> 9,240 <hr/>	<hr/> 13,700 <hr/>	<hr/> 22,940 <hr/>

The deferred tax balance arises from the pension scheme surplus arising on acquisition of the group's subsidiaries during the period. The liability has been calculated at a rate of 30% and fully provided for.

Provisions provided during the period relate to redundancies and related restructuring costs.

Notes (continued)

21 Called up share capital

	Number of shares 31 March 1997 Number	Group and company 31 March 1997 £000
<i>Authorised</i>		
'A' ordinary shares of 10p	14,500,000	1,450
'B' ordinary shares of 10p	10,000,000	1,000
Non-voting ordinary shares of 10p	37,526,300	3,753
	<hr/>	<hr/>
	62,026,300	6,203
	<hr/>	<hr/>
<i>Allotted, called up and fully paid</i>		
'A' ordinary shares of 10p	14,500,000	1,450
'B' ordinary shares of 10p	10,000,000	1,000
Non-voting ordinary shares of 10p	10,500,000	1,050
	<hr/>	<hr/>
	35,000,000	3,500
	<hr/>	<hr/>

6,166,667 of the 'A', and all of the 'B' and non-voting shares were subscribed for at a price of £1 per share. 8,333,333 'A' shares were subscribed for at a price of £1.006 per share.

The 'A', 'B' and non-voting ordinary shares rank *pari passu* as regards dividends and other distributions. No dividend or distribution may be declared whilst any amounts are outstanding in respect of the loan stock (see note 19). The 'A' and 'B' shares have equal voting rights per share.

Under the terms of the Virgin Rail Group Share Option Scheme dated 20 March 1997, options have been granted to some directors and senior employees of Virgin Rail Group Limited over 1,114,465 non-voting ordinary shares at an exercise price of £1.20.

Warrants

Under the terms of a warrant instrument dated 7 March 1997, up to 25,000,000 warrants may be issued in respect of the non-voting ordinary shares. At 31 March 1997, 3,500,000 warrants have been issued and under the formula for determining the subscription price when exercised, the maximum subscription value of the shares issued to the warrant holders would be £3,500,000 in aggregate.

The warrant holders may exercise their right to subscribe for shares immediately prior to a listing or under certain circumstances, at any time before a listing. Exercise rights lapse immediately after a listing.

The number of shares to which a warrant holder may subscribe is determined by the date on which subscription rights are exercised as follows. If subscription rights are exercised within one year of the warrant issue date (7 March 1997), each £1 of subscription value entitles the warrant holder to one new share; if subscription rights are exercised between 8 March 1998 and 7 September 1999, each £1 of subscription value entitles the warrant holder to two and a half new shares; if subscription rights are exercised after 7 September 1999, each £1 of subscription value entitles the warrant holder to between two and a half and ten and a half new shares, depending on the amount of unsecured loan stock outstanding.

Notes (continued)

22 Reserves

Group

	Share premium account 31 March 1997 £000	Profit and loss account 31 March 1997 £000
At incorporation	-	-
Shares issued during the period	31,550	-
Retained loss for period	-	(10,159)
Arising on acquisition	-	-
	<hr/>	<hr/>
	31,550	(10,159)
	<hr/> <hr/>	<hr/> <hr/>

Company

	Share premium account 31 March 1997 £000	Profit and loss account 31 March 1997 £000
At incorporation	-	-
Shares issued during the period	31,550	-
Retained loss for period	-	(609)
	<hr/>	<hr/>
	31,550	(609)
	<hr/> <hr/>	<hr/> <hr/>

Notes (continued)

23 Commitments

- (a) The company has made certain commitments to OPRAF under the terms of the Franchise Plans and Agreements in relation to future investments in rolling stock. At 31 March 1997 these had not resulted in any contracted capital commitments to any third parties.
- (b) Annual commitments under non-cancellable operating leases are as follows:

	31 March 1997	
	Land and buildings	Other
Group	£000	£000
Operating leases which expire:		
Within one year	-	4,849
In the second to fifth years inclusive	395	57,495
Over five years	10,226	29,941
	<hr/>	<hr/>
	10,621	92,285
	<hr/>	<hr/>

The company did not have any commitments under non-cancellable operating leases.

- (c) The group has, in the normal course of business, entered into a number of long term supply contracts. The most significant of these relate to track, station and depot access facilities.
- (d) Under the Franchise Agreements, the group has agreed with OPRAF annual amounts receivable or payable in respect of the operation of the franchises for future periods. These amounts progressively change from an amount of £189.7 million receivable for the year ending 31 March 1998 to an amount of £230.3 million, subject to indexation, payable for the year ending 31 March 2012. Amounts become payable from the year ending 31 March 2004.

24 Contingent liabilities

Guarantees

In accordance with the Franchise Agreements the company procured performance bonds in favour of OPRAF for both West Coast Trains Limited and CrossCountry Trains Limited. The bonds have been issued by Lloyds Bank up to £21 million for West Coast Trains Limited and up to £9 million for Cross Country Trains Limited.

Under a separate agreement, the company has lodged £30 million with Lloyds Bank as security.

Notes (continued)

24 Contingent liabilities (continued)

Season ticket bond

The season ticket bond issued by West Coast Trains Limited in favour of OPRAF secures the refund of current season tickets in the event of:

- the termination of the Franchise Agreement;
- the making of a railway administration order;
- or the occurrence of an event or default.

The value of the season ticket bond for 1997/98 is up to £1.52 million.

25 Pension scheme

Prior to their acquisition by Virgin Rail Group Limited, West Coast Trains Limited and CrossCountry Trains Limited were participating employers in the British Rail shared cost section of the Railways Pension Scheme ('RPS'). Since their acquisition the subsidiaries have participated in their own separate shared costs sections of the RPS. The RPS is a funded scheme and provides benefits based on final average pensionable pay. The assets of the RPS are held separately from those of the company and its subsidiaries.

The pension charge for the period was £196,000.

The first actuarial valuation of the subsidiaries' sections of the RPS will be undertaken with an effective date of 1 April 1999. In advance of this, the company requested an independent actuarial review to be undertaken as at 31 March 1997 in order to estimate the initial value of the surpluses within each section and the pension costs for the period in accordance with SSAP 24. The actuarial method used for these calculations was the projected unit method. The principal assumptions made were investment returns of 9.0% per annum, general salary increases (excluding promotional scale) of 6.5% per annum and present and future pensions growth of 4.5% per annum.

The estimated market value of assets of the pension scheme at the individual dates of acquisition of the subsidiaries was £149.7 million for the West Coast Trains Limited section and £39.6 million for CrossCountry Trains Limited section. The actuarial value of assets as a percentage of accrued benefits at date of acquisition (after allowing for expected future increases to earnings) was 142% and 138% for each section respectively. Pension scheme surpluses totalling £30,800,000 have been recognised in the individual acquisition balance sheets of the subsidiaries (note 14). There has been no significant amortisation of the prepayment during the period to 31 March 1997.

Notes (continued)

26 Reconciliation of operating loss to net cash inflow from operating activities

	Period 18 November 1996 to 31 March 1997 £000
Operating loss	(10,387)
Depreciation charge	13
Amortisation of negative goodwill	(98)
Decrease in stocks	237
Decrease in debtors	12,689
Increase in creditors	11,052
Increase in provisions	12,100
	<hr/>
Net cash inflow from operating activities	25,606
	<hr/> <hr/>

Notes (continued)

27 Analysis of cash flows for headings netted in the cash flow statement

		Period 18 November 1996 to 31 March 1997 £000
Returns on investment and servicing of finance	£000	£000
Interest received	358	
Interest paid	(239)	
	<hr/>	
Net cash inflow for returns on investments and servicing of finance		119
		<hr/>
Capital expenditure and financial investment		
Purchase of tangible fixed assets	(3)	
Sale of tangible fixed assets	30	
	<hr/>	
Net cash inflow for capital expenditure and financial investments		27
		<hr/>
Acquisitions and disposals		
Net cash acquired with subsidiaries	(1,407)	
	<hr/>	
Net cash outflow for acquisitions and disposals		(1,407)
		<hr/>
Management of liquid resources		
Deposits placed on security for performance bonds	(30,000)	
	<hr/>	
Net cash outflow for management of liquid resources		(30,000)
		<hr/>
Financing		
Issue of ordinary share capital	35,050	
Loans due after more than one year	25,000	
	<hr/>	
Net cash inflow from financing		60,050
		<hr/>

Notes (continued)

28 Analysis of net funds

	At incorporation	Cash flow	Acquisition	At 31 March 1997
	£000	£000	£000	£000
Cash at bank	-	49,414	4,981	54,395
Deposits placed as security for performance bonds	-	30,000	-	30,000
Overdraft	-	79,414	4,981	84,395
	-	6,388	(6,388)	-
Debt due after one year	-	85,802	(1,407)	84,395
Finance leases	-	(25,000)	-	(25,000)
	-	-	(92)	(92)
Total	-	60,802	(1,499)	59,303

1997
£000

Reconciliation of net cash flow to movement in funds

Increase in cash in the period	54,395
Cash outflow from increase in liquid resources	30,000
Change in debt resulting from cash flows	84,395
Finance leases acquired with subsidiaries	(25,000)
	(92)
Movement in net funds in period	59,303
Net debt at incorporation	-
Net funds at 31 March 1997	59,303

Notes (continued)

29 Related party transactions

At 31 March 1997 certain of the company's shareholders were trusts, or companies owned by the trusts (together the trust shareholders), the principal beneficiaries of which were RCN Branson and his immediate family. None of these trust shareholders individually has a controlling interest in the company. The trust shareholders have interests directly and indirectly in certain other companies which are considered to give rise to related party disclosures under Financial Reporting Standard No.8

During the period, certain of the trust shareholders provided Virgin Rail Group Limited with loans of £9,063,000 for the purposes of financing CrossCountry Trains Limited's performance bond. No interest was payable on these loans, which were satisfied on 9 March 1997 through the issue of fully paid shares and Loan Stock to the relevant trust shareholders. Set up and administrative costs and royalties payable on licences for use of the Virgin name incurred on behalf of and recharged to Virgin Rail Group Limited by Virgin Management Limited were £209,485. Included in other creditors is an amount of £44,699 owing to Virgin Management Limited relating to the provision of company secretarial and tax services. A further £2,364 was payable to Virgin Management Limited for providing the services of two non-executive directors, Stephen Murphy and William Whitehorn and of Mr Branson as President.

Under the terms of a Loan Instrument dated 7 March 1997, the company issued £25,000,000 of unsecured loan stock. Interest of 15% per annum is payable in arrears on 30 September 1997, for the period to 30 September 1997 and thereafter quarterly. £236,774 interest was accrued during the period in respect of this loan. Related party shareholders' interests in this loan are set out below:

	£
Trust shareholders (see above)	5,000,000
Bankers Trust International Plc	4,875,000
JP Morgan Int'l Capital Corporation	4,750,000
TPG Partners LP and TPG Parallel I, LP	5,500,000
	<hr/>
	20,125,000
	<hr/>

30 Ultimate parent company and parent undertaking of larger group

The company has no parent undertaking and therefore its results are not consolidated in the accounts of any other entity.