

# Enterprise Inns plc



Annual Report and Accounts 2006

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Here is a selection of award-winning Enterprise licensees who were recognised during the year for the quality of their businesses and their outstanding entrepreneurial skills:



**THE PACK HORSE, HAYFIELD, DERBYSHIRE**  
**WINNER – Best Pub 2006** Northern Hospitality Awards  
**REGIONAL WINNER – Gastro Pub of the Year 2006**  
 Morning Advertiser Pub Awards

The Pack Horse was taken over by Suzy Turner and Andy Williams in 2003. After careful research and a major investment, the pub is now recognised and respected throughout the region for the quality of its food offer.

Front cover pictures (left to right)

- World's End, Ecton
- World's End, Ecton
- Plough, Harborne

## The Enterprise Inns Board



**Left to right:** Hubert Reid, Chairman  
 David George, Chief Financial Officer  
 Susan Murray, Non-executive director  
 Ted Tuppen, Chief Executive  
 David Harding, Non-executive director  
 Simon Townsend, Chief Operating Officer  
 Jo Stewart, Non-executive director



**OLD WHITE BEARE, NORWOOD GREEN, WEST YORKSHIRE**  
**WINNER – Village Pub of the Year 2006** Morning Advertiser  
 Pub Awards

Since taking over this pub last summer, Chris and Nick Green have restored a neglected sixteenth Century pub to its former glory with a major refurbishment. Following the introduction of new staff and a successful PR campaign, the pub now attracts destination diners whilst remaining at the heart of the village.



**MASTER ROBERT INN, BURITON**  
**WINNER – Rural pub of the Year 2006** Calor Gas

Pauline Davey and her partner Tim Smith took over the Master Robert Inn in January 2005 and, working with the "Pub is the Hub" campaign, have added to the business by transforming the function room into a much valued post office and shop.

# Financial Highlights

	2006	2005	Increase
<b>EBITDA*</b>	<b>£547m</b>	£528m	3.6%
<b>Profit before tax and exceptional items</b>	<b>£315m</b>	£290m	8.6%
<b>Earnings per share</b>	<b>100.9p</b>	61.0p	65.4%
<b>Adjusted earnings per share†</b>	<b>68.3p</b>	58.4p	17.0%
<b>Dividends</b>	<b>27.0p</b>	18.0p	50.0%

\* Earnings before interest, tax, depreciation, amortisation and exceptional items.

† Excludes exceptional items.

- Average EBITDA per pub has increased by 5.2% to £64,200.
- The quality of the pub estate has been improved through the acquisition and disposal of pubs and capital expenditure of £54 million.
- At 30 September 2006 the estate comprised 7,809 pubs valued at £5.4 billion.
- Cash generated after interest, tax, dividends and capital expenditure amounted to £107 million.
- At 30 September 2006 underlying net debt was £3,166 million, an increase of £45 million on the prior year.
- A total of 42.3 million shares have been repurchased for consideration of £393 million (excluding costs).

# Chairman's Statement

I am delighted to report on our results for the year to 30 September 2006 in which we have delivered a strong financial performance through profit growth and a rolling share buy-back programme.

EBITDA before exceptional items increased by 3.6% over the prior year to £547m and profit before tax and exceptional items rose by 8.6% to £315 million. Adjusted earnings per share increased by 17.0% to 68.3 pence. For the second consecutive year, the Board is recommending a 50% increase in the rate of dividend paid to shareholders, giving a total for the year of 27.0 pence per share. Dividend cover based on adjusted earnings per share is 2.5 times, in line with the policy described a year ago. The final dividend of 18.0 pence per share will be payable on 22 January 2007 to shareholders on the register on 29 December 2006.

Last year we announced our intention to commence a rolling share buy-back programme to return surplus cash to shareholders and to ensure that the balance sheet remains efficient. Market purchases totalling 42.3 million of our ordinary shares were made for an aggregate consideration of £393 million (excluding costs) which, together with £70 million of dividends paid, resulted in a total of £463 million being returned to shareholders in the year. In the absence of material pub acquisitions and subject to overall market conditions and shareholder approval, we expect that at least this level of returns will be made in the year to 30 September 2007. Indeed, since the year end we have purchased a further 6.0 million shares at a cost of £65 million.

Shareholders will be aware from the interim statement that Gordon Harrison, Operations Director had decided to retire from the business at the end of September this year. The Board, in reiterating its thanks for his tremendous contribution, wishes to record in this Annual Report its appreciation of all that he has done for the Company over fifteen years.

The past year has been a challenging one for the licensed trade but we have demonstrated that our strategy for enhancing shareholder value, underpinned by the optimal use of the strong cash flows which are generated from our quality pub estate, delivers attractive financial returns for shareholders. The Board looks forward to another year of solid progress.

## **Hubert Reid**

Chairman

21 November 2006

# Chief Executive's Review

## (Incorporating the Business Review)

### RESULTS

The year to 30 September 2006 has once again seen continued improvements in the quality and profitability of the Enterprise Inns (ETI) estate and further growth in shareholder value.

Group EBITDA before exceptional items increased to £547 million, equivalent to £64,200 per pub based upon the weighted average number of pubs (8,522) owned during the year, an increase of 5.2% in EBITDA per pub over the prior year. Profit before tax and exceptional items grew by 8.6% to £315 million and adjusted earnings per share increased by 17% to 68.3p.

### STRATEGY

The key strengths of the ETI business have been clarity and focus. From the day that the business was created in 1991, our two Mission Statements have remained unchanged: "to deliver long-term sustainable growth in shareholder value" and "to be the leading specialist operator of leased and tenanted pubs in the UK".

This clarity of purpose and consistency of application has delivered excellent results over the years. Not only has our estate increased in size from the 368 pubs that we purchased in 1991 to 7,809 at 30 September 2006 but, more importantly, we have seen a continuous increase in the quality, profitability and sustainability of the pubs. This is reflected in average EBITDA per pub having increased from £19,700 in 1992 to £66,700 today.

We remain convinced that the leased and tenanted model, combining the entrepreneurial flair and commitment of independent licensees with the experience and financial strength of a major company, offers the best formula to create ongoing success in the pub industry of the future. We never cease to admire the ingenuity and professionalism of our licensees, whether it is their gritty determination in the tough times or outstanding innovation and flair in exciting times.

The clarity and simplicity of our operating model has also delivered outstanding returns to our shareholders, with Total Shareholder Return (TSR) of some 2,640% over the eleven years since our flotation on the London Stock Exchange in 1995, compared to 147% for the FTSE All-Share over the same period.

This commitment to shareholder value underlies our current strategy of returning cash to shareholders through our ongoing share buy-back programme. We believe that prices paid for pubs in some recent corporate transactions may in time prove to be value destructive, particularly where the prices paid seem not to be driven by the long-term quality and sustainability of the pubs but by the availability of large amounts of relatively cheap funding.

In such a market, we prefer to take the opportunity to sell pubs which do not fit in with our long-term quality objectives and to use the strength of the financial markets to optimise the performance of our balance sheet for the benefit of our shareholders. It is of course possible that acquisition opportunities at a sensible price may become available, in which case we would review these in detail and pursue them with vigour if appropriate.

### TEAM

Our strategy has been driven by a commitment throughout the organisation to integrity, simplicity and empowerment. These values have enabled ETI to expand rapidly through acquisition, effectively integrating large numbers of pubs into the organisation with minimum disruption. Rapid expansion does from time to time bring with it some inevitable inefficiencies and cultural differences and it has been particularly rewarding in the past twelve months to enjoy a period of stability where we were able to make some structural and organisational changes, not so much to reduce costs but primarily to streamline the business and improve the quality of support that we give to our licensees.

Ownership, commitment and reward are critical ingredients in the motivation and retention of key staff and we are delighted that 100% of senior managers at ETI have some form of interest in the ownership of the business, through direct share ownership, share options, Share Incentive Plans or the Save as you Earn scheme. Indeed, 90% of all employees who have been with ETI for two years or more have an interest in the shares of the Company.

# Chief Executive's Review

## (Incorporating the Business Review)

### ESTATE

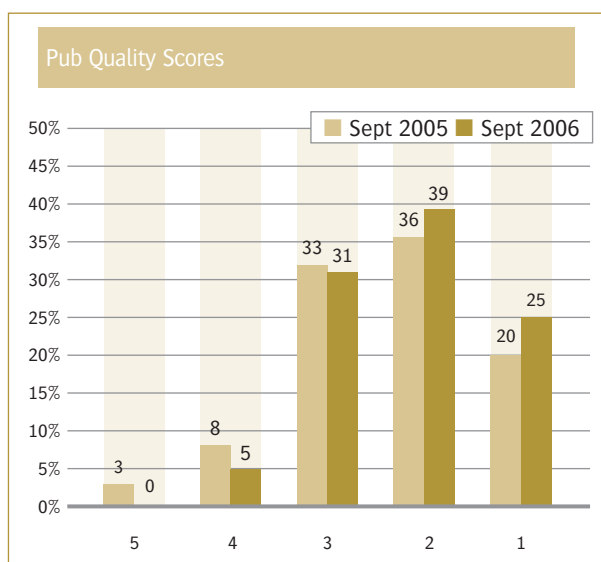
The quality, value and profitability of the ETI estate have continued to improve during the year, reflecting our investment alongside licensees and astute acquisitions and disposals.

We invested £54 million of capital expenditure into the estate and, together with a similar level of expenditure by our licensees, have improved 1,390 pubs, either through major schemes or minor refurbishments. Much of this expenditure has been focused on preparing our pub estate for the forthcoming ban on smoking, due to be introduced in Wales in April 2007 and England in July 2007. With 89% of our pubs having already developed outside trading areas and over 85% now offering food, we are confident that the majority of our licensees are well placed to benefit from the forthcoming ban which will, after all, make pubs more attractive to the significant majority of pub goers and current non-users who do not smoke.

We continued to improve the quality of the estate through churn, buying 95 excellent pubs for a total consideration of £80 million. Furthermore, we took advantage of a very strong market to sell those pubs which we had already identified as not fitting our quality and profitability profile for the future. During the year we sold 107 pubs in individual and small package transactions, generating proceeds of £48 million. In addition, in September 2006, we completed the sale of 769 pubs to Admiral Taverns for total consideration of £318 million. Our total disposal programme delivered a net profit, accounted for as an exceptional item in the accounts, of £67 million above book value.

This policy of investment and churn, plus an encouraging revaluation of 6.5% in the underlying value of the estate, has seen average EBITDA per pub increase to £66,700 for the 7,809 pubs which we owned at 30 September 2006. The book value of the pub estate at the year end, valued on an individual pub by pub basis, was £5.4 billion, equivalent to an average value per pub of £685,000. Our independent valuers advise us that the valuation would be some 15% higher if valuing the estate as a whole.

As part of our annual estates review, we form a view of the quality and sustainability of every pub in the estate. Although inevitably somewhat subjective, this process has provided a useful measure of the improving nature of the estate over time. With great pubs scoring as a 1 and potential disposals scored as a 5, we see strong correlations between pub quality and licensee profitability. It is very satisfying to see that both the average quality score and the quality profile of the estate have continued to improve over the year.



On 20 November 2006 we entered into a binding agreement for the sale of our entire Scottish estate of 137 pubs to Retail & Licensed Properties Limited for a consideration of £115 million, generating a profit over book value of £13 million. Whilst many of these pubs matched our normal retention criteria, this was a strategic sale reflecting our lack of critical mass in Scotland, a market that has many different characteristics to England and Wales and one where the leased and tenanted concept is not so well established.



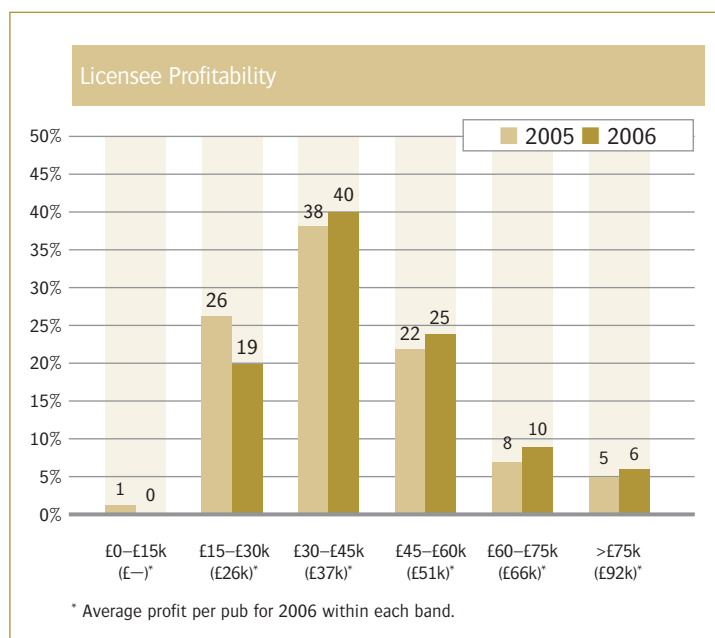
# Chief Executive's Review

## (Incorporating the Business Review)

### LICENSEES

A top quality estate of pubs generates sustainable profits for shareholders and licensees alike and it is the link between the quality of our pubs, the profitability of our licensees and our operating profit which is critical to our long-term success. If we are to attract the best licensees, they must be able to see the opportunity to achieve appropriate rewards for their hard work and investment. This is not just a function of pub quality but also, against a backdrop of increasing costs and bureaucracy, of the essential fairness of the package that we offer, particularly the level of rent charged and the help and support that we give.

In what has been a year of rising costs for licensees, we are satisfied that we have maintained our commitment to fair rents and once again we are pleased that our estate leads the way in providing worthwhile returns for our hard-working licensees. Based upon our annual review of the ETI estate, we estimate that the average level of licensee profitability in the 7,809 pubs that we owned at 30 September 2006 has increased by 7% to £45,000. There is of course a benefit of estate churn in this average increase, but we nevertheless estimate that on a like-for-like basis, licensee profitability in our pubs has increased in line with inflation.



We are pleased that licensees recognise that the higher quality and profitability of our estate, together with the essential fairness of the package that we offer, gives them real opportunities to be successful. This is once again supported by improvements in key performance indicators:

- During the year we received more than 5,000 enquiries from licensees looking to take a pub with ETI, with more than 30% of these enquiries converting to formal applications.
- We have 995 fully funded, fully screened licensees in our applicant database.
- There have been 820 lease assignments during the year, at an average premium of £68,000 (£85,000 including licensee fixtures and fittings).
- Rent concessions at 30 September 2006 remained consistent at less than 0.4% of the rent-roll.

# Chief Executive's Review

## (Incorporating the Business Review)

- 1,317 rent reviews were completed during the year and these resulted in an average rental increase of 2.1% per annum. Just two rent reviews went to arbitration.
- Adjusted for changes to licensee trading terms where appropriate, average rental income per pub increased by 2.6%, broadly in line with inflation.
- Bad debt costs once again reduced and remain around 0.1% of turnover.

We do not expect the coming year to be materially easier for the on-trade and it is clear that poorer quality pubs will struggle, particularly if they are unable to create opportunities from the forthcoming ban on smoking. Nevertheless, we are confident that our constant pursuit of quality, and the related improvements in potential licensee profitability, will once again ensure that the majority of our pubs continue to gain market share and to prosper.

### FINANCIAL STRUCTURE

#### Cash inflow

Free cash inflow during the year amounted to £107 million, based on operating cash inflow and after deduction of mandatory payments in respect of interest and tax and discretionary payments in respect of capital expenditure and dividends.

In addition, net receipts from the purchase and sale of pubs in the year amounted to £282 million, which included cash receipts of £316 million in respect of the sale of 769 pubs to Admiral Taverns.

#### Debt facilities

In May, the Group agreed a refinancing of its syndicated debt facilities at attractive rates, increasing these facilities from £490 million to £1 billion. At the end of the financial year £575 million was available for drawdown. The Group has a flexible financial structure comprising these syndicated debt facilities, a portfolio of corporate bonds and the Unique securitisation.

At 30 September 2006 underlying net debt was £3,166 million, similar to the level of £3,121 million at the start of the year. Underlying net debt represents amounts repayable to banks and other lenders net of cash retained in the business.

#### Financial leverage

The Board's policy is to maintain efficient leverage of the balance sheet in the context of the level of profit generated and the valuation of the pub estate.

The two key metrics used to measure financial leverage are interest cover based on EBITDA and the ratio of debt to EBITDA. Based on the current financing structure, the Board considers optimal leverage ratios for the Group as a whole to be around 2.2 times interest cover and approximately 6.6 times debt to EBITDA. At the end of the financial year interest cover was 2.4 times and underlying net debt to EBITDA was 5.8 times. There is therefore scope to increase leverage, providing significant headroom for continuing the share buy-back programme or for acquisitions should the opportunity arise.

#### Balance sheet

The net assets of the Group at year-end were £1,676 million which compares with £1,573 million as at 30 September 2005.

The book value of the pub estate at year-end was £5.4 billion, which included a cumulative revaluation surplus of £845 million.



# Chief Executive's Review

## (Incorporating the Business Review)

### Tax charge

The tax charge of £90 million represents 22% of profit before tax. The pre-exceptional tax charge of £95 million equates to 30% of profit before tax and exceptional items.

The £5 million exceptional tax credit comprises a credit of £34 million in relation to indexation on the tax base cost of certain properties together with a tax charge of £29 million which primarily relates to the movement in fair value of swaps and profit on sale of property, plant and equipment.

Cash outflow in respect of tax during the year was £69 million and represents 22% of profit before tax and exceptional items.

### Exceptional items

The Group has elected to classify certain items as exceptional and present them separately on the face of the Income Statement. Exceptional items are classified as those which are separately identified by virtue of their size or nature to allow a full understanding of the underlying performance of the Group. Exceptional items are generally those which the Board does not consider to be part of the core operations of the Group. As a result, the Group focuses on 'pre-exceptional' performance measures in order to compare underlying performance year on year.

The most significant exceptional items in the year are the profit on disposal of property, plant and equipment of £67 million and the movement in fair value of interest rate swaps of £40 million. The profit on disposal is highlighted as exceptional as it is not considered to be part of the core business of the Group. The profit of £67 million includes £51 million of profit arising on the batch disposal to Admiral Taverns. The movement in fair value of interest rate swaps is classified as exceptional as it is a non-cash item which is driven by factors outside of the control of the Group. The valuation of interest rate swaps in the year has led to a £40 million credit in 2006 compared to a £20 million charge in the previous year. This volatility is largely due to changes in forecast interest rates which have increased this year, reducing the forecast cost of maintaining the swaps.

### INTERNATIONAL FINANCIAL REPORTING STANDARDS

The new International Financial Reporting Standards (IFRS) apply for our 2005/6 financial year, with our Group accounts presented accordingly. The restated financial results under IFRS for the year ended 30 September 2005 and the 6 months ended 31 March 2005 were published in May 2006.

### REAL ESTATE INVESTMENT TRUSTS (REITs)

We continue to monitor the potential for creating shareholder value that REITs may offer. Detailed legislation has now been issued, albeit subject to further guidance notes and the ability of government to change the rules without reference to further legislation. We therefore continue to review with our advisers the costs, benefits and risks of structuring the Group to take advantage of this potentially favourable tax regime and the potential increase in long-term shareholder value that would result from any change.

### INDUSTRY ISSUES

#### Licensing reform

These results reflect almost a full year of trading under the new, more flexible licensing regime introduced in November 2005. Despite some early problems caused primarily by lack of clarity in the detail of the legislation, the system has now settled down and can be seen as broadly positive. Although the additional trading hours have had only a minimal effect on pub profitability, the increased flexibility in opening hours has benefited the consumer and helped to reduce alcohol related disorder. We share the government's determination to tackle irresponsible drinking and continue to work hard with our colleagues in the on-trade to tackle under-age drinking and irresponsible promotions.

# Chief Executive's Review

## (Incorporating the Business Review)

### **Ban on smoking in pubs**

Our experiences in Scotland, where the ban on smoking was introduced in March this year, confirmed that good quality pubs continued to perform well, particularly where licensees had prepared for the ban, taking advantage of available outside areas and developing their pub to reflect the changed circumstances.

The smoking ban will become effective in Wales and in England in April and July 2007 respectively and we are confident that our licensees are in a position to make the most of this evolution in pub going.

### **CONCLUSION AND OUTLOOK**

This has been another exciting year for ETI, working alongside our licensees to grow market share and profitability. The team has once again delivered substantial growth in earnings and dividends and we have made excellent progress with our ongoing share buy-back programme. The new financial year has started well and we look forward to our pubs continuing to perform ahead of the market and to the team delivering further solid growth in shareholder value.

### **Ted Tuppen**

Chief Executive

21 November 2006

# Corporate Responsibility

The Group continues to adopt an approach to the management of corporate responsibility that balances the long-term interests of stakeholders by focusing on those matters which are relevant to our long-term success and the environment in which the business operates.

The Board is committed to act in a responsible manner. This report sets out the key areas we have focused on during the period under review. Our approach to corporate responsibility includes:

- analysing and managing risk;
- maintaining a continuing dialogue with stakeholders; and
- managing the environmental and social impact of the business on employees and the community.

## Social, Ethical and Environmental Risk Management

The identification, management and monitoring of key risks is undertaken as part of the Group's system of internal control as described on page 27. In addition, we work with employees, licensees and suppliers as appropriate to ensure we understand any issues which may impact on the workplace, the community or the environment. The Chief Executive is responsible for the development and implementation of the approach to social responsibility matters. All executive directors are responsible for the promotion of good practice in environmental matters and report to the Board as necessary on significant risks.

The most significant corporate responsibility issues for the Group are considered below and the Group has put in place policies to ensure:

- compliance with relevant laws, regulations and codes of practice;
- employees are provided with a safe working environment; and
- ongoing training needs of employees are met.

## The Workplace

The Group's Health & Safety Policy (the 'H&S Policy') clearly states its intention to provide and maintain a healthy and safe working environment.

In order to deliver this policy, the Group has established an internal Health & Safety Management Group (the 'H&S Group') with responsibility for advising, reviewing and delivering the agreed management systems employed by the business to satisfy its health and safety responsibilities. The H&S Group reports to the Company Secretary who is responsible for regular reporting to the Board. The H&S Group's remit is carried out in accordance with the Health and Safety at Work Act 1974 and all other relevant health & safety statutory provisions and approved codes of practice.

The H&S Group has adopted the principles contained in the Health and Safety Executive guidance (HSG65) "Managing Health and Safety", which includes the following specific requirements:

- the establishment of a formal written policy;
- the establishment of a communication system with staff;
- the ongoing identification of risks and required responses; and
- the ongoing measurement of performance and the continual improvement of process and procedure to address changing risks.

# Corporate Responsibility

The H&S Group monitors accidents affecting staff, licensees and contractors, audits the understanding and application of the H&S policy and procedure by staff and contractors and, in July 2006, provided its annual report and risk assessment to the Board.

During the year the H&S Group has organised fire warden, first aid and lift evacuation training for office-based employees. In addition, the H&S Group has introduced a policy to provide guidance for the health and safety of employees driving on Company business.

The Directors' Report sets out employment policies and explains the way we communicate with employees. The key risk area in our working environment is the health, safety and well-being of employees. Employees work in a low risk environment. Again there has been no material health and safety issue, incident or fine for non-compliance during the period under review.

## The Environment

The Group recognises its responsibility to achieve good environmental practice and to continue to strive for improvement in areas of environmental impact. Our approach is to work towards continuous improvement through education, communication and direct action where applicable.



### (i) Carbon Management

The Group has established an Environmental Impact Committee with a view to reviewing strategy and implementing policies to deliver high quality energy services to our pubs, including, in 2006:

- continued promotion of cellar cooling maintenance contracts under which our licensees are able to utilise highly energy efficient cellar cooling equipment (4,097 pubs are currently under such contracts) and to target the replacement of 10% of inefficient cellar cooling equipment each year to ensure optimal energy performance;
- an improved working relationship with cellar cooling maintenance contractors; and
- a detailed inventory of boiler performance was undertaken across approximately 100 sites, and an action plan will be implemented in 2007 to improve boiler quality across the pub estate.

In 2006 the Group adopted the Carbon Trust's Carbon Management approach across its operations, including our head office and the pub estate. We appointed Ecofys, an external consultant, to provide specialist climate change expertise and to identify the risks and opportunities for the Group.

A comprehensive action plan was developed with the Carbon Trust to accelerate the integration of carbon issues throughout the Group and address our short, medium and long-term climate impacts. The Group will continue to be supported by the Carbon Trust in 2007 to implement a range of measures focused on our most energy intensive activities:

- pilot an energy efficient lighting programme in the pub estate, whereby discounted energy efficient lighting will be installed, delivering significant energy savings;

# Corporate Responsibility

- continue to develop an advanced maintenance contract for cooling and heating systems in the pub estate, including extensive maintenance to deliver improved energy efficiency (e.g. efficiency checks, descaling of hot water heating elements) and to ensure that the installation of all new mechanical plant carries the green flag efficiency mark to reduce wasted energy use;
- consideration of an energy aggregation programme to introduce advanced billing and energy reporting methods to the pub estate and promote energy consciousness and efficiency amongst our licensees;
- consideration of a focused awareness programme targeting our licensees who will be able to choose from a range of energy saving improvements for their pub and become involved in their implementation; and
- undertake ongoing audits of the pub estate to accurately measure energy efficiency savings and monitor the progress of the above-mentioned initiatives.

At head office, a detailed energy audit was undertaken to identify opportunities to reduce the building's energy consumption and assess the viability of alternative energy production. In 2007, an energy management programme for the head office will be introduced to deliver energy savings of over 10%, especially over the weekend and outside office hours.

## **(ii) Other Environmental Issues**

At head office materials are recycled where possible and paper is sourced from a renewable and sustainable source. Upon acquiring the building in 2002, the Group complied with the local planning authority's environmental policy relating to the construction, occupation and utilisation of office facilities. This included the provision of a transport policy aimed at reducing the demand for car parking and promoting employee behaviour consistent with local planning, environment and social policy. The Group supports home working where appropriate.

During the year a head office catering facility was introduced and the kitchen equipment installed carries the green flagged efficiency rating. Wherever possible biodegradable materials are used in its operation.

Through its membership of the British Beer and Pub Association (BBPA), the Group has participated in the Government's consultation period seeking to clarify and implement glass recycling targets under the EU Waste Directive and has registered with a compliance scheme pursuant to our obligations under the Packaging Waste Regulations.

## **The Community and Social Issues**

The Group believes that the interests of responsible, entrepreneurial pub businesses are substantially aligned with the interests of local communities and consumers. In this regard, the Group seeks to ensure that its pubs provide a friendly, safe and controlled environment, and promote the positive contributions that pubs make to their local communities.

The Group implemented the provisions of the Licensing Act 2003, which took effect on 24 November 2005, and worked extensively with licensees, local authorities and local communities to make appropriate applications for variation of licensing hours and conditions which balanced the opportunities and interests of all parties. Through its membership of the BBPA, the Group continues to engage with Government departments within the Home Office and the Department for Culture, Media and Sport, to promote understanding of, and compliance with, the new licensing regime.

# Corporate Responsibility

A ban on smoking in public places was introduced in Scotland in March 2006, and is due to be introduced across England and Wales in 2007. Notwithstanding the planned legislation, the Group has continued to promote the social and environmental benefits of a reduction in the incidence of smoking in pubs, and is continuing to work with licensees in preparation for implementation of the new legislation.

In addition:

- the Group is committed to high standards of customer service to its licensees and gives serious consideration to complaints from the local community. Procedures are in place to ensure disputes are monitored and dealt with quickly;
- training is arranged to provide support to our licensees and to develop business potential;
- the Group has recently revised and updated its Code of Practice under which the Group manages its relationships with licensees, and includes provisions in its agreements with licensees requiring licensed premises to be operated in a responsible manner; and
- the Group seeks to ensure that appropriate and reasonable actions have been implemented across the pub estate to ensure its licensees comply with the Disability Discrimination legislation.



Finally as a corporate sponsor we continue to support the philosophy and ethos of The Prince of Wales's 'Pub is the Hub' campaign, encouraging rural licensees to diversify and deliver a wider range of services to the communities they serve, ensuring that the pub becomes the heart of the community and continues to thrive as a vital part of village life. During the year a number of our licensees have developed a range of such services including the use of their premises as village shops and post offices.

## Responsible Drinking

The irresponsible consumption of alcohol can have detrimental effects on the social structures of local communities. The Group recognises that pub licensees, retailers, the government and the consumer all have responsibilities as regards the promotion and management of a responsible drinking environment. We seek to be responsible by the following means:

- the Company is a voluntary contributor to the funding of the Drinkaware Trust, a new body which brings together industry, charities, lobby groups, medical professionals and experts in the field to address alcohol misuse and promote sensible drinking across the UK;
- the Company is a signatory to the Portman Group's Code of Practice, and works proactively with drinks suppliers to ensure that they adhere to a responsible advertising, pricing and packaging regime;
- the Group actively promotes the Portman Group's 'Proof of Age Card Scheme' to all licensees and provides materials to all new licensees to enable them to operate the scheme in their premises;
- through its membership of the BBPA, the Company has actively participated in discussions with Government in the preparation of its National Alcohol Harm Reduction Strategy;
- the Group has also participated in a number of partnerships with local authorities to develop and implement local policies and strategies which are designed to address the potential consequences of alcohol misuse whilst not penalising the majority of responsible licensees and their customers; and
- a number of the Group's suppliers have introduced sensible drinking messages on their products.

## Future Corporate Responsibility Requirements

The Board is committed to continuous improvement in its corporate responsibility practices where relevant to its operations and to build appropriate measures and procedures into its existing risk management and governance systems.

# Directors and Advisers

## **H V REID** #

Chairman

Appointed to the Board 21/01/97

Hubert Reid, 65, is Chairman of Midas Income and Growth Trust PLC, Deputy Chairman of Majedie Investments PLC and a non-executive director of Michael Page International plc. He was previously Managing Director and then Chairman of the Boddington Group plc and a non-executive director and then Chairman of Istock Plc, Bryant Group plc and the Royal London Group.

## **G E TUPPEN** #

Chief Executive

Appointed to the Board 22/02/91

Ted Tuppen, 54, led the management buy-in which resulted in the formation of the Company in 1991. He is a chartered accountant and was in practice until 1980 with KPMG in London, North America and Europe. He then qualified with an MBA from the Cranfield School of Management before becoming managing director of a privately owned international engineering company where he worked until 1989. He has also worked in, and acted as a consultant to, a variety of businesses. He is a Vice President and a former Chairman of the British Beer and Pub Association.

## **A J STEWART** \*#

Senior Independent Non-Executive Director

Appointed to the Board 29/05/01

Jo Stewart, 57, is a fellow of the Institute of Grocery Distribution. He has over 30 years of experience in the food industry, was Managing Director of Pizzaland International and Chief Executive of Northern Foods plc until September 2003.

## **D A HARDING** \*#

Independent Non-Executive Director

Appointed to the Board 06/11/03

David Harding, 59, is Chairman of Coventry Building Society. He was previously Finance Director of Railtrack Group plc and Group Chief Executive of the parent company RTG plc until 2002. He was also Group Finance Director of Rugby Group plc and T&N plc. He is a fellow of the Institute of Chartered Management Accountants and a local magistrate.

## **S E MURRAY** \*#

Independent Non-Executive Director

Appointed to the Board 03/11/04

Susan Murray, 49, is a non-executive director of Imperial Tobacco plc, SSL International plc and Wm Morrison Supermarkets PLC and also a director and council member of the Advertising Standards Authority. She was previously Chief Executive of Littlewoods Stores Limited. She has also been Director of International Marketing for Diageo Plc, President and Chief Executive Officer of The Pierre Smirnoff Company and was a member of the Independent Complaints Panel of the Portman Group from 1998 to 2004.

\* Member of the Audit and Remuneration Committees

# Member of the Nominations Committee



# Directors and Advisers

## **D C GEORGE**

Chief Financial Officer

Appointed to the Board 08/07/91

David George, 55, joined the Company on its formation as part of the management buy-in team.

A qualified accountant, he spent ten years in industry including six years at Massey Ferguson Manufacturing Limited. He then spent ten years with Grand Metropolitan Brewing Limited in various finance roles, including Finance Director of The Manns and Norwich Brewery Company Limited and subsequently as Finance Director of the production division of Grand Metropolitan Brewing.

## **W S TOWNSEND**

Chief Operating Officer

Appointed to the Board 01/10/00

Simon Townsend, 44, joined the Company in February 1999, and was appointed to the Board in October 2000. He has worked in the pub and leisure industry for 20 years in various sales, marketing, commercial and operational roles, previously with Whitbread plc, Allied Domecq PLC, Rank Group PLC and Marston, Thompson & Evershed PLC.

## **Secretary**

D C George

## **Auditors**

Ernst & Young LLP, No. 1 Colmore Square, Birmingham, B4 6HQ

## **Bankers**

Bank of Scotland, 124 Colmore Row, Birmingham, B3 4AU

## **Financial Adviser**

HSBC Investment Bank plc, Vintners Place, 68 Upper Thames Street, London, EC4V 3BJ

## **Stockbrokers**

Deutsche Bank AG London, Winchester House, 1 Great Winchester Street, London, EC2N 2DB

UBS Limited, 1 Finsbury Avenue, London, EC2M 2PP

## **Registrar**

Computershare Investor Services PLC, The Pavilions, Bridgwater Road, Bristol, BS13 8AE

## **Solicitors**

CMS Cameron McKenna LLP, Mitre House, 160 Aldersgate Street, London, EC1A 4DD

## **Registered Office**

3 Monkspath Hall Road, Solihull, West Midlands, B90 4SJ

## **Company number**

2562808

# Directors' Report

The directors present their report and accounts for the year ended 30 September 2006.

## Accounts and dividends

This is the first set of accounts reported using International Financial Reporting Standards. The Group profit for the year, after taxation, amounted to £325 million (2005 – £209 million) and is dealt with as shown in the Group Income Statement.

The directors recommend the payment of a final dividend of 18.0 pence (2005 – 12.4 pence) per ordinary share to be approved at the Annual General Meeting on 16 January 2007. The final dividend will be paid on 22 January 2007 to members on the register on 29 December 2006. When added to the interim dividend of 9.0 pence (2005 – 5.6 pence), this produces a total dividend for the year of 27.0 pence (2005 – 18.0 pence) per ordinary share.

## Principal activities and review of the business

The principal activity of the Group continues to be that of a leased and tenanted pub operator in the UK.

A review of the year's activities is given in the Chairman's Statement and the Chief Executive's Review (incorporating the business review) on pages 2 to 8.

## Directors and their interests

The names of the current directors together with related biographical information are set out on pages 13 to 14. All directors served throughout the year and were in place on the date of signing of these financial statements except for Mr G W Harrison who retired on 30 September 2006.

In accordance with the Articles of Association of the Company, Mr D A Harding and Mr W S Townsend retire from the Board at the Annual General Meeting by rotation and offer themselves for reappointment. The Board believes that the performance of Messrs Harding and Townsend continues to be effective, that they demonstrate commitment to their roles and have a range of skills and experience relevant to the direction and control of the Company. In addition, Mr Harding considers that he has sufficient time to commit to the Company's affairs notwithstanding his other business commitments and has no conflicting interests.

At no time during the year did any of the directors have an interest in any contract with the Group. The interests of the directors in the share capital of the Company, other than with respect to options to acquire ordinary shares (which are detailed in the Directors' Remuneration Report), were as follows:

Ordinary Shares of 5 pence each		30 September 2006 (i)	30 September 2005
H V Reid	Beneficial	122,500	122,500
G E Tuppen	Beneficial	1,060,054	1,002,412
	As Trustee	198,150	177,980
D C George	Beneficial	1,025,947	964,854
W S Townsend	Beneficial	173,797	125,822
A J Stewart	Beneficial	14,000	14,000
D A Harding	Beneficial	500	500
S E Murray	Beneficial	2,000	500

(i) These shares include the number of shares the executive directors hold in the Enterprise Inns 2005 Share Incentive Plan purchased on 15 December 2005 at 919 pence per share as follows:

# Directors' Report

	Partnership Shares	Matching Shares	30 September 2006	30 September 2005
G E Tuppen	163	163	326	—
D C George	163	163	326	—
W S Townsend	163	163	326	—

The executive directors, along with other employees, have been granted options over the shares of the Company. Details of these interests are disclosed in the Directors' Remuneration Report. There have been no changes in the interests of directors between the balance sheet date and the date of approval of the accounts.

## Notifiable interests in shares

As at 21 November 2006 the Company had been notified of the following material holdings of 3% or more of the Company's issued share capital (excluding treasury shares):

	Number of ordinary shares	Percentage of issued share capital
Merrill Lynch Investment Managers Group Limited	32,585,001	10.8
Prudential plc	21,308,657	7.1
Landsdowne Partners Limited Partnership	19,343,473	6.4
Barclays PLC	12,048,772	4.0
The Goldman Sachs Group Inc	11,803,876	3.9
FMR Corp/Fidelity International Limited	10,856,902	3.6
Lloyds TSB Group Plc	9,574,328	3.2

## Share Capital

Details of the share capital of the Company are set out in note 27 to the accounts on page 71. The Company did not issue any shares during the period under review.

## Own shares acquired by the Company

At the Annual General Meeting held on 19 January 2006, the Company was given authority to purchase up to 51,850,998 of its ordinary shares. During the year the Company made on-market purchases totalling 42,340,815 of its own ordinary shares of 5 pence each, representing 12.11% of the issued share capital, for an aggregate consideration of £393 million (excluding costs). As at 30 September 2006, 25,000,000 of these shares were held in treasury and the balance of 17,340,815 were cancelled. The maximum number of shares held in treasury during the year ended 30 September 2006 was 32,000,000 on 14 June 2006 for a period of 105 days, representing 9.2% of total called up share capital at that time. The present authority for the Company to purchase its own shares will expire at the Annual General Meeting to be held on 16 January 2007. The directors will be seeking a new authority for the Company to purchase its ordinary shares as part of the planned continuation of the share buy-back programme. It is expected that any shares purchased pursuant to the share buy-back programme will be cancelled and the number of shares in issue reduced accordingly. Alternatively the shares may be purchased and held as treasury shares. Further details are set out in the Explanatory notes to the Notice of AGM on page 127.

# Directors' Report

## Shares acquired by Employee Share Trusts

The Company has established an employee benefit trust, the trustee of which is Halifax EES Trustees International Limited. As at 30 September 2006, the trustee held 6,617,408 shares which are used to satisfy awards made under the Enterprise Inns Incentive Plans and other share option schemes. The Company has also established a Quest trust to hold shares to satisfy awards made under the Save as you Earn share option scheme, the trustee of which is Enterprise Inns Quest Trustees Limited. As at 30 September 2006, this trustee held 252,845 shares. The executive directors as employees of the Company are potential beneficiaries of shares held by these trusts (the 'trusts').

The total number of shares held by the trusts at 30 September 2006 was 6,870,253 representing 2.07% of the total called up share capital at that date. During the year, the trusts purchased 27,884 of the Company's shares. These shares were purchased for a consideration of £0.25 million (net of expenses) and had a nominal value of £1,394. The maximum number of shares held during the year ended 30 September 2006 was 9,248,445 on 1 October 2005 for a period of 54 days, representing 2.65% of total called up share capital at that time.

During the year, 2,406,076 shares with a nominal value of £120,304 were disposed of by the trust by way of the exercise of share options under the share schemes. A total of 497,751 shares were disposed of through the short-term and long-term incentive schemes for consideration of £8. A total of 209,579 shares were disposed of through the Quest Trust for consideration of £0.26 million.

## Directors' indemnities

The Company's Articles of Association permit the Board to grant the directors indemnities in relation to their duties as directors, including qualifying third party indemnity provisions (within the meaning of the Companies Act 1985) in respect of any liabilities incurred by them in connection with any negligence, default, breach of duty or breach of trust in relation to the Company. No such indemnities have been granted.

## Employment policies

The Group is dependent on the skills and commitment of its employees and recognises the importance of creating a workplace in which all employees are inspired and enabled to give their best. A core set of common values means that employees at all levels of the business are encouraged to make the fullest possible contribution as their performance is central to the successful delivery of its objectives. To attract and retain these skills, the Group is committed to equal opportunities and the creation of an entirely non-discriminatory and diverse working environment. The aim of the policy is to ensure that no job applicant or employee receives less favourable treatment because of, amongst other matters, gender, marital status, race, age, sexual preference, religion, belief or disability. All decisions are based on merit of the individual concerned. The Group is dedicated to undertaking its business operations in a way which respects individual human rights, treats individuals with dignity and allows freedom of association.

The Group gives full consideration to applications for employment from disabled persons where the requirements of the job can be adequately fulfilled by a handicapped or disabled person.

Where existing employees become disabled, it is the Group's policy wherever practicable to provide continuing employment under normal terms and conditions and to provide training and career development and promotion to disabled employees wherever appropriate.

The Group's employment policies and procedures are described in detail in a Staff Handbook which is provided to all employees upon joining the Group. The Staff Handbook is regularly reviewed and updated to take account of relevant employment legislation and best practice, and new policies and procedures are developed if required. These include specific policies on equal opportunities, flexible working, training and development, acceptance of gifts and hospitality, and whistle-blowing.

The Group has systems in place to comply with the Data Protection Act 1998 to ensure the privacy of personal information.

# Directors' Report

## Employee involvement and reward

The Group actively encourages learning and development and believes that effective training is essential to the maintenance and improvement of the Group's success and individual performance. The Group is committed to providing all employees with relevant training to meet the business needs of the Group and to improve individual employee skills. In providing this training and support we expect high standards and commitment in return. All employees are provided with initial induction training and are set challenging personal objectives and participate in discretionary bonus schemes.

The Group operates a comprehensive employee appraisal system which ensures that clear goals are set, personal objectives are monitored, key competencies are assessed and any performance concerns addressed through appropriate training and focus. Every employee has the opportunity to discuss work-related aspirations and participate in appropriate training and development programmes.

During the year, continued emphasis has been placed on effective communication regarding matters which may affect employees and the overall performance and development of the Group. The policy of providing employees with information about the Group has continued. Employee engagement is met through a variety of means including regular briefings and team meetings through its management structure which allows a free flow of information and ideas via publications such as Eagle Eye. In addition, an annual conference is held to which all employees are invited and provides an opportunity for employees to be made aware of key objectives and strategy. The use of email and the corporate intranet supplement effective communication to all employees.

The Company continues to encourage employee ownership of its shares through the provision of the following employee share plans administered by HBOS Employee Equity Solutions:

- the Save as You Earn Scheme in which 290 employees have entered into savings contracts for either five or seven years at the end of which they are entitled to purchase shares at a discount of 20% to the market price of the shares at the time of the issue of the options; and
- the Share Incentive Plan in which 300 employees have purchased shares out of pre-tax income up to statutory limits which are held in a trust. Currently the Company awards one free matching share for each share bought by an employee.

## Charitable and Political Donations

At pub level, the Company supports local community initiatives and charitable causes through the appropriate use of marketing investment. The Company does not make any corporate charitable donations. The Company has not made any political donations during the year and intends to continue its policy of not doing so for the foreseeable future.

## Creditors' payment policy and practice

The Group agrees terms and conditions for its business transactions with suppliers. Payment is then made in accordance with these terms, subject to the terms and conditions being met by the supplier.

At the year-end the Group had an average of 26 days' purchases outstanding in trade creditors.

## Financial Instruments

For financial risk management objectives and policies, please see note 22 to the accounts.

# Directors' Report

## Directors' statement as to disclosure of information to auditors

Each person who is a director at the date of approval of this report confirms that:

- so far as the director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- the director has taken all of the steps that he/she ought to have taken as a director to make himself/herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 234ZA of the Companies Act 1985.

## Statement of directors' responsibilities in relation to the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards ('IFRS') as adopted by the European Union.

The directors are required to prepare financial statements for each financial year which present fairly the financial position of the Group and the financial performance and cash flows of the Group for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- state that the Group has complied with IFRS, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the Companies Act 1985 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

# Directors' Report

## Annual General Meeting

The AGM will be held on 16 January 2007 at 11.00 a.m. The notice convening the AGM and an explanation of the resolutions sought are set out on pages 121 to 127. At the meeting, the Company will be seeking shareholder approval, amongst other matters, for:

- the sub-division of each ordinary share of 5 pence each (issued and unissued) into two ordinary shares of 2.5 pence. If approved, the share split is expected to become effective on or around 17 January 2007; and
- authority for the Company to make market purchases of its own shares.

The directors consider that all the resolutions proposed are in the best interests of the Company and it is their recommendation that you support these proposals as they intend to do in respect of their own holdings.

## Auditors

A resolution to reappoint Ernst & Young LLP as the Group's auditors will be put to the members at the forthcoming Annual General Meeting.

By order of the Board

**D C George**

Secretary

21 November 2006



# Corporate Governance

## Introduction

The Board recognises that good governance helps the business deliver its strategy, generate long-term shareholder value and minimise risk. For the year under review the appropriate governance provisions are as set out in the Combined Code on Corporate Governance adopted by the Financial Reporting Council in July 2003 (the "Combined Code").

The Company is committed to maintaining high standards of corporate governance as set out in the Combined Code provisions, the Turnbull Report on Internal Control and appropriate best practice guidance issued by investor bodies. Our corporate governance framework is directed in a manner which is responsible and in accordance with high standards of honesty, transparency and accountability. The Board considers that this statement on governance provides the information to enable shareholders to evaluate how the provisions and principles of the Combined Code have been applied.

## Statement by the directors on compliance with the Combined Code

The Board is responsible for the policies and controls put in place to discharge the Company's responsibilities under the Combined Code. These include, for example, a sound system of internal controls and risk management procedures designed to ensure the Company's policies achieve compliance.

Throughout the year ended 30 September 2006 the Company has been in full compliance with the provisions set out in Section 1 of the Combined Code and the principles of good governance with the exception of provision A.3.2 which provides that at least half the Board, excluding the Chairman, should comprise non-executive directors determined by the Board to be independent. Following the retirement of Mr G W Harrison on 30 September 2006 the Company is now compliant with this provision.

The Company has also complied with the Smith guidance on Audit Committees.

## The Workings of the Board and its Committees

### The Board Role

The Board is responsible to the Company's shareholders for the success of the Group and for its overall strategic direction, its values and its governance. It provides the leadership necessary to enable the business objectives to be met while ensuring the obligations to its shareholders are safeguarded.

### Composition

For the year under review the Board comprised the Chairman, four executive directors and three independent non-executive directors. The role of Chairman and Chief Executive are distinct and separate and clear divisions of accountability and responsibility have been agreed by the Board, are set out in writing and operate effectively for these positions. During the year, the Board has again reviewed its composition and has concluded that its composition fully satisfies the requirements of the business and ensures proper governance of the Group.

The Chairman, Mr H V Reid, has primary responsibility for leadership of the Board, ensuring its effectiveness and setting its agenda and devotes such time to his role as is necessary to properly discharge his duties. He is responsible, jointly with the Chief Executive, for the effective communication with the Company's shareholders and representation of the Group externally.

The Chief Executive, Mr G E Tuppen, has executive responsibilities to ensure delivery of strategic and financial objectives and for executing the Group's strategy and development.

The Board requires that all non-executive directors are free from any relationship with the executive management that could result in any conflict or affect their independent judgement. The Board recognises that length of service can impact on the independence of a non-executive director and, having considered this, is satisfied that all non-executives remain independent in character and judgement for the purposes of the Combined Code. The Board membership and that of its Committees is designed to ensure that no one individual or group dominates proceedings and that the wide variety of skills allows effective leadership across the Company's business activities.

# Corporate Governance

Other than the retirement of Mr G W Harrison on 30 September 2006 there were no changes to the membership of the Board during the year.

The Board is satisfied that, as a non-executive director seeking re-election, Mr D A Harding continues to perform effectively and demonstrates commitment and time to his role and duties.

Biographical details of the Board members are set out on pages 13 to 14.

## Operation of the Board

The Company has an effective Board which leads and controls the Company and is responsible to the shareholders for its proper management. The Board reviews trading performance, sets and monitors strategy and examines major capital expenditure and acquisition opportunities.

The Board has established guidelines requiring that specific matters are reserved for a decision by the full Board. This ensures that the Board maintains control over strategic, major financial and key operational issues. Such matters include, for example, the approval of financial statements, material acquisitions and disposals of assets, risk management and governance policies. All meetings of the Board are structured to allow open discussion by all directors and ensure full participation in the decision-making process.

## Meetings and Attendance

The Board held six scheduled meetings in the past year and is expected to hold a similar number of such meetings over its next financial year. The Board convenes additional meetings to consider matters that are time critical. In addition, separate off-site meetings are held annually at which high level strategic issues, such as future business direction and its financial and operational implications, are reviewed and debated. All of the current directors attended all Board Meetings and the Strategic Review during the year.

## Non-executive directors and the Senior Independent Director

The non-executive directors complement the skills and experience of the executive directors and bring an independent judgement to the decision-making process at Board and Committee level. Their role requires a time commitment in the order of 15 days per annum plus additional time as necessary to properly discharge their duties. In terms of commitments outside of the Company, any material changes must be reported to and pre-cleared with the Chairman.

The Company has appointed a Senior Independent Director whose role and responsibilities are clearly defined, set out in writing and agreed by the Board. The Senior Independent Director is available to shareholders if they have any concerns that cannot be resolved through contact through normal channels.

In compliance with the Combined Code, the Senior Independent Director met with the other non-executives during the year to discuss matters in a forum that did not include executive directors or the Chairman. In addition, all of the non-executives including the Chairman met during the year without the executive directors being present to discuss, amongst other matters, the performance of the Chief Executive and overall feedback arising from the performance evaluation process and strategic review.

## Information and Training

The Board and its committees are supplied with full and timely information which enables the proper discharge of their responsibilities.

All directors have access to the services of the Company Secretary and may take independent professional advice at the Company's expense. There is a formal written procedure concerning independent professional advice setting out clear guidelines which have been agreed by the Board. The Company has arranged appropriate directors' and officers' liability insurance to provide cover in the event of legal action against its directors. The Company Secretary acts as secretary to the Board and its committees and is responsible for advising the Chairman on matters of corporate governance, ensuring the good flow of information to the Board and its committees and between the non-executives and senior management. The written responsibilities of the Company Secretary are available on the Company's website.

# Corporate Governance

All new directors receive an appropriately tailored induction programme arranged to develop their knowledge and understanding of the Group and the key business issues. The training needs of each director are regularly reviewed and assessed by the Board. Existing directors undertake such professional development as is necessary for them to carry out their duties as directors.

## Re-election of Directors

The Articles of Association of the Company require that any newly appointed directors will be subject to election at the next following Annual General Meeting and also that at least one-third of directors (excluding those appointed to the Board during the year) shall retire by rotation each year. This is applied so that each director will submit themselves for election or re-election at regular intervals and at least once every three years.

The Board has determined that re-election of the Chairman and non-executive directors is not automatic and is subject to formal review and recommendation by the Nominations Committee and approval by shareholders.

## Board Committees

In order to ensure effective leadership and governance the Board governs through clearly identified committees which have delegated powers to deal with specific aspects of the Company's affairs. A summary of the operation of these committees is set out below. All committees of the Board that are subject to the requirements of the Combined Code are chaired by an independent director or have a majority of independent directors as members. The names and biographical details of all Board Committee members are set out on pages 13 to 14.

### The Audit Committee

The Board's obligation to establish formal and transparent arrangements for considering how it should apply financial reporting and internal control principles and for maintaining an appropriate relationship with the Company's external auditors is met through the Audit Committee.

The Audit Committee is chaired by Mr D A Harding who has current and relevant financial experience. The Committee's other members are Mr A J Stewart and Mrs S E Murray. All members are independent. The Committee met four times during the year to coincide with the financial reporting and audit cycles of the Company including the submission of the interim and annual financial statements. All Committee members attended each meeting during the year. Representatives from the external auditors, the Chairman, Chief Executive and Chief Financial Officer were in attendance at part or all of each meeting by invitation. As a matter of best practice, the Committee is able to meet alone with external auditors as required at the end of its meetings.

The Committee has terms of reference which are set out in writing and agreed by the Board and are in accordance with the recommendations set out in the Combined Code. These are available on the Company's website.

The Committee is responsible for reviewing a wide range of financial matters including the interim and annual accounts prior to their submission to the Board, and monitoring the controls which are in force to ensure the integrity of the financial information reported to shareholders. The Committee advises the Board on the appointment of external auditors and on their remuneration and discusses the nature and scope of their work. The Committee has also been concerned to ensure that the appropriate standards of governance, reporting and compliance are being met. The Company has in place a whistle-blowing policy under which employees may, in confidence, raise concerns about possible improprieties in such matters as financial reporting.

For the year under review, the Committee:

- has monitored the integrity of the financial statements, interim and final report and accounts and relevant regulatory announcements;
- reviewed the introduction of International Financial Reporting Standards and monitored the implementation of appropriate changes to the Group's accounting principles and policies;
- agreed the annual audit plan and has considered external auditor reports and has monitored and followed up management actions in response to issues raised;

# Corporate Governance

- met regularly with management and with internal and external auditors to review the effectiveness of internal controls and business risk management and is satisfied that proper and satisfactory internal controls remain in place to identify and contain business risk;
- reviewed and monitored the independence and objectivity of external auditors; and
- carried out an annual evaluation of its performance.

The Committee has adopted a policy on the engagement of external auditors and reviews this annually. The Committee is confident that in reviewing the external auditors' Annual Audit Results Report, the objectivity and independence of the auditors are not impaired by the provision of non-audit services. The Committee is satisfied that such work is best handled by them due to knowledge of the Group. The Committee aims to have non-audit work carried out in a manner that affords full value for money.

It is considered appropriate for commercial and practical reasons, including confidentiality, to use the external auditors for certain non-audit services. The amount of non-audit fees charged by auditors is disclosed in note 6 to the accounts.

## The Nominations Committee

The Committee is chaired by Mr H V Reid and its members are the Chief Executive and the three non-executive directors Mr A J Stewart, Mr D A Harding and Mrs S E Murray.

The Committee is responsible for proactively refreshing and reviewing the Board's composition. The Committee nominates, for approval by the Board, candidates for appointment to the Board, having regard to its balance and structure. The Committee is also responsible for succession planning and takes into account the knowledge and skills mix required by the Board in the future. The Committee meets as required and met twice during the year when all Committee members attended. The Committee seeks the advice of external recruitment consultants as necessary and follows a formal and transparent procedure to ensure that new appointments comply with the principles set out in the Combined Code and satisfy the needs for the balance of the Board. Any appointments are based on merit and against objective criteria, including the time available to, and the commitment which will be required of, the potential director.

The Committee has terms of reference which are set out in writing and agreed by the Board and are in accordance with the recommendations set out in the Combined Code to ensure that no director is involved in discussions regarding his or her own succession. These terms of reference are available on the Company's website. The individual terms and conditions of appointment of directors can be inspected during normal office hours at the Company's registered office and at the Annual General Meeting.

During the year in review, the Committee:

- reviewed the plan for the retirement of directors by rotation and the framework for succession planning, the operational reorganisation of the Group including the retirement of Mr G W Harrison and the appointment of Mr W S Townsend as Chief Operating Officer;
- consulted with the Board regarding senior managerial appointments; and
- carried out an annual evaluation of its performance.

# Corporate Governance

## The Remuneration Committee

The Committee is chaired by Mr A J Stewart and its members are the two other non-executive directors Mr D A Harding and Mrs S E Murray. The Committee is responsible for determining the contract terms, remuneration and other benefits of the executive directors and senior management, including performance related bonus schemes and the Chairman's fee. The remuneration of the non-executive directors is set by the Board.

The Committee appoints external remuneration consultants and advisers as necessary to provide remuneration services and advice to the Remuneration Committee and the Company. The Committee met on four occasions during the year and all Committee members were in attendance.

The Committee has terms of reference which are set out in writing and agreed by the Board and are in accordance with the recommendations set out in the Combined Code. These are available on the Company's website.

The responsibilities of the Committee, together with an explanation of how it applies the principles set out in the Combined Code, are set out in the Directors' Remuneration Report which includes details of directors' remuneration and directors' interests in options, together with information on service contracts, and is set out on pages 28 to 37.

During the period in review, the Committee:

- determined the remuneration for executive directors and the Chairman;
- discussed levels of remuneration for senior manager appointments;
- determined the awards under the Company's incentive arrangements under the Annual Bonus Plan and Long Term Incentive Plan 2002 and 2005;
- agreed adjusted EPS figures for targets set out in the Enterprise Inns Incentive Plans following the adoption of International Financial Reporting Standards;
- agreed the content and presentation of the remuneration report for inclusion in the report and accounts; and
- carried out an annual evaluation of its performance.

## Finance Committee and Disclosure/Monitoring Committees

The Board has delegated, within agreed terms of reference, responsibility for certain matters of a routine nature which are not reserved for full Board consideration to a Finance Committee. This Committee comprises two executive directors, one of which must be the Chief Financial Officer. In addition and to ensure full compliance with its obligations under the Disclosure Rules published by the UK Listing Authority, the Company has established a Disclosure Committee comprising the Chairman, Chief Executive and Chief Financial Officer to maintain adequate procedures, systems and controls to enable it to make timely and accurate disclosure of information via a regulatory news service when it is impracticable to hold a full Board meeting. A separate Monitoring Committee has been established to monitor compliance with UK Listing Principles, including a policy based on the Model Code, which cover the dealings in securities and applies to directors, persons discharging managerial responsibility and employee insiders.

## Performance evaluation

Principle A.6 of the Combined Code provides that the Board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors. During the year, the Company has internally undertaken a critical self-assessment performance evaluation programme in accordance with this principle and has effectively evaluated the Board, its Committees and its individual directors, including the Chairman.

# Corporate Governance

## Board performance evaluation

The process was led by the Chairman and all directors completed a questionnaire in which they were asked to score a number of performance criteria. The results of the questionnaires were compiled into a report by the Deputy Company Secretary and the Chairman presented the findings to the Board at a Board meeting when all the directors were present. The review found that the Board's performance is streamlined, constructive and continues to be effective in dealing with challenging issues as and when they arise.

## Board Committee performance evaluation

For the Board Committee performance evaluation processes each Committee Chairman and Committee member completed a questionnaire in which they were asked to score a number of performance criteria. The results of the questionnaires were compiled into a report by the Deputy Company Secretary and the Chairman presented the findings to the Board. The review found that the Committees continued to deal efficiently with their remits and concluded that the membership and structure of the Committees complemented the workings of the Board.

## Non-executive director performance evaluation

This process was led by the Chairman and all non-executive directors completed a self-appraisal questionnaire in which they were asked to score a number of performance criteria. Each non-executive director then met on a confidential basis with the Chairman to review the questionnaire and to discuss matters in detail including any matters arising from the evaluation of the Board and Committee performance. In addition, the Senior Independent Director met with the other non-executives without the Chairman being present to review the Chairman's performance.

## Executive director performance evaluation

This process was led by the Chief Executive and all executive directors completed a self-appraisal questionnaire and were asked to score a number of performance criteria. Each executive director then met on a confidential basis with the Chief Executive to review the questionnaire and to discuss matters in detail. Each executive director is also set challenging performance objectives. The successful achievement of these objectives makes up part of the short-term incentive criteria under the Annual Bonus Plan.

## Shareholder relations

The Board places considerable importance on maintaining clear communications with its stakeholders directed to ensuring a mutual understanding of its objectives and has a continuing dialogue with institutional investors to discuss the progress of the business and deal with a wide range of enquiries. This includes direct face to face contact, presentations after the preliminary announcement for the year and the results for the half year and specific analyst presentations with feedback from the Company's brokers as necessary.

During the year shareholders are also informed of the progress of the Company through announcements released through the London Stock Exchange and made available on the website.

The Chairman is responsible for ensuring, via the Company Secretary, that views of major shareholders are fed back to the non-executive directors on a regular basis. The effectiveness of how shareholder views are communicated forms part of the annual Board performance evaluation process. Information about the Company, including reports, announcements and presentations, is made available simultaneously on its website so that shareholders have full access to material information. Directors regularly receive copies of analyst reports and reports on movements in major shareholdings as well as key broker comments.

The Annual General Meeting, held in January each year, is the principal opportunity to encourage participation by private investors and procedures at such meetings are in accordance with the Combined Code. The Chairmen of the Audit, Nominations and Remuneration Committees are available at the Annual General Meeting to answer questions. Details of the resolutions to be proposed at the Annual General Meeting on 16 January 2007 can be found in the Notice of the meeting on pages 121 to 124. The Notice is sent by first class post to shareholders at least 20 working days before the Annual General Meeting and details of proxy votes for and against are made available after the result of hand votes. In accordance with the Combined Code, the Company has proposed in the Notice separate resolutions on each substantial matter. Again this year the

# Corporate Governance

Company is, in accordance with the Myners Report, offering shareholders a facility for electronic proxy voting and voting through the CREST electronic proxy appointment service. The voting results are announced on the same day to the London Stock Exchange and on the Company's website.

The Company has considered innovative ways of communicating with shareholders and has given all its shareholders the opportunity to register and receive shareholder communications, such as the report and accounts, the interim report and notices of meetings, electronically via the Internet rather than in paper form through the post in accordance with good investor practice.

Finally, the Company's registrars, Computershare Investor Services PLC, deal with a wide range of investor queries on behalf of shareholders. Details of additional shareholder services are set out on page 120.

## Internal Control

The Board is responsible for the overall system of internal control for the Group and for reviewing its effectiveness. It carries out such a review at least annually covering all material controls including financial, operational and compliance controls and risk management systems.

An ongoing process on internal control has been established for identifying, evaluating and managing risks faced by the Group. This process is reviewed regularly by the Board and, with advice from its Audit Committee, is satisfied that this meets the requirements of the guidance 'Internal Control: Guidance for Directors on the Combined Code' issued by the Institute of Chartered Accountants in England and Wales in 1999 and the Turnbull guidance. The risk management process and systems of internal control are designed to manage rather than eliminate the risk of failure to achieve the Group's strategic objectives. It should be recognised that such systems can only provide reasonable and not absolute assurance against material misstatement or loss. This process has been in place since the start of the financial year and up to the date of approval of the accounts.

The key procedures which the directors have established with a view to providing effective internal control are as follows:

- regular Board meetings to consider a schedule of matters reserved for directors' consideration;
- the Board carries out an annual review of corporate strategy which includes a review of risks facing the business, and how these risks are monitored and managed on an ongoing basis within the organisation. This process is regularly reviewed by the Board;
- an established organisational structure with clearly defined lines of responsibility and delegation of authority;
- an established internal audit function which implements the annual internal audit plan as agreed by the Committee;
- documented and enforced policies and procedures;
- appointment of staff of the necessary calibre to fulfil their allotted responsibilities;
- comprehensive budgets and forecasts, approved by the Board, reviewed and revised on a regular basis, with performance monitored against them and explanations obtained for material variances;
- a detailed investment approval process, requiring Board approval for major projects. Post-investment appraisals are conducted and are reviewed by the Board; and
- the Audit Committee of the Board, comprising non-executive directors, considers significant financial control matters as appropriate.

## Going Concern

After making enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.



# Directors' Remuneration Report

## Information not subject to audit:

### Remuneration Committee and advisers

The Company's Remuneration Committee (the 'Committee') is composed entirely of independent non-executive directors and is chaired by Mr A J Stewart, its other members being Mr D A Harding and Mrs S E Murray. No member of the Committee has any personal financial interest in the matters being decided. Mr H V Reid and Mr G E Tuppen attend meetings at the invitation of the Committee, if necessary, except when their own remuneration is being discussed.

The Committee's key objectives are to:

- determine and recommend to the Board, within agreed terms of reference, an overall remuneration package for executive directors; and
- monitor the level and structure of remuneration for senior management.

The Committee has been constituted and operated throughout the year in accordance with the provisions of Schedule A and B of the Combined Code. This report also complies with Schedule 7A of the Companies Act 1985 which incorporates the Directors' Remuneration Report Regulations 2002.

During the year the Committee and the Company have continued to use the services of Ernst & Young LLP (E&Y) who have provided specific advice on remuneration matters relating to share schemes and the Enterprise Inns Incentive Plans (and who were appointed by the Committee for this purpose). E&Y are the Group's auditors and also provide advisory services in respect of non-audit matters and taxation. In addition, the Committee has sought advice relating to directors' remuneration and the Enterprise Inns Incentive Plan 2005 from New Bridge Street Consultants LLP (who were appointed by the Committee and who provide no other services to the Company save in respect of advice in connection with the operation of the Company's incentive schemes).

The Committee, amongst other matters, determines the level of awards made under the Company's incentive plans, considers feedback from shareholders and undertakes an annual review of its effectiveness.

When setting the remuneration of the executive directors, due regard is given by the Committee to pay and conditions elsewhere in the Group.

### Remuneration Policy – Executive Directors

The Remuneration Committee's policy is designed to ensure that the level and structure of remuneration arrangements allows the Company to attract, retain and motivate the exceptional individuals required to continue to enhance shareholder value. Base salaries will be set accordingly, with a significant proportion of executive directors' remuneration performance-related so that appropriate levels of reward are available for outstanding performance. In addition, the Committee is, at all times, mindful of remuneration practices in other relevant companies.

To achieve this, the remuneration package comprises:

- fixed elements: comprising basic salary, benefits and pensions; and
- performance related elements: comprising short-term performance related cash and deferred share bonuses and long-term incentive arrangements satisfied by the award of shares.

It is the Committee's policy that the performance related elements of the package should equate to around 60% of total remuneration for the executive directors based on an on-target, expected value approach to valuing the package.

The Committee believes that these performance related incentive arrangements provide rewards which reflect an appropriate balance between individual and Group performance and align the rewards to executive directors with the long-term interest of shareholders. Share-based awards are satisfied by the use of existing shares held by an Employee Benefit Trust.

# Directors' Remuneration Report

The details of individual components of the remuneration package and service contracts are as follows:

## Basic salary and benefits

Basic salary is a fixed cash sum payable monthly. The basic salary and benefits are reviewed annually against appropriate comparators and taking account of individual performance. Benefits principally comprise car allowances or the use of a motor car, fuel and private medical insurances.

## Pensions

The pension contributions are amounts equal to 25% of basic salary.

## Current Enterprise Inns Incentive Plans (the 'Plans')

For the year in review the Company had the following relevant Plans:

- at the Annual General Meeting held on 24 January 2002 an ordinary resolution was passed adopting the Enterprise Inns Incentive Plan 2002 ('the 2002 Plan'). The 2002 Plan provided for participants to earn non-pensionable cash bonuses and short-term and long-term share incentives; and
- at the Annual General Meeting held on 20 January 2005 ordinary resolutions were passed adopting the Enterprise Inns 2005 Annual Bonus Plan and the Enterprise Inns 2005 Long Term Incentive Plan ('the 2005 Plan').

The 2005 Plan has replaced the 2002 Plan and no further awards will be made except under the 2005 Plan.

Further details of the Plans are set out below:

## Short-term share incentives under the 2002 Plan

Under the terms of the 2002 Plan, the short-term incentive depended upon achievement of annual growth in adjusted EPS measured against RPI. There was a one year performance period for awards. No short-term award was made unless adjusted EPS growth exceeded RPI by at least 2.5% over the performance period. To achieve the maximum award of 20% of salary, adjusted EPS growth must have exceeded RPI by 15%. Awards between the minimum and maximum limits were calculated on a straight-line basis pro rata to the growth in adjusted EPS between the minimum and maximum targets. Short-term incentives may not ordinarily be exercised for 36 months after the end of the performance criteria period and then remain exercisable for a further period of 72 months.

## Short-term cash and share incentives under the 2005 Plan

Under the terms of the 2005 Plan executive directors are eligible to participate in an annual cash bonus scheme as determined by the Committee. The maximum award level under the 2005 Plan for the Chief Executive is 100% of salary. For the other executive directors the maximum award level is 75% of salary. Awards under the 2005 Plan are subject to demanding Company performance targets such that no less than 75% of an executive's bonus will be subject to a sliding scale of challenging annual adjusted EPS growth targets, with no more than 25% subject to challenging personal targets. 60% of any bonus earned will be paid in cash, with the remaining 40% deferred into shares (a deferred share award). Deferred share awards may not ordinarily be exercised for 36 months after the end of the performance criteria period and then remain exercisable for a further period of 6 months. Awards between the minimum and maximum limits are calculated on a straight-line basis pro rata to the growth in adjusted EPS between the minimum and maximum targets.

The cash bonus awards for the year are shown in the remuneration table on page 33.

## Long-term share incentives under the 2002 Plan

Under the 2002 Plan, awards of ordinary shares were made to participants upon achievement of compound growth in adjusted EPS measured against RPI over 3 years. To qualify for any award, adjusted EPS growth must have exceeded RPI over a three year period by 5% compound (15.8% simple), and to qualify for the maximum award of 100% of salary (averaged over a three year period), adjusted EPS growth must have exceeded RPI over a three year period by 20% compound (72.8% simple). Awards between the minimum and maximum limits are calculated on a straight-line basis pro rata to the growth in adjusted EPS between the minimum and maximum targets. Long-term incentives may not ordinarily be exercised until 24 months after the end of the performance criteria period and then remain exercisable for a further period of 108 months.

# Directors' Remuneration Report

## Long-term share incentives under the 2005 Plan

Under the 2005 Plan, long-term incentive awards have two elements:

- an award of Performance Shares (worth up to 150% of salary each year); and
- an award of Matching Shares linked to the co-investment of up to 25% of salary in 'Investment Shares', which are then matched on a 2:1 basis.

Shares that can count as Investment Shares are:

- shares subject to the Deferred Share Award under the 2005 Plan; and
- shares acquired by participants using their cash bonus or other funds, up to the 25% of salary maximum.

Performance Share and Matching Share awards vest subject to the satisfaction of a sliding scale of average compound annual adjusted EPS growth targets and the Company's TSR performance against the FTSE 100. More specifically, for awards made under the 2005 Plan in the past and (it is currently intended) in the future, one-half of an award will be subject to a performance condition based on average compound annual adjusted EPS growth. This EPS based condition will measure the Company's average compound annual adjusted EPS growth by comparing the Company's adjusted EPS for the year prior to the date of grant (the 'base year') with the adjusted EPS for the third financial year following the base year, such that awards will vest as follows:

Average compound annual adjusted EPS growth	Percentage of relevant portion of Performance Award that vests	Level of match under the relevant portion of Matching Award (Matching Award Shares: Investment Shares)
Less than 7%	0%	0:1
7%	20%	0.4:1
15%	100%	2:1

Straight-line vesting will occur if average compound annual adjusted EPS growth is between 7 per cent and 15 per cent.

The remaining half of the award will be subject to a TSR condition which compares the Company's TSR performance over the three year period commencing on the date of grant with the TSR of the FTSE 100 (as at the date of grant) as follows:

Company's TSR ranking v. the FTSE 100	Percentage of relevant portion of Performance Award that vests	Level of match under the relevant portion of Matching Award (Matching Award Shares: Investment Shares)
Below median	0%	0:1
Median	20%	0.4:1
Upper quintile	100%	2:1

Straight-line vesting will occur if the Company's TSR ranking is between median and upper quintile.

All awards vest in three equal tranches on the third, fourth and fifth anniversaries of grant and remain exercisable for a further period of 6 months.

TSR will be calculated by averaging the Net Return Index of each company over the six month period prior to grant and vesting, unless the Committee determines that a shorter or longer period is a more appropriate way of ensuring that the condition constitutes a fair measure of the Company's TSR performance over the period.

# Directors' Remuneration Report

In addition, irrespective of the Company's TSR performance, no part of this portion of the award will vest unless the Company's adjusted EPS grows by at least 10% over the performance period, unless the Committee believes that it is inappropriate to apply this underpin.

For the avoidance of doubt, if both the threshold TSR hurdle of median performance against the FTSE 100 and the threshold adjusted EPS growth hurdle of 7% average compound annual adjusted growth are met, 20% of the total award will vest.

The Committee believes that these performance conditions are appropriate for the following reasons:

- the adjusted EPS growth targets will encourage the executive team to deliver substantial annual adjusted EPS growth over the three year performance period; and
- the TSR targets will require the Company to deliver returns to shareholders in excess of its FTSE 100 peers.

The Committee will, however, review the appropriateness of these performance conditions (and the operation of the 2005 Plan as a whole) on a regular basis in light of the Company's circumstances and prospects. The Committee will seek independent advice to determine the extent to which the adjusted EPS growth and TSR targets are met.

In particular, the Committee will seek independent advice as to how to determine the extent to which EPS-based performance targets have been met in light of the transition to International Financial Reporting Standards, with the Committee's objective of achieving a consistent measurement of performance.

## Remuneration Policy – Non-executive directors

The fees for non-executive directors are determined by the Board within the limits in the Articles of Association. The non-executive directors are not involved in any discussions or decision about their own remuneration.

The remuneration of the non-executive directors takes the form solely of fees, which are set by the Board having taken advice on appropriate levels in light of the time commitment and responsibilities of each individual. The Chairman's fee is approved by the Board on the recommendation of the Committee.

## Service contracts

The Company's policy is for all executive directors to have a service contract of no fixed term under which they are entitled to receive twelve months' notice of termination. There are no special provisions in the executive directors' contracts for compensation in the event of loss of office. The Committee would consider the circumstances of any individual case of early termination and would determine compensation payments accordingly. A fair but robust principle of mitigation would be applied to the payment of compensation in the context of professional advice received as to contractual entitlement.

The service contracts of the executive directors include the following terms:

Executive Directors	Date of Agreement	Effective Date	Notice Period
G E Tuppen	25 October 1995	1 October 1995	12 months
D C George	25 October 1995	1 October 1995	12 months
W S Townsend	31 October 2000	1 October 2000	12 months

The terms of appointment for Mr H V Reid, Mr A J Stewart, Mr D A Harding and Mrs S E Murray reflect best practice. Their respective appointments shall continue on an annual basis from AGM to AGM, subject to re-election, when applicable.

# Directors' Remuneration Report

In respect of the Chairman and non-executive directors, the dates on which their appointments took effect and the current expiry dates are as follows:

Chairman and non-executive directors	Date of Appointment	Expiry Date
H V Reid	21 January 1997	Terminable on 12 months' notice
A J Stewart	29 May 2001	Terminable on 6 months' notice
D A Harding	6 November 2003	Terminable on 6 months' notice
S E Murray	3 November 2004	Terminable on 6 months' notice

Biographical details of all directors can be found on pages 13 and 14.

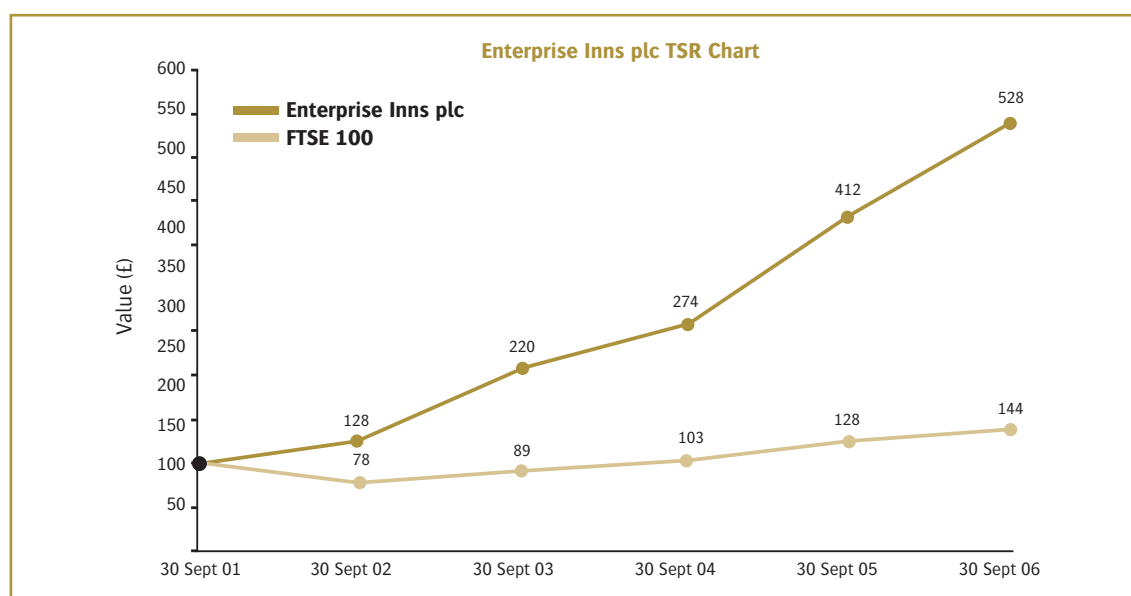
## Forward-looking statement

The Committee will keep the existing remuneration arrangements, as detailed in this report, under review during the next year to ensure that the Company's reward programmes remain competitive and provide appropriate incentives.

## Performance graph

The graph below shows the TSR, in terms of the change in value (with dividends re-invested) of an initial investment of £100 on 30 September 2001 in a holding of the Company's shares against the corresponding TSR in a hypothetical holding of shares in the companies represented in the FTSE 100 index.

The FTSE 100 Index was selected as it represents a broad equity market index in which the Company is a constituent member. The graph shows that the Company has outperformed the index over this period.



# Directors' Remuneration Report

## Information subject to audit:

### Directors' remuneration

The remuneration of the Chairman, the executive directors and fees payable to the non-executive directors are as follows:

<b>£000</b>					<b>Total</b>	<b>Total</b>
<b>Chairman and non-executive directors</b>	Fees	Basic salary	Benefits (a)	Performance related bonus (b)	<b>2006</b>	<b>2005</b>
H V Reid	180	—	—	—	<b>180</b>	160
A J Stewart	50	—	—	—	<b>50</b>	43
D A Harding	45	—	—	—	<b>45</b>	40
S E Murray	40	—	—	—	<b>40</b>	32
M F Garner (retired 20/01/05)	—	—	—	—	—	13
<b>Executive directors</b>						
G E Tuppen	—	525	23	315	<b>863</b>	789
D C George	—	315	20	142	<b>477</b>	438
G W Harrison (c)	—	270	23	122	<b>415</b>	376
W S Townsend	—	270	20	118	<b>408</b>	364
	<b>315</b>	<b>1,380</b>	<b>86</b>	<b>697</b>	<b>2,478</b>	<b>2,255</b>

- (a) Benefits include car allowances or the use of a motor car, fuel, private medical insurances and professional fees.
- (b) The Chairman and non-executive directors are not eligible for performance related bonuses or share awards under the Plans. The bonus disclosed relates to the cash bonus awarded under the 2005 Plan and earned in the year ended 30 September 2006. The performance related and deferred bonus payment reflects another year of excellent performance by the Company. Details of the share awards made under the Plans are shown separately in this report.
- (c) G W Harrison retired from the Board on 30 September 2006. On 16 October 2006 the Company entered into a new employment contract with Mr Harrison for a term of two years at a salary of £10,000 per annum.

The pension contributions paid to the directors' individual defined contribution schemes are shown below:

	<b>2006</b>	2005
	<b>£000</b>	£000
Executive directors		
G E Tuppen	<b>131</b>	120
D C George	<b>79</b>	72
G W Harrison	<b>68</b>	63
W S Townsend	<b>68</b>	60
	<b>346</b>	315

# Directors' Remuneration Report

## Interest in options

The executive directors and other employees are able to acquire shares in the Company by participating in the Enterprise Inns Savings Related Share Options Scheme and options granted under this scheme, together with details of options exercised during the year, are set out in the table below. There are no performance conditions restricting the exercise of options held under this scheme (reflecting the relevant legislation).

Name	Exercise price £	At 1 Oct 2005	Exercised	Lapsed	Granted	At 30 Sept 2006	Market price at exercise £	Aggregate gain £000
G E Tuppen	1.245	13,484	(13,484)	—	—	—	9.265	108
	7.07	—	—	—	2,277	<b>2,277(ii)</b>	—	—
		13,484	(13,484)	—	2,277	<b>2,277</b>		108
D C George	1.245	13,484	(13,484)	—	—	—	9.265	108
	7.07	—	—	—	2,277	<b>2,277(ii)</b>	—	—
		13,484	(13,484)	—	2,277	<b>2,277</b>		108
G W Harrison	1.245	10,788	(10,788)	—	—	—	9.265	86
	2.320	1,414	—	(1,414)	—	—	—	—
		12,202	(10,788)	(1,414)	—	—		86
W S Townsend	1.245	5,392	(5,392)	—	—	—	9.265	43
	2.095	4,732	—	—	—	<b>4,732(i)</b>	—	—
	7.07	—	—	—	910	<b>910(ii)</b>	—	—
		10,124	(5,392)	—	910	<b>5,642</b>		43

## Notes:

(i) Exercise period 01/02/2007 – 01/08/2007.

(ii) Exercise period 01/02/2011 – 01/08/2011.



# Directors' Remuneration Report

## Short-term share incentives

Details of short-term awards made under the 2002 and 2005 Plans, together with details of awards exercised during the year, are set out in the table below:

	Date of grant	At 1 Oct 2005	Granted	Exercised	At 30 Sept 2006	Market price at exercise £	Aggregate gain £000	Market value £000 (iii)	Exercisable From	To
<b>G E Tuppen</b>										
2002 Plan	20/12/2002	16,902	—	(16,902)	—	10.355	175	—	—	—
2002 Plan	22/12/2003	12,049(i)	—	—	<b>12,049</b>	—	—	127	1/10/2007	22/12/2013
2005 Plan	01/12/2004	21,805(ii)	—	—	<b>21,805</b>	—	—	230	17/11/2008	17/05/2009
2005 Plan	24/01/2006	—	19,905(iv)	—	<b>19,905</b>	—	—	210(v)	14/11/2009	14/05/2010
		50,756	19,905	(16,902)	<b>53,759</b>		175			
<b>D C George</b>										
2002 Plan	20/12/2002	10,142	—	(10,142)	—	10.355	105	—	—	—
2002 Plan	22/12/2003	7,229(i)	—	—	<b>7,229</b>	—	—	76	1/10/2007	22/12/2013
2005 Plan	01/12/2004	9,812(ii)	—	—	<b>9,812</b>	—	—	104	17/11/2008	17/05/2009
2005 Plan	24/01/2006	—	8,957(iv)	—	<b>8,957</b>	—	—	95(v)	14/11/2009	14/05/2010
		27,183	8,957	(10,142)	<b>25,998</b>		105			
<b>G W Harrison</b>										
2002 Plan	20/12/2002	9,296	—	(9,296)	—	10.355	96	—	—	—
2002 Plan	22/12/2003	6,627(i)	—	—	<b>6,627</b>	—	—	70	1/10/2006	30/09/2008
2005 Plan	01/12/2004	8,128(ii)	—	—	<b>8,128</b>	—	—	86	1/10/2006	30/09/2008
2005 Plan	24/01/2006	—	7,678(iv)	—	<b>7,678</b>	—	—	81(v)	1/10/2006	30/09/2008
		24,051	7,678	(9,296)	<b>22,433</b>		96			
<b>W S Townsend</b>										
2002 Plan	20/12/2002	8,028	—	(8,028)	—	10.355	83	—	—	—
2002 Plan	22/12/2003	5,849(i)	—	—	<b>5,849</b>	—	—	62	1/10/2007	22/12/2013
2005 Plan	01/12/2004	7,959(ii)	—	—	<b>7,959</b>	—	—	84	17/11/2008	17/05/2009
2005 Plan	24/01/2006	—	7,472(iv)	—	<b>7,472</b>	—	—	79(v)	14/11/2009	14/05/2010
		21,836	7,472	(8,028)	<b>21,280</b>		83			

## Notes:

- (i) These shares have vested and have been used to count towards the participant's co-investment in Investment Shares for the purposes of calculating the Matching Share award for the financial year 2004/05 under the 2005 Plan, details of which are set out below.
- (ii) These shares have vested and have been used to count towards the participant's co-investment in Investment Shares for the purposes of calculating the Matching Share award for the financial year 2005/06 under the 2005 Plan, details of which are set out below.
- (iii) Market value is calculated using the mid market price of the ordinary shares at 30 September 2006 being £10.55.

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# Directors' Remuneration Report

- (iv) The share price at which the number of deferred shares granted under the STIP scheme is calculated will not be confirmed until after the date of the approval of the accounts. The number of STIP deferred shares granted during the year is therefore estimated using the mid market price of the ordinary shares at 30 September 2006 being £10.55.
- (v) Market value is based on a percentage of basic salary earned as a result of achievement of performance objectives for the year 2005/06. These awards have become unconditional since the end of the financial year. It is intended that these awards will be used towards the participant's co-investment in Investment Shares for the purposes of calculating the Matching Share award for the financial year 2006/07 under the 2005 Plan, details of which are set out below.

£1 in aggregate is payable by the participants on the exercise of each year's short-term incentive award.

## Long-term share incentives

Details of long-term awards made under the 2002 and 2005 Plans, together with details of awards exercised during the year, are set out in the table below:

	Date of grant	At 1 Oct 2005	Awarded Performance Shares	Awarded Matching Shares	Exercised	Lapsed	At 30 Sept 2006	Market price at exercise £	Aggregate gain £000	Market value £000 (v)	Exercisable From	To
<b>G E Tuppen</b>												
2002 Plan	16/04/2002	173,152	—	—	(173,152)	—	—	10.355	1,793	—	—	—
2002 Plan	20/12/2002	157,211	—	—	—	—	<b>157,211</b>	—	—	1,659	1/10/2007	20/12/2016
2002 Plan	22/12/2003(i)	104,735	—	—	—	—	<b>104,735</b>	—	—	1,105	1/10/2008	22/12/2017
2005 Plan	04/02/2005(ii)	140,370	—	—	—	—	<b>140,370</b>	—	—	1,481	4/02/2008	4/02/2010
2005 Plan	19/12/2005(iii)	—	89,437	29,812	—	—	<b>119,249</b>	—	—	1,258	19/12/2008	19/12/2010
		575,468	89,437	29,812	(173,152)	—	<b>521,565</b>		1,793			
<b>D C George</b>												
2002 Plan	16/04/2002	103,697	—	—	(103,697)	—	—	10.355	1,074	—	—	—
2002 Plan	20/12/2002	94,327	—	—	—	—	<b>94,327</b>	—	—	995	1/10/2007	20/12/2016
2002 Plan	22/12/2003(i)	62,841	—	—	—	—	<b>62,841</b>	—	—	663	1/10/2008	22/12/2017
2005 Plan	04/02/2005(ii)	84,221	—	—	—	—	<b>84,221</b>	—	—	889	4/02/2008	4/02/2010
2005 Plan	19/12/2005(iii)	—	53,662	17,887	—	—	<b>71,549</b>	—	—	755	19/12/2008	19/12/2010
		345,086	53,662	17,887	(103,697)	—	<b>312,938</b>		1,074			
<b>G W Harrison</b>												
2002 Plan	16/04/2002	94,265	—	—	(94,265)	—	—	10.355	976	—	—	—
2002 Plan	20/12/2002	84,332	—	—	—	—	<b>84,332</b>	—	—	890	1/10/2006	30/09/2008
2002 Plan	22/12/2003(i)	54,952	—	—	—	—	<b>54,952</b>	—	—	580	1/10/2006	30/09/2008
2005 Plan	04/02/2005(ii)	73,693	—	—	—	(24,565)(iv)	<b>49,128</b>	—	—	518	1/10/2006	30/09/2008
2005 Plan	19/12/2005(iii)	—	45,996	15,332	—	(40,885)(iv)	<b>20,443</b>	—	—	216	1/10/2006	30/09/2008
		307,242	45,996	15,332	(94,265)	(65,450)	<b>208,855</b>		976			
<b>W S Townsend</b>												
2002 Plan	16/04/2002	82,269	—	—	(82,269)	—	—	10.355	852	—	—	—
2002 Plan	20/12/2002	77,064	—	—	—	—	<b>77,064</b>	—	—	813	1/10/2007	20/12/2016
2002 Plan	22/12/2003(i)	52,692	—	—	—	—	<b>52,692</b>	—	—	556	1/10/2008	22/12/2017
2005 Plan	04/02/2005(ii)	70,185	—	—	—	—	<b>70,185</b>	—	—	740	4/02/2008	4/02/2010
2005 Plan	19/12/2005(iii)	—	45,996	15,332	—	—	<b>61,328</b>	—	—	647	19/12/2008	19/12/2010
		282,210	45,996	15,332	(82,269)	—	<b>261,269</b>		852			

# Directors' Remuneration Report

## Notes:

- (i) The award is calculated using average salary paid to participants between 1 October 2003 and 30 September 2006. Market value of each share awarded is taken at the start of the incentive period (461.8 pence). As compound adjusted EPS growth over the performance criteria period has exceeded the target of 15% per annum which is the level for the achievement of the maximum award under the scheme, these awards will vest and the number of shares to be awarded are shown above subject to approval by the Remuneration Committee.
- (ii) The award is calculated at a maximum of 150% of salary at the start of the performance period (1 October 2005 to 30 September 2008). Market value is calculated on the average share price over the 5 dealing days following announcement of the results for the financial year 2003/04 (683.9 pence).
- (iii) The award is calculated at a maximum of 150% of salary at the start of the performance period (1 October 2005 to 30 September 2008). Market value is calculated on the average share price over the 5 dealing days following announcement of the results for the financial year 2004/05 (880.5 pence).
- (iv) G W Harrison retired on 30 September 2006 and the awards shown are based on a pro rata adjustment of the shares awarded over the reduced performance period.
- (v) Market value is calculated using the mid market price of the ordinary shares at 30 September 2006 being £10.55 per share.

The high and low share prices during the year were £10.70 and £7.735 pence respectively.

The fair value of short-term and long-term incentive plans recognised as a cost in the Income Statement during the year is shown in note 9 to the accounts on page 52.

Shareholders are invited to approve this report at the Annual General Meeting on 16 January 2007, details of which are set out on pages 121 to 127.

On behalf of the Board

## A J Stewart

Chairman of the Remuneration Committee

21 November 2006

# Group Income Statement

for the year ended 30 September 2006

	Notes	2006			2005 (Restated)#		
		Pre- exceptional items £m	Exceptional items £m	Total £m	Pre- exceptional items £m	Exceptional items £m	Total £m
Revenue	2	970	—	970	952	—	952
Cost of sales	3	(387)	—	(387)	(385)	—	(385)
<b>Gross profit</b>		<b>583</b>	<b>—</b>	<b>583</b>	567	—	567
Administrative expenses		(36)	(2)	(38)	(39)	—	(39)
<b>EBITDA†</b>	4	<b>547</b>	<b>(2)</b>	<b>545</b>	528	—	528
Depreciation and amortisation		(8)	—	(8)	(10)	—	(10)
<b>Operating profit</b>	5	<b>539</b>	<b>(2)</b>	<b>537</b>	518	—	518
Net profit on sale of property, plant and equipment	7	—	67	67	—	14	14
Movements from revaluation of pub estate	8	—	(2)	(2)	—	(4)	(4)
Interest receivable		6	—	6	9	—	9
Interest payable	10	(230)	—	(230)	(237)	—	(237)
Write off of unamortised issue costs	10	—	(3)	(3)	—	(5)	(5)
Movement in fair value of interest rate swaps	10	—	40	40	—	(20)	(20)
Total finance costs	10	(230)	37	(193)	(237)	(25)	(262)
<b>Profit before tax</b>		<b>315</b>	<b>100</b>	<b>415</b>	290	(15)	275
Taxation	11	(95)	5	(90)	(90)	24	(66)
<b>Profit after tax attributable to members of the parent company</b>		<b>220</b>	<b>105</b>	<b>325</b>	200	9	209
<b>Earnings per share</b>							
Basic	12			100.9p			61.0p
Basic diluted	12			100.1p			60.3p
Adjusted *	12	68.3p			58.4p		
Adjusted diluted *	12	67.8p			57.7p		
<b>Dividends</b>							
Dividends paid per share in respect of the year	13			9.0p			5.6p
Dividends proposed per share in respect of the year	13			18.0p			12.4p
				<b>27.0p</b>			<b>18.0p</b>

# See note 1.

† Earnings before interest, tax, depreciation and amortisation

\* Excludes exceptional items

# Group Statement of Recognised Income and Expense

for the year ended 30 September 2006

	<b>2006</b>	Re-stated#
	<b>£m</b>	2005 £m
Unrealised surplus on revaluation of licensed estate	<b>323</b>	273
Movement in deferred tax liability related to revaluation of licensed estate	<b>(91)</b>	(74)
Deferred tax related to share schemes recognised directly in equity	<b>5</b>	7
Write-down of non-current assets held for sale (see note 1)	—	(4)
Actuarial gain on defined benefit pension scheme	—	1
Net income recognised directly in equity	<b>237</b>	203
Profit for the year	<b>325</b>	209
Total recognised income and expense for the year attributable to members of the parent company	<b>562</b>	412

# See note 1.

# Group Balance Sheet

at 30 September 2006

	Notes	2006 £m	Re-stated# 2005 £m
<b>Non-current assets</b>			
Goodwill	14	417	417
Investments	15	2	—
Intangible assets: operating lease premiums	16	24	27
Property, plant and equipment	17	5,343	5,157
Financial assets	22	1	—
		<b>5,787</b>	5,601
<b>Current assets</b>			
Assets held for sale	18	6	7
Trade and other receivables	19	94	81
Cash		111	96
Financial assets	22	1	—
		<b>212</b>	184
Non-current assets held for sale	20	10	36
<b>Total assets</b>		<b>6,009</b>	5,821
<b>Current liabilities</b>			
Trade and other payables	21	(210)	(217)
Current tax payable		(52)	(46)
Financial liabilities	22	(54)	(122)
Provisions	24	(1)	(1)
		<b>(317)</b>	(386)
<b>Non-current liabilities</b>			
Financial liabilities	22	(3,316)	(3,260)
Accruals and deferred income		(4)	(5)
Provisions	24	(4)	(7)
Deferred tax	25	(692)	(590)
		<b>(4,016)</b>	(3,862)
<b>Total liabilities</b>		<b>(4,333)</b>	(4,248)
<b>Net assets</b>		<b>1,676</b>	1,573
<b>Equity</b>			
Called up share capital	27	16	17
Share premium account	29	486	486
Revaluation reserve	29	845	667
Capital redemption reserve	29	9	8
Merger reserve	29	77	77
Treasury share reserve	29	(227)	—
Other reserve	29	(42)	(56)
Profit and loss account	29	512	374
<b>Enterprise Inns shareholders' equity</b>	29	<b>1,676</b>	1,573

# See note 1.

Approved by the Board on 21 November 2006 and signed on its behalf by:

**G E Tuppen**  
**D C George**

# Group Cash Flow Statement

for the year ended 30 September 2006

	2006 £m	2005 £m
<b>Cash flow from operating activities</b>		
Operating profit	537	518
Depreciation and amortisation	8	10
Share-based expense recognised in profit	3	3
(Increase)/decrease in receivables	(10)	5
Decrease in payables	(2)	(12)
(Decrease)/increase in provisions	(3)	2
Decrease/(increase) in current assets held for sale	1	(2)
	<b>534</b>	524
Tax paid	(69)	(53)
<b>Net cash flows from operating activities</b>	<b>465</b>	471
<b>Cash flows from investing activities</b>		
Payments to acquire public houses	(80)	(14)
Payments made on improvements to public houses	(54)	(49)
Payments to acquire other property, plant and equipment	(7)	(1)
Receipts from sale of property, plant and equipment	362	47
<b>Net cash flows from investing activities</b>	<b>221</b>	(17)
<b>Cash flows from financing activities</b>		
Interest paid	(234)	(244)
Interest received	7	9
Issue costs of long-term loans	(4)	(2)
Equity dividends paid	(70)	(48)
Payments to acquire shares held in employee benefit trust	(17)	(23)
Payments to acquire own shares	(388)	—
Receipts from exercise of share options	5	3
Restructuring of interest rate swaps	(30)	—
Debt due beyond one year — new long-term loans	602	771
Debt due beyond one year — repayment of long-term loans	(542)	(971)
<b>Net cash flows from financing activities</b>	<b>(671)</b>	(505)
<b>Net increase/(decrease) in cash</b>	<b>15</b>	(51)
Cash at 1 October	96	147
<b>Cash at 30 September</b>	<b>111</b>	96

# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies

The consolidated financial statements of Enterprise Inns plc for the year ended 30 September 2006 were authorised for issue by the Board on 21 November 2006. Enterprise Inns plc is a public limited company incorporated and registered in England. The Company's ordinary shares are traded on the London Stock Exchange.

### Basis of preparation

The accounts are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

This is the first year in which the Group has prepared its Group financial statements under IFRS and the comparatives have been restated from UK GAAP accordingly. The Group issued a press release on 4 May 2006 which detailed the impact of transition to IFRS and included detailed reconciliations from UK GAAP to IFRS of the 2005 Income Statement and Balance Sheet. These reconciliations are included in note 33 along with a narrative explanation of the adjustments made.

Since the publication of the Restatement of Financial Information under IFRS released in May 2006, the Group has amended the 2005 Income Statement and Balance Sheet in respect of the application of IFRS 5 'Non-current assets held for sale and discontinued operations'. This amendment relates to the treatment of the write-down of property on classification as 'held for sale' under IFRS 5. The write-down to fair value less costs to sell is first recognised in the Revaluation Reserve, to the extent of any existing surplus for the asset. It is then recognised in the Income Statement within the line 'movements from revaluation of pub estate'. Previously, the entire write-down was recognised in the Income Statement within the line 'Net profit on sale of property, plant and equipment'. The impact of this amendment is as follows:

- Net profit on sale of property has been increased by £11 million being the amount previously recognised on write-down of pubs identified for sale.
- The first £4 million of these write-downs has been recognised in the Revaluation Reserve against surpluses that existed for the individual pubs concerned.
- The remaining £7 million of write downs has been recognised within the line 'movement from revaluation of pub estate', reducing the previously reported credit to a £4 million charge.
- Profit before tax has been increased by £4 million, being the combination of the amendments above.
- The tax credit within exceptional items has been reduced by £1 million being the deferred tax impact of the amendments made.
- Profit after tax is therefore increased by £3 million being the post-tax impact of the amendments made.

In addition to the above amendment, the 2005 Balance Sheet has been reclassified in respect of the application of IAS 1 'Presentation of financial statements' and IAS 39 'Financial instruments: recognition and measurement'. The interaction of these two standards means that all derivatives that are not part of a designated and effective hedging relationship should be classified as current assets or liabilities. The Group has therefore reclassified the fair value of all interest swaps as current liabilities in 2005. Previously, the fair value of the swaps was allocated between 'current' and 'non-current' liabilities. £86m of fair value was previously classified as non-current and this amount has therefore been re-classified as current.

Consolidated accounts are drawn up to 30 September each year and adjustments are made to the accounts of the subsidiaries where necessary to bring the accounting policies used in line with those used by the Group.



# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### Goodwill

Goodwill represents the excess of consideration over the fair value of identifiable assets and liabilities acquired in a business combination. Goodwill is stated at cost less any impairment. Goodwill is not amortised but is tested for impairment annually, or more frequently where events or changes in circumstances indicate that the carrying value may be impaired. On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of profit or loss on sale.

Goodwill arising on acquisitions prior to 1 October 1998 was written off against reserves and has not been reinstated. Any such goodwill is not included in determining any profit or loss on disposal.

### Property, plant and equipment

Licensed land and buildings are held at their fair value and landlords' fixtures and fittings and other assets are held at cost. The Group's licensed land and buildings, except for those non-current assets held for sale, is revalued each year by professionally qualified external valuers and employees who are professionally qualified to carry out such valuations. Surpluses arising from the revaluation exercise are taken directly to the revaluation reserve except where they reverse a revaluation decrease relating to the same asset which has previously been recognised as an expense in the Income Statement. Any deficit arising from the revaluation exercise is taken directly to the revaluation reserve to the extent that there is a surplus in place relating to the same asset. Any further decrease in value is recognised in the Income Statement as an expense.

Freehold land is not depreciated. Freehold buildings are depreciated so as to write off the difference between their carrying value and residual value over their useful economic life of 50 years. Residual value is reviewed at least at each financial year end and there is no depreciable amount if residual value is the same as, or exceeds, book value.

Landlords' fixtures and fittings are held at cost less accumulated depreciation. The useful economic life of additions to landlords' fixtures and fittings has been calculated at 30 years. Depreciation is charged on a straight-line basis to write off the total cost less residual value over their useful economic life.

Properties held under finance leases are depreciated on a straight-line basis over the lower of the remaining lease term and their useful economic life of 50 years. Depreciation is provided on other categories of property, plant and equipment over 3 to 50 years on a straight-line basis to residual value.

Profits or losses on disposal of property, plant and equipment are calculated as the difference between the net sales proceeds and the carrying amount of the asset at the date of disposal.

Property, plant and equipment are reviewed annually for indications of impairment. Where any indications are identified, assets are assessed fully for impairment. Impairment occurs where the recoverable amount of the asset is less than its carrying amount. Recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Any impairment loss is treated as a revaluation decrease to the extent that a surplus exists for the same asset, and thereafter as an expense in the Income Statement.

# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### Leases

Leases where the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Pubs acquired under finance leases are capitalised at the lower of their fair value and the present value of future lease payments. The corresponding liability is included in the balance sheet as a finance lease payable. Pubs held under finance leases are revalued along with the freehold estate on an annual basis. Lease payments are apportioned between finance charges and reduction of the lease payable so as to obtain a constant rate of interest on the remaining balance of the liability. Finance charges are charged as an expense to the Income Statement.

Leases where substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Rentals paid under operating leases are charged on a straight-line basis to the Income Statement over the lease term. The fair value attributed to pubs acquired as part of business combinations that are held as operating leases are classified in the balance sheet as 'intangible assets: lease premiums' within non-current assets and are amortised over the lease term.

### Non-current assets held for sale

Non-current assets held for sale are held at the lower of their carrying value and expected sale proceeds, net of selling costs. Pubs and operating lease intangibles are classified as held for sale when they have been identified for disposal by the Group. They must be available for immediate sale in their present condition and the sale should be highly probable. These conditions are met when management are committed to the sale, the pub or lease is actively marketed and the sale is expected to occur within one year. Pubs held for sale are not depreciated and operating lease intangibles held for sale are not amortised.

### Current assets held for sale

Current assets held for sale comprises tenants' fixtures and fittings and are held at the lower of cost and net realisable value. Net realisable value is based on estimated selling price less further costs expected to be incurred on disposal.

### Repairs and Maintenance

Repairs and maintenance expenditure is charged to the Income Statement as incurred.

### Financial instruments

#### i) Cash and cash equivalents

Cash comprises cash at bank and in hand. Any short-term deposits with an original maturity date of three months or less are classified as cash equivalents.

#### ii) Borrowings

Borrowings which include bank borrowings, syndicated debt finance, debentures, secured bonds and securitised bonds are initially recognised at fair value and are subsequently measured at amortised cost. This method is used to ensure that the interest charge associated with the debt, combined with the amortisation of the issue costs, premiums and discounts, represents a constant percentage of the borrowings across the life of the instrument.

#### iii) Derivative financial instruments

The Group uses interest rate swaps to manage the exposure to changes in interest rates and these are classified as derivative financial instruments. Interest rate swaps are initially measured at fair value on acquisition and are subsequently restated to fair value at each reporting date. Any change in the fair value of the instruments is recognised in the Income Statement unless hedge accounting has been adopted. Hedge accounting is only adopted where, at the inception of the hedge, there is formal designation documentation of the hedging relationship and it meets the Group's risk management strategy for undertaking the hedge, and it is expected to be highly effective. Where hedge accounting is adopted for interest rate swaps, they are classified as cash flow hedges.

# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### iii) Derivative financial instruments (continued)

The portion of any change in the fair value of the hedging instrument used in a cash flow hedge which meets the conditions for hedge accounting and is determined to be an effective hedge, is recognised directly in equity. Changes in fair value relating to any ineffective portions are recognised in the Income Statement. Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gains or losses arising from changes in the fair value of the hedging instrument recognised in equity are kept in equity until the forecast transaction occurs. In the case of interest rate swaps, the 'forecast transaction' is the payment of interest.

### iv) Equity instruments

Equity instruments, being ordinary shares issued by the Company, are recorded at the fair value of the proceeds received, net of any direct issue costs. The nominal value of shares issued is recorded in Share Capital and the balance of the net proceeds is recorded in Share Premium.

### Net debt

Net debt is the total of all financial assets and liabilities less cash. Underlying net debt is amounts repayable to banks and other lenders, net of cash retained in the business.

### Taxation

The income tax expense comprises both the income tax payable based on taxable profits for the year and deferred tax. Deferred tax is provided using the balance sheet liability method in respect of temporary differences between the carrying value of assets and liabilities for accounting and tax purposes. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. No deferred tax is recognised if the taxable temporary difference arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Current tax assets and liabilities are offset where there is a legally enforceable right to set off the recognised amounts and the intention is to either settle on a net basis or realise the asset and liability simultaneously. Deferred tax assets and liabilities are offset where there is a legally enforceable right to set off current tax assets and liabilities and the assets and liabilities relate to taxes levied by the same tax authority which are intended to be settled net or simultaneously.

Both current and deferred tax are recognised in the Income Statement except when it relates to items recognised directly in equity, in which case the corresponding tax is also recognised in equity. Tax is calculated using tax rates enacted or substantively enacted at the balance sheet date.

### Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. If the effect is material, the amount of the provision is discounted using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The amount of the provision would therefore represent the present value of the expenditure expected to be required to settle the obligation.

### Pension obligations

The Group has both defined contribution and defined benefit pension arrangements. The cost of defined contribution payments made to employees' own pension plans is charged to the Income Statement as incurred.

# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### Pension obligations

The defined benefit scheme is now closed to new members and for the future accrual of benefits. The net amount recognised on the balance sheet comprises the difference between the present value of the scheme's liabilities and the fair value of the scheme's assets. This is determined annually by qualified actuaries using the projected unit credit method. Current service cost and past service cost are charged to operating profit. The net of the expected return on scheme assets and interest on scheme liabilities is recognised within finance income or finance costs. Actuarial gains and losses are recognised in full in the period in which they occur in the statement of recognised income and expense.

### Treasury shares

The cost of own shares held in employee benefit trusts and in treasury is deducted from shareholders' equity until the shares are cancelled, reissued or disposed of. Any proceeds received are also taken to shareholders' equity. No gain or loss is recognised in the Income Statement on the purchase, sale, issue or cancellation of own shares held.

### Revenue recognition

Revenue represents amounts receivable for goods and services provided in the normal course of business, net of discounts and VAT. Revenue is measured as the fair value of consideration received or receivable. Sales of beverages are recognised when these goods are delivered to our customers. Rents receivable are recognised on a straight-line basis over the life of the lease. Amusement machine royalties are recognised in the accounting period to which the income relates.

### Segmental reporting

A business segment is a distinguishable component of an entity that provides a product or service that is subject to risks and returns that are different to those of other segments. The Group has one business segment, being the operation of a leased and tenanted pub estate. The Group operates solely within the UK and therefore also has just one geographical segment.

### Share-based payments

The Group has applied the transitional provisions of IFRS 2 and applied its requirements to those awards granted after 7 November 2002 that were not vested at 1 January 2005.

The Group operates a number of equity-settled share-based payment schemes for employees. Share-based payments are measured at fair value at the date of award and this value is subsequently updated at each balance sheet date for management's best estimate of the effect of non-market based vesting conditions on the number of equity instruments that will ultimately vest. The fair value is recognised as an expense over the vesting period by calculating the cumulative expense and recognising the movement in the cumulative expense in the Income Statement. A corresponding entry is made to equity. The fair value of share options is measured using valuation models.

### Dividends

Final dividends are recognised as a liability when they have been approved by shareholders at the Annual General Meeting. Interim dividends are recognised when they are paid.

### Operating profit

Operating profit as referred to in the Income Statement is defined as being profit generated from normal trading activities before interest receivable, finance costs and taxation.

### Exceptional items

The Group has elected to classify certain items as exceptional and present them separately on the face of the Income Statement. Exceptional items are classified as those which are separately identified by virtue of their size or nature to allow a full understanding of the underlying performance of the Group and include the following:

# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### Exceptional administrative costs

The exceptional item shown within administrative costs relates to restructuring costs.

### Net profit on sale of property, plant and equipment

Net profit arising from the sale of property, plant and equipment.

### Movements from revaluation of pub estate

Under IFRS any revaluation that causes the book value of a pub to fall below historic cost will lead to a charge in the Income Statement. If that same pub later recovers in value so that its book value exceeds historic cost, the increase in value is credited to the Income Statement to the extent that a debit was previously recognised. Where pubs identified for disposal are written down to 'fair value less costs to sell', this write-down is also recognised in this line. Most of the impact of the annual revaluation exercise is accounted for in equity and recognised in the Statement of Recognised Income and Expense.

### Movement in fair value of interest rate swaps

Under IFRS the interest rate swaps are revalued to fair value at each Balance Sheet date and the movement is recognised in the Income Statement unless hedge accounting is adopted. The movement in the fair value of swaps where hedge accounting is not applied is shown as an exceptional item.

### Tax

Under IFRS, a deferred tax liability has been recognised on the balance sheet relating to the pub estate. On transition to IFRS, the Group elected to apply IFRS 3 retrospectively to acquisitions from 1 January 1999. This led to an increase in goodwill in respect of this deferred tax. As this pre-acquisition liability reduces due to capital gains indexation relief, a credit is recognised in the Income Statement. This has been classified as an exceptional tax item due to its size and because it does not relate to any income or expense recognised in the Income Statement in the same period. All other movements in respect of this deferred tax liability are accounted for in equity and recognised in the Statement of Recognised Income and Expense.

The tax effect of all other exceptional items is also included within the exceptional items column in the Income Statement.

### New standards and interpretations

The Group has elected to early adopt IFRS 7 'Financial Instruments: Disclosure' which is not yet mandatory for adoption:

During the year, a number of other new standards and interpretations were issued with an effective date after the date of these financial statements. The following standards which are relevant to the Group are not expected to have a material impact on the financial statements although the Amendment to IAS 1 may require some additional disclosure. The effective dates below represent the latest date that the Group will be required to implement the standard:

- Amendment to IAS 1 — Capital Disclosures — effective from 1 October 2007
- IFRIC 4 — Determining whether an arrangement constitutes a lease — effective from 1 October 2006
- IFRIC 8 — Scope of IFRS 2 - effective from 1 October 2006

### Use of accounting estimates and judgements

The Group makes estimates and assumptions during the preparation of the financial statements. Actual results may differ from these estimates under different assumptions and conditions. The estimates and assumptions that have the most significant effect on the amounts recognised in the financial statements are discussed below:

# Notes to the Group Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### a) Property, Plant and Equipment

Properties are valued annually at open market value in accordance with the Appraisal and Valuation Manual published by the Royal Institution of Chartered Surveyors ('RICS'). The valuation is based on market observations and estimates the amount that would be paid by a willing buyer to a willing seller in an arm's length transaction after proper marketing. Non-current assets held for sale are valued at their market value less any costs that may be incurred to sell the pub. Further information about the valuation of the pub estate is provided in note 17 of these accounts.

The Group estimates the useful economic life and residual value of property, plant and equipment (PPE) and these estimates influence the depreciation charged each year. For details of these estimates, see the detailed accounting policy for PPE.

### b) Testing goodwill for impairment

The Group annually tests whether goodwill has been impaired. The recoverable amount of the cash generating unit that the goodwill has been allocated to is determined based on value-in-use calculations which require estimating future cash flows and applying a suitable discount rate. Details of the tests and carrying value of the asset are shown in note 14.

### c) Valuation of interest rate swaps

The Group measures interest rate swaps at fair value at each balance sheet date. The swap valuation rates are derived from the mid point of the zero coupon prevailing at the close of business on the balance sheet date. The fair value represents the net present value of the difference between the projected cash flows at the swap contract rate and the valuation rate for the period from the balance sheet date to the contracted expiry date. The calculation therefore uses estimates of present values and future interest rates.

### d) Taxation

Judgement is required when determining the provision for taxes as the tax treatment of some transactions cannot be finally determined until a formal resolution has been reached with the tax authorities. Tax benefits are not recognised unless it is probable that the benefit will be obtained. Tax provisions are made if it is possible that a liability will arise. The Group reviews each significant tax liability or benefit to assess the appropriate accounting treatment.

### e) Other

The Group also makes estimations and judgements in the valuation of share-based payments and the pension liability. However, the value of these items is such that any variation in the estimates used is unlikely to have a significant effect on the amounts recognised in the financial statements.

## 2. Revenue

The Group operates in one segment, that of leased and tenanted pub operator in the UK.

Revenue is derived as follows:

	2006	2005
	£m	£m
Beer and cider sales	635	617
Wines, spirits and minerals sales	36	36
Rents receivable	270	269
Income from amusement and other machines	29	30
	<b>970</b>	<b>952</b>

# Notes to the Group Accounts

at 30 September 2006

## 3. Cost of sales

	2006 £m	2005 £m
Beer and cider cost of sales	349	343
Wines, spirits and minerals cost of sales	28	29
Leasehold charges	4	6
Repairs and maintenance	6	7
	<b>387</b>	<b>385</b>

## 4. EBITDA — impact of disposal of pubs to Admiral Taverns

On 6 September 2006, the Group disposed of 769 pubs to Admiral Taverns. The pubs disposed of to Admiral Taverns generated £28 million of EBITDA in the year ended 30 September 2006 (2005 — £31 million). An analysis of the impact of the disposal of pubs to Admiral Taverns on current and prior year EBITDA together with an analysis of the application of the sales proceeds is set out below:

	2006 £m	2005 £m
<b>Revenue</b>		
Beer and cider sales	33	36
Wines, spirits and minerals sales	2	2
Rents receivable	11	13
Income from amusement and other machines	3	3
	<b>49</b>	<b>54</b>
<b>Cost of sales</b>		
Beer and cider cost of sales	(17)	(19)
Wines, spirits and minerals cost of sales	(2)	(2)
Leasehold charges	(1)	(1)
Repairs and maintenance	(1)	(1)
	<b>(21)</b>	<b>(23)</b>
<b>Administrative expenses</b>	—	—
<b>EBITDA</b>	<b>28</b>	<b>31</b>

The disposal was made for cash consideration of £316 million which has been used to repay debt (including the cancellation of equivalent swaps) with the balance to be used for general corporate purposes including future acquisitions of pubs. In addition, the Group received £2 million of preference shares.

	£m
<b>Consideration</b>	
Cash	316
Preference shares	2
	<b>318</b>
<b>Use of funds</b>	
Repayment of floating rate debt (note 22)	262
Restructuring of interest rate swaps (note 22)	30
Preference share holding (note 15)	2
Cash held for general corporate purposes	24
	<b>318</b>

# Notes to the Group Accounts

at 30 September 2006

## 4. EBITDA — impact of disposal of pubs to Admiral Taverns (continued)

The assets disposed of had a total book value of £266 million and generated a total profit on disposal of £51 million. No tax is expected to be payable on this profit due to the application of capital gains roll over relief.

	Fixtures and fittings £m	Property, Plant and Equipment £m	Total £m
Consideration	2	316	318
Selling costs	—	(1)	(1)
Net consideration	2	315	317
Book value	(2)	(264)	(266)
Profit on disposal	—	51	51

## 5. Operating profit

Operating profit is stated after charging:

	2006 £m	2005 £m
<b>Depreciation</b>		
Relating to cost of sales	6	8
Relating to administrative expenses	1	1
	<b>7</b>	<b>9</b>
<b>Amortisation:</b>		
Relating to cost of sales	1	1
Depreciation and amortisation	<b>8</b>	<b>10</b>

## 6. Auditors' Remuneration

This note is shown rounded to the nearest thousand.

	2006 £000	2005 £000
Audit of the financial statements	282	237
Audit-related services	119	109
Other fees to auditors:		
Taxation services	189	163
Accounting advice in relation to share-based payment schemes	28	63
Company secretarial services*	8	46
Other services	—	4
	<b>626</b>	<b>622</b>

Audit-related services in 2005 and 2006 primarily relate to fees charged in respect of the transition to IFRS.

\* On 29 June 2006, Ernst & Young LLP sold their company secretarial business. As a result, at 30 September 2006, the Group no longer pays any remuneration to the auditor for these services.



# Notes to the Group Accounts

at 30 September 2006

## 7. Net profit on disposal of property, plant and equipment

	2006 £m	2005 £m
Profits on disposal of property, plant and equipment	97	20
Losses on disposal of property, plant and equipment	(30)	(6)
	<b>67</b>	<b>14</b>

There is no current tax expense associated with the profit on sale of property. A deferred tax charge of £19 million (2005 – £3 million) arises as a result of the disposal of these properties.

## 8. Movements on revaluation of pub estate

	2006 £m	2005 £m
Movements on revaluation of pub estate	1	3
Write-down of non-current assets held for sale to fair value less costs to sell	(3)	(7)
	<b>(2)</b>	<b>(4)</b>

There is no current tax expense associated with these movements. A deferred tax credit of £1m (2005 – £1 million) arises as a result of the revaluation and write down of these properties.

## 9. Staff costs

	2006 £m	2005 £m
Wages and salaries	24	26
Social security costs	3	3
Other pension costs	2	2
	<b>29</b>	<b>31</b>

Included in wages and salaries is a total expense relating to share-based payments of £3 million (2005 – £3 million). All of this expense arises from transactions accounted for as equity-settled share-based payments (see note 28).

Other pension costs represents payments made into employees' individual defined contribution plans.

The average monthly number of employees comprised:

	2006 No.	2005 No.
Operations staff	244	230
Administration staff	283	309
	<b>527</b>	<b>539</b>

# Notes to the Group Accounts

at 30 September 2006

## 9. Staff costs (continued)

Directors' emoluments are summarised below to the nearest £000 with full detail given in the Directors' Remuneration Report.

	<b>2006</b>	2005
	<b>£000</b>	£000
Directors emoluments*	<b>2,478</b>	2,255
Share-based payments†	<b>2,078</b>	1,509
Aggregate gains made on exercise of share options	<b>5,499</b>	3,602

\* comprises fees, salary, benefits and performance-related cash bonus.

† fair value of share-based payments charged to the Income Statement during the year.

## 10. Finance costs

	<b>2006</b>	2005
	<b>£m</b>	£m
Bank loans and overdrafts	<b>37</b>	40
Debentures/secured bonds/securitised bonds	<b>191</b>	193
Other interest payable and finance costs	<b>2</b>	4
Interest payable	<b>230</b>	237
Exceptional finance costs:		
Write-off of unamortised issue costs	<b>3</b>	5
Movement in fair value of interest rate swaps (note 22)	<b>(40)</b>	20
Total finance costs	<b>193</b>	262

The write-off of unamortised issue costs in 2005 and 2006 resulted from refinancing exercises. This write-off was classified as exceptional as it is not expected to occur every year and is not part of the cash outflow of servicing the Group's debt. The movement in fair value of interest rate swaps arises as a result of the revaluation of the swaps at the balance sheet date (see note 1). The total interest charge under the effective interest rate method (which excludes swap fair value movements) is £233 million (2005 – £242 million).

# Notes to the Group Accounts

at 30 September 2006

## 11. Taxation

### a) Total tax expense recognised in the Group Income Statement

	2006			2005		
	Pre- exceptional items £m	Exceptional items £m	Total £m	Pre- exceptional items £m	Exceptional items £m	Total £m
<b>Current tax</b>						
UK corporation tax	82	(1)	81	74	(1)	73
Adjustments in respect of prior years	(3)	—	(3)	(3)	—	(3)
Total current tax	79	(1)	78	71	(1)	70
<b>Deferred tax</b>						
Origination and reversal of temporary differences (note 11c)	16	(4)	12	19	(23)	(4)
Taxation (note 11b)	95	(5)	90	90	(24)	66

### b) Tax charge reconciliation

	2006			2005		
	Pre- exceptional items £m	Exceptional items £m	Total £m	Pre- exceptional items £m	Exceptional items £m	Total £m
Profit before tax	315	100	415	290	(15)	275
Profit on ordinary activities before tax at 30% (2005 — 30%)	94	30	124	87	(5)	82
<b>Effects of:</b>						
Expenses not deductible for tax purposes	4	—	4	3	—	3
Indexation on property disposals	—	(14)	(14)	—	—	—
Reduction in deferred tax liability due to indexation	—	(21)	(21)	—	(19)	(19)
Adjustments in respect of prior years	(3)	—	(3)	—	—	—
Total tax charge in the Income Statement	95	(5)	90	90	(24)	66

# Notes to the Group Accounts

at 30 September 2006

## 11. Taxation (continued)

### c) Deferred tax recognised in the Group Income Statement

	2006			2005		
	Pre- exceptional items	Exceptional items	Total	Pre- exceptional items	Exceptional items	Total
	£m	£m	£m	£m	£m	£m
Accelerated capital allowances	8	—	8	13	—	13
Deferred tax on movement in fair value of interest rate swaps	9	12	21	—	(6)	(6)
Utilisation of tax losses	3	—	3	6	—	6
Temporary differences	(4)	—	(4)	—	—	—
Deferred tax on profit on sale of property	—	18	18	—	2	2
Reduction in deferred tax liability due to indexation	—	(34)	(34)	—	(19)	(19)
	<b>16</b>	<b>(4)</b>	<b>12</b>	19	(23)	(4)

### d) Deferred tax recognised directly in equity

	2006 £m	2005 £m
Increase in deferred tax liability related to revaluation of property and rolled over gains	91	74
Deferred tax relating to share schemes credited to equity	(5)	(7)
Tax charge in the statement of recognised income and expense	86	67

# Notes to the Group Accounts

at 30 September 2006

## 12. Earnings per ordinary share

The calculation of basic earnings per share is based on earnings of £325 million (2005 — £209 million) and on 322.1million (2005 — 342.4 million) shares being the weighted average number of equity shares in issue during the year after excluding shares held by trusts relating to employee share options and shares held in treasury.

Adjusted earnings per share, which the directors believe reflects the underlying performance of the Group, is based on earnings adjusted for the effects of exceptional items, net of tax, of £220 million (2005 — £200 million) and on 322.1 million (2005 — 342.4 million) shares being the weighted average number of equity shares in issue during the year after excluding shares held by trusts relating to employee share options and shares held in treasury.

Basic earnings are adjusted as follows:

	<b>2006</b>	2005
	<b>£m</b>	£m
Profit after tax	<b>325</b>	209
Exceptional finance costs:		
Write off of unamortised issue costs	<b>3</b>	5
Movement in fair value of interest rate swaps	<b>(40)</b>	20
Other exceptional items:		
Net profit on disposal of property	<b>(67)</b>	(14)
Movements from revaluation of pub estate	<b>2</b>	4
Reorganisation costs	<b>2</b>	
Tax impact of exceptional items listed above	<b>29</b>	(5)
Reduction in deferred tax liability due to indexation	<b>(34)</b>	(19)
<b>Adjusted earnings</b>	<b>220</b>	200

Diluted earnings per share is based on profit for the year of £325 million (2005 — £209 million) and adjusted profit of £220m (2005 — £200 million) and on 324.7 million (2005 — 346.6 million) ordinary shares calculated as follows:

	<b>2006</b>	2005
	<b>No.</b>	No.
Basic weighted average number of shares	<b>322.1</b>	342.4
Executive share option scheme	<b>0.9</b>	1.6
Enterprise Inns Quest share save scheme	<b>0.4</b>	0.5
Long-term and short-term incentive plans	<b>1.3</b>	2.1
Diluted weighted average number of shares	<b>324.7</b>	346.6

# Notes to the Group Accounts

at 30 September 2006

## 13. Dividends paid and proposed

	2006 £m	2005 £m
<b>Paid during the year</b>		
Equity dividends on ordinary shares:		
Final dividend relating to prior year 12.4 pence (2005 — 8.4 pence)	42	29
Interim dividend for current year 9.0p (2005 — 5.6 pence)	28	19
	<b>70</b>	<b>48</b>

### Proposed for approval by shareholders at the AGM

Final dividend for current year 18.0 pence (2005 — 12.4 pence)	54	42
--	----	----

Proposed dividends are not accounted for until they are approved at the AGM.

The dividends relating to shares held by the Employee Benefit Trust and shares held in treasury have been waived. No dividend is due on shares held in treasury.

## 14. Goodwill

	2006 £m	2005 £m
At 1 October and 30 September	417	417

### Impairment testing

Goodwill acquired via business combinations is tested annually for impairment. For this purpose, the goodwill is allocated to the pub estate. This represents the lowest level within the Group that goodwill is monitored for internal management purposes. The impairment test compares the recoverable amount of the cash-generating unit with its carrying amount. The recoverable amount is determined using a value in use calculation.

This calculation discounts estimated future cash flows using a discount rate equivalent to the Group's weighted average pre-tax cost of capital of 7.43% (2005 — 7.35%). Future cash flows are estimated using management forecasts of cash flow over a five year period. Each element of the cash flows beyond this forecast period is extrapolated using a growth rate of 3% (2005 — 3%). The impairment test did not result in any impairment of goodwill.

# Notes to the Group Accounts

at 30 September 2006

## 15. Investments

	2006 £m	2005 £m
<b>Cost and net book value:</b>		
At 1 October 2005	—	—
Additions	2	—
<b>At 30 September 2006</b>	<b>2</b>	<b>—</b>

On 6 September 2006, the Group disposed of 769 pubs to Admiral Taverns. Part of the consideration received for this disposal was £2 million of preference shares in Admiral Taverns. See note 4.

## 16. Intangible assets: operating lease premiums

	2006 £m	2005 £m
<b>Cost:</b>		
At 1 October	29	29
Transfer to non-current assets held for sale	(2)	—
<b>At 30 September</b>	<b>27</b>	<b>29</b>
<b>Amortisation:</b>		
At 1 October	2	—
Provided during the year	1	2
<b>At 30 September</b>	<b>3</b>	<b>2</b>
<b>Net book value:</b>		
<b>At 30 September</b>	<b>24</b>	<b>27</b>
At 1 October	27	29

Lease premiums are amortised on a straight-line basis over the remaining life of the lease. The amortisation is charged to the Income Statement in the line item 'depreciation and amortisation'.

# Notes to the Group Accounts

at 30 September 2006

## 17. Property, plant and equipment

	Licensed land and buildings £m	Landlords' fixtures and fittings £m	Other assets £m	Total £m
<b>Cost or valuation</b>				
At 1 October 2004	4,782	85	24	4,891
Additions	47	18	1	66
Revaluation	267	—	—	267
Write down to fair value less costs to sell	(11)	—	—	(11)
Net transfers to non-current assets held for sale	(34)	—	—	(34)
Disposals	—	—	(1)	(1)
At 1 October 2005	5,051	103	24	5,178
Additions	102	33	8	143
Revaluation	323	—	—	323
Write down to fair value less costs to sell	(3)	—	—	(3)
Net transfers to non-current assets held for sale	(263)	(12)	—	(275)
Disposals	(6)	—	(2)	(8)
<b>At 30 September 2006</b>	<b>5,204</b>	<b>124</b>	<b>30</b>	<b>5,358</b>
<b>Depreciation</b>				
At 1 October 2004	11	4	3	18
Charge for the year	6	2	1	9
Revaluation	(6)	—	—	(6)
At 1 October 2005	11	6	4	21
Charge for the year	3	2	2	7
Net transfers to non-current assets held for sale	(4)	(1)	—	(5)
Disposals	(5)	—	(2)	(7)
Revaluation	(1)	—	—	(1)
<b>At 30 September 2006</b>	<b>4</b>	<b>7</b>	<b>4</b>	<b>15</b>
<b>Net book value</b>				
<b>At 30 September 2006</b>	<b>5,200</b>	<b>117</b>	<b>26</b>	<b>5,343</b>
At 30 September 2005	5,040	97	20	5,157
At 1 October 2004	4,771	81	21	4,873

### Revaluation of property, plant and equipment

With the exception of properties identified for disposal, the Group's licensed land and buildings were revalued as at 30 September 2006 by Humberts Leisure Limited and Christie & Co., independent Chartered Surveyors, and by the internal Head of Estates, Simon Millar MRICS, Chartered Surveyor.

The land and buildings were valued at market value (as defined within RICS Appraisal and Valuation Standards 'Red Book'), reflecting the current and future rent and other income streams which are expected to be generated by each property capitalised at an appropriate yield. The valuation also takes account of the terms of the leases or tenancies under which the properties are let. Market value is influenced by factors such as income, location, pub quality and tenure. The valuations are made by reference to market transactions within the UK pub sector.



# Notes to the Group Accounts

at 30 September 2006

## 17. Property, plant and equipment (continued)

The pubs used as security for the secured bonds and debenture in Enterprise Inns plc have been valued by Humberts Leisure Limited. The balance of the estate held in Enterprise Inns plc and Voyager Pub Group Limited has been valued by the Head of Estates. The results of this internal valuation have been compared to that of the external valuers. This review ensured that the results are consistent.

A representative sample of the pubs held by Unique Pub Properties Limited ('Unique') has been valued by Christie & Co. The method of this valuation have been applied across the rest of the Unique estate on a pub by pub basis in line with the requirements of the securitisation. The results of both the Unique and Enterprise valuations are also compared, ensuring consistency.

Pubs identified for disposal which are classified in the balance sheet as 'non-current assets held for sale' are held at fair value less costs to sell. This value is based on the net estimated realisable disposal proceeds (ERV) which are provided by third party property agents who have been engaged to sell the properties.

If licensed land and buildings had been measured using the cost model, the carrying amounts would be as follows:

	Licensed land and buildings £m
At 30 September 2006	
Cost	4,093
Accumulated depreciation	(36)
Net book value	4,057
At 30 September 2005	
Cost	4,212
Accumulated depreciation	(45)
Net book value	4,167

The carrying value of property held under finance leases at 30 September 2006 was £236 million (2005 — £265 million). Additions during the year include £3m of property held under finance leases (2005 — £5 million).

At 30 September 2006, the Group had entered into contractual commitments to purchase £9 million (2005 — £9million) of property, plant and equipment.

# Notes to the Group Accounts

at 30 September 2006

## 18. Current assets held for sale

	<b>2006</b>	2005
	<b>£m</b>	£m
Fixtures and fittings and stock purchased from tenants		
<b>Cost</b>		
At 1 October	<b>11</b>	10
Additions	<b>12</b>	9
Disposals	<b>(13)</b>	(8)
At 30 September	<b>10</b>	11
<b>Provision</b>		
At 1 October	<b>4</b>	5
Charge for the year	<b>2</b>	—
Utilised during the year	<b>(2)</b>	(1)
At 30 September	<b>4</b>	4
<b>Net realisable value</b>	<b>6</b>	7

## 19. Trade and other receivables

	<b>2006</b>	Reanalysed 2005
	<b>£m</b>	£m
Trade receivables	<b>76</b>	61
Prepayments and accrued income	<b>16</b>	20
Other receivables	<b>2</b>	—
	<b>94</b>	81

2005 has been re-analysed to show receivables that related to commission income in trade receivables instead of accrued income as these amounts are now invoiced.

## 20. Non-current assets held for sale

	<b>2006</b>	2005
	<b>£m</b>	£m
At 1 October	<b>36</b>	33
Net transfer from property, plant and equipment (note 17)	<b>270</b>	34
Net transfer from intangible assets: lease premiums (note 16)	<b>2</b>	—
Disposals	<b>(298)</b>	(31)
At 30 September	<b>10</b>	36
Representing:		
Property, plant and equipment	<b>10</b>	35
Intangible assets: lease premiums	<b>—</b>	1
	<b>10</b>	36

Non-current assets held for sale comprises both freehold and leasehold licensed and unlicensed properties that have been identified by the Group for disposal as part of the continued improvement in quality of its property portfolio. Non-current assets held for sale may be sold as trading pubs or for alternative use. The sale of all assets within this category is expected to be completed within one year of the balance sheet date.

A balance of £1 million (2005 — £2 million) in relation to these pubs is held within the revaluation reserve representing revaluation surpluses.

# Notes to the Group Accounts

at 30 September 2006

## 21. Trade and other payables

	2006 £m	2005 £m
Trade payables	17	10
Accruals and deferred income	150	162
Other payables	43	45
	<b>210</b>	217

## 22. Financial assets and liabilities

	2006 £m	2005 £m
<b>Financial assets</b>		
<b>Current</b>		
Interest rate swap	1	-
<b>Non-current</b>		
Interest rate swap	1	-
Total financial assets	<b>2</b>	
	<b>2006 £m</b>	2005 £m
<b>Financial liabilities</b>		
<b>Current</b>		
Securitised bonds	13	13
Interest rate swaps	41	109
	<b>54</b>	122
<b>Non-current</b>		
Syndicated bank borrowings	421	256
Corporate bonds	1,181	1,181
Securitised bonds	1,709	1,817
Finance lease payables	5	6
	<b>3,316</b>	3,260
Total financial liabilities	<b>3,370</b>	3,382
Total financial assets and liabilities	<b>3,368</b>	3,382

### Fair values

Bank borrowings, the debenture, bonds and interest rate swaps were valued at fair value as at 30 September by J C Rathbone, independent valuers. Fair value is calculated by discounting future cash flows using prevailing interest rates. The finance lease payables are valued by calculating the present value of the future minimum lease payments.

# Notes to the Group Accounts

at 30 September 2006

## 22. Financial assets and liabilities (continued)

The book and fair values of financial assets and liabilities analysed into categories of syndicated bank borrowings, corporate bonds, securitised bonds and interest rates swaps are as follows.

		2006 Nominal value £m	2006 Book value £m	2006 Fair value £m	2005 Nominal value £m	2005 Book value £m	2005 Fair value £m
Syndicated bank borrowings	LIBOR + 0.6%	425	421	425	260	256	260
<b>Corporate bonds:</b>							
Debenture — issued 3 February 1999	6%	60	59	61	60	59	58
Secured bond — issued 9 May 2000	6.875%	125	124	144	125	124	141
Secured bond — issued 15 February 2001	6.875%	125	124	140	125	124	139
Secured bond — issued 26 February 2002	6.375%	275	272	310	275	272	298
Secured bond — issued 3 March 2003	6.5%	600	602	647	600	602	650
		<b>1,185</b>	<b>1,181</b>	<b>1,302</b>	1,185	1,181	1,286
<b>Securitised bonds:</b>							
A1N — issued 25 February 2005	LIBOR + 0.38%	34	34	34	125	125	125
A2N — issued 25 February 2005	LIBOR + 0.16%	248	248	249	262	261	262
A3 — issued 30 March 1999	6.542%	435	458	485	435	460	493
A4 — issued 20 September 2002	5.659%	535	537	566	535	536	566
M — issued 30 March 1999	7.395%	225	248	267	225	250	267
N — issued 20 September 2002	6.464%	190	197	213	190	198	209
		<b>1,667</b>	<b>1,722</b>	<b>1,814</b>	1,772	1,830	1,922
<b>Interest rate swaps:</b>							
£275m swap expiring 1 June 2012	6.662%	—	22	22	—	—	—
£350m swap expiring 30 September 2011	4.887%	—	(2)	(2)	—	—	—
£550m swap expiring 1 June 2012	6.662%	—	—	—	—	67	67
£91m swap expiring 30 December 2012	7.934%	—	—	—	—	9	9
£72m swap expiring 30 December 2012	7.873%	—	5	5	—	10	10
£87m swap expiring 30 December 2012	7.873%	—	6	6	—	10	10
£122m swap expiring 30 September 2013	6.079%	—	8	8	—	13	13
		—	<b>39</b>	<b>39</b>	—	109	109
		<b>3,277</b>	<b>3,363</b>	<b>3,580</b>	3,217	3,376	3,577
Finance lease payables (note 23)		—	5	5	—	6	6
Total debt		<b>3,277</b>	<b>3,368</b>	<b>3,585</b>	3,217	3,382	3,583
Cash		(111)	(111)		(96)	(96)	
Underlying net debt/net debt (note 30)		<b>3,166</b>	<b>3,257</b>		3,121	3,286	

Syndicated bank borrowings, corporate bonds and securitised bonds are held at amortised cost. Interest rate swaps are held at fair value and finance lease payables represents the present value of future minimum lease payments. Other categories of financial instruments include trade receivables and trade payables, however there is no difference between the book value and fair value of these items.

# Notes to the Group Accounts

at 30 September 2006

## 22. Financial assets and liabilities (continued)

### Use of disposal proceeds

During the year the Group disposed of 769 pubs to Admiral Taverns for a total consideration of 318m. Of the consideration received by the Group £2m was in the form of preference shares which accrue interest at a rate of 8%. The £316m consideration received in the form of cash has been utilised by the Group as follows:

	£m
Prepayment of A1N secured bonds	(80)
Repayment of A2N secured bonds	(3)
Repayment of syndicated bank borrowings	(179)
Cancellation and restructuring costs associated with interest rate swaps	(30)
General corporate purposes (including acquisitions and share buybacks)	(24)
	(316)

### Interest rate swaps

As part of the repayment of debt following the receipt of consideration from Admiral Taverns, a proportion of the Group swaps were cancelled or restructured. In Unique Pub Properties Limited, a subsidiary company, swaps were cancelled and restructured to ensure that the floating rate notes remain effectively hedged through to maturity. In Enterprise Inns plc a £275m swap expiring in June 2012 was restructured into a £350m swap expiring in September 2011 in order to take advantage of current market rates. The cash impact of restructuring the hedging instruments was as follows:

	£m
Cancellation of £91m swap expiring 30 December 2012	(5)
Restructuring of £72m swap expiring 30 December 2012	—
Restructuring of £275m swap expiring 1 June 2012 into £350m swap expiring 30 September 2011	(25)
	(30)

The £25m paid in order to restructure the £275m June 2012 swap into a £350m September 2011 swap effectively put the swap £2m into the money.

Following the restructuring of the swap the fair value balance is categorised as a financial asset. The swaps were restructured on 29 September 2006 and from this date the Group has chosen to designate the restructured £350m swap that expires in September 2011 as an effective hedge under IAS 39 as it meets the criteria set out in that standard. This cash flow hedge is hedging future movements in interest rates until September 2011. As a result, future changes in the fair value of the effective portion of this swap will be recognised directly in equity instead of in the Income Statement. Changes in the fair value of the ineffective portion of the hedge will continue to be recognised in the Income Statement.

The change in fair value of interest rate swaps from £109m to £39m during the year ending 30 September 2006 is made up of cash payments of £30m as shown above and changes in fair value of £40m which have been recognised in the Income Statement. The £40m movement in fair value has been recognised in the Income Statement in its entirety as the movement all relates to swaps that were not designated as hedges under IAS 39.

### Financial instruments and risk

The Group's financial instruments, other than derivatives, comprise bank loans, a debenture, secured bonds, securitised bonds and cash. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group also enters into derivative transactions, specifically interest rate swaps. The purpose of such transactions is to manage the interest rate risk arising from the Group's sources of finance.

# Notes to the Group Accounts

at 30 September 2006

## 22. Financial liabilities (continued)

The main risks arising from the Group's financial instruments are interest rate risk and liquidity risk. There is no currency exposure as all transactions are in Sterling. The Board reviews and agrees policies for managing each of these risks and they are summarised as follows.

### Liquidity risk

The Group has exposure to liquidity risk, being the risk that payments cannot be made when they fall due. The Group's objective is to maintain a balance between the continuity of funding and flexibility through the use of overdrafts, bank loans, debentures and securitised debt.

This objective is achieved through the following processes:

- Regular cash flow forecasting and reporting through the treasury function
- Regular review of the Group's debt portfolio including maturities and repayment profile
- Maintenance of undrawn committed borrowings
- Management of share buy-back programme

At 30 September 2006, the nominal value of the Group's borrowings (excluding swaps and finance lease payables) comprised:

	<b>2006</b>	2005
	<b>£m</b>	£m
Syndicated bank borrowings	<b>13%</b>	8%
Corporate bonds	<b>36%</b>	37%
Securitised bonds	<b>51%</b>	55%

The maturity of the Group's debt, including interest rate swap liabilities, is set out below:

	<b>2006</b>	2005
	<b>£m</b>	£m
In more than five years	<b>2,751</b>	2,845
In more than two years but not more than five years	<b>578</b>	435
In more than one year but not more than two years	<b>21</b>	99
In one year or less or on demand	<b>22</b>	40
	<b>3,372</b>	3,419

The table above shows the contractual, undiscounted cash flows due in future periods to settle the group's debt. The total amount payable shown above differs from the total book value of group debt of £3,363m as the book value of group debt includes the fair value of the interest rates swaps which is based on discounted cash flows.

The contractual maturity of trade and other payables is within one year. An analysis of minimum lease payments due under finance leases is set out in note 23.

# Notes to the Group Accounts

at 30 September 2006

## 22. Financial liabilities (continued)

Details of undrawn committed borrowing facilities available at 30 September are as follows:

	2006 £m	2005 £m
Expiring in		
In more than five years	190	190
In more than two years but not more than five years	575	230
In more than one year but not more than two years	—	—
In one year or less or on demand	—	—
	<b>765</b>	<b>420</b>

The undrawn facilities relate to:

	2006 £m	2005 £m
Renewable committed liquidity facility in respect of the Unique securitisation	190	190
Undrawn element of the syndicated bank facility	575	230

### Interest rate risk

The Group borrows its debenture and bonds except for the A1N and A2N bonds at a fixed rate. Bank debt and the A1N and A2N bonds are borrowed at, and cash balances attract interest at, a floating rate. The Group's objective is to manage exposure to changes in interest rates. This exposure is managed using interest rate swaps acquired with Group companies. At 30 September 2006, the Group's borrowings were 100% fixed (after including the impact of interest rate swaps) at an average rate of 6.6% for 13 years (2005 — 100% fixed at an average rate of 6.9% for 14 years). Cash flows associated with cash deposits, debt and interest rate swaps and the fair value of these instruments fluctuates with changes in interest rates.

The effect on the profit for the year would have been as follows if interest rates had been 50 basis points higher or lower during the period.

	Interest receivable £m	Interest Payable £m	Movement in fair value of interest rate swap £m
As reported in Income Statement	6	(230)	40
Effect if interest rates increased by 50 basis points	7	(230)	60
Difference	1	—	20
As reported in Income Statement	6	(230)	40
Effect if interest rates decreased by 50 basis points	5	(230)	20
Difference	(1)	-	(20)

A change in interest rates would result in no difference in respect of interest payable when taking interest payable on floating rate debt in aggregate with the interest due on interest rate swaps. This is because, if interest rates increased by 50 basis points, additional interest payable in relation to floating rate debt of £4m would be offset by a reduction in interest payable of £4m under the interest rate swaps. If interest rates decreased by 50 basis points, the same principle would apply whereby £4m less interest would be payable in relation to the floating rate debt and £4m more in relation to the swaps.

# Notes to the Group Accounts

at 30 September 2006

## 22. Financial liabilities (continued)

### Credit risk

There are no significant concentrations of credit risk within the Group. The Group is exposed to a small amount of credit risk that is primarily attributable to trade receivables and cash balances. The Group's objective is to minimise this risk by dealing with third parties with high credit ratings and carrying out credit checks where appropriate. The amount of trade and other receivables included in the Balance Sheet are net of a bad debt provision which has been estimated by management following a review of individual receivable accounts and is based on prior experience and known factors at the balance sheet date after taking into account collateral held in the form of cash deposits. Receivables are written off against the bad debt provision when management considers that the debt is no longer recoverable. At 30 September 2006 the value of collateral is £27 million (2005 — £26 million). This balance is held on the balance sheet in 'other payables'.

An analysis of the provision held against trade receivables is set out below. This provision relates to trade receivables which are primarily represented by licensees.

	2006 £m	2005 £m
Allowance as at 1 October	5	6
Increase in provision during the year	3	4
Provision utilised during the year	(1)	(1)
Provision released during the year	(3)	(4)
Allowance as at 30 September	4	5

There are no trade receivables that are past due at the balance sheet date that have not been provided against. There are no indications as at 30 September 2006 that debtors will not meet their payment obligations in respect of the amount of trade receivables recognised in the balance sheet that are neither past due nor impaired. The maximum amount of exposure to credit risk is the carrying value of trade receivables and the fair value of interest rate swaps classified as financial assets. The Group's credit risk on liquid funds is limited because the Group only invests with banks and financial institutions with high credit ratings.

### Security

Senior debt finance is secured by a security deed entered into by substantially all of the companies which comprise the Group, excluding Enterprise Inns Holding Company Limited and its subsidiaries. The lenders have a floating charge over all of the assets and undertakings of such Group companies. The floating charge ranks subsequent to the fixed charges created by the debenture and secured bonds. The value of assets secured by way of a fixed or floating charge as at 30 September 2005 is — Property, Plant and Equipment £5,317 million (2005 — £5,137 million), operating lease premiums £24 million (£27 million) and pubs held for sale £10 million (£36 million).



# Notes to the Group Accounts

at 30 September 2006

## 23. Leases

### The Group as lessee

The Group leases a proportion of its licensed estate from landlords under finance leases and operating leases. These leases have varying terms, escalation clauses and renewal rights.

#### Finance leases

	2006 £m	2005 £m
Future minimum lease payments due under finance leases:		
within one year	—	1
after one year but not more than five years	2	2
In more than five years	27	33
	29	36
Future finance lease interest	(24)	(30)
Present value of future minimum lease payments	5	6

The present value of future minimum lease payments is due in more than five years (2005 — more than five years).

Pubs that are leased from landlords under finance leases are let to tenants. Future minimum rentals receivable from non-cancellable sub-leases on the above properties are £149 million (2005 — £170 million).

#### Operating leases

	2006 £m	2005 £m
Operating lease rentals recognised as an expense in the year	4	6
	2006 £m	2005 £m
Future minimum lease payments due under operating leases:		
within one year	3	4
after one year but not more than five years	12	16
In more than five years	64	87
	79	107

Pubs that are leased from landlords under operating leases are let to tenants. Future minimum rentals receivable from non-cancellable sub-leases on the above properties are £37 million (2005 — £49 million).

# Notes to the Group Accounts

at 30 September 2006

## 23. Leases (continued)

### The Group as lessor

The Group leases its licensed estate and other non-licensed properties to tenants. The majority of lease agreements have terms of between 6 months and 30 years and are classified for accounting purposes as operating leases. Most of the leases with terms of over 3 years include provision for rent reviews on either a 3 or 5 year basis.

Future minimum lease rentals receivable under non-cancellable operating leases are as follows:

	2006 £m	2005 £m
Future minimum lease rentals receivable under operating leases:		
within one year	254	264
after one year but not more than five years	939	975
In more than five years	2,173	2,327
	<b>3,366</b>	<b>3,566</b>

## 24. Provisions

	2006 £m	2005 £m
At 1 October 2005:		
Current	1	1
Non-current	7	5
	<b>8</b>	<b>6</b>
Movement during the year:		
Release of provision during the year	(1)	(1)
Utilisation	(2)	(1)
Reclassification	—	3
	<b>(3)</b>	<b>1</b>
At 30 September 2006:		
Current	1	1
Non-current	4	7
	<b>5</b>	<b>8</b>

The provision relates to future commitments under onerous lease agreements. The provision is expected to be utilised as the pubs are disposed of. The remaining lease terms vary from 5 to 65 years.

## 25. Deferred tax

The deferred tax in the Group Balance Sheet relates to the following:

	2006 £m	2005 £m
Revaluation of property and rolled over gains	609	535
Accelerated capital allowances	98	90
Fair value of interest rate swaps	(12)	(33)
Share-based payments	(8)	(8)
Tax losses	—	(3)
Other temporary differences	5	9
	<b>692</b>	<b>590</b>

The Group has not provided deferred tax in relation to temporary differences associated with undistributed earnings of subsidiaries on the basis that under current enacted law, no tax is payable on dividends payable and receivable within the Group.

# Notes to the Group Accounts

at 30 September 2006

## 26. Pension liability

The Group makes defined contribution payments to employees' own pension plans and these payments are charged to the Income Statement as incurred.

RetailLink Management Limited (a subsidiary company) established a pension plan for its employees in January 1999. The plan has defined contribution and defined benefit schemes. The plan is now closed to new members and for the future accrual of benefits. The most recent full actuarial valuation of the defined benefit section of the plan was at 5 April 2005. This has been updated to 30 September 2006. The valuation was carried out by Mercer, independent professionally qualified actuaries, using the projected unit credit method.

### Assets and liabilities of the plan

	2006 £m	2005 £m
Fair value of plan assets:		
Equities	13	12
Bonds	6	5
	19	17
Present value of plan liabilities	(19)	(17)
Net pension liability	—	—

The present value of plan obligations relates to funded plans.

### Movement in deficit during the year

	2006 £m	2005 £m
Net liability at the start of the year	—	(3)
Employer contributions	—	2
Actuarial (loss)/gain	—	1
Net liability at the end of the year	—	—

### Analysis of amounts recognised in the Income Statement

	2006 £m	2005 £m
Interest cost on plan liabilities	(1)	(1)
Expected return on plan assets	1	1
	—	—

The amounts above are recognised within interest payable.

# Notes to the Group Accounts

at 30 September 2006

## 26. Pension liability (continued)

### Analysis of amounts recognised in the Statement of Recognised Income and Expense

	2006 £m	2005 £m
Actual return on plan assets	2	2
Less expected return on plan assets	(1)	(1)
	1	1
Other actuarial gains and losses	(1)	—
	—	1

### Changes in the fair value of plan assets

	2006 £m	2005 £m
Fair value of plan assets at the start of the year	17	13
Expected return on plan assets	1	1
Actuarial gain/(loss) on plan assets	1	1
Employer contributions	—	2
Fair value of plan assets at the end of the year	19	17

### Changes in the present value of scheme liabilities

	2006 £m	2005 £m
Present value of plan liabilities at the start of the year	(17)	(16)
Interest cost	(1)	(1)
Actuarial gain/(loss) on plan liabilities	(1)	—
Present value of plan liabilities at the end of the year	(19)	(17)

The principal assumptions made by the actuaries were:

	2006 %	2005 %
Rate of increase in pension payments	3.50	3.30
Rate of increase of pensions in deferment	3.00	2.80
Discount rate	5.00	5.00
Inflation assumption	3.00	2.80
Expected return on plan assets:		
Equities	7.00	6.00
Bonds	3.90	4.20
Longevity at age 65 for current pensioners		
Men	22 years	22 years
Women	25 years	25 years
Longevity at age 65 for future pensioners		
Men	24 years	24 years
Women	27 years	27 years

# Notes to the Group Accounts

at 30 September 2006

## 26. Pension liability (continued)

The expected rates of return on individual categories of plan assets are determined by reference to the relevant indices published by FTSE.

The expected rates of return shown for 30 September 2006 are after a deduction for plan expenses of 0.75% p.a.. The corresponding figures for 30 September 2005 showed a deduction for expenses of 1.0% p.a. for equities and 0.5% p.a. for bonds.

The mortality tables used to value the plan's liabilities are PMA92(YOB=1935)mc less 1 year age rating for current pensioners and PMA92(YOB=1965)mc less 1 year age rating for future retirees. These tables give a life expectancy as set out above.

The history of the plan for the current and prior years is as follows:

	2006 £m	2005 £m	2004* £m
Fair value of plan assets	19	17	13
Present value of plan liabilities	(19)	(17)	(16)
Net liability	—	—	(3)
Experience adjustments on plan assets	1	1	—
Experience adjustments on plan liabilities	(1)	—	1

\* Six month period ending 30 September 2004

Total contributions to the defined benefit scheme during the year to 30 September 2007 is expected to be £nil.

Since the acquisition of the defined benefit scheme on 31 March 2004, the total amount of actuarial gains and losses recognised in the Statement of Recognised Income and Expense is £1m gain (2005 — £1m gain).

## 27. Share capital

Authorised:	2006		2005	
	No.	£m	No.	£m
Ordinary shares of 5p each	500,000,000	25	500,000,000	25
<b>Allotted, called up and fully paid:</b>				
	2006		2005	
Ordinary shares of 5p each	No.	£m	No.	£m
At 1 October	349,505,390	17	349,505,390	17
Cancelled	(17,340,815)	(1)	—	—
At 30 September	332,164,575	16	349,505,390	17

Ordinary shares carry no right to fixed income. Holders of ordinary shares are entitled to vote at meetings.

At 30 September 2006, the Company owned 25 million of its own shares as treasury shares with a nominal value of £1 million and a market value of £264 million (2005 — nil). Transaction costs of £3 million (2005 — nil) have been accounted for directly in equity in the profit and loss reserve.

In addition, the Group held 6,870,253 shares with a nominal value of £0.3m and a market value of £72 million (2005 — 9,248,445 shares, nominal value £0.5 million, market value £78 million). These shares are held by the Employee Benefit Trust and Enterprise Inns Quest Trustees Limited and are shares used to satisfy awards made under the Enterprise Inns Incentive Plans and other share option schemes (note 28).

# Notes to the Group Accounts

at 30 September 2006

## 28. Share-based payments

The Group operates share-based payment schemes for both directors and other employees. Details of the Short-Term Incentive Plan (STIP) and Long-Term Incentive Plan (LTIP) which form part of the remuneration of the executive directors are given in the Directors' Remuneration Report on pages 28 to 37.

The Group also operates an Employee Share Option Scheme (ESOS), a Savings Related Share Option Scheme (SAYE) and a Share Incentive Plan (SIP).

A total expense of £3 million (2005 — £3 million) has been incurred in the year in relation to share-based payments. This expense relates wholly to the equity-settled schemes described above.

### Share Incentive Plan

The SIP is open to all employees. At times determined by the Company, employees may allocate the lower of £1,500 and 10% of pre-tax salary to purchase shares out of their salary. The Board may also decide to award matching shares. The shares are held in trust on behalf of the employee. If shares are removed from trust within three years, any allocation of matching shares may be lost. Shares can be transferred tax-free to employees after a period of five years. This scheme is operating for the first time in 2005/06 and matching shares were awarded. The cost of the matching shares is being spread over the three year vesting period of the scheme.

Details of the number of matching shares held in trust during the year are as follows:

	2006	2005
Outstanding beginning of year	—	—
Granted	44,914	—
Forfeited/expired	(2,579)	—
Outstanding at end of year	42,335	—

### Employee Share Option Scheme

The ESOS scheme is open to all employees. Share options are awarded to employees at the discretion of the Board. The current intention of the Board is to issue options with an exercise price equal to the market value of a share at grant date. Options will normally vest after 3 years if an employee remains in service and if EPS growth targets are met. For options granted during the year ended 30 September 2006 options will only vest in full if the average compound annual percentage growth in adjusted EPS between the grant date and the third anniversary of the grant date is 8.33%. Options may normally only be exercised during the period of 7 years commencing on the third anniversary of the date of grant of the option. Options will usually be settled by issuing ordinary shares held by the Employee Benefit Trust.

# Notes to the Group Accounts

at 30 September 2006

## 28. Share-based payments (continued)

Details of the share options outstanding during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price £	Weighted Number of share options	average exercise price £
Outstanding beginning of year	4,335,827	4.43	4,536,348	3.08
Granted	1,020,750	8.89	1,192,500	7.18
Exercised	(1,698,746)	2.83	(1,344,043)	2.33
Forfeited/expired	(341,697)	6.08	(48,978)	4.23
Outstanding at end of year*	3,316,134	6.45	4,335,827	4.43
Weighted average remaining contractual life		6.5 years		5.9 years

\* Included in this balance are 133,731 options (2005 – 453,327) which have not been accounted for under IFRS 2 as they were granted before 7 November 2002. Such options are not accounted for under IFRS 2 in line with the transitional provisions of this standard and of IFRS 1 'First-time adoption of IFRS' (note 33). Options will only vest in full if certain performance criteria are met.

Options outstanding at 30 September 2006 comprise the following:

Exercise date	Number of share options	Exercise price £
<b>Exercisable:</b>		
14/12/02–14/12/09	1,344	1.63
18/12/03–18/12/10	52,828	1.70
11/12/04–11/12/11	79,559	2.58
16/12/05–16/12/12	258,740	2.81
	392,471	
<b>Not yet exercisable:</b>		
08/12/06–08/12/13	940,000	4.90
07/12/07–07/12/14	800,250	7.02
18/05/08–18/05/15	289,500	7.57
06/12/09–06/12/16	893,913	8.89
	2,923,663	
	3,316,134	

The weighted average fair value of options granted during the year under the ESOS was £1.46 (2005 – £1.31).

# Notes to the Group Accounts

at 30 September 2006

## 28. Share-based payments (continued)

### Savings-Related Share Option Scheme

The SAYE scheme is open to executive directors and employees at the discretion of the Board. Participants contract to save a fixed amount each month with a savings institution for a period of five or seven years. At the end of the savings term, participants are given the option to purchase shares at a price set before the savings began. The option price will be not less than 80% of the market value of a share on the date that participants are invited to take part in the scheme, or the nominal value of a share if lower. Options will usually be settled using ordinary shares held by Enterprise Inns Quest Trustees Ltd (an employee benefit trust) and will usually be exercisable for six months after the fifth or seventh anniversary of the commencement of the savings contract.

Details of the share options outstanding during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price £	Number of share options	Weighted average exercise price £
Outstanding at beginning of year	915,136	2.70	946,134	2.18
Granted	130,774	7.07	144,016	5.45
Exercised	(209,579)	1.27	(102,135)	1.53
Forfeited/expired	(58,464)	4.78	(72,879)	3.02
Outstanding at end of year*	777,867	3.66	915,136	2.70
Weighted average remaining contractual life		2.8 years		2.9 years

\* Included in this balance are 142,146 options (2005 — 351,058) which have not been accounted for under IFRS 2 as they were granted before 7 November 2002. Such options are not accounted for under IFRS 2 in line with the transitional provisions of this standard and of IFRS 1 'First-time adoption of IFRS'. (note 33).

Options outstanding at 30 September 2006 comprise the following:

Exercise date	Number of share options	Exercise price
<b>Not yet exercisable:</b>		
01/02/07–01/08/07	28,700	1.41
01/02/08–01/08/08	5,576	1.25
01/02/07–01/08/09	107,870	2.10
01/02/08–01/08/10	267,745	2.32
01/02/09–01/08/11	137,213	3.73
01/02/10–01/08/12	116,349	5.45
01/02/11–01/08/13	114,414	7.07
	777,867	

The weighted average fair value of options granted during the year under the SAYE scheme was £2.60 (2005 — £2.12).



# Notes to the Group Accounts

at 30 September 2006

## 28. Share-based payments (continued)

### STIP and LTIP

Executive directors and other members of the executive team are eligible to participate in the STIP and LTIP plans. A summary of the rules of these schemes along with details of shares that have been granted and are outstanding in relation to individual directors is included in the Directors' Remuneration Report on pages 28 to 37.

Details of the total number of shares outstanding during the year are as follows:

	2006		2005	
	LTIP Number of share options	STIP Number of share options	LTIP Number of share options	STIP Number of share options
Outstanding at beginning of year	1,665,436	135,133	1,624,478	163,508
Granted†	347,979	48,335	410,578	52,283
Exercised	(453,383)	(44,368)	(369,620)	(80,658)
Forfeited	(111,475)	(725)	—	—
Outstanding at end of year*	1,448,557	138,375	1,665,436	135,133
Weighted average remaining contractual life	4.9 years	3.0 years	6.8 years	5.7 years

Directors pay £1 to exercise awards granted under the STIP and LTIP. This is a one-off charge. All of the shares outstanding at 30 September 2006 are not yet exercisable.

† The share price at which the number of shares granted under the STIP scheme is calculated will not be confirmed until after the date of the approval of the accounts. The number of STIP shares granted during the year is therefore estimated using the closing share price on 30 September 2006.

\* Included in this balance are 40,941 LTIP shares (2005 — 494,324) which have not been accounted for under IFRS 2 as they were granted before 7 November 2002. Such shares are not accounted for under IFRS 2 in line with the transitional provisions of this standard and of IFRS 1 'First-time adoption of IFRS' (note 33). Awards will only vest in full if certain performance criteria are met.

The weighted average fair value of shares granted during the year under the STIP was £9.51 (2005 — £8.07) and under the LTIP was £5.90 (2005 — £5.03)

The weighted average share price on exercise of shares and share options during the year was £9.56.

# Notes to the Group Accounts

at 30 September 2006

## 28. Share-based payments (continued)

### Fair value of share schemes

The fair value of equity-settled share options and share awards granted is estimated at the date of grant using share option valuation models. The ESOS, SAYE and STIP schemes are valued using the Black-Scholes model. The element of the LTIP scheme that relates to non-market conditions is valued using the Black Scholes model. The element of the LTIP that includes market conditions is valued using the Monte Carlo Simulation Model.

The following tables list the inputs to the models for options and shares granted during the year:

Weighted average:	ESOS		SAYE	
	2006	2005	2006	2005
Share price (£)	8.89	7.18	8.84	6.81
Exercise price (£)	8.89	7.18	7.07	5.45
Dividend yield	2.4%	2.2%	2.4%	2.2%
Expected volatility	21%	23%	21%	22%
Risk-free interest rate	4.22%	4.33%	4.18%	4.46%
Expected life of option (years)	3.3	3.3	5 or 7	5 or 7

Weighted average:	STIP		LTIP	
	2006	2005	2006	2005
Share price (£)	10.55	8.81	8.81	6.84
Exercise price (£)	—	—	—	—
Dividend yield	2.4%	2.2%	2.4%	2.2%
Expected volatility	22%	22%	21%	22%
Risk-free interest rate	4.31%	4.48%	4.2%	4.42%
Expected life of option (years)	4	4	3–5*	3–5*

Expected share-price volatility is based on historic volatility over the same period of time as the vesting period of the option. The expected life of an option is based on historical data.

The LTIP will only vest in full if a TSR target is met. This is a market condition and the TSR performance criteria has therefore been taken into account when calculating the fair value of the options granted under the LTIP. These conditions have been incorporated into the Monte Carlo Simulation model which is used to fair value the TSR element of the scheme.

\* The LTIP vests in three equal tranches after 3, 4 and 5 years.

# Notes to the Group Accounts

at 30 September 2006

## 29. Statement of changes in equity

	Share Capital £m	Share premium account £m	Revaluation reserve £m	Capital redemption reserve £m	Merger reserve £m	Treasury share reserve £m	Other reserve £m	Profit and loss account £m	Total £m
At 1 October 2004	17	486	472	8	77	—	(28)	208	1,240
Total recognised income and expense for the year	—	—	199	—	—	—	—	213	412
Transfer of realised revaluation surplus	—	—	(4)	—	—	—	—	4	—
Equity dividends paid (note 13)	—	—	—	—	—	—	—	(48)	(48)
Purchase of shares to be held in trust	—	—	—	—	—	—	(37)	—	(37)
Employee share option entitlements exercised in the year	—	—	—	—	—	—	6	(3)	3
Directors' share option entitlements exercised in the year	—	—	—	—	—	—	3	(3)	—
Share-based expense recognised in operating profit	—	—	—	—	—	—	—	3	3
At 1 October 2005	17	486	667	8	77	—	(56)	374	1,573
Total recognised income and expense for the year	—	—	232	—	—	—	—	330	562
Transfer of realised revaluation surplus	—	—	(54)	—	—	—	—	54	—
Equity dividends paid (note 13)	—	—	—	—	—	—	—	(70)	(70)
Consideration paid for purchase of own shares	—	—	—	—	—	(227)	—	(3)	(230)
Cancellation of ordinary shares	(1)	—	—	1	—	—	—	(166)	(166)
Purchase of shares to be held in trust	—	—	—	—	—	—	—	—	—
Employee share option entitlements exercised in the year	—	—	—	—	—	—	11	(7)	4
Directors' share option entitlements exercised in the year	—	—	—	—	—	—	3	(3)	—
Share-based expense recognised in operating profit	—	—	—	—	—	—	—	3	3
<b>At 30 September 2006</b>	<b>16</b>	<b>486</b>	<b>845</b>	<b>9</b>	<b>77</b>	<b>(227)</b>	<b>(42)</b>	<b>512</b>	<b>1,676</b>

### Share premium account

This reserve represents the amount of proceeds received for shares in excess of their nominal value of 5 pence per share.

### Revaluation reserve

This reserve shows the surplus generated on revaluation of the estate. It represents the amount by which the fair value of the estate exceeds its historic cost.

### Capital redemption reserve

This reserve arose on the repurchase and cancellation of own shares in 1995/96 and 2005/06.

### Merger reserve

This reserve arose as a consequence of the acquisition of Century Inns plc in 1998/99.

# Notes to the Group Accounts

at 30 September 2006

## 29. Statement of changes in equity (continued)

### Treasury share reserve

This reserve shows the cost of own shares purchased by the Company and held as treasury shares. These shares can be cancelled or reissued.

### Other reserve

This comprises the cost of shares in the Company that are held by employee benefit trusts. These shares are used to satisfy awards made under share incentive plans (note 28).

## 30. Additional cash flow information

### a) Reconciliation of net cash flow to movement in net debt

	2006 £m	2005 £m
Increase/(decrease) in cash in the year	15	(51)
Cash (inflow)/outflow from change in debt	(30)	200
Issue costs of new long term loans	4	2
Change in net debt resulting from cash flows	(11)	151
Amortisation of issue costs and discounts/premiums on long-term loans	(7)	(4)
Amortisation of securitised bonds	10	5
Change in fair value of interest rate swaps	40	(20)
Write-off of unamortised issue costs	(3)	(5)
Movement in net debt in the year	29	127
Net debt at start of year	(3,286)	(3,413)
Net debt at end of year	(3,257)	(3,286)

### b) Analysis of net debt

	2006 £m	2005 £m
Corporate bonds	(1,185)	(1,185)
Syndicated bank borrowings	(425)	(260)
Securitised bonds	(1,667)	(1,772)
Gross debt	(3,277)	(3,217)
Cash	111	96
<b>Underlying net debt (note 22)</b>	<b>(3,166)</b>	<b>(3,121)</b>
Capitalised debt issue costs	20	27
Fair value adjustments on acquisition of bonds	(67)	(77)
Fair value of interest rate swaps	(39)	(109)
Finance lease payables	(5)	(6)
<b>Net debt (note 22)</b>	<b>(3,257)</b>	<b>(3,286)</b>
Balance sheet:		
Current financial assets	1	—
Non-current financial assets	1	—
Current financial liabilities	(54)	(122)
Non-current financial liabilities	(3,316)	(3,260)
Cash	111	96
<b>Net debt</b>	<b>(3,257)</b>	<b>(3,286)</b>

Underlying net debt represents amounts repayable to banks and other lenders net of cash retained in the business.

# Notes to the Group Accounts

at 30 September 2006

## 31. Related party transactions

### Compensation of key management personnel

	<b>2006</b>	2005
	<b>£000</b>	£000
Short-term employee benefits	<b>2,478</b>	2,255
Post-employment benefits	<b>346</b>	315
Share-based payment	<b>2,078</b>	1,509
	<b>4,902</b>	4,079

Key management personnel comprises both executive and non-executive directors

Short-term employee benefits comprises fees, salaries, benefits and performance related bonus as reported in the Directors' Remuneration Report. Post-employment benefits comprise payments made to the directors' own personal pension schemes. Share-based payment comprises the fair value of STIP and LTIP awards charged in the year. Further information about the remuneration of individual directors is available in the Directors' Remuneration Report on pages 28 to 37.

### Principal subsidiaries

The Group's principal subsidiaries are listed in the following table. The list comprises those companies that principally affect the results or financial position of the Group.

<b>Company</b>	Country of Incorporation	Holding	Proportion of voting rights and shares held	Nature of business
<i>Held directly by Enterprise Inns plc:</i>				
Enterprise Inns Holding Company Limited	England	Ordinary shares	100%	Investment holding company
<i>Indirectly held by Enterprise Inns plc:</i>				
Unique Pub Properties Limited	England	Ordinary shares	100%	Ownership of licensed properties
The Unique Pub Finance Company plc	England	Ordinary shares	100%	Financing acquisitions of licensed property
		Cumulative Redeemable Preference shares	100%	
Voyager Pub Group Limited	England	Ordinary shares	100%	Ownership of licensed properties

## 32. Events after the balance sheet date

On 20 November 2006 the Group entered into a binding agreement to sell its entire Scottish estate of 137 pubs to Retail & Licensed Properties Limited for consideration of £115 million.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS

This is the first Annual Report and Accounts that has been prepared using IFRS. Comparatives for the year to 30 September 2005 have been restated from UK GAAP into IFRS to allow proper comparison. Reconciliations of the opening balance sheet at 1 October 2004 and of the balance sheet and results for the year ended 30 September 2005 are shown below along with details of the significant decisions made by the Group on transition to IFRS.

Since the publication of the Restatement of Financial Information under IFRS released in May 2006, the Group has amended the 2005 Income Statement and Balance Sheet in respect of the application of IFRS 5 'Non-current assets held for sale and discontinued operations'. This amendment relates to the treatment of the write-down of property on classification as 'held for sale' under IFRS 5. The write down to fair value less costs to sell is first recognised in the Revaluation Reserve, to the extent of any existing surplus for the asset. It is then recognised in the Income Statement within the line 'movements from revaluation of pub estate'. Previously, the entire write-down was recognised in the Income Statement within the line 'Net profit on sale of property, plant and equipment'.

In addition, the 2004 and 2005 Balance Sheet has been reclassified in respect of the application of IAS 1 'Presentation of financial statements' and IAS 39 'Financial instruments: recognition and measurement'. The interaction of these two standards means that all derivatives that are not part of a designated and effective hedging relationship should be classified as current assets or liabilities. The Group has therefore reclassified the fair value of all interest swaps as current liabilities in 2004 and 2005. Previously, the fair value of the swaps was allocated between 'current' and 'non-current' liabilities.

### IFRS 1 – First-time adoption decisions

IFRS 1 'First-time adoption of International Financial Reporting Standards' provides certain exemptions on transition to IFRS. The significant decisions made by the Group under IFRS 1 are set out below:

#### Business combinations

The Group has chosen to restate business combinations that have taken place since 1 January 1999 in accordance with IFRS 3 'Business Combinations'. The effect of this has been to increase goodwill for deferred tax liabilities relating to property, plant and equipment and rolled over gains that would have existed at the date of acquisition had IFRS been in place.

#### Valuation of properties

IFRS 1 provides the option to use a previous revaluation of property, plant and equipment as 'deemed cost' at the date of transition to IFRS. The Group has decided not to take this option and will also continue to revalue properties under IAS 16. This treatment is consistent with that adopted under UK GAAP. The Board considers it is appropriate to continue to adopt this treatment under IFRS to enable the accounts to reflect an up-to-date valuation of the pub estate.

#### Employee benefits

The Group has elected to recognise all cumulative actuarial gains and losses in relation to its defined benefit pension scheme on transition to IFRS. Actuarial gains and losses arising after the date of transition will also be recognised in full in accordance with the Amendment to IAS 19. This treatment is consistent with that adopted under UK GAAP (FRS 17). This scheme is now closed to new members and for the future accrual of benefits.

#### Share-based payment transactions

The Group has elected to apply IFRS 2 'Share-based payments' to awards granted after 7 November 2002 but not vested at 1 January 2005.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued)

### Non-current assets held for sale

The Group has chosen to apply IFRS 5 'Non-current assets held for re-sale and discontinued operations' from the date of transition to IFRS. This is permitted by IFRS 1 as the information required to identify assets held for re-sale was available at the date of transition. This decision has been taken to ensure consistency between accounting policies for the years to 30 September 2005 and 30 September 2006.

### Comparative information — IAS 32 and IAS 39

The Group has decided not to take the exemption allowed by IFRS 1 to delay adoption of IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' until the year ending 30 September 2006. As a result, these two standards have been applied from the date of transition to IFRS. This decision has been taken to ensure consistency between accounting policies for the years to 30 September 2005 and 30 September 2006.

### Adjustments made to the Income Statement

#### 1. Reclassification of 'other operating income' (IAS 18)

Income previously shown as 'other operating income', which predominantly represents income from amusement and other machines, has been reclassified as revenue. This follows a review of the Group's income streams under IAS 18 'Revenue'.

#### 2. Presentation of dividends (IAS 1)

Under UK GAAP, dividends payable were shown in the Profit and Loss Account. IAS 1 'Presentation of Financial Statements' states that dividends payable are shown in equity. The 'dividends' line has therefore been removed from the face of the Income Statement so that the statement ends with profit after tax.

#### 3. Goodwill (IFRS 3)

Under UK GAAP, goodwill was amortised on a straight line basis over a useful economic life of 20 years. IFRS 3 'Business Combinations' states that goodwill should not be amortised. Instead it is tested annually for impairment. As a result, the amortisation charged during 2005 has been reversed.

#### 4. Interest rate swaps — reversal of UK GAAP accounting (IAS 39)

Under UK GAAP, the interest rate swaps that the Group inherited upon acquisition of subsidiary companies were held on the balance sheet at their fair value at the date of acquisition. This fair value balance was amortised over the life of the swap with the amortisation being credited to the Profit and Loss Account. The interest rates swaps are now accounted for under IAS 39. As a result, the credit arising from the amortisation of the UK GAAP fair value balance has been reversed.

#### 5. Interest rate swaps — introduction of IFRS accounting (IAS 39)

IAS 39 'Financial Instruments: Recognition and Measurement', states that the swaps must be held on the balance sheet at fair value. Fair value is remeasured at each balance sheet date and the movement is shown in the Income Statement unless hedge accounting is adopted. The Group elected not to adopt hedge accounting for any swaps in the year ending 30 September 2005. A significant proportion of the Group's swaps are not classified as 'effective' under IAS 39 and therefore do not qualify for hedge accounting and it has been decided to apply the same accounting treatment to all existing swaps. In addition, the administration and cost of monitoring and assessing the interest rate swaps for effectiveness on a periodic basis will be avoided.

As a result, the movement in the fair value of the swaps during 2004/05 has been charged to the Income Statement. It should be noted that the movement in relation to these swaps will vary periodically and could result in increased volatility in the Income Statement.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued)

### 6. Depreciation (IAS 16)

Under UK GAAP, no depreciation was charged on any element of the pub estate on the grounds of materiality. Instead an annual impairment test was carried out on the estate. IAS 16 'Property, Plant and Equipment' ('PPE') contains no provision allowing non-depreciation on the grounds of materiality. Each part of PPE that has a cost that is significant in relation to the total cost must be depreciated separately.

The Group has concluded that an additional depreciation charge should be incurred under IAS 16 in relation to landlords' fixtures and fittings and certain improvements made to buildings. No depreciation is charged on land. Freehold buildings are depreciated to write off the difference between their carrying value and residual value over their useful economic life of 50 years. However, no depreciation charge arises in respect of 2004/05 as the residual value of freehold properties is at least equal to their carrying value.

### 7. Pub revaluations (IAS 16/IFRS 5)

Under UK GAAP, all revaluation uplifts were credited to the revaluation reserve. If a pub fell in value the revaluation deficit was debited to the revaluation reserve to the extent that there was a revaluation credit in relation to that pub and thereafter if it could be shown that the value in use exceeded the valuation.

Under IAS 16, any revaluation that causes the book value of a pub to fall below historic cost will lead to a charge in the Income Statement. The charge will represent the amount by which the pub falls below depreciated historic cost. If this same pub later recovers in value so that its book value exceeds depreciated historic cost, the increase in value is credited to the Income Statement to the extent that a debit was previously recognised.

The Income Statement will therefore contain a new line entitled 'movements from revaluation of pub estate' showing the impact on the Income Statement of the year-end revaluation exercise.

Under UK GAAP, pubs held for disposal were valued at their expected sales proceeds net of selling costs. The amount of any write-down was recognised in the profit and loss account as a 'provision for loss on sale' and shown within 'net profit on disposal of tangible fixed assets'.

Under IFRS, when pubs are classified as held for sale under IFRS 5, they are valued at the lower of book value and fair value less costs to sell. Any write-down in value as a result of this treatment is first recognised in the Revaluation Reserve to the extent of any existing surplus for that asset. It is then recognised in the Income Statement. The amount of any write-down recognised in the Income Statement is also shown in the line 'movements from revaluation of pub estate'. As a result, an amendment has been made in the Income Statement to transfer the value of any write-down that would have been recognised in the Revaluation Reserve to the Balance Sheet.

### 8. Leases (IAS 17)

The Group leases a number of pubs from landlords. Under UK GAAP most of these were accounted for within tangible fixed assets and the Group had attributed a fair value to them on acquisition. Rent was charged to the Profit and Loss Account as incurred. The Group's net interests in leasehold assets were held at valuation.

Under IAS 17, most leases have been reclassified as finance leases. The finance lease payable, representing the present value of future minimum lease payments, has been reclassified and is shown on the balance sheet under 'financial liabilities'. The carrying value of these properties has been increased by the same amount so that they are now held at fair value. The properties continue to be held at valuation but one that no longer takes account of the remaining lease payments.



# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued)

The remaining leasehold pubs have been classified as held under operating leases. The amount held on the balance sheet in respect of amounts paid for these pubs has been reclassified from tangible fixed assets to intangible assets: operating lease premiums. The revaluation surplus relating to these properties has been reversed as IAS 17 does not permit the revaluation of assets held under operating leases.

As a result of these changes, some rent payable in the Income Statement has been reclassified as interest payable. The depreciation charged on short-leasehold properties that have been reclassified as finance leases has increased as the value of the properties being depreciated has increased to fair value. Operating lease premiums that have been reclassified on the Balance Sheet are now amortised over the life of the lease.

## 9. Share-based payments (IFRS 2)

Under UK GAAP, the costs of shares awarded under the Short-Term Incentive Plan ('STIP') and Long-Term Incentive Plan ('LTIP') were recognised based on the intrinsic value of the shares at the date of grant. This cost was spread over the performance period of the scheme. No charge was recognised for the Employee Share Option Scheme (ESOS) as these options have no intrinsic value. An exemption was also in place which meant that no charge was made for Save as You Earn (SAYE) schemes.

Under IFRS 2 'Share-based payments', the fair value of share schemes are calculated and the cost is then spread over the vesting period of each scheme. This results in a new charge for SAYE and ESOS schemes and a revised charge for the STIP and LTIP. As a result, an additional charge has been recognised in the Income Statement for share-based payments.

## 10. Tax — deferred tax on pub estate (IAS 12)

Under IAS 12, a deferred tax liability has been recognised on the balance sheet relating to the revaluation of the pub estate and gains previously rolled over, or due to be rolled over, into other assets. The deferred tax liability that would have been in place at the time of business combinations that have occurred since 1 January 1999 has resulted in the recognition of additional goodwill as the fair value of the net assets acquired has been reduced. As this pre-acquisition liability reduces due to capital gains indexation relief, a credit is recognised in the Income Statement. This has been classified as an exceptional tax item due to its size and because it does not relate to any income or expense recognised in the Income Statement in the same period.

## 11. Tax (IAS 12)

An adjustment has been made to the tax charge to reflect the deferred tax effect of the other IFRS adjustments where relevant.

The two tax adjustments do not affect the amount of tax payable in respect of the year ended 30 September 2005.

## Other changes relating to the Income Statement

### Exceptional items

Exceptional items are classified as those which are separately identified by virtue of their size or nature to allow a full understanding of the underlying performance of the Group.

### Earnings per share (IAS 33)

The calculation of the number of shares for use in the diluted earnings per share calculation is different under IAS 33 'Earnings per Share' to that used under UK GAAP. This is due to the treatment of contingently issuable shares and the effects of IFRS 2 'Share-based payments'. This has resulted in a reduction in the number of shares being used in this calculation.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued)

### Other formatting adjustments

The Group has taken the opportunity to re-format the Income Statement in order to show Earnings before interest, tax, depreciation and amortisation (EBITDA) as a line item.

### Adjustments made to the Balance Sheet

#### 1. Presentation of payables (IAS 1)

IAS 1 states that current tax payable and financial liabilities should be shown separately as line items in the balance sheet. These items have therefore been split out and shown separately.

#### 2. Presentation of deferred tax (IAS 1)

IAS 1 states that deferred tax should be shown separately as a line item in the balance sheet. This has therefore been split out from 'provisions for liabilities and charges' and shown separately.

#### 3. Presentation of provisions (IAS 1)

Under UK GAAP, 'provisions for liabilities and charges' were shown after 'creditors falling due after more than one year'. IAS 1 states that all assets and liabilities should be classified as either 'current' or 'non-current'. As a result, the provisions in place that relate to a period of one year or less from the balance sheet date have been identified and moved to current liabilities.

#### 4. Presentation of pension liability (IAS 19)

Under UK GAAP, the pension liability was shown net of deferred tax. Under IFRS, the pension liability is shown gross with the related deferred tax asset shown within 'deferred tax'. As a result, the deferred tax relating to the pension liability has been reclassified on the balance sheet.

#### 5. Depreciation (IAS 16)

Under UK GAAP, no depreciation was charged on any element of the pub estate on the grounds of materiality. Under IFRS, the Group has concluded that a depreciation charge should be incurred on landlords' fixtures and fittings and certain improvements made to buildings. No depreciation is charged on land. Freehold buildings are depreciated to write off the difference between their carrying value and residual value over their useful economic life of 50 years. However, no depreciation charge arises as the residual value of these properties is at least equal to their carrying value.

As a result, an adjustment has been made to reflect the charge that would have been recognised under IFRS in relation to landlords' fixtures and fittings and certain improvements to buildings. This adjustment is a transfer between the profit and loss account reserve and the revaluation reserve.

#### 6. Pub revaluations below historic cost (IAS 16)

Under UK GAAP, all revaluation uplifts were credited to the revaluation reserve. If a pub fell in value the revaluation deficit was debited to the revaluation reserve to the extent that there was a revaluation credit in relation to that pub and thereafter if it could be shown that the value in use exceeded the valuation.

Under IAS 16, any revaluation that causes the book value of a pub to fall below historic cost will lead to a charge in the Income Statement. The charge will represent the amount by which the pub falls below historic cost. If this same pub later recovers in value so that its book value exceeds historic cost, the increase in value is credited to the Income Statement to the extent that a debit was previously recognised.

As a result, on transition to IFRS all deficit balances held in the revaluation reserve were transferred to the profit and loss account reserve as under IAS 16, these would have been charged to the Income Statement.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued)

### 7. Non-current assets held for sale (IFRS 5)

Under UK GAAP, all pubs were held within 'tangible fixed assets'. IFRS 5 'Non-current assets held for re-sale and discontinued operations' creates a new category of asset that is neither a current asset nor a non-current asset. Freehold and leasehold pubs that are considered to be held for sale rather than held for trading, and that meet the criteria laid out in IFRS 5, are moved to this new category and shown separately on the balance sheet.

### 8. Deferred tax on revaluations and rolled over gains (IAS 12)

Under UK GAAP, no deferred tax was recognised in respect of the unrealised surplus on the revaluation of tangible fixed assets unless there was a binding commitment to sell the properties at the balance sheet date. In addition, no provision was included for capital gains on the disposal of properties where the gain was deferred through the application of capital gains rollover relief as no liability was expected to crystallise.

IAS 12 'Income Taxes' states that deferred tax must be provided on all temporary differences between the tax base cost and carrying value of assets. As a result, a deferred tax liability has been recognised relating to the revaluation of the pub estate and gains previously rolled over, or due to be rolled over, into other assets. It should be noted that this liability is not expected to crystallise in the foreseeable future.

The deferred tax liability that would have been in place at the time of business combinations that have occurred since 1 January 1999 has resulted in the recognition of additional goodwill as the fair value of the net assets acquired has been reduced. The amount of indexation that would have been credited to the Income Statement in relation to these pubs is reflected in the Profit and Loss Account Reserve. The deferred tax arising from revaluations carried out by the Group (i.e. post-acquisitions) is charged to the revaluation reserve.

### 9. Goodwill (IFRS 3)

Under UK GAAP, goodwill was amortised on a straight-line basis over a useful economic life of 20 years. IFRS 3 'Business Combinations' states that goodwill should not be amortised. Instead it is tested annually for impairment. Goodwill amortisation that was charged under UK GAAP all relates to business combinations that have been restated under IFRS 3. The accumulated amortisation has therefore been reversed. Goodwill was tested for impairment on transition to IFRS and at 30 September 2005 and no impairment was identified.

### 10. Proposed dividends (IAS 10)

Under UK GAAP, dividends were accrued and shown as a liability when they were proposed. They were therefore accounted for in the period to which they related.

IAS 10 'Events after the Balance Sheet Date' states that dividends declared after the balance sheet date should not be recognised as a liability. As a result, the liability for proposed dividends has been reversed. Final dividends will now only be recognised when they are approved at the AGM and interim dividends when they are paid.

### 11. Interest rate swaps (IAS 39)

Under UK GAAP, the interest rate swaps that the Group inherited upon acquisition of subsidiary companies were held on the balance sheet at their fair value at the date of acquisition. This fair value balance was amortised over the life of the swap with the amortisation being credited to the profit and loss account.

IAS 39 'Financial Instruments: Recognition and Measurement', states that these swaps must be held on the balance sheet at fair value. Fair value is remeasured at each balance sheet date. As a result, the UK GAAP book value of the swaps has been replaced by their fair value at the balance sheet date. In addition, the fair value of swaps that are not classified as hedging instruments under IAS 39 are all shown as 'current liabilities'. Hedge accounting was not adopted for any swaps at 30 September 2005. As a result the value of swaps held within non-current liabilities has been transferred to current liabilities.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued)

### 12. Leases (IAS 17)

The Group leases a number of pubs from landlords. Under UK GAAP the Group accounted for all leases as operating leases and rent was charged to the Profit and Loss Account as incurred. Leasehold assets were held on the balance sheet within tangible fixed assets at valuation.

Under IAS 17, most leases have been re-classified as finance leases. The finance lease payable, representing the present value of future minimum lease payments, has been reclassified and is shown on the balance sheet under 'financial liabilities'. The book value of these properties has been increased by the same amount so that they are now held at fair value.

The remaining leasehold pubs have been classified as held under operating leases. The amount held on the balance sheet in relation to these pubs has been reclassified from tangible fixed assets to intangible assets: operating lease premiums. The revaluation surplus relating to these properties has been reversed as IAS 17 does not permit the revaluation of assets held under operating leases.

### 13. Tax (IAS 12)

An adjustment is made to reflect the tax impact of the other IFRS adjustments where relevant.

#### Other changes relating to the Balance Sheet

##### Net debt

The amount of underlying net debt, defined as the amount repayable to banks and other lenders, net of cash retained within the business, is unchanged by the adoption of IFRS. However, net debt as presented in the balance sheet has changed due to the treatment of interest rate swaps under IAS 39 and leases under IAS 17.

##### Cash flow statement

The transition to IFRS has no effect on reported cash flows generated by the Group. The IFRS cash flow statement is presented in a different format from that required under UK GAAP. Cash flows are split into three categories — operating activities, investing activities and financing activities. The changes made to the cash flow have no effect on the total cash flows generated by the business.

# Notes to the Group Accounts

at 30 September 2006

## 33. Transition to IFRS (continued) Reconciliation of Group Income Statement for the year ended 30 September 2005

	1	2	3	4	5	6	7	8	9	10	11
	Revenue	Dividends	Goodwill	Swaps	Swaps	Deprecia- tion	Restated# Revalua- tions	Leases	Share	Restated#	IFRS
	IAS18	IAS 1	IFRS 3	IAS 39	IAS 39	IAS 16	IAS 16	IAS 17	IFRS 2	IAS 12	Restated# Tax
	£m	IAS 1	IFRS 3	IAS 39	IAS 39	IAS 16	IAS 16	IAS 17	IFRS 2	IAS 12	IAS 12
Revenue	919.9	32.2									952.1
Cost of sales	(385.1)							0.4			(384.7)
<b>Gross profit</b>	<b>534.8</b>										<b>567.4</b>
Administrative expenses	(38.9)								(0.5)		(39.4)
Other operating income	32.2	(32.2)									0.0
<b>EBITDA</b>	<b>528.1</b>										<b>528.0</b>
Depreciation of owned property, plant and equipment	(1.4)					(5.9)					(7.3)
Depreciation and amortisation of leasehold properties	(2.2)							(0.6)			(2.8)
Amortisation of goodwill	(4.3)		4.3								0.0
<b>Group operating profit</b>	<b>520.2</b>										<b>517.9</b>
Interest receivable	8.9										8.9
Interest payable	(223.5)			(12.7)				(0.4)			(236.6)
<b>Profit before tax and exceptional items</b>	<b>305.6</b>										<b>290.2</b>
Exceptional finance costs:											
Write-off of unamortised issue costs	(4.6)										(4.6)
Movement in fair value of interest rate swaps	0.0			(19.6)							(19.6)
Other exceptional items:											
Profit on disposal of associated undertaking	0.2										0.2
Net profit on disposal of property, plant and equipment	2.7						11.1				13.8
Movements arising from revaluation of pub estate	0.0						(4.4)				(4.4)
<b>Profit before tax</b>	<b>303.9</b>										<b>275.6</b>
Tax on profit on ordinary activities	(92.1)										(85.3)
Exceptional tax item: Reduction in deferred tax liability due to indexation	0.0									19.2	6.8
<b>Group profit on ordinary activities after tax</b>	<b>211.8</b>	<b>0.0</b>	<b>4.3</b>	<b>(12.7)</b>	<b>(19.6)</b>	<b>(5.9)</b>	<b>6.7</b>	<b>(0.6)</b>	<b>(0.5)</b>	<b>19.2</b>	<b>6.8</b>
Dividends	(61.4)	61.4									—
<b>Retain profit for the period</b>	<b>150.4</b>										<b>209.5</b>
# See note 1											
<b>EPS — basic</b>	<b>61.9p</b>										<b>61.0p</b>
<b>EPS — basic diluted</b>	<b>61.1p</b>										<b>60.3p</b>
<b>EPS — adjusted</b>	<b>63.2p</b>										<b>58.4p</b>
<b>EPS — adjusted diluted</b>	<b>—</b>										<b>57.7p</b>

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# Independent Auditors' Report to the Members of Enterprise Inns plc

We have audited the Group financial statements of Enterprise Inns plc for the year ended 30 September 2006 which comprise the Group Income Statement, the Group Statement of Recognised Income and Expense, the Group Balance Sheet, the Group Cash Flow Statement and the related notes 1 to 33. These Group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of Enterprise Inns plc for the year ended 30 September 2006 and on the information in the Directors' Remuneration Report that is described as having been audited.

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

## Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report and the Group financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the Group financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the Group financial statements give a true and fair view, the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation and whether the information given in the Directors' report is consistent with the financial statements.

We also report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

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

We read other information contained in the Annual Report and consider whether it is consistent with the audited Group financial statements. The other information comprises only the Financial Highlights, the Chairman's Statement, the Chief Executive's Review (incorporating the Business Review), the Corporate Responsibility Report, Directors and Advisers and the Corporate Governance statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any other information.

## Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Group financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the Group financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming



# Independent Auditors' Report to the Members of Enterprise Inns plc

our opinion we also evaluated the overall adequacy of the presentation of information in the Group financial statements.

## Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 30 September 2006 and of its profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the directors' report is consistent with the Group financial statements.

## Ernst & Young LLP

Registered auditor

Birmingham

21 November 2006

## Note:

The maintenance and integrity of the Enterprise Inns plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

# Five Year Record

<b>Year ended 30 September</b>	<b>2006</b>	2005	2005	2004	2003	2002
	<b>IFRS</b>	IFRS	UK GAAP	UK GAAP	UK GAAP	UK GAAP
	<b>£m</b>	£m	£m	£m	£m	£m
Revenue	<b>970</b>	952	920	713	481	369
Operating profit	<b>537</b>	518	520	369	254	179
Profit before tax and exceptionals	<b>315</b>	290	306	231	173	115
Profit after tax	<b>325</b>	209	212	148	125	64
Adjusted earnings per share (pence)*	<b>68.3</b>	58.4	63.2	47.5	36.1	29.5

\* Excludes exceptional items.

<b>Year ended 30 September</b>	<b>2006</b>	2005	2005	2004	2003	2002
	<b>IFRS</b>	IFRS	UK GAAP	UK GAAP	UK GAAP	UK GAAP
	<b>£m</b>	£m	£m	£m	£m	£m
Non-current assets	<b>5,787</b>	5,601	5,293	5,012	2,692	2,387
Current assets†	<b>222</b>	220	184	237	48	60
Current liabilities	<b>(317)</b>	(386)	(331)	(309)	(306)	(224)
Non-current liabilities	<b>(4,016)</b>	(3,862)	(3,405)	(3,586)	(1,352)	(1,531)
Net assets	<b>1,676</b>	1,573	1,741	1,354	1,082	692

† Includes non-current assets held for re-sale in IFRS figures

# **Enterprise Inns plc**

## **Company Accounts 2005/06**

# Company Balance Sheet

at 30 September 2006

	Notes	2006 £m	Restated* 2005 £m
<b>Fixed assets</b>			
Tangible assets	2	2,830	2,723
Investments	3	1,963	1,011
Financial assets		1	—
		<b>4,794</b>	<b>3,734</b>
<b>Current assets</b>			
Assets held for sale	4	5	5
Debtors	5	330	240
Cash at bank and in hand		6	—
Financial assets		1	—
		<b>342</b>	<b>245</b>
<b>Creditors:</b> amounts falling due within one year	6	<b>(1,104)</b>	(1,036)
<b>Net current liabilities</b>		<b>(762)</b>	(791)
<b>Creditors:</b> amounts falling due after more than one year	7	<b>(1,606)</b>	(1,442)
<b>Provisions for liabilities and charges</b>	9	<b>(89)</b>	(61)
		<b>2,337</b>	<b>1,440</b>
<b>Capital and reserves</b>			
Called up share capital	10	16	17
Share premium account	11	486	486
Revaluation reserve	11	776	621
Capital redemption reserve	11	9	8
Treasury share reserve	11	(227)	—
Other reserve	11	(42)	(56)
Profit and loss account	11	1,319	364
<b>Shareholders' equity</b>		<b>2,337</b>	<b>1,440</b>

\* See note 1.

Approved by the Board on 21 November 2006 and signed on its behalf by:

**G E Tuppen**  
**D C George**

# Notes to the Company Accounts

at 30 September 2006

## 1. Accounting policies

### **Basis of preparation**

The accounts are prepared under the historical cost convention as modified to include the revaluation of properties and have been prepared in accordance with applicable United Kingdom accounting standards. No Profit and Loss Account is presented for Enterprise Inns plc as permitted by section 230 of the Companies Act 1985.

The Company has taken advantage of the provisions of FRS 1 (revised) which exempts companies which are part of a group which has published a consolidated cash flow statement from preparing a cash flow statement. Accordingly, no cash flow statement for the Company has been presented.

These accounts are for the Company and are not consolidated financial statements. Separate consolidated financial statements for the Group are prepared under IFRS and are published separately within this document.

### **Change in accounting policies**

The Company adopted the following new accounting standards on 1 October 2005 which require changes in accounting policy:

#### ***Share-based payments (FRS 20)***

The Company operates a number of equity-settled share-based payment schemes. Share-based payments are measured at fair value at the date of award and this value is subsequently updated at each balance sheet date for management's best estimate of the effect of non-market based vesting conditions on the number of equity instruments that will ultimately vest. The cost is recognised as an expense over the vesting period by calculating the cumulative expense and recognising the movement in the cumulative expense in the Profit and Loss Account. A corresponding entry is made to equity. The fair value of share options is measured using valuation models. On adoption of this standard a deferred tax asset was recognised.

#### ***Post-balance sheet events (FRS 21)***

Dividends declared after the balance sheet date are no longer reported as liabilities. Proposed dividends are no longer shown in the Profit and Loss Account or accrued for in the balance sheet.

#### ***Financial Instruments (FRS 26)***

The Company's existing interest rate swap is now recognised on the balance sheet at fair value. The swap is remeasured at every balance sheet date. Any change in the value of the swap is recognised in the Profit and Loss Account unless hedge accounting is adopted. Hedge accounting has not been adopted for the year ended 30 September 2006. Prior year comparatives have been restated to reflect this accounting treatment. The Company has not adopted any of the transitional provisions of FRS 26. On adoption of this standard a deferred tax asset was recognised.

# Notes to the Company Accounts

at 30 September 2006

## 1. Accounting policies (continued)

The impact on the balance sheet of these adjustments is as follows:

	Creditors: amounts falling due within one year £m	Creditors: amounts falling due after more than one year £m	Provisions for liabilities and charges £m	Shareholders' equity 30 Sept 2005 £m	Shareholders' equity 1 Oct 2004 £m
As previously reported	(1,018)	(1,479)	(89)	1,393	1,174
Adoption of FRS 20 — deferred tax asset	—	—	8	8	4
Adoption of FRS 21 — dividends	42	—	—	42	29
Adoption of FRS 26 — fair value of swaps	(60)	37	—	(23)	(3)
Adoption of FRS 26 — deferred tax asset	—	—	20	20	15
Shareholders equity as restated	(1,036)	(1,442)	(61)	1,440	1,219

The impact on the profit for 2005 is as follows:

	£m
Profit after tax as previously reported	172
FRS 20 - share based payment charge	(1)
FRS 26 - reversal of UK GAAP fair value release	(5)
FRS 26 - movement in fair value of interest rate swaps	(15)
Tax adjustments relating to above items	2
	153

The application of the above accounting policies in the current year gives rise to the recognition of a credit of £22 million arising from the movement in the fair value of interest rate swaps.

The Company also adopted the following new accounting standards but these standards have no impact on the amounts reported in the financial statements. Only those new standards that are relevant to the Company have been listed below:

- FRS 22 Earnings per Share
- FRS 25 Financial Instruments: disclosure and presentation (replaced by FRS 29)
- FRS 28 Corresponding amounts
- FRS 29 Financial instruments: Disclosure — the exemption has been taken per FRS 29.2D(b). The Company is exempt from producing the disclosures required by the standard as the Group accounts contain disclosure that complies with FRS 29.

# Notes to the Company Accounts

at 30 September 2006

## 1. Accounting policies (continued)

### Significant accounting policies

#### *Tangible fixed assets*

Expenditure on additions and improvements to tangible fixed assets is capitalised as the expenditure is incurred.

Substantially all of the Group's licensed estate is valued each year on an existing use basis. Surpluses arising from the professional valuation of the estate are recognised in the Revaluation Reserve. Valuation surpluses realised on sale are transferred to the Profit and Loss Account reserve. Any deficit arising from the valuation of properties is recognised in the Revaluation Reserve until the carrying amount reaches historical cost and, thereafter, to the extent that the value in use can be demonstrated to be higher than valuation. Any other deficit is charged to the Profit and Loss Account.

It is the Company's policy to maintain properties comprising the licensed estate in such condition that the residual values of the properties are at least equal to their book values. Having regard to this, it is the opinion of the directors that depreciation of any such property as required by the Companies Act 1985 and generally accepted accounting practice would not be material. An annual impairment review is carried out on such properties.

Short leasehold properties, defined as properties with 50 years or less of the lease remaining unexpired, are depreciated on a straight-line basis over the lease term.

Depreciation is provided on other categories of tangible fixed assets over 3 to 50 years on a straight-line basis to residual value.

#### *Leases and hire purchase commitments*

Rentals paid under operating leases are charged to the Profit and Loss Account on a straight-line basis over the lease term.

#### *Assets held for sale*

Assets held for sale are stated at the lower of cost incurred and net realisable value. Net realisable value is based on estimated selling price less further costs expected to be incurred on disposal.

#### *Investments*

Fixed asset investments are stated at cost less any provision for impairment.

#### *Deferred tax*

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.

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 results in an obligation to pay more, or a right to pay less, tax in the future have occurred at the balance sheet date, with the following exceptions:

- Provision is made for gains on disposal of fixed assets that have been rolled over into replacement assets on where, at the balance sheet date, there is a binding commitment to dispose of the replacement assets with no likely subsequent rollover or available capital losses.
- Provision is made for deferred tax on gains on revalued fixed assets only where there is a commitment to dispose of the revalued assets and the attributable gain can neither be rolled over or eliminated by capital losses.
- Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

# Notes to the Company Accounts

at 30 September 2006

## 1. Accounting policies (continued)

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

### *Treasury shares*

The cost of own shares held in employee benefit trusts and in treasury are deducted from shareholders' equity until the shares are cancelled, reissued or disposed of. Any proceeds received are also taken to shareholders' equity. No gain or loss is recognised in the Income Statement on the purchase, sale, issue or cancellation of own shares held.

### *Revenue recognition*

Beer and cider sales and wines, spirits and minerals sales are recognised when these goods are delivered to our customers. Rents receivable from the licensed estate and machine income are recognised in the accounting period to which the income relates.

### *Capital instruments*

Finance costs in respect of capital instruments other than equity shares is allocated to periods over the term of the instrument at a constant rate on the carrying amount.

### *Use of accounting estimates and judgements*

The Company makes estimates and assumptions during the preparation of the financial statements. Actual results may differ from these estimates under different assumptions and conditions. The estimates and assumptions that have the most significant effect on the amounts recognised in the financial statements are discussed below:

#### **a) Property, Plant and Equipment**

Properties are valued annually at open market value in accordance with the Appraisal and Valuation Manual published by the Royal Institution of Chartered Surveyors. The valuation is based on market observations and estimates the amount that would be paid by a willing buyer to a willing seller in an arms' length transaction after proper marketing. Non-current assets held for sale are valued at their market value less any costs that may be incurred to sell the pub.

The Company estimates the useful economic life and residual value of property, plant and equipment (PPE) and these estimates influence the depreciation charged each year. For details of these estimates, see the detailed accounting policy for PPE.

#### **b) Valuation of interest rate swaps**

The Company measures interest rate swaps at fair value at each balance sheet date. The swap valuation rates are derived from the mid point of the zero coupon prevailing at the close of business on the balance sheet date. The fair value represents the net present value of the difference between the projected cash flows at the swap contract rate and the valuation rate for the period from the balance sheet date to the contracted expiry rate. The calculation therefore uses estimates of present values and future interest rates.



# Notes to the Company Accounts

at 30 September 2006

## 2. Tangible fixed assets

	Licensed land and buildings £m	Landlords fixtures and fittings £m	Other assets £m	Total £m
<b>Cost or valuation</b>				
At 1 October 2005	2,614	100	16	2,730
Reclassifications	(3)	—	3	—
Additions	85	26	8	119
Provision for loss on sale	(2)	—	—	(2)
Revaluations	176	—	—	176
Disposals	(171)	(13)	(1)	(185)
<b>At 30 September 2006</b>	<b>2,699</b>	<b>113</b>	<b>26</b>	<b>2,838</b>
<b>Depreciation</b>				
At 1 October 2005	4	—	3	7
Charge for the year	1	—	2	3
Disposals	(1)	—	(1)	(2)
<b>At 30 September 2006</b>	<b>4</b>	<b>—</b>	<b>4</b>	<b>8</b>
<b>Net book value</b>				
<b>At 30 September 2006</b>	<b>2,695</b>	<b>113</b>	<b>22</b>	<b>2,830</b>
At 30 September 2005	2,610	100	13	2,723

Assets held for use by lessees under operating leases are detailed below:

	<b>2006</b> £m	2005 £m
Gross book value	<b>2,577</b>	2,523
Accumulated depreciation	<b>(3)</b>	(3)
Net book value	<b>2,574</b>	2,520

### Revaluation of property, plant and equipment

With the exception of properties identified for disposal, the Company's licensed land and buildings were revalued as at 30 September 2006 by Humberts Leisure Limited, independent Chartered Surveyors, and by the Head of Estates, Simon Millar MRICS, Chartered Surveyor.

The land and buildings were valued at market value (as defined within RICS Appraisal and Valuation Standards 'Red Book'), reflecting the current and future rent and other income streams which are expected to be generated by each property capitalised at an appropriate yield. The valuation also takes account of the terms of the leases or tenancies under which the properties are let. Market value is influenced by factors such as income, location, pub quality and tenure. The valuations are made by reference to market transactions within the UK pub sector.

The pubs used as security for the secured bonds and debenture in Enterprise Inns plc have been valued by Humberts Leisure Limited. The balance of the estate held in Enterprise Inns plc has been valued by the Head of Estates. The results of this valuation have been compared to that of the external valuers confirming that the results are entirely consistent.

Pubs identified for disposal are held at their realisable value. This value is based on the estimated realisable disposal proceeds (ERV) which are provided by third party property agents who have been engaged to sell the properties.

# Notes to the Company Accounts

at 30 September 2006

## 2. Tangible fixed assets (continued)

The net book value of licensed land and buildings comprises:

	<b>2006</b>	2005
	<b>£m</b>	£m
Freehold	<b>2,581</b>	2,481
Long leasehold	<b>98</b>	108
Short leasehold	<b>16</b>	21
	<b>2,695</b>	2,610

The net book value of licensed land and buildings and landlords' fixtures and fittings comprises:

	<b>2006</b>	2005
	<b>£m</b>	£m
Licensed estate at valuation	<b>2,807</b>	2,702
Licensed estate at cost	<b>1</b>	8
	<b>2,808</b>	2,710

The historical cost net book value of licensed premises included at valuation is as follows:

	<b>2006</b>	2005
	<b>£m</b>	£m
	<b>2,035</b>	2,081

## 3. Investments

	Subsidiary undertakings £m	Other Investment £m	Total £m
<b>Cost:</b>			
At 1 October 2005	1,034	—	1,034
Additions	950	2	952
<b>At 30 September 2006</b>	<b>1,984</b>	<b>2</b>	<b>1,986</b>
<b>Provision</b>			
At 1 October	(23)	—	(23)
Charge in year	—	—	—
<b>At 30 September 2006</b>	<b>(23)</b>	<b>—</b>	<b>(23)</b>
<b>Net book value</b>			
<b>At 30 September 2006</b>	<b>1,961</b>	<b>2</b>	<b>1,963</b>
At 30 September 2005	1,011	—	1,011

# Notes to the Company Accounts

at 30 September 2006

### 3. Investments (continued)

During the year, the Company disposed of 511 pubs to Admiral Taverns. Part of the consideration received was £2 million of preference shares which are shown above as other investment'. Details of the investment held are as follows:

	Country of Incorporation	Country of Incorporation	Proportion of voting rights and Holding shares held	Proportion of voting rights	Nature of business	
Admiral Taverns (780) Limited	England	England	Non-redeemable Preference Shares	100%	Nil	Ownership of licensed properties

The non-redeemable preference shares accrue interest daily at the rate of 8 pence per share per annum. The dividend is payable in priority over any dividend to ordinary share holders. The dividend is payable monthly in arrears and any dividend that is not paid on the due date attracts interest at a fixed rate of 8% per annum.

The Company's principal subsidiaries are listed in the following table.

#### Company

	Country of Incorporation	Country of Incorporation	Holding	Proportion rights and shares held	Nature of business
<i>Held directly by Enterprise Inns plc:</i>					
Enterprise Inns Holding Company Limited	England	England	Ordinary shares	100%	Investment holding company
<i>Indirectly held by Enterprise Inns plc:</i>					
Unique Pub Properties Limited	England	England	Ordinary shares	100%	Ownership of licensed properties
The Unique Pub Finance Company plc	England	England	Ordinary shares	100%	Financing acquisitions of licensed property
			Cumulative Redeemable Preference shares	100%	
Voyager Pub Group Limited	England	England	Ordinary shares	100%	Ownership of licensed properties

# Notes to the Company Accounts

at 30 September 2006

## 4. Assets held for sale

	2006 £m	2005 £m
Fixtures and fittings and stock purchased from tenants	5	5

## 5. Debtors

	2006 £m	2005 £m
Trade debtors	55	42
Amounts owed by subsidiary undertakings	254	175
Other debtors	2	—
Prepayments and accrued income	19	23
	<b>330</b>	<b>240</b>

## 6. Creditors: amounts falling due within one year

	2006 £m	Restated# 2005 £m
Bank overdraft	16	4
Interest rate swap	22	67
Trade creditors	17	10
Amounts due to subsidiary undertakings	853	758
Corporation tax	36	29
Other creditors including tax and social security	34	37
Accruals and deferred income	126	131
	<b>1,104</b>	<b>1,036</b>

# See note 1.

## 7. Creditors: amounts falling due after more than one year

	2006 £m	Restated# 2005 £m
Syndicated bank borrowings	421	256
Corporate bonds	1,181	1,181
Accruals and deferred income	4	5
	<b>1,606</b>	<b>1,442</b>

# See note 1.

# Notes to the Company Accounts

at 30 September 2006

## 8. Financial Instruments

	Interest rate	2006 Book value £m	2005 Book value £m
<b>Overdraft</b>		<b>16</b>	4
Syndicated bank borrowings	LIBOR + 0.6%	<b>421</b>	256
Corporate bonds:			
Debenture — issued 3 February 1999	6%	<b>59</b>	59
Secured bond — issued 9 May 2000	6.875%	<b>124</b>	124
Secured bond — issued 15 February 2001	6.875%	<b>124</b>	124
Secured bond — issued 26 February 2002	6.375%	<b>272</b>	272
Secured bond — issued 3 March 2003	6.5%	<b>602</b>	602
		<b>1,181</b>	1,181
<b>Interest rate swaps:</b>			
£275m swap expiring 1 June 2012	6.662%	<b>22</b>	—
£350m swap expiring 30 September 2011	4.887%	<b>(2)</b>	—
£550m swap expiring 1 June 2012	6.662%	<b>—</b>	67
		<b>20</b>	67
Total financial assets and liabilities		<b>1,638</b>	1,508

Bank debt and corporate bonds are repayable in full at maturity.

The maturity of the Company's debt and undrawn committed borrowings, including interest rate swaps, is set out below:

	2006 £m	2005 £m
In more than five years	<b>1,184</b>	1,203
In more than two years but not more than five years	<b>435</b>	242
In more than one year but not more than two years	<b>4</b>	73
In one year or less or on demand	<b>20</b>	19
	<b>1,643</b>	1,537

The table above shows the contractual, undiscounted cash flows due in future periods to settle the company's debt. The total amount payable shown above differs from the total book value of company debt of £1,638m as the book value of debt includes the fair value of the interest rates swaps which is based on discounted cash flows.

Details of undrawn committed borrowing facilities available at 30 September are as follows:

	2006 £m	2005 £m
Expiring in		
In more than five years	<b>—</b>	—
In more than two years but not more than five years	<b>575</b>	230
In more than one year but not more than two years	<b>—</b>	—
In one year or less or on demand	<b>—</b>	—
	<b>575</b>	230

The undrawn facilities relate to the undrawn element of the syndicated bank facility.

# Notes to the Company Accounts

at 30 September 2006

## 8. Financial Instruments (continued)

### Security

The syndicated bank borrowings of £421 million and corporate bonds of £1,181 million are secured creditors.

Syndicated bank borrowings are secured by a security deed entered into by the Company and its subsidiaries excluding Enterprise Inns Holding Company Limited and its subsidiaries and Unique Pubs Limited and its subsidiaries. The lenders have a floating charge over all of the assets and undertakings of such companies. The floating charge ranks subsequent to the fixed charges created by the debenture and secured bonds.

Debenture and secured bond finance in the Company is secured pursuant to Trust Deeds entered into by the Company.

- The debenture issued on 3 February 1999 is secured by fixed charges over 190 properties created in a trust deed dated 3 February 1999.
- The secured bonds issued on 9 May 2000 are secured by fixed charges over 318 properties created in a trust deed dated 9 May 2000.
- The secured bonds issued on 15 February 2001 are secured by fixed charges over 269 properties created in a trust deed dated 15 February 2001.
- The secured bonds issued on 26 February 2002 are secured by fixed charges over 578 properties created in a trust deed dated 26 February 2002.
- The secured bonds issued on 3 March 2003 are secured by fixed charges over 1,290 properties created in a trust deed dated 3 March 2003.

# Notes to the Company Accounts

at 30 September 2006

## 9. Provisions for liabilities and charges

	<b>2006</b>	Restated*
	<b>£m</b>	2005 £m
Deferred tax (note 9a)	<b>86</b>	58
Onerous lease (note 9b)	<b>3</b>	3
	<b>89</b>	61

### a) Deferred tax

	£m
At 1 October 2005	86
Deferred tax impact of adoption of FRS 20 (note 1)	(8)
Deferred tax impact of adoption of FRS 26 (note 1)	(20)
At 1 October 2005 restated	58
Transfer of deferred tax provision relating to interest rate swap novation	12
Deferred tax charge in the profit and loss account:	
Accelerated capital allowances	4
Fair value of interest rate swaps	14
Interest rate swap novation	(2)
<b>At 30 September 2006</b>	<b>86</b>

The deferred tax in the Company balance sheet at 30 September comprises:

	<b>2006</b>	Restated*
	<b>£m</b>	2005 £m
Accelerated capital allowances	<b>90</b>	86
Interest rate swap novation	<b>10</b>	—
Fair value of interest rate swaps	<b>(6)</b>	(20)
Share-based payments	<b>(8)</b>	(8)
	<b>86</b>	58

\* See note 1.

# Notes to the Company Accounts

at 30 September 2006

## 9. Provisions for liabilities and charges (continued)

The amounts of deferred tax not provided in the accounts are as follows:

	2006 £m	2005 £m
Rolled over gains	63	24
Unrealised surplus on the revaluation of fixed assets	340	321
	<b>403</b>	<b>345</b>

No provision has been included in respect of capital gains on the disposal of properties that have already been deferred, or are expected to be deferred, through application of capital gains rollover relief into replacement assets as no liability is expected to arise.

No deferred tax has been recognised in respect of unrealised surplus on the revaluation of fixed assets as there was no binding commitment to sell properties at the balance sheet date.

### b) Onerous lease provision

	£m
<b>At 1 October 2005 and 30 September 2006</b>	<b>3</b>

The provision relates to future commitments under onerous lease agreements. The provision is expected to be utilised as the pubs are disposed of. The remaining lease terms vary from 5 to 64 years.

## 10. Share capital

Authorised:	No.	2006 £m	No.	2005 £m
Ordinary shares of 5p each	500,000,000	25	500,000,000	25
<b>Allotted, called up and fully paid:</b>				
Ordinary shares of 5p each	No.	2006 £m	No.	2005 £m
At 1 October	349,505,390	17	349,505,390	17
Cancelled	(17,340,815)	(1)	—	—
At 30 September	332,164,575	16	349,505,390	17

Ordinary shares carry no right to fixed income. Holders of ordinary shares are entitled to vote at meetings.

At 30 September 2006, the Company owned 25 million of its own shares as treasury shares with a nominal value of £1 million and a market value of £264 million (2005 — nil). Transaction costs of £3 million (2005 — nil) have been accounted for directly in equity in the profit and loss reserve.

In addition, the Company held 6,870,253 shares with a nominal value of £0.3 million and a market value of £72 million (2005 — 9,248,445 shares, nominal value £0.5 million, market value £78 million). These shares are held by the Employee Benefit Trust and Enterprise Inns Quest Trustees Limited and are shares used to satisfy awards made under the Enterprise Inns Incentive Plans and other share option schemes (note 15).



# Notes to the Company Accounts

at 30 September 2006

## 11. Reconciliation of movements in shareholders' equity

	Share Capital £m	Share premium account £m	Revaluation reserve £m	Capital redemption reserve £m	Treasury share reserve £m	Other reserve* £m	Profit and loss account £m	Total £m
At 1 October 2004 as reported	17	486	483	8	—	(28)	208	1,174
Effect of adopting FRS 21 (note 1)	—	—	—	—	—	—	29	29
Effect of adopting FRS 26 (note 1)	—	—	—	—	—	—	(3)	(3)
Deferred tax impact of adoption of FRS 20 (note 1)	—	—	—	—	—	—	4	4
Deferred tax impact of adoption of FRS 26 (note 1)	—	—	—	—	—	—	15	15
At 1 October 2004 restated	17	486	483	8	0	(28)	253	1,219
Profit for the year	—	—	—	—	—	—	153	153
Surplus on revaluation of estate	—	—	140	—	—	—	—	140
Transfer of realised Revaluation surplus	—	—	(2)	—	—	—	2	—
Equity dividends paid	—	—	—	—	—	—	(48)	(48)
Purchase of shares to be held in trust	—	—	—	—	—	(37)	—	(37)
Employee share option entitlements exercised in the year	—	—	—	—	—	3	(3)	—
Directors' share option entitlements exercised in the year	—	—	—	—	—	6	(3)	3
Share-based expense recognised in operating profit	—	—	—	—	—	—	3	3
Deferred tax on share schemes recognised in reserves	—	—	—	—	—	—	7	7
At 1 October 2005 restated	17	486	621	8	0	(56)	364	1,440
Profit for the year	—	—	—	—	—	—	1,175	1,175
Surplus on revaluation of estate	—	—	176	—	—	—	—	176
Transfer of realised revaluation surplus	—	—	(21)	—	—	—	21	—
Equity dividends paid	—	—	—	—	—	—	(70)	(70)
Consideration paid for purchase of own shares	—	—	—	—	(227)	—	(3)	(230)
Cancellation of shares	(1)	—	—	1	—	—	(166)	(166)
Employee share option entitlements exercised in the year	—	—	—	—	—	11	(7)	4
Directors' share option entitlements exercised in the year	—	—	—	—	—	3	(3)	—
Share-based expense recognised in operating profit	—	—	—	—	—	—	3	3
Deferred tax on share schemes recognised in reserves	—	—	—	—	—	—	5	5
<b>At 30 September 2006</b>	<b>16</b>	<b>486</b>	<b>776</b>	<b>9</b>	<b>(227)</b>	<b>(42)</b>	<b>1,319</b>	<b>2,337</b>

\* Other reserve comprises own shares held by employee share trusts.

# Notes to the Company Accounts

at 30 September 2006

## 12. Profit earned for ordinary shareholders

The Profit and Loss Account is not included in the Company's accounts by virtue of the exemption granted by section 230 of the Companies Act 1985. Profit after tax during the year amounted to £1,175 million (2005 — £153 million as restated for the adoption of FRS 20 and FRS 26 — see note 1).

Remuneration paid to the auditors in the year was as follows. This note is shown rounded to the nearest thousand.

	<b>2006</b> <b>£000</b>	2005 £000
Audit of the financial statements	<b>154</b>	130
Other fees to auditors:		
Taxation services	<b>120</b>	103
Accounting advice in relation to share-based payment schemes	<b>28</b>	63
Company secretarial services	<b>8</b>	46
Other services	—	4
	<b>310</b>	346

## 13. Staff costs

	<b>2006</b> <b>£m</b>	2005 £m
Wages and salaries	<b>24</b>	26
Social security costs	<b>3</b>	3
Other pension costs	<b>2</b>	2
	<b>29</b>	31

Included in wages and salaries is a total expense relating to share-based payments of £3 million (2005 — £3 million). All of this expense arises from transactions accounted for as equity-settled share-based payments

Other pension costs represents payments made into employees individual defined contribution plans.

The average monthly number of employees comprised:

	<b>2006</b> <b>No.</b>	2005 No.
Operations staff	<b>244</b>	230
Administration staff	<b>283</b>	309
	<b>527</b>	539

Details of Directors' Remuneration is given in the Directors' Remuneration Report.

# Notes to the Company Accounts

at 30 September 2006

## 14. Dividends

	2006	2005
<b>Paid during the year</b>	<b>£m</b>	<b>£m</b>
Equity dividends on ordinary shares:		
Final dividend relating to prior year 14.4 pence (2004 — 8.4 pence)	<b>42</b>	29
Interim dividend for current year 9.0 pence (2005 — 5.6 pence)	<b>28</b>	19
	<b>70</b>	48
<b>Proposed for approval by shareholders at the AGM</b>		
Final dividend for current year 18.0 pence (2005 — 14.4 pence)	<b>54</b>	42

The dividends relating to shares held by the Employee Benefit Trust and shares held in treasury have been waived.

## 15. Share-based payments

The Company operates share-based payment schemes for both directors and other employees. Details of the Short-Term Incentive Plan (STIP) and Long-Term Incentive Plan (LTIP) which form part of the remuneration of the executive directors' are given in the Directors' Remuneration Report on pages 28 to 37.

The Company also operates an Employee Share Option Scheme (ESOS), a Savings Related Share Option Scheme (SAYE) and a Share Incentive Plan (SIP).

### Share Incentive Plan

The SIP is open to all employees. At times determined by the Company, employees may allocate the lower of £1,500 and 10% of pre-tax salary to purchase shares out of their salary. The Board may also decide to award matching shares. The shares are held in trust on behalf of the employee. If shares are removed from trust within three years, any allocation of matching shares may be lost. Shares can be transferred tax-free to employees after a period of five years. This scheme is operating for the first time in 2005/06 and matching shares were awarded. The cost of the matching shares is being spread over the three year vesting period of the scheme.

### Employee Share Option Scheme

The ESOS scheme is open to all employees. Share options are awarded to employees at the discretion of the Board. The current intention of the Board is to issue options with an exercise price equal to the market value of a share at grant date. Options will normally vest after 3 years if an employee remains in service and if EPS growth targets are met. For options granted during the year ended 30 September 2006 options will only vest in full if the average compound annual percentage growth in adjusted EPS between the grant date and the third anniversary of the grant date is 8.33%. Options may normally only be exercised during the period of 7 years commencing on the third anniversary of the date of grant of the option. Options will usually be settled by issuing ordinary shares held by the Employee Benefit Trust.

# Notes to the Company Accounts

at 30 September 2006

## 15. Share-based payments (continued)

Details of the share options outstanding during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price £	Number of share options	Weighted average exercise price £
Outstanding at 1 October	4,335,827	4.43	4,536,348	3.08
Granted	1,020,750	8.89	1,192,500	7.18
Exercised	(1,698,746)	2.83	(1,344,043)	2.33
Forfeited/expired	(341,697)	6.08	(48,978)	4.23
Outstanding at 30 September*	3,316,134		4,335,827	4.43
Weighted average remaining contractual life		6.5 years		5.9 years

\* Included in this balance are 133,731 options (2005 — 453,327) which have not been accounted for under FRS 20 as they were granted before 7 November 2002. Such options are not accounted for under FRS 20 in line with the transitional provisions of this standard. Options will only vest in full if certain performance criteria are met.

Options outstanding at 30 September 2006 comprise the following:

Exercise date	Number of share options	Exercise price
<b>Exercisable:</b>		£
14/12/02–14/12/09	1,344	1.63
18/12/03–18/12/10	52,828	1.70
11/12/04–11/12/11	79,559	2.58
16/12/05–16/12/12	258,740	2.81
	392,471	
<b>Not yet exercisable:</b>		
08/12/06–08/12/13	940,000	4.90
07/12/07–07/12/14	800,250	7.02
18/05/08–18/05/15	289,500	7.57
06/12/09–06/12/16	893,913	8.89
	2,923,663	
	3,316,134	

The weighted average fair value of options granted during the year under the ESOS was £1.46 (2005 — £1.31).

# Notes to the Company Accounts

at 30 September 2006

## 15. Share-based payments (continued)

### Savings-Related Share Option Scheme

The SAYE scheme is open to executive directors and employees at the discretion of the Board. Participants contract to save a fixed amount each month with a savings institution for a period of five or seven years. At the end of the savings term, participants are given the option to purchase shares at a price set before the savings began. The option price will be not less than 80% of the market value of a share on the date that participants are invited to take part in the scheme, or the nominal value of a share if lower. Options will usually be settled using ordinary shares held by Enterprise Inns Quest Trustees Ltd (an employee benefit trust) and will usually be exercisable for six months after the fifth or seventh anniversary of the commencement of the savings contract.

Details of the share options outstanding during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price £	Number of share options	Weighted average exercise price £
Outstanding at 1 October	915,136	2.70	946,134	2.18
Granted	130,774	7.07	144,016	5.45
Exercised	(209,579)	1.27	(102,135)	1.53
Forfeited/expired	(58,464)	4.78	(72,879)	3.02
Outstanding at 30 September*	777,867		915,136	2.70
Weighted average remaining contractual life		2.8 years		2.9 years

\* Included in this balance are 142,146 options (2005: 351,058) which have not been accounted for under FRS 20 as they were granted before 7 November 2002. Such options are not accounted for under FRS 20 in line with the transitional provisions of this standard.

Options outstanding at 30 September 2006 comprise the following:

Exercise date	Number of share options	Exercise price
<b>Not yet exercisable:</b>		
01/02/07–01/08/07	28,700	1.41
01/02/08–01/08/08	5,576	1.25
01/02/07–01/08/09	107,870	2.10
01/02/08–01/08/10	267,745	2.32
01/02/09–01/08/11	137,213	3.73
01/02/10–01/08/12	116,349	5.45
01/02/11–01/08/13	114,414	
	777,867	

The weighted average fair value of options granted during the year under the SAYE scheme was £2.60 (2005 – £2.12).

# Notes to the Company Accounts

at 30 September 2006

## 15. Share-based payments (continued)

### STIP and LTIP

Executive directors are eligible to participate in the STIP and LTIP plans. A summary of the rules of these schemes along with details of options that have been granted and are outstanding in relation to individual directors is included in the Directors' Remuneration Report on pages 28 to 37.

Details of the total number of shares outstanding during the year are as follows:

	2006		2005	
	LTIP Number of share options	STIP Number of share options	LTIP Number of share options	STIP Number of share options
Outstanding at 1 October	<b>1,665,436</b>	<b>135,133</b>	1,624,478	163,508
Granted†	<b>347,979</b>	<b>48,335</b>	410,578	52,283
Exercised	<b>(453,383)</b>	<b>(44,368)</b>	(369,620)	(80,658)
Forfeited/expired	<b>(111,475)</b>	<b>(725)</b>	—	—
Outstanding at 30 September*	<b>1,448,557</b>	<b>138,375</b>	1,665,436	135,133
Weighted average remaining contractual life	<b>4.9 years</b>	<b>3.0 years</b>	6.8 years	5.7 years

Directors pay £1 to exercise awards granted under the STIP and LTIP. This is a one-off charge. All of the shares outstanding at 30 September are not yet exercisable.

† The share price at which the number of shares granted under the STIP scheme is calculated will not be confirmed until after the date of the approval of the accounts. The number of STIP shares granted during the year is therefore estimated using the closing share price on 30 September 2006.

\* Included in this balance are 40,941 LTIP shares (2005: 494,324) which have not been accounted for under FRS 20 as they were granted before 7 November 2002. Such shares are not accounted for under FRS 20 in line with the transitional provisions of this standard.

Awards will only vest in full if certain performance criteria are met.

The weighted average fair value of shares granted during the year under the STIP was £9.51 (2005 — £8.07) and under the LTIP was £5.90 (2005 — £5.03).

The weighted average share price on exercise of shares and share options during the year was £9.56.

# Notes to the Company Accounts

at 30 September 2006

## 15. Share-based payments (continued)

### Fair value of share schemes

The fair value of equity-settled share options granted is estimated at the date of grant using share option valuation models. The ESOS, SAYE and STIP schemes are valued using the Black-Scholes model. The element of the LTIP scheme that relates to non-market conditions is valued using the Black-Scholes model. The element of the LTIP that includes market conditions is valued using the Monte Carlo Simulation Model.

The following tables list the inputs to the models for options granted during the year:

Weighted average:	ESOS		SAYE	
	2006	2005	2006	2005
Share price (£)	9	7.18	9	6.81
Exercise price (£)	9	7.18	7	5.45
Dividend yield	2.4%	2.2%	2.4%	2.2%
Expected volatility	21%	23%	21%	22%
Risk-free interest rate	4.2%	4.3%	4.2%	4.46%
Expected life of option (years)	3.3	3.3	5 or 7	5 or 7

Weighted average:	STIP		LTIP	
	2006	2005	2006	2005
Share price (£)	10.55	8.81	8.81	6.84
Exercise price (£)	—	—	—	—
Dividend yield	2.4%	2.2%	2.4%	2.2%
Expected volatility	22%	22%	21%	22%
Risk-free interest rate	4.3%	4.48%	4.2%	4.42%
Expected life of option (years)	4	4	3-5*	3-5*

Expected share price volatility is based on historic volatility over the same period of time as the vesting period of the option. The expected life of an option is based on historical data.

The LTIP will only vest in full if a TSR target is met. This is a market condition and the TSR performance criteria has therefore been taken into account when calculating the fair value of the options granted under the LTIP. These conditions have been incorporated into the Monte-Carlo Simulation model which is used to fair value the TSR element of the scheme.

\* The LTIP vests in three equal tranches after 3, 4 and 5 years.

## 16. Related parties

The Company has taken advantage of the exemption in FRS 8 not to disclose transactions with other Group companies.

# Notes to the Company Accounts

at 30 September 2006

## 17. Capital commitments

Amounts contracted for but not provided in the accounts amounted to £6 million (2005 — £5 million).

## 18. Other financial commitments

At 30 September 2006 the Company had annual commitments under non-cancellable operating leases for land and buildings as set out below:

	2006 £m	2005 £m
Operating leases that expire:		
within one year	—	—
within two to five years	—	—
in over five years	2	4
	<b>2</b>	<b>4</b>

## 19. Events after the balance sheet date

On 20 November 2006 the Company entered into a binding agreement to sell its entire Scottish estate of 41 pubs to Retail & Licensed Properties Limited for consideration of £32 million.



# Directors' Responsibilities

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Generally Accepted Practice.

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 of the profit or loss of the Company 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 Company 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 to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

# Independent Auditors' Report to the Members of Enterprise Inns plc

We have audited the parent company financial statements of Enterprise Inns plc for the year ended 30 September 2006 which comprise Balance Sheet and the related notes 1 to 19. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Group financial statements of Enterprise Inns plc for the year ended 30 September 2006.

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, the Directors' Remuneration Report and the parent company financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the parent company financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the parent company financial statements give a true and fair view, the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and whether the information given in the parent company Directors' Report is consistent with the financial statements.

We also report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the Financial Highlights, the Chairman's Statement, the Chief Executive's Review (incorporating the Business Review), the Corporate Responsibility Report, Directors and Advisers and the unaudited part of the Directors' Remuneration Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

## Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent company financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the parent company financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the parent company financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the parent company financial statements and the part of the Directors' Remuneration Report to be audited.

# Independent Auditors' Report to the Members of Enterprise Inns plc

## Opinion

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 30 September 2006;
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the directors' report is consistent with the parent company financial statements.

## Ernst & Young LLP

Registered auditor  
Birmingham

21 November 2006

## Note:

The maintenance and integrity of the Enterprise Inns plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

## Analysis of Ordinary Shareholders

Range	Number of Shareholders	%	Shares Held	%
1-1,000	1,025	37.7	468,293	0.1
1,001-10,000	1,012	37.2	3,376,027	1.0
10,001-50,000	305	11.2	7,366,718	2.2
50,001-100,000	89	3.3	6,333,746	1.9
100,001-150,000	56	2.1	7,049,219	2.1
150,001-500,000	116	4.3	31,775,270	9.6
500,001-1,000,000	57	2.1	41,504,336	12.5
1,000,001-5,000,000	45	1.7	95,838,165	28.9
5,000,001 and over	12	0.4	138,452,801	41.7
	2,717	100.0	332,164,575	100.0

The total number of shares held includes 25,000,000 shares held in treasury and 6,870,253 shares held in Employee Benefit Trusts.

# Financial Calendar

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## 2006

Preliminary announcement of annual results to 30 September 2006	21 November
Final dividend — ordinary shares: ex dividend date	27 December
Final dividend — ordinary shares: record date	29 December

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## 2007

Annual General Meeting	16 January
Final dividend — ordinary shares: payment date	22 January
Announcement of interim results	15 May
Interim dividend — ordinary shares: record date	8 June
Interim dividend — ordinary shares: payment date	4 July
Preliminary announcement of annual results to 30 September 2007	20 November

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# Shareholder Information

## Shareholder Enquiries



The Company's registrars, Computershare Investor Services PLC, keep the Company's register of shareholders up to date, distribute statutory documents and administer the payment of dividends. If you have a query regarding your shareholding please contact them direct by using the dedicated telephone enquiry line 0870 889 4080.

You can also use the registrar's website to check your shareholding and maintain your records. Details can be found at [www.computershare.com/uk/investor/etp](http://www.computershare.com/uk/investor/etp)

## Dividend Payments

Dividends can be paid direct to UK bank or building society accounts using the BACS system so that your dividend can be paid into your account on the same day the Company makes payment. A tax voucher will still be provided and sent to shareholders by post. Shareholders who wish to arrange direct payment using this method should telephone the registrars on 0870 889 4080. You can also register online or download a printable mandate form at [www.computershare.com/uk/investor/etp](http://www.computershare.com/uk/investor/etp)

## Electronic Communications



The Company has introduced innovative ways of communicating with shareholders electronically via eTree, an environmental incentive programme. For every shareholder who signs up to receive electronic communications we will donate a sapling to the Woodland Trust, the UK's leading woodland conservation charity. All saplings will be planted through the Trust's 'Tree for All' campaign, a national tree planting and education programme, working with schools and communities to plant 12 million trees. For details and to register to receive future communications electronically, please visit [www.etreeuk.com/enterpriseinns](http://www.etreeuk.com/enterpriseinns)

## Share Dealing Service

The registrars also offer a share dealing service which allows you to buy and sell the Company's shares if you are a UK resident. You can deal in your shares on the internet or by phone.

Log onto [www.computershare.com/dealing/uk](http://www.computershare.com/dealing/uk) or call 0870 703 0084 between 8.00 am and 4.30 pm, Monday to Friday, for more information about this service and details of the rates.

# Notice of Annual General Meeting

**This notice is important and requires your immediate attention. If you are in any doubt about the action you should take, you should immediately consult your stockbroker, bank manager, solicitor, accountant or other independent financial adviser duly authorised under the Financial Services and Markets Act 2000.**

**The 2007 Annual General Meeting of Enterprise Inns plc (the “Company”) will be held at the offices of the Company, 3 Monkspath Hall Road, Solihull, West Midlands, B90 4SJ at 11.00 a.m. on 16 January 2007 for the following purposes:**

## **Ordinary resolutions**

To consider and, if thought fit, to pass the following resolutions, which will be proposed as ordinary resolutions:

1. To receive the directors’ report and the audited accounts for the year ended 30 September 2006 and the auditors’ report on the accounts.
2. To approve the directors’ remuneration report for the year ended 30 September 2006.
3. To declare a final dividend of 18 pence per ordinary share of the Company for the year ended 30 September 2006, which shall be payable to shareholders who are on the register of members as at the close of business on 29 December 2006.
4. To reappoint Mr D A Harding as a director.
5. To reappoint Mr W S Townsend as a director.
6. To reappoint Ernst & Young LLP as auditors of the Company, to hold office until the conclusion of the next Annual General Meeting of the Company.
7. To authorise the directors to determine Ernst & Young LLP’s remuneration as auditors of the Company.
8. THAT the directors be generally and unconditionally authorised (in substitution for all subsisting authorities to the extent unused) to exercise all powers of the Company to allot relevant securities (within the meaning of section 80(2) of the Companies Act 1985) up to an aggregate nominal amount of £4,982,879. This authority shall expire (unless previously varied, revoked or renewed by the Company in general meeting) 15 months after the date of the passing of this resolution or, if earlier, at the conclusion of the Annual General Meeting of the Company in 2008, except that the Company may

before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the directors may allot relevant securities in pursuance of such offer or agreement as if the authority conferred by this resolution had not expired.

9. THAT, conditional upon the admission of the new ordinary shares of 2<sup>1</sup>/<sub>2</sub> pence each (as referred to below) to the Official List of the UK Listing Authority and to trading on London Stock Exchange plc’s market for listed securities occurring by 8.00 a.m. on 17 January 2007 (or such other time and/or date as the directors may in their absolute discretion determine), each of the Company’s issued and unissued existing ordinary shares of 5 pence each be sub-divided into two new ordinary shares of 2<sup>1</sup>/<sub>2</sub> pence each.

## **Special resolutions**

To consider and, if thought fit, to pass the following resolutions, which will be proposed as special resolutions:

10. THAT, subject to the passing of resolution 8, the directors be and are empowered pursuant to section 95 of the Companies Act 1985 to allot equity securities (as defined in section 94(2) of that Act) for cash pursuant to the general authority conferred on them by resolution 8 and/or to sell equity securities held as treasury shares for cash pursuant to section 162D of that Act, in each case as if section 89(1) of that Act did not apply to any such allotment or sale, provided that this power shall be limited to:
  - (a) any such allotment and/or sale of equity securities in connection with an issue or offer by way of rights or other pre-emptive issue or offer, open for acceptance for a period fixed by the directors, to holders of ordinary shares (other than the Company) on the register on any record date fixed by the directors in proportion (as nearly as may be) to the respective number of ordinary shares deemed to be held by them, subject to such exclusions or other arrangements as the directors may deem necessary or expedient in relation to fractional entitlements, legal or practical problems arising in any overseas territory, the requirements of any regulatory body or stock exchange or any other matter whatsoever; and
  - (b) any such allotment and/or sale, otherwise than

# Notice of Annual General Meeting

pursuant to sub-paragraph (a) above, of equity securities for cash having, in the case of relevant shares (as defined in section 94(5) of that Act), an aggregate nominal value, or, in the case of other equity securities, giving the right to subscribe for or convert into relevant shares having an aggregate nominal value, not exceeding in aggregate the sum of £810,006.

This authority shall expire, unless previously renewed, revoked or varied by the Company in general meeting, at such time as the general authority conferred on the directors by resolution 8 expires, except that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted or equity securities held as treasury shares to be sold after such expiry and the directors may allot equity securities and/or sell equity securities held as treasury shares in pursuance of such offer or agreement as if the power conferred by this resolution had not expired.

11. THAT the Company be and is generally and unconditionally authorised to make market purchases (as defined in section 163(3) of the Companies Act 1985) of:

- (a) (if resolution 9 is passed) its ordinary shares of 2½ pence each provided that:
- (i) the maximum number of ordinary shares that may be acquired is 89,641,002;
  - (ii) the minimum price per ordinary share that may be paid for any such share (excluding expenses) is 2½ pence; and
  - (iii) the maximum price (exclusive of expenses) which may be paid for each ordinary share shall not be more than the higher of:
    - (A) 105% of the average of the market values of such ordinary shares (as derived from the Daily Official List of the London Stock Exchange) for the five business days immediately preceding the date on which the purchase is made; and
    - (B) that stipulated by Article 5 (1) of the Buy-back and Stabilisation Regulation (EC 2273/2003); or
- (b) (if resolution 9 is not passed) its ordinary shares of 5 pence each provided that:

- (i) the maximum number of ordinary shares that may be acquired is 44,820,501;
- (ii) the minimum price per ordinary share that may be paid for any such share (excluding expenses) is 5 pence; and
- (iii) the maximum price (exclusive of expenses) which may be paid for each ordinary share shall not be more than the higher of:
  - (A) 105% of the average of the market values of such ordinary shares (as derived from the Daily Official List of the London Stock Exchange) for the five business days immediately preceding the date on which the purchase is made; and
  - (B) that stipulated by Article 5 (1) of the Buy-back and Stabilisation Regulation (EC 2273/2003).

This authority shall expire, unless previously renewed, revoked or varied by the Company in general meeting, 15 months after the date of the passing of this resolution or, if earlier, at the conclusion of the Annual General Meeting of the Company in 2008, except that the Company may, at any time before the expiry of this authority, enter into a contract or contracts to purchase ordinary shares which would or might be completed wholly or partly after such expiry and purchase ordinary shares in accordance with such contract as if the authority conferred by this resolution had not expired.

**The directors believe that the proposals in resolutions 1 to 11 are in the best interests of shareholders as a whole and they unanimously recommend that you vote in favour of all the resolutions.**

On behalf of the Board

**D C George**  
Company Secretary

21 November 2006

Registered office:

3 Monkspath Hall Road  
Solihull  
West Midlands, B90 4SJ

Registered in England and Wales No. 2562808



# Notice of Annual General Meeting

## Notes

1. A shareholder of the Company who is entitled to attend and vote at the Annual General Meeting may appoint one or more proxies to attend and, on a poll, vote instead of him. A proxy does not need to be a shareholder of the Company.
2. A personalised form of proxy for use in connection with the Annual General Meeting is enclosed with the document of which this notice forms part. If you do not have a personalised form of proxy and believe that you should, please contact the Company's registrars, Computershare Investor Services PLC, on 0870 889 4080 or at Computershare Investor Services PLC, P.O. Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH. Completion and return of a form of proxy will not preclude a shareholder from attending and voting at the Annual General Meeting.
3. To appoint a proxy or proxies shareholders must complete: (a) a form of proxy, sign it and return it, together with the power of attorney or other authority (if any) under which it is signed, or a notarially certified copy of such authority, to the Company's registrars, Computershare Investor Services PLC, PO Box 1075, The Pavilions, Bridgwater Road, Bristol, BS99 3FA; or (b) a CREST Proxy Instruction (as set out in paragraph 4 below); or (c) an online proxy appointment at [www.computershare.com/uk/voting/etp](http://www.computershare.com/uk/voting/etp) (you will need your unique PIN and Shareholder Reference Number printed on your personalised form of proxy), in each case so that it is received no later than 11.00 a.m. on 14 January 2007.
4. CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so for the Annual General Meeting and any adjournment(s) of the meeting by using the procedures described in the CREST Manual. CREST Personal Members or other CREST sponsored members and those CREST members who have appointed any voting service provider(s) should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf.

In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with

CRESTCo Limited's specifications and must contain the information required for such instructions, as described in the CREST Manual. The message, regardless of whether it constitutes the appointment of a proxy or an amendment to the instruction given to a previously appointed proxy must, in order to be valid, be transmitted so as to be received by the Company's agent (ID 3RA50) by the latest time for receipt of proxy appointments set out in paragraph 3 above. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the Company's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

CREST members and, where applicable, their CREST sponsors or voting service providers should note that CRESTCo Limited does not make available special procedures in CREST for any particular messages. Normal system timings and limitations will therefore apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member or sponsored member or has appointed any voting service provider(s), to procure that his CREST sponsor or voting service provider(s) take(s)) such action as is necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting service providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.

The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001.

5. Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, the Company gives notice that only those shareholders included in the register of members of the Company at 6.00 p.m. on 14 January 2007 or, if the meeting is adjourned, in the register of members at 6.00 p.m. on the day

# Notice of Annual General Meeting

which is two days before the day of any adjourned meeting, will be entitled to attend and to vote at the Annual General Meeting in respect of the number of shares registered in their names at that time.

Changes to entries on the share register after 6.00 p.m. on 14 January 2007 or, if the meeting is adjourned, in the register of members at 6.00 p.m. on the day which is two days before any adjourned meeting, will be disregarded in determining the rights of any person to attend or vote at the Annual General Meeting.

6. Copies of the directors' service contracts, the directors' remuneration report and the register of directors' interests are available for inspection at the Company's registered office during normal business hours on any weekday (excluding Saturdays, Sundays and public holidays) until the end of the Annual General Meeting and will also be available for inspection at the place of the Annual General Meeting for at least 15 minutes before and during the Annual General Meeting.
7. If you have sold or otherwise transferred all your ordinary shares in the Company, please forward this document to the purchaser or transferee or to the stockbroker, bank or other person through whom the sale or transfer was effected for transmission to the purchaser or transferee.

# Explanatory Notes to the Notice of Annual General Meeting

**The notice of the Annual General Meeting of the Company to be held on Thursday, 16 January 2007 is set out on pages 121 to 124 of this document. The following notes provide an explanation as to why the resolutions set out in the notice are to be put to shareholders.**

**Resolutions 1 to 8 are ordinary resolutions. These resolutions will be passed if more than 50% of the votes cast for or against are in favour.**

## **Resolution 1 – Laying of Accounts**

The directors are required by the Companies Act 1985 (the “Act”) to present to the shareholders of the Company at a general meeting the reports of the directors and auditors, and the audited accounts of the Company, for the year ended 30 September 2006. The report of the directors and the audited accounts have been approved by the directors, and the report of the auditors has been approved by the auditors, and a copy of each of these documents may be found in the annual report and accounts, starting at page 1.

## **Resolution 2 – Remuneration Report**

The Act requires the Company to seek shareholder approval for the Directors’ Remuneration Report at the general meeting before which the Company’s annual accounts are laid. The Directors’ Remuneration Report is included in the annual report and accounts, starting at page 28. If shareholders vote against the report the directors will still be paid but the Remuneration Committee will reconsider its policy.

## **Resolution 3 – Declaration of a Final Dividend**

An interim dividend of 9 pence (net) has already been paid in respect of the 2005/2006 financial year. The directors are recommending a final dividend of 18 pence (net) per ordinary share of 5 pence, payable on 22 January 2007 to holders on the register as at 6.00 p.m. on 29 December 2006. The final dividend will not be paid without shareholder approval and its amount may not exceed the amount recommended by the directors.

For the avoidance of doubt, the final dividend will not be paid to those persons that are holders of ordinary shares of 2½ pence each at the date of payment in respect of their shareholdings on the payment date. It will be paid to those persons that were recorded on

the register at close of business on 29 December 2006 as holders of ordinary shares of 5 pence each in respect of their respective holdings at close of business on 29 December 2006.

## **Resolutions 4 and 5 – Reappointment of Mr D A Harding and Mr W S Townsend**

The Company’s articles of association require that any director who was not appointed or reappointed at either of the last two annual general meetings before this meeting must retire, although they may offer themselves for reappointment. Mr D A Harding and Mr W S Townsend are retiring and seeking reappointment. Biographical information for Mr D A Harding and Mr W S Townsend is shown on pages 13 to 14 of the annual report and accounts. Details of why the Board believes they should be re-elected are included in the directors reporting in the annual report and accounts starting at page 15.

## **Resolution 6 – Auditors’ appointment**

The Act requires that auditors be appointed at each general meeting at which accounts are laid, to hold office until the next such meeting. The resolution seeks shareholder approval for the reappointment of Ernst & Young LLP. The Audit Committee keeps under review the independence and objectivity of the external auditors, further information on which can be found in the annual report and accounts on page 24. After considering relevant information the Audit Committee recommended to the Board of directors the reappointment of Ernst & Young LLP.

## **Resolution 7 – Auditors’ remuneration**

This resolution gives the directors the authority to determine the remuneration of the auditors for the audit work to be carried out by them in the next financial year. The amount of the remuneration paid to the auditors for the next financial year will be disclosed in the next audited accounts of the Company.

## **Resolution 8 – Authority to the directors to allot shares**

Under the Act the directors may only allot shares if authorised by shareholders to do so. If passed, this resolution will authorise the directors to allot and issue new shares up to an aggregate nominal value of £4,982,879 (up to 199,315,186 new ordinary shares of

# Explanatory Notes to the Notice of Annual General Meeting

2<sup>1</sup>/<sub>2</sub> pence each if resolution 9 is passed and up to 99,657,593 new ordinary shares of 5 pence each if resolution 9 is not passed), which is equal to approximately one-third (33.33%) of the issued share capital of the Company (excluding treasury shares) as at 1 December 2006, being the latest practicable date prior to the publication of the notice. The authority will expire 15 months after the date of passing of the resolution or, if earlier, at the conclusion of the Annual General Meeting of the Company in 2008.

Passing this resolution will continue the directors' flexibility to act in the best interests of shareholders, when opportunities arise, by issuing new shares. The directors currently have no intention of issuing new shares.

As at 1 December 2006, being the latest practicable date prior to the publication of the notice, the Company had 299,002,681 ordinary shares of 5 pence each in issue and held 25,000,000 treasury shares, which is equal to approximately 8.36% of the issued share capital of the Company (excluding treasury shares) as at that date.

## **Resolution 9 — Sub-division of ordinary share capital**

This resolution, if passed, will sub-divide each of the ordinary shares of 5 pence in the Company into two ordinary shares of 2<sup>1</sup>/<sub>2</sub> pence. The directors believe that having a larger number of shares with a lower market value should attract and retain larger numbers of private shareholders and ensure the continuing liquidity of the Company's shares.

The financial position of the Company will not be affected by the sub-division of the ordinary shares. The sub-division will not reduce the Company's assets, liabilities or shareholders' funds. The Company's authorised and issued share capital will remain of the same amount. Each shareholder will hold the same percentage interest in the issued capital of the Company immediately after the sub-division becomes effective as that shareholder held before. The new ordinary shares of 2<sup>1</sup>/<sub>2</sub> pence each will in all respects carry the same rights as the existing ordinary shares of 5 pence each.

If resolution 9 is passed, application will be made for

the admission of the new ordinary shares of 2<sup>1</sup>/<sub>2</sub> pence each to the Official List of the UK Listing Authority and for their admission to trading on the market for listed securities of London Stock Exchange plc. Dealings in the new ordinary shares are expected to commence on 17 January 2007. At that time the Company's former ordinary shares of 5 pence each will be removed from the Official List and no longer traded.

For holdings in uncertificated form, it is expected that the appropriate share accounts in CREST will be credited with shareholders' entitlements to the new ordinary shares with effect from 17 January 2007. For holdings in certificated form, new share certificates will be sent to shareholders (at their own risk) as soon as practicable after 17 January 2007. Certificates for the former ordinary shares of 5 pence each will cease to be valid upon the issue of the new share certificates; they should be destroyed or, at the Company's request, delivered to the Company or as it may direct.

In accordance with the rules of the Enterprise Inns 1995 Executive Share Option Scheme, Enterprise Inns 1995 Savings Related Share Option Scheme, Enterprise Inns Incentive Plan 2002, Enterprise Inns 2005 Share Incentive Plan, Enterprise Inns 2005 Annual Bonus Plan, Enterprise Inns 2005 Employee Share Option Scheme, Enterprise Inns 2005 Save as you Earn Scheme and Enterprise Inns 2005 Long Term Incentive Plan (together the "Share Schemes"), the directors may, if appropriate, make adjustments to the number of ordinary shares comprised in each outstanding option and the price at which such options are exercisable. In the case of HMRC approved share options, such adjustments will be subject to HMRC approval. Option holders will be informed of the adjustments in accordance with the terms of the Share Schemes. The remuneration committee is empowered to adjust, in any manner, the number of ordinary shares comprised in any incentive after it has vested that it deems appropriate to counteract the effect of the proposed sub-division on the value of the incentive. The Company's auditors must confirm in writing that any such adjustment is fair and reasonable before it is implemented.

# Explanatory Notes to the Notice of Annual General Meeting

**Resolutions 10 and 11 are special resolutions. These resolutions will be passed if not less than 75% of the votes cast for and against are in favour.**

## **Resolution 10 — Disapplication of statutory pre-emption rights**

If the Company issues new shares for cash it must first offer them to existing shareholders in proportion to their current holdings, in compliance with their statutory pre-emption rights. If passed, this resolution will authorise the directors to modify these rights to deal with legal, regulatory or practical problems that may arise on a rights or other pre-emptive offer or issue.

The resolution also seeks shareholder authority to issue a limited number of shares for cash and/or sell treasury shares without offering them to shareholders first. The authority is for an aggregate nominal amount of up to 5% of the aggregate nominal value of the issued share capital of the Company as at 1 December 2006, being the latest practicable date prior to the publication of the notice (up to 32,400,268 new ordinary shares of 2½ pence each if resolution 9 is passed and up to 16,200,134 new ordinary shares of 5 pence if resolution 9 is not passed). The authority will expire at the same time as the authority to allot shares given pursuant to resolution 8.

The directors consider this authority necessary in order to give them flexibility to deal with opportunities as they arise, subject to the restrictions contained in the resolution.

## **Resolution 11 — Purchase of own shares by the Company**

If passed this resolution will grant the Company authority for a period of up to 15 months after the date of passing of the resolution to buy its own shares in the market. The resolution limits the number of shares that may be purchased to 14.99% of the Company's issued share capital (excluding treasury shares) as at 1 December 2006, being the latest practicable date prior to the publication of the notice. The price per ordinary share that the Company may pay is set at a minimum amount (excluding expenses) of 2½ pence per ordinary share (if resolution 9 is passed) and 5 pence per ordinary share (if resolution 9 is not passed) and a maximum amount (excluding expenses) of the higher of: (i) 5 per cent over the average of the previous 5 days' middle market prices

and (ii) the higher of the price of the last independent trade and the highest current independent bid on the trading venues where the purchase is carried out. This authority will only be exercised if market conditions make it advantageous to do so.

On 21 November 2006 (the date of the notice) the Company announced its intention to continue its rolling share buy-back programme. The directors intend to use the authority granted pursuant to this resolution in pursuance of the share buy-back programme. Further details of the share buy-back programme are set out in the Chairman's Statement and the Chief Executive's Review in the annual report and accounts, starting at page 2.

The directors' present intention is that shares purchased pursuant to this authority (to the extent statutory requirements are met) will be cancelled immediately on purchase. Alternatively the shares may be held in treasury (provided any treasury shares held do not exceed 10% of the Company's issued share capital), sold for cash (provided Listing Rule requirements are met) or transferred to an employee share scheme. The effect of any cancellation would be to reduce the number of shares in issue. For most purposes, while held in treasury shares are treated as if they have been cancelled (for example, they carry no voting rights and do not rank for dividends). The directors will only make purchases under this authority and/or the rolling share buy-back programme if they believe that to do so would result in an increased earnings per share and would be in the interests of shareholders generally.

As at 1 December 2006, being the latest practicable date prior to the publication of the notice, options were outstanding over 4,057,974 ordinary shares of 5 pence each in the Company representing approximately 1.36% of the issued share capital of the Company (excluding treasury shares) at that date. If the proposed market purchase authority were used in full, shares over which options were outstanding would, as at 1 December 2006, being the latest practicable date prior to the publication of the notice, represent approximately 1.60% of the Company's adjusted issued share capital (excluding treasury shares) at that date.







The Piccadilly

**THE PICCADILLY, CAERPHILLY, MID GLAMORGAN**  
**WINNER – Tenanted or leasehold Pub of the Year**  
 Morning Advertiser Pub Awards

Mark Parry and Tracy Hammond’s business plan transformed a basic local pub into a stylish venue, including a grand dining room overlooking Caerphilly Castle. They have attracted a new set of customers whilst retaining their place in the community.



The Lion

**LION, TEDDINGTON**  
**WINNER – London Pub of the Year** CAMRA

Cask ale is the lifeblood of the Lion, where Don Witts and Myfawny Williams maintain exceptional quality standards whilst constantly reviewing and updating their mix of beer styles and brands.



Inn on the Green

**INN ON THE GREEN, BRISTOL**  
**WINNER – Bristol Pub of the Year 2006** CAMRA

Oliver Bainbridge’s transformation of this pub began in 2003. As well as offering a distinctly upmarket food menu, the pub currently serves a range of more than 10 different real ales and attracts a wide range of clientele.



Ye Old Sun Inn

**YE OLD SUN INN, COLTON, NORTH YORKSHIRE**  
**WINNER – Pub Food innovation of the year 2006**

The Publican Food Awards

Since Ashley and Kelly McCarthy’s arrival at the pub two years ago, Ye Old Sun’s status has evolved from a good-food venue into innovative gastropub. Head chef Ashley grows his own range of herbs and vegetables to provide a constant supply of fresh kitchen ingredients. In addition, an on-site delicatessen, with fresh bread baked daily, has proved a major bonus for local residents.



Thorverton Arms

**THORVERTON ARMS, EXETER**  
**WINNER – Newcomer of the year award 2006**

The Publican Food Awards

The Thorverton Arms dates back to 1542, when it first opened as a coaching inn. Garth and Melissa Pearse offer an extensive range of locally sourced products: simple fresh home-made food is presented in a comfortable and relaxed atmosphere and offered at affordable prices.

Back cover pictures (left to right)

Bell, Welford-on-Avon

English lounge, Manchester

English lounge, Manchester



## Enterprise Inns plc

3 Monkspath Hall Road, Solihull, West Midlands, B90 4SJ

Tel: +44 (0)121 733 7700

Fax: +44 (0)121 733 6447

[www.enterpriseinns.com](http://www.enterpriseinns.com)

