

Accounting policies

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and IFRS Interpretations Committee (IFRS IC) interpretations and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. Inchcape Plc is a public company limited by shares, registered in England and Wales.

ACCOUNTING CONVENTION

The consolidated financial statements have been prepared under the historical cost convention, except for available for sale financial assets, and those financial assets and financial liabilities (including derivative instruments) held at fair value through profit or loss, which are measured at fair value.

GOING CONCERN

Having assessed the principal risks and the other matters discussed in connection with the viability statement, the Directors have considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements.

CHANGES IN ACCOUNTING POLICY AND DISCLOSURES

The accounting policies have been applied consistently throughout the reporting period, other than in respect of the following standards which have been newly adopted with effect from 1 January 2018:

IFRS 9 Financial instruments

IFRS 9 brings together the classification and measurement, impairment and hedge accounting aspects of the International Accounting Standards Board's project to replace IAS 39.

Classification and measurement

IFRS 9 amends the classification and measurement of financial assets:

- Financial assets are measured at amortised cost, fair value through other comprehensive income (FVTOCI) or fair value through profit or loss (FVTPL);
- Financial assets are measured at amortised cost or FVTOCI if certain restrictive conditions are met. All other financial assets are measured at FVTPL; and
- All investments in equity instruments are measured at fair value. For those investments in equity instruments that are not held for trading, there is an irrevocable election to present gains and losses in other comprehensive income (OCI). Dividends are recognised in profit or loss.

The adoption of IFRS 9 has had no impact on the classification and measurement of the Group's financial assets or financial liabilities.

Impairment

The new impairment model in IFRS 9 is now based on an 'expected loss' model rather than an 'incurred loss' model. Under the impairment approach in IFRS 9, it is not necessary for a credit event to have occurred before credit losses are recognised. Instead, an entity should account for expected credit losses and changes in those expected credit losses. A simplified impairment model is applicable to trade and other contractual receivables with maturities that are less than 12 months. For trade and other contractual receivables with maturity longer than 12 months, entities have a choice of applying the complex three-stage model or the simplified model. The Group has applied the simplified approach to the recognition of lifetime expected credit losses for its trade receivables and the calculation of the loss allowance for these assets as at 1 January 2018 was broadly in line with the loss allowance calculated under IAS 39.

Hedge accounting

On initial application of IFRS 9, an entity may choose, as its accounting policy, to continue to apply the hedge accounting requirements of IAS 39 instead of the hedge accounting requirements of IFRS 9. The Group has elected to apply IFRS 9 hedge accounting requirements because they are more closely aligned with the way that the Group manages its risks. Under the new hedge accounting requirements:

- The 80-125% highly effective threshold has been removed;
- Risk components of non-financial items can qualify for hedge accounting provided that the risk component is separately identifiable and reliably measurable;
- An aggregated position (i.e. combination of a derivative and a non-derivative) can qualify for hedge accounting provided that it is managed as one risk exposure;
- When entities designate the intrinsic value of options, the initial time value is deferred in Other Comprehensive Income (OCI) and subsequent changes in time value are recognised in OCI;
- When entities designate only the spot element of a forward contract, the forward points can be deferred in OCI and subsequent changes in forward points are recognised in OCI. Initial foreign currency basis spread can also be deferred in OCI with subsequent changes recognised in OCI; and
- Net foreign exchange cash flow positions can qualify for hedge accounting.

IFRS 9 Financial instruments continued

The Group currently applies hedge accounting to:

- the Group’s cross currency interest rate swaps that are used to hedge the fixed interest rate risk and the forward foreign currency risks associated with the Group’s Private Placement loan notes denominated in US dollars; and
- the transactional currency exposures on the purchases of vehicles and parts in a currency other than an operating unit’s functional currency.

An assessment of the Group’s hedging relationships under IFRS 9 has been performed and it has been determined that the relationships qualify as continuing hedging relationships under the new standard and therefore the application of IFRS 9 has not had a material impact on the Group’s consolidated financial statements.

The Group has elected not to restate comparatives on initial application of IFRS 9.

IFRS 15 Revenue from contracts with customers

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. It supersedes the previous revenue recognition guidance including IAS 18 *Revenue* and IAS 11 *Construction contracts*, and has been effective for the Group from 1 January 2018.

The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the standard introduces a five-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer
- Step 2: Identify the performance obligations in the contract
- Step 3: Determine the transaction price
- Step 4: Allocate the transaction price to the performance obligations in the contract
- Step 5: Recognise revenue when (or as) each performance obligation is satisfied

The following revenue streams have been identified as being impacted by the adoption of the new standard:

Area	Previous treatment	New treatment under IFRS 15
The provision of extended warranties to customers over and above the OEM warranty where the Group acts as the principal in the supply of the warranty service.	The Group provides an estimate of the cost of fulfilling the future obligation on the sale of the vehicle. The cost of fulfilling the obligation when it arises is then charged against the provision.	A proportion of revenue will be allocated to the extended warranty obligation and deferred to the balance sheet. The revenue will subsequently be recognised over time along with the costs incurred in fulfilling any warranty obligations.
The sale of vehicles which are subject to a buyback commitment and the possibility of the buyback being exercised by the customer is not highly likely as the buyback price set is below the expected market value.	Revenue and profit associated with vehicles sold subject to a buyback commitment are deferred and recognised over the period of the commitment.	Revenue is recognised in full when the vehicle is sold. However, an estimate of the value of the buyback payments is deducted from revenue and deferred to the balance sheet. Similarly, an estimate of the value of the vehicles to be returned is deducted from cost of sales and also deferred to the balance sheet.
Payments made by a Distribution business to a dealer in the form of a discount, rebate, credit note or some other form of incentive.	In most cases, these are deducted from revenue.	The new standard clarifies that all transactions that fall within this category should be accounted for as a reduction in revenue by the Distributor and not as an expense within cost of sales.
Additional services included in the sale of a vehicle to a customer as part of the total vehicle package (e.g. free servicing, roadside assistance, fuel coupons etc) where the Group is acting as a principal in the fulfilment of the service at a future date, rather than simply as an agent in selling the additional service and with no continuing obligation.	Varies dependent on the conclusions reached with regards to whether the Group is acting as principal or agent. Where the Group is acting as an agent, revenue is recognised in full on the sale of a vehicle. Where the Group is acting as principal, revenue is deferred.	The new standard sets out more comprehensive guidance on principal and agent relationships. Where the Group acts as principal, the value of the additional services should be separately identified, deducted from revenue, recognised as deferred revenue on the balance sheet and subsequently recognised as revenue when the service is provided, or over the period to which the service relates. Where the Group acts as an agent, the net amount retained after the deduction of any costs paid to the principal is recognised as revenue. If a product or service is provided free to a customer, then the costs paid to the principal should be deducted from revenue rather than charged to cost of sales.

Area	Previous treatment	New treatment under IFRS 15
Vehicle registration and similar fees which are charged to the customer on the sale of a vehicle and which are collected by the Group on behalf of an authority.	In most, but not all, cases these are excluded from revenue.	The new standard sets out more comprehensive guidance on principal and agent relationships. As a consequence of the new guidance, where it is concluded that the Group is acting as an agent of a government in the collection of such fees, the amount of the vehicle registration fee should be excluded from revenue.

The Group has elected to apply the new standard retrospectively to each prior reporting period, and has accordingly restated the comparative information for the immediately preceding periods in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Further details of the restatement can be seen in note 32.

Standards not effective at the balance sheet date

The following standards were in issue but were not yet effective at the balance sheet date. These standards have not yet been early adopted by the Group, and will be applied for the Group's financial years commencing on or after 1 January 2019:

- IFRS 16, *Leases*
- Amendments to IFRS 3 – Definition of a Business
- Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 issued in the Annual Improvement Cycle 2015-2017
- Amendments to IAS 1 and IAS 8 – Definition of Material
- Amendments to IAS 19 – Plan Amendment, Curtailment or Settlement
- Amendments to IAS 28 – Long-term interests in Associates and Joint Ventures
- Amendments to References to the Conceptual Framework in IFRS Standards
- IFRIC 23 – Uncertainty over Income Tax Treatments

Management are currently reviewing the new standards to assess the impact that they may have on the Group's reported position and performance. Management do not expect that the adoption of the standards listed above will have a material impact on the financial statements of the Group, except as noted below:

IFRS 16 *Leases*

IFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessees and lessors. IFRS 16 will supersede the current guidance on leases including IAS 17 and the related interpretations when it becomes effective for the Group's financial year commencing 1 January 2019. The Group has assessed the estimated impact that the application of IFRS 16 will have on its consolidated financial statements, and these are described below.

Under IFRS 16, the distinction between operating leases (off balance sheet) and finance leases (on balance sheet) is removed for lessee accounting and replaced with a model where a right-of-use asset and a corresponding liability are recognised for all leases by lessees. As a result, all leases will be on balance sheet except for short-term leases and leases of low value assets.

The right-of-use asset is initially measured at cost and subsequently measured at cost less accumulated depreciation. The lease liability is initially measured at the present value of the lease payments. Subsequently, the lease liability is adjusted for interest and lease payments. As a consequence, earnings before interest, depreciation, amortisation and tax (EBITDA) will increase because operating lease expenses currently included in EBITDA will be replaced with a depreciation charge in respect of the right-of-use asset and an interest expense on the lease liability. However, there will be an overall reduction in profit before tax in the early years of a lease because the depreciation and interest charges will exceed the current straight-line expense incurred under IAS 17. In addition, the classification of cash flows will also be affected because operating lease payments under IAS 17 are presented within operating cash flows, whereas under IFRS 16 the payments will be split into a principal and interest portion which will be presented as financing and operating cash flows respectively.

Leases in which the Group is a lessee

The Group will recognise new right-of-use assets and lease liabilities for all its operating leases in the consolidated statement of financial position, initially valued at the present value of the future lease payments. Operating leases which will be now recognised on balance sheet include various dealerships, offices, warehouses and equipment, except for short-term leases and leases of low value assets.

The nature of expenses related to those leases will now change because the Group will recognise a depreciation charge for right-of-use assets and interest expense on lease liabilities. Previously, the Group recognised operating lease expense on a straight-line basis over the term of the lease, and recognised assets and liabilities only to the extent that there was a timing difference between actual lease payments and the expense recognised. In addition, the Group will no longer recognise provisions for vacant leasehold properties as described in note 21. Instead, the right-of-use assets will be tested for impairment in accordance with IAS 36 *Impairment of Assets*.

Lease incentives will be recognised as part of the measurement of the right-of-use assets and lease liabilities, whereas under IAS 17 they resulted in the recognition of a lease liability incentive; this was amortised as a reduction of rental expense on a straight-line basis. For short-term leases (lease term of 12 months or less) and leases of low-value assets (such as personal computers and office furniture), the Group will opt to recognise a lease expense on a straight-line basis as permitted by IFRS 16. The Group has previously classified certain vehicles and buildings as finance leases. The adoption of IFRS 16 is not expected to have a material impact on these leases.

IFRS 16 Leases continued

The Group plans to apply a fully retrospective approach to leases where the Group is the lessee. Therefore, the cumulative effect of adoption of IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2018, with restatement of comparative information. The Group is currently finalising its assessment of the IFRS 16 and estimates that the impact on initial application will be as follows:

	As at 31 December 2018	As at 1 January 2018
Recognition of right-of-use asset	£410m to £430m	£380m to £400m
Recognition of lease liability	£450m to £470m	£420m to £440m

Leases in which the Group is a lessor

Under IFRS 16, a lessor continues to classify leases as either finance leases or operating leases and account for those two types of leases differently. To classify each lease, the Group makes an assessment of whether the lease transfers to the lessee substantially all the risks and rewards of ownership incidental to the ownership of the underlying asset. As part of this assessment the Group considers whether the lease is for a major part of the economic life of the asset.

The Group has reassessed the classification of sub-leases in which the Group is a lessor. When the Group is an intermediary lessor it will account for its interests in the head lease and sub-lease separately. It will assess the lease classification of a sub-lease with reference to the right-of-use asset arising from the head lease, not with reference to the underlying asset. Cash flows received from the principal and interest on finance lease receivables will be classified as cash flows from investing activities. As required by IFRS 9 an allowance for expected credit losses will be recognised on finance lease receivables where appropriate.

The Group expects to reclassify certain sub-leases as finance leases under IFRS 16, resulting in the recognition of a finance lease receivable of c£6m and c£5m as at 1 January 2018 and 31 December 2018 respectively.

Following the adoption of IFRS 16 the new right-of-use asset will be subject to the impairment requirements of IAS 36 *Impairment of Assets*. Management is currently assessing how the right-of-use assets should be tested for impairment and consequently the impact, if any, on the financial statements at adoption.

BASIS OF CONSOLIDATION

The consolidated financial statements comprise the financial statements of the parent company (Inchcape plc) and all of its subsidiary undertakings (defined as those where the Group has control), together with the Group's share of the results of its joint ventures (defined as those where the Group has joint control) and associates (defined as those where the Group has significant influence but not control). The results of subsidiaries are consolidated and the Group's share of results of its joint ventures and associates is equity accounted for as of the same reporting date as the parent company, using consistent accounting policies.

The results of newly acquired subsidiaries are consolidated using the acquisition method of accounting from the date on which control of the net assets and operations of the acquired company are effectively transferred to the Group. Similarly, the results of subsidiaries disposed of cease to be consolidated from the date on which control of the net assets and operations are transferred out of the Group.

The Group treats transactions with non-controlling interests as transactions with equity owners of the Group. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

Investments in joint ventures and associates are accounted for using the equity method, whereby the Group's share of post-acquisition profits or losses is recognised in the consolidated income statement, and its share of post-acquisition movements in shareholders' equity is recognised in shareholders' equity. If the Group's share of losses in a joint venture or associate equals or exceeds its investment in the joint venture or associate, the Group does not recognise further losses, unless it has contractual obligations or made payments on behalf of the joint venture or associate.

Intercompany balances and transactions and any unrealised profits arising from intercompany transactions are eliminated in preparing the consolidated financial statements.

FOREIGN CURRENCY TRANSLATION

Transactions included in the results of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in Sterling, which is the functional currency of the parent company, Inchcape plc, and the presentation currency of the Group.

In the individual entities, transactions in foreign currencies are translated into the functional currency at the rates of exchange prevailing at the dates of the individual transactions. Monetary assets and liabilities denominated in foreign currencies are subsequently retranslated at the rate of exchange ruling at the end of the reporting period. All differences are taken to the consolidated income statement, except those arising on long-term foreign currency borrowings used to finance or hedge foreign currency investments which on consolidation are taken directly to other comprehensive income.

The assets and liabilities of foreign operations are translated into Sterling at the rate of exchange ruling at the end of the reporting period. The income statements of foreign operations are translated into Sterling at the average rates of exchange for the period. Exchange differences arising from 1 January 2004 are recognised as a separate component of shareholders' equity. On disposal of a foreign operation, any cumulative exchange differences held in shareholders' equity are transferred to the consolidated income statement.

REVENUE, OTHER INCOME AND COST OF SALES

Revenue is measured at the fair value of consideration receivable, net of any discounts, rebates, trade allowances, incentives, or amounts collected on behalf of third parties. It is recognised to the extent that the transfer of promised goods or services to a customer has been satisfied and the revenue can be reliably measured. Revenue excludes sales-related taxes and intra-group transactions. In practice this means that:

Revenue from the sale of goods is recognised when the obligation to transfer the goods to the customer has been satisfied and the revenue can reliably be measured. The obligation to transfer goods to the customer is considered to have been satisfied when the vehicles or parts are invoiced and physically dispatched or collected.

Revenue from the rendering of services to the customer is considered to have been satisfied when the service has been undertaken.

Where the Group acts as an agent on behalf of a principal in relation to finance, insurance and similar products, the associated commission income is recognised within revenue in the period in which the related finance or insurance product is sold and receipt of payment can be assured.

Where a vehicle is sold to a leasing company and the Group undertakes to repurchase the vehicle for a specified value at a predetermined date, the sale is not recognised on the basis that the possibility of the buyback being exercised is highly likely. Consequently, such vehicles are retained within 'property, plant and equipment' in the consolidated statement of financial position at cost and are depreciated to their residual value over the life of the lease. The difference between the initial amounts received from the leasing company and the repurchase commitment is recognised as deferred income in the consolidated statement of financial position and is released to the consolidated income statement on a straight line basis over the life of the lease. The repurchase commitment, which reflects the price at which the vehicle will be bought back, is held within 'trade and other payables', according to the date of the commitment.

Where a vehicle is sold subject to a buyback commitment and the possibility of the buyback being exercised by the customer is not highly likely as the buyback price set is below the expected market value, revenue is recognised in full when the vehicle is sold. However, an estimate of the value of the buyback payments is deducted from revenue and deferred to the balance sheet. Similarly, an estimate of the value of the vehicles to be returned is deducted from cost of sales and also deferred to the balance sheet. These balances are considered to be contract liabilities.

Where additional services are included in the sale of a vehicle to a customer as part of the total vehicle package (e.g. extended warranty, free servicing, roadside assistance, fuel coupons etc) and the Group is acting as a principal in the fulfilment of the service, the value of the additional services should be separately identified, deducted from revenue, recognised as deferred revenue on the balance sheet and subsequently recognised as revenue when the service is provided, or over the period to which the service relates. These balances are considered to be contract liabilities.

Finance income is recognised when it is probable that the economic benefits will flow to the Group and the amount of income can be measured reliably. It is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable.

Dividend income is recognised when the right to receive payment is established.

Cost of sales includes the expense relating to the estimated cost of self-insured product warranties offered to customers. These warranties form part of the package of goods and services provided to the customer when purchasing a vehicle and are not a separable product.

SHARE-BASED PAYMENTS

The Group operates various share-based award schemes. The fair value at the date at which the share-based awards are granted is recognised in the consolidated income statement (together with a corresponding credit in shareholders' equity) on a straight-line basis over the vesting period, based on an estimate of the number of shares that will eventually vest. At the end of each reporting period, the Group revises its estimates of the number of awards that are expected to vest. The impact of any revision is recognised in the consolidated income statement with a corresponding adjustment to equity.

For equity-settled share-based awards, the services received from employees are measured by reference to the fair value of the awards granted. With the exception of the Group Save As You Earn scheme, the vesting of all share-based awards under all schemes is solely reliant upon non-market conditions, therefore no expense is recognised for awards that do not ultimately vest. Where an employee or the Company cancels an award, the charge for that award is recognised as an expense immediately, even though the award does not vest.

FINANCE COSTS

Borrowing costs which are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of that asset from the first date on which the expenditure is incurred for the asset and until such time as the asset is ready for its intended use. A Group capitalisation rate is used to determine the magnitude of borrowing costs capitalised on each qualifying asset. This rate is the weighted average of Group borrowing costs, excluding those borrowings made specifically for the purpose of obtaining a qualifying asset.

All other borrowing costs are recognised as an expense in the period in which they are incurred.

INCOME TAX

The charge for current income tax is based on the results for the period as adjusted for items which are not taxed or are disallowed. It is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred income tax is accounted for using the liability method in respect of temporary differences arising from differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

In principle, deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference is due to goodwill arising on a business combination, or to an asset or liability, the initial recognition of which does not affect either taxable or accounting income.

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

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

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle balances net.

EXCEPTIONAL ITEMS

In order to facilitate comparability with other companies, certain items which are material are presented as exceptional items within their relevant consolidated income statement category. The separate reporting of exceptional items helps provide additional useful information regarding the Group's underlying business performance and is used by management to facilitate internal performance analysis. Examples of events which may give rise to the classification of items as exceptional include gains or losses on the disposal of businesses, acquisition costs, restructuring of businesses, litigation, asset impairments and exceptional tax-related matters.

GOODWILL

Goodwill represents the excess of the cost of acquisition of a business combination over the Group's share of the fair value of identifiable net assets of the business acquired at the date of acquisition. Goodwill is initially recognised at cost and is held in the functional currency of the acquired entity and revalued at the closing exchange rate at the end of each reporting period.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. At the date of acquisition, the goodwill is allocated to cash generating units for the purpose of impairment testing and is tested at least annually for impairment.

Gains and losses on disposal of a business include the carrying amount of goodwill relating to the business sold except for goodwill arising on business combinations on or before 31 December 1997 which has been deducted from shareholders' equity and remains indefinitely in shareholders' equity.

OTHER INTANGIBLE ASSETS

Intangible assets, when acquired separately from a business (including computer software), are carried at cost less accumulated amortisation and impairment losses. Cost comprises the purchase price from third parties as well as internally generated development costs where relevant. Amortisation is provided on a straight line basis to allocate the cost of the asset over its estimated useful life, which in the case of computer software is three to eight years. Amortisation is recognised in the consolidated income statement within 'net operating expenses'.

Intangible assets acquired as part of a business combination are capitalised separately from goodwill if the benefit of the intangible asset is obtained through contractual or other legal rights and the fair value can be measured reliably on initial recognition. The principal intangible assets are agreements with manufacturers for the distribution of New vehicles and parts, which represent the estimated value of distribution rights acquired in business combinations. Such agreements have varying terms and periods of renewal and have historically been renewed indefinitely without substantial cost. The Group therefore expects these agreements to be renewed indefinitely and accordingly no amortisation is charged on these assets. The Group assesses these distribution rights for impairment on an annual basis.

Other intangible assets acquired in a business combination may include order books and customer contracts. These intangible assets are amortised on a straight line basis over their estimated useful life, which is generally less than a year.

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses. Cost comprises the purchase price and directly attributable costs of the asset and includes, where relevant, capitalised borrowing costs. Depreciation is based on cost less estimated residual value and is included within 'net operating expenses' in the consolidated income statement, with the exception of depreciation on 'interest in leased vehicles' which is charged to 'cost of sales'. It is provided on a straight line basis over the estimated useful life of the asset, except for freehold land which is not depreciated. For the following categories, the annual rates used are:

Freehold buildings and long leasehold buildings	2.0%
Short leasehold buildings	shorter of lease term or useful life
Plant, machinery and equipment	5.0% – 33.3%
Interest in leased vehicles	over the lease term

The residual values and useful lives of all assets are reviewed at least at the end of each reporting period and adjusted if necessary.

IMPAIRMENT

Assets that are subject to amortisation or depreciation are reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. Any impairment losses are included within 'net operating expenses' in the consolidated income statement.

In addition, goodwill is not subject to amortisation but is tested at least annually for impairment. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount, the latter being the higher of the asset's fair value less costs to sell and value in use. Value in use calculations are performed using cash flow projections, discounted at a pre-tax rate which reflects the asset specific risks and the time value of money.

A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the consolidated income statement within 'net operating expenses'. When a trade receivable is not collectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against 'net operating expenses' in the consolidated income statement.

Non-financial assets, other than goodwill, which have previously been impaired, are reviewed for possible reversal of the impairment at each reporting date.

INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost comprises expenditure incurred in bringing inventories to their present location and condition. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution. Used vehicles are carried at the lower of cost or fair value less costs to sell, generally based on external market data available for Used vehicles.

Vehicles held on consignment are included within inventories as the Group is considered to have the risks and rewards of ownership. The corresponding liability is included within 'trade and other payables'.

Inventory can be held on deferred payment terms. All costs associated with this deferral are expensed in the period in which they are incurred.

An inventory provision is recognised in situations where net realisable value is likely to be less than cost (such as obsolescence, deterioration, fall in selling price). When calculating the provision, management considers the nature and condition of the inventory, as well as applying assumptions around anticipated saleability, determined on conditions that exist at the end of the reporting period. With the exception of parts, generally net realisable value adjustments are applied on an item-by-item basis.

TRADE RECEIVABLES

Trade receivables are amounts due from customers for goods sold or services performed in the ordinary course of business. These are recognised as current assets if collection is due in one year or less. If collection is due in over a year, they are presented as non-current assets.

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment is established when based on an expected loss model. The amount of the provision is the difference between the asset's carrying amount and the expected value of the amounts to be received.

TRADE PAYABLES

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business. These are classified as current liabilities if payment is due in one year or less. If payment is due at a later date, they are presented as non-current liabilities.

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

Trade payables include the liability for vehicles held on consignment, with the corresponding asset included within inventories.

BORROWINGS

Borrowings are recognised initially at fair value, net of transaction costs incurred, and are subsequently stated at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the consolidated income statement over the period of the borrowings, using the effective interest method.

PENSIONS AND OTHER POST-RETIREMENT BENEFITS

The Group operates a number of retirement benefit schemes.

The major schemes are defined benefit pension funds with assets held separately from the Group. The cost of providing benefits under the plans is determined separately for each plan using the projected unit credit actuarial valuation method.

The current service cost and gains and losses on settlements and curtailments are included in 'cost of sales' or 'net operating expenses' in the consolidated income statement. Past service costs are similarly recognised in the consolidated income statement. Administrative scheme expenses associated with the plans are recorded within 'net operating expenses' when incurred, in line with IAS 19 (revised). Net interest income or interest cost relating to the funded defined benefit pension plans is included within 'finance income' or 'finance costs', as relevant, in the consolidated income statement.

Changes in the retirement benefit obligation or asset due to experience and changes in actuarial assumptions are included in the consolidated statement of comprehensive income, as actuarial gains and losses, in full in the period in which they arise.

Where scheme assets exceed the defined benefit obligation, a net asset is only recognised to the extent that an economic benefit is available to the Group, in accordance with the terms of the scheme and, where relevant, statutory requirements.

The Group's contributions to defined contribution plans are charged to the consolidated income statement in the period to which the contributions relate.

The Group also has a liability in respect of past employees under post-retirement healthcare schemes which have been closed to new entrants. These schemes are accounted for on a similar basis to that for defined benefit pension plans in accordance with the advice of independent qualified actuaries.

PROVISIONS

Provisions are recognised when the Group has a present obligation in respect of a past event, when it is more likely than not that an outflow of resources will be required to settle the obligation and where the amount can be reliably estimated. Provisions are discounted when the time value of money is considered to be material, using an appropriate risk-free rate on government bonds.

PRODUCT WARRANTY PROVISION

A product warranty provision corresponds to warranties provided as part of the sale of a vehicle and provide assurance to the customer that the product will work as sold. Provision is made for the expected cost of labour and parts based on historical claims experience and expected future trends.

VACANT LEASEHOLD PROVISION

A vacant leasehold provision is recognised when the Group is committed to certain leasehold premises for which it no longer has a commercial use. It is made to the extent of the estimated future net cost, including existing subtenant arrangements if any.

LITIGATION PROVISION

A litigation provision is recognised when a litigation case is outstanding at the end of the reporting period and there is a likelihood that the legal claim will be settled.

DISPOSAL GROUP AND ASSETS HELD FOR SALE

Where the Group is actively marketing a business and disposal is expected within one year of the end of the reporting period, the assets and liabilities of the associated businesses are separately disclosed in the consolidated statement of financial position as a disposal group. Assets are classified as assets held for sale if their carrying amount is to be recovered principally through a sale transaction rather than through continuing use. Both disposal groups and assets held for sale are stated at the lower of their carrying amount and fair value less costs to sell.

SEGMENTAL REPORTING

Segment information is reported in accordance with IFRS 8 *Operating segments*, which requires segmental reporting to be presented on the same basis as the internal management reporting. The Group's operating segments are countries or groups of countries and the market channels, Distribution and Retail. These operating segments are then aggregated into reporting segments to combine those with similar characteristics.

FINANCIAL INSTRUMENTS

The Group classifies its financial instruments in the following categories: measured at amortised cost; measured at fair value through profit and loss; and measured at fair value through other comprehensive income. The classification is determined at initial recognition and depends on the purpose for which the financial instruments are required.

Measured at amortised cost includes non-derivative financial assets and liabilities with fixed or determinable payments that are not quoted in an active market. Financial assets are included in current assets, except where the maturity date is more than 12 months after the end of the reporting period. They are initially recorded at fair value and subsequently recorded at amortised cost. Financial liabilities are included in current liabilities, except where the maturity date is more than 12 months after the end of the reporting period. They are initially measured at original cost, less amortisation or provisions raised.

Measured at fair value through profit and loss includes derivative financial assets and liabilities, which are further explained below. They are classified according to maturity date, within current and non-current assets and liabilities respectively.

Measured at fair value through other comprehensive income includes derivative financial assets and liabilities, which are further explained below, and available for sale financial assets such as bonds and equity investments. Derivative financial assets and liabilities are included in current assets and liabilities, except where the maturity date is more than 12 months after the end of the reporting period. Available for sale financial assets are classified as non-current assets unless management intends to dispose of them within 12 months of the end of the reporting period and are held at fair value.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents in the consolidated statement of financial position comprise cash at bank and in hand, short-term bank deposits and money market funds.

In the consolidated statement of cash flows, cash and cash equivalents comprise cash and cash equivalents, as defined above, net of bank overdrafts.

LEASES

Finance leases, which transfer to the Group substantially all the risks and rewards of ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to the consolidated income statement. Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term.

Leases where the Group does not hold substantially all the risks and rewards of ownership of the asset are classified as operating leases. Operating lease rental payments are recognised as an expense in the consolidated income statement on a straight line basis over the lease term.

OFFSETTING

Netting in the consolidated statement of financial position only occurs to the extent that there is the legal ability and intention to settle net. As such, bank overdrafts are presented in current liabilities to the extent that there is no intention to offset with the cash balance.

DERIVATIVE FINANCIAL INSTRUMENTS

An outline of the objectives, policies and strategies pursued by the Group in relation to its financial instruments is set out in note 23 to the consolidated financial statements.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as:

- hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedge); or
- hedges of a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (cash flow hedge).

FAIR VALUE HEDGE

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the consolidated income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The Group only applies fair value hedge accounting for hedging fixed interest risk on borrowings and future fixed amount currency liabilities (on its cross currency interest rate swaps). The gain or loss relating to the effective portion of interest rate swaps hedging fixed rate borrowings and changes in the fair value of those borrowings are recognised in the consolidated income statement within 'finance costs'. The gain or loss relating to the ineffective portion is also recognised in the consolidated income statement within 'finance costs'.

CASH FLOW HEDGE

For cash flow hedges that meet the conditions for hedge accounting, the portion of the gains or losses on the hedging instrument that is determined to be an effective hedge is recognised directly in other comprehensive income and the ineffective portion is recognised within 'net operating expenses' in the consolidated income statement. When the hedged forecast transaction results in the recognition of a non-financial asset or liability then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in other comprehensive income are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in other comprehensive income are transferred to the consolidated income statement in the same period in which the hedged forecast transaction affects the consolidated income statement.

AVAILABLE FOR SALE FINANCIAL ASSETS

Gains and losses on available for sale financial assets are recognised in other comprehensive income, until the investment is sold or is considered to be impaired, at which time the cumulative gain or loss previously reported in other comprehensive income is included in the consolidated income statement. Cumulative gains and losses on investments held for operational reasons are included within 'net operating expenses'. Cumulative gains and losses on investments held for financing purposes are included within 'finance income' and 'finance costs' respectively.

SHARE CAPITAL

Ordinary shares are classified as equity. Where the Group purchases the Group's equity share capital (treasury shares), the consideration paid is deducted from shareholders' equity until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity.

DIVIDENDS

Final dividends proposed by the Board of Directors and unpaid at the year-end are not recognised in the consolidated financial statements until they have been approved by the shareholders at the Annual General Meeting. Interim dividends are recognised when they are paid.

CRITICAL ACCOUNTING JUDGEMENTS AND SOURCES OF ESTIMATION UNCERTAINTY

The preparation of financial statements in accordance with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge, actual results may ultimately differ from those estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. The Directors have made a number of estimates and assumptions regarding the future, and made some significant judgements in applying the Group's accounting policies. These are discussed below:

SOURCES OF ESTIMATION UNCERTAINTY

IMPAIRMENT OF GOODWILL AND OTHER INDEFINITE LIFE INTANGIBLE ASSETS

Goodwill and other indefinite life intangible assets are tested at least annually for impairment in accordance with the accounting policy set out above. The recoverable amount of cash generating units is determined based on value in use calculations. These impairment calculations require the use of estimates including projected future cash flows (see note 11).

INCENTIVES AND OTHER REBATES FROM BRAND PARTNERS

The Group receives income in the form of various incentives which are determined by our brand partners. The amount we receive is generally based on achieving specific objectives, such as a specified sales volume, as well as other objectives including maintaining brand partner standards which may include, but are not limited to, retail centre image and design requirements, customer satisfaction survey results and training standards. Objectives are generally set and measured on either a quarterly or annual basis.

Where incentives are based on a specific sales volume or number of registrations, the related income is recognised as a reduction in cost of sales when it is reasonably certain that the income has been earned. This is generally the later of the date the related vehicles are sold or registered or when it is reasonably certain that the related target will be met. Where incentives are linked to retail centre image and design requirements, customer satisfaction survey results or training standards, they are recognised as a reduction in cost of sales when it is reasonably certain that the incentive will be received for the relevant period.

The Group may also receive contributions towards advertising and promotional expenditure. Where such contributions are received, they are recognised as a reduction in the related expenditure in the period to which they relate.

PENSIONS AND OTHER POST-RETIREMENT BENEFITS – ASSUMPTIONS

Pension and other post-retirement benefit liabilities are determined based on the actuarial assumptions detailed in note 5. A number of these assumptions require estimates to be made, including the rate of inflation and expected mortality rates. These assumptions are subject to a review on an annual basis and are determined in conjunction with an external actuary. The use of different assumptions could have a material effect on the value of the relevant liabilities and could result in a material change to amounts recognised in the income statement over time.

In November 2015, the TKM Group Pension Scheme completed a buy-in transaction whereby the assets of the scheme were invested in a bulk purchase annuity contract that matches the benefits payable to the members of the scheme. The contract has been structured to enable the scheme, in time, to move to a full buy-out, following which the insurance company will become directly responsible for the pension payments under the scheme. The scheme has now been fully bought out and it was formally wound up on 3 August 2018.

TAX

The Group is subject to income taxes in a number of jurisdictions. Some degree of estimation is required in determining the worldwide provision for income taxes (see note 8). There are a number of transactions and calculations during the ordinary course of business for which the ultimate tax determination is uncertain. The Group recognises liabilities for anticipated tax audit issues based on best estimates of whether additional taxes will be due without taking into account whether tax authorities would detect any particular issue. The estimate is made separately for each jurisdiction and takes into account management's view of the relevant tax laws and environment applicable to the operations of the Group in those jurisdictions. No single item is expected to give rise to a material adjustment in the following or subsequent years.

Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current tax and deferred tax provisions in the period in which such determination is made.

In addition, the recognition of deferred tax assets is dependent upon an estimation of future taxable profits that will be available against which deductible temporary differences can be utilised (see notes 8 and 16). In the event that actual taxable profits are different, such differences may impact the carrying value of such deferred tax assets in future periods.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

Property, plant and equipment and intangible assets are reviewed for impairment if events or circumstances indicate that the carrying value may not be recoverable. When an impairment review is carried out, the recoverable value is determined based on value in use calculations which require estimates to be made of future cash flows (see notes 11 and 12).

REPURCHASE COMMITMENTS

The Group has entered into commitments in relation to certain leased vehicles to repurchase the vehicle for a specified value at a predetermined date. These commitments are an estimate of future market value at a specified point in time. The actual market value of vehicles bought back may vary from the committed purchase value. To the extent that the actual market value of such vehicles is expected to be less than the repurchase commitment, a provision is recognised and is included with Other Provisions in note 21. Where the repurchase commitment is in respect of a vehicle sold by the Group to a leasing company, the repurchase commitment is held within 'trade and other payables'. Where the Group has entered into a repurchase commitment in respect of vehicles that have not been sourced from within the Group, then the repurchase commitment is included as a purchase commitment (see note 30).

CRITICAL ACCOUNTING JUDGEMENTS

PENSIONS – DISCOUNT RATE

The Group's defined benefit obligations are discounted at a rate set by reference to market yields at the end of the reporting period on high quality corporate bonds. Significant judgement is required when setting the criteria for bonds to be included in the population from which the yield curve is derived. The most significant criteria considered for the selection of bonds include the issue size of the corporate bonds, quality of the bonds and the identification of outliers which are excluded.