



**AA INTERMEDIATE CO LIMITED**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**FOR THE YEAR ENDED 31 JANUARY 2016**

**Company registration number: 5148845**

# Strategic Report

## Executive Chairman's Statement

### Results in line with expectations and reflecting a robust performance in Roadside Assistance

The robust performance of Roadside Assistance, which represents 77% of Group trading EBITDA <sup>1</sup> excluding Head Office costs, against a background of major transformation reinforces our conviction in the potential of this business. It grew revenue 1.8% and trading EBITDA 0.8%, reflecting not just its resilient business model but our successful execution of several strategic initiatives in the first year of the transformation.

Overall revenue, excluding the Glass business which we sold in September 2015, reduced 0.5% to £960m. This was the result of the continued pressures in both the Insurance Services and Driving Services markets and the adverse foreign exchange movements affecting the reported results of the Ireland business. This decline, as well as new IT operating costs and a full year of the Group's share of additional costs from the new company structure, together with the investment in marketing and diagnostic technology offset both the positive performance of Roadside Assistance and cost reductions. As a result, Group Trading EBITDA, excluding the Glass business, reduced 3.0% to £417m, in line with expectations, and the EBITDA margin was consequently slightly lower than last year at 43.0% (2015: 44.6%).

Operational cash flow was strong and cash conversion before tax and exceptional items was 99%. Net cash flow was £95m before dividends and the one-off costs of the refinancing. This was achieved despite the abnormally high level of capital expenditure relating to the transformation.

### Our strategy

We set out three strategic priorities at the time of the AA plc IPO in June 2014 and in March 2015 we laid out the objectives and investment needed to deliver them. We have made good progress in our first full year since the AA plc IPO and are now well on our way to turning the AA into the UK's pre-eminent Membership services organisation and taking advantage of technical opportunities.

The progression of the transformation is as follows:

- **Year 1 (2016 financial year): strengthening the foundations.** Our achievements are discussed in more detail below.
- **Year 2 (2017 financial year): building the momentum for change.** As expected this is another year of investment with further significant capital expenditure related to the transformation. All of this will create momentum for the following year when the benefits will begin to be realised. In addition, the focus on productivity and efficiency throughout the business will continue to generate savings.
- **Year 3 (2018 financial year): beginning to realise the transformation.** We expect positive trends in revenue growth and cost savings to be clear. This will be the final year of our transformation and associated capital expenditure investments are expected to be much lower than in the previous two years. We will start to apply our significant cash generation to a programme of deleveraging.
- **Year 4 (2019 financial year): delivering growth.** After three years of investment in the transformation, we believe that the AA will be strengthened and revolutionised resulting in revenue growth, cost savings, enhanced profitability and lower net debt. The transformation will increase the value we deliver to our Members, customers and shareholders.

<sup>1</sup> Trading EBITDA (earnings before interest, tax, depreciation and amortisation) excludes exceptional items and items not allocated to a segment. In the current period items not allocated to a segment principally relate to the difference between the cash contributions to the pension scheme for on-going service and the calculated annual service cost and share-based payments.

## **Delivering our strategic priorities in year one of the transformation**

In this past year, the first of our transformation, we have made significant progress against the objectives by which we expect to deliver our strategic priorities. These are set out below.

### ***Priority 1: Strengthen the AA's foundations to become the pre-eminent Membership services organisation in the UK by reversing the effect of years of under-investment.***

The progress against the three strategic objectives to deliver this priority is as follows:

- 1. Grow the core Roadside Assistance business by reversing the decline in Membership and increasing income per Member.** We are encouraged by the improvement in retention, by two percentage points compared with last year, and the slowing of the decline in personal Members to 2.6% compared with 4.5% last year. The decline in the second half of the year was 1.4% compared with 2.8% in the corresponding period in the prior year. The investment in the brand, improved marketing, and better retention tools are all having the positive effect we planned.
- 2. Evolve the Insurance and Financial Services business models based on the strength of our brand and the value we offer our customers.** We are encouraged by the progress we are seeing in both these new businesses and we expect them to become profitable in the medium term.

We relaunched AA-branded financial services through our 10-year exclusive arrangement with Bank of Ireland (BOI UK). We intend to rebuild our position in a market which was previously highly successful for the AA by combining our marketing strength with the financial services expertise of BOI UK.

- 3. Improve our business customer positioning through partnerships, underpinned by our high service levels.** Our leading position in business-to-business Roadside Assistance for the Manufacturing, Fleet and Leasing and Added Value Accounts markets, lends scale to our operations and provides a platform for innovation across the industry. Our new contract with Lex Autoleasing, the UK's biggest leasing company, adds 280,000 customer vehicles and 50 patrols helping to maintain high service standards while optimising costs.

### ***Priority 2: Revolutionise the customer experience through investing in and embracing new technologies.***

We are already increasing the value of Membership and generating savings by investing in our patrols, brand, IT systems and digital capabilities. Progress against our three objectives to deliver this strategic priority is as follows:

- 1. Invest in systems, people and processes to improve our customers' and Members' experience and our efficiency.** The critical IT transformation is on time and budget and includes the following:
  - The new IT infrastructure which is supporting our back-office and call centre systems. This establishes a sound base on which to build new operating systems and achieves greater efficiency and smoother processes.
  - The marketing package of the new Customer Relationship Management system (CRM), went live in March, ahead of plan. This enables better segmented, personalised and relevant marketing which will reduce the quantity but increase the effectiveness of communication. The remainder of the CRM will follow with uploading of data in the second half of the year to provide an integrated sales platform. This will reduce time and costs for call centres; result in a smoother customer experience; and, increase the number of products per customer from the current level.

- New technology is improving the effectiveness of our patrols. In addition to the Bosch diagnostic technology, new smartphones and tablets improve despatch efficiencies, give them critical information ahead of and during a job and save time spent on administration. This is improving diagnostics, repair rates, response times and number of jobs done while offering customers a better service. Plans for the 2017 financial year include new battery testing equipment. This will improve the output and timing of battery testing. The launch of the universal spare wheel will also significantly improve productivity and benefit customers.
- 2. Deliver a step change in our digital capability.** Our digital investment is improving the attractiveness and efficiency of the AA's products and processes by making them more immediate, intuitive and relevant. Achievements in the past year include the following:
- Encouraging take up of the app, which is used in 11% of personal Members' breakdown. This is lowering the number of calls to call centres and, as a result, reducing costs.
  - The first version of 'My AA' enables customers to view and manage their AA products in a single profile. This first step towards self-service will modernise customer experience, deliver savings and increase online sales.
  - The new website was launched in May enhancing our online commercial processes including speeding up our ability to update information and prices.
  - The AA is pioneering the use of connected car technology. In addition to the direct benefits to drivers of monitoring safety, security, logistics and driving costs, this technology will give the AA the capability to improve prognostics, diagnostics, accuracy of deployment and speed of repair. Our Intelomatics Europe joint venture and the launch of Trakm8 telematics to our Fleet and Leasing customers significantly strengthens our ability to innovate and take a leading position in the development of car connectivity.
- 3. Transform Membership, the brand and our commercial model to retain existing Members, win new Members and sell products across all our businesses.** We are invigorating the value of AA Membership as follows:
- Our brand advertising TV campaign, the first in eight years, reinforced our marketing messages highlighting the AA's expertise and product range.
  - We have improved the Membership proposition to attract new and to retain existing Members as well as drive the sale of additional products to them. We have also introduced an improved pricing model to ensure our products are more rationally tiered. New benefits for Members, such as 20% discounts at a range of Mitchell & Butlers' outlets, have been well received and there has been a pickup in usage of the discounts available at MOTO service stations.
  - We have also expanded services such as AA Tyres and Automyze which reduce the administrative burden for motorists.

***Priority 3: Reduce Group Borrowings and the associated interest costs.***

The AA is highly cash generative and converts on around 100% of EBITDA to operating cash flow. We have very low working capital requirements and low levels of maintenance capital expenditure. On a normalised basis, after the transformation, we expect to use our significant level of net free cash to redeem debt.

In the refinancing completed in July, we issued new bonds of £735m allowing the retirement of the most expensive element of the debt, the pre-existing Class B notes that we inherited from the previous private equity owners. While the refinancing generated significant one-off finance charges, it reduced the annual cash cost of servicing our debt by more than £28m per year. Net debt was £2,881m at 31 January 2016, compared with £2,832m at 31 January 2015. The refinancing also facilitated the payment of dividends to AA plc.

### **The financial implications of the transformation**

When we set out the plan for the transformation, we announced that the capital investment required for the IT element of the transformation was £128m over three years and this is unchanged. However, the phasing of that investment has altered and we invested £54m capital expenditure in the 2016 financial year, below the level expected due to timing of payments around the year end. We expect to invest approximately £65m during the 2017 financial year and £9m in the 2018 financial year.

Based on the success of the brand marketing during the past year, we continue to expect to invest approximately £10m per year in brand advertising. As previously stated, we also expect to make additional investment into product development such as connected car and Automyze services, which will significantly enhance the Membership proposition.

We remain confident in our ability to reduce costs and continue to expect savings to our 2015 cost base of at least £40m per year from the 2019 financial year. The cost to achieve these savings is expected to be £45m over three years. We made savings in the 2016 financial year of £8m which are largely related to higher productivity throughout the organisation, efficiencies in our call centres and back office and in rationalising property.

We expect incremental IT operational maintenance costs, mainly comprising fees and licences, to amount to £8m per year.

Once the transformation is complete, we expect to continue to invest approximately £40m per year on maintenance capital expenditure split between vehicles (approximately £20m net of proceeds), IT systems (approximately £10m) and property and equipment (approximately £10m).

## **Outlook**

We have made a positive start to the 2017 financial year which is the second year of the transformation programme. While we are already building momentum from the actions taken last year to strengthen the foundations and revolutionise the business, the 2017 financial year will, as anticipated, be another year of investment.

Based on the success of last year's advertising campaign and other marketing actions, we will continue to invest in brand advertising in the 2017 financial year. We will continue to invest in our products and connected car developments as outlined at the interims.

A shift in the phasing of the transformation capital expenditure results in the investment of approximately £65m in the 2017 financial year following lower than expected investment of £54m in 2016. The total will remain unchanged at £128m over three years.

We continue to target cost savings off the 2015 base of at least £40m per annum from the 2019 financial year. In the 2017 financial year we expect to increase savings compared with the 2016 financial year.

We expect net debt reduction in the 2017 financial year to be relatively modest. Thereafter, as we revert to more normalised levels of capital expenditure, we expect to accelerate deleveraging.

## Business performance review

### Introduction

The directors present the condensed financial statements of AA Intermediate Co Limited (“the Company”) and its subsidiary undertakings (together “the Group”) for the year ended 31 January 2016. The Company is an Obligor and a parent company of each of the other Obligors that provide security and guarantees under the financing arrangements entered into by the AA on 2 July 2013. The Company’s immediate parent is AA Mid Co Limited. There is no material difference in the financial conditions and results of operations between the AA Intermediate Co Limited group and the AA Mid Co Limited group.

### Roadside Assistance

Roadside Assistance contributed 75% of Group revenue and 77% of trading EBITDA excluding Head Office costs. Its performance is driven by our highly valued personal Member base. However, business customers provide close to half the jobs for the patrol force, supporting the scale of our operations, which is critical to our success.

Roadside Assistance also includes additional services such as vehicle inspections, tyre fitting and publishing. Collectively these businesses generate approximately £7m of Trading EBITDA.

In September 2015 we completed the disposal of our mobile windscreen repair business and prior year figures are restated for the purposes of this analysis in the table below.

### Results

	2016	2015
Revenue (£m)	724	711
Trading EBITDA (£m)	361	358
Trading EBITDA margin (%)	49.9	50.4
Roadside Assistance personal Members (000s)	3,673	3,770
Average income per personal Member (£)	141	135
Personal Members excluding free Memberships (000s)	3,331	3,393
Average income per personal Members excluding free Memberships (£)	156	150
Business customers (000s)	10,216	9,640
Average income per Business customer (£)	18	19
Number of breakdowns (m)	3.4	3.5

Roadside Assistance revenue of £724m grew 1.8%, driven by the increase in income per member, improved retention rates and a full year impact from the Volkswagen Group contract, launched in June 2014.

We have slowed the rate of decline of personal Members to -2.6% (to 3,673k) versus a decline of -4.5% last year. Average income per personal Member rose 4.4% compared with a rise of 7.1% in the prior year. It remains our intention to limit price increases.

We have ceased to give away free Memberships to insurance customers, and excluding these free Memberships, we have 3,331k personal Members. The rate of decline in this category is slower at -1.8% (-5.2% last year) demonstrating the greater value Membership holds for those who pay for it. The broader Membership base which includes joint and family Members was 4,712k Members, compared with 4,773k last year. This wider category represents the potential reach of cross-selling opportunities which the new CRM system will enable us to address.

During the year our retention rate reached 81% compared with 79% last year. This reflects the positive impact of enhancements to our product offering, pricing, investment in advertising and training at our call centres including particularly the Stay AA programme. We are receiving fewer incoming calls from Members requesting a review of their cover and our Stay AA team is retaining more of those who call at lower discounts, largely owing to better product communication. Revenue from new Members was broadly flat.

In the business-to-business segment we grew revenue with a 6% increase in business customers driven by retention of contracts with Northgate and Toyota, the extension of our contract with Vauxhall, and winning of the Lex Autoleasing contract which started in January 2016. Lex Autoleasing, the UK's largest leasing company, added approximately 280,000 customer vehicles and increased our share of the Fleet and Leasing market to around 60%. The increase in customer numbers offset a lower average income per business customer resulting from the first full year effect of the Lloyds contract which we retained in March 2015.

We recognise the importance of our patrols in the service we offer and have invested considerably in giving them what they need to improve both their service and efficiency. We have invested in diagnostic and communications technology to reduce time spent on each job, to enhance the accuracy of identifying problems and to help ensure optimum resourcing. We have increased the repair rate to 82% during the past year.

Trading EBITDA increased by £3m to £361m, mostly from the improvement in revenue and cost savings generated by efficiencies in the patrol force and call centres. Trading EBITDA margin however decreased from 50.4% to 49.9% due to the investment in brand advertising of approximately £10m and new technology for the patrols.

### **Insurance Services (including Financial Services)**

Insurance Services, which includes Financial Services, contributed 14% of Group revenue and 16% of Group trading EBITDA excluding Head Office costs. We arranged 2.1m policies last year for motor insurance, home insurance and Home Services, providing emergency repairs to boilers, heating systems and other domestic installations.

We launched our financial services partnership with the Bank of Ireland through which the AA offers a range of savings, loans and credit cards. By building on a long history of AA financial services, and developing products highly relevant to our Members, we will further enhance our Membership proposition.

The introduction of new operating systems and products into Home Services, prepares the ground for the many opportunities we see in that market.

### *Results*

	<b>2016</b>	<b>2015</b>
Revenue (£m)	131	142
Trading EBITDA (£m)	78	84
Trading EBITDA margin (%)	59.5	59.2
Policy numbers in force <sup>1</sup> (000s)	2,074	2,163
Average income per policy (£)	63	66

<sup>1</sup> Excluding business customers

The decline in Insurance Services revenue, to £131m, reflected the 4.1% decline in policy numbers. This was due to higher motor premiums, which drove increased customer churn as well as a decrease in motor ancillary income; and, reflected our focus on profitability over volumes.

Trading EBITDA, of £78m, reflected this decline and the credit card run off from the legacy financial services business which benefitted the prior year results by £5m. However, improvements in efficiency within our contact centres and lower marketing spend on aggregators helped offset these adverse effects.

## Driving Services

This division which comprises Driving Schools and DriveTech contributed 7% of Group revenue and 4% of Group trading EBITDA excluding Head Office costs. Through the AA and BSM brands the AA is the largest driving school in the UK whilst DriveTech is the market leader in providing speed awareness courses for Police forces in the UK and fleet training services.

Since the year end, we have aligned Driving Schools more effectively with our Roadside Assistance business. This should enable us to take advantage of its strong brand and leading position and encourage relationships with potential Members at an earlier stage in their experience as motorists.

### Results

	2016	2015
Revenue (£m)	67	73
Trading EBITDA (£m)	19	20
Trading EBITDA margin (%)	28.4	27.4
Number of driving instructors	2,574	2,670

Driving Services revenue declined by £6m to £67m due to lower volumes in both Driving Schools and DriveTech. Whilst the overall number of people learning to drive in the market increased, Driving School revenue declined in line with the 3.6% fall in the number of franchised instructors. The continued buoyancy of the market has led to many instructors becoming independent. We are revamping the proposition for AA driving instructors and clarifying to learner drivers the advantages of association with the AA brand.

In DriveTech, revenue was affected by a decline in speed awareness courses following the loss of two contracts in the prior year.

Driving Services trading EBITDA was lower than last year as a result of the fall in revenue, although this decline was partly offset by the full year benefit of the reclassification of the vehicle leasing contracts.

## Ireland

AA Ireland contributed 4% of Group revenue and 3% of Group trading EBITDA excluding Head Office costs. It is one of Ireland's leading consumer services businesses, providing insurance and breakdown cover.

### Results

	2016	2015
Revenue (£m)	38	39
Trading EBITDA (£m)	13	15
Trading EBITDA margin (%)	34.2	38.5
Personal Members (000s)	128	119
Insurance policies (000s)	185	178

Revenue declined by 3% to £38m compared to the prior period due to foreign exchange movements. On a constant currency basis, revenue rose by £3m to £38m and all products contributed to this strong performance.

Personal Members increased by 8%, reflecting a 12% growth in new business volumes and continued strong retention. The 4% increase in insurance policy numbers was driven by good performance in motor insurance with retention rates strong despite an inflationary pricing environment.

Trading EBITDA on a constant currency basis was flat, with higher revenue offset by higher marketing and staff costs. However, as a result of foreign exchange movements, reported trading EBITDA declined by £2m to £13m.

## Risk Management

Our Risk Management Framework Policy requires the following:

- All areas of the business to maintain a risk register which is to be reviewed at least quarterly
- Each senior member of the Management team has his/her own set of "Top Risks" which are reviewed each month
- Risks from this "bottom up" risk identification exercise are linked to the principal risks identified by the AA plc board
- Identification and reporting of incidents and near misses which help inform our assessment of risk and helps highlight areas for control improvements
- The operation and reporting of management 'snap checks' (control effectiveness tests) and quarterly self-certification by risk register owners to confirm the effective operation of key controls
- The reporting of Key Risk Indicators (KRIs) to monitor the position against our desired risk exposure and to monitor trends and changing factors enabling us to take early corrective action

### Principal Risks

A Principal Risk is a risk or combination of risks that can seriously affect the performance, future prospects or reputation of the entity. These should include those risks that would threaten the AA's business model, future performance, solvency or liquidity.

The Directors have carried out a robust assessment of the Principal Risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. Inputs to the assessment include the strategic objectives of the Group, internal and external factors, and the risks identified by management. These principal risks have been monitored and updated by the Risk Committee during the year. These risks are detailed below together with the key mitigating actions / controls.

<b>Principal Risks</b>	<b>Description</b>	<b>Mitigating actions</b>
<b>We are unable to maintain an outstanding service at a fair price</b>	The AA's brand and its continued success rely on delivering outstanding service at a fair price. The lack of any significant investment in IT processes and systems in recent years might, if not addressed impact on our continued ability to deliver the service level our Members expect.	We will continue to maintain and protect the ability of our patrols to deliver excellent customer service by providing them with better information delivered through enhanced IT systems and connectivity. We will enhance our marketing and increase the extent of our customer engagement to demonstrate the value of our Membership offerings. On-going monitoring of complaints, press reports and social media informs our service offerings.
<b>We are unable to maintain our market share and gross margin on our roadside services</b>	Competitors that provide roadside services at a lower price together with changes in car technology threaten our roadside revenues. This requires us to demonstrate more clearly that we deliver a consistent, superior level of service and ensure our pricing remains competitive for the services we deliver.	The IT transformation programme we are undertaking will enable us to improve our overall contact with customers materially, consolidating disparate customer data and information systems, enhancing our digital offerings and improving further our roadside response. We are developing and expanding existing added value products and services which will enhance our Membership experience and enable us to be more active in demonstrating the relative benefit of our service levels. Programmes of immediate and long term initiatives are being undertaken to understand issues and drive lower costs.
<b>We are unable to grow the business in a manner that complements and sustains the brand</b>	We will be unable to develop and grow new profitable business products and lines that complement the customer experience and which demonstrate standards and values that underly our core brand.	We continue to pursue new opportunities that complement our core brand. We are developing new protocols, enhanced database management, and strengthened compliance and risk functions to ensure that we consistently deliver good products and good customer outcomes.
<b>Aggregators and price comparison sites will further damage the insurance broker model</b>	The further growth of price comparison sites may continue to transfer value from our insurance broking business.	We are using our strengths in the brand, channels and data to mitigate this risk. We are building new capability that should enable us to provide a competitive response to these intermediary sites.
<b>A changing regulatory environment may adversely affect our activities</b>	The changing regulatory environment could cause currently compliant services to become non-compliant with material implications for customer offerings, pricing and profitability. Failure to comply with regulatory obligations could result in substantial fines. Changes in Government legislation or taxation could impact the business model.	Close engagement with regulatory objectives is coupled with good governance and strong monitoring processes to ensure that we continue to focus on delivering products and services that result in good customer outcomes. Our Regulatory and Legal change Committee tracks forthcoming changes and advises the business on changes required.

<p><b>We are unable to successfully complete the essential business transformation</b></p>	<p>We need to continue to develop new management processes to achieve the transformation required to develop the business.</p>	<p>An accelerated business transformation programme is underway to recruit, develop and retain the required talent and enhance existing management processes. We have a talent management model which we use. Where gaps are identified, development and/or recruitment interventions are put in place.</p>
<p><b>We are unable to successfully deliver the essential IT transformation required</b></p>	<p>An essential programme of renewal and enhancement of our IT estate is in progress to address the risks to our brand and our competitive capability. It is extensive and involves a complex programme of work over the next 6 to 12 months. Given the scale and complexity, the programme involves inherent risks to the timely delivery of this implementation.</p>	<p>The management team is driving the overall programme supported by enhanced risk management processes. The IT transformation is being led by executives with a proven track record of IT delivery. It is generally using proven technologies and where possible is being implemented and rolled out in discrete stages. Progress is overseen by the IT &amp; Digital Transformation Steering Group.</p>
<p><b>The AA is a highly leveraged company with a substantial pension fund, currently in deficit</b></p>	<p>The Company is unable to repay or refinance its debt at an acceptable price. The Company has a large pension scheme, currently in deficit, whose assets and obligations are subject to future variation from investment returns, longevity and other similar factors.</p>	<p>We have strong recurring cash flows which support the current capital structure, and which will enable us to reduce leverage over time in line with our stated strategy. The AA pension scheme is supported by a Company covenant and the assets and obligations of the scheme are kept under review.</p>
<p><b>Information Security / Cyber Crime</b></p>	<p>Critical information is not available where and when it is needed. The integrity of critical information is corrupted or the confidentiality of commercially sensitive, private or customer information is compromised by inappropriate disclosure.</p>	<p>The AA has an ongoing programme of security improvements to try and maintain a suitable level of security for the increasingly sophisticated world-wide cyber threats. Controls include information security awareness training, preventative and detective security, a specialist information security team, and information security requirements being included in third party arrangements. The AA benchmarks its security controls against the Center for Protection of National Infrastructure (CPNI) and associated Critical Security Controls (CSC).</p>

The Group risk profile will evolve as mitigating activities succeed in reducing the net risks over time, or as new risks emerge.

Further information on the financial risks and management objectives and policies, including market, credit and liquidity risks, is included in note 25.

## Management discussion and analysis

A detailed review of the consolidated income statement, segmental analysis (see note 2) and consolidated statement of cash flows is discussed below.

### Management discussion and analysis – Consolidated income statement for the year ended 31 January 2016

**Revenue:** Revenue decreased by £12 million or 1.2% from £982 million in the year ended 31 January 2015 to £970 million in the year ended 31 January 2016. The decrease in revenue was primarily driven by a reduction in the insurance services and driving services segments as outlined below.

*Roadside Assistance:* Roadside Assistance revenue increased by £13 million or 1.8% from £711 million in the year ended 31 January 2015 to £724 million in the year ended 31 January 2016. The increase in revenue was primarily driven by increased income per Member, improved retention rate and a full year impact from the Volkswagen Group contract, launched in June 2014.

*Insurance Services:* Insurance Services revenue decreased by £11 million or 7.8% from £142 million in the year ended 31 January 2015 to £131 million in the year ended 31 January 2016. The decrease in revenue reflected the 4.1% decline in policy numbers. This was due to higher motor premiums which drove increased customer churn; as well as a decrease in motor ancillary income; and reflected our focus on profitability over volumes.

*Driving Services:* Driving Services revenue decreased by £6 million or 8.2%, from £73 million in the year ended 31 January 2015 to £67 million in the year ended 31 January 2016. The decrease in revenue was primarily driven by lower franchised instructors in Driving Schools and decline in speed awareness courses.

*Ireland:* Ireland revenue decreased by £1 million or 2.6% from £39 million in the year ended 31 January 2015 to £38 million in the year ended 31 January 2016. The decrease in revenue was primarily driven by adverse exchange movements.

**Cost of sales:** Cost of sales remained flat at £344m in both the years ended 31 January 2016 and 31 January 2015 mainly due to improved cost control in Road Operations.

**Administrative and marketing expenses:** Administrative and marketing expenses increased by £20 million or 6.7% from £298 million in the year ended 31 January 2015 to £318 million in the year ended 31 January 2016. The increase in administrative and marketing expenses was primarily driven by an increase in amortisation of software development expenditure, an increase in depreciation of vehicles and an increase in the pension service cost.

**Share of profits of joint venture and associates:** Share of profits of joint venture and associates remained at £1m in both the years ended 31 January 2016 and 31 January 2015.

**Operating profit:** Operating profit decreased by £32 million or 9.4% from £341 million in the year ended 31 January 2015 to £309 million in the year ended 31 January 2016. The decrease in operating profit was primarily driven by the increase in administrative and marketing expenses as well as the decrease in revenue as described above.

**Finance costs:** Finance costs increased by £52 million or 22.8% from £228 million in the year ended 31 January 2015 to £280 million in the year ended 31 January 2016. The increase in finance costs was driven by the refinancing that occurred in the year, see note 4.

**Finance income:** Finance income remained flat at £1m in both the years ended 31 January 2016 and 31 January 2015.

**Taxation:** Taxation increased by £13 million from £nil in the year ended 31 January 2015 to an expense of £13 million in the year ended 31 January 2016. The increase in tax expense was driven by the effect of a change in the tax rate and a credit of £22 million in the prior year that was recognised for tax losses that are forecast to be utilised against future taxable profits following the IPO of AA plc.

## **Trading EBITDA**

Trading EBITDA is a non-IFRS measure and is not a substitute for any International Accounting Standards measure.

Trading EBITDA decreased by £13 million or 3.0% from £430 million in the year ended 31 January 2015 to £417 million in the year ended 31 January 2016. The decrease in Trading EBITDA was primarily driven by the Insurance Services segment and increased costs in Head Office as outlined below.

*Roadside Assistance:* Roadside Assistance Trading EBITDA increased by £3 million or 0.8% from £358 million in the year ended 31 January 2015 to £361 million in the year ended 31 January 2016. Trading EBITDA margins remained quite flat reducing slightly from 50.4% in the year ended 31 January 2015 to 49.9% in the year ended 31 January 2016. The increase in Trading EBITDA and relatively flat Trading EBITDA margin was driven by improvement in revenue and cost savings generated by efficiencies in the patrol force and call centres offset by the investment in brand marketing of approximately £10m and new technology for the patrols as part of the IT transformation.

*Insurance Services:* Insurance Services Trading EBITDA decreased by £6 million or 7.1% from £84 million in the year ended 31 January 2015 to £78 million in the year ended 31 January 2016. Trading EBITDA margins increased from 59.2% in the year ended 31 January 2015 to 59.5% in the year ended 31 January 2016. The decrease in Trading EBITDA reflected the decline in policy numbers and the credit card run off from the legacy financial services business which benefitted the prior year results by £5m. However, improvements in efficiency within our contact centres and lower marketing spend on aggregators helped offset these adverse variances and Trading EBITDA margin was broadly in line.

*Driving Services:* Driving Services Trading EBITDA decreased by £1 million or 5.0% from £20 million in the year ended 31 January 2015 to £19 million in the year ended 31 January 2016. Trading EBITDA margins increased from 27.4% in the year ended 31 January 2015 to 28.4% in the year ended 31 January 2016. The decrease in the Trading EBITDA margin was driven by the fall in revenue. However, this was partially offset by the full year benefit of the reclassification of the vehicle leasing contracts and Trading EBITDA margins increased as a result.

*Ireland:* Ireland Trading EBITDA decreased by £2 million or 13.3% from £15 million in the year ended 31 January 2015 to £13 million in the year ended 31 January 2016. Trading EBITDA margins decreased from 38.5% in the year ended 31 January 2015 to 34.2% in the year ended 31 January 2016. The decrease in Trading EBITDA and Trading EBITDA margin was due to adverse exchange movements.

*Head Office Costs:* Head Office Costs increased by £7 million or 14.9% from £47 million in the year ended 31 January 2015 to £54 million in the year ended 31 January 2016. The increase in head office costs is primarily due to the full year impact of the Group's management structure, increase in IT costs and the costs of opening the London office.

## Management discussion and analysis – Consolidated statement of cash flows

**Net cash flow from operating activities before tax:** £374 million in the year ended 31 January 2015 compared to £376 million in the year ended 31 January 2016. This was due to a reduction in Trading EBITDA offset by favourable working capital movements.

**Tax paid:** Cash outflow from tax paid was £9 million in the year ended 31 January 2015 compared to £6 million in the year ended 31 January 2016. The reduction in cash outflow from tax paid is due to a lower payment for use of tax losses made to AA plc, partially offset by a higher tax charge for the year.

**Investing activities:** Cash outflow from investing activities was £21 million in the year ended 31 January 2015 compared to £61 million in the year ended 31 January 2016 which primarily related to software development expenditure.

**Financing transactions:** Cash outflow from financing transactions was £6 million in the year ended 31 January 2015 compared to £203 million in the year ended 31 January 2016. The increase in cash outflows on financing transactions relates to the refinancing that took place in the current year including debt repayment penalties of £58 million and the net repayment of debt.

**Interest paid on borrowings:** Cash outflow from the interest paid on borrowings was £184 million in the year ended 31 January 2015 compared to £172 million in the year ended 31 January 2016. The decrease in interest paid on borrowings is due to the full year impact of the refinancing that took place in the current year.

**Payment of finance lease capital and interest:** Cash outflow from the payment of finance lease capital and interest was £35 million in the year ended 31 January 2015 compared to £42 million in the year ended 31 January 2016. The increase in cash outflows from payment of finance lease capital and interest was primarily driven by the full year impact of the change in classification of the driving school leases in the prior year.

**Dividends paid:** Cash outflow from dividends paid was £nil in the year ended 31 January 2015 compared to £60 million in the year ended 31 January 2016. The increase in cash outflow from dividends was due to a dividend paid to the parent company, AA plc.

By order of the Board

M Clarke  
Director

29 June 2016

## Directors' report

The Directors present their report and audited consolidated financial statements of AA Intermediate Co Limited ("the Company") and its subsidiary undertakings for the year ended 31 January 2016.

The Directors who held office during the year were as follows:

Bob Mackenzie	Executive Chairman	
Martin Clarke	Chief Financial Officer	
Nick Hewitt	Executive Director	Resigned 31 July 2015
Mark Millar	Director	Appointed 16 October 2015
Gillian Pritchard	Director	Appointed 30 April 2016
Rob Scott	Director	Resigned 30 April 2016
Mark Millar	Company Secretary	

AA Intermediate Co Limited is a Private Limited Company registered and domiciled in England and Wales, registered address Fanum House, Basing View, Basingstoke, Hampshire, RG21 4EA.

### Directors' indemnities

The Company maintains directors' and officers' liability insurance, which gives appropriate cover for any legal action brought against its directors and officers. The Company has also granted indemnities to each of its directors and the Company Secretary to the extent permitted by Law. Qualifying third party indemnity provisions (as defined by section 234 of the Act) were in force during the year ended 31 January 2016 and remain in force, in relation to certain losses and liabilities which the directors or Company Secretary may incur to third parties in the course of acting as directors or Company Secretary or employees of the Company or any associated company.

### Charitable work

Our contribution to the community at large is represented by the extensive work of the AA Charitable Trust for Road Safety and the Environment (1125119). It was established in 2008 to educate and campaign on road safety and to show how the environmental impact of motoring can be reduced. The Trust, which is largely funded by donations from the Group, has conducted the following practical initiatives during the last year.

### Improving road safety

We have continued a programme of driver training that aims to improve skills and confidence, thus making our roads safer. Specific initiatives are:

- **Drive Motorway** Free training to improve the confidence of drivers who are nervous of motorways, one of the most common fears as confirmed by AA Populus research.
- **Drive Confident** Training to renew the confidence and improve the competence of nervous and lapsed drivers.
- **Drive Smart** Training to teach young drivers, considered "at risk", safe and eco-friendly driving techniques.
- The AA also supports events such as Thames Valley Police's **Safe Drive Stay Alive** roadshow.

### Driving lessons for young people in care

The Trust completed the pilot of the Driving for Looked After Young People project, which gave four teenagers in the care system the rare opportunity to learn to drive. The project was undertaken in conjunction with Bristol University and Bristol Council and the results highlighted the disproportionately positive effect of driving lessons on the candidates' self-esteem and confidence. The scheme is now being rolled-out in Newcastle, Medway and Westminster and a further pilot is planned in Bristol.

## **Directors' report (*continued*)**

### **Employee charitable work**

At a more individual level AA employees raised in excess of £150,000 for a wide range of national charities including the Children's Heart Unit Fund and the Royal National Institute of Blind People. We also responded to the devastating earthquake in Nepal by collecting blankets and funds. More locally, we raised funds for smaller charities and supported our communities through such events as litter clean-ups.

Many AA employees support BEN, the UK's dedicated charity for those who work, or have worked, in automotive-related industries. Our patrols once again supported the Help for Heroes 4x4 rally and various charity bike rides.

### **Our campaigning**

Since our foundation in 1905 we have campaigned to protect the interests of motorists and our Members, striving to be the responsible motorists' champion. As a result the AA is widely associated with road safety and our best known awareness campaign is 'Think Bikes'.

In 2015, the campaign won the Fédération Internationale de l'Automobile (FIA) Innovation award; a UK fleet safety award; the Public Relations Consultants' Association (PRCA) Automotive Award; and the Fédération Internationale de Motorcyclisme (FIM) campaign award. The Charitable Trust worked with the FIA to launch Think Bikes in Brussels outside the European Parliament and road safety groups in 24 countries, including Iceland, Italy, Iran and Lithuania, have adopted the 'Think Bikes' campaign.

Today we continue to influence Government policy in line with AA Members' views and concerns as expressed to us via the AA Populus Panel. This panel comprises more than 300,000 drivers and attracts approximately 25,000 responses each month. We know that AA Members' biggest concerns are the condition of the roads, in particular potholes, and the cost of motoring and road safety. The panel gives us the views with which to influence policy on issues such as fuel price transparency. We also use Populus data to work with external bodies on road safety campaigns, such as our joint work with the UK Environment Agency on flooding.

During the 2016 financial year, the AA continued to work on campaigns including the following:

- Road Safety – SURVIVE group for motorway hard shoulder safety.
- AA/Jameson joint anti drink-driving campaigns.
- Support for EuroNCAP crash testing programme.
- Presentations to Road Safety GB, TISPOL international traffic Police conference.
- The AA regularly meets with ministers and opposition front bench, Select Committees and responds to Government consultations on important issues such as the driving test.
- Support for UN Decade of Action on Road Safety.

### **OBE Award for AA President Edmund King**

The AA is extremely proud that Edmund King was appointed an Officer of the Order of the British Empire (OBE) in the 2016 New Year's Honour List for his services to road safety. While his efforts at the AA have ensured AA Members are represented and their voice is heard, Edmund has been a tireless and dedicated campaigner on road safety over the past 25 years in his various roles with the AA, leading think-tanks and charities. He has measurably helped to improve road safety across the UK and internationally and this honour is a reflection of his long-standing commitment and the success of the campaigns, such as Think Bikes! that he has played a prominent role in delivering.

## **Directors' report (*continued*)**

Edmund King acknowledged the collaborative nature of campaigns by describing the OBE as a “clear reflection of the efforts of my present and past colleagues and the road safety partners and organisations that I have worked with over the years”. He remains dedicated to advancing road safety and educating drivers and many future campaigns are planned.

### **Our People**

Our employees are key to our success. Their work is at the heart of what we do, meeting Members' needs and delivering the full range of services, products and benefits offered by the AA. We promote a culture where employees are empowered and incentivised to offer high quality customer service.

During the 2016 financial year we employed an average of 7,860 people. Our customer-facing patrols and advisors make up more than half our employees and deliver our core Roadside Assistance services 24 hours a day throughout the year.

### **Human Rights**

We aim to engage all our stakeholders with fairness, dignity and respect and endorse the UN Declaration of Human Rights. The AA does not tolerate child labour and forced labour. We respect freedom of association and the rights of employees to be represented by trade unions or works councils. The AA is a fair employer and does not discriminate on the basis of gender, religion, age, disability and ethnicity.

Our policy applies throughout the AA and it is communicated to our employees and contractors during induction training.

### **Diversity**

The Board recognises the benefits of diversity, including gender diversity, throughout the AA and ensures that we have an appropriate balance of skills and experience.

### **Employee engagement**

We engage in regular dialogue with our employees through multiple channels. We communicate internally through the intranet and global emails, one to one meetings, in-house magazines and conferences and we engage in consultation with the AA's recognised union, the IDU and have an elected Management Forum.

### **Training and Education**

We are currently completely reviewing our management learning and development approach with the introduction of revised management training, and essential e-learning for all employees covering key areas such as Data Protection, Equality and Diversity, and Anti-Bribery and Corruption.

During the year, we trained line managers in our key human resources (HR) policies with the aim of developing them and equipping them with the necessary skills to support and lead their teams. This training was completed by the end of 2015 and from 2016, all new managers will be trained through available E-learning modules.

We encourage all employees to carry out their work to the best of their ability. We promote learning and skills development opportunities across the organisation.

We have a further education policy where financial assistance is provided to employees wishing to follow a vocational course aligned to their work.

Extensive training is provided for patrols to keep their technical knowledge up to date at the AA's training centre in the Midlands. All contact centres have training departments that provide induction training and update employees on new processes and products.

## **Directors' report (*continued*)**

### **Employee Wellbeing**

We offer a confidential Employee Wellbeing Programme to all AA employees and their immediate families. Various levels of support, including face-to-face counselling if appropriate, is provided free of charge and in confidence. During the 2016 financial year, 264 AA people used this service.

We also have a dedicated occupational health provider, who offers professional advice and assessments in relation to physical and mental health issues to both the employee and the manager to ensure appropriate support is given.

### **AA and the Armed Forces**

In January 2016 the AA was recognised by the Prime Minister and the Defence Secretary as showing an outstanding commitment to supporting the Armed Forces. The AA has hired over 60 Armed Forces leavers in the past year alone.

We received a Gold Award in the Armed Forces Covenant Employer Recognition Scheme. This recognises businesses that support those who serve or have served in the Armed Forces, or their families and ensures they are treated fairly. In addition to recognition for promoting the benefits of employing reserves and developing supportive HR policies, our work with The Poppy Factory, a charity which helps injured service personnel back into work, was also recognised.

### **Apprentices**

We aim to develop talent in our localities to help address youth unemployment and have run an apprenticeship programme in our call centre in Oldbury since 2009. More than 200 apprentices have completed the programme including 34 last year, the highest intake in a year. We are proud to have trained and developed 50 apprentices to work in full-time and critical, customer-facing roles delivering AA services and handling emergency calls.

Our apprentices complete an NVQ Level 2 or 3 in customer service and functional skills through our partnership with Sandwell College. They are recruited from Birmingham and the Black Country where youth employment has been in excess of 20% for people aged between 16 and 24.

### **Work Experience**

Every summer we invite eight students from a local school to do work experience in Roadside Assistance. We also offer a programme with local schools to develop skills for employment, participating in mock interviews, assisting in CV writing, giving tips on applying for jobs and allowing visits to our sites to see how our business operates. This helps our local community and serves as a recruitment stream.

We also work with local schools, colleges and businesses. We participated in a 'Mindshop Excellence' week with a local firm of solicitors to give Year 12 students from a local academy a 'real-world' business problem to solve.

### **Health and Safety at the AA**

Health and safety is one of our highest priorities. We strive to protect the health and safety of our employees and all the people we come into contact with. We are committed to fostering and maintaining a healthy and safe working environment.

Our safety management system is written to OSHAS 18001 standards, with AA DriveTech being certified to this standard. This helps us to identify risks and hazards and ensure our existing suite of policies and codes of behaviour are up-to-date and effective. Our systematic and comprehensive approach to health and safety includes goal setting, planning and performance measurement.

## **Directors' report (*continued*)**

Our patrols work in potentially dangerous situations where the risks include moving traffic, slips, trips and falls, manual handling of equipment and road traffic collisions. We minimise risks through training, the equipment we give them and by reporting, investigating and learning lessons from accidents and near misses.

### **Safety Performance**

High health and safety standards are implicit in our service to Members. During the year, we continued to focus on risk management, empowerment of our staff through their knowledge of health and safety and improving Near-Miss reporting.

We look for continual improvement by monitoring performance and auditing our systems to ensure our management of health and safety remains effective. In addition, we also have in place improvement programmes which identify objectives and targets along with the action plan we will implement to achieve these.

Since 2010 we have seen year on year improvement in our accident performance with the number of accidents halving over five years. This improvement has been achieved through implementation and delivery of safety training programmes and focusing on performance monitoring and measurement.

In the 2016 financial year, we improved our Near-Miss reporting system with an on-line reporting tool for patrols which has resulted in more near-misses being reported to us than accidents. The AA is the only UK breakdown company to actively collect, collate and act upon Near-Miss reporting, enabling us to take action to minimise potential accidents.

### **Protecting our Members**

We were the first UK breakdown company to begin our response to breakdown calls with safety advice to ensure Members are given this all-important information immediately. We were also the first to pioneer three-way telephone calls between us, the Member and the Police for breakdown situations in dangerous locations.

### **Protecting all motorists and road users**

We work closely with motor manufacturers and the UK Government to help improve the safety of our roads. For example, AA DriveTech trainers lead Ford's Driving Skills for Life courses aimed at young drivers. In addition, we have trialled smaller recovery trucks in London which are designed to meet the requirements of the London Safe Lorry Scheme. This has been successful and plans are in place to bring these lorries to 50% of our London fleet, helping us to do our part in supporting Transport for London's "Safe Streets for London" project.

### **Disclosure of information to the auditors**

Each director has made enquiries of their fellow directors and the Group's auditor and taken all the steps that they are obliged to take as a director in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

Relevant audit information is that information needed by the auditor in connection with preparing the report. So far as each director approving this report is aware, and based on the above steps, there is no relevant audit information of which the auditor is unaware.

## **Directors' report (*continued*)**

### **Statement of Directors' responsibilities**

The Directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable laws and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and Group and the profit or loss of the Company and Group for that period.

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRS has been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company, or the Group, will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company, and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

It is the Group's policy to maintain indemnity insurance for Directors and officers.

## **Directors' report (*continued*)**

### **Going concern**

The Group's business activities, together with the factors likely to affect its future development, performance, position and risk management objectives are described in the strategic report.

The Group has long-term contracts with a number of suppliers across different industries and its activities are highly cash generative. The Group's borrowings are long-term in nature and the Group had £94 million of cash and cash equivalents of which £74 million is freely available to use within the business. The Directors believe that the Group is well placed to manage its business risks successfully.

The Directors have reviewed cash flow projections and financial covenant forecasts and have concluded that the Group has sufficient funds to continue trading for the foreseeable future, being at least one year from the date of signing of these financial statements. Therefore, the financial statements have been prepared using the going concern basis.

### **Post balance sheet events**

Details of post balance sheet events can be found in note 34.

By order of the Board

M Clarke  
Director

29 June 2016

Fanum House  
Basing View  
Basingstoke  
Hampshire  
RG21 4EA

## **INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF AA INTERMEDIATE CO LIMITED**

We have audited the financial statements of AA Intermediate Co Limited for the year ended 31 January 2016 which comprise the Consolidated Income Statement, the Consolidated Statement of Financial Position, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Cash Flows, the Consolidated Statements of Changes in Equity and the related notes 1 to 34 in the Group financial statements, the Parent Company Balance Sheet, the Parent Company Statement of Changes in Equity and notes 1 to 8 in the Company financial statements. The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 "Reduced Disclosure Framework".

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 auditor's 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 auditor**

As explained more fully in the Directors' Responsibilities Statement set out on page 20 the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### **Opinion on financial statements**

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 January 2016 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including FRS 101 "Reduced Disclosure Framework"; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

### **Opinion on other matters prescribed by the Companies Act 2006**

In our opinion:

- based on the work undertaken in the course of the audit:
  - the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.
  - the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements;

In light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have identified no material misstatements in the Strategic Report or Directors' Report

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Kathryn Barrow (Senior Statutory Auditor)  
For and on behalf of Ernst & Young LLP  
London

## Consolidated income statement

		for the year ended 31 January	
	Note	2016 £m	2015 £m
Revenue	2	970	982
Cost of sales		(344)	(344)
<b>Gross profit</b>		<b>626</b>	638
Administrative & marketing expenses		(318)	(298)
Share of profits of joint venture and associates, net of tax		1	1
<b>Operating profit</b>		<b>309</b>	341
Trading EBITDA	2	417	431
Items not allocated to a segment	2	(18)	(8)
Amortisation and depreciation	9,10	(54)	(48)
Exceptional items	3	(36)	(34)
<b>Operating profit</b>	3	<b>309</b>	341
Finance costs	4	(280)	(228)
Finance income	5	1	1
<b>Profit before tax</b>		<b>30</b>	114
Tax expense	8	(13)	-
<b>Profit for the year</b>		<b>17</b>	114

The accompanying notes are an integral part of this consolidated income statement.

## Consolidated statement of comprehensive income

for the year ended 31 January			
	Note	2016 £m	2014 £m
<hr/>			
<b>Profit for the year</b>		<b>17</b>	114
<hr/>			
<b>Other comprehensive income on items that may be reclassified to profit and loss in subsequent years</b>			
Exchange differences on translation of foreign operations		1	(1)
Effective portion of changes in fair value of cash flow hedges		10	(14)
Tax effect (expense) / credit	8	(2)	3
		<b>9</b>	(12)
<hr/>			
<b>Other comprehensive income on items that will not be reclassified to profit and loss in subsequent years</b>			
Remeasurement gains / (losses) on defined benefit schemes	22	149	(167)
Tax effect (expense) / credit	8	(26)	32
		<b>123</b>	(135)
<hr/>			
<b>Total other comprehensive income</b>		<b>132</b>	(147)
<hr/>			
<b>Total comprehensive income for the year</b>		<b>149</b>	(33)
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The accompanying notes are an integral part of this consolidated statement of comprehensive income.

## Consolidated statement of financial position

		as at 31 January	
	Note	2016 £m	2015 £m
<b>Non-current assets</b>			
Goodwill and other intangible assets	9	1,290	1,256
Property, plant and equipment	10	122	100
Investments in joint ventures and associates	11	6	4
Deferred tax assets	8	52	81
Other receivables	13	-	21
		<b>1,470</b>	<b>1,462</b>
<b>Current assets</b>			
Inventories	12	5	5
Trade and other receivables	13	170	185
Current tax receivable		-	1
Amounts owed by parent undertaking	15	1,214	1,205
Cash and cash equivalents	14	94	262
		<b>1,483</b>	<b>1,658</b>
<b>Total assets</b>		<b>2,953</b>	<b>3,120</b>
<b>Current liabilities</b>			
Trade and other payables	16	(517)	(495)
Current tax payable		(7)	-
Amounts owed to parent undertaking	15	-	(4)
Provisions	19	(8)	(8)
		<b>(532)</b>	<b>(507)</b>
<b>Non-current liabilities</b>			
Borrowings and loans	17	(2,920)	(3,068)
Finance lease obligations	26	(21)	(16)
Defined benefit pension scheme liabilities	22	(296)	(434)
Provisions	19	(7)	(12)
		<b>(3,244)</b>	<b>(3,530)</b>
<b>Total liabilities</b>		<b>(3,776)</b>	<b>(4,037)</b>
<b>Net liabilities</b>		<b>(823)</b>	<b>(917)</b>
<b>Equity</b>			
Share capital	20	20	20
Currency translation reserve	21	(1)	(2)
Cashflow hedge reserve	21	(10)	(18)
Retained earnings	21	(832)	(917)
<b>Total equity attributable to equity holders of the parent</b>		<b>(823)</b>	<b>(917)</b>

Signed for and on behalf of the Board on 29 June 2016 by

M Clarke  
Director

The accompanying notes are an integral part of this consolidated statement of financial position.

## Consolidated statement of changes in equity

	Note	Attributable to the equity holders of the parent					Total £m
		Share capital £m	Currency translation reserve £m	Cashflow hedge reserve £m	Retained earnings £m		
<b>At 1 February 2014</b>		<b>20</b>	<b>(1)</b>	<b>(7)</b>	<b>(898)</b>	<b>(886)</b>	
Profit for the year		-	-	-	114	114	
Other comprehensive income		-	(1)	(11)	(135)	(147)	
Total comprehensive income		-	(1)	(11)	(21)	(33)	
Share-based payments	31	-	-	-	2	2	
<b>At 31 January 2015</b>		<b>20</b>	<b>(2)</b>	<b>(18)</b>	<b>(917)</b>	<b>(917)</b>	
Profit for the year		-	-	-	17	17	
Other comprehensive income		-	1	8	123	132	
Total comprehensive income		-	1	8	140	149	
Dividends		-	-	-	(60)	(60)	
Share-based payments	31	-	-	-	5	5	
<b>At 31 January 2016</b>		<b>20</b>	<b>(1)</b>	<b>(10)</b>	<b>(832)</b>	<b>(823)</b>	

The accompanying notes are an integral part of this consolidated statement of changes in equity.

## Consolidated statement of cash flows

	Note	for the year ended 31 January	
		2016 £m	2015 £m
Profit before tax		30	114
Amortisation and depreciation		54	48
Net finance costs		279	227
Other adjustments to profit before tax		10	1
Working capital:			
Decrease/(increase) in trade and other receivables		5	(24)
Increase in trade and other payables		5	25
Decrease in provisions		(6)	(8)
Difference between pension charge and cash contributions		(1)	(9)
Total working capital adjustments		3	(16)
<b>Net cash flows from operating activities before tax</b>		<b>376</b>	<b>374</b>
Tax paid		(6)	(9)
<b>Net cash flows from operating activities</b>		<b>370</b>	<b>365</b>
<b>Investing activities</b>			
Capital expenditure		(74)	(37)
Proceeds from sale of fixed assets		11	15
Acquisitions and disposals, net of cash acquired or disposed of		1	-
Interest received		1	1
<b>Net cash flows used in investing activities</b>		<b>(61)</b>	<b>(21)</b>
<b>Financing activities</b>			
Proceeds from borrowings		735	913
Issue costs on borrowings		(16)	(6)
Repayment of borrowings		(864)	(913)
Debt repayment penalties		(58)	-
Refinancing transactions		(203)	(6)
Interest paid on borrowings		(172)	(184)
Payment of finance lease capital		(34)	(31)
Payment of finance lease interest		(8)	(4)
Dividends paid		(60)	-
<b>Net cash flows from financing activities</b>		<b>(477)</b>	<b>(225)</b>
<b>Net increase in cash and cash equivalents</b>		<b>(168)</b>	<b>119</b>
Net foreign exchange differences		-	(2)
Cash and cash equivalents at 1 February	14	262	145
<b>Cash and cash equivalents at 31 January</b>	<b>14</b>	<b>94</b>	<b>262</b>

The accompanying notes are an integral part of this consolidated statement of cash flows.

## Consolidated statement of cash flows (continued)

The cash flows from operating activities are stated net of cash outflows relating to exceptional items of £36m (2015: £43m). This relates to the cost of business transformation of £21m (2015: £nil), costs incurred in connection with the IPO of AA plc of £nil (2015: £18m), re-financing of the Group's borrowings £4m (2015: nil), acquisition earn-out payments of £nil (2015: £2m), non-recurring costs of IT system implementation and cost restructuring activities of £7m (2015: £19m) and onerous property provision lease costs in respect of vacant properties of £4m (2015: £4m).

Other adjustments to profit before tax of £10m (2015: £1m) include share of profit from joint ventures and associates of (£1m) (2015: (£1m)), share based payments of £5m (2015 £2m), loss on sale of fixed assets of £3m (2015: £nil) and loss on disposal of subsidiary of £3m (2015: £nil).

## Notes to the consolidated financial statements

### 1 Basis of preparation

#### 1.1 General information

The consolidated financial statements for the year ended 31 January 2016 comprise the financial statements of AA Intermediate Co Limited ('the Company') and its subsidiaries (together referred to as 'the Group'). AA Intermediate Co Limited is a limited company incorporated and domiciled in the United Kingdom.

These statements have been presented to the nearest £million and the prior year comparatives have been restated accordingly.

#### 1.2 Basis of preparation

The Group has prepared these statements under International Financial Reporting Standards (IFRS) as adopted by the European Union, International Financial Reporting Interpretation Council (IFRIC) interpretations and those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

These consolidated financial statements have been prepared under the historic cost convention as modified by the measurement of derivatives and liabilities for contingent consideration in business combinations at fair value.

##### a) Going concern

The Group is highly cash generative with a large proportion of its revenues coming from recurring transactions. The significant customer loyalty demonstrated by the high renewal rates and lengthy customer tenure underpins this. The Group's borrowings are long-term in nature and in addition to the cash balances at the reporting date the Group has agreed undrawn credit facilities. Additionally, the Group has ready access to both public debt and equity markets allowing these borrowings to be easily refinanced in due course. The Directors have reviewed projected cash flows for a period of one year from the date of signing these financial statements and have concluded that the Group has sufficient funds to continue trading for this period and the foreseeable future. Therefore, the financial statements have been prepared using the going concern basis.

##### b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has rights to variable returns from its involvement with the entity and has the ability to influence those returns through its power over the entity.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies into line with those used by the Group. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

#### 1.3 Accounting policies

The principal accounting policies are set out below.

##### a) Interests in joint ventures and associates

An associate is an entity over which the Group is in a position to exercise significant influence, but not control or joint control, through participating in the financial and operating policy decisions of the entity. Joint ventures are joint arrangements whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

The results, assets and liabilities of joint ventures and associates are incorporated in these financial statements using the equity method of accounting. Investments in joint ventures and associates are carried in the Group balance sheet at cost as adjusted by post-acquisition changes in the Group's share of the net assets less any impairment losses.

### 1.3 Accounting policies (*continued*)

#### b) Foreign currencies

These financial statements are presented in pounds sterling which is the currency of the primary economic environment in which the Group operates.

Transactions in currencies other than the functional currency of each consolidated undertaking are recorded at rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the respective functional currency at rates of exchange ruling at the balance sheet date. Gains and losses arising on the translation of assets and liabilities are taken to the income statement.

The results of overseas operations are translated into sterling at average rates of exchange for the period. Exchange differences arising on the retranslation of the opening net assets of overseas operations are transferred to the Group's cumulative translation reserve in equity.

#### c) Business combinations and goodwill

All business combinations are accounted for by applying the acquisition method.

Costs related to the acquisition, other than those associated with the issue of debt or equity securities, are expensed as incurred.

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identified assets and liabilities of a subsidiary at the date of acquisition. Goodwill is recognised as an asset at cost less accumulated impairment losses.

Any contingent consideration payable is recognised at fair value at the acquisition date, and subsequent changes to the fair value of the contingent consideration are recognised in profit or loss. Any consideration paid to a former owner who continues to work for the business as part of the acquisition that is contingent on future service is excluded from goodwill and treated as acquisition earn-out costs within administrative and marketing expenses.

#### d) Intangible assets

Intangible assets other than goodwill which are acquired separately are stated at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and impairment losses. Intangible assets with finite lives are amortised over the useful economic life.

#### e) Software and development costs

Software development expenditures on an individual project are recognised as an intangible asset when the Group can demonstrate:

- The technical feasibility of completing the intangible asset so that it will be available for use or sale
- Its intention to complete and its ability to use or sell the asset
- How the asset will generate future economic benefits
- The availability of resources to complete the asset
- The ability to measure reliably the expenditure during development

Following initial recognition of the development expenditure as an asset, the cost model is applied. The asset is carried at cost less any accumulated amortisation and impairment losses. Amortisation of the asset begins when development is complete and the asset is available for use. It is amortised over its useful life of three to five years.

### **1.3 Accounting policies (continued)**

#### **f) Property, plant and equipment**

Land and buildings held for use in the production of goods and services or for administrative purposes are stated in the balance sheet at cost or fair value for assets acquired in a business combination less any subsequent accumulated depreciation and impairment losses. No capitalised interest is included in the cost of items of property, plant and equipment.

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses. Such costs include costs directly attributable to making the asset capable of operating as intended. The cost of property, plant and equipment less their expected residual value is depreciated by equal instalments over their useful economic lives. These lives are as follows:

Buildings	50 years
Related fittings	3 – 20 years
Leasehold properties	over the period of the lease
IT Systems (hardware)	3 – 5 years
Plant, vehicles and other equipment	3 – 10 years

Assets held under finance leases are depreciated on a straight line basis over the lease term.

#### **g) Inventories**

Inventories are stated at the lower of cost and net realisable value. Costs include all costs incurred in bringing each product to its present location and condition. Net realisable value is based on estimated selling price less any further costs expected to be incurred to completion and disposal.

#### **h) Financial instruments**

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument. They are classified according to the substance of the contractual arrangements entered into. At each reporting date the Group assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

##### *Trade receivables and trade payables*

Trade receivables (excluding instalment debtors) and trade payables are not interest bearing and are recognised initially at fair value. Instalment debtors accrue interest on the month end balance. 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.

##### *Cash and cash equivalents*

Cash and cash equivalents comprise cash balances and call deposits with an original maturity less than three months.

##### *Debt instruments*

Debt is initially recognised in the balance sheet at fair value less transaction costs incurred directly in connection with the issue of the instrument. Debt issue fees in respect of the instruments, including discounts on issue, are capitalised at inception and charged to the income statement over the term of the instrument using the effective interest method.

##### *Equity instruments (share capital issued by the Group)*

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all its liabilities. Equity instruments are recognised at the fair value of proceeds received less direct issue costs.

##### *Derivative financial instruments*

The Group's capital structure exposes it to the financial risk of changes in interest rates. The Group uses interest rate swap contracts to hedge these exposures. Early repayment penalty clauses are assessed as to whether they should be classified as derivative financial instruments.

### **1.3 Accounting policies (continued)**

Derivative financial instruments are recorded in the balance sheet at fair value. The fair value of derivative financial instruments is determined by reference to market values for similar financial instruments. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss unless they qualify for hedge accounting as described below.

#### *Cashflow hedges*

Changes in the fair value of derivative financial instruments that are designated as highly effective hedges of future cashflows are recognised in other comprehensive income. Any ineffective portion of the hedge is recognised immediately in the income statement. Amounts recognised in other comprehensive income are reclassified from equity to profit and loss (within finance costs) in the period when the hedged item affects profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised in the other comprehensive income at that time remains in equity and is reclassified when the hedged transaction is ultimately recognised in the income statement.

In order to qualify for hedge accounting, the Group is required to document from inception the relationship between the item being hedged and the hedging instrument and demonstrate that the hedge will be highly effective on an on-going basis. This effectiveness testing is performed at each period end to ensure that the hedge remains highly effective.

#### **i) Impairment of assets**

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. In addition goodwill and intangible assets not yet available for use are tested for impairment annually.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the cash generating units or "CGUs"). The goodwill acquired in a business combination is allocated to CGUs so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognised if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any allocated goodwill and then to reduce the carrying amounts of the other assets on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

#### **j) Leases**

Finance leases transfer substantially all of the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is shown as a financial liability. Lease payments are apportioned between finance charges and the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the income statement.

Rentals payable and receivable under operating leases are charged, or credited, to the income statement on a straight-line basis over the term of the relevant lease. Any incentives to enter into an operating lease are recognised evenly over the lease term.

### **1.3 Accounting policies (continued)**

#### **k) Provisions**

A provision is required when the Group has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required of an amount that can be reliably estimated. Provisions are discounted where the impact is material.

Provisions for restructuring costs are recognised when the Group has a detailed formal plan for the restructuring that has been communicated to affected parties.

For property leases, where a decision has been made prior to the year end to permanently vacate the property, provision is made for future rent and similar costs net of any rental income expected to be received up to the estimated date of final disposal.

#### **l) Retirement benefit obligation**

The Group's position in respect of defined benefit pension plans is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets (at bid price) is deducted. The Group determines the net interest on the net defined benefit liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability.

The discount rate is the yield at the reporting date on bonds that have a credit rating of at least AA with maturity dates approximating the terms of the Group's obligations and that are denominated in the currency in which the benefits are expected to be paid.

Remeasurements arising from defined benefit plans comprise actuarial gains and losses and the return on plan assets (excluding interest). The Group recognises them immediately in other comprehensive income and all other expenses related to defined benefit plans in administrative and marketing expenses in profit or loss.

When the benefits of a plan are changed, or when a plan is curtailed, the portion of the changed benefit related to past service by employees, or the gain or loss on curtailment, is recognised immediately in profit or loss when the plan amendment or curtailment occurs.

The calculation of the defined benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of any minimum funding requirements.

For defined contribution schemes, the amounts recognised in profit or loss are the contributions payable in the year.

#### **m) Revenue recognition**

Revenue is measured at the fair value of the consideration receivable less any discounts and excluding value added tax and other sales related taxes.

Roadside membership subscriptions and premiums receivable on underwritten insurance products are apportioned on a time basis over the period where the Group is liable for risk cover. The unrecognised element of subscriptions and premiums receivable, relating to future periods, is held within liabilities as deferred income.

Commission income from insurers external to the Group is recognised at the commencement of the period of risk.

Where customers choose to pay by instalments, the Group charges interest based on the principal outstanding and disclosed interest rate and recognises this income over the course of the loan.

For all other revenue, income is recognised at point of delivery of goods or on provision of service. This includes work which has not yet been fully invoiced, provided that it is considered to be fully recoverable.

### **1.3 Accounting policies (*continued*)**

#### **n) Insurance contracts**

An insurance contract is a contract under which insurance risk is transferred to the issuer of the contract by another party. The Group accepts insurance risk from its customers under roadside recovery service contracts by agreeing to provide services whose frequency and cost is uncertain. Claims and expenses arising from these contracts are recognised in profit or loss as incurred.

At the balance sheet date, a liability adequacy test is performed to ensure the adequacy of the insurance contract liabilities. In performing these tests, current estimates of future cash outflows arising under insurance contracts are considered and compared with the carrying amount of deferred income and other insurance contract liabilities. Any deficiency is immediately recognised in profit or loss and an onerous contract provision is established.

The estimation of the ultimate liability from claims made under insurance contracts is not considered to be one of the Group's most critical accounting estimates. This is because there is a very short period of time between the receipt of a claim, i.e. a breakdown, and the settling of that claim. Consequently there are no significant provisions for unsettled claims costs in respect of the roadside assistance services.

#### **o) Exceptional items**

Exceptional items are events or transactions that fall within the operating activities of the Group and which by virtue of their size or incidence have been disclosed in order to improve a reader's understanding of the financial statements. See note 3 for further information on the nature of exceptional items.

In addition, occasionally there are events or transactions that fall below operating profit that are one-off in nature and items within operating profit that relate to transactions that do not form part of the on-going segment performance and which by virtue of their size or incidence have been separately disclosed in the financial statements.

#### **p) Finance income and costs**

Finance costs comprise interest payable, finance charges on finance leases recognised in profit or loss using the effective interest method, unwinding of the discount on provisions (including the net defined benefit obligations) and net foreign exchange losses that are recognised in the income statement (see foreign currency accounting policy).

Finance income comprises interest receivable on funds invested and net foreign exchange gains.

Foreign currency gains and losses are reported on a net basis.

#### **q) Taxation**

Tax on the profit or loss for the year comprises current and deferred tax.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

#### **r) Segmental analysis**

The Group reports its operations using the segments that are reported for management purposes. Segments are based on business operations because this is where Group risk and return is focussed, with the exception of Ireland which represents the Group's only material operations outside of the UK.

### 1.3 Accounting policies (*continued*)

#### s) Share-based payments

The Group operates a number of equity settled, share-based payment compensation plans for employees. The fair value of the equity settled awards is measured at the grant date based on expectations of performance conditions being met. The fair value of the awards is recognised as an expense with a corresponding credit to reserves.

#### t) Critical accounting estimates and judgements

Estimates are evaluated continually and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions about the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

Management have exercised judgement in applying the Group's accounting policies and in making critical estimates. The underlying assumptions on which these judgements are based, are reviewed on an on-going basis and include the selection of assumptions in relation to the retirement benefit obligation and assumptions for future growth of cash flows to support the value-in-use calculations for the goodwill impairment review.

The principal estimates and assumptions that have a risk of causing an adjustment to the carrying amounts of assets and liabilities within the next financial period are discussed below.

##### *Retirement benefit obligation*

The Group's retirement benefit obligation, which is actuarially assessed each period, is based on key assumptions including return on plan assets, discount rates, inflation, future salary and pension costs. These assumptions may be different to the actual outcome.

##### *Derivative financial Instruments*

The fair value of derivative financial instruments is determined by reference to market values for similar financial instruments. The Group is therefore required to identify changes in market conditions around expectations for interest rates. These assumptions may be different to the actual outcome.

##### *Goodwill*

The Group tests goodwill for impairment annually. The recoverable amounts of cash generating units have been determined based on value-in-use calculations which require the use of estimates. Management have prepared discounted cash flows based on the latest strategic plan.

##### *Share-based payments*

The Group has issued a number of share-based payment awards to employees during the year which are measured at fair value. This involves estimates about the expected volatility of the share price and the number of leavers over the vesting period.

## 2 Segmental information

	2016 £m	2015 £m
<b>Revenue</b>		
Roadside Assistance	724	711
Insurance Services	131	142
Driving Services	67	73
Ireland	38	39
<b>Trading Revenue</b>	<b>960</b>	965
Revenue from business disposed of	10	17
<b>Group Revenue</b>	<b>970</b>	982
<b>Trading EBITDA</b>		
Roadside Assistance	361	358
Insurance Services	78	84
Driving Services	19	20
Ireland	13	15
Head Office costs	(54)	(47)
<b>Trading EBITDA</b>	<b>417</b>	430
EBITDA from business disposed of	-	1
<b>Group Trading EBITDA</b>	<b>417</b>	431
Items not allocated to a segment	(18)	(8)
Amortisation and depreciation	(54)	(48)
Exceptional items	(36)	(34)
<b>Operating profit</b>	<b>309</b>	341
Net finance costs	(279)	(227)
<b>Profit before tax</b>	<b>30</b>	114

With the exception of Ireland, all other segments operate wholly in the UK. Turnover by destination is not materially different from turnover by origin.

During August 2015, the Group disposed of its windscreen replacement subsidiary Autowindshields (UK) Limited. The results of this business have been presented above as business disposed of.

## **2 Segmental information (*continued*)**

For management purposes, the Group is organised into business units based on their products and services, with the exception of Ireland, which represents a separate geographical area. The Group has five reportable operating segments as follows:

- *Roadside Assistance*: This segment is the largest part of the AA business. The AA provides a nationwide service, sending patrols out to members stranded at the side of the road, repairing their vehicles where possible and getting them back on their way quickly and safely.
- *Insurance Services*: This segment includes the insurance brokerage activities of the AA, primarily in arranging motor and home insurance for customers, its home services activities and its intermediary financial services business.
- *Driving Services*: This segment contains the AA Driving School and the British School of Motoring, which are the two largest driving schools in the UK, as well as AA DriveTech, which provides driver training and educative programmes.
- *Ireland*: This segment competes in the same segment types as the AA UK business, with the largest part of its business being Insurance Services and Roadside Assistance.
- *Head Office costs*: This segment includes IT, finance, property and other back office support functions.

Segment performance is primarily evaluated using the Group's key performance measure of Trading EBITDA. Trading EBITDA is profit after tax as reported adjusted for depreciation, amortisation, net finance costs, taxation, exceptional items and items not allocated to a segment and better reflects the Group's underlying performance.

Items not allocated to a segment relate to transactions that do not form part of the on-going segment performance and include transactions which are one-off in nature. In the year ended 31 January 2016 these principally relate to the difference between the cash contributions to the pension schemes for on-going service and the calculated annual service cost and share based payments (see note 31).

Depreciation, amortisation, exceptional items, net finance costs and tax expense are not allocated to individual segments as they are managed on a group basis.

Segmental information is not presented for items in the Statement of Financial Position as management do not view this information on a segmental basis.

### 3 Operating profit

Operating profit is stated after charging:

	2016 £m	2015 £m
Amortisation of owned intangible assets	23	20
Depreciation of owned tangible fixed assets	11	9
Depreciation of leased tangible fixed assets	20	19
Operating lease rentals payable – land and buildings	5	4
Operating lease rentals payable – plant and machinery	-	6
Exceptional items	36	34

Exceptional costs include £5m for the loss on disposal of Autowindshields (UK) Limited (2015: £nil), £1m gain on disposal of AA Technical Solutions Limited (2015: £nil), £3m relating to financing transactions (2015: £1m), £22m relating to business transformation costs (2015: £nil) and £7m mainly relating to non-recurring costs for IT system implementation, onerous property lease costs, loss on disposal of fixed assets and cost restructuring activities (2015: £13m). In addition, in the prior year, £20m related to costs in connection with the AA plc IPO.

### 4 Finance costs

	2016 £m	2015 £m
Interest on external borrowings	(175)	(180)
Finance charges payable under finance leases	(7)	(4)
Penalties on early repayment of debt	(58)	-
<b>Total cash finance costs</b>	<b>(240)</b>	<b>(184)</b>
Amortisation of debt issue fees	(20)	(26)
Transfer from cashflow hedge reserve for extinguishment of cashflow hedge	(8)	(7)
Net finance expense on defined benefit pension schemes	(12)	(11)
<b>Total non-cash finance costs</b>	<b>(40)</b>	<b>(44)</b>
<b>Total finance costs</b>	<b>(280)</b>	<b>(228)</b>

During the year, the Group repaid the original Class B notes of £655m (see note 18). As a result, the Group incurred early repayment penalties of £58m (2015: £nil).

The Group also repaid £209m of the Senior Term Facility, following which, the Group has transferred the fair value of the cashflow hedges related to the repayment of £8m (2015: £7m) from other comprehensive income to the income statement.

Within interest on external borrowings is £13m (2015: £21m) of interest charged on the Senior Term Facility and £8m (2015: £10m) charged in relation to the interest rate swaps used to hedge the variable element of the Senior Term Facility (see note 18).

Also included within interest on external borrowings is £19m (2015: £nil) of interest costs relating to the double-running of the Class B/B2 notes from the time of issue of the Class B2 notes in April 2015 until the repayment of the Class B notes in July 2015.

Amortisation of debt issue fees includes £16m (2015: £19m) that was immediately written off following the repayment of borrowings.

**5 Finance income**

	2016 £m	2015 £m
Interest receivable	1	1
<b>Total finance income</b>	<b>1</b>	<b>1</b>

**6 Staff costs**

	2016 £m	2015 £m
Wages and salaries	269	258
Social security costs	24	25
Retirement benefit costs	34	28
	<b>327</b>	<b>311</b>

The average monthly number of persons employed under contracts of service during the year was:

	2016	2015
Operational	6,620	6,876
Management and administration	1,240	1,277
	<b>7,860</b>	<b>8,153</b>

**7 Directors' remuneration**

	2016 £m	2015 £m
Directors' remuneration	3	3
Long-term incentive plans	2	1
Aggregate remuneration in respect of qualifying services	5	4
Compensation for loss of office	-	1
Members of defined benefit pension schemes	2	2
The amounts paid in respect of the highest paid director were as follows:		
Remuneration	3	2

The accrued pension of the highest paid director was £nil at 31 January 2016 (2015: £nil). The highest paid director had contributions to a money purchase pension plan of £88,000 (2015: £52,000).

## 8 Tax

The major components of the income tax expense are:

	2016 £m	2015 £m
<b>Consolidated income statement</b>		
<b>Current income tax</b>		
Current income tax charge	12	10
Adjustments in respect of previous years	-	-
	<b>12</b>	<b>10</b>
<b>Deferred tax</b>		
Effect of tax rate change on opening balances	7	-
Relating to origination and reversal of temporary differences – current year	(6)	(9)
Relating to origination and reversal of temporary differences – prior years	-	(1)
	<b>1</b>	<b>(10)</b>
<b>Tax expense in the income statement</b>	<b>13</b>	<b>-</b>

	2016 £m	2015 £m
<b>Consolidated statement of comprehensive income</b>		
Tax on the effective portion of changes in fair value of cash flow hedges	2	(3)
Tax on remeasurements of defined benefit pension liability	26	(32)
<b>Income tax charged / (credited) directly to other comprehensive income</b>	<b>28</b>	<b>(35)</b>

Reconciliation of tax expense to profit before tax multiplied by UK's corporation tax rate:

	2016 £m	2015 £m
Profit before tax	30	114
Tax at rate of 20.16% (2015: 21.3%)	6	24
Movement on unprovided deferred tax	-	(22)
Lower rate of foreign tax	(1)	(1)
Rate change adjustment on temporary differences	7	(1)
Expenses not deductible for tax purposes:		
- Other non-deductible expenses / non-taxed income	1	-
<b>Income tax expense reported in the consolidated income statement</b>	<b>13</b>	<b>-</b>

## 8 Tax (continued)

Deferred tax by type of temporary difference

	Consolidated statement of financial position		Consolidated income statement	
	2016 £m	2015 £m	2016 £m	2015 £m
Accelerated depreciation for tax purposes	9	13	4	(2)
Revaluations of land and buildings to fair value	(1)	(1)	-	-
Rollover relief	(2)	(2)	-	-
Pension	15	42	1	(1)
Revaluation of cashflow hedges	5	6	(1)	(1)
Short-term temporary differences	9	1	(8)	1
Losses available for offsetting against future taxable income	17	22	5	(7)
<b>Deferred tax expense / (income)</b>			<b>1</b>	<b>(10)</b>
<b>Net deferred tax assets</b>	<b>52</b>	<b>81</b>		

Reconciliation of net deferred tax assets

	2016 £m	2015 £m
<b>At 1 February</b>	<b>81</b>	<b>36</b>
Tax (expense) / income recognised in the income statement	(1)	10
Tax income recognised in OCI	(28)	35
<b>At 31 January</b>	<b>52</b>	<b>81</b>

The Group offsets tax assets and liabilities if and only if it has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same tax authority.

The UK corporation tax rate will reduce from 20% to 19% on 1 April 2017 and then to 18% on 1 April 2020. These rates have been substantially enacted at the balance sheet date and have therefore been included in the deferred tax calculations.

Deferred tax has been recognised at an overall rate of 18.4% for the UK at 31 January 2016 (2015: 20%) and 12.5% for Ireland (2015: 12.5%). The UK rate has been adjusted to reflect the expected reversal profile of the group's temporary differences.

The Group has tax losses which arose in the UK of £92m (2015: £110m) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose. In the prior year, following the IPO, a deferred tax asset of £22m was recognised on these tax losses as the Group expected to have sufficient taxable profits to be able to recover these losses.

**9 Goodwill and other intangible assets**

	Goodwill £m	Software £m	Total £m
<b>Cost</b>			
At 1 February 2014	1,198	100	1,298
Additions	-	31	31
Disposals	-	(2)	(2)
<b>At 31 January 2015</b>	<b>1,198</b>	<b>129</b>	<b>1,327</b>
Additions	-	62	62
Disposals	-	(7)	(7)
<b>At 31 January 2016</b>	<b>1,198</b>	<b>184</b>	<b>1,382</b>
<b>Amortisation and impairment</b>			
At 1 February 2014	-	52	52
Amortisation	-	20	20
Disposals	-	(1)	(1)
<b>At 31 January 2015</b>	<b>-</b>	<b>71</b>	<b>71</b>
Amortisation	-	23	23
Disposals	-	(2)	(2)
<b>At 31 January 2016</b>	<b>-</b>	<b>92</b>	<b>92</b>
<b>Net book value</b>			
<b>At 31 January 2016</b>	<b>1,198</b>	<b>92</b>	<b>1,290</b>
At 31 January 2015	1,198	58	1,256

Within software, £51m (2015: £10m) relates to assets under construction which are not amortised.

Software additions comprise £13m (2015: £14m) in relation to internally developed assets and £49m (2015: £17m) in relation to separately acquired assets.

**10 Property, plant and equipment**

	Freehold Land & Buildings £m	Long Leasehold Land & Buildings £m	Vehicles £m	Plant & equipment £m	Total £m
<b>Cost</b>					
At 1 February 2014	24	10	66	104	204
Additions	-	-	62	5	67
Disposals	-	-	(36)	(1)	(37)
Exchange adjustments	-	-	-	(1)	(1)
<b>At 31 January 2015</b>	<b>24</b>	<b>10</b>	<b>92</b>	<b>107</b>	<b>233</b>
Additions	-	-	47	21	68
Disposals	-	-	(50)	(3)	(53)
<b>At 31 January 2016</b>	<b>24</b>	<b>10</b>	<b>89</b>	<b>125</b>	<b>248</b>
<b>Depreciation and impairment</b>					
At 1 February 2014	5	3	41	78	127
Charge for the year	1	1	16	10	28
Disposals	-	-	(20)	(1)	(21)
Exchange adjustments	-	-	-	(1)	(1)
<b>At 31 January 2015</b>	<b>6</b>	<b>4</b>	<b>37</b>	<b>86</b>	<b>133</b>
Charge for the year	1	-	21	9	31
Disposals	-	-	(36)	(2)	(38)
<b>At 31 January 2016</b>	<b>7</b>	<b>4</b>	<b>22</b>	<b>93</b>	<b>126</b>
<b>Net book value</b>					
<b>At 31 January 2016</b>	<b>17</b>	<b>6</b>	<b>67</b>	<b>32</b>	<b>122</b>
At 31 January 2015	18	6	55	21	100

The net book amount of vehicles includes £65m (2015: £54m) held under finance lease agreements. The accumulated depreciation on these assets is £19m (2015: £35m).

The net book amount of other assets includes £nil (2015: £nil) in respect of plant & machinery held under finance lease agreements. The accumulated depreciation on these assets is £8m (2015: £8m).

**11 Investments in joint ventures and associates**

	2016			2015		
	Joint ventures £m	Associates £m	Total £m	Joint ventures £m	Associates £m	Total £m
At 1 February	1	3	4	-	3	3
Additions	1	-	1	-	-	-
Share of profits	-	1	1	1	-	1
<b>At 31 January</b>	<b>2</b>	<b>4</b>	<b>6</b>	<b>1</b>	<b>3</b>	<b>4</b>

The joint ventures of the Group which are indirectly held are detailed below.

Company	Country of registration	Nature of business
AA Law Limited (49% interest held) <sup>1</sup>	England	Insurance services
Motoriety UK Limited (50% interest held)	England	Roadside services

<sup>1</sup> The Group exercises joint control over AA Law Limited through its equal representation on the Board.

The associates of the Group which are indirectly held are listed below.

Company	Country of registration	Nature of business
ARC Europe S.A. (20% interest held)	Belgium	Roadside services
A.C.T.A. Assistance S.A. (22% interest held)	France	Roadside services

**12 Inventories**

	2016 £m	2015 £m
Finished goods	5	5
	<b>5</b>	<b>5</b>

**13 Trade and other receivables**

	2016 £m	2015 £m
<b>Current</b>		
Trade receivables	144	155
Prepayments and accrued income	22	25
Other receivables	4	5
	170	185
<b>Non-current</b>		
Interest rate swap derivatives (see note 24)	-	21
	-	21

Included in trade receivables are amounts of £89m (2015: £89m) relating to amounts due from insurance broking customers.

**14 Cash and cash equivalents**

	2016 £m	2015 £m
Cash at bank and in hand – available	74	244
Cash at bank and in hand – restricted	20	18
	94	262

Cash at bank and in hand, short term deposits include £20m (2015: £18m) held by and on behalf of the Group's insurance businesses which are subject to contractual or regulatory restrictions. These amounts are not readily available to be used for other purposes within the Group.

**15 Amounts owed by/to parent undertaking**

Amounts owed by/to parent undertaking are unsecured, have no repayment terms and bear no interest.

## 16 Trade and other payables

	2016 £m	2015 £m
Trade payables	110	115
Other taxes and social security costs	23	26
Accruals	65	65
Deferred income	248	238
Other payables	31	16
Obligations under finance lease agreements (note 26)	40	35
	<b>517</b>	495

Included in trade payables are amounts of £86m (2015: £85m) relating to amounts due to underwriters in respect of insurance broking activities.

## 17 Borrowings and loans

	2016 £m	2015 £m
Borrowings (see note 18)	2,893	3,018
Interest rate swap used for hedging (see note 24)	27	50
	<b>2,920</b>	3,068

## 18 Borrowings

	Expected maturity date	Interest rate	Principal £m	Issue costs £m	Amortised issue costs £m	Total at 31 January 2016 £m	Total at 31 January 2015 £m
Senior Term Facility	31 January 2019	4.36%	454	(3)	1	452	661
Class A1 notes	31 July 2018	4.72%	475	(3)	2	474	473
Class A2 notes	31 July 2025	6.27%	500	(1)	-	499	499
Class A3 notes	31 July 2020	4.25%	500	(3)	1	498	498
Class A4 notes	31 July 2019	3.78%	250	(2)	1	249	248
Class B notes	31 July 2019	-	-	-	-	-	639
Class B2 notes	31 July 2022	5.50%	735	(16)	2	721	-
		<b>4.97%</b>	<b>2,914</b>	<b>(28)</b>	<b>7</b>	<b>2,893</b>	3,018

**18 Borrowings (continued)**

A summary of the Group's financing transactions are shown below:

	Senior term facility £m	Class A1 £m	Class A2 £m	Class A3 £m	Class A4 £m	Class B £m	Class B2 £m	Total £m
As at 1 February 2015	663	475	500	500	250	655	-	<b>3,043</b>
Issue date:								
25 March 2015	(97)	-	-	-	-	-	-	<b>(97)</b>
13 April 2015	-	-	-	-	-	-	735	<b>735</b>
30 April 2015	(112)	-	-	-	-	-	-	<b>(112)</b>
31 July 2015	-	-	-	-	-	(655)	-	<b>(655)</b>
<b>Total</b>	<b>454</b>	<b>475</b>	<b>500</b>	<b>500</b>	<b>250</b>	<b>-</b>	<b>735</b>	<b>2,914</b>

At 31 January 2016, the Senior Term Facility carried interest at a rate of LIBOR plus a margin of 2%. The variable element has been fully hedged using matching interest rate swap arrangements which fix LIBOR at 2.36% until 31 July 2018 and then at 3.00% until 31 January 2019. All other borrowings have fixed interest rates. The weighted average interest rate for all borrowings of 4.97% has been calculated using the effective interest rate and carrying values on 31 January 2016.

In order to show the Group's net borrowing, the notes and the issue costs have been offset. Issue costs are shown net of any premium on the issue of borrowings. Interest rate swaps are recognised in the Balance Sheet at fair value at the period end.

All of the Class A notes and Senior Term Facility are secured by first ranking security in respect of the undertakings and assets of AA Intermediate Co Limited and its subsidiaries. The Class A facility security over the AA Intermediate Co Limited group's assets ranks ahead of the Class B2 notes. The Class B2 notes have first ranking security over the assets of the immediate parent undertaking of the AA Intermediate Co Limited group, AA Mid Co Limited. AA Mid Co Limited group can only pay a dividend when certain net debt to EBITDA and cashflow criteria are met.

The Class B2 notes have an initial period to 31 July 2018 when any voluntary repayment would incur a make-whole payment and incur all remaining interest due to 31 July 2018. After this period, there is a further two year period when any voluntary repayment would be made at a fixed premium based on the date of redemption. Any voluntary early repayments of the Class A notes would incur a make-whole payment.

Due to the early repayment of the Class B notes, early repayment fees of £58m were incurred in the year.

Following the repayment of £209m of the Senior Term Facility and repayment of the Class B notes, amortisation of the associated issue fees has been accelerated and an additional £16m (2015: £19m) has been written off in the year.

In order to comply with the requirements of the Class A notes, we are required to maintain the Class A free cash flow to debt service ratio in excess of 1.35x and the senior leverage ratio below 5.5x. The Class B2 notes require us to maintain the Class B2 free cash flow to debt service ratio in excess of 1x.

The Class A and Class B2 notes therefore place restrictions on the Group's ability to upstream cash from the key trading companies to pay external dividends and finance activities unconstrained by the restrictions embedded in the debt documents.

The Class A notes only permit the release of cash providing the senior leverage ratio after payment is less than 5.5x and providing there is sufficient excess cash flow to cover the payment. The Class B2 note restrictions came into effect during the 2016 financial year refinancing and only permit the release of cash providing the fixed charge cover ratio after payment is more than 2:1 and providing that the aggregate payments do not exceed 50% of the accumulated consolidated net income.

## 19 Provisions

	Property Leases £m	Restructuring £m	Other £m	Total £m
At 1 February 2014	25	2	1	28
Utilised during the year	(4)	(1)	(1)	(6)
Released unutilised during the year	(4)	-	-	(4)
Charge for the year	1	-	1	2
<b>At 31 January 2015</b>	<b>18</b>	<b>1</b>	<b>1</b>	<b>20</b>
Utilised during the year	(4)	-	(1)	(5)
Released unutilised during the year	(2)	-	-	(2)
Charge for the year	1	-	1	2
<b>At 31 January 2016</b>	<b>13</b>	<b>1</b>	<b>1</b>	<b>15</b>
Current	6	1	1	8
Non-current	7	-	-	7
<b>At 31 January 2016</b>	<b>13</b>	<b>1</b>	<b>1</b>	<b>15</b>
Current	6	1	1	8
Non-current	12	-	-	12
<b>At 31 January 2015</b>	<b>18</b>	<b>1</b>	<b>1</b>	<b>20</b>

The property lease provision relates to future onerous lease costs of vacant properties for the remaining period of the lease, net of expected sub-letting income. These sums are mainly expected to be paid out over the next 7 years however it will take 38 years to fully pay out all amounts provided for. The provision has been calculated on a pre-tax discounted basis.

The restructuring provision relates to redundancy and other related costs following the restructuring of operations in the current and prior periods.

Other provisions primarily comprise a provision for an onerous contract of £1m (2015: £1m). These items are reviewed and updated annually.

## 20 Share capital

	2016 £m	2015 £m
<b>Allotted, called up and fully paid</b>		
20,000,002 ordinary shares of £1 each	<b>20</b>	20
	<b>20</b>	20

The voting rights of the holders of all ordinary shares are the same and all ordinary shares rank pari passu on a winding up.

The Company has 20,000,100 authorised shares of £1 each.

**21 Reserves**

	Currency translation reserve £m	Cashflow hedge reserve £m	Retained earnings £m	Total £m
At 1 February 2014	(1)	(7)	(898)	(906)
Retained profit for the year	-	-	114	114
<b>Other comprehensive income:</b>				
Exchange differences on translation of foreign operations	(1)	-	-	(1)
Remeasurement losses on defined benefit schemes (note 22)	-	-	(167)	(167)
Tax effect of remeasurement losses on defined benefit schemes (note 8)	-	-	32	32
Effective portion of changes in fair value of cash flow hedges	-	(14)	-	(14)
Tax effect of effective portion of changes in fair value of cash flow hedges	-	3	-	3
Share-based payments (note 31)	-	-	2	2
<b>At 31 January 2015</b>	<b>(2)</b>	<b>(18)</b>	<b>(917)</b>	<b>(937)</b>
Retained profit for the year	-	-	17	17
<b>Other comprehensive income:</b>				
Exchange differences on translation of foreign operations	1	-	-	1
Remeasurement losses on defined benefit schemes (note 22)	-	-	149	149
Tax effect of remeasurement losses on defined benefit schemes (note 8)	-	-	(26)	(26)
Effective portion of changes in fair value of cash flow hedges	-	10	-	10
Tax effect of effective portion of changes in fair value of cash flow hedges	-	(2)	-	(2)
Share-based payments (note 31)	-	-	5	5
Dividends paid	-	-	(60)	(60)
<b>At 31 January 2016</b>	<b>(1)</b>	<b>(10)</b>	<b>(832)</b>	<b>(843)</b>

*Currency translation reserve*

The translation reserve comprises foreign exchange differences arising from the translation of the financial statements of foreign operations, as well as from the translation of liabilities that hedge the Group's net investment in a foreign subsidiary.

*Cashflow hedge reserve*

The cashflow hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

*Dividends*

In the year ended 31 January 2016, total dividends of £3 per qualifying ordinary share were paid. Dividends are paid from the unconsolidated distributable reserves of AA Intermediate Co Limited 'the Company'. As at 31 January 2016, the Company had distributable reserves of £77k (2015: £85k). The dividend paid during the current year was paid following receipt of a dividend of £60m from a subsidiary undertaking, AA Acquisition Co Limited.

## 22 Pensions

The Group operates two funded defined benefit pension schemes: the AA UK Pension Scheme (AAUK) and the AA Ireland Pension Scheme (AAI). The assets of the schemes are held separately from those of the Group in independently administered funds. New entrants to the AAUK scheme accrue benefits on a career average salary basis. The AAUK scheme has final salary sections that are closed to new entrants but open to future accrual for existing members. The AAI scheme is closed to new entrants and future accrual of benefits. The Group also operates an unfunded post-retirement Private Medical Plan scheme (AAPMP), which is a defined benefit scheme that is not open to new entrants.

On 29 November 2013, the Group completed the AAUK pension scheme triennial valuations agreeing a deficit of £202m with the pension trustees and implementing an asset backed funding scheme. The asset backed funding scheme provides a long-term deficit reduction plan where the Group makes an annual deficit reduction contribution of £12.5m increasing with inflation, over a period of up to 25 years from 29 November 2013 secured on the Group's brands.

The valuations have been based on a full assessment of the liabilities of the schemes which have been updated where appropriate to 31 January 2016 by independent qualified actuaries.

The Group expects to pay £25m in on-going employer contributions and £13m in deficit reduction employer contributions to its defined benefit plans (AAUK and AAI) in the year ending 31 January 2017.

### The amounts recognised in the balance sheet are as follows:

	As at 31 January 2016			
	AAUK £m	AAI £m	AAPMP £m	Total £m
Present value of the defined benefit obligation in respect of pension plans	(2,053)	(46)	(47)	(2,146)
Fair value of plan assets	1,815	35	-	1,850
<b>Deficit</b>	<b>(238)</b>	<b>(11)</b>	<b>(47)</b>	<b>(296)</b>

  

	As at 31 January 2015			
	AAUK £m	AAI £m	AAPMP £m	Total £m
Present value of the defined benefit obligation in respect of pension plans	(2,178)	(51)	(49)	(2,278)
Fair value of plan assets	1,809	35	-	1,844
<b>Deficit</b>	<b>(369)</b>	<b>(16)</b>	<b>(49)</b>	<b>(434)</b>

The decrease in the deficit is mainly due to changes in financial assumptions, mostly from a rise in the discount rates in all of the schemes. This has been partially offset by a loss on assets.

22 Pensions (*continued*)

	Assets £m	Liabilities £m	Income statement £m	Statement of comprehensive income £m
Balance at 1 February 2015	<b>1,844</b>	<b>(2,278)</b>	-	-
Current service cost	-	(34)	(34)	-
Past service cost	-	(2)	(2)	-
Interest on defined benefit scheme assets / (liabilities)	56	(68)	(12)	-
<b>Amounts recognised in the income statement</b>	<b>56</b>	<b>(104)</b>	<b>(48)</b>	-
Effect of changes in financial assumptions	-	185	-	185
Effect of experience adjustment	-	1	-	1
Return on plan assets excluding interest income	(37)	-	-	(37)
<b>Amounts recognised in the statement of comprehensive income</b>	<b>(37)</b>	<b>186</b>	-	<b>149</b>
<b>Foreign exchange loss</b>	-	<b>(1)</b>	-	<b>(1)</b>
Contribution from scheme participants	1	(1)	-	-
Benefits paid from scheme assets	(52)	52	-	-
Ongoing employer contributions	24	-	-	-
Deficit reduction employer contributions	14	-	-	-
<b>Movements through cash</b>	<b>(13)</b>	<b>51</b>	-	-
<b>Balance at 31 January 2016</b>	<b>1,850</b>	<b>(2,146)</b>	-	-

A redundancy exercise was carried out during the 2016 financial year which affected 28 members of the AAUK Scheme. Under the terms of the AAUK Scheme the members were entitled to enhanced pension benefits upon redundancy and the impact of this was a past service cost of £2m (2015: £nil) in relation to the AAUK scheme.

22 Pensions (*continued*)

	Assets £m	Liabilities £m	Income statement £m	Statement of comprehensive income £m
Balance at 1 February 2014	<b>1,580</b>	<b>(1,846)</b>	-	-
Current service cost	-	(27)	(27)	-
Interest on defined benefit scheme assets / (liabilities)	68	(79)	(11)	-
<b>Amounts recognised in the income statement</b>	<b>68</b>	<b>(106)</b>	<b>(38)</b>	-
Effect of changes in financial assumptions	-	(373)	-	(373)
Effect of experience adjustment	-	(3)	-	(3)
Return on plan assets excluding interest income	209	-	-	209
<b>Amounts recognised in the statement of comprehensive income</b>	<b>209</b>	<b>(376)</b>	-	<b>(167)</b>
<b>Foreign exchange (loss) / gain</b>	<b>(3)</b>	<b>5</b>	-	<b>2</b>
Contribution from scheme participants	1	(1)	-	-
Benefits paid from scheme assets	(46)	46	-	-
Ongoing employer contributions	21	-	-	-
Deficit reduction employer contributions	14	-	-	-
<b>Movements through cash</b>	<b>(10)</b>	<b>45</b>	-	-
<b>Balance at 31 January 2015</b>	<b>1,844</b>	<b>(2,278)</b>	-	-

## 22 Pensions (continued)

### Fair value of plan assets

The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the plan's investment portfolio.

The table below shows the AAUK plan assets split between those that have a quoted market price and those that are unquoted. Of the AAI scheme, 26.6% (2015: 22.0%) of assets do not have a quoted market price.

The fair value of the AAUK plan assets and the return on those assets were as follows:

	2016		2015	
	Assets with a quoted market price £m	Assets without a quoted market price £m	Assets with a quoted market price £m	Assets without a quoted market price £m
Equities	136	264	237	206
Bonds	667	122	731	113
Property	79	172	67	132
Hedge funds	-	356	-	305
Cash / net current assets	17	1	15	3
<b>Total plan assets</b>	<b>899</b>	<b>915</b>	<b>1,050</b>	<b>759</b>
<b>Actual return on AAUK plan assets</b>	<b>18</b>		<b>272</b>	

### Pension plan assumptions

The principal actuarial assumptions were as follows:

	AAUK		AAI		AAPMP	
	2016 %	2015 %	2016 %	2015 %	2016 %	2015 %
Pensioner discount rate	<b>3.6</b>	2.9	<b>1.7</b>	1.2	<b>3.6</b>	2.9
Non pensioner discount rate	<b>3.8</b>	3.2	<b>2.6</b>	2.0	<b>3.8</b>	3.2
Pensioner RPI	<b>2.9</b>	2.6	-	-	<b>2.9</b>	2.6
Non pensioner RPI	<b>3.2</b>	2.9	-	-	<b>3.2</b>	2.9
Rate of increase of pensions in payment - pensioner	<b>2.8</b>	2.5	-	-	-	-
Rate of increase of pensions in payment - non pensioner	<b>3.0</b>	2.7	-	-	-	-
Pensioner increase for deferred benefits	<b>2.2</b>	1.9	<b>1.5</b>	1.5	-	-
Medical premium inflation rate	-	-	-	-	<b>6.9</b>	6.6

Mortality assumptions are set using standard tables based on scheme specific experience where available. Each scheme's mortality assumptions are based on standard mortality tables which allow for future mortality improvements. The AA schemes' assumptions are that an active male retiring in normal health currently aged 60 will live on average for a further 28 years and an active female retiring in normal health currently aged 60 will live on average for a further 30 years.

## 22 Pensions (*continued*)

### Sensitivity analysis

The Scheme exposes the Group to risks such as longevity, interest rate risk and market (investment) risk. The AA Pension Scheme Trustees have hedged around 50% of interest rate risk and 74% of inflation risk as part of a policy to reduce financial risks to the Scheme.

Reasonably possible changes at the reporting date to one of the relevant actuarial assumptions, holding other assumptions constant, would have affected the defined benefit liability by the amounts shown below:

	For the year ending 31 January 2016		
	AAUK £m	AAI £m	AAPMP £m
Increase of 0.25% in discount rate	108	2	2
Increase of 0.25% in Inflation rate	(97)	(1)	-
Increase of 1% in medical claims inflation	-	-	(7)
Increase of one year of life expectancy	(59)	(1)	-

An equivalent decrease in the assumptions at 31 January 2016 would have had the equal but opposite effect on the amounts shown above, on the basis that all other variables remain constant.

The weighted average duration of plan liabilities at 31 January 2016 is 22 years.

## 23 Impairment of intangible assets

Goodwill acquired through business combinations has been allocated to cash-generating units (“CGUs”) on initial recognition and for subsequent impairment testing.

The carrying value of goodwill by CGU is as follows:

	2016 £m	2015 £m
Roadside Assistance	<b>874</b>	874
Insurance Services	<b>240</b>	240
Driving Schools	<b>26</b>	26
DriveTech	<b>32</b>	32
Ireland	<b>26</b>	26
	<b>1,198</b>	1,198

The Group has performed impairment testing at 31 January 2016 and 31 January 2015. The impairment test compares the recoverable amount of the CGU to its carrying value.

The recoverable amount of each CGU has been determined based on a value in use calculation using cash flow projections from the Group’s three year plan up to 31 January 2019 and a reasonable expectation of growth in the subsequent two years. For the purposes of the impairment test terminal values have been calculated using the Gordon growth model and a nil growth assumption which is lower than the expected long term average growth rate of the UK economy. Cash flows have been discounted at a pre-tax rate reflecting the time value of money and the risk specific to these cash flows. This has been determined as a pre-tax rate of 9.9% (2015: 12.2%).

The value in use calculation used is most sensitive to the assumptions used for growth and for the discount rate. Accordingly, stress testing has been performed on these key assumptions as part of the impairment test to further inform the consideration of whether any impairment is evident. Further to this, management believes that no reasonably foreseeable change in any of the key assumptions would cause the recoverable amount of the CGU to be lower than its carrying amount, and consequently no impairment has been recognised.

## 24 Financial assets and financial liabilities

The carrying amount of all financial assets and financial liabilities by class are as follows:

### Financial assets

	2016 £m	2015 £m
<b>Measured at fair value through other comprehensive income</b>		
Interest rate swaps used for hedging	-	21
<b>Loans and receivables</b>		
Cash and cash equivalents	94	262
Trade receivables	144	155
Other receivables and accrued income	16	18
Amounts owed by parent undertaking	1,214	1,205
<b>Total financial assets</b>	<b>1,468</b>	<b>1,661</b>

### Financial liabilities

	2016 £m	2015 £m
<b>Measured at fair value through other comprehensive income</b>		
Interest rate swaps used for hedging	27	50
<b>Loans and borrowings</b>		
Trade payables	110	115
Other payables	63	59
Obligations under finance lease agreements	61	51
Borrowings	2,893	3,018
Amounts owed to parent undertaking	-	4
<b>Total financial liabilities</b>	<b>3,154</b>	<b>3,297</b>

## 24 Financial assets and financial liabilities (continued)

### Fair values

Financial instruments held at fair value are valued using quoted market prices or other valuation techniques.

Valuation techniques include net present value and discounted cash flow models, and comparison to similar instruments for which market observable prices exist. Assumptions and market observable inputs used in valuation techniques include interest rates.

The objective of using valuation techniques is to arrive at a fair value that reflects the price of the financial instrument at each year end at which the asset or liability would have been exchanged by market participants acting at arm's length.

Observable inputs are those that have been seen either from counterparties or from market pricing sources and are publicly available. The use of these depends upon the liquidity of the relevant market. When measuring the fair value of an asset or a liability, the Group uses observable inputs as much as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation as follows:

**Level 1** - Quoted market prices in an actively traded market for identical assets or liabilities. These are the most reliable.

**Level 2** - Inputs other than quoted prices included in Level 1 that are observable for the assets or liabilities. These include valuation models used to calculate the present value of expected future cash flows and may be employed either when no active market exists or when there are quoted prices available for similar instruments in active markets. The models incorporate various inputs including interest rate curves and forward rate curves of the underlying instrument.

**Level 3** - Inputs for assets or liabilities that are not based on observable market data.

If the inputs used to measure the fair values of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level as the lowest input that is significant to the entire measurements.

The fair values are periodically reviewed by the Group Treasury function. The following tables provide the quantitative fair value hierarchy of the Group's interest rate swaps and loan notes.

The carrying values of all other financial assets and liabilities (including the Senior Term Facility) are approximate to their fair values:

#### At 31 January 2016:

	Carrying value £m	Fair value measurement using		
		Quoted prices in active markets (Level 1) £m	Significant observable inputs (Level 2) £m	Significant unobservable inputs (Level 3) £m
<b>Financial liabilities measured at fair value</b>				
Interest rate and fuel swaps (note 17)	27	-	27	-
<b>Liabilities for which fair values are disclosed</b>				
Loan notes (note 18)	2,441	2,528	-	-

**24 Financial assets and financial liabilities (continued)**

At 31 January 2015:

	Carrying value £m	Fair value measurement using		
		Quoted prices in active markets (Level 1) £m	Significant observable inputs (Level 2) £m	Significant unobservable inputs (Level 3) £m
<b>Financial assets measured at fair value</b>				
Interest rate swaps (note 13)	21	-	21	-
<b>Financial liabilities measured at fair value</b>				
Interest rate swaps (note 17)	50	-	50	-
<b>Liabilities for which fair values are disclosed</b>				
Loan notes (note 18)	2,357	2,680	-	-

There have been no transfers between the levels and no non-recurring fair value measurements of assets and liabilities during the two years to 31 January 2016.

**25 Financial risk management objectives and policies**

The Group's principal financial liabilities comprise borrowings as well as trade and other payables. The main purpose of these financial liabilities is to finance the Group's operations. The Group's principal financial assets include deposits with financial institutions, money market funds and trade receivables.

The Group is exposed to market risk, credit risk and liquidity risk. The Group's senior management oversees the management of these risks, supported by the Group Treasury function. The Group Treasury function ensures that the Group's financial risks are governed by appropriate policies and procedures and that financial risks are identified, measured and managed in accordance with the Group's policies and risk objectives. All derivative activities are for risk management purposes and are carried out by the Group Treasury function. It is the Group's policy not to trade in derivatives for speculative purposes.

The Board of Directors reviews and agrees policies for managing each of these risks, which are summarised below.

**Market risk**

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in prices set by the market. The key market risk that the Group is exposed to is interest rate risk. The Group has policies and limits approved by the Board for managing the interest rate risk exposure. The Group's policy is to fully hedge all of its exposure to variable interest rates. The Group has therefore taken out interest rate swaps to the value of its variable rate instruments.

## 25 Financial risk management objectives and policies *(continued)*

The interest rate profile of the Group's interest-bearing financial instruments is as follows:

	2016 £m	2015 £m
<b>Fixed rate instruments</b>		
Financial liabilities	(2,502)	(2,408)
Effect of interest rate swaps	(454)	(663)
<b>Net exposure to fixed rate instruments</b>	<b>(2,956)</b>	<b>(3,071)</b>
<b>Variable rate instruments</b>		
Financial liabilities	(452)	(661)
Effect of interest rate swaps	454	663
<b>Net exposure to variable rate instruments</b>	<b>2</b>	<b>2</b>

### Sensitivity of fixed-rate instruments

The Group does not account for any fixed-rate financial assets and financial liabilities at fair value through profit or loss and does not use derivative instruments in fair value hedges. Consequently, having regard to fixed rate instruments, a change in market interest rates at the reporting date would not affect profit or loss.

### Sensitivity of variable rate instruments

An increase of 50 basis points in interest rates at 31 January 2016 would have increased equity by £4m (2015: £9m) and had no impact on profit or cash. A decrease to interest rates of the same magnitude will have an equal and opposite effect on equity and profit. This calculation assumes that the change occurred at the year end and had been applied to risk exposures existing at that date.

This analysis assumes that all other variables remain constant and considers the effect of financial instruments with variable interest rates and the fixed rate element of interest rate swaps. The analysis is performed on the same basis for all comparative periods.

### Credit risk

Credit risk is the risk that a counterparty will not meet its obligations under a financial instrument or customer contract, leading to a financial loss. The Group is exposed to credit risk in relation to its financial assets, outstanding derivatives and trade and other receivables. The Group assesses its counterparty exposure in relation to the investment of surplus cash and undrawn credit facilities. The Group primarily uses published credit ratings to assess counterparty strength and therefore to define the credit limit for each counterparty, in accordance with approved treasury policies.

The credit risk for the Group is limited as payment from customers is generally required before services are provided.

Credit risk in relation to deposits and derivative counterparties is managed by the Group's treasury function in accordance with the Group's policy. Investments of surplus funds are made only with approved counterparties and within credit limits assigned to each counterparty. The limits are set to mitigate financial loss through any potential counterparty failure.

The Group's maximum exposure to credit risk for the components of the statement of financial position at each reporting date is the carrying amount except for derivative financial instruments. The Group's maximum exposure for financial derivative instruments is noted under liquidity risk.

**25 Financial risk management objectives and policies (continued)**

The ageing analysis of trade receivables is as follows:

	Total £m	Neither past due nor impaired £m	Past due but not impaired		
			< 30 days £m	30 - 60 days £m	60+ days £m
<b>2016</b>	<b>144</b>	<b>135</b>	<b>2</b>	<b>2</b>	<b>5</b>
2015	155	143	5	2	5

The movements in the provision for the collective impairment of receivables are as follows:

	2016 £m	2015 £m
At 1 February	2	4
Charge for the year	1	1
Utilised	-	(2)
Unused amounts reversed	(1)	(1)
<b>At 31 January</b>	<b>2</b>	<b>2</b>

**Liquidity risk**

Liquidity risk is the risk that the Group either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure them only at excessive cost. The Group's approach to managing liquidity risk is to evaluate current and expected liquidity requirements to ensure that it maintains sufficient reserves of cash and headroom on its working capital facilities.

The table below analyses the maturity of the Group's financial liabilities on a contractual undiscounted cash flow basis and includes any associated debt service costs. The analysis of non-derivative financial liabilities is based on the remaining period at the reporting date to the contractual maturity date.

**At 31 January 2016:**

	On demand £m	Less than 1 year £m	1 to 2 years £m	2-5 years £m	over 5 years £m	Total £m
Loans and borrowings	-	138	140	1,990	1,436	<b>3,704</b>
Obligation under finance leases	-	43	14	8	-	<b>65</b>
Other payables and accruals	-	63	-	-	-	<b>63</b>
Trade payables	-	110	-	-	-	<b>110</b>
	-	354	154	1,998	1,436	<b>3,942</b>

**Interest rate swaps used for  
hedging**

Assets (inflow)	-	(9)	(3)	-	-	<b>(12)</b>
Liabilities	-	16	8	5	-	<b>29</b>
	-	7	5	5	-	<b>17</b>
	-	361	159	2,003	1,436	<b>3,959</b>

**25 Financial risk management objectives and policies (continued)**

**At 31 January 2015:**

	On demand £m	Less than 1 year £m	1 to 2 years £m	2-5 years £m	over 5 years £m	Total £m
Loans and borrowings	-	165	168	2,468	1,183	<b>3,984</b>
Obligation under finance leases	-	38	10	5	2	<b>55</b>
Amounts owed to parent undertaking	4	-	-	-	-	<b>4</b>
Other payables and accruals	-	59	-	-	-	<b>59</b>
Trade payables	-	115	-	-	-	<b>115</b>
	4	377	178	2,473	1,185	<b>4,217</b>
<b>Interest rate swaps used for hedging</b>						
Assets (inflow)	-	(6)	-	(14)	-	<b>(20)</b>
Liabilities	-	13	3	14	-	<b>30</b>
	-	7	3	-	-	<b>10</b>
	4	384	181	2,473	1,185	<b>4,227</b>

**25 Financial risk management objectives and policies (continued)**

**Capital management**

The Group considers its capital to be a combination of net debt and share capital. The capital structure at 31 January 2016 can be summarised as below:

	Expected maturity date	Interest rate %	Principal £m
Senior Term Facility	31 January 2019	4.36	454
Class A1 notes	31 July 2018	4.72	475
Class A2 notes	31 July 2025	6.27	500
Class A3 notes	31 July 2020	4.25	500
Class A4 notes	31 July 2019	3.78	250
Class B2 notes	31 July 2022	5.50	735
Total borrowings		<b>4.97</b>	<b>2,914</b>
Finance lease obligations			<b>61</b>
Cash and cash equivalents			<b>(94)</b>
Total net debt			<b>2,881</b>
Share capital			<b>20</b>
<b>Total capital</b>			<b>2,901</b>

The weighted average interest rate for all borrowings of 4.97% has been calculated using the effective interest rate and carrying values on 31 January 2016.

The Group's objectives when managing capital are:

- to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- to further strengthen the AA as the pre-eminent motoring services organisation in the UK;
- to revolutionise the customer experience through investing in and embracing new technologies and
- to reduce Group borrowings and associated interest costs.

As a highly leveraged Group, our intention is to reduce debt through trading cashflows to reduce overall gross borrowings and the cost of servicing it over time. This is a key medium term focus for the business while maintaining our competitive advantage through investment in technology. The other strategic objectives are of equally high priority but require lower levels of cash to deliver. Given the strong cash generation of the business over many years we do not have to trade these objectives off against each other – we can achieve all these objectives over different strategic timeframes.

Given the penalties associated with making early repayments of the bonds we have issued, we do not envisage making material voluntary repayments of these at this stage. The substantial IT investment we are making will transform the business both in terms of customer/staff experience but also being able to make further IT changes without the need to invest such substantial amounts of capital. Once this is complete we expect to be able to make repayments to our Senior Term Facility over its remaining life before refinancing any residue (either with a further bank loan or additional Class A notes). The existing Class A and Class B2 notes in issue would be refinanced at or around their existing maturity dates.

**25 Financial risk management objectives and policies (continued)**

The Group monitors capital using net debt to Trading EBITDA ratios. The key ratios are Senior Secured Debt to Trading EBITDA, and Net Debt to Trading EBITDA as calculated below:

	2016 £m	2015 £m
Senior Term Facility	454	663
Class A notes	1,725	1,725
Less: cash and cash equivalents	(94)	(262)
Net Senior Secured Debt <sup>1</sup>	2,085	2,126
Class B2 / B notes	735	655
Finance lease obligations	61	51
<b>Net Debt</b>	<b>2,881</b>	<b>2,832</b>
Net debt ratio <sup>2</sup>	6.9x	6.6x
Senior leverage ratio <sup>3</sup>	5.0x	4.9x
Class A free cash flow: debt service	3.6x	3.5x
Class B free cash flow: debt service	2.4x	2.2x

1 Principal amounts of the Senior Term Facility and Class A notes less cash and cash equivalents

2 Ratio of Net Debt to Trading EBITDA for the last 12 months

3 Ratio of Net Senior Secured Debt to Trading EBITDA for the last 12 months

The Senior Term Facility, Class A notes and Class B2 notes have interest cover covenants attached to them.

The Group includes regulated companies which are required to hold sufficient capital to meet acceptable solvency levels based on the relevant regulators' requirements (see note 14). There are no other externally imposed capital requirements.

The cash within the ring-fenced group headed by AA Mid Co Limited (the parent company of AA Intermediate Co Limited) is part of the whole business securitisation (WBS). A dividend cannot be paid from the ring-fenced group until a number of criteria have been met and therefore the Group's policy is to pay dividends from the AA Mid Co Limited group in accordance with the terms of the debt covenants as outlined below.

The Class A and Class B2 notes place restrictions on the Group's ability to upstream cash from the key trading companies to pay external dividends and finance activities unconstrained by the restrictions embedded in the debts.

The Class A notes only permit the release of cash providing the senior leverage ratio after payment is less than 5.5x and providing there is sufficient excess cash flow to cover the payment.

The Class B2 note restrictions came into effect during the 2016 financial year refinancing and permit the release of cash providing the fixed charge cover ratio after payment is more than 2:1 and providing that the aggregate payments do not exceed 50% of the consolidated net income.

In order to comply with the requirements of the Class A notes, we are required to maintain the Class A free cash flow to debt service ratio in excess of 1.35x and the senior leverage ratio below 5.5x. The Class B2 notes require us to maintain the Class B free cash flow to debt service ratio in excess of 1x.

The Group was in compliance with all covenants throughout the period and as at 31 January 2016.

## 25 Financial risk management objectives and policies *(continued)*

### Key Cash Release Metrics

	2016	2015
Net senior leverage <sup>1</sup>	<b>5.0x</b>	5.1x
Excess cash flow <sup>2</sup>	<b>£165m</b>	£225m
Fixed charge cover ratio <sup>3</sup>	<b>2.8x</b>	n/a
Consolidated net income <sup>4</sup>	<b>£514m</b>	£356m

1 Ratio of Net Senior Secured Debt to Trading EBITDA for the last 12 months.

2 Cumulative free cash flow since 1 February 2013, reduced by dividends and adjusted for items required by the financing documents.

3 Ratio of fixed finance charges to Trading EBITDA.

4 Cumulative profit after tax since 1 May 2013 adjusted for items required by the financing documents.

## 26 Commitments and contingencies

### Operating lease commitments

Future minimum rentals payable under non-cancellable operating leases as at 31 January are as follows:

	Land and Buildings	
	2016	2015
	£m	£m
Leases expiring:		
Within one year	-	2
Between one and five years	11	13
After five years	28	30
	<b>39</b>	45
Income from operating sub-leases	<b>(4)</b>	(6)
Amounts included in onerous lease provisions	<b>(6)</b>	(8)
	<b>29</b>	31

Where a property is no longer used by the Group for operational purposes, tenants are sought to reduce the Group's exposure to lease payments. Where the future minimum lease payments are in excess of any expected rental income due, a provision is made.

**26 Commitments and contingencies (continued)**

**Finance lease commitments**

The Group has finance lease contracts for various items of plant and machinery. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments are as follows:

	2016		2015	
	Present value of payments £m	Minimum payments £m	Present value of payments £m	Minimum payments £m
Within one year	40	43	35	38
Between one and five years	21	22	16	17
Total minimum lease payments	61	65	51	55
Less amounts representing finance charge	-	(4)	-	(4)
Present value of minimum lease payments	61	61	51	51

**Commitments**

Amounts contracted for but not provided in the financial statements amounted to £15m (2015: £5m).

**27 Principal subsidiary undertakings**

The subsidiary undertakings of AA Intermediate Co Limited, all of which are wholly owned except where stated, are listed in note 8 of the Company financial statements.

**28 Auditor's remuneration**

	2016 £m	2015 £m
<b>Amounts receivable by the Company's auditor and its associates in respect of:</b>		
Audit of financial statements of subsidiaries of the Company	1	1
Corporate finance services	1	2

The fee for the audit of these financial statements was £10,000 (2015: £10,000).

Corporate finance services mainly relate to reporting accountant work that would normally be undertaken by the auditor.

## 29 Related party transactions

The following table provides the total value of transactions that have been entered into with associates during each financial year:

### Transactions with associates:

Associate	Nature of transaction	2016 £m	2015 £m
A.C.T.A. S.A.	Call handling fees paid	2	2
A.R.C. Europe S.A.	Registration fees paid	1	1

### Cross-company guarantees

The Company has an interest in a partnership, AA Pension Funding LP, which is fully consolidated in the Group financial statements. The Group has taken advantage of the exemption conferred by Regulation 7 of the Partnership (Accounts) Regulations 2008 and has, therefore, not appended the accounts of this qualifying partnership to the Group financial statements. Separate accounts for the partnership are not required to be, and have not been, filed at Companies House.

The Company made an on-going guarantee of the liabilities of its wholly-owned subsidiary undertakings AA Ireland Limited, Tourist Accommodation Management Services Limited and Breakdown Assistance Services Limited in the Republic of Ireland for the financial year ended 31 January 2015. No such guarantee has been given for the financial year ended 31 January 2016.

## 30 Compensation of key management personnel of the Group

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the Group.

Key management personnel consists of the Executive Chairman, Chief Financial Officer and the Executive Management Committee. With effect from 1 August 2015, the Executive Management Committee was restructured reducing key management personnel from 27 to 8.

The amounts recognised as an expense during the financial year in respect of key management personnel are as follows:

	2016 £m	2015 £m
Short-term employee benefits	6	6
Share-based payments	2	1
Termination payments	-	2
<b>Total compensation paid to key management personnel</b>	<b>8</b>	<b>9</b>

**31 Share-based payments**

	2016 £m	2015 £m
Share-based payments - MVP shares	2	1
Share-based payments - LTBP	2	-
Share-based payments - staff share incentive plan	1	1
	<b>5</b>	<b>2</b>

**Management value participation shares (MVP shares)**

On 23 June 2014, the ultimate parent company, AA plc issued 24 million convertible, redeemable MVP shares to certain key members of senior management at £0.001 per share. These shares were divided into three classes and are convertible into AA plc ordinary shares following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% per annum compound growth against the AA plc admission price of £2.50 which is tested on the third, fourth and fifth anniversaries of admission to the London Stock Exchange.

A further 36 million MVP shares were issued at £0.001 per share on 22 December 2015.

The MVP share-based payments are equity settled. The following table illustrates the number and fair value of the MVP shares:

	Vesting date	2016 No. of shares	2015 No. of shares	2016 Fair value per share £	2015 Fair value per share £
A1 shares	23 June 2017	8,000,000	8,000,000	0.25	0.25
B1 shares	23 June 2018	8,000,000	8,000,000	0.26	0.26
C1 shares	23 June 2019	8,000,000	8,000,000	0.26	0.26
A2 shares	23 June 2017	12,000,000	-	0.38	-
B2 shares	23 June 2018	12,000,000	-	0.40	-
C2 shares	23 June 2019	12,000,000	-	0.40	-
Total		60,000,000	24,000,000		

The A1 and A2 shares can also be converted on the 4th or 5th anniversary of admission and the B1 and B2 shares can also be converted on the 5th anniversary of admission.

All MVP shares were valued using a Binomial model and 25% volatility assumption to calculate the fair value using the following risk-free interest rates:

	Vesting period		
	3 year %	4 year %	5 year %
Risk-free interest rate for A1, B1 and C1 MVP shares	0.88	1.35	1.82
Risk-free interest rate for A2, B2 and C2 MVP shares	0.55	0.77	0.98

The expected volatility reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

### 31 Share-based payments (*continued*)

#### Long Term Bonus Plan (LTBP)

On 13 August 2015, the ultimate parent company, AA plc issued 3 million conditional ordinary shares to certain key members of senior management at nil cost. A further 1 million conditional ordinary shares were issued on 16 November 2015.

These shares were divided into three tranches, A, B and C and vest following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% per annum compound growth against the AA plc admission price of £2.50 which is tested on the third, fourth and fifth anniversaries of admission to the London Stock Exchange and satisfaction of certain individual performance targets.

The LTBP share-based payments are equity settled. The following table illustrates the number and fair value of the LTBP shares:

	Vesting date	2016	
		No. of shares	Fair value per share £
August 2015 awards:			
A shares	26 June 2017	1,010,219	2.93
B shares	26 June 2018	1,010,219	2.39
C shares	26 June 2019	1,010,219	1.88
November 2015 awards:			
A shares	26 June 2017	247,104	1.43
B shares	26 June 2018	247,104	1.12
C shares	26 June 2019	247,104	0.83
<b>Total</b>		<b>3,771,969</b>	

If the awards do not vest on the 3<sup>rd</sup> or 4<sup>th</sup> anniversary of admission, then they are retested on the 5<sup>th</sup> anniversary.

The shares issued in August 2015 were valued using a Monte Carlo simulation model and 20% volatility assumption to calculate the fair value using the following risk-free interest rates:

	Vesting period		
	3 year	4 year	5 year
Risk-free interest rate (%)	0.70	0.72	1.00

The shares issued in November 2015 were valued using a Monte Carlo simulation model and 24% volatility assumption to calculate the fair value using the following risk-free interest rates:

	Vesting period		
	3 year	4 year	5 year
Risk-free interest rate (%)	0.58	0.79	0.99

The expected volatility reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

### 31 Share-based payments (*continued*)

#### Staff share incentive plans

The Group has a number of Share Incentive Plans (SIP).

Under the SIP, employees are able to buy Partnership shares by making weekly or monthly payments into the SIP.

In addition, for every Partnership share an employee purchases the ultimate parent company, AA plc will match this on a 1:1 basis (Matching Shares).

The SIP share-based payments are equity settled. The following table illustrates the fair value and vesting period of the SIPs:

Share type	Award date	Vesting date	No. of shares <sup>1</sup>	Volatility %	Risk-free interest rate %	Fair value per share £	Charge for year ended 31 January 2016 £m	Charge for year ended 31 January 2015 £m
<b>2015 SIP</b>								
Partnership shares	29 August 2014	29 August 2015	2,132,766	21	0.55	0.23	-	-
Matching shares	29 August 2014	29 August 2018	2,132,766	21	0.55	2.58	1	1
<b>2016 SIP</b>								
Matching shares	11 January 2016	11 January 2019	111,577	26	0.76	2.93	-	-
<b>4,377,109</b>							<b>1</b>	<b>1</b>

<sup>1</sup> The number of shares shown above is the estimated number as at 31 January 2016.

The SIPs are valued using a Black Scholes model.

The expected volatility reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

### 32 Ultimate parent undertaking and controlling party

AA plc is the ultimate controlling party and parent undertaking of the Group, whose registered office is at Fanum house, Basing View, Basingstoke, RG21 4EA. Copies of the consolidated parent financial statements are available from the Company Secretary at the relevant registered office address.

### **33 Accounting standards, amendments and interpretations**

#### **New accounting standards, amendments and interpretations adopted in the year**

In the year ended 31 January 2016 the Group did not adopt any new standards or amendments issued by the IASB or interpretations issued by the IFRS Interpretations Committee (IFRS IC) that have had a material impact on the consolidated financial statements. Other new standards, amendments and interpretations adopted, that have not had a material impact on the amounts reported in these financial statements but may impact the accounting for future transactions and arrangements, were:

	Effective date
<ul style="list-style-type: none"> <li>• IAS 19 Defined Benefit Plans – employee contributions</li> </ul>	1 July 2014
<ul style="list-style-type: none"> <li>• Annual Improvements to IFRS 2010-2012, 2011-2013</li> </ul>	1 July 2014

#### **New accounting standards, amendments and interpretations not yet adopted**

A number of new standards, amendments and interpretations, which have not been applied in preparing these financial statements, have been issued and are effective for annual reports beginning after 1 February 2015:

	Effective date
<ul style="list-style-type: none"> <li>• IAS 1: Disclosure Initiative</li> </ul>	1 January 2016
<ul style="list-style-type: none"> <li>• Annual Improvements to IFRS 2012-2014</li> </ul>	1 January 2016
<ul style="list-style-type: none"> <li>• IFRS 11: Accounting for Acquisitions of Interests in Joint Operations</li> </ul>	1 January 2016
<ul style="list-style-type: none"> <li>• IAS 12: Recognition of Deferred Tax assets for unrealised losses</li> </ul>	1 January 2017
<ul style="list-style-type: none"> <li>• IAS 7: Disclosure Initiative</li> </ul>	1 January 2017
<ul style="list-style-type: none"> <li>• IFRS 15: Revenue from Contracts with Customers</li> </ul>	1 January 2018
<ul style="list-style-type: none"> <li>• IFRS 9: Financial Instruments</li> </ul>	1 January 2018
<ul style="list-style-type: none"> <li>• IFRS 16: Leases</li> </ul>	1 January 2019

The Group is currently assessing whether the above standards will have a material impact on the financial statements for the year ended 31 January 2017.

### **34 Events after the reporting period**

On 16 March 2016 the Chancellor presented the 2016 budget in which he announced a reduction in the future corporation tax rate. Instead of the corporation tax rate reducing from 19% to 18%, on 1 April 2020, the rate will now fall to 17%. As the new rate of 17% was not substantively enacted at the balance sheet date the impact of this reduction has not been reflected in the deferred tax calculations. The effect of this rate reduction would be to reduce the carrying value of the deferred tax asset in the balance sheet by £2m.

Subsequent to the year end, the wholly owned trading subsidiaries in Ireland met the definition of assets held for sale as a result of current plans being put in place to dispose of these subsidiaries. See note 2 for the revenue and Trading EBITDA associated with this segment. The Group is currently in discussion with potential buyers and the proceeds from a sale would be used to repay debt.

## Company balance sheet as at 31 January

	Notes	2016 £m	2015 £m
<b>Non-current assets</b>			
Investment in subsidiaries	2	1,661	1,661
<b>Current assets</b>			
Trade and other receivables	3	129	129
<b>Total assets</b>		<b>1,790</b>	1,790
<b>Current liabilities</b>			
Trade and other payables	4	(1,770)	(1,770)
<b>Total liabilities</b>		<b>(1,770)</b>	(1,770)
<b>Net assets</b>		<b>20</b>	20
<b>Equity</b>			
Called up share capital	5	20	20
Retained earnings		-	-
<b>Total equity attributable to equity holders of the parent</b>		<b>20</b>	20

The profit for the financial year of the Company is £nil (2015: £nil).

As at 31 January 2016, the Company had distributable reserves of £77,000 (2015: £85,000).

Signed for and on behalf of the Board on 29 June 2016 by:

M Clarke  
Director

The accompanying notes are an integral part of this company balance sheet.

## Company statement of changes in equity

	Share capital £m	Retained earnings £m	Total £m
<b>At 1 February 2014</b>	<b>20</b>	-	<b>20</b>
Profit for the year	-	-	-
<b>At 31 January 2015</b>	<b>20</b>	-	<b>20</b>
Profit for the year	-	-	-
Dividends paid	-	(60)	(60)
Dividends received	-	60	60
<b>At 31 January 2016</b>	<b>20</b>	-	<b>20</b>

The accompanying notes are an integral part of this company statement of changes in equity.

## Notes to the Company financial statements

### 1 Presentation of financial statements and Company accounting policies

#### 1.1 Presentation of financial statements

These financial statements were prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework (FRS101). The financial statements are prepared under the historical cost convention.

No profit and loss account is presented by the Company as permitted by Section 408 of the Companies Act 2006.

The accounting policies which follow set out those policies which apply in preparing the financial statements for the year ended 31 January 2016. The financial statements are prepared in Sterling and are rounded to the nearest million pounds (£m).

#### 1.2 Basis of preparation

The Company has transitioned to FRS 101 from previously extant UK Generally Accepted Accounting Practice for all periods presented. The Company has early adopted SI 2015/980.

The Company has taken advantage of the following disclosure exemptions under FRS 101:

- IAS 1 paragraph 10(d) (statement of cash flows),
- IAS 1 paragraph 16 (statement of compliance with all IFRS),
- IAS 1 paragraph 38A (requirement for minimum of two primary statements, including cash flow statements),
- IAS 1 paragraph 111 (cash flow statement information),
- IAS 1 paragraphs 134-136 (capital management disclosures),
- IFRS 1 paragraphs 6 and 21,
- Paragraphs 45(b) and 46 to 52 of IFRS 2, 'Share-based payment',
- IAS 7 'Statement of cash flows',
- IFRS 7 'Financial Instruments: Disclosures',
- IAS 8 paragraphs 30 and 31,
- The requirements in IAS 24, 'Related party disclosures' to disclose related party transactions entered into between two or more members of a group.

#### 1.3 Accounting policies

##### a) Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward foreign currency contract. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date or if appropriate at the forward contract rate. All differences are taken to the profit and loss account.

## Notes to the Company financial statements (*continued*)

### b) Investments

Fixed asset investments are included in the balance sheet at cost, less any provisions for permanent impairment.

Investments in Group undertakings are stated at the lower of cost and net realisable value.

The carrying amounts of the Company's assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of the fixed asset may not be recoverable. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its income-generating unit exceeds its recoverable amount. Impairment losses are recognised in the profit and loss account unless it arises on a previously revalued fixed asset.

The recoverable amount of fixed assets is the greater of their net realisable value and value in use. In assessing value in use, the expected future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the rate of return expected on an investment of equal risk. For an asset that does not generate largely independent income streams, the recoverable amount is determined for the income-generating unit to which the asset belongs.

### c) Critical accounting estimates and judgements

Estimates are evaluated continually and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions about the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The principal estimates and assumptions that have a risk of causing an adjustment to the carrying amounts of assets and liabilities within the next financial period are discussed below.

Management have exercised judgement in applying the Group's accounting policies and in making critical estimates. The underlying assumptions on which these judgements are based, are reviewed on an on-going basis and include the assumptions for future growth of cash flows to support the value-in-use calculations for the investment impairment review.

#### *Investments*

The Group tests the investment balances for impairment annually. The recoverable amounts of the investments have been determined based on value-in-use calculations which require the use of estimates. Management have prepared discounted cash flows based on the latest strategic plan.

## Notes to the Company financial statements (*continued*)

### 2 Investments

	2016 £m	2015 £m
Investment in subsidiary at cost		
At 1 February and 31 January	<b>1,661</b>	1,661

No indicators of impairment in the value of subsidiaries have been identified.

### 3 Trade and other receivables

	2016 £m	2015 £m
Amounts owed by subsidiary undertakings	<b>129</b>	129

The amounts owed by subsidiary undertakings are unsecured, have no repayment terms and bear no interest.

### 4 Trade and other payables

	2016 £m	2015 £m
Amounts owed to parent undertakings	<b>1,756</b>	1,756
Amounts owed to subsidiary undertakings	<b>14</b>	14
	<b>1,770</b>	1,770

The amounts owed to parent and subsidiary undertakings are unsecured, have no repayment terms and bear no interest.

### 5 Share capital

	2016 £m	2015 £m
<b>Allotted, called up and fully paid</b>		
20,000,002 ordinary shares of £1 each	<b>20</b>	20
	<b>20</b>	20

The voting rights of the holders of all ordinary shares are the same and all ordinary shares rank pari passu on a winding up.

The Company has 20,000,100 authorised ordinary shares of £1 each.

During the year, the company paid a dividend of £3.00 per share (2015: nil).

## Notes to the Company financial statements (*continued*)

### 6 Auditor's remuneration

The fee for the audit of these financial statements was £10k (2015: £10k).

### 7 Staff costs

The Company had no employees or employee staff costs in the current or prior year.

### 8 Subsidiary undertakings

All subsidiaries are wholly owned and incorporated and registered where stated below.

The principal subsidiary undertakings of the Company at 31 January 2016 are:

Name	Country
AA Acquisition Co Limited <sup>1</sup>	United Kingdom
AA Bond Co Limited	Jersey
AA Corporation Limited	United Kingdom
AA Financial Services Limited	United Kingdom
AA Ireland Limited	Ireland
AA Media Limited	United Kingdom
AA Senior Co Limited	United Kingdom
AA The Driving School Agency Limited	United Kingdom
Automobile Association Developments Limited	United Kingdom
Automobile Association Insurance Services Limited	United Kingdom
Drivetech (UK) Limited	United Kingdom
Intelligent Data Systems (UK) Limited	United Kingdom

<sup>1</sup> Directly owned by AA Intermediate Co Limited, all other subsidiaries are indirectly held.

## Notes to the Company financial statements *(continued)*

### 8 Subsidiary undertakings *(continued)*

The other subsidiary undertakings of the Company at 31 January 2016 are:

Name	Country
1Stop Travel Insurance Services Limited	United Kingdom
A.A. Insurance Services Limited	United Kingdom
A.A. Pensions Trustees Limited	United Kingdom
AA Assistance Limited	United Kingdom
AA Brand Management Limited	United Kingdom
AA Ireland Pension Trustees Limited	Ireland
AA J Quartz Limited	United Kingdom
AA Legal Services Limited	United Kingdom
AA Parking Solutions Limited	United Kingdom
AA Pension Funding GP Limited	United Kingdom
AA Pension Funding LP	United Kingdom
AA Road Services Limited	United Kingdom
AA Signs Limited	United Kingdom
AA Underwriting Limited	United Kingdom
Automobile Association Commercial Services Limited	United Kingdom
Automobile Association Holdings Limited	United Kingdom
Automobile Association Insurance Services Holdings Limited	United Kingdom
Automobile Association Protection and Investment Planning Limited	United Kingdom
Automobile Association Services Limited	United Kingdom
Automobile Association Travel Services Limited	United Kingdom
Automobile Association Underwriting Services Limited	United Kingdom
Breakdown Assistance Services Limited	Ireland
Drakefield Group Limited	United Kingdom
Drakefield Holdings Limited	United Kingdom
Drakefield Insurance Services Limited	United Kingdom
Drakefield Services Limited	United Kingdom
Drive Publications Limited	United Kingdom
Drivetech Advantage Agency Limited	United Kingdom
Driving Services UK Limited	United Kingdom
E Travel Insurance Services Limited	United Kingdom
Fanum Services Limited	United Kingdom
Go Insurance Services Limited	United Kingdom
Go Travel Insurance Services Limited	United Kingdom
Intelematics Europe Limited	United Kingdom
Nationwide 4 X 4 Ltd	United Kingdom
Peak Performance Management Limited	United Kingdom
Personal Insurance Mortgages and Savings Limited	United Kingdom
Quotebanana Limited	United Kingdom
The Automobile Association Limited	Jersey
The British School of Motoring Limited	United Kingdom
Tourist Accommodation Management Services Limited	Ireland