

AA INTERMEDIATE CO LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 JANUARY 2018

Company registration number: 5148845

Strategic Report

Financial results

Trading Revenue¹ grew 1.0% to £946m driven principally by the strong performance of Insurance as well as Roadside. Driving Services, which is now within Roadside, was broadly flat.

Trading EBITDA² was £393m. The 3.2% decline compared to last year was due to the reduction in Roadside Trading EBITDA, reflecting higher costs from third-party garaging due to workload peaks and the higher number of breakdowns attended. The 6.0% increase in Insurance Trading EBITDA reflects the improved performance of our brokers and the AA plc group underwriter. Head Office costs, which have now been allocated to segments, were broadly flat during the year. Group Trading EBITDA margin reduced from 43.3% to 41.5% as a result of the lower profitability in Roadside.

Operating profit before exceptional items decreased by 3.8% to £308m principally due to the reduction in Trading EBITDA and the increase in amortisation and depreciation reflecting the recent investment in transformation capital expenditure.

Exceptional operating items were lower at £5m income (2017: £32m cost), including £24m relating to business transformation costs and £27m impairment of goodwill offset by a £6m gain on the disposal of the Home Emergency Services consumer business, a one-off past service credit of £34m from the restructuring of the UK pension scheme, a credit of £7m for the reversal of share-based payment charges for the former Executive Chairman, and a £9m improvement in onerous property provisions.

Cash flow from continuing operating activities before exceptional items and taxation decreased from £374m to £367m. Capex included £34m of IT transformation capex, the final tranche of the investment originally set out at the IPO of AA plc, and £53m of maintenance capex (including finance leases net of proceeds of sale of vehicles). Free cash flow before equity for continuing operations was an outflow of £6m (2017: inflow of £89m).

Strategy update announced 21 February 2018

Following the appointment of Simon Breakwell as CEO to AA plc in September 2017, a strategic review was conducted which included a comprehensive bottom-up analysis of every aspect of the business. The conclusion was that the AA is a phenomenal business and that we could build on our leading position in Roadside, our trusted brand and our highly-skilled and committed employees with a deeply embedded customer service ethos. Our confidence about our ability to realise the opportunities convinced us of the positive long-term outlook for the AA.

The objectives of the strategic plan are to deliver targeted investment in our people, our products, our systems and operations. We are building on the solid foundation that our investments since the IPO have created, and addressing the challenges we face.

This strategic plan will deliver front line resource to improve the efficiency, predictability and resilience of our Roadside operations as well as investment in game-changing growth drivers – Insurance and connected car. These investments, while reducing our short term profitability, are vital to our long term success. Our development in connected car – started with the launch of Car Genie in August 2017 - could take the AA from being a service helping when you break down to one which potentially predicts when you might break down in the first place, allowing scheduling of repairs and a great experience for customers.

We are confident the priorities we set out in February will transform our products and service offerings to our customers by creating a truly innovative and differentiated product proposition which will deliver long term shareholder value.

Pensions

In June 2017, we concluded the triennial review of the AA's UK defined benefit pension scheme and agreed a funding plan for the deficit which had increased, largely as a result of the reduction in long term gilt yields. A nine-year plan of incremental funding is now in place, taking into account the continued funding of the previous deficit. The next triennial actuarial review is scheduled for 31 March 2019.

Changes successfully made to the defined benefit pension scheme mitigated some of the recent increases in ongoing pension service costs. Overall, the changes have reduced our exposure to pension risks, increased our competitiveness within our industry, and provided for a more consistent pension offering across our business.

Refinancing

The refinancing in July 2017, which included the use of cash to repay £98m of the Senior Term Facility, further reduced the cost of borrowings and extended the average maturity of our debt with the first repayment due in July 2020. Since the IPO in June 2014 we will have reduced the annual debt interest cost on our borrowings by £90m excluding the hedging costs.

New segmental reporting

In line with our new strategy, we have altered our segmental reporting to align it more closely with the way the business is managed. Roadside Assistance and Driving Services are now shown together as Roadside. Insurance Services is shown as Insurance.

Head office costs have been apportioned to our two new segments. Costs are directly allocated where it is possible to do this, all other costs are allocated on the basis of a pro-rata share of revenue.

In addition to these changes, the reconciliation from Trading EBITDA to operating profit before exceptional items will now include a divisional apportionment to Roadside and Insurance for share-based payments, pension service charge adjustments and amortisation and depreciation.

	2018	2017
	£m	£m
TRADING REVENUE		
Roadside Assistance	747	742
Driving Services	66	64
Roadside Revenue	813	806
Insurance Services	133	131
Insurance Revenue	133	131
Trading Revenue	946	937
TRADING EBITDA		
Roadside Assistance	346	366
Driving Services	22	20
Head Office Costs	(46)	(47)
Roadside Trading EBITDA	322	339
Insurance Services	79	76
Head Office Costs	(8)	(9)
Insurance Trading EBITDA	71	67
Trading EBITDA	393	406

The following definitions apply throughout the report:

¹ Trading Revenue is revenue excluding discontinued operations and exceptional revenue items.

² Trading EBITDA (earnings before interest, tax, depreciation and amortisation) excludes exceptional operating items, share-based payments and pension service charge adjustment.

³ The pension service charge adjustment relates to the difference between the cash contributions to the pension scheme for ongoing contributions and the calculated annual service costs

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 2018. 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

Roadside includes Roadside Assistance and Driving Services.

Roadside Assistance performance is driven by our personal membership base and supported by our business customer (B2B) base, underpinning the scale of our operations which is critical to our success. Each provide approximately half the jobs for the 2,900-strong patrol force.

We have 2,742 driving instructors in our franchised driving schools, the AA and BSM, providing driving lessons for approximately 80,000 learners each year. DriveTech is joint market leader in providing speed awareness courses for police forces in the UK and fleet training services.

	2018	2017
Trading Revenue (£m)	813	806
Trading EBITDA (£m)	322	339
Trading EBITDA margin (%)	39.6	42.1
Personal Members excluding free Memberships (000s)	3,289	3,335
Average income per personal Members excluding free Memberships (£)	157	158
Business customers (000s)	9,928	9,976
Average income per Business customer (£)	20	20
Number of breakdowns ('000s)	3,679	3,635
Driving instructors	2,742	2,607

Trading Revenue grew 0.9% to £813m driven largely by increased pay-for-use B2B revenue. Trading EBITDA declined by 5.0% to £322m primarily reflecting the cost increases of service delivery. Head office costs declined from £47m to £46m. Trading EBITDA margin decreased from 42.1% to 39.6% reflecting the EBITDA decline.

Roadside Assistance

The contribution from Roadside Assistance rose 0.7% to £747m despite a decline in memberships and business customers. Growth was the result of increased pay-for-use revenue from B2B, increased ancillary sales and increased revenue from vehicle inspections, AA Cars and publishing.

Paid personal memberships declined 1.4% to 3.29m. New member growth of 7% (2017: 14%) was good, particularly against last year's strong performance, driven again by digital sales. Our expansion into younger segments has begun, helped by our effective and well-received "singing baby" advertising campaign. Retention was broadly flat at 82%, a strong performance given the significant challenges we faced. These included the impact of the rise in IPT in June 2017; the dilution from an increase in new members, whom we retain at lower rates; our completed programme of redress for customers affected by duplicate cover; and the introduction in April of new renewal price transparency regulations. StayAA, our proactive retention programme, achieved all-time high results, retaining 72% of those who call to cancel, with discounts averaging 22%, compared with 57% and 35% respectively when the programme was launched in 2014. The discontinuation of the free-to-paid insurance channel from December 2015 has resulted in a reduction in membership by approximately 70,000 in FY18 and this pipeline of additional paid members has now ceased.

Average income per paid member declined 0.6% to £157 (2017: +1.3% to £158), reflecting our constraint in passing through price rises above the increase in IPT and the dilution of introductory discounts from the increased number of new members.

Business customers declined 0.5%, falling to 9.9m reflecting the anticipated decline in the number of Added Value Accounts (AVAs) with our banking partners Lloyds Banking Group and TSB and the lower number of new cars sales for our manufacturing partners. During the year we retained or extended a number of contracts including VW Group and Ford.

Average income per business member was flat at £20.

Trading EBITDA fell by £20m to £346m. Apart from the decline in membership numbers and business customers, this was largely the result of the increased costs of third-party garaging due to workload peaks and wage inflation which we were unable to absorb through price rises. Trading EBITDA margin declined from 49.3% to 46.3%.

Driving Services

Trading Revenue increased by £2m to £66m. The 5.2% rise in driving instructor franchises to 2,742 (2017: 2,607) was the result of improvements to our franchise proposition and the strength of the AA and BSM brands. This was partially offset by the marginal decline from fewer courses delivered by DriveTech. While the number of speed awareness courses for the police increased, the number of courses for our corporate partners declined.

Trading EBITDA rose £2m to £22m, driven by the improvement in Driving Schools and efficiency savings in both businesses. Trading EBITDA margin rose from 31.2% to 33.3%.

INSURANCE

Insurance includes Insurance Services, comprising our Insurance Broker and our Financial Services partnership with Bank of Ireland.

Growth was driven by our insurance broker which has focused on the core products of motor and home insurance and returned our broker motor book to growth while slowing the anticipated decline in home policies.

Our financial services partnership with the Bank of Ireland, launched in July 2015, builds on a long past history of AA financial services and enables us to enhance our membership proposition.

	2018	2017
Trading Revenue (£m)	133	131
Trading EBITDA (£m)	71	67
Trading EBITDA margin (%)	53.4	51.1
Total policy numbers in force ¹ (000s)	1,447	1,451
Average income per policy (Motor and Home) (£)	74	70
Total Motor policies (000s)	629	594
Total Home policies (000s)	818	857
Financial Services products ('000s)	142	100

¹ Excludes Financial Services

Trading Revenue rose 1.5% to £133m driven by higher revenue from motor insurance broking. Trading EBITDA rose 6.0% to £71m with flat head office costs of £8m. Trading EBITDA margin increased from 51.1% to 53.4% as a result of the increase in motor insurance broking.

Insurance Services

Trading Revenue rose 1.5% to £133m. We grew our motor book by 5.9% to 629,000 policies, benefitting from incremental sales and renewals through the AA plc group in-house underwriter, which continues to perform ahead of expectations. We did well to achieve stable retention despite the challenges of the new renewal pricing transparency regulations from April; the impact of the Ogden rate change on cost of premiums, which drove churn; and the IPT increases. We benefited from improved pricing agility following the installation of insurance hosted pricing (IHP) with five of our motor panel members, including our underwriter. This has enabled us to price more competitively and convert a greater proportion of quotes on price comparison websites (PCWs).

In line with expectations, home policies fell 4.6% to 818,000 as we have not yet made the investment in IHP to improve pricing agility. Overall policy numbers are down as we continue to retreat from less profitable business lines, including insurance categories such as weddings and pets. Home Emergency Services policies for emergency repairs to boilers, heating systems and other domestic installations were down year-on-year. The sale of our Home Emergency Services consumer book was completed in January 2018.

The focus on greater profitability has driven average income per motor and home policy up 5.7% to £74 (2017: £70).

Financial Services revenue was broadly flat at £8m. By the end of January 2018, we had 142,000 Financial Services products across our credit cards, personal loans and savings portfolio. This represents a balance sheet of approximately £400m, broadly match-funded by deposits. Our partnership with the Bank of Ireland, continues to build positive momentum on the strength of our brand and marketing expertise and Bank of Ireland's operational excellence. The AA membership base and brand are benefiting the business with over 17% of the non-ISA savings books held by members and 39% of our personal loans being written for vehicles. The completion of the acquisition of 100% of the AA Cars platform will enable us to expand our loan offering into the growing used car market.

Trading EBITDA rose 4% to £79m as a result of the growth of the motor book, the focus on the more profitable business lines and disciplined cost management. Trading EBITDA margin was higher at 59.4% (2017: 58.0%).

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
- Each risk register ‘owner’ is required to formally self-certify the completeness and correctness of their risk register(s) on a quarterly basis.

Principal risks

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 AA, 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, a summary of changes during the year and the primary key performance indicators (KPIs).

Principal Risks	Description	Mitigation	Change in the year	Impact, likelihood and trend
<p>1. Outstanding service: We are unable to maintain an outstanding service</p> <p>Primary KPIs:</p> <ul style="list-style-type: none"> • Breakdowns attended 	<p>The AA's brand and its continued success, and, in particular, the loyalty of its customers, relies on delivering outstanding service that is superior to the rest of the market. Inadequate investment in technology, systems, people and processes would place this objective at increasing risk.</p>	<p>We will continue to protect the ability of our Patrols to provide excellent service through providing them with connectivity to state of the art scheduling systems, investing in in-van technology and equipment and providing excellent training and support.</p> <p>Ongoing monitoring of complaints, press reports and social media through structured processes, including Compliance and Risk oversight, helps inform our service performance and offerings.</p>	<p>While our repair rate and single-task-completion are at an 11-year high and under-bonnet times a 9-year low, restricted operational flexibility and extreme weather events resulted in an increased use of third party garages in busy periods which added cost and decreased profitability. Work is ongoing to increase the flexibility of the patrol force, reduce cost and improve customer service. Our AA breakdown app has now been downloaded by more than one million personal members and is being actively used in 29% of breakdowns.</p>	<p>Delivering outstanding service is fundamental to our future and our brand. The impact of failure to deliver the best service in the market would be very high. The actions we are taking to increase the flexibility of the patrol force and improve our forecasting will reduce the probability of this risk crystallising.</p> <p>Inclement weather will always have an impact on demand and we are revisiting our winter surge plan to make sure we are in the best position to deal with significant weather extremes.</p>
<p>2. Roadside market share and margin: We are unable to maintain our market share and an ability to command a price premium on our roadside services</p> <p>Primary KPIs:</p> <ul style="list-style-type: none"> • Paid personal members • Business customers • Average income per member • Average income per business customer 	<p>Competitors, such as Green Flag, that provide roadside services at a lower price or have a different business model together with changes in car technology threaten our market share. If we charge a price premium that is above what our service can sustain, we will not grow our member or B2B customer base and, in the long-term, sustainably grow profits. We need to improve, innovate, demonstrate and deliver a superior proposition and ensure our pricing is competitive relative to this position.</p>	<p>We are continuing to improve our roadside membership proposition by strengthening our roadside product offerings and engaging more members in additional benefits.</p> <p>We have put in place processes for significantly more effective advertising campaigns and are introducing new CRM systems to improve our communications with members, which includes engaging members in their existing services and benefits to drive loyalty.</p> <p>Our pricing team has significant expertise to monitor market pricing levels.</p>	<p>Car Genie, our Connected Car product, was launched during the year.</p>	<p>Long-term the AA will find it challenging to grow profit sustainably if its membership is declining. Therefore, the impact of membership growth is critical in the long-term, as is maintaining key business relationships such as the Lloyds Banking Group contract which is up for renewal in 2018.</p> <p>Membership has remained relatively stable in the last 12 months.</p> <p>The business is focused on realising a sustainably growing membership and recognises the need for a more distinctive and differentiated offering to mitigate competitive pressures.</p>
<p>3. Insurance broking business: Price comparison sites will further damage the insurance broker model</p> <p>Primary KPIs:</p> <ul style="list-style-type: none"> • Insurance policies • Average income per motor and home policy 	<p>The consumer use of price comparison sites may continue to transfer value from our insurance broking business.</p>	<p>We continue to use our strengths in the brand, channels and data to mitigate this risk.</p>	<p>Our Motor Insurance book has increased in the year as a result of the growth in our underwriter and roll out of insurer hosted pricing. The Home Insurance book declined as we took a longer term approach to our underwriting strategy and product offerings.</p>	<p>The competitive threat from aggregators remains unchanged, however the success of AA plc group underwriter and the adoption of insurer hosted pricing enables us to better respond to this threat. We will broaden our footprint by targeting new customers who have never been members of the AA, and younger drivers.</p>

<p>4. Business transformation: We are unable to successfully complete essential business transformation</p>	<p>We must continue to transform the AA to achieve the required efficient customer centric services and to develop the business.</p> <p>There is still much to do and the required improvements to process, embedded ways of working and culture, inherently involves risks in a customer facing service environment</p>	<p>There is an ongoing cost efficiency and process improvement programme in place with progress tracked at regular Management Business Reviews.</p> <p>A rigorous approach is taken in implementing changes to achieve satisfactory control, with ongoing monitoring and reporting.</p> <p>We have a talent management model in place, where skills gaps are identified and development and/or recruitment initiatives are actioned.</p>	<p>The year has seen increasing management and employee stretch as the various change and product development initiatives have been rolled out.</p> <p>The AA has invested in people to effectively manage transformation in the business, with the recruitment of a new COO, CIO and a dedicated transformation team.</p>	<p>Strong management capability and oversight have been put in place to better manage this risk.</p>
<p>5. IT transformation: We are unable to successfully deliver the essential IT transformation required</p>	<p>An essential programme of renewal and enhancement of our IT estates is in progress to address the risks to our brand and our competitive capability. The IT transformation is extensive and involves a continuing complex programme of work. Given the scale and complexity, the programme involves inherent risks to the timely delivery of this implementation.</p>	<p>Proven methodology with specialist IT development skills is in place to manage this risk. The programme is being led by executives with a proven track record in IT transformation.</p> <p>The programme is subject to considerable scrutiny by the executive management team and regular progress reports are reviewed by both the AA plc Risk Committee and the AA plc board.</p>	<p>Investment in new IT systems over the last three years has improved our productivity and marketing and digital capabilities. We have committed to slowing the pace of the implementation phase to mitigate the risk of management stretch and ensure adequate impact assessments are undertaken. We are building on the strong, new foundations now in place.</p> <p>Further investment in IT development forms part of the new strategy.</p>	<p>The ability to manage and enhance existing legacy systems as well as implementing new IT systems are key to the successful ongoing development of the AA. The adverse impact of a material delay to the implementation of the programme would be high.</p>
<p>6. Safety: We are unable to maintain the safety of our workforce and members</p>	<p>We must continue to effectively manage the risks to the safety of our workforce and members and ensure controls are deployed to achieve this. Accountability to take action is essential in this as is oversight, review and embracing continual improvement.</p>	<p>We have a robust and externally audited integrated health, safety and environmental (HS&E) management system as well as local arrangements where appropriate.</p> <p>We regularly review all our HS&E risks and controls to ensure they remain fit for purpose.</p> <p>We have in place safety improvement programmes which are SMART and drive the continual improvements we aspire to.</p> <p>We have a robust monitoring and assurance process which includes safety performance and is reviewed at the AA plc Risk Committee and the Executive Risk and Compliance Committee.</p> <p>We have a dedicated team of health and safety advisors who are all members of the chartered body IOSH (Institution of Occupational Safety and Health).</p>	<p>This is a new principal risk. The AA continues to strive to maintain a safe environment for employees and members.</p>	<p>Protecting our employees' safety whilst they are at work is fundamental to our values and our brand. The impact of failure to look after our employees would be very high and could result in not only death or serious injury, but an increase in civil claims and enforcement action against the Company and/or its Directors.</p> <p>Protecting our members is also of paramount importance. As the market leader for roadside repair and recovery our members' safety is always considered when agreeing working practices. This will always be the case and members can rely on the AA to put safety first.</p> <p>The consequences of poor safety at the roadside can be fatal. AA working practices are designed to reduce the probability of accidents to a minimum although given the environment in which we provide roadside service it is not possible to eliminate this risk.</p>

<p>7. Growing the business: We are unable to grow the business in a manner that complements and sustains the brand</p> <p>Primary KPIs:</p> <ul style="list-style-type: none"> • Paid personal members • Insurance policies • Franchised driving instructors • Trading EBITDA 	<p>We may be unable to develop and grow new profitable business products and lines that complement the customer experience and which demonstrate standards and values that underlie our core brand.</p>	<p>We continue to pursue new opportunities that complement our core brand.</p> <p>Proposed new products and changes to existing products are put through our product development process and are reviewed by the Product Outcomes Forum, (which meets frequently throughout the year) and includes Executive and senior attendees from the various business areas together with Compliance and Risk oversight.</p>	<p>A new business strategy was announced in February 2018 to innovate and grow the Roadside business and invest to accelerate the growth of the Insurance business.</p> <p>We expect increased product innovation aligned to our Connected Car and insurance growth strategy.</p>	<p>The immediate impact is low as this is more a long-term matter.</p> <p>In the long term without our effective control framework which is in place, our products would become uncompetitive, less relevant to the market place and fail to keep pace with member and customer needs.</p> <p>We are uniquely positioned to play a central role in shaping the way the market reacts to emerging trends, such as Connected Car, electric and hybrid vehicle growth and changing ownership models.</p>
<p>8. Our people: Ineffective human resources to achieve the AA objectives</p>	<p>Failure to recruit, train, develop and retain employees who have the skills and experience required by the business. Employee costs excessive. Staff of insufficient calibre.</p>	<p>The AA operates an emerging talent programme to help develop employees through external qualifications. To attract and develop new talent we operate apprentice schemes for both indoor and outdoor roles.</p>	<p>Our recent employment engagement survey highlighted a number of cultural challenges and employee morale issues. A plan is in place to improve the AA as a place to work and we have established channels for open communication.</p> <p>Following the dismissal of Bob Mackenzie (see page 56 for further details) our corporate governance has been significantly improved by splitting the roles of CEO and Chairman.</p> <p>Simon Breakwell has initiated a number of senior management changes and a full review of our priorities to ensure we have the right resources focused on the correct activity. Significant re-organisations have taken place in our contact centres.</p>	<p>If the AA does not have the right people skills in sufficient numbers, this will impact on our ability to deliver our strategy and three-year plan and the level of customer service which is expected from the AA brand.</p>

<p>9. Debt leverage: We are unable to manage our debt</p> <p>Primary KPIs:</p> <ul style="list-style-type: none"> • Leverage • Interest cover • Trading EBITDA • Free cash flow before equity 	<p>The Company is unable to repay or refinance its debt at an acceptable price.</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.</p>	<p>The Group completed a further debt refinancing structuring this year taking advantage of the low interest rate environment to reduce near term debt. No debt is due to be repaid until 31 July 2020 (the A3 notes). In order for the Group to be able to refinance its borrowings, it is a key assumption of the Directors that the Capital Markets remain open to the Group. The Directors continue to be confident that they will be able to refinance these borrowings at an acceptable price. We will continue to make additional repayments to reduce the debt burden as opportunities for this arise.</p> <p>Whilst the Group remains highly leveraged, this further restructuring improves the ability of the Company to manage unforeseen financial shocks.</p>	<p>If this risk materialised, the Group's bondholders would appoint an administrative receiver to run the business for cash until all secured debt is repaid. However, the AA continues to be a high cash generating organisation and the likelihood is therefore very low. A downgrade of the Class A notes would impact our ability to refinance (see the viability statement). However, S&P have recently reaffirmed the current ratings. Interest rates may increase in the future and may therefore be higher when debt is due to be repaid or refinanced in July 2020.</p>
<p>9. Pension: We are unable to meet our pension liabilities</p> <p>Primary KPIs:</p> <ul style="list-style-type: none"> • Trading EBITDA 	<p>The Company has a large defined benefit (DB) pension scheme, currently in deficit, whose assets and obligations are subject to future variation from investment returns, longevity and other similar factors.</p>	<p>The UK pension scheme is supported by a company covenant and the assets and obligations of the scheme are kept under review. The DB scheme is closed to new entrants.</p>	<p>A pension consultation process with employees has been successfully completed and changes to the pension schemes implemented, including closure of the final salary pension scheme and move of participants to the Career Average Section, to mitigate future exposure on the pension liability risk. The Group is still exposed to future variation from investment returns, longevity and other similar factors. In June 2017, the Group completed the triennial valuation of the UK pension scheme agreeing a funding deficit of £366m. We have agreed a nine-year deficit recovery additional funding plan with the Trustee, taking into account the continued funding of the previous deficit.</p>	<p>With the potential continuing volatility in the markets and global economic uncertainty the likelihood of the risk of increasing pension deficits remains high.</p>

<p>10. Information security/Cyber crime/Data breach: We are unable to protect ourselves from a significant data breach or cyber security incident</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. A serious data breach occurs.</p>	<p>The AA has an ongoing programme of security improvements to 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.</p> <p>The AA benchmarks its security controls against the Center for Protection of National Infrastructure (CPNI) and associated Critical Security Controls (CSC).</p>	<p>While we have made further progress enhancing our IT security and defences against cyber-crime, the external environment continues to be increasingly hostile to all businesses. A third-party provider of services to the AA had an incorrectly configured server and this exposed data for 91,590 customers. The vulnerability in the third party's systems was closed promptly when it was identified. An exercise was undertaken to communicate with the affected customers and the matter was reported to the ICO and the FCA, although it did not arise in our regulated business. We consider this to be an emerging/evolving risk and will continue to take additional steps to improve our controls, taking guidance from external specialists.</p> <p>We have recently hired a Data Protection Officer and a new Information Security Officer to strengthen the management of this area.</p>	<p>As for any company the impact of this risk crystallising could be substantial. The external environment continues to be increasingly hostile to all businesses with cyber-attacks on companies continuing to be more sophisticated and more frequent.</p>
<p>11. Regulatory and legal environment: A changing regulatory environment may adversely affect our activities</p> <p>Material litigation against the AA</p>	<p>The changing regulatory environment could cause currently compliant services to become non-compliant, with material implications to customer offerings, pricing and profitability.</p> <p>Failure to comply with regulatory obligations could result in fines and reputational damage.</p> <p>Changes in Government legislation or taxation could impact the business model.</p>	<p>The AA has a zero appetite for systemic non-compliance with Legal and Regulatory requirements.</p> <p>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.</p> <p>Regular dialogue is maintained with the FCA, the Gibraltar Financial Services Commission and other regulatory bodies.</p> <p>Our Regulatory and Legal Change Committee tracks forthcoming changes and advises the business on changes required.</p> <p>Products are reviewed regularly to reaffirm they are fit for purpose.</p> <p>The AA has in house Legal and Compliance teams and also takes external legal advice.</p>	<p>Regulatory changes that have the potential to impact on this risk include implementation of the FCA's Insurance Distribution Directive and preparing for the Senior Managers and Certification Regime (SMCR) in 2018. A project is being initiated to prepare for the SMCR.</p> <p>We have updated our renewal processes to comply with the new requirements on price transparency.</p> <p>The new General Data Protection Regulation (GDPR) requirements come into force in May 2018. A major multi-disciplinary project has been put in place to prepare the AA for the changes to data protection that will come into effect.</p> <p>Duplicate cover: The previously reported remediation exercise relating to duplicate breakdown cover has now been concluded.</p> <p>The dismissal of Bob Mackenzie for gross misconduct has resulted in litigation which the AA will vigorously contest. See note 37.</p>	<p>As in previous years the regulatory environment is expected to continue to be dynamic with a continuing programme of regulatory initiatives. These additional requirements may drive further commoditisation into the market at the expense of superior service differentiation.</p> <p>Continued increases in IPT could make insurance products including Roadside Assistance less affordable for our customers.</p> <p>Involvement in litigation is time consuming and a distraction for the Board and the management team.</p>

<p>12. Brexit: Negative impact on the AA as a result of Brexit</p>	<p>At this stage of Brexit negotiations, it is difficult to fully identify and assess potential risks. The following have been highlighted as of potential concern for the AA:</p> <ul style="list-style-type: none"> - Passporting for insurers and other regulatory change - Impact on EU nationals in the UK and potential skill shortages - Increasing future costs of supplies and services received by the AA - UK recession as a result of Brexit reducing the demand for AA products and services 	<p>The AA's Brexit Committee meets to support the AA business in monitoring and understanding likely impacts of Brexit by:</p> <ul style="list-style-type: none"> - Coordinating and evaluating information in respect of the potential impact of changes to external laws, regulations and codes that affect the AA business - Considering any other matters as may be referred to the Committee by the Board and other groups/individuals within the AA Group in respect of the implications of Brexit on the business 	<p>This is a new risk and the uncertainty resulting from Brexit is already being reflected in various external and internal risks.</p>	<p>While at this stage in Brexit negotiations it is not possible to identify risks with certainty, concerns which may have a significant impact include:</p> <ul style="list-style-type: none"> - Potential impact on non UK domiciled panel members/insurers - Impact on the services we provide covering European travel - Consequences for EU nationals working for the AA - Uncertainty on future cost base where goods/services are received from the EU/abroad - Changes to regulation - Potential recession and changes in consumer behaviour impacting on demand for our products and services
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Further information on the financial risks and management objectives and policies, including market, credit and liquidity risks, is included in note 28 of the financial statements.

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 2018

Revenue: Group revenue increased by £17m or 0.2% from £930m in the year ended 31 January 2017 to £947m in the year ended 31 January 2018. The increase in revenue was driven principally by the strong performance of Roadside.

Roadside Assistance: Roadside Assistance revenue increased by £5m or 0.7% from £742m in the year ended 31 January 2017 to £747m in the year ended 31 January 2018. This reflected the robust performance of B2B with an increase in pay-for-use volumes as well as higher ancillary sales. This offset the decline in paid personal members as well as the anticipated reduction in added value accounts. Roadside Assistance Trading Revenue includes the consolidated results from the 100% acquisition of AA Cars.

Driving Services: Driving Services Trading revenue increased by £2m or 3.1% from £64m in the year ended 31 January 2017 to £66m in the year ended 31 January 2018.

Insurance Services: Insurance Services revenue increased by £2m or 1.5% from £131m for the year ended 31 January 2017 to £133 in the year ended 31 January 2018. This was due to the growth in motor policies.

Exceptional Revenue Provision: We released £1m from the exceptional revenue provision in the year, relating to the £7m exceptional revenue provision for duplicate breakdown cover that we created in the prior year. In total we had provided £10m for refunds to customers of which £3m was charged to exceptional finance costs in the prior year. We agreed a programme of remediation with the regulatory authority and this programme is now substantially complete. The release of £1m reflects what we believe to be the final position for this programme. (See note 22 for further information.)

Cost of sales: Cost of sales increased by £17m or 5% from £339m in the year ended 31 January 2017 to £356m in the year ended 31 January 2018 reflecting higher costs from third-party garaging due to workload peaks and the higher number of breakdown attended.

Administrative and marketing expenses: Administrative and marketing expenses decreased by £26m or 8.6% from £304m in the year ended 31 January 2017 to £278m in the year ended 31 January 2018. The decrease in administrative and marketing expenses was primarily driven by the exceptional pension past service credit of £34m arising from the benefit changes implemented during the year for the AAUK pension scheme.

Share of profits of joint venture and associates: Share of profits of joint venture and associates decreased by £1m from £1m in the year ended 31 January 2017 to £nil in the year ended 31 January 2018.

Operating profit: Operating profit increased by £25m or 8.7% from £288m in the year ended 31 January 2017 to £313m in the year ended 31 January 2018. The increase in operating profit was primarily driven by the decrease in administrative and marketing expenses described above.

Finance costs: Finance costs decreased by £18m or 9.7% from £185m in the year ended 31 January 2017 to £167m in the year ended 31 January 2018. The decrease in finance costs was driven by the lower debt repayment premium and penalties and lower interest on external borrowings following the refinancing in the prior year.

Finance income: Finance income remained flat at £1m in both the years ended 31 January 2018 and 31 January 2017.

Taxation: Taxation increased by £4m from £27m in the year ended 31 January 2017 to £31m in the year ended 31 January 2018. The increase in tax expense was largely as a result of profits increasing by £43m which accounts for £8m of tax at the effective rate of tax of 19.1%.

Trading EBITDA

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

Trading EBITDA decreased by £13m or 3.2% from £406m in the year ended 31 January 2017 to £393m in the year ended 31 January 2018. The decrease in Trading EBITDA was primarily driven by Roadside Assistance as outlined below.

Roadside Assistance: Roadside Assistance Trading EBITDA decreased by £20m or 5.5% from £366m in the year ended 31 January 2017 to £346m in the year ended 31 January 2018. Trading EBITDA margins reduced from 49.3% in the year ended 31 January 2017 to 46.3% in the year ended 31 January 2018. The decrease in Trading EBITDA and Trading EBITDA margin was driven by the decline in membership numbers and business customers, the increased costs of third-party garaging and wage inflation.

Driving Services: Driving Services Trading EBITDA increased by £2m or 10% from £20m in the year ended 31 January 2017 to £22m in the year ended 31 January 2018. Trading EBITDA margins increased from 31.3% in the year ended 31 January 2017 to 33.3% in the year ended 31 January 2018. The increase in Trading EBITDA and the Trading EBITDA margin was driven by efficiency savings.

Insurance Services: Insurance Services Trading EBITDA increased by £3m or 3.9% from £76m in the year ended 31 January 2017 to £79m in the year ended 31 January 2018. Trading EBITDA margins increased from 58.0% in the year ended 31 January 2017 to 59.4% in the year ended 31 January 2018. The increase Trading EBITDA reflected the growth of the motor book, the focus on the more profitable business lines and cost savings.

Head Office Costs: Head Office Costs decreased by £2m or 3.6% from £56m in the year ended 31 January 2017 to £54m in the year ended 31 January 2018. The decrease in head office costs is primarily driven by efficiency savings.

Management discussion and analysis – Consolidated statement of cash flows

Net cash flow from operating activities before tax: £369m in the year ended 31 January 2017 compared to £338m in the year ended 31 January 2018. This was due to a decrease in profit before tax and negative working capital movements.

Tax paid: Cash outflow from tax paid was £23m in both years ended 31 January 2017 and 31 January 2018.

Investing activities: Cash flow from investing activities was an inflow of £48m in the year ended 31 January 2017 compared to an outflow of £43m in the year ended 31 January 2018. The prior year inflow primarily related to the proceeds from the disposal of our Ireland operations.

Financing transactions: Cash outflow from financing transactions was £102m in the year ended 31 January 2017 compared to £96m in the year ended 31 January 2018. The decrease in cash outflows on financing transactions related to lower repayment of debt premium and penalties in the current year.

Interest paid on borrowings: Cash outflow from the interest paid on borrowings was £143m in the year ended 31 January 2017 compared to £136m in the year ended 31 January 2018. The decrease in interest paid on borrowings is due to the refinancing in the prior year.

Payment of finance lease capital and interest: Cash outflow from the payment of finance lease capital and interest was £50m in the year ended 31 January 2017 compared to £46m in the year ended 31 January 2018. The decrease in cash outflows from payment of finance lease capital and interest was primarily driven by the timing of driving school finance lease disposals and the timing of the associated end of lease termination payments.

Dividends paid: Cash outflow from dividends paid was £60m in the year ended 31 January 2017 and £80m in the year ended 31 January 2018.

By order of the Board

M Clarke
Director

14 June 2018

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 2018.

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

Martin Clarke	Chief Financial Officer	
Gillian Pritchard	Director	
Mark Strickland	Director	Appointed on 7 August 2017
Mark Millar	Director	Resigned on 17 April 2018
Bob Mackenzie	Executive Chairman	Dismissed on 1 August 2017
Mark Millar	Company Secretary	Resigned on 17 April 2018
Catherine Hammond	Company Secretary	Appointed on 17 April 2018

AA Intermediate Co Limited is a 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 2018 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

Driver distraction

During 2017, The AA Trust continued to focus on the very important safety risk of driver distraction, building further on the success of the awareness campaigns we ran during the previous year.

We worked closely with our advertising agency, adam&eveDDB, to make a short advertisement 'Designated Driver' to highlight the dangers of texting at the wheel. This was a hard-hitting approach, using the slogan, 'You are twice as likely to crash text driving as drink driving'.

This won several prestigious awards including gold awards at both The British Arrows Awards (UK's most respected marketing awards) and the Clios (leading American/international creative awards).

We continued the campaign in association with the FIA Foundation which included:

- Hundreds of external posters on bus shelters and ad sites depicting the singer Pharrell Williams
- Just prior to Christmas releasing a hard-hitting anti-text driving video entitled "Make it home for Christmas". It was made by M&C Saatchi and Mad Ruffian, set to the 1943 Bing Crosby hit "I'll be home for Christmas". It shows a young girl texting her father while he is driving home for Christmas and the consequences of his actions. It received global coverage and appeared on the Today Show in Los Angeles

The full Driver Distraction Campaign #nevertexdrive was also shortlisted for the Broadcast Award at the PRCA Awards.

AA President Edmund King OBE also worked with the Road Safety Minister and Think! Campaign and won their agreement to pay for the distribution of the short advertisement in cinemas and Video on Demand across the UK. The ad was used as the cornerstone of our campaign with the DFT to raise awareness of the new penalties introduced for using a hand-held mobile phone on 1 March 2017.

Directors' report (*continued*)

This achieved widespread national coverage from BBC Breakfast TV to BBC Crime Watch. We are grateful to the FIA Road Safety Grant Programme for a contribution of 29,000 euros towards the campaign.

Drive Electric

The AA Trust developed a new free course, Drive Electric, to show drivers how to get the best out of driving an electric vehicle. The course is being piloted at the Milton Keynes EV Driving Experience Centre, located in a 4,000 sq ft, state-of-the-art showroom. It will help inform the town's residents and visitors about the benefits of electric vehicle ownership in a relaxed setting. Showcasing the latest EVs from a range of leading vehicle manufacturers, visitors will be able to discuss all elements of owning and running an electric vehicle, as well as having the option to test a range of cars on local roads.

AA campaigns

Smart motorways: We are campaigning for more lay-bys on smart motorways where the hard-shoulder is used as a running lane as we believe safety is compromised.

Street lights: We have raised concerns on some roads where coroners have indicated that turning off streetlights has led to deaths.

Potholes: We campaign for ring-fenced funds to improve the state of the roads and raised the issue highlighted by a coroner that lack of repairs can lead to deaths of cyclists.

Air quality: We have pushed for local authorities to target the 10% of polluters that cause 50% of the issue rather than 'demonising' all diesels.

Cost of driving: We have warned that increases in Insurance Premium Tax could make it unaffordable for many young drivers or lead to more uninsured drivers. We continue to monitor fuel prices with a monthly report.

Changes to the Highway Code: We have written to and met the Road Safety Minister to suggest various changes to the Highway Code to make motorways safer for drivers, recovery workers and the emergency services, following the deaths of two non-AA recovery workers on the hard shoulder.

Caught in a trap: We have sent a dossier to the Transport Secretary on how to improve the enforcement of parking and speeding offences.

Future car: We have promoted the take-up of electric and hybrid vehicles through a partnership with Chargemaster, the leading supplier of electric charging points. AA president, Edmund King OBE, developed a blog on 'Living with an EV' and has spoken at numerous conferences on the issue.

Health and Safety

We are dedicated to providing a sustainable, expert and dynamic service to our customers that demonstrates we care by delivering operational excellence through high standards of health, safety and environmental (HS&E) management. In line with our policy, we aim to continually improve our HS&E performance, always seeking to reduce any risks. We believe in always doing the right thing and in doing it safely, without unnecessary risk to people's health or to the environment.

To demonstrate our commitment we continue to have our management system externally audited to the OSHAS18001 standard.

Directors' report (*continued*)

While DriveTech is the business that is in scope for certification purposes, the management system applies to all our operations; they are internally audited for the effective implementation of it. Alongside this audit programme we monitor the effectiveness of our management strategies through regular performance reviews with senior management. The Roadside operation continues to be certified to PAS43, the publicly available management system specification for the safe working of vehicle breakdown and recovery operations. We require all of our garage agents to hold this standard too.

We continue to maintain our record of zero fatalities. The number of major injuries we report to the Health and Safety Executive (HSE) remains lower than the national rate for industries operating in a similar environment.

We continued to maintain our high gas safety standards with no Health and Safety Executive or Gas Safe action being taken.

Last year we reported that, following a change in our procedures to encourage a focus on safety with our patrols, we had seen an increase in accident numbers. Significant focus has been given to this area throughout this year to address the increase. Highlights this year include:

- Behavioural safety programme trialled
- New communication platforms utilised to deliver the safety message, including an HSE Blog for managers of our field based teams and dedicated quarterly team safety briefings for the patrol force
- Updating and re-focusing our HSE induction training for patrols
- Trialling new tools and equipment to further minimise safety risks

As a result of this focus and effort, we are very pleased to report that, this year, we have achieved not only the lowest number of accidents and reportable incidents (reportable under the Reporting of Diseases and Dangerous Occurrences Regulations (RIDDOR)) in the last five years, but also the lowest frequency rates for that period too. Our outstanding near miss reporting also continues to enable us to make a positive impact on risk reduction.

Our People

Achieving our strategic priorities depends on our people. They represent our Company among customers and communities. Our aim is to be a great place to work, providing interesting and challenging opportunities, excellent career progression, a collaborative, inclusive and values-based culture for our people. This is the key to creating value for all our stakeholders which is why our people are identified as a principal risk to the successful and sustainable operation of our service. The most significant areas which impact this risk are:

- Attracting the right talent/our employer brand
- Retaining talent through development, engagement and wellbeing
- Gender and diversity
- Anti-corruption and anti-bribery

These areas are controlled through our policies and processes as well as the monitoring of our management and control strategies through regular reviews with senior management. Both internal and external audits are undertaken as part of the ISO certifications relating to our road operations.

Attracting talent and developing our employer brand

This year we launched the new AA careers website www.theaacareers.co.uk which won an award in the 2017 National Online Recruitment Awards (NORAs) against some stiff competition. The NORAs views the recruitment sector from the perspective of the jobseeker, shining a light on the very best examples in our industry. Organisations in our category included LV=, McLaren, British Gas, npower and The National Trust.

Directors' report (*continued*)

To deliver the required attraction levels we have adopted a combination of recruitment channels all with a new common creative theme and messaging, to underscore the new central careers site employer brand message: Ready for Anything. We also entered a partnership for candidate management to ensure we're able to deal with the volume of applications and take care of the candidate experience.

This fundamental change in recruitment strategy and brand messaging has helped attract over 30,000 candidate applications (up 200%) and recruit almost 700 new employees during 2017.

The AA currently offers Level 2/3 apprenticeship programmes within our indoor operations, with plans to introduce these schemes across the organisation in the near future.

We continued to actively support the redeployment of armed services personnel into civilian roles, promoting AA job opportunities through both the CTP and Early Re-Settlement Magazine.

Wellbeing

Providing support for employee health and wellbeing is important to our people strategy. We provide an Employee Assistance Programme which provides free confidential 24/7 support for our people both online and over the phone. Qualified counsellors support on a range of home and work issues including medical concerns.

As one of the leading causes of illness among our people, mental health is an area of growing importance to our business. Working alongside Ben, a not-for-profit organisation which partners with the automotive industry, we have delivered a comprehensive mental health awareness training programme to all line managers who work within our Customer Operation function.

Engagement with our people

This year we ran our first engagement survey for five years. It was called OurVoice to represent all our colleagues. As employee engagement is an output of working for a company, it was important that consistency of behaviour was determined as part of the survey. Therefore, we decided to use a cultural index measurement rather than a more traditional employee engagement scoring system. This gave us a better understanding of the current employee experience and a better insight into our culture. It assessed how it feels to work in the AA as well as how we work with our colleagues and our customers. We had an excellent response with 78% participation and over 6,000 comments. The four stand out areas for action were:

- Respecting and supporting customer facing teams and providing more support for them
- Improving cross-team working
- Identifying ways to improve and increase opportunities for development and career progression
- Involving employees in sharing their ideas to improve the business

The survey results have been shared Group wide with local and functional action plans currently being developed for implementation in the year to 31 January 2019.

Throughout this year we have focused on improving Company-wide communication, setting up a Communication and Engagement function to better support our engagement strategy. It's important that our people have a voice and the opportunity to share their thoughts, feedback and suggestions for the business. Highlights from this year have included:

- 'Ask Simon', an email channel to our CEO Simon Breakwell was established. This has enabled our people to ask questions, contribute ideas to improve the business and to raise any concerns they may have
- Members of the Executive addressed hundreds of colleagues and managers at quarterly business update meetings
- The senior leadership team engaged many of our contact centre Team Leaders and Roadside Area Managers at team building and strategic planning sessions

Directors' report (*continued*)

We continue to work closely with our recognised Union, the Independent Democratic Union (IDU) as well as the Management Forum (an elected group for management-level employees) to ensure our employees' views are heard, as well as meeting our legal obligation for information and consultation. Meetings dedicated to the operational area are held with the IDU once a quarter to discuss all employee', related matters, including safety and workers' rights and we engage with them on matters related to pay.

It is important to us that our people are actively involved with our safety risk assessments so, wherever relevant, at least one Union representative joins the group who are carrying out the assessment to ensure they are represented.

We maintained our Employee Share Incentive Plan, giving our people an opportunity to invest in our brand and share in any success. Participants receive a free matching share for every share purchased as well as shares which represent a dividend on their holding. As at the 31 January 2018, 33% of our eligible employees participated in the plan.

Developing high performance culture

This year we introduced Evolve, our Emerging Talent Programme which offers a range of development qualifications for employees at every stage in their career as well as for new Apprentices into the business. It enables us to nurture emerging talent through offering apprenticeship Pathways (industry recognised qualifications) to help our people develop their skills, knowledge and expertise while learning on-the-job, supporting their career progression. We have expert apprenticeship partners to provide support to our people every step of the way on their chosen pathway.

We rolled out the Learning Management System which we had developed in the latter part of 2016 which has enabled us to more effectively support our teams in improving their skills and continuous personal development. It provides us with a holistic view of pan-AA development with some of the highlights in its first year of release being:

- Over 7,000 employees have completed online learning (excluding mandatory E-Learning)
- Almost 29,000 mandatory E-Learning modules have been issued
- New governance process implemented to ensure consistency and alignment of new training requests to employees' development plans
- Management of all regulated training requirements ensuring our people have the right accreditation to maintain the level of service to our members and customers
- The minimum training all staff are issued with when they join our Company, and then on a scheduled basis throughout their career are:
 - Data Protection
 - Information Security
 - Conduct Risk
 - Financial Crime Prevention
 - Complaints Handling
 - Equality and Diversity
 - Anti-Bribery
 - Treating Customers Fairly
 - Health and Safety

Whistleblowing Policy

A Whistleblowing policy encourages employees to confidently raise concerns internally so that these can be investigated in an independent, timely and effective manner. This helps us to ensure that our commitment to conducting our business with honesty and integrity is met. During the year, ten cases were escalated for review by HR and the Executive Risk and Compliance Committee, all have been investigated and concluded. Some of the consistent themes included allegations regarding staff conduct, management behaviour, discrimination and performance management.

Directors' report (*continued*)

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.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and 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) and the Company financial statements in accordance with Financial Reporting Standard (FRS) 101. 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.

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 £50 million of cash and cash equivalents of which £42 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.

Directors' report (*continued*)

Dividend

The Group has paid a dividend of £80m (2017: £60m) during the year.

Post balance sheet events

Details of post balance sheet events can be found in note 37.

By order of the Board

M Clarke
Director

14 June 2018
Fanum House
Basing View
Basingstoke
Hampshire
RG21 4EA

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

Opinion

We have audited the financial statements of AA Intermediate Co Limited for the year ended 31 January 2018 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Financial Position, the Consolidated Statements of Changes in Equity, the Consolidated Statement of Cash Flows and the related notes 1 to 37 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".

In our opinion, the financial statements:

- give a true and fair view of the group's and of the parent company's affairs as at 31 January 2018 and of the group's profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the group and parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the group's or the parent company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

**INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF AA INTERMEDIATE CO LIMITED
(continued)**

Opinions 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; and
- the strategic report and directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or directors' report.

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

- adequate accounting records have not been kept, 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

Responsibilities of directors

As explained more fully in the directors' responsibilities statement (see page 22), the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

Use of our report

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.

Kathryn Barrow (Senior Statutory Auditor)
For and on behalf of Ernst & Young LLP
London
15 June 2018

Consolidated income statement

for the year ended 31 January

	Note	2018 £m	2017 £m
Continuing operations			
Trading Revenue	2	946	937
Exceptional revenue provision	5	1	(7)
Group Revenue	2	947	930
Cost of sales		(356)	(339)
Gross profit		591	591
Administrative & marketing expenses		(278)	(304)
Share of profits of joint venture and associates, net of tax		-	1
Operating profit	4	313	288
Trading EBITDA	2	393	406
Share-based payments	34	(7)	(12)
Pension service charge adjustment	2	(10)	(8)
Amortisation and depreciation	11, 13	(68)	(66)
Operating profit before exceptional items		308	320
Exceptional operating items	5	5	(32)
Operating profit	4	313	288
Finance costs	6	(167)	(185)
Finance income	7	1	1
Profit before tax		147	104
Tax expense	10	(31)	(27)
Profit for the year from continuing operations		116	77
Discontinued operations			
Profit for the year from discontinued operations	3	-	80
Profit for the year		116	157

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

Consolidated statement of comprehensive income

for the year ended 31 January			
	Note	2018 £m	2017 £m
Profit for the year (including discontinued operations)		116	157
Other comprehensive income on items that may be reclassified to profit and loss in subsequent years			
Exchange differences on translation of foreign operations		(1)	2
Effective portion of changes in fair value of cash flow hedges		8	13
Tax effect	10	(3)	(1)
		4	14
Other comprehensive income on items that will not be reclassified to profit and loss in subsequent years			
Remeasurement gains / (losses) on defined benefit schemes	25	120	(99)
Tax effect	10	(21)	17
		99	(82)
Total other comprehensive income		103	(68)
Total comprehensive income for the year		219	89

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

Consolidated statement of financial position

		as at 31 January	
	Note	2018 £m	2017 £m
Non-current assets			
Goodwill and other intangible assets	11	1,296	1,276
Property, plant and equipment	13	127	131
Investments in joint ventures and associates	14	6	6
Deferred consideration	16	3	-
Deferred tax assets	10	30	62
		1,462	1,475
Current assets			
Inventories	15	7	6
Trade and other receivables	16	173	164
Amounts owed by parent undertakings	18	1,214	1,214
Cash and cash equivalents	17	50	136
		1,444	1,520
Total assets		2,906	2,995
Current liabilities			
Trade and other payables	19	(497)	(502)
Amount due to parent undertakings	18	(22)	-
Current tax payable		(10)	(11)
Provisions	22	(13)	(19)
		(542)	(532)
Non-current liabilities			
Borrowings and loans	20	(2,736)	(2,819)
Finance lease obligations	29	(16)	(20)
Defined benefit pension scheme liabilities	25	(240)	(395)
Provisions	22	(4)	(11)
Deferred consideration	19	(11)	-
		(3,007)	(3,245)
Total liabilities		(3,549)	(3,777)
Net liabilities		(643)	(782)
Equity			
Share capital	23	-	-
Currency translation reserve	24	-	1
Cashflow hedge reserve	24	5	2
Retained earnings	24	(648)	(785)
Total equity attributable to equity holders of the parent		(643)	(782)

Signed for and on behalf of the Board on 14 June 2018 by

M Clarke
Director

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

Consolidated statement of changes in equity

	Attributable to the equity holders of the parent				
	Share capital £m	Currency translation reserve £m	Cashflow hedge reserve £m	Retained earnings £m	Total £m
At 31 January 2016	20	(1)	(10)	(832)	(823)
Profit for the year	-	-	-	157	157
Other comprehensive income	-	2	12	(82)	(68)
Total comprehensive income	-	2	12	75	89
Dividends	-	-	-	(60)	(60)
Share-based payments	-	-	-	12	12
Capital reduction	(20)	-	-	20	-
At 31 January 2017	-	1	2	(785)	(782)
Profit for the year	-	-	-	116	116
Other comprehensive income	-	(1)	5	99	103
Total comprehensive income	-	(1)	5	215	219
Other reserves	-	-	(2)	2	-
Dividends	-	-	-	(80)	(80)
At 31 January 2018	-	-	5	(648)	(643)

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

Consolidated statement of cash flows

for the year ended 31 January

	Note	2018 £m	2017 £m
Profit before tax from continuing and discontinued operations		147	188
Amortisation and depreciation	11, 13	68	67
Net finance costs	6, 7	166	184
Other adjustments to profit before tax		20	(62)
Working capital:			
Increase in trade and other receivables		(5)	(16)
(Decrease) / Increase in trade and other payables		(1)	6
(Decrease) / Increase in provisions		(13)	12
Difference between pension charge and cash contributions		(44)	(10)
Total working capital adjustments		(63)	(8)
Net cash flows from operating activities before tax		338	369
Tax paid		(23)	(23)
Net cash flows from operating activities		315	346
Investing activities			
Capital expenditure		(63)	(70)
Proceeds from sale of fixed assets		18	18
Acquisitions and disposals, net of cash acquired or disposed of		1	99
Interest received		1	1
Net cash flows used in investing activities		(43)	48
Financing activities			
Proceeds from borrowings		250	700
Issue costs on borrowings		(7)	(6)
Debt repayment premium and penalties		(11)	(30)
Repayment of borrowings		(328)	(766)
Refinancing transactions		(96)	(102)
Interest paid on borrowings		(136)	(143)
Payment of finance lease capital		(41)	(43)
Payment of finance lease interest		(5)	(7)
Dividends paid		(80)	(60)
Net cash flows from financing activities		(358)	(355)
Net (decrease)/increase in cash and cash equivalents		(86)	39
Net foreign exchange differences		-	3
Cash and cash equivalents at 1 February	17	136	94
Cash and cash equivalents at 31 January	17	50	136

Consolidated statement of cash flows (continued)

The cash flows from operating activities are stated net of cash outflows relating to exceptional items of £29m (2017: £15m). This relates to the cost of business transformation of £14m (2017: £11m), non-recurring costs of IT system implementation and cost restructuring activities of £5m (2017: £7m), costs of reimbursing customers who bought duplicate breakdown cover of £8m (2017: £nil) and a net cash outflow from onerous property lease provisions in respect of vacant properties of £2m (2017: £3m inflow).

Other adjustments to profit before tax of £20m (2017: outflow of £62m) include impairment of goodwill £27m (2017: £nil), profit on sale of home services business £6m (2017: £nil), profit on sale of Ireland £nil (2017: £77m), share of loss from joint ventures and associates of £nil (2017: profit of £1m), share based payment charge of £7m (2017: £12m), profit on sale of fixed assets of £1m (2017 loss: £3m), credit for reversal of MVP share based payment charge (see note 34) £7m (2017: £nil) and impairment of investment in joint ventures of nil (2017: £1m).

Operating cash flows from discontinued operations were £nil (2017: £10m) (see note 3).

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

Notes to the consolidated financial statements

1 Basis of preparation and accounting policies

1.1 General information

The consolidated financial statements for the year ended 31 January 2018 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 England and Wales.

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

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 high renewal rates and lengthy customer tenure underpins this and in addition to the cash balances at the reporting date the Group has agreed undrawn credit facilities. The majority of the Group's borrowings are long term in nature with no borrowings due within 12 months from the date of signing of these financial statements. For the Group's longer term viability, it remains a key assumption of the Directors that the Group continues to have ready access to both public debt and equity markets to enable 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, including direct acquisition costs, 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 through other comprehensive income.

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.

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 and trade payables are not interest bearing and are recognised initially at fair value. 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 premiums and discounts on issue, are capitalised at inception and charged to the income statement over the term of the instrument using the effective interest method. Issue costs relating to the extinguishment of debt are charged to the profit and loss account immediately.

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 and fuel prices. The Group uses interest rate and fuel swap contracts to hedge these exposures.

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.

Cash flow 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 ongoing 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 and contingent liabilities

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. Material contingent liabilities are disclosed unless the transfer of economic benefits is remote. Contingent assets are only disclosed if an inflow of economic benefits is probable.

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 and provision for unearned premium.

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. In the Roadside segment, 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, provision for unearned premiums 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 for breakdown recovery 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 operating 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.

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 ongoing 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, amortisation of debt issue fees, 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.

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) Discontinued operations and disposals

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

- Represents a separate major line of business or geographical area of operations;
- Is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or
- Is a subsidiary acquired exclusively with a view to re-sale

Classification as a discontinued operation occurs on disposal or when the operation meets the criteria to be classified as held for sale, if earlier.

When an operation is classified as a discontinued operation, the comparative statement of comprehensive income is represented as if the operation had been discontinued from the start of the comparative year.

u) 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 ongoing 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.

Contingent consideration

The Group calculates contingent consideration based on the probability weighted payout approach.

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

Following the recent strategic announcement and reflecting the way that the Group will be managed going forward, the Group has determined that it has two key segments – Roadside and Insurance. Roadside incorporates the previous Roadside Assistance and Driving Services segments. Head Office costs have been allocated to these two key segments as these costs principally directly support the operations of these segments.

The Group has two reportable operating segments as follows:

- *Roadside*: 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. In addition this segment includes the Group's publishing and hotels business, the AA and BSM driving schools and DriveTech which provides driver training and educative programs.
- *Insurance*: This segment includes the insurance brokerage activities of the AA, primarily in arranging motor and home insurance for customers, its home emergency activities and its intermediary financial services business.

	2018 £m	2017 £m
Revenue		
Roadside	813	806
Insurance	133	131
Trading Revenue	946	937
Exceptional revenue provision (see note 22)	1	(7)
Group Revenue	947	930
Trading EBITDA		
Roadside	322	339
Insurance	71	67
Trading EBITDA	393	406
Share-based payments (see note 34)	(7)	(12)
Pension service charge adjustment	(10)	(8)
Amortisation and depreciation	(68)	(66)
Operating profit before exceptional items	308	320
Exceptional operating items (see note 5)	5	(32)
Operating profit	313	288
Net finance costs (see note 6 and 7)	(166)	(184)
Profit before tax from continuing operations	147	104

All segments operate principally in the UK. Turnover by destination is not materially different from turnover by origin.

Segment performance is primarily evaluated using the Group's key performance measure of Trading Revenue and Trading EBITDA as well as operating profit before exceptional costs.

2 Segmental information (continued)

Trading Revenue is revenue on a continuing basis adjusted for exceptional items. Trading EBITDA is profit after tax on a continuing basis as reported, adjusted for depreciation, amortisation, exceptional operating items, share-based payments, pension service charge adjustments, net finance costs and tax expense. This better reflects the Group's underlying performance.

The pension service charge adjustment relates to the difference between the cash contributions to the pension scheme for ongoing contributions and the calculated annual service costs.

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 does not view this information on a segmental basis.

The segmental analysis based on the previous segmental view is as follows:

	2018 £m	2017 £m
Revenue		
Roadside Assistance	747	742
Insurance Services	133	131
Driving Services	66	64
Trading Revenue	946	937
Exceptional revenue provision (see note 22)	1	(7)
Group Revenue	947	930

Trading EBITDA

Roadside Assistance	346	366
Insurance Services	79	76
Driving Services	22	20
Head Office costs	(54)	(56)
Trading EBITDA	393	406

Reconciliation of new segmental analysis

Revenue

	Roadside		Insurance	
	2018 £m	2017 £m	2018 £m	2017 £m
Former segment presentation				
Roadside Assistance	747	742	-	-
Insurance Services	-	-	133	131
Driving Services	66	64	-	-
Trading Revenue	813	806	133	131

2 Segmental information (continued)

Operating profit before exceptional items	Roadside		Insurance	
	2018 £m	2017 £m	2018 £m	2017 £m
Former segment presentation				
Roadside Assistance	346	366	-	-
Insurance Services	-	-	79	76
Driving Services	22	20	-	-
Head Office costs	(46)	(47)	(8)	(9)
Trading EBITDA	322	339	71	67
Share-based payments	(6)	(10)	(1)	(2)
Pension service charge adjustment	(8)	(7)	(2)	(1)
Amortisation and depreciation	(63)	(60)	(5)	(6)
Operating profit before exceptional items	245	262	63	58

3 Discontinued operations

On 11 August 2016 the Group completed the sale of its Irish business. The entities sold were AA Ireland Limited and its subsidiary undertakings. The Ireland business segment has therefore been reported as a discontinued operation as it represented a separate geographical area and the whole of the Irish operation was disposed of in the year.

As part of the transaction, the AA Ireland pension scheme, which is closed to future accrual, was transferred to AA Corporation Limited, a UK subsidiary of the Group and will continue to be the responsibility of the Group.

a) Results of discontinued operations

	2017 £m
Revenue	23
Expenses	(15)
Trading EBITDA	8
Depreciation and amortisation	(1)
Exceptional items	-
Operating profit	7
Profit on disposal of discontinued operations	77
Profit before tax	84
Tax	(4)
Profit for the year from discontinued operations	80

Tax includes a charge of £1m in relation to the trading results of the discontinued operation and a charge of £3m in relation to tax due on the licencing of the brand to the Irish business segment.

No additional tax arises on the profit on disposal of the Irish business segment mainly due to the application of the substantial shareholding exemption.

3 Discontinued operations (continued)

The profit from the sale of the Ireland business segment consisted of the following:

	2017 £m
Proceeds	133
Fees	(3)
Net assets	(53)
Profit on disposal of discontinued operations	77

Proceeds, net of fees were £130m and allowed £106m of the Senior Term Facility to be repaid on 31 August 2016. Under the terms of our borrowings, we have held back £24m from the net proceeds in ring-fenced available cash to be used for potential future acquisitions. The £24m was used to make a partial repayment of the STF on 13 July 2017.

b) Net cash flows of discontinued operations

	2017 £m
Operating cash flow	10
Investing cash flow	(3)
Total cash flows	7

During the year, the following cash flows arose as a result of Group acquisitions and disposals:

	2017 £m
Cash proceeds from sale of Irish business segment	133
Fees	(3)
Net cash proceeds from sale of Irish business segment	130
Cash held in Irish business at point of disposal	(31)
Acquisitions and disposals, net of cash acquired or disposed of	99

c) Net assets of discontinued operations at point of disposal

	2017 £m
Goodwill	26
Other intangible assets	9
Property, plant and equipment	3
Trade and other receivables	25
Cash and cash equivalents	31
Trade and other payables	(39)
Provisions - restructuring	(1)
Cumulative foreign exchange adjustment in reserves	(1)
Total	53

4 Operating profit

Operating profit from continuing operations is stated after charging:

	2018 £m	2017 £m
Amortisation of owned intangible assets	29	32
Depreciation of owned tangible fixed assets	14	12
Depreciation of leased tangible fixed assets	25	22
Operating lease rentals payable – land and buildings	3	4

5 Exceptional operating items

	2018 £m	2017 £m
Pension past service credit	34	-
Impairment of investment in joint venture (see note 14)	-	(1)
Duplicate breakdown cover	1	(7)
Impairment of goodwill (see note 26)	(27)	-
Exceptional operating items	(3)	(24)
Total exceptional items	5	(32)

The Group has recognised a one-off pension past service credit of £34m as a result of the benefit changes implemented during the year (see note 25). This comprised a £12m gain from closure of the Final Salary sections of the AAUK scheme, due to the assumed deferred pension revaluation being lower than the assumed pensionable earnings increases, and a £22m gain from the change in pension indexation in the CARE section from RPI-based to CPI-based, which is expected to be lower in the long term.

Exceptional revenue included £1m for duplicate breakdown cover release (2017: £7m provision). In addition, £nil (2017: £3m) was charged to exceptional finance charges, bringing the total exceptional amount for duplicate breakdown cover to £1m release (2017: £10m provision). See note 22 for further information.

Other exceptional operating costs include £24m relating to business transformation costs (2017: £14m), £1m gain on disposal of fixed assets (2017: loss £3m), £2m for IT systems transformation (2017: £3m), £9m improvement in onerous properties position (2017: loss £1m), £6m gain on the disposal of the home services book (2017: £nil), £7m credit for the reversal of share based payment charge relating to the former executive chairman (see note 34) (2017: £nil) and £nil mainly relating to non-recurring costs for cost restructuring activities (2017: £3m).

Costs from the current year refinancing in July 2017 and the prior period refinancing in December 2016 were directly attributable to the issue and repayment of loan notes and have therefore been included either in finance costs or in borrowings as debt issue fees (see notes 6 and 20).

6 Finance costs

	2018 £m	2017 £m
Interest on external borrowings	(132)	(147)
Finance charges payable under finance leases	(6)	(8)
Total ongoing cash finance costs	(138)	(155)
Ongoing amortisation of debt issue fees	(10)	(5)
Net finance expense on defined benefit pension schemes	(10)	(10)
Total ongoing non-cash finance costs	(20)	(15)
Debt repayment premium and penalties	(10)	(2)
Transfer from cashflow hedge reserve for extinguishment of cashflow hedge	2	(6)
Debt issue fees immediately written off following repayment of borrowings (see note 21)	(1)	(4)
Duplicate breakdown cover – interest on refunds (see note 22)	-	(3)
Exceptional finance costs	(9)	(15)
Total finance costs	(167)	(185)

Within interest on external borrowings is £7m (2017: £10m) of interest charged on the Senior Term Facility and £9m (2017: £8m) charged in relation to the interest rate swaps used to hedge the variable element of the Senior Term Facility (see note 21).

During the year, the Group repaid Class A1 notes of £175m (2017: £300m) and Class A4 notes of £55m (2017: £195m). As a result, the Group incurred an early repayment penalty of £10m (2017: £nil). As part of the refinancing during the prior year, the Group incurred a £2m premium cost in relation to the repayment of £165m of the Class B2 notes (see note 21). This premium was written off in the income statement.

During the year, there were £1m (2017: £4m) of amortised debt issue fees immediately written off following the refinancing.

During the year, the Group repaid £98m of the Senior Term Facility (2017: £106m) and made a non-cash adjustment to the cash flow hedge reserve of £2m. In the prior year, the Group transferred the fair value of the cash flow hedges related to the £106m repayment of the Senior Term Facility of £6m from other comprehensive income to the income statement.

7 Finance income

	2018 £m	2017 £m
Interest receivable	1	1
Total finance income	1	1

8 Staff costs

	2018 £m	2017 £m
Wages and salaries	241	248
Social security costs	25	25
Retirement benefit costs	26	29
Share-based payments expense	7	12
	299	314

The pension past service credit of £34m (2017: £nil) is excluded from retirement benefit costs above, see note 25.

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

	2018	2017
Operational	6,028	6,266
Management and administration	1,149	1,176
	7,177	7,442

9 Directors' remuneration

	2018 £m	2017 £m
Directors' remuneration	2	3
Long-term incentive plans	-	-
Aggregate remuneration in respect of qualifying services	2	3
Members of defined benefit pension schemes	2	2
	1	1

The amounts paid in respect of the highest paid director were as follows:

Remuneration	1	1
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The accrued pension of the highest paid director was £nil at 31 January 2018 (2017: £nil). The highest paid director had contributions to a money purchase pension plan of £56,160 (2017: £88,000).

10 Tax

The major components of the income tax expense are:

	2018 £m	2017 £m
Consolidated income statement		
Current income tax		
Current income tax charge	23	22
Adjustments in respect of previous years	-	(1)
	23	21
Deferred tax		
Effect of tax rate change on opening balances	(1)	2
Origination and reversal of temporary differences	10	2
Adjustment in respect of prior years	(1)	2
	8	6
Tax expense in the income statement	31	27

	2018 £m	2017 £m
Consolidated statement of comprehensive income		
Tax on the effective portion of changes in fair value of cash flow hedges	3	1
Tax on remeasurements of defined benefit pension liability	21	(17)
Income tax charged/(credited) directly to other comprehensive income	24	(16)

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

	2018 £m	2017 £m
Profit before tax	147	104
Tax at rate of 19.1% (2017: 20.0%)	28	21
Adjustments relating to prior year	(1)	1
Rate change adjustment on temporary differences	(1)	2
Expenses not deductible for tax purposes:		
- Share based payments	(1)	2
- Impairment of goodwill	5	-
- Other non-deductible expenses / non-taxed income	1	1
Income tax expense reported in the consolidated income statement at effective rate of 19.1% (2017: 22.1%)	31	27

In addition to the tax expense disclosed above, a charge of £nil (2017: £4m) has arisen on discontinued operations (see note 3).

The effective rate has been calculated by excluding the rate change adjustment that has arisen as a result of the future reduction in corporation tax rates affecting the carrying value of the deferred tax balances, the impact of share-based payments and the impairment of goodwill.

10 Tax (continued)

Deferred tax by type of temporary difference

	Consolidated statement of financial position		Consolidated income statement	
	2018 £m	2017 £m	2018 £m	2017 £m
Accelerated depreciation for tax purposes	8	8	-	1
Revaluations of land and buildings to fair value	(1)	(1)	-	-
Rollover relief	(2)	(2)	-	-
Pension	6	32	5	-
Revaluation of cashflow hedges	2	4	(1)	-
Short-term temporary differences	5	7	2	2
Losses available for offsetting against future taxable income	12	14	2	3
Deferred tax expense			8	6
Net deferred tax assets	30	62		

Reconciliation of net deferred tax assets

	2018 £m	2017 £m
At 1 February	62	52
Tax expense recognised in the income statement	(8)	(6)
Tax (expense) / income recognised in OCI	(24)	16
At 31 January	30	62

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 19% to 17% on 1 April 2020. These rates have been substantively 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 17.3% for the UK at 31 January 2018 (2017: 17.2%) and 12.5% for Ireland as at 31 January 2017. The UK rate has been adjusted to reflect the expected reversal profile of the Group's temporary differences.

The Group has brought forward tax losses which arose in the UK of £66m (2017: £76m) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose. A deferred tax asset has been recognised in respect of these losses.

The new corporate interest restriction legislation was introduced with effect from 1 April 2017. As the majority of the Group activity is taxed within the UK these restrictions have not had a significant impact on the deductibility of the Group's interest. The residual interest disallowance has not resulted in a material increase in the tax charge above.

11 Goodwill and other intangible assets

	Goodwill £m	Software £m	Total £m
Cost			
At 31 January 2016	1,198	184	1,382
Additions	-	56	56
Disposals	-	(29)	(29)
Disposed with sale of subsidiary	(26)	(14)	(40)
At 31 January 2017	1,172	197	1,369
Additions	25	51	76
At 31 January 2018	1,197	248	1,445
Amortisation and impairment			
At 31 January 2016	-	92	92
Amortisation	-	32	32
Amortisation within discontinued operations	-	1	1
Disposals	-	(29)	(29)
Disposed with sale of subsidiary	-	(4)	(4)
Exchange differences	-	1	1
At 31 January 2017	-	93	93
Amortisation	-	29	29
Impairment	27	-	27
At 31 January 2018	27	122	149
Net book value			
At 31 January 2018	1,170	126	1,296
At 31 January 2017	1,172	104	1,276

Within software, £32m (2017: £53m) relates to assets under construction which are not amortised.

Software additions comprise £12m (2017: £5m) in relation to internally developed assets and £39m (2017: £42m) in relation to separately acquired assets.

Goodwill additions of £25m (2017: £nil) relate to future growth prospects following the acquisition of Used Car Sites Limited (trading as AA Cars).

12 Business combinations

Acquisitions during the year ended 31 January 2018

On 1 October 2017 the company assumed control of Used Car Sites Limited (trading as AA Cars), a used car sales platform for a provisional consideration of £26m. At the point of acquisition Used Car Sites Limited had receivables of £1.8m, cash of £1.8m and payables of £2.4m. Used Car Sites Limited made a profit before tax of £nil for the year to 30 September 2017 and a profit before tax of £1m for the period 1 October 2017 to 31 January 2018.

On 1 March 2018 the Group completed the purchase of the entire share capital of Used Car Sites Limited. A payment of £12m was made to the former owners and £3m was paid into an escrow account and is payable to the former owners subject to certain conditions being met. These transactions cleared the balance of deferred consideration due within 1 year. This transaction left a remaining balance of £11m provisional deferred consideration which is due in more than one year based on the probability weighted payout approach. The range of potential contingent consideration is £nil-£21m. The assessment of goodwill arising on acquisition includes deferred consideration. The fair value attributed to the contingent deferred consideration is provisional as at 31 January 2018.

Acquisitions during the year ended 31 January 2017

There were no acquisitions during the year ended 31 January 2017.

13 Property, plant and equipment

	Freehold Land & Buildings £m	Long Leasehold Land & Buildings £m	Vehicles £m	Plant & equipment £m	Total £m
Cost					
At 31 January 2016	24	10	89	125	248
Additions	-	-	50	14	64
Disposals	-	-	(36)	(42)	(78)
Disposed with sale of subsidiary	-	(3)	(6)	(8)	(17)
Exchange difference	-	-	1	1	2
At 31 January 2017	24	7	98	90	219
Additions	-	-	40	14	54
Disposals	-	-	(34)	-	(34)
At 31 January 2018	24	7	104	104	239
Depreciation and impairment					
At 31 January 2016	7	4	22	93	126
Charge for the year	-	1	22	11	34
Disposals	-	-	(16)	(44)	(60)
Disposed with sale of subsidiary	-	(2)	(3)	(9)	(14)
Exchange difference	-	-	1	1	2
At 31 January 2017	7	3	26	52	88
Charge for the year	1	1	25	12	39
Disposals	-	-	(15)	-	(15)
At 31 January 2018	8	4	36	64	112
Net book value					
At 31 January 2018	16	3	68	40	127
At 31 January 2017	17	4	72	38	131

The net book amount of vehicles includes £68m (2017: £72m) held under finance lease agreements. The accumulated depreciation on these assets is £36m (2017: £26m).

The net book amount of other assets includes £nil (2017: £nil) in respect of plant & machinery held under finance lease agreements. The accumulated depreciation on these assets is £8m (2017: £8m).

Within plant and equipment £9m (2017: £4m) relates to assets under construction which are not depreciated.

14 Investments in joint ventures and associates

	2018			2017		
	Joint ventures £m	Associates £m	Total £m	Joint ventures £m	Associates £m	Total £m
At 1 February	2	4	6	2	4	6
Additions	-	-	-	1	1	2
Disposals	-	-	-	-	(1)	(1)
Share of profits	-	-	-	-	1	1
Dividend received	-	-	-	-	(1)	(1)
Impairment	-	-	-	(1)	-	(1)
At 31 January	2	4	6	2	4	6

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) ¹	England	Insurance
Intelematics Europe Limited (32% interest held) ²	England	Roadside

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

² The Group exercises joint control over Intelematics Europe Limited through its joint influence over key decision making.

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

During the prior year, the Group sold its interest in the shares of ACTA Assistance SA to ARC Europe SA. The other parties owning shares in ACTA Assistance SA and ARC Europe SA also sold their interest in ACTA Assistance for shares in ARC Europe so that the overall interest held in ARC Europe remained the same for each party. The Group also received a dividend from ACTA Assistance during the prior year of £1m.

15 Inventories

	2018 £m	2017 £m
Finished goods	7	6
	7	6

16 Trade and other receivables

	2018 £m	2017 £m
Current		
Trade receivables	135	139
Deferred consideration	3	-
Prepayments and accrued income	31	23
Other receivables	4	2
	173	164
Non-current		
Deferred consideration	3	-

Included in trade receivables are amounts of £75m (2017: £70m) relating to amounts due from insurance broking customers.

Non-current receivables of £3m (2017: £nil) relate to deferred consideration following the disposal of the consumer home services business.

17 Cash and cash equivalents

	2018 £m	2017 £m
Cash at bank and in hand – available	42	128
Cash at bank and in hand – restricted	8	8
	50	136

Cash at bank and in hand, short term deposits include £8m (2017: £8m) 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.

18 Amounts owed by/to parent undertakings

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

19 Trade and other payables

	2018 £m	2017 £m
Current		
Trade payables	100	103
Other taxes and social security costs	16	25
Accruals	56	56
Deferred income	233	239
Deferred consideration	15	-
Other payables	29	32
Obligations under finance lease agreements (note 29)	48	47
	497	502
Non-current		
Deferred consideration	11	-

Included in trade payables are amounts of £66m (2017: £82m) relating to amounts due to underwriters in respect of insurance broking activities.

Current and non-current deferred consideration relates to the acquisition of Used Car Sites Limited, see notes 12 and 37.

20 Borrowings and loans

	2018 £m	2017 £m
Borrowings (see note 21)	2,727	2,799
Interest rate swap used for hedging (see note 27)	9	20
	2,736	2,819

The interest rate swap liability is shown on a net basis as the liability is settled with each counterparty on a net basis. On a gross basis, the asset is £8m (2017: £19m) and the liability is £17m (2017: £39m).

21 Borrowings

	Expected maturity date	Interest rate	Principal £m	Issue costs £m	Amortised issue costs £m	Total at 31 January 2018 £m	Total at 31 January 2017 £m
Senior Term Facility	31 July 2021	5.71%	250	(4)	3	249	347
Class A1 notes	31 July 2018	-	-	-	-	-	175
Class A2 notes	31 July 2025	6.27%	500	(1)	1	500	499
Class A3 notes	31 July 2020	4.25%	500	(3)	2	499	499
Class A4 notes	31 July 2019	-	-	-	-	-	55
Class A5 notes	31 January 2022	2.88%	700	(37)	8	671	664
Class A6 notes	31 July 2023	2.75%	250	(4)	-	246	-
Class B2 notes	31 July 2022	5.50%	570	(16)	8	562	560
		4.52%	2,770	(65)	22	2,727	2,799

At 31 January 2018, the Senior Term Facility carried interest at a rate of LIBOR plus a margin of 1.75%. The variable element has been fully hedged using matching interest rate swap arrangements which fix LIBOR at 3.96% until 31 July 2018, then 6.67% until 31 January 2019. All other borrowings have fixed interest rates. The weighted average interest rate for all borrowings of 4.52% has been calculated using the effective interest rate and carrying values on 31 January 2018. The net decrease of £72m in the carrying amount during the current year consists of £328m for repayment of loan notes and £250m issue of loan notes (see table below) and a £6m change in unamortised issue costs.

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

	As at 1 February 2017 £m	Issue/repayment date 13 July 2017 £m	As at 31 January 2018 £m
Senior Term Facility	348	(98)	250
Class A1 Notes	175	(175)	-
Class A2 notes	500	-	500
Class A3 notes	500	-	500
Class A4 notes	55	(55)	-
Class A5 notes	700	-	700
Class A6 notes	-	250	250
Class B2 notes	570	-	570
Total £m	2,848	(78)	2,770

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 Consolidated statement of financial position at fair value at the year end.

21 Borrowings (*Continued*)

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 cash flow 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 of all interest due to expected maturity date, except the Class A5 and Class A6 notes which can be settled without penalty within 3 months and 2 months respectively of the expected maturity date.

On 13 July 2017, the Group issued £250m of Class A6 notes at an interest rate of 2.75%. £4m of costs associated with the issue of the A6 notes were capitalised. This consisted of £1m of premium and £3m of new issue fees.

From the proceeds of the A6 notes, the Group repaid the remaining £175m of A1 notes incurring an interest penalty of £7m and £55m of A4 notes incurring an interest penalty of £3m. In line with the Group accounting policy, this was accounted for as an extinguishment of debt and therefore issue costs associated with the A1 and A4 notes have been written off but totalled under £1m.

Following the sale of the Irish business during the prior year (see note 3), we held back £24m from the net proceeds in ring-fenced available cash to be used for potential future acquisitions or repayment of debt. On 13 July 2017 the £24m was used as part of a repayment of £98m of the Senior Term Facility. This was treated as an extinguishment of debt and therefore the issue costs of just under £1m associated with the repayment were written off. The balance of the STF was renegotiated and its maturity extended to 31 July 2021. This was treated as a modification and therefore the fees associated with this, which were under £1m, were capitalised.

On the 13 July 2017 the working capital facility was reduced from £150m to £75m. The fees associated with this were under £1m and were written off.

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 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 notes 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.

22 Provisions and contingent liabilities

	Property Leases £m	Restructuring £m	Other £m	Duplicate breakdown cover £m	Total £m
At 31 January 2016	13	1	1	-	15
Utilised during the year	(1)	(1)	(1)	-	(3)
Transfer to discontinued operations	-	(1)	-	-	(1)
Charge for the year	5	4	-	10	19
At 31 January 2017	17	3	-	10	30
Utilised during the year	(2)	(2)	-	(8)	(12)
Released during the year	(9)	(1)	-	(1)	(11)
Charge for the year	-	10	-	-	10
At 31 January 2018	6	10	-	1	17
Current	2	10	-	1	13
Non-current	4	-	-	-	4
At 31 January 2018	6	10	-	1	17
Current	6	3	-	10	19
Non-current	11	-	-	-	11
At 31 January 2017	17	3	-	10	30

The property lease provision primarily relates to dilapidations. These sums are mainly expected to be paid out over the next 11 years, however it will take 36 years to fully pay out all amounts provided for. The provision has been calculated on a pre-tax discounted basis. On the 23 March 2018, the Group signed a settlement agreement to exit from the onerous Halfords service Centres lease contracts, agreeing a final settlement of £2m. The restructuring provision relates to redundancy and other related costs following the restructuring of operations in the current and prior periods. Other provisions primarily comprised a provision for an onerous contract which was utilised in the previous financial year.

In the previous financial year, we became aware that there was some duplication of roadside assistance cover taken by a limited number of business-to-business customers who were personal Members and held AVAs (Added Value Accounts) with our banking partners. We proposed a programme of remediation for them which has the support of the regulatory authority. While some were unaware that they had duplicate cover, others chose to maintain this to receive the benefits of Membership. Through the review of data for the new Customer Relationship Management systems, we identified a group of customers for whom the benefit of holding both forms of cover were not clear. We proposed a programme of remediation for them which has the support of the regulatory authority. We provided a total of £10m for our estimate of the refunds due of which £7m was expected to relate to premiums previously paid for breakdown cover and £3m for interest payable on those premiums. During the period £5m has been paid out relating to premiums and £3m relating to interest, £1m has been released and we expect to pay out the remaining amount during the next financial year.

On 7 March 2018, the Group received notification that former Executive Chairman, Bob Mackenzie, who was dismissed for gross misconduct on 1 August 2017, had on 6 March 2018 issued a Claim Form in the High Court, Chancery Division against AA plc, its subsidiary Automobile Association Developments Limited and personally against a number of their directors and the Company Secretary. The Claim Form seeks a permanent injunction to retain his MVP shares and up to £225m in damages. As this litigation is active at the date of signing these financial statements, the directors of the Group have considered any potential financial impact. The Group has not made a provision for these amounts as the Group expects to be successful in rigorously defending these claims. However, the Group will incur legal costs of approximately £1m to defend these claims during the next two financial years which it would seek to recover from Bob Mackenzie when the litigation concludes.

23 Share capital

	2018 £	2017 £
Allotted, called up and fully paid		
20 ordinary shares of £1 each	20	20
	20	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.

In the prior year, the Company has undertaken a capital reduction to reduce the nominal value of share capital and increase the distributable reserves.

24 Reserves

	Currency translation reserve £m	Cashflow hedge reserve £m	Retained earnings £m	Total £m
At 31 January 2016	(1)	(10)	(832)	(843)
Retained profit for the year	-	-	157	157
Other comprehensive income:				
Exchange differences on translation of foreign operations	2	-	-	2
Remeasurement losses on defined benefit schemes (note 25)	-	-	(99)	(99)
Tax effect of remeasurement losses on defined benefit schemes (note 10)	-	-	17	17
Effective portion of changes in fair value of cash flow hedges	-	13	-	13
Tax effect of effective portion of changes in fair value of cash flow hedges (note 10)	-	(1)	-	(1)
Share-based payments (note 34)	-	-	12	12
Capital reduction	-	-	20	20
Dividends paid	-	-	(60)	(60)
At 31 January 2017	1	2	(785)	(782)
Retained profit for the year	-	-	116	116
Dividends paid	-	-	(80)	(80)
Other reserves	-	(2)	2	-
Other comprehensive income:				
Exchange differences on translation of foreign operations	(1)	-	-	(1)
Remeasurement gains on defined benefit schemes (note 25)	-	-	120	120
Tax effect of remeasurement gains on defined benefit schemes (note 10)	-	-	(21)	(21)
Effective portion of changes in fair value of cash flow hedges	-	8	-	8
Tax effect of effective portion of changes in fair value of cash flow hedges (note 10)	-	(3)	-	(3)
At 31 January 2018	-	5	(648)	(643)

24 Reserves (continued)

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 2018, total dividends of £4m (2017: £3, based on 20m shares at the time of distribution) 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 2018, the Company had distributable reserves of £23m (2017: £20m). The dividend paid during the current year was paid following receipt of a dividend of £80m from a subsidiary undertaking, AA Acquisition Co Limited.

25 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. The AAUK scheme has closed final salary sections and a Career Average Revalued Earnings (CARE) section which provides for benefits to accrue on an average salary basis. Since 2004, new entrants to the AAUK scheme accrue benefits in the CARE section but the AAUK scheme was closed to new entrants from 1 October 2016. On 1 July 2017 accrual ceased under the final salary sections and members were moved to the CARE section for future accrual of benefits. In addition, pension indexation in the CARE section will now be based on CPI inflation, rather than RPI inflation, from April 2018 onwards. During the prior year, following the sale of the Irish business by the Group (see note 3), AA Corporation Limited, a UK subsidiary of the Group, became the sponsor of the AAI scheme. The Group also operates an unfunded post-retirement Private Medical Plan (AAPMP), which is treated as a defined benefit scheme and it is not open to new entrants.

The AAUK scheme is governed by a corporate trustee whose board is currently composed of member-nominated and company-nominated directors. The AAI scheme is governed by a corporate trustee whose board is currently composed of company-nominated directors of which some are also members of the scheme. For both pension schemes the company-nominated directors include an independent director whom the trustee board directors have nominated as Chairman. The Trustee of each scheme is responsible for paying members' benefits and for investing scheme assets, which are legally separate from the Group.

The AAUK and AAI schemes are subject to full actuarial valuations every three years using assumptions agreed between the Trustee of each scheme and the Group. The purpose of this valuation is to design a funding plan to ensure that the pension scheme has sufficient assets available to meet the future payment of benefits to scheme members.

The valuation of liabilities for funding purposes differs to the valuation for accounting purposes, mainly due to the different assumptions used and changes in market conditions between different valuation dates. For funding valuation purposes the assumptions used to value the liabilities are agreed between the Trustee and Group with the discount rate, for example, being based on a bond yield plus a margin based on the assumed rate of return on scheme assets. For accounting valuation purposes the assumptions used to value the liabilities are determined in accordance with IAS19 with the discount rate, for example, being based on high quality (AA rated) corporate bonds.

The valuations have been based on a full assessment of the liabilities of the schemes which have been updated where appropriate to 31 January 2018 by independent qualified actuaries.

25 Pensions (continued)

The amounts recognised in the balance sheet are as follows:

	As at 31 January 2018			Total £m
	AAUK £m	AAI £m	AAPMP £m	
Present value of the defined benefit obligation in respect of pension plans	(2,491)	(50)	(45)	(2,586)
Fair value of plan assets	2,303	43	-	2,346
Deficit	(188)	(7)	(45)	(240)

	As at 31 January 2017			Total £m
	AAUK £m	AAI £m	AAPMP £m	
Present value of the defined benefit obligation in respect of pension plans	(2,515)	(53)	(59)	(2,627)
Fair value of plan assets	2,190	42	-	2,232
Deficit	(325)	(11)	(59)	(395)

The decrease in the deficit is due to the strong performance of plan assets, falling long-term inflationary expectations, changes in the demographic assumptions (reflecting the latest outlook for mortality rates), the past service credit in respect of the closure of the final salary sections and change to CPI-linked pension indexation for the CARE section within the AAUK scheme and Group contributions paid into the schemes. This was partially offset by falling discount rates over the period.

In June 2017 the Group completed the AAUK scheme triennial valuation as at 31 March 2016 agreeing a funding deficit of £366m with the pension trustees. The Group has committed to paying an additional £8m per annum from July 2017 to March 2019, £11m per annum from April 2019 to March 2021, uplifted in line with RPI from 1 April 2020 and £13m per annum from April 2021 to June 2026 uplifted in line with RPI from 1 April 2022 annually. In November 2013 the Group implemented an asset backed funding scheme which remains in place. The asset backed funding scheme provides a long-term deficit reduction plan where the Group makes an annual deficit reduction contribution of £13m increasing annually with inflation, until October 2038, secured on the Group's brands. The next triennial valuation of the AAUK scheme will take place as at 31 March 2019.

Using an inflation assumption of 3.1% and a discount rate assumption of 2.5%, the present value of the future deficit reduction contributions has been calculated. Based on these assumptions, the Group expects the present value of deficit reduction contributions to exceed the IAS 19 deficit. The Group notes that, in the event that a surplus emerges, it would have an unconditional right to a refund of the surplus assuming the gradual settlement of AAUK scheme liabilities over time until all members have left the scheme.

The Group has recognised a one-off past service credit of £34m as a result of the benefit changes described above. This comprised a £12m gain from closure of the Final Salary sections of the AAUK scheme, due to the assumed deferred pension revaluation being lower than the assumed pensionable earnings increases, and a £22m gain from the change in pension indexation in the CARE section from RPI-based to CPI-based, which is expected to be lower in the long term.

The last triennial valuation for the AAI scheme was as at 31 December 2016, the result of which was an increase in the Going Concern deficit with the contribution level remaining the same. The Group made deficit reduction contributions of c. £2m in the year ended 31 January 2018 and will continue to make annual deficit reduction contributions, increasing with inflation, until December 2023 or until an alternative agreement is signed with the trustees. The next triennial valuation of the AAI scheme will take place as at 31 December 2019.

In total, the Group is currently committed to pay c. £22m in on going employer contributions and c. £24m in deficit reduction employer contributions to its defined benefit plans (AAUK and AAI) in the year ending 31 January 2019.

25 Pensions (continued)

In November 2017 the Group completed a full accounting valuation of the AAPMP with a valuation date of 31 January 2017. This updated the previous full accounting valuation of the AAPMP that was performed as at 31 January 2013 and was projected forward to relevant reporting dates.

The 31 January 2017 full accounting valuation of the AAPMP revealed a reduction in reported deficit as a result of the actual level of medical premium inflation experienced being lower than that assumed over the period between full valuations and the impact of the latest longevity expectations.

	Assets £m	Liabilities £m	Income statement £m	Statement of comprehensive income £m
Balance at 1 February 2017	2,232	(2,627)	-	-
Current service cost	-	(31)	(31)	-
Past service gain	-	34	34	-
Interest on defined benefit scheme assets / (liabilities)	61	(71)	(10)	-
Amounts recognised in the income statement	61	(68)	(7)	-
Effect of changes in financial assumptions	-	(56)	-	(56)
Effect of changes in demographic expectations	-	65	-	65
Effect of experience adjustment	-	38	-	38
Return on plan assets excluding interest income	73	-	-	73
Amounts recognised in the statement of comprehensive income	73	47	-	120
Foreign exchange gain / (loss)	1	(1)	-	-
Contribution from scheme participants	1	(1)	-	-
Benefits paid from scheme assets	(64)	64	-	-
Ongoing employer contributions	21	-	-	-
Deficit reduction employer contributions	21	-	-	-
Movements through cash	(21)	63	-	-
Balance at 31 January 2018	2,346	(2,586)	-	-

25 Pensions (*continued*)

	Assets £m	Liabilities £m	Income statement £m	Statement of comprehensive income £m
Balance at 1 February 2016	1,850	(2,146)	-	-
Current service cost	-	(29)	(29)	-
Interest on defined benefit scheme assets / (liabilities)	68	(78)	(10)	-
Amounts recognised in the income statement	68	(107)	(39)	-
Effect of changes in financial assumptions	-	(613)	-	(613)
Effect of changes in demographic expectations	-	110	-	110
Effect of experience adjustment	-	81	-	81
Return on plan assets excluding interest income	323	-	-	323
Amounts recognised in the statement of comprehensive income	323	(422)	-	(99)
Foreign exchange gain / (loss)	5	(6)	-	(1)
Contribution from scheme participants	1	(1)	-	-
Benefits paid from scheme assets	(55)	55	-	-
Ongoing employer contributions	20	-	-	-
Deficit reduction employer contributions	20	-	-	-
Movements through cash	(14)	54	-	-
Balance at 31 January 2017	2,232	(2,627)	-	-

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 scheme assets split between those that have a quoted market price and those that are unquoted. Of the AAI scheme 43.5% (2017: 33.1%) of assets do not have a quoted market price.

25 Pensions (*continued*)

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

	2018		2017	
	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	174	352	184	258
Bonds/ Swaps	813	211	876	183
Property	88	183	81	168
Hedge funds	23	440	-	401
Cash / net current assets	17	2	37	2
Total AAUK scheme assets	1,115	1,188	1,178	1,012
Actual return on AAUK plan assets		132		388

Investment strategy

The AAUK trustee determines its investment strategy after taking advice from a professional investment adviser. The AAUK scheme's investment strategy has been set following an asset/liability review which considered a wide range of investment opportunities available to the Scheme and how they might perform in combination. Other factors were also taken into account such as the strength of the employer covenant, the long term nature of the liabilities and the funding plan agreed with the employer.

The trustee aims to achieve the scheme's investment objectives through investing in a diversified portfolio of growth assets which, over the long term, are expected to grow in value by more than low risk assets like cash and gilts. This is done within a broad liability driven investing framework that uses such cash, gilts and other hedging instruments like swaps in a capital efficient way. In combination this efficiently captures the trustee risk tolerances and return objectives relative to the scheme's liabilities. A number of investment managers are appointed to promote diversification by assets, organisation and investment style.

To diversify sources of return and risk, the AAUK scheme invests in many asset classes and strategies, including equities, bonds and property funds which primarily rely on the upward direction of the underlying markets for returns, and also hedge funds which also invest in asset classes like equities, bonds and currencies, but in such a way that relies more on the skill of the investment manager to add returns whilst hedging against downward market moves.

The trustee's investment advisors carry out detailed ongoing due diligence on funds in all asset classes from both operational and investment capability standpoints and any funds which are not expected to achieve their investment performance targets are replaced where possible.

25 Pensions (*continued*)

Pension plan assumptions

The principal actuarial assumptions were as follows:

%	AAUK		AAI		AAPMP	
	2018 %	2017 %	2018 %	2017 %	2018 %	2017 %
Pensioner discount rate	2.5	2.7	1.6	1.6	2.5	2.7
Non-pensioner discount rate	2.6	2.9	2.3	2.4	2.5	2.7
Pensioner RPI	3.3	3.5	-	-	3.3	3.5
Non-pensioner RPI	3.3	3.5	-	-	3.3	3.5
Pensioner CPI	2.2	2.4	1.6	1.5	2.2	2.4
Non-pensioner CPI	2.2	2.4	1.6	1.5	2.2	2.4
Rate of increase of pensions in payment (final salary sections) - pensioner	3.1	3.2	-	-	-	-
Rate of increase of pensions in payment (final salary sections) - non pensioner	3.1	3.2	-	-	-	-
Rate of increase of pensions in payment (CARE section) - pensioner	1.7	2.2	-	-	-	-
Rate of increase of pensions in payment (CARE section) - non pensioner	1.7	2.2	-	-	-	-
Pensioner increase for deferred benefits	2.2	2.4	1.6	1.5	-	-
Medical premium inflation rate	-	-	-	-	7.3	7.5

Mortality assumptions are set using standard tables based on scheme specific experience where available and an allowance for future improvements. For 2018, the assumptions used were in line with the SAPS (S2) series mortality tables (2017 – SAPS (S2) series) with future improvements in line with the CMI_2016 model with a 1.25% long-term rate of improvement (2017 – CMI_2015 model with a 1.5% long-term rate of improvement). The AAI scheme mortality assumptions are set using standard tables with scheme specific adjustments.

The AA schemes' overall assumptions are that an active male retiring in normal health currently aged 60 will live on average for a further 27 years and an active female retiring in normal health currently aged 60 will live on average for a further 29 years.

Sensitivity analysis

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 2018		
	AAUK £m	AAI £m	AAPMP £m
Increase of 0.25% in discount rate	126	2	2
Increase of 0.25% in Inflation rate	(100)	(1)	-
Increase of 1% in medical claims inflation	-	-	(9)
Increase of one year of life expectancy	(93)	(1)	-

25 Pensions (*continued*)

An equivalent decrease in the assumptions at 31 January 2018 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 AAUK scheme liabilities at 31 January 2018 is around 21 years.

Pension scheme risks

The AAUK and AAI schemes have exposure to a number of risks because of the investments they make in following their investment strategy. Investment objectives and risk limits are implemented through the investment management agreements in place with the schemes' investment managers and monitored by the Trustees by regular reviews of the investment portfolios. In addition, under guidance from their investment advisers the Trustees monitor estimates of key risks on an ongoing basis such as those shown below. A number of measures are taken to mitigate these risks where possible.

Credit risk - this is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. This risk mainly relates to the schemes' bonds and is mitigated by carrying out due diligence and investing only in bond funds which are well diversified in terms of credit instrument, region, credit rating and issuer of the underlying bond assets. To reduce risk further, the underlying bond assets within a fund are ring fenced, and the scheme diversifies across a number of bond funds.

Currency risk - the scheme is subject to currency risk because some of the scheme's investments are in overseas markets. The Trustee hedges some of this currency risk by investing in investment funds which hold currency derivatives to protect against adverse fluctuations in the relative value of its portfolio positions as a result of changes in currency exchange rates.

Market price risk - this is the risk that the fair value or future cash flows of a financial asset such as equities will fluctuate because of changes in market prices (other than those arising from interest rate, inflation or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. The scheme manages this exposure to overall price movements by constructing a diverse portfolio of investments across various markets and investment managers.

Financial derivatives risk – The scheme does not directly hold any financial derivatives but instead invests in investment funds which hold the derivatives required to hedge the scheme's interest rate, inflation and currency risks. The scheme also permits some of the investment managers to use derivative instruments if these are being used to contribute to a reduction of risks or facilitate efficient portfolio management of their funds. The main risks associated with financial derivatives include: losses may exceed the initial margin; counterparty risk where the other party defaults on the contract; and liquidity risk where it may be difficult to close out a contract prior to expiry. These risks are managed by monitoring of investment managers to ensure they use reasonable levels of market exposure relative to initial margin and positions are fully collateralised on a daily basis with secure cash or gilts collateral.

The AAUK scheme had hedged around 60% of interest rate risk and around 65% of inflation risk (of the liabilities) as at 31 January 2018 as part of a policy to reduce financial risks to the Scheme. The current longer term objective is to aim to hedge around 75% of both the interest rate risk and inflation risk of the liabilities; this will help to further reduce funding level volatility. More interest rate hedging will be added in due course as, and when, prevailing pricing is regarded as reasonable value in the circumstances, or if any other reasons drive a policy change on risk appetite.

26 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. CGUs represent the smallest group of assets that independently generate cash flow and whose cash flow is largely independent of the cash flows generated by other assets.

The carrying value of goodwill by CGU is as follows:

	2018	2017
	£m	£m
Roadside Assistance	874	874
Insurance Services	240	240
Driving Schools	-	26
Used Car Sites (see note 12)	25	-
DriveTech	31	32
	1,170	1,172

The Group has performed impairment testing at 31 January 2018 and 31 January 2017. 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 2021 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 9.6% (2017: 9.0%).

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.

As a result of this review the Driving Schools’ goodwill has been impaired by £26m (2017: £nil) and the Drivetech goodwill has been impaired by £1m (2017: £nil).

27 Financial assets and financial liabilities

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

Financial assets

	2018 £m	2017 £m
Loans and receivables		
Cash and cash equivalents	50	136
Trade receivables	135	139
Deferred consideration	6	-
Other receivables and accrued income	21	16
Amounts owed by parent undertaking	1,214	1,212
Total financial assets	1,426	1,503

Financial liabilities

	2018 £m	2017 £m
Measured at fair value through other comprehensive income		
Interest rate and fuel swaps used for hedging	9	20
Loans and borrowings		
Trade payables	100	103
Other payables	51	55
Deferred consideration	26	-
Obligations under finance lease agreements	64	67
Borrowings	2,727	2,799
Total financial liabilities	2,977	3,044

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.

27 Financial assets and financial liabilities (continued)

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 2018:

	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
Financial liabilities measured at fair value				
Interest rate and fuel swaps (note 20)	9	-	9	-
Deferred consideration (due in more than one year)	11	-	11	-
Liabilities for which fair values are disclosed				
Loan notes (note 21)	2,478	2,639	-	-

At 31 January 2017:

	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
Financial liabilities measured at fair value				
Interest rate and fuel swaps (note 20)	20	-	20	-
Liabilities for which fair values are disclosed				
Loan notes (note 21)	2,452	2,656	-	-

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 2018.

28 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.

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

	2018	2017
	£m	£m
Fixed rate instruments		
Financial liabilities	(2,532)	(2,518)
Effect of interest rate swaps	(250)	(348)
Net exposure to fixed rate instruments	(2,782)	(2,866)
Variable rate instruments		
Financial liabilities	(249)	(347)
Effect of interest rate swaps	250	348
Net exposure to variable rate instruments	1	1

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 2018 would have increased equity by £1m (2017: £2m) and would have had no impact on profit or cash because the Senior Term facility is hedged (see note 21). 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.

28 Financial risk management objectives and policies (continued)

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.

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
2018	135	129	4	-	2
2017	139	131	4	-	4

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

	2018 £m	2017 £m
At 1 February	2	2
Charge for the year	3	2
Utilised	(1)	(1)
Unused amounts reversed	(1)	(1)
At 31 January	3	2

28 Financial risk management objectives and policies (continued)

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 2018:

	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	-	117	117	2,282	832	3,348
Obligation under finance leases	-	52	10	7	-	69
Other payables and accruals	-	51	-	-	-	51
Contingent consideration	-	-	6	5	-	11
Trade payables	-	100	-	-	-	100
	-	320	133	2,294	832	3,579

Interest rate swaps used for hedging

Assets (inflow)	-	(7)	-	-	-	(7)
Liabilities	-	19	2	3	-	24
	-	12	2	3	-	17
	-	332	135	2,297	832	3,596

At 31 January 2017:

	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	-	126	641	1,536	1,195	3,498
Obligation under finance leases	-	51	13	8	-	72
Other payables and accruals	-	55	-	-	-	55
Trade payables	-	103	-	-	-	103
	-	335	654	1,544	1,195	3,728

Interest rate swaps used for hedging

Assets (inflow)	-	(14)	(8)	-	-	(22)
Liabilities	-	23	18	-	-	41
	-	9	10	-	-	19
	-	344	664	1,544	1,195	3,747

28 Financial risk management objectives and policies (continued)

Capital management

The Group considers its capital to be a combination of net debt and equity.

The capital structure at 31 January 2018 can be summarised as below:

	Expected maturity date	Interest rate %	Principal £m
Senior Term Facility	31 July 2021	5.71	250
Class A2 notes	31 July 2025	6.27	500
Class A3 notes	31 July 2020	4.25	500
Class A5 notes	31 January 2022	2.88	700
Class A6 notes	31 July 2023	2.75	250
Class B2 notes	31 July 2022	5.50	570
Total borrowings		4.52	2,770
Finance lease obligations			64
Cash and cash equivalents			(50)
Total net debt			2,784
Share capital			-
Total capital			2,784

The weighted average interest rate for all borrowings of 4.52% has been calculated using the effective interest rate and carrying values on 31 January 2018.

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 put service, innovation and data at the heart of the AA;
- to deliver targeted and strategic investment in our people, our products, our systems and operations;
- 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. 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.

In July 2017, we completed a further refinancing package which resulted in the extension of the maturity of debt and further savings in annual interest costs. We used some of our free cash flow partially to pay down debt.

The Group issued Class A6 notes for a principal amount of £250m under the multicurrency note programme listed on the Irish Stock Exchange and used the proceeds to redeem the remaining Class A1 and Class A4 notes. At the same time, the Group used available cash resources to reduce by £98m its senior term debt and extended that facility through the replacement of the existing Senior Term Facility with a new Senior Term Facility. The new facility extends the maturity of the senior term debt from 31 January 2019 to 31 July 2021.

The Class A6 notes were issued on 13 July 2017 and have an expected maturity date of 31 July 2023. The notes have a coupon of 2.75% payable semi-annually in arrears. The proceeds from the issue were used to redeem all of the remaining £175m 4.72% Class A1 notes and £55m 3.78% Class A4 notes plus make-whole payments that were paid on 31 July 2017.

As described above, a new Working Capital Facility of £75m, reduced from the previous £150m facility, was put in place to 31 July 2021 on a reduced margin. This remains undrawn.

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

The extension in maturity of debt means that the next repayment of borrowings is due in July 2020. The initial annual interest saving is expected to be c£3m for the years ending 31 July 2018 and 31 July 2019, then will increase to an annual interest saving of c£14m for the year ending 31 January 2020 as a result of the expiry of the existing hedging arrangements allowing the use of more of our free cash flow to pay down debt. In addition, there will be a saving of fees amounting to £0.6m following the reduction of the Working Capital Facility.

The refinancing is in line with our capital management strategy to reduce overall group borrowings as well as the associated interest cost.

The Company continues to evaluate the optimal refinancing strategy of its debt maturities and coupon payments including the A notes, B notes and Senior Term Facility. Early redemption of the A notes will result in make-whole interest penalties up to the date of maturity, the B2 note also has make-whole interest penalty provisions up to 31 July 2018, after which, a reducing sliding scale premium on redemption of the principal needs to be paid up to 31 July 2020. The cash generative nature of the business and the strategic priorities outlined for growth mean that we remain confident in our ability to service the interest obligations on our debt for the foreseeable future.

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:

	2018	2017
	£m	£m
Senior Term Facility	250	348
Class A notes	1,950	1,930
Less: cash and cash equivalents	(50)	(136)
Net Senior Secured Debt¹	2,150	2,142
Class B2 notes	570	570
Finance lease obligations	64	67
Net Debt	2,784	2,779
Net debt ratio ²	7.1x	6.7x
Senior leverage ratio ³	5.47x	5.2x
Class A free cash flow: debt service ⁴	3.3x	3.3x
Class B free cash flow: debt service ⁵	2.4x	2.3x

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

4 Ratio of last 2 months free cash flow to proforma debt service relating to the Senior Term Facility and Class A notes

5 Ratio of last 12 months free cash flow to proforma debt service

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 2018.

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 17). There are no other externally imposed capital requirements.

28 Financial risk management objectives and policies (continued)

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 generally 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.

Key Cash Release Metrics

	2018	2017
Net senior leverage ¹	5.47x	5.2x
Excess cash flow ²	£91m	£194m
Fixed charge cover ratio ³	3.0x	3.0x
Consolidated net income ⁴	£208m	£214m

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 and reduced by dividends.

29 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	
	2018	2017
	£m	£m
Leases expiring:		
Within one year	-	1
Between one and five years	3	10
After five years	37	23
	40	34
Income from operating sub-leases	-	(4)
Amounts included in onerous lease provisions	(1)	(4)
	39	26

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.

29 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:

	2018		2017	
	Present value of payments £m	Minimum payments £m	Present value of payments £m	Minimum payments £m
Within one year	48	52	47	51
Between one and five years	16	17	20	21
Total minimum lease payments	64	69	67	72
Less amounts representing finance charge	-	(5)	-	(5)
Present value of minimum lease payments	64	64	67	67

Capital commitments

Amounts contracted for but not provided in the financial statements amounted to £22m (2017: £14m).

30 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.

31 Auditor's remuneration

	2018 £m	2017 £m
Amounts receivable by the Company's auditor and its associates in respect of:		
Audit of financial statements of subsidiaries of the Company	1	1

The fee for the audit of these financial statements was £14,000 (2017: £12,000).

32 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	2018 £m	2017 £m
ACTA SA.	Call handling fees paid	-	2
ARC Europe SA.	Registration fees paid	4	1

Note that the Group's interest in ACTA SA. was sold in the prior year to ARC Europe SA (see note 14).

The outstanding balances with other AA plc group companies are as follows:

Entity	Relationship	2018 £m	2017 £m
AA Mid Co Limited	Immediate parent	1,205	1,205
AA plc	Indirect parent	9	9
		1,214	1,214

Cross-company guarantees

The Group 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.

33 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 Chief Executive Officer, Chief Financial Officer, Non-Executive Directors and the Executive Committee, as well as the former Executive Chairman until his dismissal.

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

	2018 £m	2017 £m
Short-term employee benefits	5	6
Share-based payments – MVP and LTBP shares (see note 34)	(2)	8
Total compensation paid to key management personnel	3	14

34 Share-based payments

	2018 £m	2017 £m
Share-based payments – MVP shares	4	8
Share-based payments – LTBP	1	2
Share-based payments – Retention	-	-
Share-based payments – staff share incentive plan	2	2
	7	12
Share-based payments – MVP shares – exceptional item	(7)	-
Total share-based payments	-	12

Management value participation shares (MVP shares)

On 23 June 2014, the Company 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 ordinary shares following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% (or above) per annum compound growth against the 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.

14.2% of the issued MVP shares were held in the Employee Benefit Trust (EBT) on 22 April 2016 awards were granted by the EBT to further key members of senior management over ordinary shares which convert from the remaining 14.2% (amounting to 8,520,000) MVP shares.

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

		2018	2017	2018	2017
	Vesting Date	No. of shares	No. of shares	Fair value per share £	Fair value per share £
June 2014 awards:					
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
December 2015 awards:					
A2 shares	23 June 2017	9,160,000	9,160,000	0.38	0.38
B2 shares	23 June 2018	9,160,000	9,160,000	0.40	0.40
C2 shares	23 June 2019	9,160,000	9,160,000	0.40	0.40
April 2016 awards:					
A2 shares	23 June 2017	2,840,000	2,840,000	0.35	0.35
B2 shares	23 June 2018	2,840,000	2,840,000	0.35	0.35
C2 shares	23 June 2019	2,840,000	2,840,000	0.35	0.35
Total		60,000,000	60,000,000		

Unvested A1 and A2 shares can also be converted on the fourth or fifth anniversary of admission and unvested B1 and B2 shares can also be converted on the fifth anniversary of admission.

34 Share-based payments (continued)

All MVP shares were valued using a Binomial model and 25% volatility assumption to calculate the fair value using risk-free interest rates in a range of 0.38% - 1.82%. The expected volatility reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

On 1 August 2017, the former Executive Chairman, who held 55% of the MVP shares, was dismissed for gross misconduct. Under the rules of the scheme he was deemed to be a bad leaver and therefore the Company has the right to request transfer (and failing compliance, transfer itself) all those MVP shares for a total consideration of 1 penny. The Company issued the transfer notice on 9 March 2018 and transferred the shares on 16 April 2018 to its Employee Benefit Trust. As per IFRS 2, the share-based payment charge in relation to his shares, has been reversed resulting in a credit to exceptional operating items in the income statement of £7m and a corresponding debit to equity.

Long Term Bonus Plan (LTBP)

As at 31 January 2018, the Company's EBT had issued 4 million conditional awards over market-purchased ordinary shares to certain key members of senior management at nil cost. 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 admission prices which is tested on the third, fourth and fifth anniversaries of admission to the London Stock Exchange and satisfaction of certain individual performance targets.

If the awards over A shares do not vest on the third or fourth anniversary of admission, then they are retested on the fourth and fifth anniversary. If the awards over B shares do not vest on the fourth anniversary of admission, then they are retested on the fifth anniversary.

The fair values of awards were calculated using a Monte Carlo simulation model. The expected volatility range of 20% - 32% reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

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

		2018	2017	2018	2017
		No. of shares	No. of shares	Weighted fair value per share	Weighted fair value per share
Vesting Date				£	£
A shares	26 June 2017	873,423	1,004,896	2.49	2.56
B shares	26 June 2018	859,069	993,060	1.98	2.07
C shares	26 June 2019	842,036	987,340	1.54	1.62
Total		2,574,528	2,985,296		

The number of ordinary shares over which awards are held has reduced by 410,768 due to leavers during the financial year. The difference between the 4 million issued awards and the current number of outstanding awards is due to leavers.

34 Share-based payments *(continued)*

Retention Award

On 19 December 2017, the Company issued 2 million conditional awards over market purchased ordinary shares to certain key members of senior management who were already in the LTBP scheme, at nil cost.

These shares were divided into two tranches, 1 and 2, and vest following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% per annum compound growth against the issue price which is tested on 6 November 2018 and/or 6 November 2019 and satisfaction of certain individual performance targets.

The Retention award will lapse or partially lapse if the original LTBP awards vest in full or in part.

The fair values of awards were calculated using a Monte Carlo simulation model. The expected volatility range of 32% - 36% reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

The following table illustrates the number and fair values of the Retention Award shares:

	Vesting Date	2018 No. of shares	2017 No. of shares	2018 fair value per share £	2017 fair value per share £
Tranche 1	6 November 2018	914,230	-	0.87	-
Tranche 2	6 November 2019	914,230	-	0.57	-
Total		1,828,460	-		

34 Share-based payments *(continued)*

Staff share incentive plans

The Group has a number of all employee 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 Company 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 2018 ¹	Weighted fair value per share £
2015 SIP				
Partnership shares	29 August 2014	29 August 2015	2,132,766	0.23
Matching shares	29 August 2014	29 August 2018	2,132,766	2.58
2016 SIP				
Matching shares	See below	See below	1,366,211	2.20
2017 SIP				
Matching shares	See below	See below	1,727,537	1.64
Total			7,359,280	

¹ The number of shares shown above is the estimated number

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.

SIP shares were issued on the 11th of each month with the vesting period of 36 months from the date they were issued.

Performance Share Plan (PSP)

During the year awards were granted under the PSP scheme to the Chief Executive Officer and other members of Senior Management. As at 31 January 2018, no performance criteria had been set for these shares and therefore, as there was no shared understanding of the terms of the scheme, no IFRS 2 charge has been made.

35 Ultimate parent undertaking and controlling party

The Group is a wholly owned subsidiary of AA Mid Co Limited, a company registered in United Kingdom and Wales whose registered office is Fanum House, Basing View, Basingstoke, RG21 4EA.

The ultimate parent undertaking and controlling party, which is also the parent of the largest group to consolidate these financial statements, is AA plc whose registered office is at Fanum House, Basing View, Basingstoke, RG21 4EA. Copies of the consolidated parent financial statements are available from the website www.theaapl.com/investors.

36 Accounting standards, amendments and interpretations

New accounting standards, amendments and interpretations adopted in the year

In the year ended 31 January 2018, 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:

- IAS 1: Disclosure Initiative
- Annual Improvements to IFRS 2012-2014
- IFRS 11: Accounting for Acquisitions of Interests in Joint Operations

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 2017:

	Effective date
• IFRS 15: Revenue from Contracts with Customers	1 January 2018
• IFRS 9: Financial Instruments	1 January 2018
• IFRS 2: Classification and Measurement of Share Based Payment Transactions - Amendments to IFRS 2	1 January 2018
• IFRS 16: Leases	1 January 2019
• IFRS 17: Insurance Contracts	1 January 2021

Management has completed a detailed impact assessment ahead of the implementation of IFRS 9, IFRS 15 and IFRS16.

IFRS 9

Management's analysis has focused on receivables, hedging and the change in accounting options for debt issue fees.

It has been concluded that there will not be a material change to receivables as a result of the new standard and there will be no change to the Group's hedging policy.

Management has concluded that as a result of the change in accounting requirements regarding debt issue fees there will be a one-off gain of c£10m which will be recognised in opening retained earnings in line with IFRS 9.

36 Accounting standards, amendments and interpretations (continued)

IFRS15

Management have performed a detailed analysis of each Group revenue stream, with particular focus on our bundling arrangements and variable consideration. We do not believe that the conversion to IFRS 15 will lead to a material impact on the timing or value of revenue in any given period.

Management do anticipate a requirement for a more detailed disclosure providing greater disaggregation of our different revenue streams into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

IFRS 16

Management expects the adoption of IFRS 16 to have a significant impact on the Group due to the number of property leases. The Group expects to adopt IFRS 16 from 1 February 2019 and will apply the standard retrospectively, with the cumulative impact of initially applying the standard recognised at 1 February 2019.

The initial impact assessment indicates that the adoption of IFRS 16 will result in:

- an additional finance lease liability of c£30m
- a tangible fixed asset of £20m - £30m, (after adjusting for forecast onerous lease provisions and any rent free accrual at 1 February 2019)
- increase in trading EBITDA of c1% in FY20, representing rental expense which will now reduce the lease liability rather than being charged to the income statement
- additional depreciation and interest expense of c£4m in FY20

This impact assessment is based on current estimates of discount rate and also current expectations of the property portfolio at 1 February 2019. IFRS 16 requires lease liabilities to be discounted using the incremental borrowing rate on the date of initial application. The final impact of adoption of IFRS 16 cannot be determined before 1 February 2019.

The Group is currently assessing whether the other standards listed above will have a material impact on the financial statements for the year ended 31 January 2019.

37 Events after the reporting period

Bob Mackenzie Litigation

On 7 March 2018, the Group received notification that former Executive Chairman, Bob Mackenzie, who was dismissed for gross misconduct on 1 August 2017, had on 6 March 2018 issued a Claim Form in the High Court, Chancery Division against AA plc, its subsidiary Automobile Association Developments Limited and personally against a number of their Directors and the Company Secretary. The Claim Form seeks a permanent injunction to retain his MVP shares and up to £225m in damages. As this litigation is active at the date of signing these financial statements, the Board have considered any potential financial impact. The Group has not made a provision for these amounts as the Group expects to be successful in rigorously defending these claims. However, the Group will incur legal costs of approximately £1m to defend these claims during the next two financial years which it would seek to recover from Bob Mackenzie when the litigation concludes.

Other post balance sheet events

On 1 March 2018 the Group completed the purchase of the entire share capital of Used Car Sites Limited (trading as AA Cars). A payment of £12m was made to the former owners and £3m was paid into an escrow account and is payable to the former owners subject to certain conditions being met.

Company balance sheet as at 31 January

	Notes	2018 £m	2017 £m
Non-current assets			
Investment in subsidiaries	2	1,661	1,661
Current assets			
Trade and other receivables	3	132	129
Total assets		1,793	1,790
Current liabilities			
Trade and other payables	4	(1,770)	(1,770)
Total liabilities		(1,770)	(1,770)
Net assets		23	20
Equity			
Called up share capital	5	-	-
Retained earnings		23	20
Total equity attributable to equity holders of the parent		23	20

The profit for the financial year of the Company is £83m (2017: £60m).

As at 31 January 2018, the Company had distributable reserves of £23m (2017: £20m).

Signed for and on behalf of the Board on 14 June 2018 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
At 31 January 2016	20	-	20
Capital reduction	(20)	20	-
Dividends paid	-	(60)	(60)
Profit for the year	-	60	60
At 31 January 2017	-	20	20
Dividends paid	-	(80)	(80)
Profit for the year	-	83	83
At 31 January 2018	-	23	23

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 and on a going concern basis.

The Company is incorporated and domiciled in England and Wales.

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 2018. The financial statements are prepared in Sterling and are rounded to the nearest million pounds (£m).

1.2 Basis of preparation

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),
- 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. All differences are taken to the income statement.

Notes to the Company financial statements (*continued*)

b) Investments in subsidiaries and joint ventures

Investments in subsidiaries and joint ventures 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 cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement 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 cash-generating unit to which the asset belongs.

Joint ventures are joint arrangements whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

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 ongoing 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.

2 Investments

	2018 £m	2017 £m
Investment in subsidiary at cost		
At 1 February and 31 January	1,661	1,661

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

Notes to the Company financial statements (continued)

3 Trade and other receivables

	2018 £m	2017 £m
Amounts owed by subsidiary undertakings	129	129
Group tax relief	3	-
	132	129

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

4 Trade and other payables

	2018 £m	2017 £m
Amounts owed to parent undertakings	1,756	1,756
Amounts owed to subsidiary undertakings	14	14
	1,770	1,770

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

5 Share capital

	2018 £	2017 £
Allotted, called up and fully paid		
20 ordinary shares of £1 each	20	20
	20	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.

In the prior year, the Company undertook a capital reduction to reduce the nominal value of share capital and increase the distributable reserves.

During the year, the company paid a dividend of £4m per share (2017: £3.00, based on 20m shares at the time of distribution).

6 Auditor's remuneration

The fee for the audit of these financial statements was £14k (2017: £12k).

7 Staff costs

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

Notes to the Company financial statements (*continued*)

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 2018 are:

Name	Country
AA Acquisition Co Limited ^{1, 2}	United Kingdom
AA Bond Co Limited ^{1, 3}	Jersey
AA Corporation Limited ²	United Kingdom
AA Financial Services Limited ²	United Kingdom
AA Media Limited ²	United Kingdom
AA Senior Co Limited ²	United Kingdom
AA The Driving School Agency Limited ²	United Kingdom
Automobile Association Developments Limited ²	United Kingdom
Automobile Association Insurance Services Limited ²	United Kingdom
Drivotech (UK) Limited ²	United Kingdom
Intelligent Data Systems (UK) Limited ²	United Kingdom

The other subsidiary undertakings of the Company at 31 January 2018 are:

Name	Country
A.A. Pensions Trustees Limited ²	United Kingdom
AA Brand Management Limited ²	United Kingdom
AA Garage Services Limited ²	United Kingdom
AA Ireland Pension Trustees DAC ⁴	Ireland
AA Pension Funding GP Limited ⁵	United Kingdom
AA Pension Funding LP ⁵	United Kingdom
AA Road Services Limited ²	United Kingdom
AA Underwriting Limited ²	United Kingdom
Automobile Association Holdings Limited ²	United Kingdom
Automobile Association Insurance Services Holdings Limited ²	United Kingdom
Automobile Association Protection and Investment Planning Limited ²	United Kingdom
Automobile Association Services Limited ²	United Kingdom
Automobile Association Underwriting Services Limited ²	United Kingdom
Breakdown Assistance Services Limited ⁶	United Kingdom
Breakdown Hero Limited ⁶	
Drakefield Group Limited ²	United Kingdom
Drakefield Holdings Limited ²	United Kingdom
Drakefield Insurance Services Limited ²	United Kingdom
Nationwide 4 X 4 Ltd ²	United Kingdom
Peak Performance Management Limited ²	United Kingdom
Personal Insurance Mortgages and Savings Limited ²	United Kingdom
The Automobile Association Limited ³	Jersey

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

² Company registered office: Fanum House, Basing View, Basingstoke, Hampshire, RG21 4EA, England.

³ Company registered office: 22 Greenville Street, St Helier, Jersey, JE4 8PX.

⁴ Company registered office: 61a South William Street, Dublin 2, Ireland.

⁵ Company registered office: 50 Lothian Road, Festival Square, Edinburgh, EH3 9WJ, Scotland.

⁶ Company registered office: 90 Long Acre, London, WC2E 9RA.