

Report and Financial Statements

Year ended 31 March 2020



Registered number: 10098233

**AA PENSION SCHEME
REPORT AND FINANCIAL STATEMENTS
YEAR ENDED 31 MARCH 2020**

Risk. Reinsurance. Human Resources.



AA PENSION SCHEME

CONTENTS

Trustee and its Advisers	1
Trustee's Report	3
Independent Auditor's Report to the Trustee.....	23
Fund Account.....	25
Statement of Net Assets (Available for Benefits).....	26
Notes to the Financial Statements.....	27
Independent Auditor's Statement about Contributions	43
Summary of Contributions	44
Actuarial Certificate.....	45
Appendix – Extracts from Statement of Investment Principles.....	46

AA PENSION SCHEME

TRUSTEE AND ITS ADVISERS YEAR ENDED 31 MARCH 2020

Trustee	A.A. Pensions Trustees Limited
Company Appointed Directors	Mr T Bonnin-Barkham (appointed 20 November 2019, resigned 4 September 2020) Mr L Jones (appointed 25 April 2019) Mr C Norman (resigned 1 September 2019) Mr J Stewart Mr M Sullivan Mr R Warner (resigned 25 April 2019)
Member-Nominated Directors	Mr P Foster Mr D Glover Mr S Millman
Independent Director	Mr S Delo representing PAN Trustees UK LLP (Chairman)
Principal Employer	Automobile Association Developments Limited
Secretary to the Trustee	Mrs L Birks
Actuary	Mr D Eteen, FIA Aon Solutions UK Limited (formerly Aon Hewitt Limited)
Administrator	Aon Solutions UK Limited (formerly Aon Hewitt Limited)
Independent Auditor	Crowe U.K. LLP
Banker	Bank of Scotland plc
Covenant Adviser	RSM Restructuring Advisory LLP ('RSM')
Investment Advisers	Aon Solutions UK Limited (formerly Aon Hewitt Limited) Valuation Consulting LLP
Investment Managers	Aon Investments Limited (formerly Hewitt Risk Management Services Limited) ('AIL') Arcmont Asset Management (previously part of Bluebay Asset Management as of 31 October 2019) ('Arcmont') Ares Management LLC ('Ares') BlackRock Investment Management (UK) Limited ('BlackRock') BlackRock Private Equity ('BlackRock Quellos') Bluebay Asset Management ('Bluebay') (removed 3 April 2020) Brockton Capital LLP ('Brockton') BV Partners (appointed 26 February 2020) ('BV') Clearbell Capital LP ('Clearbell') DRC Capital LLP ('DRC') EMK Capital Fund II (appointed 12 June 2020) ('EMK') GAM Fund Management Limited ('GAM') Insight Investment Management (Global) Limited (appointed 6 June 2019) ('Insight') Keyhaven Capital Partners Limited ('Keyhaven') Legal & General Investment Management Limited ('LGIM') Magnitude Capital, LLC ('Magnitude') (removed 1 April 2019) Mesirow Advanced Strategies, Inc. ('Mesirow') Nuveen Real Estate Limited (formerly TH Real Estate) ('Nuveen') Threadneedle Asset Management Limited ('Colombia Threadneedle') Warburg Pincus Global Growth-E, L.P. ('Warburg')

AA PENSION SCHEME

TRUSTEE AND ITS ADVISERS YEAR ENDED 31 MARCH 2020

AVC Providers	Utmost Life and Pensions ('Utmost') (transferred from The Equitable Life Assurance Society on 1 January 2020) The Prudential Assurance Company Limited
Annuity Providers	Canada Life Limited ('Canada Life') Just Retirement Limited (appointed 5 September 2019) ('Just')
Custodian	Bank of New York Mellon Corporation ('BNYM')
Legal Advisers	Burness Paul LLP Hogan Lovells LLP Squire Patton Boggs (UK) LLP
Data Consultant	ITM Limited
Fiduciary Overseer	Hymans Robertson LLP
Contact Details	Mrs L Birks Trustee Services Manager The AA Fanum House Basing View Basingstoke Hants, RG21 4EA lorraine.birks@theaa.com 01256 491060

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Introduction

The Trustee of AA Pension Scheme (the 'Scheme') is pleased to present the annual report together with the audited financial statements for the year ended 31 March 2020.

Constitution and management

The Scheme is a Defined Benefit ('DB') scheme. The Scheme is governed by a Trust Deed as amended from time to time and is administered by Aon Solutions UK Limited in accordance with the establishing document and Rules solely for the benefit of its members and other beneficiaries.

The Scheme has five categories of benefits:

- Staff Section
- Management (Sections 1, 2 and 3)
- Career Average Revalued Earnings Section ('CARE')

The Scheme is closed to future accrual with effect from 1 April 2020.

The Trustee is shown on page 1.

Each Trustee Director is eligible to vote, whether Member-Nominated, Company Appointed or Independent and the Memorandum of Association and Scheme Rules set out the basis on which decisions are made.

The Principal Employer may appoint Trustee Directors and may remove any Trustee Director it has appointed at any time. Member-Nominated Trustee Directors ('MNTDs') are appointed for four years but can be re-selected for a further term of office provided they are still eligible. A Trustee Director can resign by giving written notice to the Secretary to the Trustee at any time. The power of removing and/or appointing the Corporate Trustee rests with the Principal Employer.

In accordance with the Pensions Act 2004 at least one third of the total number of Trustee Directors must be nominated by Scheme members. The Member-Nominated Trustee Directors are selected from the membership.

The Trustee has appointed professional advisers and other organisations to support it in delivering the Scheme objectives. These individuals and organisations are listed on pages 1 and 2. The Trustee has written agreements in place with each of them.

In addition to the professional advisers, the Trustee is supported by the AA Pensions Department, from which secretarial services are provided.

Trustee meetings

The Trustee Board met formally seven times during the year to consider the business of the Scheme. The Trustee has also set up an Audit, Risk and Compliance Committee, Administration Committee, Investment Committee and a Valuation Committee which all met during the year.

Scheme changes

Following the year end it was agreed by the Employer and the Trustee to close the Scheme for future accrual effective 1 April 2020.

The Trustee invested in a "pensioner buy-in" annuity contract with Just, an insurance company, to secure some of the liabilities. This investment is held specifically to hedge against the individual liabilities of part of the Scheme membership. The annuity contract as at 9 September 2019, with a purchase price of £247.3m, covers 1,784 individuals who were pensioner members as at this date.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Financial statements

The financial statements included in this annual report have been prepared and audited in accordance with the regulations made under Sections 41 (1) and (6) of the Pensions Act 1995.

Membership

Details of the membership changes of the Scheme in the year are as follows:

	Actives	Deferreds	Pensioners	Total
Members at the start of the year	3,074	13,189	8,413	24,676
Adjustments to members	(42)	24	26	8
New spouses and dependants	-	-	109	109
Retirements	(40)	(336)	383	7*
Members leaving with preserved benefits	(205)	205	-	-
Deaths	(3)	(23)	(240)	(266)
Trivial commutations	-	(3)	(21)	(24)
Cessation of pension	-	-	(13)	(13)
Transfers out	-	(85)	-	(85)
Members at the end of the year	2,784	12,971	8,657	24,412

* These 7 members partially retired during the year taking their pre-2017 final salary benefits but who continued accruing CARE benefits in the Scheme.

	Actives	Deferreds	Pensioners	Total
Staff	-	9,852	8,130	17,982
Management Section 1	-	176	58	234
Management Section 2	-	65	107	172
Management Section 3	-	6	-	6
CARE	2,784	2,872	362	6,018
Members at the end of the year	2,784	12,971	8,657	24,412

These membership figures do not include movements notified to the Administrator after the completion of the annual renewal.

The adjustments to members shown above are the result of retrospective updating of member records.

Included in the above are 3,476 (2019: 2,092) pensioners and 643 (2019: 418) beneficiaries whose benefits are financed by annuity policies.

Pensioners include 1,305 (2019: 1,277) individuals receiving a pension upon the death of their spouse who was a member of the Scheme. Pensioners also include 95 (2019: 85) child dependants in receipt of a pension in respect of the following Sections:

	Widows	Child Dependents	Total
CARE	22	18	40
Staff	1,279	76	1,355
Management Section 1	4	-	4
Management Section 2	-	1	1
Members at the end of the year	1,305	95	1,400

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Pension increases

Pensions in payment are increased in April each year in line with the increase in the Consumer Prices Index ('CPI') up to a maximum of 5.0% for pre-1 July 2010 service and up to a maximum of 2.5% for post 1 July 2010 service. Proportional increases are applied to new pensioners during the year.

A history of recent non-CARE, Jersey and Guernsey pension increases are summarised below:

April 2014	3.2% on pre-1 July 2010 accrued pension; 2.5% on post 1 July 2010 accrued pension
April 2015	2.3% on pre-1 July 2010 accrued pension; 2.3% on post 1 July 2010 accrued pension
April 2016	0.8% on pre-1 July 2010 accrued pension; 0.8% on post 1 July 2010 accrued pension
April 2017	2.0% on pre-1 July 2010 accrued pension; 2.0% on post 1 July 2010 accrued pension
April 2018	3.9% on pre-1 July 2010 accrued pension; 2.5% on post 1 July 2010 accrued pension
April 2019	3.3% on pre-1 July 2010 accrued pension; 2.5% on post 1 July 2010 accrued pension

As the CPI was less than 5.0% for the purposes of the April 2019 pension increases, increases were not capped in accordance with the Scheme Rules. Certain limited elements of members' pensions are not subject to a cap and received full increases in line with the Retail Prices Index ('RPI') or CPI in accordance with the Scheme Rules.

A different level of pension increase, in excess of Guaranteed Minimum Pension ('GMP'), was awarded to CARE pensioners:

Pre-1 July 2010 accrued pension	2.4% increase on 1 April 2019 (CPI capped at 5.0% and floored at 0.0%)
Post 1 July 2010 accrued pension	2.4% increase on 1 April 2019 (CPI capped at 2.5% and floored at 0.0%)

Different levels of pension increase, in excess of GMP, are awarded to pensioners whose service accrued in Jersey and Guernsey:

Jersey	
Pre-23 September 1999:	4.3% increase on 1 April 2019 (Jersey cost of living index floored at 0.0%)
Post 23 Sept 1999:	4.3% increase on 1 April 2019 (Jersey cost of living index capped at 5.0% and floored at 0.0%)
Guernsey	
Pre-23 September 1999:	2.9% increase on 1 April 2019 (Guernsey retail price index floored at 0.0%)
Post 23 Sept 1999:	2.9% increase on 1 April 2019 (Guernsey retail price index capped at 5.0% and floored at 0.0%)

There were no discretionary pension increases in the year.

Deferred benefits are increased in line with legislation and the Scheme Rules.

Transfers

Members leaving service can normally transfer the value of their benefits under the Scheme to another scheme that they join or to an insurance contract or personal pension.

The transfer value of the Scheme members' benefits includes no allowance for any discretionary benefits which might be awarded in the future.

Transfers into the Scheme are not allowed.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Contributions

Contributions were paid in accordance with the Schedules of Contributions certified by the Scheme Actuary on 16 June 2017 and 24 February 2020.

- Member contributions were receivable at 5.5%, 7.0%, 8.5% or 10.0% of Pensionable Pay; Age related contributions calculated as a percentage of Pensionable Pay are receivable for members who opted for a build up rate of 1.82%. These contributions are reviewed annually in March.
- Employer contribution were receivable at 9.2%, 11.1%, 12.1% and 13.9% of Pensionable Pay depending on whether the member elected for a build-up rate of 1.00%, 1.25%, 1.43% and 1.67% or 1.82% respectively.

Deficit contributions will be payable as follows:

- Asset Backed Funding ('ABF') contributions were payable monthly by the Employer at a rate of £1,184,433. The Schedules of Contributions specify that these deficit contributions are increased annually in line with retail price index and be offset against monthly payments received by the Scheme from the ABF arrangement.
- Additional cash deficit funding contributions were receivable as follows:
 - from the Employer at an amount of £916,667 per month from April 2019 to January 2020, £833,330 for February 2020 and £nil for March 2020;
 - from the Employer at an amount of £833,333 per month from April 2020 to March 2021;
 - from the Employer at an amount of £916,667 per month from April 2021 to March 2022; and
 - from the Employer at an amount of £1,000,000 per month from April 2022 to July 2025.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Going concern and COVID-19

The Sponsor is, at the date of signing the annual report having ongoing discussions with two private equity bidders, as part of its ongoing refinancing programme. The future impact of this on the Scheme is, as yet, unknown, as is the effect this could have on the Sponsor's refinancing programme should a private equity bid not go ahead. A successful bid and /or changes to the Sponsor's refinancing programme could have an impact on the strength of the Employer covenant.

Having given careful consideration to all of this, the Trustee is, at the date of signing, of the view that while there is no going concern issue at present, there could be challenges next year if a private equity bid did not go ahead and / or the Sponsor experienced problems with its re-financing timetable.

The Trustee has been considering the impact of COVID-19 on the Scheme and its covenant since early 2020. Operations have proven robust and Aon, as Scheme administrator, has been able to maintain an acceptable level of service and has demonstrated a robust approach to having many staff operating from home. There has been no evidence of significant member issues emerging during this period that would suggest the administration service has been compromised. The Scheme has been employing a well-diversified (sectorally and internationally) investment strategy and has maintained a high level of interest rate and inflation hedging - this strategy has therefore been resilient in the face of market fluctuations and should continue to be robust over the next year. The Trustee has had extensive discussions with the Company, via the Chief Financial Officer, and has had strong reassurance that the business is faring well in the face of COVID adversity. The half year results recently reported were encouraging. The Trustee has also sought covenant advice from RSM which has provided reassurance regarding the ability of the Company to trade successfully following COVID 19 impacts. The Trustee Board has successfully migrated its entire programme of meetings, including sub-committees, to an on-line/videoconference basis and is continuing to operate the governance of the Scheme in a rigorous and comprehensive manner.

The Trustee does not believe that COVID-19 and the changes to the Sponsor's refinancing programme will give rise to a material uncertainty on the Scheme's going concern status for the next 12 months from the date of signing the annual report.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Report on Actuarial Liabilities

As required by Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ('FRS 102'), the financial statements do not include liabilities in respect of promised retirement benefits.

Under Section 222 of the Pensions Act 2004, every scheme is subject to the Statutory Funding Objective, which is to have sufficient and appropriate assets to cover its technical provisions. The technical provisions represent the present value of the benefits members are entitled to based on pensionable service to the valuation date. This is assessed using the assumptions agreed between the Trustee and the Employer and set out in the Statement of Funding Principles, which is available to Scheme members on request.

The most recent triennial actuarial valuation of the Scheme was carried out as at 31 March 2019. All figures quoted exclude AVC investments from both the assets and liabilities.

The value of the technical provisions was:	£2,535 million
The value of the assets was:	£2,404 million
As a percentage of technical provisions	95.0%

Although there are no current plans to discontinue the Scheme and buy-out liabilities with an insurance company, the Trustee also considers the level of funding relative to the estimated costs of such a buy-out (known as "solvency liabilities") at the valuation date.

Value of solvency liabilities	£3,886 million
Value of assets available to meet solvency liabilities	£2,405 million
As a percentage of solvency liabilities	62.0%

The value of technical provisions is based on Pensionable Service to the valuation date and assumptions about various factors that will influence the Scheme in the future, such as the levels of investment returns and price inflation, when members will retire and how long members will live. The method and significant actuarial assumptions used in the calculations are as follows:

Method

The actuarial method to be used in the calculation of the technical provisions is the Projected Unit Method.

Significant actuarial assumptions

Pre-retirement discount rate: The term dependent rates on the Aon Solutions UK Limited gilt yield curve based on the Bank of England gilt yield curve at the actuarial valuation date plus 2.75% p.a.

Post-retirement discount rate: The term dependent rates on the Aon Solutions UK Limited gilt yield curve based on the Bank of England gilt yield curve at the actuarial valuation date.

Future Retail Price Inflation ('RPI'): The term dependent rates on the Aon Solutions UK Limited RPI yield curve based on the Bank of England RPI curve. No allowance is made for any inflation risk premium.

Future Consumer Price Inflation ('CPI'): The assumption is derived at the actuarial valuation date by deducting 1.1% p.a. from the RPI inflation assumption.

The difference between the long term assumption for RPI and CPI inflation may vary over time to reflect changing views of long term structural differences between the calculation of RPI and CPI inflation at the date subsequent calculations are carried out.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Report on Actuarial Liabilities (continued)

Pension increases: Inflation-linked pension increase assumptions are derived from the RPI inflation assumption (except in respect of post 5 April 1988 GMP and CARE pension increases which are derived from the CPI inflation assumption) on the advice of the Scheme Actuary, allowing for the maximum and minimum annual increase, and the fact that inflation varies from year to year.

Deferred revaluations:

- **Final Salary Sections:** revaluation of deferred pensions in excess of GMP are in line with the CPI inflation assumption. Where the total inflation over the period from date of leaving to retirement is higher than the cap applied to the increase for a certain tranche of pension benefit (for example, the 2.5% p.a. compound cap for pensions accruing after 5 April 2009), the assumption for revaluations of deferred pensions in excess of GMP will instead revert to the relevant cap.
- **CARE Section:** Derived from CPI inflation assumption in a similar manner to that used to derive the pension increase assumptions i.e. on the advice of the Scheme Actuary, allowing for the maximum and minimum annual increase, and the fact that inflation varies from year to year. The same approach is applied to derive the assumption for in service revaluations for active members of the CARE Section.

Pay increases: Each member's salary is assumed to increase in line with the assumed rate of RPI inflation plus 1.1% p.a. together with an allowance for promotional increases.

Accrual in the Final Salary Sections ceased on 30 June 2017. As a result, benefits accrued up to 30 June 2017 are treated as deferred benefits and assumed to increase in future in line with deferred revaluations rather than salary increases.

All active members have accrued CARE benefits from 1 July 2017.

Mortality: for the period in retirement, standard tables S3PMA for male members and S3PFA for female members, adjusted for year of birth with an allowance for improvements between 2013 and 2018. Applicable average scaling factors for each member category are set out below:

Member category	Males	Females
Active members	116%	116%
Deferred members	113%	111%
Pensioner members	111%	110%

An allowance for future improvements has been made in line with the CMI_2018 with an A parameter of 0.25, a Sk parameter of 7 and a long-term annual rate of improvement in mortality rates of 1.5% for men and women.

These arrangements were formalised in a Schedule of Contributions which the Scheme Actuary certified on 24 February 2020. A copy of this certificate is included on page 45.

Next actuarial valuation

The next actuarial valuation is due as at 31 March 2022.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Management and custody of investments

As required by the Pensions Act 1995, the Trustee has prepared a Statement of Investment Principles ('SIP') setting out its policy on investment, which includes the Trustee's policy on Socially Responsible Investment. A copy of the Statement can be found on the Scheme website and is available on request.

The Trustee has delegated management of investments to the investment managers shown on page 1. These managers, who are regulated by the Financial Conduct Authority in the United Kingdom, manage the investments in line with the investment managers' agreements which are designed to ensure that the objectives and policies captured in the SIP are followed.

During the year some of the Scheme's assets were invested in an insurance contract with Just following a prior year insurance contract investment with Canada Life both of which are authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

The Trustee has considered environmental, social and governance factors for investments (including but not limited to climate change) and has delegated to the investment managers the responsibility for taking these considerations into account when assessing the financial potential and suitability of an investment and for exercising the rights (including voting rights) relating to the Scheme's investments.

The investment managers are paid fees for their services. The fees are calculated as a percentage of the market value of the part of the Scheme that they manage.

The Trustee has appointed BNYM as custodian of the Scheme's investments other than pooled investment vehicles where managers make their own arrangements for custody of underlying investments.

The Custodian is responsible for the safe keeping, monitoring and reconciliation of documentation relating to the ownership of listed investments. Investments are held in the name of the Custodian's nominee company, in line with common practice for pension scheme investments.

The Trustee has considered the nature, disposition, marketability, security and valuation of the Scheme's investments and believe them to be appropriate relative to the reasons for holding each class of investments.

Statement of Investment Principles

With effect 30 September 2020, the Trustee updated their SIP for their policies in relation to: 'Arrangements with asset managers'; 'Monitoring of Investment Manager Costs'; and 'Evaluation of Investment Manager Performance and Remuneration'. The Trustee policies in these areas are covered in detail in the SIP, dated September 2020, but broadly summarise as:

Arrangements with asset managers: The Trustee, with support from their investment advisers, monitor the Scheme investments to consider the extent to which the investment strategy and decisions of the investment managers are aligned with the Trustee policies. This extends to existing managers and on the appointment of any new manager. The policies are aligned by amending the appropriate governing documentation or where this is not possible, expressing the expectation to the investment managers by other means. There is typically no set duration for arrangements with investment managers, although the continued appointment all for investment managers will be reviewed periodically, and at least every three years.

Monitoring of Investment Manager Costs: The Trustee will receive annual cost transparency reports from their Investment Consultant which will monitor the total cost and the impact these costs can have on the overall value of the Scheme's assets. The Scheme's investment advisers monitor total investment manager costs on behalf of the Trustee as part of the ongoing manager monitoring they provide to the Trustee and flags to the Trustee where there are concerns.

Evaluation of Investment Manager Performance and Remuneration: The Trustee will assess the (net of all costs) performance of their investment managers on a rolling three-year basis against the Scheme's investment objectives as per the investment strategy review following triennial actuarial valuation.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Statement of Investment Principles (continued)

The Trustee believes that having appropriate governing documentation, setting clear expectations to the investment managers by other means (where necessary), and regular monitoring of investment managers' performance and investment strategy, is in most cases sufficient to incentivise the Trustee's appointed investment managers to make decisions that align with the Trustee's policies, and are based on assessments of medium- and long-term financial performance.

Investment strategy

The Trustee is responsible for determining the Scheme's investment strategy.

The benchmark asset allocation was updated on January 2020 to reflect additions, reductions and increases in the asset targets over the past year. The strategic allocations to listed equities, multi asset credit and hedge funds, were all reduced whilst the strategic allocations to the cashflow matching portfolio (including a second bulk annuity) increased. A 1% strategic allocation to cash was added to the benchmark asset allocation.

The Trustee sets the investment strategy taking into account considerations such as the strength of the employer covenant, the long term liabilities, the level of overall risk (called value at risk) and the funding agreed with the Employer. The Investment strategy is set out in its SIP.

The investment strategy as at 31 March 2020 is to hold

- 19.0% in a diversified portfolio (core property and illiquid) of pooled funds which hold return seeking investments comprising UK commercial property, opportunistic property, property debt, direct lending and private equity.
- 30% in leveraged and un-leveraged index linked gilts (cashflow matching), where the market value moves in line with the long term liabilities of the Scheme, the purpose of which is to hedge against the impact of interest rate movement and inflation on long term liabilities, and two bulk annuity policies to match the benefit payments to selected members.
- 50% in a delegated investment portfolio where the investment manager AIL invests in a diversified portfolio of pooled funds which hold return seeking investments comprising UK and overseas equities, investment property, hedge funds, various credit instruments, infrastructure and liability hedging investments. The market value of the liability hedging assets moves in line with the actuarial value of the long term liabilities of the Scheme, as their purpose is to hedge against the impact of adverse movements in interest rates and inflation on the Scheme's funding position.
- 1.0% in cash to meet pension and other payments.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment transitions

During the year the strategic targets in the Statement of Investment Principles were updated resulting in the following investment transitions:

	2020	2019
Liquid Return Seeking Assets Sub-Portfolio	0.0%	10.5%
Cashflow matching sub-portfolio (including buy-in)	30.0%	20.0%
Core Property sub-portfolio	7.0%	7.0%
Illiquid sub-portfolio	12.0%	12.0%
Delegated sub-portfolio	50.0%	50.0%
Cash	1.0%	0.5%

- 100% redemption (£93m) from Magnitude Hedge Funds, received 1 April 2019 which was used as cash to de-leverage the cashflow matching sub-portfolio in May 2019;
- 100% redemption from Mesirow Fund of Hedge Funds. As at 31 March 2020, c. £58m out of c. £75m returned – earmarked to fund pensioner buy-in premium.
- c.£110m disinvestment from LGIM equities sold over May/June 2019 – earmarked to fund pensioner buy-in premium.
- c.£65m disinvestment from Bluebay Multi Asset Credit (MAC), fund sold over May/June 2019 – earmarked to fund pensioner buy-in premium.
- c. £250m invested in government bonds with LGIM (held in the cashflow matching sub-portfolio) as of May/June 2019, held temporarily until payment of pensioner buy-in premium (5 September 2019).
- In September 2019, disinvestment from LGIM Fixed Interest Gilt and LGIM Index-Linked Gilt Fund and proceeds amounting to £251.6m paid as an initial payment to purchase an annuity policy. Following an adjustment to the price for market conditions, £4.3m was returned to the Trustee, resulting in the final payment being £247.3m.
- c.£45m switched from regional passive equity funds in to global factor equity funds on 17 October 2019.
- 100% redemption of residual holdings in Bluebay MAC Fund (c.£27m) which was held as cash.
- Over the year, the Scheme purchased and sold leveraged and un-leveraged gilts, within the cashflow matching sub-portfolio, at various points. This was done to add or reduce the amount of leverage in the Scheme assets as cash was returned from hedge fund redemptions. The Scheme purchased leveraged gilts of c.£92m and sold leveraged gilts of c.£167m. The Scheme purchased unleveraged gilts of c.£300m and sold unleveraged gilts of c.£165m.
- Capital calls and distributions from the limited partnership vehicles (within the illiquid sub-portfolio) accounted for purchase of c. £52m and sales of c.£24m.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment report

Investment performance

The Trustee assesses the performance of the Scheme's investments by reference to benchmarks and performance targets set and agreed with each manager. The Trustee receives monthly reports from its performance measurer (BNYM) showing actual performance by manager and fund. Investment managers regularly present to the Investment Committee (IC), to report on compliance with their agreements and to be questioned by the IC members. Performance of the Scheme's investments (after fees) over short and longer periods to 31 March 2020 is summarised as follows:

Period	Scheme return (% p.a.)	Benchmark return (% p.a.)
1 year	4.8	0.7
3 years	4.2	2.6
5 years	7.2	3.7

Scheme performance

With this market background over the year to 31 March 2020, the Scheme returned 4.8%, outperforming its benchmark return of 0.7% as reported by BNY Mellon.

The delegated investment portfolio returned 6.8% over the year, underperforming the liability proxy benchmark by 2.7% (and outperforming the cash benchmark by 6.0% as reported by BNYM). This return of 6.8% comprised of individual quarterly performance of 4.1% in Q2 2019 (driven by strong global equity performance); 10.5% in Q3 2019 (the major contributor over the quarter was falling long term interest expectations and strong outperformance of the delegated portfolio); -8.6% in Q4 2019 (where long-term UK interest rate expectations rose, as improved economic growth expectations coincided with an increase in trade and greater Brexit certainty) and 1.7% in Q1 2020 (where falling interest rates expectations again contributed significantly offset by a significant fall in growth assets due to COVID-19).

LGIM passive equities and gilts performed within accepted levels over the quarters. In Q4 2019, the Scheme transitioned from its regional equities with LGIM to the developed balanced factor equities with LGIM. Over Q1 2020, the funds had negative returns similar to the broader equity market. The developed balanced factor equity index fund returned -17.2% against a benchmark of -17.4% and the hedged share class has returned -22.9% against a benchmark of -22.8% in Q1 2020.

The established private equity funds performance was mixed over the year. BlackRock Quellos returned 9.3% outperforming its benchmark by 11.3%, while Keyhaven returned -1.4% and Warburg returned -12.8% underperforming their respective benchmarks by 3.4% and 9.3% as reported by BNY Mellon.

Core property returns were poor over the year, with BlackRock returning -1.1% and Threadneedle returning -0.3% against their shared benchmark of 0.0%. The negative performance is largely a reflection of the market uncertainty that arose as a result of COVID-19 where broadly yields shifted outwards or remained stable, resulting in a decline in portfolio values across the market. For Threadneedle, quarterly returns were 0.1%, 0.3%, 0.3%, -1.3% over the year while BlackRock posted quarterly returns of 0.2%, 0.2%, 0.7%, -2.5% over the year.

The opportunistic property funds returns were strong in absolute terms, and mixed relative to benchmark over the year. Brockton returned 16.4%, outperforming its benchmark by 1.4% whilst Clearbell II and III returned 2.9% and 0.2% underperforming the benchmark by 11.1% and 13.8% respectively as reported by BNY Mellon.

Property Debt performed well over the year although remains slightly behind benchmark at this stage in the deal sourcing process. Over the year DRC returned 4.9% in absolute terms, against a target of 6.8%. The investment with GAM over the year has shown return of 6.3% which has underperformed against the benchmark of 8.0%.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment report (continued)

Scheme performance (continued)

Direct lending performed well over the year, although the impact of Covid-19 on the two portfolios is (Ares and Arcmont) unclear and will take time to materialise given the nature of the portfolios. Both managers are senior lenders in the majority of deals and are therefore able to actively engage with sponsors and management during this period. Both portfolios are in the deal sourcing phase of the investment and are on track to achieve their target internal rate of returns. Ares returned 7.9% (vs. 6.0%) over the year and Arcmont returned 3.9% (vs 8.0%).

Hedge fund performance was also weak over the year. The full redemption from Magnitude finalised over the year with the final proceeds from the Mesirow redemption expected on 30 June 2020. For the year ending 31 March 2020, Mesirow returned absolute negative performance of 6.1% with a relative underperformance of 9.9%.

Engagement Policy Implementation Statement

Introduction

This statement has been prepared to meet the requirement of the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019 on the Trustees' stewardship policy of the Scheme's assets as set out in the Statement of Investment Principles ('SIP') effective as at 31 March 2020.

The relevant extracts from the SIP (dated January 2020) in relation to 'Stewardship – Voting and Engagement' are referred to in the Appendix.

Scheme activity over the year

In November 2019, the Trustee carried out a survey of their Responsible Investment ('RI') beliefs, which led to the identification of a number of consensus beliefs and statements. These were reflected in the Scheme's policies on financially material factors, including Environmental, Social and Governance ('ESG') and climate change.

The Trustee has informed the managers of the importance of appropriately considering ESG factors with regards to the companies that they invest in. Similarly, the Trustee has made explicit its expectation that asset managers should use their shareholder rights to influence and improve the companies they invest in, to generate better long-term financial outcomes.

The Scheme's fiduciary manager, Aon Investments Limited ('AIL') presented to the Investment Committee ('IC') on a quarterly basis engaging on a number of areas including performance, strategy, risk, corporate governance. AIL report their ESG ratings for all rated managers within the fiduciary portfolio on a quarterly basis. These ESG Ratings reflect the extent of ESG integration as well as the features and impact of their respective Stewardship programs.

The Scheme's non-fiduciary managers, present to the IC on an annual basis (including at manager days held in April 2019 and October 2019). The IC engaged with the managers on performance, strategy, risk, corporate governance and ESG practice. Reporting on performance and Aon's ESG rating of a manager is provided by the Scheme's investment adviser on a quarterly basis.

In appointing two new managers over the year (BV Partners and EMK Capital), the IC considered the ESG policies of these managers before making the appointments and concluded these to be in line with the Trustee's ESG policy.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment report (continued)

Engagement Policy Implementation Statement (continued)

Engagement – Fiduciary Manager

Under the Trustee's fiduciary mandate managed by AIL, AIL appoint underlying asset managers to achieve an overall target return. The Trustee delegates the monitoring of ESG integration and stewardship quality to AIL and AIL have confirmed that all equity and fixed income managers have been rated 2 or above on Aon's four-tier ESG ratings system¹ This means that all the appointed asset managers are at least aware of potential ESG risks in the investment strategy and have taken some steps to identify, evaluate and potentially mitigate these risks.

AIL have undertaken a considerable amount of engagement activity during the first half of 2020 across 22 ESG specific "deep-dive" meetings covering the equity and fixed income managers that are invested in by AIL across all delegated funds in which AIL's clients invest. At these meetings, AIL were able to analyse and discuss the voting and activities undertaken during calendar year 2019, highlighting areas of improvement and discussing manager strategy in the area of responsible investment moving forward.

The Trustee has reviewed the AIL Annual Stewardship Report and is content that Aon is using its resources to appropriately influence positive outcomes in the managers they invest.

¹ More information on engagement the Aon ESG Ratings process can be found here: <https://www.aon.com/getmedia/0b52d7ec-db77-41bc-bb45-9386034db392/AonCanada-Publication-Investment-GuideESGRatings.aspx>

Voting and Engagement - Equity

Over the year, the Scheme was invested in the following equity funds, either through the fiduciary arrangement with AIL or with funds managed by Legal and General Investment Management ('LGIM'):

- AIL Global Active Equity Strategy
- AIL Emerging Markets Wealth Strategy
- AIL Global Multi-Factor Equity Strategy (LGIM (Multi Factor Fund))
- LGIM (Regional Equity Index Funds)

The Trustee acknowledges that a number of managers were unable to provide data on significant votes (The Trustee considers a significant vote broadly as a vote which the respective manager deems most significant to the Scheme or a vote where more than 15% of votes were cast against management) and note that AIL will be asking these managers to track and provide such information moving forward.

All equity managers in these funds utilise at least the Institutional Shareholder Service ('ISS') and/or Glass Lewis for various services that may include research, vote recommendations, vote execution and record keeping.

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment report (continued)

Engagement Policy Implementation Statement (continued)

Voting and Engagement – Equity (continued)

AIL Global Equity Strategy

Within the active global equity strategy, most managers voted in over 90% of resolutions through 2019 and Q1 of 2020, with only GQG (in relation to the Global Equity Fund) falling below that mark in Q1 2020. AIL was disappointed with this and will raise this concern with GQG at the next quarterly meeting. The Trustee shares this concern and note that AIL will provide feedback that such a level of voting activity is not acceptable.

AIL was mixed in its satisfaction of voting behaviour through 2019. For Harris, they were not fully satisfied with the records they had maintained to justify their voting decisions on some shareholder resolutions. For example, Harris voted against a shareholder resolution requesting a gender pay gap report, this vote was in line with their standard guideline to typically vote against shareholder proposals requesting that a company disclose or amend certain business practices unless they believe a proposal would have a substantial positive economic impact on the company. However, AIL felt this standard guideline was not robust enough rationale in this case given the company circumstances. The Trustee shares this concern and notes that AIL have provided formal feedback to Harris explaining that they must make improvements in this area, by ensuring they can provide sufficient rationale to justify voting decisions which are contentious.

AIL Emerging Markets Wealth Equity Strategy

All managers voted in over 95% of eligible resolutions. No more than 10% of votes were abstained by any manager during the period in question.

All managers voted against management in a relatively high proportion of times compared to active managers in other of their equity strategies.

Information has been requested from all underlying managers at a strategy (i.e. fund specific) level, however, a small number of managers have only been able to provide data at a manager level. The Trustee notes that AIL will continue engaging and asking these managers to improve the detail of their reporting over time.

Legal and General Investment Management

Over the year to 31 March 2020, LGIM voted on at least 98% of all resolutions in both the Multi-Factor Fund and the World Equity Index Fund². Both Funds had at least 14% of resolutions that were voted against management recommendation.

LGIM use ISS as a proxy advisor for voting on this fund. LGIM regularly monitor the proxy voting services through quarterly due diligence meetings to ensure execution is in line with their voting policy.

LGIM are currently in the process of building a tool to collate specific engagement and voting data at a strategy level and will align this and their definition of a significant vote with PLSA guidelines. LGIM also strengthened its voting policy in 2020 to state they will not vote against misaligned pensions for directors. Weekly voting meetings are recorded and audited annually within the team, with all votes having a rationale behind them.

² Assets were transitioned from LGIM regional equity index funds into the LGIM (Developed Balanced Factor Fund) over the reporting period. As an illustration of the Scheme's investments over the year, we refer to the voting records of the LGIM All World Equity Index.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment report (continued)

Engagement Policy Implementation Statement (continued)

Engagement – Fixed Income

The Scheme invests in Fixed Income securities predominantly through their AIL fiduciary mandate. As at 31 March 2020, the Scheme was invested in over 20 Fixed Income Investment Funds. AIL have engaged with fixed income managers over the year to address responsible investment policies where those were deemed to fall short of the Trustee's expectations and have seen tangible improvements in response.

While equity managers may have more direct influence on the companies they invest in, fixed income managers are also increasingly influential in their ability to encourage positive change. The Trustee believes that engagements of this nature are key to reducing ESG risks within the Scheme's portfolio, as well as having the added benefit of contributing to the transition towards a low carbon economy.

Engagement - Alternatives

The Scheme invest in a number of alternative strategies (property, infrastructure, private debt, private equity, hedge funds) both within and outside of the AIL fiduciary mandate.

All the private equity managers are either Principles for Responsible Investment ('PRI') signatories or adopt guidelines from the PRI and the Trustee is comfortable that all consider financially material ESG factors in their due diligence processes and make reasonable efforts to encourage their portfolio companies to consider relevant ESG-related principles and to support their implementation.

The Trustee recognises that the respective investment processes and often illiquid nature of the alternative investments may mean that stewardship is potentially less applicable or may have a less tangible financial benefit. Nonetheless, the Trustee expects that all their managers should open a dialogue to engage with issuers/companies they invest in should they identify concerns that may be financially material.

AIL have engaged with some of the appointed hedge funds where voting and stewardship are more applicable. From the information received, it is apparent managers acknowledge the importance of climate change and have taken specific steps to integrate these issues into investment decisions. However, the integration of climate change risk and other ESG factors are not carried out systematically at the portfolio wide level. The Trustee notes that this to a large extent is a function of the asset class, investment process; and may carry out further training on this subject in the future with AIL, or with the underlying appointed hedge fund managers, to ensure the Trustee is comfortable with ongoing arrangements and identify where there is a need to encourage improved reporting.

The Trustee acknowledges voting activity from the hedge fund managers may be limited due to the potentially short-term/opportunistic nature of hedge fund investments. This is evident from the voting records provided by managers thus far. The Trustee notes that AIL will ask these RI related questions and engage with hedge fund managers where appropriate and expect that over time, more detail will be provided.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Investment report (continued)

Engagement Policy Implementation Statement (continued)

**Summary – overall
adherence to
Trustee's policy**

Overall, the Trustee is of the opinion the stewardship carried out on behalf of the Scheme is adequate but with room for improvement:

1. The Trustee expects that equity managers vote more than 95% of the time, and
2. The Trustee expects increased levels of detail from certain equity managers with respect to rationale for significant votes.

The Trustee delegates responsibility to AIL to encourage and monitor this within the appointed underlying equity managers.

The Trustee acknowledge that stewardship may be less applicable to certain asset classes such as hedge funds and real estate, but generally would still expect to see RI type policies and processes formalised and developed over time.

The Trustee recognises that it has a responsibility as a large institutional investor to encourage and promote high standards of stewardship in relation to the assets that the Scheme invests in.

The Trustee will continue to use its influence to drive positive behaviour and change among the managers that it has employed to invest the assets of the Scheme, and with other third parties that the Trustee relies on such as its investment advisor. The Trustee will, as appropriate, set increasingly higher standards for these parties in future, and will monitor, assess and ultimately hold them to account to ensure that the stewardship responsibility in relation to the assets of the Scheme are appropriately administered.

Employer related investments

The investments of the Scheme are invested in accordance with Section 40 of the Pensions Act 1995. Details of any Employer related investments are disclosed in note 23 to the financial statements.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Further information

Further information about the Scheme is available, on request, to members, their spouses and other beneficiaries together with all recognised trade unions. In particular, the documents constituting the Scheme, the Rules and a copy of the latest actuarial report and the Trustee's Statement of Investment Principles can be inspected.

Individual benefit statements are provided to active members annually and for deferred DB members on request. In addition to the information shown on these statements members can request details of the amount of their current transfer value and, if applicable, the current amount of any refund of contributions to which they would be entitled on leaving service. Such requests are available free of charge once a year.

If members have any queries concerning the Scheme or their own pension position, or wish to obtain further information, they should contact Aon Solutions UK Limited who will also be able to provide them with a further copy of the Scheme's booklet should they require one and answer any queries that they may have about entitlement to benefits.

The Trustee of AA Pension Scheme care of:

AA Pension Scheme
Aon Solutions UK Limited
PO Box 196
Huddersfield
HD8 1EG

aa.pensions@aon.com

If you have any complaints in relation to the Scheme you should in the first instance, contact:

Mrs L Birks
Trustee Services Manager
The AA
Fanum House
Basing View
Basingstoke
Hants
RG21 4EA

pensions@theaa.com

The Trustee and Aon Solutions UK Limited take the matter of protecting members personal information seriously. Further details can be found at www.aapensions.com/privacy-policy.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Compliance Statement

HM Revenue & Customs Registration

The Scheme is a registered pension scheme in accordance with the Finance Act 2004. This means that the contributions paid by both the Employer and the members qualify for full tax relief, and enables income earned from investments by the Trustee to receive preferential tax treatment.

Pension Tracing

The Scheme is registered with the Pension Tracing Service which maintains a list of up to date addresses of schemes to assist ex-members in tracing their rights if they have lost contact with the previous Employers' scheme. The address for the Pension Tracing Service is:

The Pension Tracing Service 9
Mail Handling Site A
Wolverhampton
WV98 1LU

0800 731 0193
www.gov.uk/find-pension-contact-details

The Pensions Regulator

The Pensions Regulator ('TPR') is the United Kingdom ('UK') regulator of work-based pension schemes.

TPR's role is to act to protect the interest of pension scheme members and to enforce the law as it applies to occupational pension schemes.

The regulations set out clearly the areas that TPR covers and the powers that are vested in it. For example, TPR can prohibit or disqualify trustees for acting unlawfully, and can impose fines on wrong doers.

TPR can be contacted at:

The Pensions Regulator
Napier House
Trafalgar Place
Brighton
BN1 4DW

0345 600 1011
customersupport@tpr.gov.uk
www.thepensionsregulator.gov.uk

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Compliance Statement (continued)

The Pension Protection Fund

The Pension Protection Fund was established to provide compensation to members of eligible pension schemes, when there is a qualifying insolvency event in relation to the Employer and where there are insufficient assets in the pension scheme to cover Pension Protection Fund levels of compensation.

The Pension Protection Fund can be contacted at:

PPF Member Services
Pension Protection Fund
PO Box 254
Wymondham
NR18 8DN

0330 123 2222
ppfmembers@ppf.co.uk
www.ppf.co.uk

Questions about pensions

If you have any questions about your pension, The Pensions Advisory Service ('TPAS'), which is part of the Money and Pensions Service, provides professional, independent and impartial help with pensions for free. Services include independent information and general guidance on pension matters.

TPAS can be contacted at:

Money and Pensions Service
120 Holborn
London
EC1N 2TD

0800 011 3797
www.pensionsadvisoryservice.org.uk

Resolving difficulties/Internal Dispute Resolution

It is expected that most queries relating to benefits can be resolved with the Scheme's Administrator. In the event that a complaint cannot be resolved members can make a formal complaint using the Scheme's Internal Dispute Resolution ('IDR') procedure details of which can be obtained from Mrs L Birks.

If the complaint is not resolved satisfactorily, the Government appointed Pensions Ombudsman can investigate complaints of injustice due to bad administration either by the Trustee or the Scheme's Administrator, or disputes of fact of law. The Pensions Ombudsman can be contacted at:

The Pensions Ombudsman
10 South Colonnade
Canary Wharf
London
E14 4PU

0800 917 4487
enquiries@pensions-ombudsman.org.uk
www.pensions-ombudsman.org.uk

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2020

Statement of Trustee's Responsibilities

The financial statements, which are prepared in accordance with UK Generally Accepted Accounting Practice, including the Financial Reporting Standard applicable in the UK (FRS 102) are the responsibility of the Trustee. Pension scheme regulations require, and the Trustee is responsible for ensuring, that those financial statements:

- show a true and fair view of the financial transactions of the Scheme during the Scheme year and of the amount and disposition at the end of the Scheme year of its assets and liabilities, other than liabilities to pay pensions and benefits after the end of the Scheme year; and
- contain the information specified in Regulation 3A of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, including making a statement whether the financial statements have been prepared in accordance with the relevant financial reporting framework applicable to occupational pension schemes.

In discharging the above responsibilities, the Trustee is responsible for selecting suitable accounting policies, to be applied consistently, making any estimates and judgments on a prudent and reasonable basis, and for the preparation of the financial statements on a going concern basis unless it is inappropriate to presume that the Scheme will not be wound up.

The Trustee is also responsible for making available certain other information about the Scheme in the form of an Annual Report.

The Trustee also has a general responsibility for ensuring that adequate accounting records are kept and for taking such steps as are reasonably open to them to safeguard the assets of the Scheme and to prevent and detect fraud and other irregularities, including the maintenance of an appropriate system of internal control.

The Trustee is responsible under pensions legislation for preparing, maintaining and from time to time reviewing and if necessary revising a Schedule of Contributions showing the rates of contributions payable towards the Scheme by or on behalf of the Employer and the active members of the Scheme and the dates on or before which such contributions are to be paid. The Trustee is also responsible for keeping records in respect of contributions received in respect of any active member of the Scheme and for adopting risk-based processes to monitor whether contributions are made to the Scheme by the Employer in accordance with the Schedule of Contributions. Where breaches of the schedule occur, the Trustee is required by the Pensions Acts 1995 and 2004 to consider making reports to The Pensions Regulator and the members.

Approval

Signed for and on behalf of the Trustee:



Trustee Director:



Trustee Director:

Date: 20.10.2020

AA PENSION SCHEME

INDEPENDENT AUDITOR'S REPORT TO THE TRUSTEE FOR THE YEAR ENDED 31 MARCH 2020

Independent auditor's report to the Trustee of the AA Pension Scheme

Opinion

We have audited the financial statements of the AA Pension Scheme for the year ended 31 March 2020 which comprise the Fund Account, the Statement of Net Assets and the related notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:

- show a true and fair view of the financial transactions of the Scheme during the year ended 31 March 2020, and of the amount and disposition at that date of its assets and liabilities, other than liabilities to pay pensions and benefits after the end of the year;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- contain the information specified in Regulation 3A of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, made under the Pensions Act 1995.

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. We are independent of the Scheme 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 Trustee's use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Trustee has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Scheme'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 Trustee is responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

INDEPENDENT AUDITOR'S REPORT TO THE TRUSTEE FOR THE YEAR ENDED 31 MARCH 2020

Other information (continued)

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 this other information, we are required to report that fact.

We have nothing to report in this regard.

Responsibilities of the Trustee

As explained more fully in the Statement of Trustee's Responsibilities set out on page 22 the Trustee is responsible for the preparation of the financial statements, for being satisfied that they give a true and fair view, and for such internal control as the Trustee determines 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 Trustee is responsible for assessing the Scheme'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 Trustee either intends to wind up the Scheme or has 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 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: 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 Scheme's Trustee, as a body, in accordance with Regulation 3 of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, made under the Pensions Act 1995. Our audit work has been undertaken so that we might state to the Scheme's Trustee 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 Scheme's Trustee as a body, for our audit work, for this report, or for the opinions we have formed.



Crowe U.K. LLP
Statutory Auditor
London

Date: 22 October 2020

AA PENSION SCHEME

FUND ACCOUNT FOR THE YEAR ENDED 31 MARCH 2020

	Note	2020 £000	2019 £000
Employer contributions	4	27,673	27,116
Employee contributions	4	991	1,055
		28,664	28,171
Other income	5	6	2
		28,670	28,173
Benefits paid or payable	6	(51,494)	(53,324)
Payments to and on account of leavers	7	(21,911)	(33,298)
Administrative expenses	8	(1,365)	(2)
		(74,770)	(86,624)
Net withdrawals from dealing with members		(46,100)	(58,451)
Returns on investments			
Investment income	9	26,242	15,797
Change in market value of investments	10	51,655	182,139
Investment management expenses	11	(1,205)	(1,399)
Net returns on investments		76,692	196,537
Net increase in the fund during the year		30,592	138,086
Opening net assets		2,688,598	2,550,512
Closing net assets		2,719,190	2,688,598

The notes on pages 27 to 42 form part of these financial statements.

AA PENSION SCHEME

STATEMENT OF NET ASSETS (AVAILABLE FOR BENEFITS) AS AT 31 MARCH 2020

	Note	2020 £000	2019 £000
Investment assets			
Pooled investment vehicles	13	1,835,110	2,020,508
Insurance policies	14	614,200	383,600
Asset backed funding	15	213,600	254,700
AVC investments	16	5,435	5,909
Cash	17	38,539	8,685
Other investment balances	17	1,436	891
		2,708,320	2,674,293
Total net investments		2,708,320	2,674,293
Current assets	21	13,522	15,340
Current liabilities	22	(2,652)	(1,035)
Net assets available for benefits at 31 March		2,719,190	2,688,598

The financial statements summarise the transactions of the Scheme and deal with the net assets at the disposal of the Trustee. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Scheme year. The actuarial position of the Scheme, which does take account of such obligations, is dealt with in the Report on Actuarial Liabilities included in the Trustee's Report. These financial statements and Actuarial Certificate should be read in conjunction with this report.

The notes on pages 27 to 42 form part of these financial statements.

These financial statements were approved by the Trustee and were signed on its behalf by:

Trustee Director:

Trustee Director:

Date: 20.10.2020

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

1. Basis of preparation

The financial statements have been prepared in accordance with the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, Financial Reporting Standard 102 ('FRS 102') – The Financial Reporting Standard applicable in the UK and Republic of Ireland issued by the Financial Reporting Council and the guidance set out in the Statement of Recommended Practice ('SORP') (2018) - Financial Reports of Pension Schemes, published by the Pensions Research Accountants Group ('PRAG').

2. General information

AA Pension Scheme is a DB occupational pension scheme established under trust under English Law.

The address of the Scheme's principal office is The AA, Fanum House, Basing View, Basingstoke, Hants, RG21 4EA.

3. Accounting policies

The principal accounting policies applied to the preparation of the financial statements are set out below. These policies have been consistently applied unless otherwise stated.

Functional and presentational currency

The Scheme's functional and presentational currency is Pounds Sterling (GBP).

Assets in other currencies are converted to Pounds Sterling at the rates of exchange ruling at the year end. Transactions in other currencies are translated into Pounds Sterling at the spot exchange rate at the date of the transaction.

Gains and losses arising on conversion or translation are dealt with as part of the change in market value of investments.

Contributions

Normal contributions, both from employees and the Employer, are accounted for on an accruals basis in the period to which they relate.

Employer's deficit funding is accounted for in the year in which it falls due in line with the Schedules of Contributions.

ABF contributions have been received in accordance with the Schedules of Contributions.

Benefits paid or payable

Pensions in payment, including pensions funded by annuity contracts, are accounted for in the period to which they relate.

Benefits are accounted for in the period in which the member notifies the Trustee of their decision on the type and amount of the benefit to be taken, or if there is no member choice, on the date of retiring or leaving.

Where tax liabilities are settled on behalf of members, for example where the lifetime allowance or annual allowance is exceeded, the tax due is accounted for on the same basis as the benefit.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

3. Accounting policies (continued)

Payments to and on account of leavers

Individual transfers to other schemes are accounted for when member liability is discharged which is normally when the transfer amount is paid.

Administrative expenses

Administrative expenses are accounted for on an accruals basis.

Investment income

Income from pooled investment vehicles is accounted for when declared by the fund manager.

Income arising from the underlying investments of the pooled investment vehicles, which is reinvested within the pooled investment vehicles, is reflected in the unit price. Such income is reported within the change in market value.

Income from cash and short-term deposits is accounted for in these financial statements on an accruals basis.

All investment income is stated inclusive of any related recoverable taxation but net of any irrecoverable tax, including overseas withholding taxes and the costs of collection.

Income arising from insurance policies held by the Trustee to fund benefits payable to Scheme members is included within investment income and is accounted for on an accruals basis.

Change in market value of investments

The change in market value of investments during the year comprise all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments and unrealised changes in market value. In the case of pooled investment vehicles which are accumulation funds, where income is reinvested within the fund without issue of further units, change in market value also includes such income.

Investment management expenses

Investment management fees and rebates are accounted for on an accruals basis.

Management fees for pooled investment vehicles are incorporated in the unit price and reflected in change in the market value of investments in the Fund Account.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

3. Accounting policies (continued)

Valuation of investment assets

Investments

Investment assets are included in the financial statements at fair value. The methods of determining fair value for the principal classes of investment are:

Pooled investment vehicles which are unquoted or not actively traded are stated at bid price or single price where there is no bid/offer spread as provided by the investment managers at the year end.

In the case of property funds included within pooled investment vehicles, these are valued by the investment managers. In the case of property fund of funds, the unit price used by the fund manager is based on the net asset valuations ("NAVs") provided by the underlying fund managers. As at 31 March 2020, trading in the Threadneedle Property Unit Trust and BlackRock UK Property Fund, which are property pooled investment vehicles, was suspended. This decision followed notification from the Funds' independent valuers that they were unable to value the Fund's assets with certainty in the current exceptional market environment. Whilst there is a material uncertainty over the valuation of these funds, the implications of COVID 19 are reflected in the valuations.

Insurance policies are valued by the Actuary at the present value of the related obligation, determined using the most recent Scheme Funding valuation assumptions updated for market conditions at the reporting date. These policies are to provide pension benefits for all members or define the group covered. Insurance policies bought to provide members' benefits are included in the Statement of Net Assets at their actuarial value as determined by the Actuary as at 31 March 2020.

With profits insurance policies held as AVC investments are reported at the policy value provided by the insurer based on cumulative reversionary bonuses declared and the current terminal bonus.

AVC funds are included within the Statement of Net Assets on the basis of fair values provided by the AVC provider at the year end.

In the case of private equity investments, these are valued by the investment managers using the International Private Equity and Venture Capital Guidelines. These are valued at the year end, or if a valuation is not available as at the year end, at the latest valuation available adjusted for known cash movements.

Asset backed funding

The ABF has been stated at an estimated fair value. The fair value of the arrangement is based on the net present value of the cash flows expected from the arrangement, with due allowance for credit and illiquidity risk and the funding level of the Scheme. If, within the lifetime of the ABF, the Scheme becomes fully funded (excluding the value of the Trustee's interest) on a technical provisions basis for four consecutive quarter ends during the term of the ABF, then the payments from the ABF to the Scheme will cease. Similarly, if the technical provisions funding position subsequently falls beneath fully funded for two successive quarter ends, the payments from the ABF will resume. An independent valuation has been undertaken at the year end date by the Scheme Actuary.

ABF sales are in respect of receipts generated by the underlying asset and are accounted for on an accruals basis.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

4. Contributions

	2020 £000	2019 £000
Employer:		
Normal	17,673	19,116
Deficit funding	10,000	8,000
	<u>27,673</u>	<u>27,116</u>
Employee:		
Normal	<u>991</u>	<u>1,055</u>

Under the Schedule of Contributions certified by the Scheme Actuary on 24 February 2020, deficit funding contributions were payable monthly by the Employer at a rate of £1,184,433 per month from April 2019 to March 2020. The Schedule of Contributions specifies that these contributions be offset against monthly payments received by the Scheme from the ABF Investment (see note 10).

In addition, monthly deficit contributions (as detailed below) are being paid by the Employer to the Scheme in accordance with the Recovery Plan dated 24 February 2020 in order to improve the Scheme funding position.

- from April 2019 up to and including January 2020, were £916,667.
- for February 2020, was £833,333.
- for March 2020, was £nil.
- from April 2020, up to and including March 2021, will be £833,333.
- from April 2021, up to and including March 2022, will be £916,667.
- from April 2022, up to and including July 2025, will be £1,000,000.

5. Other income

	2020 £000	2019 £000
Other income	<u>6</u>	<u>2</u>

6. Benefits paid or payable

	2020 £000	2019 £000
Pensions	42,394	40,526
Commutations of pensions and lump sum retirement benefits	8,200	11,885
Purchase of annuities	9	-
Lump sum death benefits	891	742
Taxation where lifetime or annual allowance exceeded	-	171
	<u>51,494</u>	<u>53,324</u>

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

7. Payments to and on account of leavers

	2020 £000	2019 £000
Individual transfers to other schemes	21,925	33,298
Payments to members joining state scheme	(14)	-
	<u>21,911</u>	<u>33,298</u>

Payments to members joining the state scheme includes a receipt of £32k in respect of funds received from HMRC due to a financial reconciliation of State Scheme premia.

8. Administrative expenses

	2020 £000	2019 £000
Administration and processing	334	-
Actuarial fees	599	-
Audit fees	54	-
Legal fees	191	-
Other professional fees	165	-
Trustee fees and expenses	18	-
Sundry expenses	4	2
	<u>1,365</u>	<u>2</u>

From 1 February 2020, under the revised Schedule of Contributions certified by the Scheme Actuary on 24 February 2020, certain administrative expenses are now borne directly by the Scheme.

In the current year, administrative expenses were incurred relating to project work on the annuity contract buy in and costs relating to the GMP reconciliation, including contingent spouses. These expenses included costs amounting to £753k which were incurred before 1 February 2020 but were borne by the Scheme following agreement by the Trustee and in accordance with the previous Schedule of Contributions certified on 16 June 2017.

All other administrative expenses of the Scheme are provided by the Principal Employer.

9. Investment income

	2020 £000	2019 £000
Income from pooled investment vehicles	5,993	6,460
Interest on cash deposits	234	216
Annuity income	20,015	9,121
	<u>26,242</u>	<u>15,797</u>

During the year a pensioner buy-in annuity contract with Just was completed. Income from the Just annuity contract is £5,100k (2019: £nil).

In the prior year a pensioner buy-in annuity contract with Canada Life was completed. Income from the Canada Life annuity contract is £14,915k (2019: £9,121k).

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

10. Investments

	Opening value at 1 Apr 2019	Purchases at cost	Sales proceeds	Change in market value	Closing value at 31 Mar 2020
	£000	£000	£000	£000	£000
Pooled investment vehicles	2,020,508	779,268	(1,059,653)	94,987	1,835,110
Asset backed funding	254,700	-	(14,175)	(26,925)	213,600
Insurance policies	383,600	247,304	-	(16,704)	614,200
AVC investments	5,909	-	(771)	297	5,435
	<u>2,664,717</u>	<u>1,026,572</u>	<u>(1,074,599)</u>	<u>51,655</u>	<u>2,668,345</u>
Cash	8,685				38,539
Other investment balances	891				1,436
Total net investments	<u>2,674,293</u>				<u>2,708,320</u>

Income is received from the ABF of £12,200k each year from 1 November 2013 for 25 years in equal monthly instalments and is shown under ABF sales. This income increases annually by RPI up to a maximum of 5% p.a. Payments totalling of £14,175k have been received in this Scheme year.

Following a review of the investment strategy of the Scheme at the end of 2018, c. £233 million was transferred to the LGIM bond portfolio in the first part of the year. This was financed through the disinvestment of the investments held with Bluebay, Mesirow and the LGIM equity portfolio. In addition the investment held with Magnitude was fully disinvested and used to finance capital calls and further investment into the LGIM bond portfolio. Following the transition, the LGIM bond portfolio was adjusted to better reflect the liabilities of the Scheme.

In September 2019, c. £251.6m was disinvested from the LGIM bond portfolio and used to purchase a buy-in policy with Just Retirement covering the existing pensioner and dependent liabilities of the Scheme. The purchase price of the Just annuity contract was adjusted to £247.3m to reflect the terms and conditions of the contract.

Details of pooled investment vehicles purchases and sales can be found on pages 11 and 12 of the Trustee's Report.

Transaction costs

There are no direct transaction costs in the year nor in the previous year. Indirect costs are incurred through the bid-offer spread on pooled investment vehicles. With the exception of the direct transaction costs incurred on the AIL delegated investment fund (see note 11), it is not possible for the Trustee to quantify these indirect costs.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

11. Investment management expenses

	2020 £000	2019 £000
Administration and management fees	1,752	2,301
Management fee rebates	(547)	(902)
	1,205	1,399

Investment management expenses disclosed above do not include monthly fees and any annual performance fee payable to AIL in respect of the delegated investment fund. These fees are deducted from cash within that fund and are therefore reflected in the change in market value of pooled investment vehicles. The base fees payable during the year amounted to £956k (2019: £1,786k). The structure of the fund's investment management fees for the Scheme changed with effect from 1 January 2019 following the introduction of the non-discretionary portfolio. As a result, the Scheme no longer has a performance fee (2019: £2,440k).

12. Taxation

The Scheme is a registered pension scheme in accordance with the Finance Act 2004. This means that the contributions paid by both the Employer and the members qualify for full tax relief, and is exempt from income tax and capital gains tax except for withholding tax on overseas investment income.

13. Pooled investment vehicles

	2020 £000	2019 £000
Bond funds	144,523	-
Cash & liquidity funds	-	9,779
Equity funds	36,814	149,607
Hedge funds	25,045	261,727
LDI funds	15,908	97,328
AIL delegated investment fund	1,337,053	1,250,213
Private equity funds	122,218	89,648
Property funds	153,549	162,206
	1,835,110	2,020,508

The legal nature of the Scheme's pooled arrangements is:

	2020 £000	2019 £000
Open ended investment company	248,642	311,917
Mutual fund	202	89,589
Authorised unit trust	1,439,003	1,449,636
Limited partnership	147,263	169,366
	1,835,110	2,020,508

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

13. Pooled investment vehicles (continued)

The Scheme is the sole investor in the AIL delegated investment fund which is managed by Aon Investments Limited. A breakdown of the underlying assets at the year end is set out below:

	2020 £000	2019 £000
Equities	181,852	254,954
Bonds	137,801	67,089
Property	149,374	119,198
Hedge funds	280,931	250,493
Opportunities portfolio - multi asset	49,930	46,144
Emerging market equities	49,400	54,156
Emerging market bonds	54,280	81,874
Cash and working capital	10,352	2,477
LDI investments	423,133	373,828
	<u>1,337,053</u>	<u>1,250,213</u>

14. Insurance policies

	2020 £000	2019 £000
Insurance policies	<u>614,200</u>	<u>383,600</u>

The Trustee holds insurance policies with Canada Life and Just which provide annuity income to cover pensions for certain members.

Method and assumptions

The values of the bulk annuity policies as at 31 March 2020 are consistent with the technical provisions calculations for the formal actuarial valuation as at 31 March 2019 using the post retirement discount rate, which is the gilt yield curve without any allowance for outperformance. The assumptions used have been modified only insofar as is necessary to maintain consistency with the Statement of Funding Principles dated 12 February 2020, reflecting the change in the effective date and in relevant market conditions.

15. Asset backed funding

	2020 £000	2019 £000
Asset backed funding	<u>213,600</u>	<u>254,700</u>

This facility is provided via an ABF through a Scottish Limited Partnership and secured against the assets of AA Brand Management Limited which is the owner of all of the AA Group's intellectual property.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

16. AVC investments

	2020 £000	2019 £000
Utmost	635	658
Prudential	4,800	5,251
	5,435	5,909

The Trustee holds assets which are separately invested from the main Scheme to secure additional benefits on a money purchase basis for those members electing to pay additional voluntary contributions. Members participating in this arrangement each receive an annual statement made up to 31 March each year confirming the amounts held to their account and movements during the year.

The total amount of AVC investments at the year end is shown above.

Following High Court approval with effect from 1 January 2020, Equitable Life policies were uplifted, investment guarantees and switching rights removed and converted to unit linked policies. The conversion of the Equitable Life Policies has been excluded from sales and purchases in note 10. Subsequent to this, policies were transferred to Utmost Life and Pensions Limited.

AVC investments can be further analysed as:

	2020 £000	2019 £000
With profits	1,870	2,620
Unit trusts	635	98
Other*	2,930	3,191
	5,435	5,909

* The amount represents 31 unitised funds held by Prudential in various investment institutions.

17. Cash and other investment balances

	2020 £000	2019 £000
Cash	38,539	8,685
Amounts due from investment manager	38	-
Other investment balances	1,398	891
	39,975	9,576

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

18. Fair value of investments

FRS102 requires for each class of financial instrument an analysis of the level in the following fair value hierarchy into which the fair value measurements are categorised. A fair value measurement is categorised in its entirety on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

Level 1: The unadjusted quoted price in an active market for an identical asset or liability that the entity can access at the assessment dates;

Level 2: Inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability either directly or indirectly;

Level 3: Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

The Scheme's investment assets fall within the above hierarchy as follows:

	Level 1 £000	Level 2 £000	Level 3 £000	2020 Total £000
Investment assets				
Pooled investment vehicles	-	197,245	1,637,865	1,835,110
Asset backed funding	-	-	213,600	213,600
Insurance policies	-	-	614,200	614,200
AVC investments	-	3,565	1,870	5,435
Cash	38,539	-	-	38,539
Other investment balances	38	-	1,398	1,436
	<u>38,577</u>	<u>200,810</u>	<u>2,468,933</u>	<u>2,708,320</u>

	Level 1 £000	Level 2 £000	Level 3 £000	2019 Total £000
Investment assets				
Pooled investment vehicles	-	256,713	1,763,795	2,020,508
Asset backed funding	-	-	254,700	254,700
Insurance policies	-	-	383,600	383,600
AVC investments	-	3,289	2,620	5,909
Cash	8,685	-	-	8,685
Other investment balances	-	-	891	891
	<u>8,685</u>	<u>260,002</u>	<u>2,405,606</u>	<u>2,674,293</u>

Where the absence of regular trading or the unsuitability of recent transaction prices as a proxy for fair values applies, valuation techniques are adopted and the investment assets are included in Level 3.

Valuation techniques as described in note 3 are applied.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

19. Investment risks

FRS 102 requires the disclosure of information in relation to certain investment risks.

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.

Market risk: this comprises currency risk, interest rate risk and other price risk.

Currency risk: this is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

Interest rate risk: this is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Other price risk: this is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk 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 Trustee determines its investment strategy after taking advice from a professional investment adviser. The Scheme has exposure to these risks because of the investments it makes in following the investment strategy set out below. The Trustee manages investment risks, including credit risk and market risk, within agreed risk limits which are set taking into account the Scheme's strategic investment objectives. These investment objectives and risk limits are implemented through the investment management agreements in place with the Scheme's investment managers and monitored by the Trustee by regular reviews of the investment portfolio.

Investment strategy

The investment objective is to maintain a portfolio of suitable assets of appropriate liquidity which will generate investment returns to meet, together with future contributions, the benefits payable under the Trust Deed and Rules as they fall due.

Further details in respect of 'investment strategy' can be found on page 11 of the Trustee's Report.

i. Credit risk

Credit risk arising on bonds is mitigated by investing in pooled investment vehicles holding leveraged index linked gilts of £15.9m (2019: £97.3M) and non-leveraged gilts of £144.5m (2019: £0m), where the credit risk is minimal. The Scheme's investments with the delegated investment manager AIL totalling £1,337.6m (2019: £1,250.2m) was also exposed to indirect credit risk of £202.2m (2019: £254.1m) in relation to publicly traded bonds and privately agreed credit arrangements held in pooled investment vehicles. Indirect credit risk also arises via direct investments in property debt funds of £31.0m (2019: £14.8m) and direct lending funds of £28.5m (2019: £12.4m). Of the indirect credit risk to which the Scheme is exposed, £261.7m is unrated.

Direct credit risk arises from the Scheme's investments in pooled investment vehicles, as there is the possibility that the pooled fund managers will fail to discharge their obligations to investors. This risk is mitigated by the underlying assets of the pooled arrangements being ring-fenced from the pooled manager, the regulatory environments in which the pooled managers operate and diversification of investments amongst a number of pooled arrangements. The Trustee carries out due diligence checks on the appointment of new pooled investment managers and on an ongoing basis monitors any changes to the operating environment of the pooled manager.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

19. Investment risks (continued)

i. Credit risk (continued)

Within the delegated portfolio, AIL carries out due diligence checks on the appointment of new pooled investment managers and on an ongoing basis monitors any changes to the operating environment of a pooled manager. Pooled investment arrangements used by the Scheme primarily comprise unit linked insurance contracts, authorised unit trusts and limited partnerships (see note 13).

Direct credit risk also arises in respect of the bulk annuity policy held with Canada Life £363.0m (2019: £383.6m) and the new bulk annuity policy with Just £251.2m (2019: £0.0m), which is secured to pay a proportion of the Scheme's liabilities. Whilst insurers in the UK are required to meet stringent solvency requirements, there is nevertheless a small risk of the insurer failing. The Financial Services Compensation Scheme ('FSCS') may provide compensation in this unlikely scenario.

Indirect credit risk arises in relation to underlying investments held in the credit pooled investment vehicle. This risk is mitigated by investing in funds which are well diversified in terms of credit instrument, region, credit rating and issuer. Indirect credit risk arises in relation to exposure via AIL to underlying bond and liability matching pooled investment vehicles. This risk is mitigated through the underlying exposures on an aggregate basis being predominantly investment grade credit securities; however, they may invest in debt securities which may be unrated by a recognised credit rating agency or below investment grade and which are subject to greater risk of loss of principal and interest than higher-rated debt securities. The funds may also invest in debt securities which rank junior to other outstanding securities and obligations of the issuer, all or a significant portion of which may be secured on substantially all of that issuer's assets. The funds may invest in debt securities which are not protected by financial covenants or limitations on additional indebtedness. Risk is mitigated by holding a diverse portfolio of investments with exposure to a range of issues and issuers.

Cash is held by BNYM within financial institutions which are at least investment grade credit rated.

There is also credit risk associated with the ABF not being able to make coupon payments as required by the terms of the ABF. This is mitigated in part by the ABF being backed by the Employer's brand and by the legal structure of the ABF.

ii. Currency risk

Indirect currency risk arises because some of the Scheme's investments £210.2m (2019: £435.4m) are held in overseas markets via pooled investment vehicles. The Trustee has an informal target to hedge c.50% of the currency risk associated with the non-delegated assets. Of the Scheme's investments with AIL c.£91.9m (2019: £18.7m) are held in pooled investment vehicles denominated in overseas currencies. AIL may enter into currency exchange transactions and/or use techniques and instruments to seek to protect against fluctuation in the relative value of its portfolio positions as a result of changes in currency exchange rates between the trade and settlement dates of specific securities transactions or anticipated securities transactions.

iii. Interest rate risk

The Scheme is subject to interest rate and inflation risk because some of the Scheme's investments are held in leveraged index linked gilt funds managed by LGIM totalling £160.4m (2019 £97.3m) and in gilts and index linked gilts on leveraged and unleveraged bases, cash and swaps, through pooled vehicles managed by AIL totalling £423.1m (2019: £373.8m). These investments are held in order to mitigate the impact of interest rate and inflation changes on the Scheme's funding position.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

19. Investment risks (continued)

iii. Interest rate risk (continued)

If interest rates fall the value of these funds will rise to help offset some of the increase in actuarial liabilities because of a decrease in the discount rate. The Scheme no longer has exposure to pooled bond investment vehicles through a multi asset credit fund although previously had exposure of £89.5m as at 31 March 2019. Via the delegated manager, the Scheme had pooled bond investment vehicle exposure of £192.1m (2019: £149.0m) where the market values could fluctuate from interest rate changes.

The value of the annuity will be impacted by changes to interest rate expectations, however this acts to hedge similar movements in a section of the Scheme's liabilities and is designed to reduce overall risk.

iv. Other price risk

Other price risk arises principally in relation to the underlying assets in the Scheme's return seeking portfolio which is held in pooled vehicles directly or through AIL as shown below

	2020	2019
	£	£
Global equities	261m	459m
Return seeking bonds and other credit strategies	199m	184m
Hedge funds	268m	370m
Infrastructure	17m	19m
Private equity	27m	23m
Property and property debt	280m	269m

This exposure to overall price movements is managed by constructing a diverse portfolio of investments across various markets.

20. Concentration of investments

The following investments, excluding UK Government securities, account for more than 5% of the net assets of the Scheme.

	2020		2019	
	Value £000	%	Value £000	%
Canada Life	363,000	13.3	383,600	14.3
Just	251,200	9.2	-	-
ABF - Scottish Limited Partnership	213,600	7.9	254,700	9.5
Insight LDI SO 25 GBPNPV*	182,991	6.7	151,929	5.7
Adept SF27*	181,831	6.7	135,168	5.0

* The Scheme is the sole investor in a delegated investment fund – see note 13. The investment in the Hewitt Main Portfolio AO1 represents 49.2% (2019: 46.5%) of the net assets of the Scheme. The Insight LDI SO 25 GBPNPV and Adept SF27 are funds within the Hewitt Main Portfolio AO1

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

21. Current assets

	2020 £000	2019 £000
Employer contributions due	1,417	2,205
Employee contributions due	85	85
Cash balances	11,907	12,862
Sundry debtors	113	188
	<u>13,522</u>	<u>15,340</u>

All contributions due to the Scheme were received in accordance with the Schedule of Contributions.

22. Current liabilities

	2020 £000	2019 £000
Accrued expenses	927	585
Accrued benefits	718	444
HM Revenue & Customs	2	6
Sundry creditors	1,005	-
	<u>2,652</u>	<u>1,035</u>

The sundry creditor of £1,005k (2019: £Nil) represents annuity income received in advance.

23. Employer related investments

There were no direct Employer related investments during the year or at the year end (2019: nil). The Trustee recognises that indirect investment in the Employer's sponsor group, is possible through holdings in pooled investment vehicles. The Trustee believes that any indirect exposure to shares in the Employer sponsor group were less than 5% at any time during the year and at year end.

The Scheme has taken legal advice to confirm that the ABF is not an Employer related investment.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

24. Related party transactions

Contributions received into the Scheme and any benefits paid in respect of Trustee Directors who are members of the Scheme have been made in accordance with the Trust Deed and Rules.

The Principal Employer is considered a related party. All transactions involved with these entities relate to remittance of monthly contributions required under the Rules of the Scheme.

The Scheme entered into an ABF arrangement during the year ended 2014. An amount of £198m was paid into the ABF which is underpinned by a 25-year loan note backed by royalties payable in respect of the AA's brands. Income is received from the ABF of £12.2m each year for 25 years in equal monthly instalments increasing annually by RPI up to a maximum of 5%. The current value is £214.0m (2019: £255.0m).

Fees and expenses were paid to the Independent Trustee Director in the amount of £18k (2019: £nil) by the Scheme. At the year end a creditor balance of 15k (2019: £nil) is due to be paid.

During the year the Employer paid £4,115k (2019: £3,941k) of administrative costs including PPF levy of £1,312k (2019: £1,032k) and Trustee expenses of £95k (2019: £1k) which related to the operation of the Scheme.

25. Contingent assets and liabilities

GMP Equalisation

On 26 October 2018, the High Court handed down a judgment involving the Lloyds Banking Group's defined benefit pension schemes. The judgment concluded that schemes should be amended to equalise pension benefits for men and women in relation to guaranteed minimum pension benefits. The issues determined by the judgment arise in relation to many other defined benefit pension schemes. The Trustee of the Scheme is aware that the issue will affect the Scheme and will be considering this at a future meeting and decisions will be made as to the next steps. Under the ruling schemes are required to backdate benefit adjustments in relation to GMP equalisation and provide interest on the backdated amounts. Based on an initial assessment of the likely backdated amounts and related interest the Trustee does not deem these to be material to the financial statements and therefore have not included a liability in respect of these matters in these financial statements. They will be accounted for in the year they are determined.

Equalisation of normal retirement ages

Following the Barber judgement in May 1990, the Scheme took steps to equalise Normal Retirement Ages ('NRAs') in April 1992. As a result of preparation for the upcoming GMP equalisation exercise, it was identified that there was some uncertainty surrounding the method of equalising NRAs adopted in 1992. Based on an initial assessment of the likely backdated amounts the Trustee does not deem these to be material to the financial statements and therefore have not included a liability in respect of these matters in these financial statements. They will be accounted for in the year they are determined.

Bulk annuity

The Trustee is undergoing a data cleanse project with the liabilities insured with Canada Life and Just. Depending on the outcome of this project, the Scheme may either have to pay an additional premium, or receive a refund from the premium already paid. Given the uncertainty surrounding the results and subsequent financial impact of this project, it is not possible to make a reasonable estimate of any likely cost or refund arising, and therefore no estimate has been included in these financial statements.

In the opinion of the Trustee, the Scheme had no other contingent assets and liabilities as at 31 March 2020 (2019: £nil).

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2020

26. Capital commitments

The Trustee has invested in a number of private equity arrangements where there are capital commitments which have not been fully drawn. Such commitments are detailed below:

Manager	2020 Total Commitment £000	2020 Commitment Paid £000	2020 Remaining Capital Commitment £000	2019 Remaining Capital Commitment £000
Arcmont	30,000	9,458	20,542	30,000
Ares	30,000	18,336	11,664	21,948
BlackRock Quellos	39,537	37,085	2,452	2,177
Brockton	40,000	19,693	20,307	40,000
BV	10,484	-	10,484	-
Clearbell	80,000	55,728	24,272	30,872
DRC	40,000	22,523	17,477	28,297
GAM	20,000	8,575	11,425	16,470
Keyhaven	32,742	30,224	2,518	2,611
Warburg	41,937	7,926	34,011	39,391
	364,700	209,548	155,152	208,766

INDEPENDENT AUDITOR'S STATEMENT ABOUT CONTRIBUTIONS FOR THE YEAR ENDED 31 MARCH 2020

Statement about contributions payable under the Schedules of contributions

We have examined the Summary of Contributions payable to the AA Pension Scheme, for the Scheme year ended 31 March 2020 which is set out in the Trustee's report on page 44.

In our opinion contributions for the Scheme year ended 31 March 2020 as reported in the Summary of Contributions and payable under the Schedules of Contributions have in all material respects been paid at least in accordance with the Schedules of Contributions certified by the Scheme actuary on 16 June 2017 and 24 February 2020.

Basis of opinion

Our objective is to obtain sufficient evidence to give reasonable assurance that contributions reported in the attached Summary of Contributions have in all material respects been paid at least in accordance with the Schedules of Contributions. This includes an examination, on a test basis, of evidence relevant to the amounts of Contributions payable to the Scheme and the timing of those payments under the Schedules of Contributions.

Responsibilities of Trustee

As explained more fully in the Statement of Trustee's Responsibilities, the Scheme's Trustee is responsible for ensuring that there is prepared, maintained and from time to time revised a Schedule of Contributions which sets out the rates and due dates of certain contributions payable towards the Scheme by or on behalf of the Employer and the active members of the Scheme. The Trustee is also responsible for keeping records in respect of contributions received in respect of active members of the Scheme and for monitoring whether contributions are made to the Scheme by the Employer in accordance with the Schedules of Contributions.

Auditor's responsibilities for the statement about contributions

It is our responsibility to provide a Statement about Contributions paid under the Schedules of Contributions and to report our opinion to you.

Use of our statement

This statement is made solely to the Scheme's Trustee, as a body, in accordance with The Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 made under the Pensions Act 1995. Our work has been undertaken so that we might state to the Scheme's Trustee those matters we are required to state to them in an auditor's statement about contributions and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Scheme's Trustee as a body, for our work, for this statement, or for the opinion we have formed.



Crowe U.K. LLP
Statutory Auditor
London

Date: 22 October 2020

AA PENSION SCHEME

SUMMARY OF CONTRIBUTIONS FOR THE YEAR ENDED 31 MARCH 2020

During the year ended 31 March 2020 the contributions payable to the Scheme were as follows:

	Employer 2020 £000	Employees 2020 £000	Total 2020 £000
Contributions payable under the Schedules of Contributions and as reported by the Scheme auditor			
Normal	17,673	991	18,664
Deficit funding	10,000	-	10,000
	<u>27,673</u>	<u>991</u>	<u>28,664</u>
Contributions payable in addition to those payable under the Schedules and total contributions reported in the financial statements			
Deficit contributions from ABF shown under investment sale proceeds	14,175	-	14,175
Total contributions reported in the financial statements	<u>41,848</u>	<u>991</u>	<u>42,839</u>

Approved by the Trustee and signed on its behalf:

Trustee Director:



Trustee Director:



Date: 20.10.2020

AA PENSION SCHEME

ACTUARIAL CERTIFICATE

Name of scheme: AA Pension Scheme

Adequacy of rates of contributions

1. I certify that, in my opinion, the rates of contributions shown in this schedule of contributions are such that the statutory funding objective could have been expected on 31 March 2019 to be met by the end of the period specified in the recovery plan dated 12 February 2020.

Adherence to statement of funding principles

2. I hereby certify that, in my opinion, this schedule of contributions is consistent with the Statement of Funding Principles dated 12 February 2020.

The certification of the adequacy of the rates of contributions for the purpose of securing that the statutory funding objective can be expected to be met is not a certification of their adequacy for the purpose of securing the scheme's liabilities by the purchase of annuities, if the scheme were to be wound up.

Signature



Date.....24/2/20.....

David Eteen
Fellow of the Institute and Faculty of Actuaries

Aon Hewitt Limited
Verulam Point
Station Way
St. Albans
AL1 5HE

APPENDIX – EXTRACTS FROM STATEMENT OF INVESTMENT PRINCIPLES

Extracts from the Statement of Investment Principles - dated January 2020

The Scheme's stewardship policy

The relevant extract of the SIP (as at Scheme year end 31 March 2020), covering the Scheme's voting and engagement policies, is as follows:

6.2

As part of their delegated responsibilities, the Trustee expects the Scheme's investment managers to:

- Where appropriate, engage with investee companies with the aim to protect and enhance the value of assets; and exercise the Trustee's voting rights in relation to the Scheme's assets.*
- The Trustee regularly reviews the continuing suitability of the appointed managers and takes advice from the Investment Consultant with regard to any changes. This advice includes consideration of broader stewardship matters and the exercise of voting rights by the appointed managers.*

6.3

The Trustee supports the Codes on the corporate governance of UK companies and accordingly expects its appointed Investment Managers to comply with these Codes. Voting should fully consider the "comply or explain" basis of the Codes, with explanations given by companies for non-compliance. The Trustee would also expect the Investment Managers always to exercise their voting rights in UK companies, including when appropriate by registering "votes withheld". Regarding non-UK companies, the Trustee expects the Investment Managers similarly to vote its shares where it is practicable to do so taking account of recognised best practice in corporate governance in the country or market concerned.

6.4

On issues not covered by the UK Corporate Governance and Stewardship Codes, or similar overseas best practice guidance, the Trustee would expect the Investment Managers to vote actively on contentious issues, with the objective of securing the best outcome for the shareholders generally and, where appropriate, setting an example that is appropriate to other companies.

6.5

The Trustee would expect that the Investment Managers should always vote in the best interests of the investee company and never vote in any way that is influenced by their own interests, e.g. because the investee company concerned has a pension fund where the assets are managed by certain Investment Managers.

6.6

The Trustee expects Investment Managers to report to it, when voting on contentious issues, particularly on difficult issues of a fundamental or far reaching nature.

APPENDIX – EXTRACTS FROM STATEMENT OF INVESTMENT PRINCIPLES

Extracts from the Statement of Investment Principles - dated January 2020 (continued)

**The Scheme's
stewardship
policy
(continued)**

6.7

The Trustee generally considers that the responsibility of owning shares in companies carries with it the obligation to exercise shareholder rights in a responsible and proactive way, as this is in the general interests of the shareholder community in which the Trustee must participate as a significant investor.

Through this report, the Trustee reviews how the actions of its asset managers and fiduciary manager have aligned with its expectations and principles set out in the SIP. The Trustee will set out where it expects more information or engagement to be undertaken by its managers.