

Report and Financial Statements

Year ended 31 March 2019

AA PENSION SCHEME

CONTENTS

Trustee and its Advisers	1
Trustee's Report	3
Statement of Trustee's Responsibilities	16
Independent Auditor's Report to the Trustee.....	17
Fund Account.....	19
Statement of Net Assets Available for Benefits.....	20
Notes to the Financial Statements.....	21
Independent Auditor's Statement about Contributions	35
Summary of Contributions	36
Actuarial Certificate.....	37

AA PENSION SCHEME

TRUSTEE AND ITS ADVISERS YEAR ENDED 31 MARCH 2019

Trustee	AA Pensions Trustees Limited
Company Appointed Directors	Mr S Delo representing PAN Governance LLP Independent Trustee (Chairman) Mr C Norman (resigned 1 September 2019) Mr J Stewart Mr M Sullivan (resigned 31 May 2018 and reappointed 1 July 2018) Mr R Warner (resigned 25 April 2019) Mr L Jones (appointed 25 April 2019)
Member-Nominated Directors	Mr P Foster Mr S Millman Mr D Glover
Principal Employer	Automobile Association Developments Limited
Secretary to the Trustee	Mrs Lorraine Birks (appointed 1 July 2018) Mr Mike Sullivan (resigned 31 May 2018)
Actuary	Mr D Eteen (Fellow of the Institute and Faculty of Actuaries (FIA)) Aon Hewitt Limited
Administrator	Aon Hewitt Limited
Independent Auditor	Crowe U.K. LLP
Banker	Bank of Scotland plc
Investment Advisers	Aon Hewitt Limited Valuation Consulting LLP
Investment Managers	Ares Management LLC (appointed 2 May 2018) BlackRock Investment Management Ltd BlackRock Private Equity (formerly Quellos Capital Management) Bluebay Asset Management Brockton Capital LLP Clearbell Capital LP Colombia Threadneedle (formerly Threadneedle Pensions Limited) DRC Capital LLP GAM Fund Management Limited (appointed 12 April 2018) Hewitt Risk Management Services Limited (HRMSL) Keyhaven Capital Partners Legal & General Assurance (Pensions Management) Ltd (LGIM) Magnitude Capital, LLC Mesirow Advanced Strategies, Inc. TH Real Estate (formerly Henderson Global Investors) Warburg Pincus Global Growth-E, L.P. (appointed 29 March 2019)
AVC Providers	The Equitable Life Assurance Society The Prudential Assurance Company Limited
Annuity Providers	Canada Life Limited (Canada Life) (appointed August 2018)

AA PENSION SCHEME

TRUSTEE AND ITS ADVISERS YEAR ENDED 31 MARCH 2019

Custodian	Bank of New York Mellon Corporation (BNYM)
Legal Advisers	Hogan Lovells LLP Squire Patton Boggs (UK) LLP Burness Paul LLP
Data Consultant	ITM Limited
Covenant Adviser	RSM Restructuring Advisory LLP
Fiduciary Overseer	Hymans Robertson LLP
Contact Address	Mrs Lorraine Birks Trustee Services Manager The AA Fanum House Basing View Basingstoke Hants, RG21 4EA Email: lorraine.birks@theaa.com Telephone: 01256 491060

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

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 2019.

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 Hewitt 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 Staff and Management sections are closed to new entrants. The CARE Section is also closed to new entrants for any new employees joining after 1 October 2016.

The Trustee is shown on page 1.

Each Trustee Director is eligible to vote, whether Member Nominated or Employer Appointed 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 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 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 (MNTs) 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 page 1 and 2. The Trustee has written agreements in place with each of them.

Mr Mike Sullivan resigned as Secretary on 31 May 2018. Lorraine Birks was appointed as Secretary on 1 July 2018.

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

Trustee meetings

The full Trustee Board met four times over the year. 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.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Scheme changes

The Trustee invested in a "pensioner buy-in" annuity contract with Canada Life Limited, 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 policy covers pensions for 2,092 members and 418 dependants (data on the day of purchasing the policy, as at September 2018).

Future pension increases regarding the CARE Section, starting from the increase due on 1 April 2018, are based on Consumer Price Index rather than Retail Price Index.

Strength of Employer Covenant

The Trustee monitors the credit rating and financial strength of the AA by having good communication and exchange of information with the AA. The Trustee meets with the Chief Finance Officer or his representative on a six monthly basis. The Trustee's covenant adviser is RSM Restructuring Advisory LLP.

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 members	Deferreds Members	Pensioners	Total
Members at the start of the year	3,573	13,239	8,126	24,938
Adjustments to members	(116)	70	56	10
New spouses and dependant pensions	-	-	81	81
Retirements	(60)	(327)	387	-
Deaths	(2)	(14)	(183)	(199)
Trivial commutations	-	(4)	(41)	(45)
Members leaving with Preserved benefits	(320)	320	-	-
Cessation of pension	-	-	(13)	(13)
Transfers out	-	(95)	-	(95)
Leavers - no further liability	(1)	-	-	(1)
Members at the end of the year	3,074	13,189	8,413	24,676

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Membership (continued)

	Active members	Deferreds members	Pensioners	Total
Staff	-	10,241	7,962	18,203
Management Section 1	-	178	55	233
Management Section 2	-	69	107	176
Management Section 3	-	6	-	6
CARE	3,074	2,695	289	6,058
<hr/>				
Total members at the end of the year	3,074	13,189	8,413	24,676

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

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

Included in the above are 2,092 (2018: nil) pensioners and 418 (2018: nil) beneficiaries whose benefits are provided by annuities.

Included in the number of pensioners above are 1,362 (2018: 1,357) beneficiaries in respect of the following sections:

CARE	43
Staff	1,315
Management Section 1	4
Total	<u>1,362</u>

Pension increases

Pensions in payment are increased in April each year in line with the increase in the Customer Prices Index up to a maximum of 6.0% 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. Deferred pensions are increased in line with legislative requirements.

A history of recent pension increases has been:

April 2013	2.6% on pre 1 July 2010 accrued pension; 2.5% on post 1 July 2010 accrued pension
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

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Pension increases (continued)

As the Consumer Prices Index was less than 5.0% for the purposes of the April 2018 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 or Consumer Prices Index in accordance with the Scheme rules.

There were discretionary increases in the year. The Trustee provided a 3.0% discretionary revaluation on CARE benefits accrued prior to 1 April 2010 for those members who joined the CARE section after 1st October 2005.

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

Jersey	
Pre 23 September 1999:	3.1% increase on 1 April 2018 (Jersey cost of living index floored at 0.0%)
Post 23 Sept 1999:	3.1% increase on 1 April 2018 (Jersey cost of living index capped at 5.0% and floored at 0.0%)
Guernsey	
Pre 23 September 1999:	2.0% increase on 1 April 2018 (Guernsey retail price index floored at 0.0%)
Post 23 Sept 1999:	2.0% increase on 1 April 2018 (Guernsey retail price index capped at 5.0% and floored at 0.0%)

Transfer values

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 member's benefits includes no allowance for any discretionary benefits which might be awarded in the future.

Transfers into the Scheme are not allowed.

Contributions

During the year, contributions were receivable under the Schedule of Contributions certified by the Scheme Actuary on 16 June 2017 as follows:

- 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 contribution rates 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 were receivable:
 - from the employer at an amount of £666,667 per month; and
 - in addition, deficit funding contributions were payable monthly by the Employer at a rate of £1,146,595. The Schedule of Contributions specifies that the contributions of £666,667 per month be offset against monthly payments received by the Scheme from the Asset Backed Funding Investment.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

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 base 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 2016. All figures quoted exclude AVCs from both the assets and liabilities.

The value of the Technical Provisions was:	£2,201 million
The value of the assets was:	£1,835 million
As a percentage of Technical Provisions	83%

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	£4,013 million
Value of assets available to meet solvency liabilities	£1,835 million
As a percentage of solvency liabilities	46%

The Scheme also carried out an actuarial assessment as at 31 March 2018 and the results are shown below:

The value of the Technical Provision was:	£2,655 million
The value of Assets was:	£2,313 million
As a percentage of Technical Provision:	87 %

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 pay increases, 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 Hewitt 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 Hewitt gilt yield curve based on the Bank of England gilt yield curve at the actuarial valuation date.

Future retail price inflation: The term dependent rates on the Aon Hewitt RPI yield curve based on the Bank of England RPI curve. No allowance is made for any inflation risk premium.

Future consumer price inflation: The assumption is derived at the actuarial valuation date by deducting 1.1% p.a. from the RPI inflation assumption.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Report on Actuarial liabilities (continued)

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.

Pension increases: Inflation-linked pension increase assumptions are derived from the RPI inflation assumption (except in respect of post 5 April 1988 GMP which is 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.

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.

However, active members' benefits accrued up to 30 June 2010 are assumed to increase in future in line with deferred revaluations rather than salary increases. Benefits accrued after 30 June 2010 are assumed to increase each year in line with increases in salaries but subject to individual member-specific pensionable salary caps that apply on a year by year basis (and work in a similar way to the earnings cap). Note that pensionable salary caps were introduced on 1 July 2010 and were set equal to each member's Final Pensionable Earnings as at 30 June 2010 with an uplift of 2.5% or 3% depending on member election.*

Pensionable salary caps are increased at each 1 April at either 2.5% or 3% depending on member selection.

Mortality: for the period in retirement, 100% of standard tables S2PMA for male members and S2PFA for female members, adjusted for year of birth with an allowance for improvements between 2007 and 2015.

An allowance for future improvements has been made in line with the CMI_2015 Core Projections assuming 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 16 June 2017. A copy of this certificate is included on page 37 of the annual report.

*This assumption reflected the approach agreed for the purposes of Technical Provisions for the 2016 actuarial valuation. Subsequent to this actuarial valuation accrual in the final salary sections ceased on 30 June 2017 and those benefits are treated as deferred benefits.

Next actuarial valuation

The next actuarial valuation, due as at 31 March 2019, is currently being prepared.

GMP Equalisation

Following the High Court On 26 October 2018 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. 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 has not included a liability in respect of these matters in these financial statements.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Investment strategy and principles

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

In accordance with section 35 of the Pensions Act 1995, the Trustee has agreed a Statement of Investment Principles ("SIP") which was last revised on January 2019. In July 2019 the Trustee further reviewed its SIP to incorporate the Trustee's policy on Responsible Investing. In summary, when setting the Scheme's investment strategy, the Trustee's primary concern is to act in the best financial interests of the Scheme and its beneficiaries, seeking the best return that is consistent with a prudent and appropriate level of risk. The risks considered include the risk that environmental, social and governance factors including climate change negatively impact the value of investments held if not understood and evaluated properly. The Trustee considers this risk by taking advice from its investment adviser when setting the Scheme's asset allocation, when selecting managers and when monitoring their performance. A copy of the SIP may be obtained from the contact for enquiries on page 2.

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 Statement of Investment Principles ("SIP").

The investment strategy at 31 March 2019 is to hold:

- 29.5% in a diversified portfolio of pooled funds which hold return seeking investments comprising UK and overseas equities, UK commercial property, opportunistic property, property debt, direct lending, hedge funds, multi asset credit and private equity.
- 20% in leveraged index linked gilts, 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 a bulk annuity to match the benefit payments to selected members.
- 50% in a delegated investment portfolio where the investment manager (HRMSL) 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.
- 0.5% in cash to meet pension and other payments.

Investment transitions

During the year, investments of £407.9million held in the LGIM over 15 year gilt and index linked gilt funds were redeemed and the proceeds were invested in LGIM single-stock gilt and index-linked gilt funds.

In August 2018, £141.0million and £209.8million were disinvested from the LGIM single-stock gilt and index-linked gilt funds via cash and in specie respectively and £350.8million was invested in a "pensioner buy-in" annuity contract from Canada Life Limited, an insurance company, to secure some of the liabilities.

Further to the above transaction, investments of £8.1million, £4.4million and £3.5million were made in private equity funds held with the investment managers, Ares, Bluebay and GAM.

In addition, other smaller disinvestments were made to meet cashflow requirements over the period.

Following the year end, in September 2019, monies were disinvested from LGIM Fixed Interest Gilt and LGIM Index-Linked Gilt Fund and proceeds amounting to £251.6 million 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.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

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 is available on request.

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

The Trustee has considered ethical and socially responsible investments and has delegated to the Investment Managers the responsibility for taking social, environmental and ethical considerations into account when assessing the financial potential and suitability of an investment and for exercising the 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 manager makes its 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.

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 2019 is summarised as follows:

Period	Scheme return (%)	Benchmark return (%)
1 year	3.4	3.8
3 years	10.7	5.0
5 years	10.0	5.2

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Investment report (continued)

The principal economic factors which have affected the benchmarks against which performance is compared over the year to 31 March 2019 were as follows:

- In contrast to the strong and relatively stable equity market uptrend seen through much of 2016 and 2017, 2018 and 2019 have seen lower returns and higher volatility. Having fallen at the start of 2018 and largely recovered by the middle of the year, global equities were again rocked. Rising concerns of slowing global growth and corporate earnings, alongside trade war fears, led to a 12.5% fall in global equities over Q4 2018, the steepest quarterly decline since 2011. Concerns eased in the new year, helping markets rise by 12.3% over Q1 2019
- The US Federal Reserve (Fed) continued its course to normalise monetary policy though 2018 but abruptly changed track in January 2019 by announcing that further rate hikes would be put on hold and their bond buying program would end. Over the period to March 2019, the Fed hiked the Federal Funds rate on three occasions, reaching 2.25%-2.50% in December 2018. The European Central Bank (ECB) ended their asset purchase program in December, although reinvestment of principal payments is continuing indefinitely. Meanwhile, the Bank of England (BoE) raised rates to 0.75% in August as economic data stabilised and inflation remained above target.
- Production cuts undertaken by the Organization of the Petroleum Exporting Countries (OPEC) and increased geopolitical tensions drove up Brent oil prices over much of the first half of the year, peaking at \$86/bbl in October. Prices rebounded somewhat in Q1 2019 as fears eased with the price of Brent Crude ending the year down 2.7% at \$68/bbl. Amidst weakening Chinese economic data and heightened trade tensions, industrial metals also fell sharply in Q4 2018 but rebounded over Q1 2019, falling 4.1% over the year and resulting in the S&P GSCI Commodity index finishing the year to March 2019 down 3.0%.
- UK fixed interest gilt yields had a volatile year, tending to rise and fall in tandem with global yields and Brexit developments. Yields fell sharply over the second half of the period amidst lowered monetary tightening expectations and downgraded growth and inflation outlooks. Yields fell across the curve but particularly at longer maturities. Index-linked gilts outperformed fixed interest gilts as they returned 5.5% versus 3.7%, boosted by higher breakeven inflation.
- UK investment grade corporate bond credit spreads widened by 16bps to end the twelve-month period at 142bps. Spreads widened steadily through the first half of the year before widening more rapidly in Q4 2018 against a backdrop of heightened volatility of risky assets. Spreads narrowed, however, in Q1 2019 as risk sentiment improved.
- UK commercial property returned 5.6%, supported by a steady income return. Capital value appreciation slowed through the year with capital values falling in Q4 2018 and Q1 2019. The retail sector underperformed over the year as fears over the health of the high street took hold and UK economic performance remained lacklustre.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Investment report (continued)

Scheme performance

With this market background, over the year to 31 March 2019 the Scheme returned 3.4%, underperforming its benchmark return of 3.8% as reported by BNY Mellon.

The delegated investment portfolio returned 6.7% over the year, matching the liability proxy benchmark. This return of 6.7% was comprised of 0.0% in Q2 2018 (where strong returns in global equities were offset by negative returns of -0.8% on the hedging component); -0.8% in Q3 2018 (where returns of -2.2% on the hedging component was offset by strong returns on equities); -1.6% in Q4 2018 (largely due to sharp declines in global equities and negative returns on the hedging component) and 9.4% in Q1 2019 (main contributors were the liability hedging assets returning 6.2% and the global equity managers returning between 7% and 13%).

LGIM passive equities and gilts performed broadly in line with their respective benchmarks. The Scheme has a bespoke mix of regional equity funds with returns over year ranging from -4.5% on Japanese equities (currency hedged) to 17.6% on North American equities (currency unhedged).

The private equity funds had mixed performance over the year. Quellos returned 30.7%, with 22.7% coming from asset selection and management and 8% from Sterling weakening against other US dollar. Keyhaven returned -16.3% underperforming its benchmark by 31.4%, as reported by BNY Mellon.

Core property returns were close to their benchmark, with BlackRock returning 4.9% (0.1% ahead of benchmark) and Threadneedle returning 4.6% (0.2% behind the benchmark). Threadneedle's relative returns were influenced positively by an overweight allocation to industrial sector and negatively by an overweight exposure to retail sector and a larger than average cash holding. Quarterly returns were 1.7%, 1.4%, 1.0%, 0.4% over the year. Blackrock's relative returns were influenced positively by an overweight allocation to the alternatives sector and by an underweight exposure to retail sector. Quarterly returns were 1.9%, 1.7%, 1.2%, 0.1% over the year.

The opportunistic property funds returns were very strong in absolute terms, and mixed relative to benchmark, over the year. Brockton returned 18.1%, outperforming its benchmark by 3.0% whilst Clearbell funds returned 12.3% and 13.1% underperforming their respective benchmarks by 1% to 2%.

Property Debt performed reasonably over the year given they are early in their fund lives when costs are incurred by the fund managers. Over the year DRC returned 5.2% in absolute terms, against a target of 6.8%. The investment with GAM commenced in August 2018, so only 8 months during which returns have been negative as is often the case with such illiquid, closed ended funds.

Hedge fund performance was weak over the year, with both Magnitude and Mesirov underperforming their benchmarks and returning absolute returns of 0.3% and -0.6% respectively. Redemptions from both managers have been made.

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 22 to the financial statements.

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

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. 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's or their own pension position, or wish to obtain further information, they should contact Aon Hewitt 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 Hewitt Limited
PO Box 196
Huddersfield
HD8 1EG
Email: aa.pensions@aonhewitt.com

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

Lorraine Birks
Trustee Services Manager
The AA
Fanum House
Basing View
Basingstoke
Hants
RG21 4EA
Email: pensions@theaa.com

The Trustee and Aon Hewitt 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 2019

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.

Other information

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 trace 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
<https://www.gov.uk/find-pension-contact-details>

Resolving difficulties/Internal Dispute Resolution

It is expected that most queries relating to benefits can be resolved with the Scheme's administration office. 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 the Trustee office.

If the complaint is not resolved satisfactorily, the Government appointed Pensions Ombudsman can investigate complaints of injustice by bad administration either by the Trustee or the Scheme's Administrators, 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
enquires@pensions-ombudsman.org.uk
www.pensions-ombudsman.org.uk

AA PENSION SCHEME

TRUSTEE'S REPORT YEAR ENDED 31 MARCH 2019

Compliance Statement (continued)

The Pensions Regulator

The Pensions Regulator (TPR) is the 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 pensions.

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

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

Further information

Requests for additional information about the Scheme generally, or queries relating to members' own benefits, should be made to the contact address shown on page 2.

AA PENSION SCHEME

STATEMENT OF TRUSTEE'S RESPONSIBILITIES YEAR ENDED 31 MARCH 2019

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 the 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.

Signed for and on behalf of the Trustee:

Trustee Director:

Trustee Director:

Date:

AA PENSION SCHEME

INDEPENDENT AUDITOR'S REPORT TO THE TRUSTEE YEAR ENDED 31 MARCH 2019

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

We have audited the financial statements of the AA Pension Scheme ("the Scheme") for the year ended 31 March 2019 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 2019, 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.

AA PENSION SCHEME

INDEPENDENT AUDITOR'S REPORT TO THE TRUSTEE YEAR ENDED 31 MARCH 2019

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 16, 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 it 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:

AA PENSION SCHEME

FUND ACCOUNT FOR THE YEAR ENDED 31 MARCH 2019

	Note	2019 £000	2018 £000
Employer contributions	3	27,116	28,883
Employee contributions	3	1,055	1,386
		28,171	30,269
Other income	4	2	77
		28,173	30,346
Benefits paid or payable	5	(53,324)	(48,370)
Transfers out	6	(33,298)	(26,317)
Administrative expenses	7	(2)	(1)
		(86,624)	(74,688)
Net withdrawals from dealing with members		(58,451)	(44,342)
Returns on investments			
Investment income	8	15,797	5,893
Change in market value of investments	9	182,139	91,147
Investment management expenses	10	(1,399)	(1,013)
Net return on investments		196,537	96,027
Net increase in the fund during the year		138,086	51,685
Opening net assets		2,550,512	2,498,827
Closing net assets		2,688,598	2,550,512

The notes on pages 21 to 34 form part of these financial statements.

AA PENSION SCHEME

STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AS AT 31 MARCH 2019

	Note	2019 £000	2018 £000
Investment assets			
Pooled investment vehicles	12	2,020,508	2,298,154
Asset backed funding	14	254,700	230,200
Insurance policies	13	383,600	-
AVC investments	15	5,909	7,480
Cash	16	8,685	3,455
Other investments balances	16	891	606
		2,674,293	2,539,895
Total net investments		2,674,293	2,539,895
Current assets	20	15,340	11,434
Current liabilities	21	(1,035)	(817)
Net assets available for benefits at 31 March		2,688,598	2,550,512

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 and Actuarial Certificate and these financial statements should be read in conjunction with them.

The notes on pages 21 to 34 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:

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

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 guidelines set out in the Statement of Recommended Practice (SORP) (2015) - Financial Reports of Pension Schemes.

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.

2. Accounting policies

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

Functional and Presentational Currency

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

Assets and liabilities in other currencies are converted to Sterling at the rates of exchange ruling at the year end. Transactions in other currencies are translated into 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 and prior year additional voluntary contributions, both from employees and employers, are accounted for on an accruals basis in the period to which they relate.

Employers' deficit funding is accounted for in the year in which it falls due in line with the Schedule of Contributions.

ABF Contributions have been received in accordance with the Schedule of Contributions.

Transfers to other schemes

Individual transfers to other schemes are accounted for when funds are paid.

Benefits paid or payable

Pensions in payment are accounted for in the period to which they relate.

Benefits to members are accounted for in the period in which they fall due for payment. Where there is a choice, 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. If there is no member choice, benefits are accounted for on the date of 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.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

2. Accounting policies (continued)

Administrative expenses

Administrative expenses are accounted for on an accruals basis.

Investment income

Income from any pooled investment vehicle which distributes income is accounted for on an accruals basis on the date stock is declared ex dividend.

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 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.

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

Change in market value

The change in market value of investments during the year comprises 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.

Transaction costs

Transaction costs are included in the cost of purchases and sale proceeds. Transaction costs include costs charged directly to the Scheme such as fees, commissions, stamp duty and other fees. Other investment management expenses are accounted for on an accruals basis and shown separately within investment returns.

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 market value of investments in the fund account.

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 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.

Insurance policies are valued by the Actuary at the amount 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 for all members or define the group covered.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

2. Accounting policies (continued)

Investments (continued)

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 2019.

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.

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. Where the formal pricing of these funds has been frozen due to lack of liquidity within the property market, the funds have been valued at the year end NAVs provided by the underlying property managers or if not available at an estimate provided by the property fund of fund manager.

Asset backed funds

The Asset Backed Funding (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.

3. Contributions

	2019 £000	2018 £000
Employer:		
Normal	19,116	20,883
Deficit funding	8,000	8,000
	<u>27,116</u>	<u>28,883</u>
Employee:		
Normal	1,055	1,282
Additional voluntary contributions	-	104
	<u>1,055</u>	<u>1,386</u>

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

3. Contributions (continued)

Under the Schedule of Contributions certified by the Scheme Actuary on 16 June 2017, deficit funding contributions were payable monthly by the Employer at a rate of £1,146,595 per month from April 2018 to March 2019. The Schedule of Contributions specifies that these contributions be offset against monthly payments received by the Scheme from the Asset Backed Funding Investment (see note 9).

From April 2018 up to and including March 2019, monthly deficit contributions were £666,667.

From April 2019 up to and including March 2021, monthly deficit contributions will be £916,667 increased from April 2020 by RPI up to a maximum of 5% per annum and a minimum of 0%.

From April 2021 up to and including June 2026, monthly deficit contributions will be £1,083,333 increased each April by RPI up to a maximum of 5% and minimum of 0%.

4. Other income

	2019 £000	2018 £000
Other income	2	77

5. Benefits paid or payable

	2019 £000	2018 £000
Pensions	40,526	38,438
Commutations of pensions and lump sum retirement benefits	11,885	9,321
Lump sum death benefits	742	597
Taxation where lifetime or annual allowance exceeded	171	14
	<u>53,324</u>	<u>48,370</u>

6. Transfers out

	2019 £000	2018 £000
Individual transfers out to other schemes	<u>33,298</u>	<u>26,317</u>

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

7. Administrative expenses

	2019 £000	2018 £000
Sundry expenses	2	-
Bank charges	-	1
	2	1

Other than Sundry Expenses, the administration and management of the Scheme is provided by the Principal Employer. These costs are not charged to the Scheme.

8. Investment income

	2019 £000	2018 £000
Income from pooled investment vehicles	6,460	5,725
Interest on cash deposits	216	168
Annuity income	9,121	-
	15,797	5,893

9. Investments

	Opening value at 1 Apr 2018 £000	Purchases at cost £000	Sales proceeds £000	Change in market value £000	Closing value at 31 Mar 2019 £000
Pooled investment vehicles	2,298,154	523,591	(912,240)	111,003	2,020,508
Asset backed funding	230,200	-	(13,716)	38,216	254,700
Insurance policies	-	350,839	-	32,761	383,600
AVCs	7,480	-	(1,730)	159	5,909
	2,535,834	874,430	(927,686)	182,139	2,664,717
Cash	3,455				8,685
Other investments balances	606				891
Total net investments	2,539,895				2,674,293

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% per annum.

Payments totalling of £13,717k have been received in this Scheme year.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

9. Investments (continued)

During the year, investments of £407.9million held in the LGIM over 15 year gilt and index linked gilt funds were redeemed and the proceeds were invested in LGIM single-stock gilt and index-linked gilt funds.

In August 2018, £141.0 million and £209.8 million were disinvested from the LGIM single-stock gilt and index-linked gilt funds via cash and in specie respectively and £350.8million was invested in a "pensioner buy-in" annuity contract from Canada Life Limited, an insurance company, to secure some of the liabilities.

Further to the above transactions, investments of £8.1million, £4.4million and £3.5million were made in private equity funds held with Ares, Bluebay and GAM.

10. Investment management expenses

	2019 £000	2018 £000
Administration and management fees	2,301	1,269
Management fee rebates	(902)	(256)
	<u>1,399</u>	<u>1,013</u>

Investment management expenses disclosed above do not include monthly fees and any annual performance fee payable to Hewitt Risk Management Services Limited in respect of the delegated investment fund (see note 11). These fees are deducted from cash within the fund and are therefore reflected in the change in market value of pooled investment vehicles. The base fees payable during the year amounted to £1,786k (2018: £1,800k) and the performance fee that became payable during the year amounted to £2,440k (2018: £1,413k).

11. Transaction costs

Indirect costs are incurred through the bid-offer spread on pooled investment vehicles. 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 2019

12. Pooled investment vehicles

	2019 £000	2018 £000
Bond funds	-	421,169
Cash & liquidity funds	9,779	-
Equity funds	149,607	149,080
Hedge funds	261,727	260,264
LDI funds	97,328	-
Other - delegated investment fund	1,250,213	1,228,944
Private equity funds	89,648	79,984
Property funds	162,206	158,713
	2,020,508	2,298,154

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

	2019 £000	2018 £000
Open ended investment company	256,714	570,249
Mutual fund	89,589	92,757
Authorised unit trust	1,449,636	1,426,435
Other	224,569	208,713
	2,020,508	2,298,154

The delegated investment fund is managed by Hewitt Risk Management Services Limited and invests in a diversified range of pooled funds which hold equities, bonds, property, infrastructure, hedge funds, derivatives and liability hedging investments. The Scheme is the sole investor in this fund. A breakdown of the underlying assets at the year end is set out below.

	2019 £000	2018 £000
Equities	254,954	240,793
Bonds	67,089	88,497
Property	119,198	106,385
Hedge Funds	250,493	294,086
Opportunities Portfolio - multi asset	46,144	42,267
Emerging Market Equities	54,156	52,450
Emerging Market Bonds	81,874	83,071
Cash	2,477	2,139
LDI Investments	373,828	319,256
	1,250,213	1,228,944

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

13. Insurance policies

	2019 £000	2018 £000
Insurance policies	383,600	-

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

14. Asset backed funding

	2019 £000	2018 £000
Asset backed funding	254,700	230,200

This facility is provided via an Asset backed fund (ABF) arrangement 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.

15. AVC investments

	2019 £000	2018 £000
Equitable Life	658	703
Prudential	5,251	6,777
	5,909	7,480

The Trustee holds assets which are separately invested from the main Scheme to secure additional benefits on a money purchase basis for those members who elected 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.

AVC providers can be further analysed as:

	2019 £000	2018 £000
With profits	2,620	3,339
Unit trust	98	123
Other	3,191	4,018
	5,909	7,480

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

16. Cash and other investment balances

	2019 £000	2018 £000
Cash	8,685	3,356
Cash in transit	-	99
Other investment balances	891	606
	9,576	4,061

17. 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 measurement date;

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.

	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 fund	-	-	254,700	254,700
Insurance policies	-	-	383,600	383,600
AVC investments	-	3,289	2,620	5,909
Cash	8,685	-	-	8,685
Other investments balances	-	-	891	891
	8,685	260,002	2,405,606	2,674,293

	Level 1 £000	Level 2 £000	Level 3 £000	2018 Total £000
Investment assets				
Pooled investment vehicles	-	570,249	1,727,905	2,298,154
Asset backed fund	-	-	230,200	230,200
AVC investments	-	4,141	3,339	7,480
Cash	3,455	-	-	3,455
Other investments balances	-	-	606	606
	3,455	574,390	1,962,050	2,539,895

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

18. 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 asset 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 asset 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 asset 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.

Illiquidity risk: this is the risk that an asset is not readily realisable very quickly to meet unforeseen expected cashflow requirements.

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 can be found on page 9 of the Trustee's Report within 'Investment strategy and principle.

i. Credit risk

Credit risk arising on bonds is mitigated by investing in pooled investment vehicles holding leveraged index linked gilts (£97.3m) (2018: £86.9m) which has been added over the past year, where the credit risk is minimal. The Scheme's investment in a pooled total return diversified credit fund (£89.5m) (2018: £92.1m), property debt fund (£14.8m) (2018: £9.5m) and investments with the delegated investment manager (HRMSL) totalling £1,250.2m (2018: £1,228.9m), of which £254.1m (2018: £256.9m) was invested in pooled credit funds, exposes it to indirect credit risk in relation to publicly traded bonds and privately agreed credit arrangements held in these pooled investment vehicles.

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.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

18. Investment risks (continued)

i. Credit risk (continued)

Within the delegated portfolio, HRMSL 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 and authorised unit trusts.

Direct credit risks also arises in respect of the new bulk annuity policy held with Canada Life, which is secured to pay a proportion of the Scheme's liabilities (2019 - £383.6m). 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 HRMSL 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 HRMSL and BNYM within financial institutions which are at least investment grade credit rated.

There is also credit risk associated with the Asset Backed Funding arrangement (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 (£435.4m) (2018: £399.4m) 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 HRMSL c.£18.7m (2018: £18.4m) are held in pooled investment vehicles denominated in overseas currencies.

HRMSL 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 Legal and General Investment Management totalling £97.3m (2018 gilt funds: £86.9m; 2018 index linked gilts funds £334.2m) and in gilts and index linked gilts on leveraged and unleveraged bases, cash and swaps, through pooled vehicles managed by HRMSL totalling £373.8m (2018: £319.3m). 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 2019

18. 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 also has some exposure to pooled bond investment vehicles – a multi asset credit fund (£89.5m) (2018: £92.1m) and via the delegated manager (£149.0m) (2018: £171.6m) 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 HRMSL as shown below:

	2019	2018
	£	£
Global Equities	459m	442m
Return Seeking Bonds and other credit strategies	184m	263m
Hedge Funds	370m	397m
Infrastructure	19m	17m
Private Equity	23m	27m
Property and Property Debt	269m	266m

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

19. Concentration of investments

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

	2019		2018	
	Value £000	%	Value £000	%
Hewitt Main Portfolio A01	1,250,213	46.5	1,228,944	48.2
Canada Life	383,600	14.3	-	-
Asset backed fund	254,700	9.5	230,200	9.0
Legal & General Over 15yr Index-Linked Gilts Fund	-	-	334,234	13.1

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

20. Current assets

	2019 £000	2018 £000
Employer contributions due	2,205	2,640
Employee contributions due	85	103
Prepayments	-	2,998
Bank	12,862	5,693
Sundry debtors	188	-
	<u>15,340</u>	<u>11,434</u>

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

21. Current liabilities

	2019 £000	2018 £000
Accrued expenses	585	179
Accrued benefits	444	625
HM Revenue & Customs	6	13
	<u>1,035</u>	<u>817</u>

In the current year and prior year, all accrued expenses relate to the investment managers expenses.

22. Employer related investments

There were no direct Employer related investments during the year. The Trustee recognises that indirect investment in the Employer's parent company, is possible through holdings in pooled investment vehicles. Based on information provided by the investment managers the Trustee believes that any indirect exposure to shares in the Employer has not exceeded 0.1% of the Scheme assets at any time during the year.

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

23. Related party transactions

During the year the Employer paid £3,941k (2018: £2,878k) of administrative costs including PPF levy of £1,032k (2018: £684k) and Trustee expenses of £1k (2018: £2k) which related to the operation of the Scheme.

During the year two Trustee Directors, Mr P Foster and Mr M Sullivan, received a pension from the Scheme and contributions were paid in accordance with the Scheme Rules for six current or former Trustee Directors who are or were active members of the Scheme: Mr S Millman, Mr C Norman, Mr R Warner, Mr M Sullivan, Mr D Glover and Mr J Stewart.

AA PENSION SCHEME

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

23. Related party transactions (continued)

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 £216.5m.

The Trustee is not aware of any other material related party transactions that require disclosure in the financial statements.

24. Contingent assets and liabilities

In the opinion of the Trustee, the Scheme had no contingent assets and liabilities as at 31 March 2019 (2018: £nil).

25. 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	Total Commitment £000	Commitment Paid £000	Remaining Capital Commitment £000	Remaining Capital Commitment \$/€000
Ares	30,000	8,052	21,948	-
BlackRock Quellos	37,588	35,411	2,177	\$2,839
Bluebay Asset Management	30,000	-	30,000	-
Brockton Capital	40,000	-	40,000	-
Clearbell Capital	80,000	49,128	30,872	-
DRC Capital	40,000	11,703	28,297	-
GAM	20,000	3,530	16,470	-
Keyhaven	31,814	29,203	2,611	€3,037
Warburg Pincus	39,870	479	39,391	\$51,376
	349,272	102,095	208,766	-

26. 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.

AA PENSION SCHEME

INDEPENDENT AUDITOR'S STATEMENT ABOUT CONTRIBUTIONS FOR THE YEAR ENDED 31 MARCH 2019

Statement about contributions

We have examined the summary of contributions payable to the AA Pension Scheme ("the Scheme"), for the year ended 31 March 2019 which is set out on page 36.

In our opinion contributions for the year ended 31 March 2019 as reported in the Summary of Contributions and payable under the Schedule of Contributions have in all material respects been paid at least in accordance with the Schedule of Contributions certified by the Actuary on 16 June 2017.

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 Schedule 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 Schedule of Contributions.

Responsibilities of the 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 Schedule of Contributions.

Auditor's responsibilities for the statement about contributions

It is our responsibility to provide a statement about contributions paid under the Schedule 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:

AA PENSION SCHEME

SUMMARY OF CONTRIBUTIONS FOR THE YEAR ENDED 31 MARCH 2019

During the year ended 31 March 2019 the contributions payable to the Scheme were as follows:

	Employer 2019 £000	Employees 2019 £000	Total 2019 £000
Contributions payable under the Schedule of Contributions			
Normal	19,116	1,055	20,171
Deficit funding	21,716	-	21,716
	<hr/>	<hr/>	<hr/>
	40,832	1,055	41,887
Contributions payable in addition to those payable under the Schedule and total contributions reported in the financial statements			
Deficit contributions from Asset backed fund shown under investment sales	(13,716)	-	(13,716)
	<hr/>	<hr/>	<hr/>
Total contributions reported in the financial statements	27,116	1,055	28,171

Approved by the Trustee and signed on its behalf:

Trustee Director:

Trustee Director:

Date:

AA PENSION SCHEME

ACTUARIAL CERTIFICATE

Actuarial Certificate of the Schedule of Contributions

AA Pension Scheme

Adequacy of rates of contributions

- 1 I certify that, in my opinion, the rates of the contributions shown in this Schedule of Contributions are such that the statutory funding objective could have been expected on 31 March 2016 to be met by the end of the period specified in the recovery plan dated 7 June 2017.

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 7 June 2017.

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 wound up.

Signature

DAVID ETEEN

Date **16 June 2017**

David Eteen

Fellow of the Institute and Faculty of Actuaries

Aon Hewitt Limited

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