Registered in England and Wales: No. 02355834

RAC INSURANCE LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2019

RAC Insurance Limited

Contents

RAC Insurance Limited

Company information

Directors:

J Baker
P Gale
D Hobday
R Templeman
G M Wood

Auditor:

Deloitte LLP
Statutory Auditor
Four Brindleyplace
Birmingham
United Kingdom
B1 2HZ

Registered office:

RAC House
Brockhurst Crescent
Walsall
West Midlands
United Kingdom
WS5 4AW

Company number:

Registered in England and Wales: No. 02355834

Other information:

RAC Insurance Limited is authorised and regulated by the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA").

RAC Insurance Limited ("the Company") is a member of the RAC Group of Companies ("the Group"), which includes RAC Group (Holdings) Limited and its subsidiaries, which during 2019 included RAC Midco Limited, RAC Finance Limited (until 8 January 2019), RAC Finance Group Limited (until 15 January 2019), RAC Finance (Holdings) Limited (until 8 January 2019), RAC Midco II Limited, RAC Bidco Limited, RAC Bond Co plc, RAC Limited, RAC Group Limited, RAC Motoring Services (Holdings) Limited, RAC Motoring Services, RACMS (Ireland) Limited, RAC Financial Services Limited, RAC Insurance Limited, RAC Brand Enterprises LLP, RAC Cars Limited and Risk Telematics UK Limited.

These Financial Statements are presented for the year ended 31 December 2019. Comparatives are presented for the year ended 31 December 2018.

RAC Insurance Limited

Strategic report

For the year ended 31 December 2019

The Directors present their Strategic report for the year ended 31 December 2019.

Basis of preparation

This business review is addressed to, and written for, the Members of the Company with the aim of providing a fair review of business development and performance during the financial year and position at the end of the financial year . In providing this review, the aim is to present a view that is both balanced and comprehensive and is consistent with the size and complexity of the business.

Principal activity

The principal activity of the Company is the provision of insurance relating to roadside assistance and legal expenses products sold by other Group companies.

Review of the business including major events

There were no major events during the current or prior year.

Objectives and future developments

The strategy for the Company is determined by the Directors of the Company's ultimate Parent Company, RAC Group (Holdings) Limited and disclosed in the Annual Report and Financial Statements of that Company. There are no specific future developments expected for this Company.

During early 2020, the worldwide economic environment has been impacted by the emergence of Covid-19 and financial markets have fallen around the world as a result of Covid-19. Given the nature of the Company's business, the type of assets held and the reinsurance arrangements in place, it is not yet possible to determine the full quantitative impact of Covid-19 on the Company. The Group initiated its financial risk response plan and actions to ensure the Group position remains resilient in particular any impact on the supply chain, personnel and delivery of services to customers. The Company's operations and its abliity to service its customers have continued unabated.

Key Performance Indicators ("KPIs")

The financial KPIs set out in the table below are fundamental to the Company's business and reflect focus on the drivers of value that will enable and inform the management team to achieve the Company's business plans, strategic aims and objectives.

	2019	**2018**
Net written premiums (£000's)	13,648	13,233
Increase in net written premiums	3%	2%
Combined operating ratio	91%	84%
Net incurred claims ratio	70%	68%
Net written expenses ratio	22%	16%

The Company also uses a range of other financial and non-financial performance indicators to monitor performance.

The KPIs presented provide management with analysis of the underwriting profitability of the products underwritten by the Company.

The net incurred claims ratio compares the claims paid and the movement in the claims provision, net of reinsurance, against net earned premiums. The net written expenses ratio compares other operating expenses to net written premiums. The combined operating ratio compares the total of the net incurred claims ratio and the net written expenses ratio.

Financial review
The financial position of the Company as at 31 December 2019 is shown in the Statement of financial position on page 17, with the trading results shown in the Income statement on page 16 and the Statement of cash flows on page 19.

Profit before tax decreased by £1,111 thousand to £1,563 thousand (2018: increase of £74 thousand to £2,674 thousand). This was driven by an increase of gross written premiums of £481 thousand as a result of volume increases on Corporate customers offset by net change in provision for unearned premiums of £726 thousand and an increased operating expenses of £813 thousand.

It is the Company's intention to maintain its operating ratio, whilst adhering to strict underwriting disciplines.

Principal risks and uncertainties
A description of the principal risks and uncertainties facing the Company and the Company's risk management policies are set out below with further details in note 18, contingent liabilities and other risk factors are set out in note 16 to the Financial Statements.

Market risk
Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments as a result of fluctuations in interest rates and foreign currency exchange rates. The Company has limited exposure to fluctuations in foreign exchange rates. However, RAC continues to monitor its exposure and will take steps to mitigate its exposure should the value and volume of foreign currency transactions increase in the future. Interest is generated on cash balances, however as this is not a cost to the business, there is limited risk as a result of adverse movements.

Credit risk
Credit risk is the risk of loss in the value of financial assets due to counterparties failing to meet all or part of their obligations.

Management of credit risk is carried out in accordance with the Group's credit risk processes, which include setting exposure limits and monitoring exposures in accordance with ratings set by credit ratings agencies such as Standard & Poor's.

Liquidity risk
Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

The Group has set its investment strategy to ensure it has sufficient liquid funds to meet its expected obligations as they fall due. The risk is measured through review of forecast liquidity each month by the Treasurer to determine whether there are sufficient credit facilities to meet forecast requirements. The Company does not have any obligations for which liquidity risk would be significant.

Regulatory risk
As a regulated entity, the Company is required to hold sufficient capital to meet acceptable solvency levels based on applicable FCA and PRA regulations. The Company's ability to transfer retained earnings to its shareholders is therefore restricted to the extent that these earnings form part of UK regulatory capital.

Relevant capital and solvency regulations ("Solvency II") continue to be used to measure and report the financial strength of regulated companies within the Company.The Company is also subject to regulatory requirements, as set out by the FCA, in relation to product design, marketing materials, sales processes and data protection. To mitigate these risks the Company employs regulatory and compliance specialists to ensure the regulatory and legislative requirements are fully understood and adhered to.

Principal risks and uncertainties (continued)

Brexit risk

The Group defines this as the risk of adverse economic conditions in light of increased uncertainty following the process of the UK leaving the European Union. Furthermore, there is the potential for disruption to the supplies of key products and services required to repair vehicles.

Whilst there remains uncertainty over the practicalities of the UK leaving the European Union, as the UK is currently negotiating new trading relationships with EU countries, fundamentally RAC is a UK focused business, with very limited trade outside of the UK's borders. We expect to be able to continue providing service in other European countries, either directly (as is the case in Ireland) or through existing partnerships. Should there be any negative impact from Brexit to growth prospects for the UK economy, our business has proved in the past to be resilient during recessionary times. RAC continues to monitor the impact of the Brexit transition process process and will take appropriate steps to maintain RAC's competitive position. RAC has also engaged with key suppliers in order to ensure the continuity of supplies following Brexit.

Climate risk

The Group defines this as the risk of damaging the environment in which we operate.

As a motoring organisation we are aware of our environmental impact, with roadside operations being our highest contributor to carbon emissions. We have attained ISO14001 accreditation across the whole of our operation and use a risk management process to identify and address environmental issues resulting from our business.

Our environmental management system focuses on the following areas:

- Identify opportunities to reduce fuel consumption and cut greenhouse gas emissions from our fleet and in our offices;
- Minimise the amount of waste we create, recycle where we can and avoid waste going to landfill; and
- Reducing our demand for water and the amount of water that is lost or wasted on our premises.

Covid-19 risk

The worldwide outbreak of Covid-19 has impacted the global economic environment with financial markets falling around the world. The Group has initiated its financial risk response plan and actions have been taken to ensure the Group position remains resiliant. The Company's operations and its abliity to service its customers have continued unabated.

Capital management

In managing its capital, the Company seeks to:

i. Match the expected cash inflows from its assets with the expected cash outflows from its liabilities as they fall due;
ii. Maintain financial strength to support new business growth and to satisfy the requirements of its members and regulators;
iii. Retain financial flexibility by maintaining strong liquidity; and
iv. Allocate capital efficiently to support growth and repatriate excess capital where appropriate.

General

The Company is a regulated company which holds sufficient capital to meet acceptable solvency levels based on applicable PRA regulations. The Company has been fully compliant with the requirements of Solvency II since 1 January 2016 with Minimum Capital Requirement cover and Solvency Capital Requirement cover of over 2.5 times throughout the year.

RAC Insurance Limited

Strategic report (continued)
For the year ended 31 December 2019

Regulatory bases
Relevant capital and solvency regulations are used to measure and report on the financial strength of the Company. These measures are based on the PRA's current regulatory requirements. Regulatory capital tests verify adequate excess of solvency capital above the required minimum level calculated using a series of prudent assumptions about the type of business that is underwritten. There have not been any regulatory breaches in the reported periods. The emergence of Covid-19 in early 2020 has also not had a material impact on the solvency position of the Company due to the nature of the assets held by the Company.

Section 172(1) Statement
In accordance with the provisions of The Companies (Miscellaneous Reporting) Regulations 2018, RAC Insurance Limited (the "Company") is required to include a statement in its Strategic Report describing how the directors have had regard to the matters set out in s.172 (1) (a)-(f) of the Companies Act 2006 for the 2019 financial year.

The long term success of the Company is at the heart of the Company's "RAC 2025" strategy and the directors play an active role in the development of the strategy. Delivery of the strategy will enable the RAC to take advantage of the changing automotive and mobility markets, providing new products and services that meet customers changing needs allowing the Company to build closer relationships with customers and suppliers, all of which will drive sustainable long term growth at the same time as providing opportunities for colleagues. The Company operates a risk management framework, ensuring that the key risks to the delivery and implementation of the strategy are identified, monitored and managed and the directors discharge their responsibility in this respect through membership of the Board Risk, Audit and Compliance Committee. Further details on the Company's risk management framework are set out on page 3 of the Strategic Report section of this report and note 18 of the Financial Statements.

Long term sustainable growth will only be achieved through strong colleague engagement. The Company ensures that interests of colleagues are taken into consideration through various forums that allow colleagues to meet with and provide feedback to the CEO, the Executive team and the senior leadership team. The Company is also aware of the contribution that other stakeholders, in addition to colleagues, make to the long-term success of the Company and recognises the importance of developing strong relationships with customers, suppliers and community groups, amongst others. The directors receive regular updates on stakeholder engagement at board meetings.

Managing the impact of the Company's operations on the community and the environment is a strategic imperative. This helps to preserve the environment in which the Company operates at the same time as helping to control costs and supporting efficient business performance. A number of business initiatives have been implemented that have had a significant impact on carbon emissions and the Company has attained ISO14001 accreditation. The Company also has in place a number of Community Priorities, reviewed annually, which seek to create long term benefits for local communities. The Company considers that maintaining its reputation for the highest standard of business conduct is a key priority. The board ensures that an appropriate framework, including relevant policies and codes of conduct, is in place to support this and the board is made aware of and involved in the management of all issues that might have a material impact on the Company's reputation for high standards.

As approved by the Board on 02 June 2020

Jo Baker

J Baker
Chief Financial Officer

RAC Insurance Limited

Directors' report
For the year ended 31 December 2019

The Directors present their Annual Report on the affairs of RAC Insurance Limited, together with the audited Financial Statements for the year ended 31 December 2019.

Directors

The names of the current Directors of the Company appear on page 1.

Those in office during the year and up to the date of signing have been as follows:

J Baker
P Gale
D Hobday
R Templeman
G M Wood

None of the Directors had any interest in the shares of the Company during the year.

Objectives and future developments

The Company's strategy is determined by the Directors of the Company's ultimate Parent Company, RAC Group (Holdings) Limited and is disclosed in the Annual Report and Financial Statements of that Company (see note 19(f)).

Dividends

No interim dividends were paid during the year (2018: £6,500 thousand) and the Directors do not recommend payment of a final dividend (2018: £nil).

Employees

The Company has no employees. All employees of the Group are employed and remunerated by RAC Motoring Services, a fellow Group company. Disclosures relating to employees may be found in the Annual Report and Financial Statements of RAC Bidco Limited.

Directors' indemnities

RAC Group (Holdings) Limited, the Company's ultimate Parent Company, has granted an indemnity to the Directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 2006. The indemnity was first granted in 2011 to the Directors of the then RAC Group holding company and was novated to the Directors of this Company in December 2014. The provisions in the Company's Articles of Association constitute "qualifying third party indemnities" for the purposes of section 236 of the Companies Act 2006. These qualifying third party indemnity provisions remain in force as at the date of approving the Directors' report by virtue of the transitional provisions of the Companies Act 2006.

RAC Insurance Limited

Directors' report (continued)

For the year ended 31 December 2019

Going concern

The financial statements have been prepared on a going concern basis, which assumes that the Company has adequate resources to continue in operational existence for the foreseeable future.

The Company made a profit of £1,283 thousand for the year ended 31 December 2019 (2018: £2,166 thousand) and at 31 December 2019 had net assets of £12,824 thousand (2018: £11,541 thousand). The Group's and Company's business activities, together with the factors likely to affect their future development, performance and position are set out in the Strategic report on pages 2 to 5. Details of cash facilities are set out in note 11 to the Financial Statements. The Group's objectives, policies and processes for managing its capital, its financial risk management objectives and its exposure to credit risk and liquidity risk are set out in note 18 to the Financial Statements.

The Directors have assessed the financial position and the prospects and future funding requirements of the Group and compared them to the level of available committed borrowing facilities. This assessment included a review of the Group's financial forecasts and financial instruments for the 15 month period from the date of this report and a consideration of the uncertainties following the emergence of Covid-19. The Directors considered a range of potential scenarios and how these may impact on cash flow, facility headroom and the Group's ability to comply with the terms of its bank debt. The Directors also consider what mitigating actions the Group could take to limit any adverse consequences.

The Company has net assets of £12,824 thousand (2018: £11,541 thousand). The Directors have considered the financial position and future prospects of the Company along with the current and future regulatory requirements. Accordingly, the Directors continue to adopt the going concern basis in preparing the 2019 Annual Report and Financial Statements.

Having undertaken this assessment, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. For these reasons, they continue to adopt the going concern basis in preparing the Company's Financial Statements.

Auditor

Deloitte LLP has expressed its willingness to continue in office as auditor of the Group and Company and their reappointment was proposed to the Board at the April 2020 Board meeting.

Disclosure of information to the auditor

Each person who was a Director of the Company on the date that this report was approved confirms that, so far as the Director is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing their report, of which the auditor is unaware. Each Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

Strategic Report

The Companies Act 2006 requires the Company to prepare a Strategic Report, set out on pages 2 to 5. The Strategic Report includes information about the Company's operations and business model, financial performance throughout the year, likely future developments, key performance indicators, and principal risks.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Financial Statements for each financial year. Under that law the Directors have elected to prepare the Financial Statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union. Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these Financial Statements, International Accounting Standard 1 requires that Directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRS are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

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

Events since the Statement of financial position date

There have been no events since the Statement of financial position date which have a material impact on the Company's financial position as at 31 December 2019.

Since the Statement of financial position date, the worldwide economic environment has been impacted by the emergence of Covid-19 and financial markets have fallen around the world as a result of Covid-19. Given the nature of the Company's business, the type of assets held and the reinsurance arrangements in place it is not yet possible to determine the full quantitive impact of Covid-19 on the Company. The Company remains solvent and its solvency capital ratio remains strong at over 275% (unaudited) as at 30 April 2020 (31 December 2019: 260%) and remained within the Company's risk appetite as at the date of issuing the financial statements (unaudited). Due to its economic signficance, the emergence of Covid-19 in 2020 is considered to be a non-adjusting post balance sheet event.

Approved by the Board on 02 June 2020

J Baker
Chief Financial Officer

RAC Insurance Limited

Independent auditor's report to the members of RAC Insurance Limited

In our opinion the Financial Statements of RAC Insurance Limited (the 'Company'):

- give a true and fair view of the state of the Company's affairs as at 31 December 2019 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the Financial Statements of which comprise:

- the Income statement;
- the Statement of comprehensive income;
- the Statement of financial position;
- the Statement of changes in equity;
- the Statement of cash flows;
- the Accounting policies; and
- the related notes 1 to 20.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union.

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 Company in accordance with the ethical requirements that are relevant to our audit of the Financial Statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the company.

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

Summary of our audit approach

Key audit matters	The key audit matter that we identified in the current year was the valuation of insurance liabilities.
Materiality	The materiality that we used in the current year was £415k which represents 3% of the company's net assets.
Scoping	Audit work to respond to risks of material misstatement was performed directly by the audit engagement team.
Significant changes in our approach	There were no significant changes to our approach compared to 2018, though we refined our focus of the key audit matter related to insurance liabilities. New business was underwritten during year by the Company resulting in changes to the composition of the insurance liabilities when compared to 2018. Accordingly we focused our testing on the Motor Legal Protection (MLP) new product reserving assumptions instead of those related to the Household Legal Protection Policies ("HLPP").

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

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

We have nothing to report in respect of these matters.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the Financial Statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

<table>
<tr><td colspan="2">Covid-19 non-adjusting post balance sheet event</td></tr>
<tr><td>Key audit matter description</td><td>As disclosed in note 20 to the financial statements, non-adjusting post balance sheet event, a global pandemic of Covid-19 has emerged. The responses taken by organisations and governments to manage its spread have led to increased volatility and economic disruption. Management judge the matter to be a non-adjusting event in accordance with accounting standards, since it is indicative of conditions that arose after the reporting period. It is therefore not reflected in the measurement of assets and liabilities at the statement of financial position date.

In response to Covid-19, management has made updates to its financial statements to disclose Covid-19 as a subsequent event, and has assessed the impact on going concern. To support this management performed actions to assess the financial and operational impacts of Covid-19 up to the date of approval of the financial statements. Key actions comprise:

• Revising the going concern forecasts and related assumptions for the RAC group on which the company primarily rely on for its going concern basis;
• Performing scenario testing including reverse stress testing of the key assumptions used in assessing the going concern of the RAC group;
• Monitoring the RAC group and the company's capital and liquidity position including taking action where defined triggers are met in relation to market and other applicable risks;
• Assessing if the appropriate capital surplus is maintained to meet liabilities as they fall due and meet regulatory capital requirements. This includes having robust plans for certain management actions if the RAC group and the company falls outside its approved risk appetite;
• Frequent monitoring of the RAC group's outsourced operations and its ability to continue to serve customers, comply with conduct regulations and maintain appropriate internal controls.

The Company has made disclosures throughout the annual report and financial statements to reflect the results of its assessment, in line with applicable accounting standards and company law. Due to the inherent management judgement in, and the increased level of audit effort, focused on the appropriateness of the financial statement disclosures, we considered this to be a key audit matter. Refer to management's disclosure in notes B and 20 of the financial statements. Further detail is also included in the Directors' Report on page 7 and the Strategic Report on pages 2 and 4.</td></tr>
<tr><td>How the scope of our audit responded to the key audit matter</td><td>We evaluated management's approach to assessing the impact of Covid-19 on the company and its financial statement disclosures by performing the following procedures:

We evaluated management's stress and scenario testing including reverse stress testing and challenged management's key assumptions, assessing its consistency with other available information and our understanding of the RAC group businesses;

We evaluated management's assessment of the risks facing the RAC group and the company including liquidity risk, asset credit risk and operational matters as appropriate;

We made inquiries of senior management in relation to their assessment of the impacts of Covid-19 on the RAC group and company, including further steps the company will take in case economic and other factors deteriorate further;

We inspected key regulatory submissions including correspondence between the company and its regulators related to the RAC group and the company's responses to the emergence of Covid-19; and</td></tr>
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RAC Insurance Limited

Independent auditor's report to the members of RAC Insurance Limited (continued)

Key audit matters (continued)

Covid-19 non-adjusting post balance sheet event (continued)	
How the scope of our audit responded to the key audit matter	We assessed the post balance sheet events and going concern disclosures made by management in the financial statements against applicable accounting standards and guidance issued by the Financial Reporting Council, assessed management's judgment that Covid-19 is a non-adjusting event and evaluated the consistency of the disclosures with our knowledge of the RAC group and company.
Key observations	We consider based on the procedures performed above, and the evidence obtained that the potential impact of Covid-19, that the post balance sheet event disclosures in the financial statements are appropriately stated.

Valuation of Insurance Liabilities	
Key audit matter	Included in insurance liabilities are total gross provisions for outstanding claims, with a balance at 31 December 2019 of £409k (2018: £221k) comprising collective and specific elements. The collective element is the incurred but not reported (IBNR) collective provision, while the specific provision relates to instances where there is objective evidence for claims made by customers against their insurance policies. We have determined our key audit matter as the accuracy of the cost per policy assumption utilised in valuing the IBNR collective insurance liabilities. This is on the basis that significant management judgment is required to determine an appropriate methodology to best reflect the nature of the claims payable with limited or no actual claims experience. Inappropriate use of this assumption either due to fraud or error could give rise to a material misstatements. Management's accounting policies are detailed in accounting policy G to the financial statements while the key sources of estimation are outlined in note O to the financial statements. Note 13 discloses the outstanding balance as at year end.
How the scope of our audit responded to the key audit matter	We obtained an understanding of the relevant controls in place to manage the risk of inappropriate assumptions used in the IBNR collective insurance liabilities reserving. We challenged the appropriateness of the key assumptions used in the collective IBNR insurance liabilities, including the cost per policy used. With the involvement of our actuarial specialists we performed benchmarking to a range of peer group companies. Given the inherent susceptibility to misstatements in estimates, we considered management's judgements for indicators of management bias. As a wider procedure, we tested the mechanical accuracy of the model, which is used to determine the collective insurance liabilities, and agreed a sample of model inputs back to underlying source data. We also reviewed management minutes and legal correspondence to identify customer claims with notifications but not currently modelled by management in their insurance liabilities reserving.
Key observations	We found the insurance liabilities reserving models to be working as intended by management and that the approach adopted by the company was in line with industry practice. We concluded that the liabilities are materially accurate.

Our application of materiality

We define materiality as the magnitude of misstatement in the Financial Statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the Financial Statements as a whole as follows:

Materiality	£385k (2018: £353k)

RAC Insurance Limited

Independent auditor's report to the members of RAC Insurance Limited (continued)

Our application of materiality (continued)

Basis for determining materiality	When determining materiality, as the company is part of RAC Group (Holdings) Limited group, we also considered that this materiality is appropriate for the consolidation of this set of Financial Statements into that group's results. Our determined materiality equates to 3% of the net asset balance held by the Company.
Rationale for the benchmark applied	The overall capital base is a key focus area for the company and its key regulators; Prudential Risk Authority (PRA) and Financial Conduct Authority (FCA). The company's strategy is therefore centred on maintaining a stable capital base rather than driving profitability. Revenue or profit measures are considered to be less relevant for the company than they are for a listed insurance entity. This is consistent with other insurance companies of a similar size and nature as the Company.

Performance materiality

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the Financial Statements as a whole. Performance materiality was set at 70% of materiality for the 2019 audit (2018: 70%).

We determined performance materiality with reference to factors such as our understanding of the RAC group, the entity's complexity and purpose within the group, the centralised finance function, the quality of the control environment, extent of material misstatements applicable to the company, the low level of uncorrected misstatements in previous audits.

Error reporting threshold

We agreed with the Audit and Risk Committee that we would report to the Committee all audit differences in excess of £19k (2018: £18k), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit and Risk Committee on disclosure matters that we identified when assessing the overall presentation of the Financial Statements.

An overview of the scope of our audit

Our audit was scoped by obtaining an understanding of the company and its environment, including RAC group-wide controls, and assessing the risks of material misstatement relevant for the Company.

Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

Other information

The directors are 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.

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 respect of these matters.

Statement of Director's responsibilities

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

Independent auditor's report to the members of RAC Insurance Limited (continued)

Statement of Director's responsibilities (continued)

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

Auditor's responsibilities for the audit of the financial statements

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

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud and non-compliance with laws and regulations are set out below.

A further description of our responsibilities for the audit of the Financial Statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Extent to which the audit was considered capable of detecting irregularities, including fraud

We identify and assess the risks of material misstatement of the Financial Statements, whether due to fraud or error, and then design and perform audit procedures responsive to those risks, including obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion.

Identifying and assessing potential risks related to irregularities

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we considered the following:

- the nature of the industry and sector, control environment and business performance including the design of wider RAC group's remuneration policies, key drivers for directors' remuneration, bonus levels and performance targets;
- results of our enquiries of management, internal audit, internal legal team and the Audit & Risk Committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the RAC group's documentation of their policies and procedures relating to:
  - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
  - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
  - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations;
- the matters discussed among the audit engagement team and involving relevant internal specialists, including tax, valuations, acturial, IT specilaists and conduct risk regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in the following areas: insurance liabilities. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory framework that the company operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the Financial Statements. The key laws and regulations we considered in this context included the Companies Act 2006, pensions and tax legislations.

RAC Insurance Limited

Independent auditor's report to the members of RAC Insurance Limited (continued)

Identifying and assessing potential risks related to irregularities (continued)

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the company's ability to operate or to avoid a material penalty. These included the Company's operating licence and regulatory solvency requirements imposed by the Prudential Risk Authority (PRA) and the Financial Conduct Authority (FCA).

Audit response to risks identified

As a result of performing the above, we identified insurance liabilities as a key audit matter related to the potential risk of fraud. The key audit matters section of our report explains the matter in more detail and also describes the specific procedures we performed in response to that key audit matter.

In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the Financial Statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the Financial Statements;
- enquiring of management, the Audit and Risk Committee and in-house legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with HMRC, FCA and PRA;
- discussing among the engagement team and involving relevant internal specialists, including tax, financial instruments and information technology specialists regarding how and where fraud might occur in the Financial Statements and any potential indicators of fraud. As part of this discussion, we identified potential for fraud in management override of controls and related party transactions; and
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists, and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the Financial Statements; and
- the Strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic report or the Directors' report.

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Independent auditor's report to the members of RAC Insurance Limited (continued)

Matters on which we are required to report by exception (continued)

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of Directors' remuneration have not been made.

We have nothing to report in respect of these matters.

Other matters

Auditor tenure

Following the recommendation of the Audit and Risk Committeee, we were appointed by the Board of Directors in May 2014 to audit the Financial Statements for the year ending 31 December 2014 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is six years, covering the years ending 31 December 2014 to 31 Decemebr 2019.

Consistency of the audit report with the additional report to the audit committee

Our audit opinion is consistent with the additional report to the Audit and Risk Committee we are required to provide in accordance with ISAs (UK).

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's Members those matters we are required to state to them in an Auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Kieren Cooper, FCA (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
Birmingham, United Kingdom
02 June 2020

RAC Insurance Limited
Financial Statements 2019
Income statement

For the year ended 31 December 2019

	Note	2019	2018
		£000	£000
Income	1		
Gross written premiums		14,607	14,126
Premiums ceded to reinsurers		(959)	(893)
Premiums written, net of reinsurance		13,648	13,233
Net change in provision for unearned premiums		(726)	(180)
Net earned premiums		12,922	13,053
Rental income		562	436
Net investment income		50	64
Other charges, including value adjustments	8	-	90
		13,534	**13,643**
Expenses	2		
Claims paid, net of reinsurance		(8,844)	(9,361)
Change in claims provisions, net of reinsurance		(188)	518
Other operating expenses		(2,939)	(2,126)
		(11,971)	**(10,969)**
Profit before tax		**1,563**	**2,674**
Tax charge	7	(280)	(508)
Profit for the year		**1,283**	**2,166**

The Company has no other comprehensive income other than that included in the results above and therefore a separate Statement of comprehensive income has not been presented.

The accounting policies and notes on pages 20 to 44 are an integral part of these Financial Statements.

RAC Insurance Limited
Financial Statements 2019 (continued)

Registered in England and Wales: No. 02355834

Statement of financial position

As at 31 December 2019

	Note	2019	2018
		£000	£000
ASSETS			
Investment property	8	2,900	2,900
Reinsurance assets	9	439	455
Receivables	10	14,016	9,743
Cash and cash equivalents	11	7,987	7,935
		25,342	**21,033**
LIABILITIES			
Insurance liabilities	13(a)	(8,239)	(7,341)
Other payables	12	(4,279)	(2,151)
		(12,518)	**(9,492)**
Net assets		**12,824**	**11,541**
EQUITY			
Ordinary share capital	15	7,250	7,250
Retained earnings		5,574	4,291
Total equity		**12,824**	**11,541**

The accounting policies and notes on pages 20 to 44 are an integral part of these Financial Statements.

Approved by the Board on 02 June 2020

Jo Baker

J Baker
Chief Financial Officer

RAC Insurance Limited
Financial Statements 2019 (continued)
Statement of changes in equity

For the year ended 31 December 2019

	Note	Ordinary share capital £000	Retained earnings £000	Total equity £000
Balance at 1 January 2018		**7,250**	**8,625**	**15,875**
Profit for the year		-	2,166	2,166
Total comprehensive income		-	2,166	2,166
Dividend paid	**4**	-	(6,500)	(6,500)
Balance at 31 December 2018		**7,250**	**4,291**	**11,541**
Profit for the year		-	1,283	1,283
Total comprehensive income		-	1,283	1,283
Balance at 31 December 2019		**7,250**	**5,574**	**12,824**

The accounting policies and notes on pages 20 to 44 are an integral part of these Financial Statements.

RAC Insurance Limited
Financial Statements 2019 (continued)
Statement of cash flows

For the year ended 31 December 2019

	Note	2019	2018
		£000	**£000**
Operating activities			
Profit before tax		1,563	2,674
Adjustments to reconcile profit before tax to net cash flows:			
Gain from fair value adjustment of investment property (non-cash)	8	-	(90)
Decrease/(increase) in reinsurance assets (non-cash)	9(c)	16	(147)
Increase in receivables (non-cash)	10	(4,273)	(1,494)
Increase/(decrease) in insurance liabilities (non-cash)	13(a)	898	(190)
Decrease in payables and other financial liabilities	12	1,848	1,552
Net cash inflow from operating activities		**52**	**2,305**
Investing activities			
Dividend paid	4	-	(6,500)
Net cash outflow from investing activities		**-**	**(6,500)**
Net (decrease)/increase in cash and cash equivalents		**52**	**(4,195)**
Cash and cash equivalents at 1 January		7,935	12,130
Cash and cash equivalents at 31 December	11	**7,987**	**7,935**

The accounting policies and notes on pages 20 to 44 are an integral part of these Financial Statements.

RAC Insurance Limited

Accounting policies

(A) Corporate information

The Company is a private limited liability company, limited by shares, incorporated and domiciled in the United Kingdom, registered in England & Wales. The principal activity of the Company is the provision of insurance relating to roadside assistance and legal expenses insurance. The registered office is located at RAC House, Brockhurst Crescent, Walsall, West Midlands, United Kingdom, WS5 4AW.

Information on other related party relationships of the Company is provided in note 19.

The Financial Statements of RAC Insurance Limited for the year ended 31 December 2019 were approved for issue by the Board on 2 June 2020.

(B) Basis of preparation

The Financial Statements of the Company have been prepared on the historical cost basis, except for certain properties that are measured at fair value, as explained in the accounting policies. Historical cost is generally based on the fair value of consideration given in exchange for assets.

The Financial Statements of the Company have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

The principal accounting policies adopted in the preparation of these Financial Statements are set out below.

The Financial Statements are presented in pounds sterling, which is the Company's functional and presentational currency. Unless otherwise noted, the amounts shown in these Financial Statements are in thousands of pounds sterling ("£000").

Adoption of new International Financial Reporting Standards

The following new and amended IFRSs are effective and relevant for these Financial Statements. The adoption of these Standards has not had any material impact on the disclosures or on the amounts reported in the Company's Financial Statements.

- IFRIC 23 Uncertainty over income tax treatments
- Annual Improvements to IFRSs 2015–2017 Cycle (Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23)

At 31 December 2019, the Company has not applied the following new and revised IFRS that have been issued but are not yet effective and in some cases had not yet been adopted by the EU:

- IFRS 17 Insurance contracts [1]

The Company is currently in the process of evaluating the impact of the adoption of IFRS 17 on the Company's financial reporting. It is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

Going concern

The financial statements have been prepared on a going concern basis, which assumes that the Company has adequate resources to continue in operational existence for the foreseeable future.

The Company made a profit of £1,283 thousand for the year ended 31 December 2019 (2018: £2,166 thousand) and at 31 December 2019 had net assets of £12,824 thousand (2018: £11,541 thousand). The Group's and Company's business activities, together with the factors likely to affect their future development, performance and position are set out in the Strategic report on pages 2 to 5. Details of cash facilities are set out in note 11 to the Financial Statements. The Group's objectives, policies and processes for managing its capital, its financial risk management objectives and its exposure to credit risk and liquidity risk are set out in note 18 to the Financial Statements.

(B) Basis of preparation (continued)

Going concern (continued)

The Directors have assessed the financial position and the prospects and future funding requirements of the Group and compared them to the level of available committed borrowing facilities. This assessment included a review of the Group's financial forecasts and financial instruments for the 15 month period from the date of this report. The Directors considered a range of potential scenarios and how these may impact on cash flow, facility headroom and the Group's ability to comply with the terms of its bank debt. The Directors also consider what mitigating actions the Group could take to limit any adverse consequences.

Having undertaken this assessment, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. For these reasons, they continue to adopt the going concern basis in preparing the Company's Financial Statements.

(C) Product classification

Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause an insurer to make significant additional payments in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. Contracts can be reclassified as insurance contracts after inception if insurance risk becomes significant. Any contracts not considered to be insurance contracts under IFRS are classified as investment or service contracts.

Accounting for insurance contracts, as allowed by IFRS 4, was previously determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers, the most recent version of which was issued in December 2005 and amended in December 2006. The Statement of Recommended Practice has since been withdrawn, but there have been no changes to the methodology followed.

(D) Premiums earned

Premiums written reflect business incepted during the year, and exclude any sales-based taxes or duties or levies. Written premiums include an estimate of pipeline premiums less a provision for anticipated lapses. Unearned premiums are those proportions of the premiums written in a year that relate to periods of risk after the Statement of financial position date. Unearned premiums are computed on a monthly pro rata basis.

(E) Other operating income

Lessor income

Lease payments received under operating leases are recognised as income on a straightline basis over the lease term as part of 'other operating income'. The lease payments are a fixed cost and not subject to changes in any index or rate.

(F) Net investment income

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

(G) Insurance contract liabilities

Claims

Insurance claims incurred includes an estimate of all losses occurring during the year, whether reported or not, loss adjustment expenses, a reduction for the value of salvage and other recoveries, and any adjustments to claims incurred in previous years.

RAC Insurance Limited

Accounting policies (continued)

(G) Insurance contract liabilities (continued)

Claims (continued)
Loss adjustment expenses include internal and external costs incurred in connection with the negotiation and settlement of claims. Internal costs include all direct expenses of the claims handling department and any part of the general administrative costs directly attributable to the loss adjustment function.

Outstanding claims provisions
Insurance outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the Statement of financial position date, whether reported or not, together with related loss adjustment expenses. Significant delays are experienced in the notification and settlement of certain types of general insurance claims, the ultimate cost of which cannot be known with certainty at the statement of financial position date. Any estimate represents a determination within a range of possible outcomes. Further details of estimation techniques are given in note 13(c).

Provision for unearned premiums
The proportion of written premiums, gross of commission payable to intermediaries, attributable to subsequent periods is deferred as a provision for unearned premiums. The change in this provision is recognised in the Income statement in order that revenue is recognised over the period of risk.

Liability adequacy
At each reporting date, the Company reviews its unexpired risks and carries out a liability adequacy test for any overall excess of expected claims over unearned premiums, using the current estimates of future cash flows under its contracts, after taking account of the investment return expected to arise on assets relating to the relevant general business provisions. If these estimates show that the carrying amount of its insurance liabilities is insufficient in light of the estimated future cash flows, the Company recognises the deficiency in the Income statement by setting up a provision in the Statement of financial position.

Other assessments and levies
The Company is subject to various periodic insurance related assessments or guarantee fund levies. Related provisions are established where there is a present obligation (legal or constructive) as a result of a past event. Such amounts would not be included within insurance liabilities but would be included under "other payables" in the Statement of financial position.

(H) Reinsurance

The Company cedes reinsurance in the normal course of business in respect of two add-on products. The cost of reinsurance is accounted for over the life of the underlying reinsurance policies.

Reinsurance assets primarily include balances due from both insurance and reinsurance companies for ceded insurance liabilities. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provisions or settled claims associated with the reinsured policies and in accordance with the relevant reinsurance contract.

If a reinsurance asset is impaired, the Company reduces the carrying amount accordingly and recognises that impairment loss in the Income statement. A reinsurance asset is impaired if there is objective evidence, as a result of an event that occurred after initial recognition of the reinsurance asset, that the Company may not receive all amounts due to it under the terms of the contract, and the event has an impact that can be reliably measured on the amounts that the Company will receive from the reinsurer.

RAC Insurance Limited

Accounting policies (continued)

(I) Investment property

Investment properties are carried at their revalued amounts, being the fair value at the date of revaluation on a vacant possession basis, which are supported by market evidence. A gain or loss arising from movement in the fair value of the investment property is recognised in the Income statement in the period in which it occurs. Third party valuations are obtained every three years to support management's internal valuations, carried out on an annual basis.

Gains and losses on disposal of investment property are determined by reference to their carrying amount and are recorded in the Income statement.

(J) Cash and cash equivalents

Cash and cash equivalents consist of cash at banks and in hand and deposits held at call with banks. Such investments are those with less than three months' maturity from the date of acquisition, or which are redeemable on demand with only an insignificant change in their fair values. For the purposes of the Statement of cash flows, cash and cash equivalents also include bank overdrafts, which are included in payables and other financial liabilities in the Statement of financial position.

(K) Provisions and contingent liabilities

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is more probable than not that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Where the Company expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset, up to the amount of the provision, but only when the reimbursement is virtually certain.

Contingent liabilities are disclosed if there is a possible future obligation as a result of a past event, or if there is a present obligation as a result of a past event but either a payment is not probable yet still possible or the amount cannot be reliably estimated.

(L) Financial assets

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is more probable than not that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Where the Company expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset, up to the amount of the provision, but only when the reimbursement is virtually certain.

(i) Impairment of financial assets
An impairment is recognised on financial assets if there is considered to be expected credit losses. The amount of expected credit losses is updated at each reporting date to reflect changes in credit risk since initial recognition of the financial asset. Losses arising from impairment are recognised in the Income statement in finance costs for loans and in other operating expenses for other receivables.

(ii) Impairment of non-financial assets
Non-financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows.

RAC Insurance Limited

Accounting policies (continued)

(M) Income taxes

Income taxes include both current and deferred taxes. Income taxes are charged/credited to the Income statement except where they relate to items charged/credited directly to other comprehensive income or equity. In this instance, the income taxes are also charged/credited directly to other comprehensive income or equity respectively.

Current tax is the expected tax payable or receivable on the Company's taxable income or loss for the year, using tax rates enacted or substantively enacted at the Statement of financial position date, and any adjustment to tax payable in respect of previous years.

(N) Share capital and dividends

Equity instruments

An equity instrument is a contract that evidences a residual interest in the assets of an entity after deducting all its liabilities. Accordingly, a financial instrument is treated as equity if:

(i) there is no contractual obligation to deliver cash or other financial assets or to exchange financial assets or liabilities on terms that may be unfavourable; and

(ii) the instrument will not be settled by delivery of a variable number of shares or is a derivative that can be settled other than for a fixed amount of cash, shares or other financial assets.

Dividends

Interim dividends on ordinary shares are recognised in equity in the period in which they are paid. Final dividends on these shares are recognised when they have been approved by shareholders.

RAC Insurance Limited

Accounting policies (continued)

(O) Critical accounting judgements and key sources of estimation uncertainty

The preparation of the Financial Statements in conformity with IFRS requires the Company to make estimates and judgements using assumptions that affect items reported in the Statement of financial position and Income statement and the disclosure of contingent assets and liabilities at the reporting date. Estimates are based on management's best knowledge of current facts, circumstances and, to some extent, future events and actions. Actual results may differ from those estimates, possibly significantly. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Set out below are items where management have taken a judgement or which management consider particularly susceptible to changes in estimates and assumptions, and the relevant accounting policy.

(i) Critical judgements in applying the Company's accounting policies

There are no critical judgements apart from those involving estimations (which are dealt with separately below), that the Directors have made in the process of applying the Company's accounting policies on the amounts recognised in the Financial Statements.

(ii) Key sources of estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the Statement of financial position date are discussed below:

Insurance liabilities

Insurance outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the Statement of financial position date, whether reported or not, together with related loss adjustment expenses. Significant delays are experienced in the notification and settlement of certain types of general insurance claims, the ultimate cost of which cannot be known with certainty at the Statement of financial position date. Refer to note 13 for details of the outstanding claims provision.

Fair value measurements and valuation process

The Company measures non-financial assets including investment properties, at fair value at each reporting date.

The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- in the principal market for the asset or liability; or
- in the absence of a principal market, in the most advantageous market for the asset or liability.

The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data is available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

(O) Critical accounting judgements and key sources of estimation uncertainty (continued)

Fair value measurements and valuation process (continued)

All assets and liabilities for which fair value is measured or disclosed in the Financial Statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2: Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3: Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

RAC Insurance Limited

Notes to the Financial Statements

1 Income

	2019	2018
	£000	£000
Premiums earned		
Gross written premiums	14,607	14,126
Less: Premiums ceded to reinsurers	(959)	(893)
Gross change in provision for unearned premiums	(710)	(327)
Reinsurers' share of change in provision for unearned premiums	(16)	147
Net change in provision for unearned premiums	(726)	(180)
Net earned premiums	12,922	13,053
Rental income	562	436
Total revenue	13,484	13,489
Net investment income	50	64
Other income (note 8)	-	90
Total income	**13,534**	**13,643**

2 Expenses

	2019	2018
	£000	£000
Claims paid, net of reinsurance		
Claims paid to policyholders	9,113	9,570
Less: Claims recoveries from reinsurers	(269)	(209)
	8,844	9,361
Change in claims provisions, net of reinsurance		
Change in net claims provisions (see note 13(d))	188	(518)
	9,032	8,843
Fee and commission expenses		
Other operating expenses	2,939	2,126
Total expenses	**11,971**	**10,969**

RAC Insurance Limited

Notes to the Financial Statements (continued)

3 Employee information

The Company has no employees. All employees of the Group are employed and remunerated by RAC Motoring Services, a fellow Group Company. Disclosures relating to employees may be found in the Consolidated Annual Report and Financial Statements of RAC Bidco Limited.

4 Dividends

No interim dividends were paid during the year (2018: £6,500 thousand, 89.66 pence per share). No final dividend were paid or are proposed for the year ended 31 December 2019 (31 December 2018: £nil).

5 Directors

Executive Directors of the Company are remunerated as employees of RAC Motoring Services, a fellow Group Company. Management recharges for the wider executive group, which includes the executive Directors of the Company, have been charged to the main trading subsidiaries of the Group, which includes RAC Insurance Limited. It is not deemed practical to separate the remuneration of the executive Directors from the wider management recharges.

Disclosures relating to Directors' remuneration can be found in the Annual Report and Audited Financial Statements of RAC Group (Holdings) Limited.

6 Auditor's remuneration

The total remuneration payable by the Company, excluding VAT, to its auditor, Deloitte LLP, is shown below.

	2019	2018
	£000	£000
Audit services		
Statutory audit of the Company's Financial Statements	30	16
Other services		
Audit related assurance services	8	20
Total remuneration payable to Deloitte LLP	**38**	**36**

Audit fees are borne and paid by RAC Motoring Services, a fellow Group Company.

7 Tax

(a) Tax charged to the income statement

	2019 £000	2018 £000
Current tax:		
For the year	297	508
Adjustment in respect of prior years	(17)	-
Total current tax	280	508
Total tax charged to the income statement	**280**	**508**

(b) Tax reconciliation

The tax on the Company's profit before tax is the same as the theoretical amount that would arise using the tax rate in the UK as follows:

	2019 £000	2018 £000
Profit before tax	1,563	2,674
Tax calculated at standard UK corporation tax rate of 19.00% (2018: 19.00%)	297	508
Adjustment to tax charge in respect of previous periods - corporation tax	(17)	-
Total tax charged to the income statement (note 7(a))	**280**	**508**

The headline rate of UK corporation tax is 19%.

The Company has unrecognised unrealised capital losses of £7,768 thousand (2018: £7,768 thousand) to carry forward indefinitely. On realisation these could be set against future capital gains.

RAC Insurance Limited

Notes to the Financial Statements (continued)

8 Investment property

	Investment property
	£000
Fair value:	
At 1 January 2018	2,810
Gain from fair value adjustment recognised in income statement	90
At 31 December 2018 and 2019	**2,900**

During 2018, the property was reclassified from Property, Plant and Equipment to Investment Property to better reflect the use of the asset by the Company as rentals are received. This had no material impact on the financial statements. The property is held at fair value, level 2 in the hierarchy in accordance with IFRS 13 and in line with the Company's accounting policy, the property was revalued during 2018 by Colliers International, an accredited independent valuer. As at 31 December 2019 management do not consider there to have been a material change in the value of the property. If the investment occupied property was measured using the cost model, the cost would be £3,000 thousand.

9 Reinsurance assets

(a) Carrying amount

Gross reinsurance assets at 31 December comprise:

	2019	2018
	£000	£000
Provision for unearned premiums	439	455

(b) Assumptions

The assumptions used for reinsurance contracts follow those used for insurance contracts, shown in note 13(c).

Reinsurance assets are valued net of any provisions for their recoverability.

RAC Insurance Limited

Notes to the Financial Statements (continued)

9 Reinsurance assets (continued)

(c) Movements

Reinsurers' share of the provision for unearned premiums:

	2019	2018
	£000	£000
Carrying amount at 1 January	**455**	**308**
Premiums ceded to reinsurers in the)	959	893
Less: reinsurers' share of premiums earned during the year	(975)	(746)
Change in reinsurance asset	(16)	147
Carrying amount at 31 December	**439**	**455**

10 Receivables

	2019	2018
	£000	£000
Amounts due from reinsurers	14	14
Amounts due from intermediaries - related parties (note 19 (a)(ii))	14,000	9,724
Other receivables	2	5
Total	**14,016**	**9,743**
Expected to be recovered in less than one year	**14,016**	**9,743**

Receivables are measured at amortised cost net of any impairment losses which are based on a loss allowance for expected credit losses. No material impairment losses have been recognised in 2019 (2018: £nil).

11 Cash and cash equivalents

Cash and cash equivalents as at 31 December 2019 comprises of £7,987 thousand of cash at bank and in hand (2018: £7,935 thousand).

12 Other payables

	2019	2018
	£000	£000
Amounts due to intermediaries - related parties (note 19 (a)(ii))	4,262	2,125
Other payables	17	26
Total expected to be payable within one year	**4,279**	**2,151**

All payables are financial liabilities and carried at amortised cost which is considered to be a reasonable approximation of the fair value.

Within the cash flow statement, "Decrease in payables and other financial liabilities" is stated after adjusting for £280 thousand (£508 thousand) of corporation tax liability settled by group relief.

13 Insurance liabilities

(a) Carrying amount

Gross insurance liabilities at 31 December comprise:	2019	2018
	£000	£000
Provisions for outstanding claims (see note 13(d))	409	221
Provision for unearned premiums (see note 13(f))	7,830	7,120
Total	**8,239**	**7,341**

(b) Provisions for outstanding claims

Delays occur in the notification and settlement of claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the Statement of financial position date. The reserves are based on information currently available. However, it is inherent in the nature of the business written that the ultimate liabilities may vary as a result of subsequent developments.

Outstanding claims includes a provision of £nil (2018: £nil) for "After The Event" insurance cover. The Company stopped writing new "After The Event" business in 2008. No further claims are anticipated for this insurance cover.

The Company is permitted to undertake various types of general insurance business, including Assistance and Legal Expenses insurance.

(c) Judgements

Outstanding claims provisions are estimated based on known facts at the date of estimation. Case estimates are set taking into account all available information and correspondence regarding the circumstances of the claim, such as medical reports, investigations and inspections.

No adjustments are made to the case estimates included in booked claims provisions, except for rare occasions when the estimated ultimate cost of a large or unusual claim may be adjusted to allow for uncertainty regarding, for example, the outcome of a court case. The ultimate cost of outstanding claims is then estimated by using a range of standard claims projection techniques. The main judgement underlying these techniques is that the Company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claims numbers based on the observed development of earlier years and expected loss ratios.

RAC Insurance Limited

Notes to the Financial Statements (continued)

13 Insurance liabilities (continued)

(d) Movements

The following changes have occurred in the claims provisions during the year:

	2019	2018
	£000	£000
Carrying amount at 1 January	**221**	**738**
Claims losses and expenses incurred in the current year	9,366	9,655
Claims losses and expenses incurred in prior years	(65)	(601)
Incurred claims losses and expenses	9,301	9,054
Less:		
Payments made on claims incurred in the current year	(9,005)	(9,518)
Payments made on claims incurred in prior years	(108)	(53)
Claims payments made in the year	(9,113)	(9,571)
Carrying amount at 31 December	**409**	**221**

(e) Loss development tables

The table that follows presents the development of claims payments and the estimated ultimate cost of claims for the accident years 2010 to 2019. The upper half of the table shows the cumulative amounts paid during successive years related to each accident year. For example, with respect to the accident year 2010, by the end of 2019, £8,656 thousand had actually been paid in settlement of gross claims.

Any change from the original estimate could generally be a combination of a number of factors, including claims being settled for larger or smaller amounts than originally estimated. The original estimates may also be increased or decreased, as more information becomes known about the individual claims and overall claims frequency and severity patterns.

13 Insurance liabilities (continued)

(e) Loss development tables (continued)

Accident year	All Prior Years	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
Gross cumulative claims payments												
At end of accident year		(8,446)	(7,580)	(7,372)	(7,157)	(6,830)	(7,336)	(8,435)	(8,873)	(9,518)	(9,005)	
One year later		(8,622)	(7,688)	(7,536)	(7,212)	(6,888)	(7,337)	(8,492)	(8,931)	(9,627)		
Two years later		(8,622)	(7,774)	(7,536)	(7,212)	(6,888)	(7,337)	(8,492)	(8,931)			
Three years later		(8,656)	(7,797)	(7,536)	(7,212)	(6,888)	(7,337)	(8,492)				
Four years later		(8,656)	(7,797)	(7,536)	(7,212)	(6,888)	(7,337)					
Five years later		(8,656)	(7,797)	(7,536)	(7,212)	(6,888)						
Six years later		(8,656)	(7,797)	(7,536)	(7,212)							
Seven years later		(8,656)	(7,797)	(7,536)								
Eight years later		(8,656)	(7,797)									
Nine years later		(8,656)										
Estimate of gross ultimate claims												
At end of accident year		8,622	7,853	7,978	7,212	7,031	7,451	8,676	8,966	9,655	9,366	
One year later		8,788	7,944	7,978	7,214	7,028	7,341	8,495	8,931	9,637		
Two years later		8,722	7,944	7,963	7,214	7,036	7,350	8,492	8,931			
Three years later		8,722	7,948	7,963	7,212	6,938	7,337	8,492				
Four years later		8,722	7,948	7,930	7,212	6,888	7,337					
Five years later		8,722	7,921	7,905	7,212	6,888						
Six years later		8,722	7,911	7,620	7,212							
Seven years later		8,722	7,797	7,574								
Eight years later		8,656	7,797									
Nine years later		8,656										
Estimate of ultimate claims		8,656	7,797	7,574	7,212	6,888	7,337	8,492	8,931	9,637	9,366	
Cumulative payments		(8,656)	(7,797)	(7,536)	(7,212)	(6,888)	(7,337)	(8,492)	(8,931)	(9,627)	(9,005)	
Outstanding claims provisions recognised in the Statement of financial position	-	-	-	38	-	-	-	-	-	10	361	409

RAC Insurance Limited

Notes to the Financial Statements (continued)

13 Insurance liabilities (continued)

(e) Loss development tables (continued)

After the effect of reinsurance, the loss development table is:

Accident year	All prior years	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
Net cumulative claims payments												
At end of accident year		(7,672)	(7,024)	(6,815)	(7,043)	(6,713)	(6,949)	(8,019)	(8,547)	(9,308)	(8,736)	
One year later		(7,848)	(7,132)	(6,979)	(7,098)	(6,771)	(6,950)	(8,076)	(8,629)	(9,417)		
Two years later		(7,848)	(7,218)	(6,979)	(7,098)	(6,771)	(6,950)	(8,076)	(8,629)			
Three years later		(7,882)	(7,241)	(6,979)	(7,098)	(6,771)	(6,950)	(8,076)				
Four years later		(7,882)	(7,241)	(6,979)	(7,098)	(6,771)	(6,950)					
Five years later		(7,882)	(7,241)	(6,979)	(7,098)	(6,771)						
Six years later		(7,882)	(7,241)	(6,979)	(7,098)							
Seven years later		(7,882)	(7,241)	(6,979)								
Eight years later		(7,882)	(7,241)									
Nine years later		(7,882)										
Estimate of net ultimate claims												
At end of accident year		7,848	7,297	7,421	7,098	6,914	7,064	8,260	8,640	9,445	9,097	
One year later		8,014	7,388	7,421	7,100	6,911	6,954	8,079	8,629	9,427		
Two years later		7,948	7,388	7,406	7,100	6,919	6,963	8,076	8,629			
Three years later		7,948	7,392	7,406	7,098	6,821	6,950	8,076				
Four years later		7,948	7,392	7,373	7,098	6,771	6,950					
Five years later		7,948	7,365	7,348	7,098	6,771						
Six years later		7,948	7,355	7,063	7,098							
Seven years later		7,948	7,241	7,017								
Eight years later		7,882	7,241									
Nine years later		7,882										
Estimate of ultimate claims		7,882	7,241	7,017	7,098	6,771	6,950	8,076	8,629	9,427	9,097	
Cumulative payments		(7,882)	(7,241)	(6,979)	(7,098)	(6,771)	(6,950)	(8,076)	(8,629)	(9,417)	(8,736)	
Net outstanding claims provisions recognised in the Statement of financial position	-	-	-	38	-	-	-	-	-	10	361	409

13 Insurance liabilities (continued)

(f) Provision for unearned premiums

The following changes have occurred in the provision for unearned premiums during the year:

	2019	2018
	£000	£000
Carrying amount at 1 January	**7,120**	**6,793**
Premiums written during the year	14,607	14,126
Less: premiums earned during the year	(13,897)	(13,799)
Change in year	710	327
Carrying amount at 31 December	**7,830**	**7,120**

14 Tax liabilities

All current tax liabilities have been settled via group relief as at 31 December 2019 (£280 thousand) and 31 December 2018 (£508 thousand). See the statement of cash flows and related party transactions (note 19(a)(iv)).

15 Ordinary share capital

Details of the Company's ordinary share capital are as follows:

	2019	2018
	£000	£000
Allotted, called up and fully paid		
7,250,000 (2018: 7,250,000) ordinary shares of £1 each	7,250	7,250

16 Contingent liabilities and other risk factors

Uncertainty over claims provisions

Note 13(c) gives details of the estimation techniques used in determining the outstanding claims provisions. These are estimated to give a result within the normal range of outcomes. To the extent that the ultimate cost falls outside this range, for example where future claims inflation differs from that expected, there is uncertainty in respect of this liability, that is not able to be calculated.

Levy schemes

The Company pays contributions into various levy schemes in the UK including a pension levy scheme and a FSCS levy scheme, in respect of the Group's regulatory activities. The Directors continue to monitor the situation but are not aware of any need to increase provisions at the Statement of financial position date.

17 Lease arrangements

The contractual maturity dates of lease payments receivable under IFRS 16 are:

	2019	2018
	£000	£000
Within 1 year	562	562
Later than 1 year and not later than 5 years	1,546	2,108
Later than 5 years	-	-
	2,108	2,670

Lease arrangements arise in respect of a property lease. The Company acts as a lessor for one investment property and the lessee is RAC Motoring Services, a fellow Group Company, the risks associated with the property are mitigated on a group basis due to the nature of the lease.

18 Risk management

The Group operates a risk management framework, which is the collection of processes and tools that have been put in place to ensure that the risks to which the Group is exposed are identified, measured, managed, monitored and reported on a regular basis. The key instruments of the framework include the risk management policies, risk reports and the governance and oversight infrastructure.

18 Risk management (continued)

Risks are usually grouped by risk type: market, credit, liquidity, strategic, operational and regulatory risk. Risks falling within these types may affect a number of key metrics including those relating to Statement of financial position strength, liquidity and profit. They may also affect the performance of the products that the Company delivers to customers and the service to customers and distributors, which can be categorised as risks to brand and reputation. The key risks faced by the Group are set out in this note.

The Group's measurement of risk is used to support the monitoring and reporting of the risk profile and in the evaluation of alternative risk management actions. The Group carries out a range of stress and scenario tests to evaluate their impact on the business and the management actions available to respond to the potential conditions.

The Company has an established governance framework, which has the following key elements:

- defined terms of reference for the Board and the associated executive management and other committees across the Group;
- a clear organisational structure with documented delegated authorities and responsibilities from the Board to executive management committees and senior management; and
- adoption of the risk policy framework that defines risk appetite measures and sets out risk management and control standards.

Policies for managing financial risks are governed by Board approved policies and procedures, which are reviewed on an annual basis.

(a) Treasury policy

The Group Treasury department's main responsibilities are to:

- Ensure adequate funding and liquidity for the Group;
- Manage the interest risk of the Group's debt; and
- Ensure that the Group's banking and card transmissions operate effectively.

The Group's debt management policy is to provide an appropriate level of funding to finance the Group's medium term plans at a competitive cost and ensure flexibility to meet the changing needs of the Group.

(i) Market risk

Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments as a result of fluctuations in interest rates and foreign currency exchange rates.

The Company has no borrowings based on market interest rates. Therefore there would be no impact in any reported year on profit before tax or shareholders' equity as a result of changes in market interest rates.

Interest rate movements on trade payables, trade receivables and other financial instruments do not present a material exposure to the Company's Statement of financial position.

The Company undertakes transactions denominated in foreign currencies and is consequently exposed to exchange rate fluctuations. The level of foreign currency transactions is relatively low and so is not considered to present a material exposure to the Company's Statement of financial position.

18 Risk management (continued)

(a) Treasury policy (continued)

(ii) Credit risk

Credit risk is the risk of loss in the value of financial assets due to counterparties failing to meet all or part of their obligations.

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date is set out below:

	2019	2018
	£000	£000
Trade and other receivables (note 10)	14,016	9,743
Cash and cash equivalents (note 11)	7,987	7,935
	22,003	17,678

Management of credit risk is carried out in accordance with the Group's credit risk processes, which include setting exposure limits and monitoring exposures in accordance with ratings set by credit ratings agencies such as Standard & Poor's.

Financial assets are graded according to current credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. Financial assets which fall outside this range are classified as speculative grade. Credit limits for each counterparty are set based on default probabilities that are in turn based on the rating of the counterparty and the type of exposure concerned.

The Company has not been exposed to significant concentrations of credit risk to third parties due to the nature of trading activity undertaken and the size of individual balances. All trade and other receivables are non-rated (2018: non-rated).

The Company is exposed to concentrations of risk with individual banks which are within approved counterparty exposure limits. Cash and cash equivalents throughout the periods reported on were held with institutions who are A rated. The Company's largest cash and cash equivalent counterparty is Morgan Stanley (2018: Morgan Stanley). At 31 December 2019 the balance held at this counterparty was £2,205 thousand (2018: £2,190 thousand).

18 Risk management (continued)

(a) Treasury policy (continued)

(iii) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

The Group has set its investment strategy to ensure it has sufficient liquid funds to meet its expected obligations as they fall due. The risk is measured through review of forecast liquidity each month by the Treasurer to determine whether there are sufficient credit facilities to meet forecast requirements. The Company does not have any obligations for which liquidity risk would be significant.

(iv) General insurance risk

The Company considers insurance risk within its general insurance activity to comprise the following:

- inaccurate pricing and selection of risks when underwritten;
- fluctuations in the timing, frequency and severity of claims and claims settlements, relative to expectations;
- unexpected claims arising from a single source;
- inadequate reinsurance protection or other risk transfer techniques; and
- inadequate reserves.

The majority of the insurance business underwritten by the Company is of a short-tail nature such as roadside assistance, and is managed and priced in the same country as the domicile of the customer, predominantly in the UK.

Risk based capital models are being used to support the quantification of risk under the Individual Capital Assessment ("ICA") framework. RAC undertakes regular reviews of insurance risks, the output from which is a key input into the ICA and risk based capital assessments.

General insurance claims liabilities are estimated by extrapolating the claims development for each accident year based on the observed development of earlier years. In most cases, no explicit assumptions are made as projections are based on assumptions implicit in the historic claims development on which the projections are based. Due to the short tail nature of the majority of the insurance business underwritten, the risk of significant variances due to claims development is reduced.

(b) Strategic and operational risk

The strategy (including operational risks) for the Group and the Company is determined by the Directors of the Company's ultimate Parent Company, RAC Group (Holdings) Limited and disclosed in the Financial Statements of that company.

18 Risk Management (continued)

(c) Capital risk management

The Group's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

In managing its capital, the Group seeks to:
(i) match the expected cash inflows from its assets with the expected cash outflows from its liabilities as they fall due;
(ii) maintain financial strength to support new business growth and satisfy the requirements of its members and regulators;
(iii) retain financial flexibility by maintaining strong liquidity; and
(iv) allocate capital efficiently to support growth and repatriate excess capital where appropriate.

(d) Regulatory risk

As a regulated entity, the Company is required to hold sufficient capital to meet acceptable solvency levels based on applicable FCA and PRA regulations. The Company's ability to transfer retained earnings to its shareholders is therefore restricted to the extent that these earnings form part of UK regulatory capital.

Relevant capital and solvency regulations ("Solvency II") continue to be used to measure and report the financial strength of regulated companies within the Company. The regulatory capital tests verify that an adequate excess of solvency capital above the required minimum level calculated is maintained using a series of prudent assumptions about the type of business that is underwritten. Regulatory requirements have been complied with throughout all periods reported. RAC Insurance Limited transitioned to comply with the Solvency II requirements from 1 January 2016.

The Company is also subject to regulatory requirements, as set out by the FCA, in relation to product design, marketing materials, sales processes and data protection. Failure to comply with these requirements could result in the Company having to suspend, either temporarily or permanently, certain activities. To mitigate these risks the Company employs regulatory and compliance specialists to ensure the regulatory and legislative requirements are fully understood and adhered to.

(e) Sensitivity testing

The results of sensitivity testing are set out below. For each sensitivity test the impact of a change in a single factor is shown, with other assumptions left unchanged.

Sensitivity factor	Description of sensitivity factor applied
Gross loss ratios	The impact of an increase in gross loss ratios by 5%.
Expenses	The impact of an increase in expenses by 10%.
Interest rate and investment return	The impact of a 1% increase or decrease in market interest rates (e.g. if a current interest rate is 5%, the impact of an immediate change to 4% or 6%). The test allows consistency for similar changes to investment returns and movements in the market value of fixed interest securities.

18 Risk management (continued)

(e) Sensitivity testing (continued)

Due to the importance of reinsurance, the impact of sensitivities on profit and equity is shown gross and net of reinsurance. The impact of the expense sensitivity on profit also includes any increase in ongoing administration expenses in addition to the increase in the loss adjustment expense provision.

The sensitivity factors are applied, with the following pre-tax impacts on profit and shareholder's equity at 31 December 2019 and 31 December 2018.

	Increase/(decrease) in shareholder's equity		Increase/(decrease) in profit before tax	
	Gross of reinsurance	Net of reinsurance	Gross of reinsurance	Net of reinsurance
	2019 £000	2019 £000	2019 £000	2019 £000
Gross loss ratios + 5%	(563)	(523)	(695)	(646)
Expenses +10%	(227)	(227)	(280)	(280)
Interest rates +1%	65	65	80	80
Interest rates -1%	(40)	(40)	(49)	(49)

	Increase/(decrease) in shareholder's equity		Increase/(decrease) in profit before tax	
	Gross of reinsurance	Net of reinsurance	Gross of reinsurance	Net of reinsurance
	2018 £000	2018 £000	2018 £000	2018 £000
Gross loss ratios + 5%	(560)	(530)	(691)	(654)
Expenses +10%	(174)	(174)	(215)	(215)
Interest rates +1%	81	81	100	100
Interest rates -1%	(52)	(52)	(64)	(64)

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The Directors have also considered the impact of the uncertainty on the Company's key financial balances. The Company has no investments outside of the UK and the cash and cash equivalents balance is not materially impacted by changes in interest rates which could be impacted by Brexit uncertainty. The Directors therefore do not consider that this risk will have a material impact on the key financial balances of the Company.

19 Related party transactions

(a) The Company had the following transactions with related parties in 2019 and 2018:

(i) The Company has entered into agreements with RAC Motoring Services, a fellow Group company, where income, claims costs and other expenses for certain products are initially recorded by RAC Motoring Services on behalf of the Company, and then transferred to the Company through intercompany accounts. The net value of these transfers was £4,887 thousand of net costs in the year (2018: £4,112 thousand).

(ii) The Company had the following amounts due from related parties:

	2019 £000	2018 £000
Other Group companies- current accounts	14,000	9,724

The related party receivables are not secured and no guarantees were received in respect thereof. The receivables are interest free and will be settled in accordance with normal credit terms.

(iii) The Company had the following amounts due to related parties:

	2019 £000	2018 £000
Other Group companies- current accounts	4,262	2,125

(iv) Auditor's remuneration of £38 thousand (2018: £36 thousand) is borne by RAC Motoring Services, a fellow Group company.

(v) Taxation of £280 thousand (2018: £508 thousand) has been settled by group relief with other Group companies.

(b) Key management compensation

The Directors and key management that are compensated by the Company are considered to be the same as for RAC Bidco Limited. Information on key management compensation may be found in the Consolidated Annual Report and Financial Statements of RAC Bidco Limited.

(c) Key management interests

No key management personnel held equity stakes in the Company at 31 December 2019 or 31 December 2018.

At no time during the reported periods did any Director hold a material interest in any contract of significance with any Group company other than an indemnity provision between each Director and a Group company and a service contract between each Director and a Group company.

(d) Property transaction

During 2013, the Company acquired a property with a market value of £3,000 thousand from RAC Motoring Services for cash consideration of £3,000 thousand. Following acquisition, the Company leased the property back to RAC Motoring Services. The value of rent was £562 thousand in 2019 (2018: £435 thousand). The property is classified as an investment property at fair value in its Statement of financial position. In accordance with IFRS 16 the property has also been recognised as a Right of use asset within RAC Motoring Services.

RAC Insurance Limited

Notes to the Financial Statements (continued)

19 Related party transactions (continued)

(e) Immediate Parent Company

The Company's immediate Parent Company is RAC Group Limited, registered in England and Wales.

(f) Ultimate controlling entity

The ultimate controlling entity is RAC Group (Holdings) Limited. Its Annual Report and Financial Statements are available on application to the Company Secretary, RAC Group (Holdings) Limited, RAC House, Brockhurst Crescent, Walsall, West Midlands, United Kingdom, WS5 4AW (Registered Office).

The smallest level at which consolidated Financial Statements are prepared is RAC Bidco Limited, registered office is the same as for RAC Group (Holdings) Limited.

The largest level at which consolidated Financial Statements are prepared is RAC Group (Holdings) Limited.

20 Post Balance Sheet Event

Since the Statement of financial position date, the worldwide economic environment has been impacted by the emergence of Covid-19 and financial markets have fallen around the world as a result of Covid-19. Given the nature of the Company's business, the type of assets held and the reinsurance arrangements in place, it is not yet possible to determine the full quantitive impact of Covid-19 on the Company.

The Company remains solvent and it's solvency coverage ratio remains strong at over 275% (unaudited) as at 30 April 2020 (31 December 2019: 260%) and remained within the Company's risk appetite as at the date of issuing the financial statements (unaudited). Due to its economic signficance, the emergence of Covid-19 in 2020 is considered to be a non-adjusting post balance sheet event. The RAC Group initiated its financial risk response plan and actions were taken to ensure the Group position remains resilient. The Company's operations and its abliity to service its customers have continued unabated.