

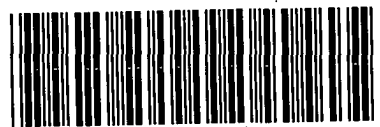
AIRE VALLEY MORTGAGES 2007 - 1 PLC

Annual Report and Financial Statements

for the 15 months to 31 March 2014

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Aire Valley Mortgages 2007 - 1 plc

Annual Report and Financial Statements for the 15 months to 31 March 2014

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Aire Valley Mortgages 2007 - 1 plc

Strategic Report for the 15 months to 31 March 2014

The Directors present their Annual Report and Financial Statements of Aire Valley Mortgages 2007 -1 plc ('the Company') for the 15 months to 31 March 2014. The Company is a public limited liability company incorporated and domiciled in the United Kingdom.

The Company's accounting reference date has been changed from 31 December to 31 March to align to the year end of the Company's controlling party, HM Treasury.

Principal activities

The Company's principal activity is to issue floating and/or fixed rate debt securities and to enter into financial arrangements to fund the activities of certain subsidiaries of Aire Valley Holdings Limited and ultimately UK Asset Resolution Limited ('UKAR') by means of intercompany loans. The debt securities are issued in US Dollars, Euros and Sterling and are secured on a beneficial interest in a portfolio of mortgage loans originated by Bradford & Bingley plc ('B&B') and held under a master trust arrangement by Aire Valley Trustee Limited (the 'Trustee'). These mortgage loans are secured on residential properties in the United Kingdom. Details are set out in the offering circular pertinent to this issue. The Company issued £2,495.1m floating rate notes to the market on 9 May 2007. £570.7m of the notes were redeemed in 2009, £169.4m in March 2010, £232.8m in June 2010, £168.0m in September 2010 and £32.5m in December 2010. In December 2011 £13.6m of loan notes were redeemed. In 2012, £9.0m of loan notes were redeemed in March, £16.9m in September and £15.0 in December. At the exchange rates at date of issue, as at 31 March 2014 £1,123.2m (2012: £1,267.3) remained in issue. Interest expense for the period was £11.4m (12 months to December 2012: £22.3). Fair value profits of £0.4m (12 months to December 2012: £8.0 loss) arose due to the movements in interest rates and exchange rates over the course of the period.

B&B, the originator of the mortgage loans in the Aire Valley Master Trust pool, carries the pool mortgages on its balance sheet. The cash receipts in respect of the mortgage loans in the pool are collected by B&B and paid to the Trustee. Each month and pursuant to the terms of the securitisation transaction documents the Trustee allocates cash between the beneficiaries Aire Valley Funding 1 Limited, the other funding companies in the Aire Valley Master Trust structure and to B&B. Aire Valley Funding 1 Limited allocates the cash received each month between the Company and the other issuing companies in the Aire Valley Funding 1 Limited structure. The Company uses its cash receipts to pay noteholders.

The fair value gain in the period is a timing effect only, which will reverse, and does not have cash implications.

Controlling party

The Company's immediate parent undertaking is Aire Valley Holdings Limited, a private limited liability company incorporated and domiciled in the United Kingdom.

The Company's ultimate parent undertaking is SFM Corporate Services Limited, a private limited liability company incorporated and domiciled in the United Kingdom, which holds the shares of Aire Valley Holdings Limited on a discretionary trust basis for the benefit of certain charities.

Under IFRS, the Company's controlling party during the period and previous year was B&B a public limited company incorporated and domiciled in the United Kingdom. B&B heads the smallest group of companies into which the Financial Statements of the Company are consolidated.

Aire Valley Mortgages 2007 - 1 plc

Strategic' Report for the 15 months to 31 March 2014 (continued)

Controlling party (continued)

The ultimate parent undertaking of B&B is UKAR, a private limited company incorporated and domiciled in the United Kingdom, which is wholly owned by the Treasury Solicitor as nominee for HM Treasury. The Company considers Her Majesty's Government to remain its ultimate controlling party.

Review of the business

During the 15 months to 31 March 2014, Aire Valley Funding 1 Limited made repayments totalling £98m (2012: £24m) to the Company in accordance with the terms of an Inter-Company Loan Confirmation Agreement. These repayments were used to redeem notes. The Company made all interest payments due in line with the securitisation transaction documents.

On 10 May 2012 a non-asset trigger event occurred within the structure of the Aire Valley Master Trust, due to the aggregate current balance of loans comprising the trust property falling below the minimum trust size of £10.7 billion. This affected the order of priority of payments as set out in the Company's Offering Circular. As a result, scheduled redemptions of any outstanding notes will not be paid on their scheduled redemption dates and may not be paid on their final maturity date. All principal receipts in respect of the trust property are allocated to Aire Valley Funding 1 Limited and will continue to be so allocated until the relevant share of the trust property is zero. The principal receipts are utilised by Aire Valley Funding 1 Limited to repay all intercompany term advances until they have been repaid in full, if sufficient funds are available. The issuing companies, including the Company, use this principal to pay down notes pro-rata and sequentially by class. The timing of future redemptions will be dependent on the availability of funds.

Results

The Company is entitled to a pre-determined retained profit under the securitisation transaction documents. Under the terms of the securitisation, the Company retains the right to 0.01% of the interest received under the inter-company loan (as defined within the securitisation transaction documents). This is reflected in the statement of comprehensive income on page 11. The Company is taxed in accordance with the permanent regime for securitisation companies.

Aire Valley Mortgages 2007 - 1 plc

Strategic Report for the 15 months to 31 March 2014 (continued)

Key Performance Indicators (KPIs)

The KPIs used by management in assessing the performance of the Company are the quality of the assets in the mortgage pool and the compliance of the Company with the terms of the securitisation documentation. During the period the Company has complied with the terms of the securitisation documentation. Information about the quality of the assets in the mortgage pool is provided in the monthly trustee reports to investors, available on the website of B&B at <http://www.bbg.co.uk/corporate/financial-information/debt-investors/securitisation>, including the following:

		At 31 March 2014	At 31 December 2012
Number of outstanding mortgage loans	Number	80,378	84,769
Outstanding mortgage loans	£bn	9.8	10.4
Number of mortgage loans 3 months or more in arrears	Number	795	1,098
Principal value of mortgage loans 3 months or more in arrears	£m	107.4	158.6
Arrears value of mortgage loans 3 months or more in arrears	£m	2.7	3.9
Mortgage loans in repossession	Number	118	207
Value of mortgage loans in repossession	£m	14.3	29.2
Weighted average indexed current LTV	%	78.6	84.4

Principal risks and uncertainties

In the ordinary course of business the Company is exposed to, and manages, a variety of risks, with credit risk, liquidity risk and market risk (foreign currency risk and interest rate risk) being of particular significance. The Directors have responsibility for the overall system of internal control and for reviewing its effectiveness. In general, when a transaction or group of transactions is entered into, derivative instruments are taken out to manage the associated risks. The effectiveness of the risk management is then monitored on an ongoing basis. Details of the Company's risks and their management and control are provided in note 13, and further discussion in the context of the B&B Group as a whole is provided on pages 7-9 of that Group's 2014 Annual Report & Accounts, which do not form part of this Report and Financial Statements.

The Company has entered into contracts with a number of third parties to provide operational support including corporate service providers, paying agents and swap providers. B&B acts as a bank account and cash manager

The transaction documentation also sets out a number of business risks through a number of asset and non asset trigger events. The occurrence of trigger events could lead to early redemption of the floating rate notes.

By order of the Board.



Helena Whitaker

per pro SFM Corporate Services Limited

Company Secretary

29 August 2014

Aire Valley Mortgages 2007 - 1 plc

Directors' Report for the 15 months to 31 March 2014

Dividends

The profit for the 15 months to 31 March 2014 £0.4m (2012: loss £8.0m) has been transferred to reserves. No dividends were paid during the 15 months to 31 March 2014 (2012: nil), and the Directors do not recommend the payment of a final dividend for 2014 (2012: £nil). The Company's profits over the lifetime of the securitisation will be limited to the predetermined retained profit.

Future outlook

Although the legal and contractual maturity of the loan notes issued by the Company is in September 2066, the rate at which the loan to Aire Valley Funding 1 Limited and the loan notes will actually reduce will depend upon the Company's allocation of Aire Valley Funding 1 Limited's share of the Trustee's principal receipts. Any significant changes in the level of the Trustee's underlying mortgage redemptions or removals will have an impact upon the maturity profiles of the loan to Aire Valley Funding 1 Limited and the loan notes. A significant increase in arrears and/or repossession losses could ultimately lead to Aire Valley Funding 1 Limited failing to repay all amounts due to the Company in respect of the inter company loan. This in turn could result in the Company failing to make all payments due to note holders in respect of principal and/or interest. Such a situation would not render the Company insolvent because the Company is only obliged to make payments to note holders to the extent that the inter company loan repayments allow.

The Directors expect that during 2014 and 2015 the Company will continue to meet the interest payments on the notes. At the present time the Directors do not foresee any changes in the Company's activities.

Financial risk management objectives and policies

Information regarding the financial risk management objectives and policies of the Company, in relation to the use of financial instruments, is given in note 13. A description of the principal risks to which the Company is exposed is provided on page 5 which forms an integral part of the audited Financial Statements.

Corporate governance

The Directors have been charged with governance in accordance with the transaction documents describing the structure and operation of the transaction. The governance structure of the Company is such that the key policies have been predetermined at the time of issuance and the operational roles have been assigned to third parties with their roles strictly governed by the transaction documents.

The transaction documents provide for procedures that have been designed for safeguarding assets against unauthorised use or disposition; for maintaining proper accounting records; and for the reliability and usefulness of financial information used within the business or for publication. Such procedures are designed to manage rather than eliminate the risk of failure to achieve business objectives whilst enabling the Directors to comply with the regulatory obligations.

Due to the nature of the securities which have been issued, the Company is exempt from the requirements of the Financial Conduct Authority ('FCA') Disclosure and Transparency Rules 7.1 Audit Committees and 7.2 Corporate Governance statements (save for the rule 7.2.5 requiring description of the features of the internal control and risk management systems), which would otherwise require the Company respectively to have an audit committee in place and to include a corporate governance statement in the report of the Directors. The Directors are satisfied that there is no requirement for an audit committee or for a supervisory body entrusted to carry out the functions of an audit committee or to publish a corporate governance statement.

Aire Valley Mortgages 2007 - 1 plc

Directors' Report for the 15 months to 31 March 2014 (continued)

Directors and their interests

The Directors who served during the period and up to the date of signing the Financial Statements were as follows:

Phillip McLelland (resigned 1 December 2013)

Ian Hares (appointed 1 December 2013)

SFM Directors Limited

SFM Directors (No. 2) Limited

Mr McLelland was until 25 November 2013 a director of B&B and UKAR.

Mr Hares is a director of B&B and UKAR.

None of the Directors have any beneficial interest in the ordinary share capital of the Company or Aire Valley Holdings Limited. None of the Directors had any interest during the period in any material contract or arrangement with the Company.

Directors' indemnities

Qualifying third party indemnity provision for the benefit of all Directors was in force during the period under review, and remains in force at the date of approval of the Directors' Report and Financial Statements.

Company Secretary

The Company Secretary during the period and subsequently was SFM Corporate Services Limited.

Aire Valley Mortgages 2007 - 1 plc

Directors' Report for the 15 months to 31 March 2014 (continued)

Statement of Directors' responsibilities

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

Company law requires the Directors to prepare Financial Statements for each financial year. Under that law the Directors have prepared the Financial Statements in accordance with International Financial Reporting Standards ('IFRS') 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, the Directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and accounting estimates that are reasonable and prudent;
- State whether applicable IFRS as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the Financial Statements; and
- Prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

Disclosure of information to auditors

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware, and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418(2) of the Companies Act 2006.

Independent auditors

The independent auditors, PricewaterhouseCoopers LLP, have expressed their willingness to continue in office until the next annual general meeting. Pursuant to section 489 of the Companies Act 2006, a resolution for the re-appointment of PricewaterhouseCoopers LLP will be proposed at the forthcoming annual general meeting of the Company.

By order of the Board.



Helen Whitaker

per pro SFM Corporate Services Limited

Company Secretary

29 August 2014

Registered Office:

35 Great St. Helens

London EC3A 6AP

Aire Valley Mortgages 2007 - 1 plc

Independent Auditors' Report to the members of Aire Valley Mortgages 2007 - 1 plc

Report on the Financial Statements

Our Opinion

In our opinion the Financial Statements, defined below:

- give a true and fair view of the state of the Company's affairs as at 31 March 2014 and of its profit and cash flows for the period then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

This opinion is to be read in the context of what we say in the remainder of this report.

What we have audited

The Financial Statements, which are prepared by Aire Valley Mortgages 2007 - 1, comprise:

- the Balance Sheet as at 31 March 2014;
- the Statement of Comprehensive Income for the period then ended;
- the Cash Flow Statement for the period then ended;
- the Statement of Changes in Equity for the period then ended; and
- the notes to the Financial Statements, which include a summary of principal accounting policies and other explanatory information.

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

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

What an audit of Financial Statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)'). An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the Financial Statements.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited Financial Statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Aire Valley Mortgages 2007 - 1 plc

Independent Auditors' Report to the members of Aire Valley Mortgages 2007 - 1 plc (continued)

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial period for which the Financial Statements are prepared is consistent with the Financial Statements.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

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 no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

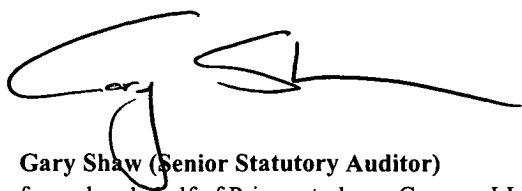
Responsibilities for the Financial Statements and the audit

Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 7, the Directors are responsible for the preparation of the Financial Statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the Financial Statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.



Gary Shaw (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

Leeds

29 August 2014

Aire Valley Mortgages 2007 - 1 plc

Statement of Comprehensive Income for the 15 months to 31 March 2014

	Note	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Interest receivable and similar income	3	11,426	22,382
Interest expense and similar charges	4	(11,371)	(22,344)
Net interest income		55	38
Fair value movements	5	430	(7,950)
Administrative expenses	6	(55)	(36)
Profit/(loss) before taxation		430	(7,948)
Taxation	7	-	(3)
Profit/(loss) for the period/year		430	(7,951)
Other comprehensive income		-	-
Total comprehensive income/(expense) for the financial period/year		430	(7,951)

The results above arise from continuing activities.

The notes on pages 15 to 36 form an integral part of these Financial Statements.

Aire Valley Mortgages 2007 - 1 plc

Balance Sheet as at 31 March 2014

	Note	At 31 March 2014 £000	At 31 December 2012 £000
Assets			
Loans to Group undertakings	10	1,090,309	1,199,809
Derivative financial instruments	12 (c)	134,390	150,934
Total non-current assets		1,224,699	1,350,743
Loans to Group undertakings	10	86,610	74,730
Cash and cash equivalents		217,714	178,146
Current tax assets		1	1
Total current assets		304,325	252,877
Total assets		1,529,024	1,603,620
Liabilities			
Debt securities in issue	8	1,307,990	1,422,572
Total non-current liabilities		1,307,990	1,422,572
Amounts due to banks	9	217,697	178,129
Debt securities in issue	8	317	329
Total current liabilities		218,014	178,458
Total liabilities		1,526,004	1,601,030
Equity			
Issued capital and reserves:			
Share capital	15	13	13
Retained earnings		3,007	2,577
Total equity		3,020	2,590
Total equity and liabilities		1,529,024	1,603,620

The notes on pages 15 to 36 form an integral part of these Financial Statements. The Financial Statements on pages 11 to 36 were approved by the Board of Directors on 29 August 2014 and signed on its behalf by:



Helena Whitaker
As Director per pro SFM Directors Limited
29 August 2014

Aire Valley Mortgages 2007 - 1 plc is registered in England and Wales under Company Number 06133249.

Aire Valley Mortgages 2007 - 1 plc

Statement of Changes in Equity for the 15 months to 31 March 2014

For the 15 months to 31 March 2014

	Share capital £000	Retained earnings £000	Total equity £000
Balance at 1 January 2013	13	2,577	2,590
Total comprehensive income for the period	-	430	430
Balance at 31 March 2014	13	3,007	3,020

For the 12 months to 31 December 2012

	Share capital £000	Retained earnings £000	Total equity £000
Balance at 1 January 2012	13	10,528	10,541
Total comprehensive expense for the year	-	(7,951)	(7,951)
Balance at 31 December 2012	13	2,577	2,590

Aire Valley Mortgages 2007 - 1 plc

Cash Flow Statement for the 15 months to 31 March 2014

	Note	15 months to 31 Mar 2014	12 months to 31 Dec 2012
		£000	£000
Cash flows from operating activities:			
Profit/(loss) before taxation for the financial period/year		430	(7,948)
Cash flows generated from/(used in) operating activities before changes in operating assets and liabilities		430	(7,948)
Net decrease in operating assets:			
- loans to Group undertakings		97,620	34,139
- derivative financial instruments		16,544	46,903
Net increase/(decrease) in operating liabilities:			
- debt securities in issues		(114,594)	(73,094)
- amounts due to banks		39,568	178,129
Net cash generated from operating activities		39,568	178,129
Net increase in cash and cash equivalents		39,568	178,129
Cash and cash equivalents at beginning of period/year		178,146	17
Cash and cash equivalents at end of period/year		217,714	178,146
Cash collateral held	9	217,697	178,129
Cash at bank		17	17
		217,714	178,146

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014

1. Principal accounting policies

Aire Valley Mortgages 2007 - 1 plc ('the Company') is a public limited company incorporated and domiciled in the United Kingdom. The Company's accounting reference date has been changed from 31 December to 31 March to align to the year end of the Company's controlling party, HM Treasury.

(a) Statement of compliance

The Financial Statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ('adopted IFRS').

For these Financial Statements, including the 2012 comparative financial information where applicable, the Company has adopted for the first time the following statements:

- IFRS 13 'Fair Value Measurement' and the associated amendments to IFRS 7 'Financial Instruments: Disclosures'. IFRS 13 sets out principles for measurement of the fair value of financial assets and liabilities, but does not change which items are carried at fair value. In order to comply with IFRS 13, the Company has made minor changes to methods for calculating fair values; the impacts on the 2014 Financial Statements were not material. In accordance with IFRS 13, no restatement has been made of prior period fair values. IFRS 13 and the amended IFRS 7 also introduced additional disclosure requirements.
- The December 2011 amendments to IFRS 7 'Financial Instruments: Disclosures' and IAS 32 'Financial Instruments: Presentation' relating to the offsetting of financial assets and financial liabilities. These amendments had no material impact on the Company.
- The Annual Improvements to IFRSs 2009-2011 Cycle, issued in May 2012. These changes had no material impact on the Company.

For these Financial Statements the Company has not adopted the following statements; the Company is assessing the impacts of these statements on its Financial Statements:

- IFRS 9 'Financial Instruments', sections of which have been issued as part of the International Accounting Standard Board's ('IASB's') project to replace IAS 39 'Financial Instruments: Recognition and Measurement'; this statement has not yet been adopted for use in the EU. The Company continues to monitor developments.
- The June 2013 amendments to IAS 39 relating to 'Novation of Derivatives and Continuation of Hedge Accounting', which will be mandatory for the Company's Financial Statements for the year to 31 March 2015. This restricts the circumstances in which a novation of a derivative contract may be treated as a continuation of an existing hedge relationship.
- The Annual Improvements to IFRSs 2010-2012 Cycle, issued in December 2013. These changes are mandatory for the Company's Financial Statements for the year to 31 March 2016.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

1. Principal accounting policies (continued)

(a) Statement of compliance (continued)

- The Annual Improvements to IFRSs 2011-2013 Cycle, issued in December 2013. These changes are mandatory for the Company's Financial Statements for the year to 31 March 2016.

All other new standards, amendments to standards and interpretations are not considered relevant to, and have no impact upon, the Financial Statements of the Company.

(b) Basis of preparation

The Financial Statements are prepared on the historical cost basis except for financial instruments classified as 'at fair value through profit or loss'.

The Financial Statements are presented in pounds sterling, which is the currency of the Company's primary operating environment, and on a going concern basis.

The Directors consider that the accounting policies set out in this note are the most appropriate to the Company's circumstances, have been consistently applied by the Company in dealing with items which are considered material, and are supported by reasonable and prudent estimates and judgements.

The Financial Statements have been prepared in accordance with EU adopted IFRS, IFRIC interpretations issued by the IFRS Interpretations Committee and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. A summary of accounting policies is set out below. The preparation of the Financial Statements in conformity with these accounting policies and generally accepted accounting principles requires the use of estimates and assumptions that affect the reported values of assets and liabilities at the date of the Financial Statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amounts, event or actions, actual results ultimately may differ from those estimates (see note 2).

(c) Interest income and expense

For all interest-bearing financial instruments except derivatives, interest income and expense are recognised in the Income Statement on an Effective Interest Rate ('EIR') basis.

The EIR method calculates the amortised cost of a financial asset or financial liability and spreads interest income or interest expense on a level yield basis over the expected life of the instrument, or an appropriate shorter period. The calculation includes all directly attributable incremental fees and costs and all premia and discounts as well as interest. The EIR is the rate which at the inception of the instrument exactly discounts expected future cash flows over the appropriate period to the initial carrying amount. When calculating the EIR, future cash flows are estimated, considering all contractual terms of the instrument (for example prepayment options), but potential future credit losses are not considered.

Interest on derivatives is included in interest income where the derivative is hedging interest income, and interest expense where the derivative is hedging interest expense.

When a financial asset or a group of similar financial assets is written down as a result of an impairment loss, interest income continues to be recognised by applying the applicable EIR to the reduced balance.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

1. Principal accounting policies (continued)

(d) Debt securities in issue

On initial recognition, debt issued is measured at its fair value net of directly attributable transaction costs and discounts, in accordance with IAS 39. Subsequent measurement is at amortised cost using the EIR method to amortise incremental attributable issue and transaction costs, premia and discounts over the life of the instrument; these costs are charged along with interest on the debt to 'interest expense and similar charges'. The carrying value of the instrument includes the amount of these adjustments which still remains to be charged to the Statement of Comprehensive Income.

(e) Financial instruments

In accordance with IAS 39 each financial asset is classified at initial recognition into one of four categories:

- (i) Financial assets at fair value through profit or loss;
- (ii) Held to maturity investments;
- (iii) Loans and receivables; or
- (iv) Available-for-sale;

and each financial liability into one of two categories:

- (v) Financial liabilities at fair value through profit or loss; or
- (vi) Other liabilities.

Measurement of financial instruments is either amortised cost (categories (ii), (iii) and (vi) above) or at fair value (categories (i), (iv) and (v) above), depending on the category of financial instrument. The Company does not carry any financial instruments at fair value other than derivative financial instruments.

Amortised cost is the amount measured at initial recognition, adjusted for subsequent principal and other payments, less cumulative amortisation calculated using the EIR method; the amortisation is taken to interest income or expense depending on whether the instrument is an asset or a liability. For assets, the amortised cost balance is reduced where appropriate by an allowance for amounts which are considered to be impaired or uncollectible. The loans to Group undertakings will not become impaired unless the mortgages in the pool become impaired to the extent that all credit enhancement is used up.

IFRS 13 'Fair Value Measurement' defines 'fair value' as 'the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date'. Where an active market is considered to exist, fair values are based on quoted prices or lead manager prices. For instruments which do not have active markets, fair value is calculated using discounted cash flows, applying independently sourced market parameters including interest rates and currency rates. Any net movements in fair value are included in the Statement of Comprehensive Income as 'fair value movements'.

(f) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the Balance Sheet when and only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

1. Principal accounting policies (continued)

(g) Derivative financial instruments and hedge accounting

All of the Group's derivative contracts are used for commercial management of exposures to interest rate risks and foreign currency risks.

The Company applied fair value hedge accounting to its floating rate notes to hedge interest and exchange rate movements. In 2011 the Company ceased to apply hedge accounting. The carrying amount of floating rate notes still includes legacy fair value hedge adjustments which are being amortised to the Statement of Comprehensive Income over the instruments' remaining lives by recalculating their effective interest rate.

Each derivative is carried at fair value in the Balance Sheet; as an asset when the fair value is positive and as a liability when the fair value is negative. The fair value of a derivative includes any interest accrued on that derivative. Changes in the fair value of derivatives are charged to the Income Statement.

(h) Impairment losses

The Company assesses its financial assets for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event (or events) that has occurred after initial recognition and before the balance sheet date and that has a reliably measurable impact on the estimated future cash flows of the financial assets.

The only asset held by the Company that is at risk of material impairment is the loan to Aire Valley Funding 1 Limited, the repayment of which is dependent upon the performance of the residential mortgage portfolio as represented by the loan to originator from Aire Valley Funding 1 Limited to B&B. The risk of impairment is mitigated to a degree by the existence of reserve funds as detailed in note 13. The performance of the mortgage portfolio is continually assessed by B&B and external credit rating agencies. It follows that the impairment policies of B&B are applied by the Company.

(i) Recognition and derecognition of financial instruments

A financial asset is derecognised (i.e. removed from the Balance Sheet) only when substantially all of the risks and rewards associated with that asset have been transferred to another party.

A financial liability is derecognised only when the contractual obligation is discharged, cancelled or has expired.

(j) Foreign currencies

The presentational and functional currency of the Company is pounds sterling.

Transactions which are not denominated in pounds sterling are translated into sterling at the spot rate of exchange on the date of the transaction. Monetary assets and liabilities which are not denominated in pounds sterling are translated into pounds sterling at the closing rate of exchange at the Balance Sheet date.

Foreign exchange gains and losses resulting from the restatement and settlement of such transactions are recognised in the Income Statement.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

1. Principal accounting policies (continued)

(k) Cash and cash equivalents

Cash and cash equivalents comprise balances which are highly liquid and have an original maturity of three months or less.

As the cash can only be used to meet certain specific liabilities and is not available to be used with discretion, it is viewed as restricted cash.

(l) Taxation

The Company is taxed in accordance with the permanent regime for securitisation companies. Under the permanent regime, as the tax charge is based purely on contractually retained profit, neither the current tax charge nor deferred tax will be affected by any fair value gains or losses arising on derivatives and other financial instruments.

(i) Current tax

The charge for taxation is based on the result for the period and takes into account taxation deferred or accelerated arising from temporary differences between the carrying amounts of certain items for taxation and for accounting purposes. Tax relating to items which are taken directly to reserves is also taken directly to reserves.

(ii) Deferred tax

Deferred tax is calculated using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Financial Statements. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the Balance Sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

2. Critical accounting judgements and estimates

In preparing the Financial Statements, management are required to make a series of judgements and estimates. Judgements involve an interpretation of requirements to decide how to allocate, value or recognise an item. Estimates arise from using assumptions which result in a range of possible outcomes. The most important judgements and estimates used in preparing the Financial Statements are described below.

(a) Effective interest rate

Certain financial instruments are accounted for at amortised cost on an effective interest rate basis, under which the income or expense associated with the instrument is spread over the instrument's expected life. On a quarterly basis, models are reviewed to re-assess expected life.

(b) Fair value calculations

Certain financial instruments are carried at fair value. Where a market exists, fair values are based on quoted market prices or lead manager prices. For instruments which do not have an active market, fair value is calculated using expected future cash flows for which assumptions are made.

Fair value is defined as the value at which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Where quoted market prices are not available, fair value is calculated using discounted cash flows, applying independently sourced market parameters including interest rates and currency rates. Other factors are also considered, such as counterparty credit quality and liquidity. Management must use judgement to arrive at estimates where not all necessary data can be externally sourced or where factors specific to the Company's holdings need to be considered. The accuracy of the fair value calculations may therefore be affected by unexpected market movements, or variations in actual outcomes when compared to estimates and assumptions used for modelling purposes. For example, if management were to use a tightening in the credit spread of 10 basis points, the fair value of derivatives would decrease from the reported fair values by £0.03m (2012: £0.03m).

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

3 Interest receivable and similar income

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Interest on loans to Group undertakings	11,426	22,382
	11,426	22,382

Interest income for the period on impaired assets was £nil (2012: £nil) as no financial asset is impaired.

4 Interest expense and similar charges

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Interest on floating rate notes	8,898	20,119
Amortisation of issue costs	-	99
Swap interest	2,473	2,126
	11,371	22,344

5 Fair value movements

Fair value movements in the Statement of Comprehensive Income comprised the following:

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Net losses on derivatives	(16,544)	(46,803)
Net gains on debt securities in issue due to exchange rate movements	17,214	38,748
Amortisation of the carrying value of de-designated fair value hedge	(240)	105
	430	(7,950)

Cross-currency swaps are used to hedge the interest and exchange rate risk on the floating rate notes. This represents an effective economic hedge, but for accounting purposes there is some hedge ineffectiveness which is a timing issue only.

The Company applied fair value hedge accounting to its floating rate notes to hedge interest and exchange rate movements. In 2011 the Company ceased to apply hedge accounting. The carrying amount of floating rate notes still includes legacy fair value hedge adjustments which are being amortised to the Statement of Comprehensive Income over the instruments' remaining lives by recalculating their effective interest rate.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

6 Administrative expenses

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Corporate services fee - Structured Finance Management Limited	21	11
Audit fees	4	-
Other legal and professional fees	28	25
	53	36

Auditors' remuneration of £4,000 for 2012 was borne by B&B.

There were no employees during the period (2012: none) and none of the Directors received emoluments in respect of their services to the Company. A fee is paid to Structured Finance Management Limited for the provision of corporate administration services including the provision of directors (see note 11).

7 Taxation

The taxation charge/(credit) relates to the profit/(loss) for the period/year as follows:

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Current taxation charge:		
- UK Corporation tax on profit for the year	-	-
- Adjustments in respect of previous years	-	3
Total taxation charge per the Statement of Comprehensive Income	-	3
Profit/(loss) before taxation	430	(7,948)
UK Corporation tax at 23.2% (2012: 24.5%)	100	(1,947)
Effects of:		
- Expenses not deductible for taxation	-	1,947
- Income not taxable	(100)	-
- Adjustments in respect of previous years	-	3
Total taxation charge per the Statement of Comprehensive Income	-	3

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

8 Debt securities in issue

Class	Interest rate	In currency 31 March 2014	In currency 31 December 2012	31 March 2014 £000	31 December 2012 £000
Series 1 B	3M LIBOR + 0.52	£62,500,000	£62,500,000	62,500	62,500
Series 1 C	3M LIBOR + 0.52	£62,500,000	£62,500,000	62,500	62,500
Series 2 A1	3M US LIBOR + 0.23	\$599,305,592	\$663,352,222	359,350	408,644
Series 2 A2	3M EURIBOR + 0.26	€ 492,286,736	€544,896,467	406,998	442,674
Series 2 A3	3M LIBOR + 0.26	£256,845,254	£284,293,809	256,845	284,294
Series 2 B	3M LIBOR + 0.44	£75,000,000	£75,000,000	75,000	75,000
Series 2 C	3M LIBOR + 1.10	£81,250,000	£81,250,000	81,250	81,250
				1,304,443	1,416,862
Unamortised carrying value of de-designated fair value hedge				(890)	(1,120)
				1,303,553	1,415,742
Accrued interest - non-current				4,437	6,830
Accrued interest - current				317	329
				1,308,307	1,422,901

Debt securities in issue comprise floating rate notes issued on 9 May 2007, with a final maturity of September 2066.

Subject to their scheduled redemption dates, the Class A notes rank, irrespective of series, without preference or priority amongst themselves. Subject to the relevant scheduled and/or, as applicable, permitted redemption dates or other payment conditions of the issuer notes, payments of principal and interest due and payable on the Class A notes will rank ahead of payments of principal and interest due and payable on the Class B and Class C notes, subject to the terms and conditions of the notes, the Issuer Cash Management Agreement, the Issuer Deed of Charge and the other issuer transaction documents. Similarly, payments of principal and interest due and payable on the Class B notes will rank ahead of payments of principal and interest due and payable on the Class C notes.

Under the terms of the notes, any shortfalls arising on the redemption of the loans to Group undertakings, over which the noteholders have a charge, may result in a reduction in the liability under the notes, due to their limited recourse nature. Such shortfall on the redemption of the loan to Group undertakings may arise if the underlying mortgage pool against which the loan to Group undertakings is secured does not generate sufficient cash to repay the loan to Group undertakings and the credit enhancement in the structure is not sufficient to cover such shortfall.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

8 Debt securities in issue (continued)

On 10 May 2012 a non-asset trigger event occurred within the structure of the Aire Valley Master Trust, due to the aggregate current balance of loans comprising the trust property falling below the minimum trust size of £10.7billion. This affected the order of priority of payments as set out in the Company's Offering Circular. As a result, the outstanding notes will be redeemed on their scheduled redemption dates and may not be redeemed on their final maturity date. All principal receipts in respect of the trust property are allocated to Aire Valley Funding 1 Limited and will continue to be so allocated until the relevant share of the trust property is zero. The principal receipts are utilised by Aire Valley Funding 1 Limited to repay all intercompany term advances until they have been repaid in full, if sufficient funds are available. Therefore the notes are now in 'pass through' and will be partially redeemed on each quarterly interest payment date to the extent that funds are available in accordance with the terms set out in the Offering Circular. The timing of future redemptions will be dependent on the availability of funds, and could not be reliably forecast and hence the notes have all been described as non-current liabilities.

Interest is payable on the Series 2 Class A1 notes at variable rates based upon three month US Dollar LIBOR. Interest is payable on Series 2 Class A2 notes at variable rates based upon three month EURIBOR. Interest is payable on the Series 1 Class B and C and Series 2 Class A3, B and C notes at variable rates based upon the three month sterling LIBOR. On 10 May 2012 a non-asset trigger event occurred. All outstanding notes have passed their 'step-up' date and interest is being paid at the step-up rate. The step up has been accounted for on an EIR basis.

The Company's obligations to noteholders and to other secured creditors are secured under a Deed of Charge which grants security over all its assets in favour of the Security trustee. The principal assets of the Company are loans made by it to Aire Valley Funding 1 Limited, a fellow subsidiary of Aire Valley Holdings Limited, whose obligations in respect of these loans are secured pursuant to a Deed of Charge which grants security over all its assets, primarily consisting of its beneficial interest in a portfolio of residential mortgage loans, in favour of the Security trustee. The Security trustee holds this security for the benefit of all secured creditors of Aire Valley Funding 1 Limited, including the Company.

9 Amounts due to banks

	At 31 Mar 2014 £000	At 31 Dec 2012 £000
Cash collateral which the Company has received	217,697	178,129
Total	217,697	178,129

All of the cash collateral held is in respect of collateral received from derivative counterparties pursuant to the provisions of associated credit support agreements.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

10 Loans to Group undertakings

The loans to Group undertakings comprise a single loan to Aire Valley Funding 1 Limited, denominated in sterling and at a variable rate of interest linked to 3 month LIBOR. The loan has ultimately been secured against a beneficial interest in a mortgage portfolio held in trust on behalf of the Aire Valley Holdings Limited Group.

The ability of Aire Valley Funding 1 Limited to pay amounts due on the intercompany loan will depend mainly upon it receiving sufficient revenue receipts and principal on the trust property from Aire Valley Trustee Limited, receiving the required funds from the swap provider and amounts available in the reserve funds.

The terms of the loans to Group undertakings are set such that the Company's income is sufficient to service its liabilities and to retain a profit prescribed by the terms of the securitisation structure.

Amounts classified as 'current' represent expected repayments due within the next twelve months.

11 Related party disclosures

The Company is a special purpose vehicle controlled by its Board of Directors, which comprises three Directors. Two of the Company's three Directors are corporate Directors provided by Structured Finance Management Limited and the third Director is a director of B&B (the controlling party under IFRS). The Company pays a fee to Structured Finance Management Limited for the provision of corporate administration services including the provision of directors. The Company undertook the following transactions with related parties during the period:

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Corporate services fee payable to Structured Finance Management Limited		
Expense	21	11
Interest receivable and similar income		
Interest on loans to Group undertakings	11,426	22,382
Non-current assets		
Loans to Group undertakings	1,176,919	1,274,539

At 31 March 2014 B&B held £281,250,000 (31 December 2012: £281,250,000), €20,548,000 (31 December 2012: €22,744,000) and \$25,685,000 (31 December 2012: \$28,429,000) of the Company's floating rate notes and earned interest in the amount of £5,186,000 (12 months to 31 December 2012: £4,129,000), €203,000 (12 months to 31 December 2012: €226,000) and \$160,000 (12 months to 31 December 2012: \$191,000) during the 15 months to 31 March 2014.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

12 Financial instruments

(a) Categories of financial assets and financial liabilities: carrying value compared to fair value

The following table summarises the carrying amounts and fair values of financial assets and liabilities. Assets are generally presented bid prices, whereas offer prices are used for liabilities. The accounting policy note 1(e) sets out the key principles used for estimating the fair values of financial instruments. This note provides some additional information in respect of the methodologies used.

At 31 March 2014

	Assets at fair value through profit or loss	Loans and receivables	Total carrying value	Fair value
	£000	£000	£000	£000
Financial assets				
Loans to Group undertakings	-	1,176,919	1,176,919	1,176,919
Derivative financial instruments	134,390	-	134,390	134,390
Cash and cash equivalents	-	217,714	217,714	217,714
Total financial assets	134,390	1,394,633	1,529,023	1,529,023

	Liabilities at fair value through profit or loss	Liabilities measured at amortised cost	Total carrying value	Fair value
	£000	£000	£000	£000
Financial liabilities				
Debt securities in issue	-	1,308,307	1,308,307	1,249,909
Amounts due to banks	-	217,697	217,697	217,697
Total financial liabilities		1,526,004	1,526,004	1,467,606

At 31 December 2012

	Assets at fair value through profit or loss on initial recognition	Loans and receivables	Total carrying value	Fair value
	£000	£000	£000	£000
Financial assets				
Loans to Group undertakings	-	1,274,539	1,274,539	1,274,539
Derivative financial instruments	150,934	-	150,934	150,934
Cash and cash equivalents	-	178,146	178,146	178,146
Total financial assets	150,934	1,452,685	1,603,619	1,603,619

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

12 Financial instruments (continued)

(a) Categories of financial assets and financial liabilities: carrying value compared to fair value (continued)

	Liabilities at fair value through profit or loss	Liabilities measured at amortised cost	Total carrying value	Fair value
	£000	£000	£000	£000
Financial liabilities				
Debt securities in issue	-	1,422,901	1,422,901	1,271,719
Amounts due to banks	-	178,129	178,129	178,129
Total financial liabilities	-	1,601,030	1,601,030	1,449,848

Note: The fair values above as at 31 December 2012 have not been restated to comply with IFRS 13. However, any differences between the fair values above and IFRS 13-compliant fair values would not be material.

No financial assets or liabilities were reclassified during the period between amortised cost and fair value categories (2012: none).

Valuations methods for calculations of fair values in the table above are set out in note 12 (d).

(b) Interest income and expense on financial instruments that are not at fair value through profit or loss

	15 months to 31 Mar 2014 Income £000	15 months to 31 Mar 2014 Expense £000	12 months to 31 Dec 2012 Income £000	12 months to 31 Dec 2012 Expense £000
Interest on loans to Group undertakings	11,426	-	22,382	-
Interest earned on cash collateral deposited (see note 9)	-	-	-	-
Interest on floating rate notes	-	8,898	-	20,119
Amortisation of issue costs	-	-	-	99

These amounts represent interest income and expense before hedging arrangements.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

12 Financial instruments (continued)

(c) Derivatives

The Company had the following types of derivatives:

	Fair value £000	Nominal amount £000
At 31 March 2014		
Cross-currency interest rate swaps	134,390	
Total asset balances	134,390	766,348

	Fair value £000	Nominal amount £000
At 31 December 2012		
Cross-currency interest rate swaps	150,934	851,318
Total asset balances	150,934	851,318

(d) Fair value measurement

Financial assets and liabilities carried at fair value are valued on the following bases:

At 31 March 2014	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial assets				
Derivative financial instruments	-	134,390	-	134,390

At 31 December 2012	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial assets				
Derivative financial instruments	-	150,934	-	150,934

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices that are observable for the asset or liability, whether directly (i.e. as price) or indirectly (i.e. derived from the implications of prices).

Level 3: Inputs for the asset or liability that are not based on observable market data or have significant unobservable inputs.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

12 Financial instruments (continued)

(d) Fair value measurement (continued)

Instruments which had been disclosed as 'Level 3' at 31 December 2012 have now been recategorised as 'Level 2' as the unobservable inputs have been assessed to be insignificant.

There were no transfers between Level 1 and Level 2 during the period (2012: none).

Derivative financial instruments which are categorised as Level 2 are those which either:

(a) Have future cash flows which are known dates and for which the cash flow amounts are known or calculable by reference to observable interest and foreign currency exchange rates; or

(b) Have future cash flows which are not pre-defined, but which the fair value of the instrument has very low sensitivity to unobservable inputs.

In each case the fair value is calculated by discounting cash flows using observable market parameters including swap rates, interest rates and currency rates.

The fair value of loans to Group undertakings reflects the market yields implied by the floating rate valuations.

The fair value of interest-bearing loans and borrowings is based upon quoted market prices.

For financial assets and liabilities which are not carried at fair value, the fair values disclosed in note 12(a) are calculated on the following bases:

At 31 March 2014	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial assets				
Loans to Group undertakings	-	-	1,176,919	1,176,919
Cash and cash equivalents	217,714	-	-	217,714
	217,714	-	1,176,919	1,394,633
Financial liabilities				
Debt securities in issue	-	1,249,909	-	1,249,909
Amounts due to banks	217,697	-	-	217,697
	217,697	1,249,909	-	1,467,606

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

12 Financial instruments (continued)

(d) Fair value measurement (continued)

Valuation methods for calculations of fair values in the table above are as follows:

Loans to Group undertakings

Loans to Group undertakings are held in Sterling and are at variable rates of interest. Therefore the carrying value of these loans is considered to approximate to fair value.

Cash and cash equivalents

Fair value is estimated by using discounted cash flows applying either market rates where practicable or rates offered by other financial institutions for accounts with similar characteristics. The fair value of floating rate placements, fixed rate placements with less than six months to maturity and overnight deposits is estimated to be their carrying amount.

Debt securities in issue

Fair values are based on quoted prices or lead manager prices where available, or by using discounted cash flows, applying independently sourced market parameters including interest rates and currency rates.

Amounts due to banks

The fair value is considered to approximate the carrying value, as the balances are at variable interest rates and could be demanded to be repaid at short notice.

(e) Offsetting

No financial assets have been offset against financial liabilities, and none are subject to enforceable master netting arrangements or similar agreements.

(f) Collateral

The Company holds cash collateral in respect of certain derivatives (see note 9).

13 Financial risk management

The Company's exposure to risk on financial instruments and the management of this risk are established at the commencement of the securitisation transactions, with the Company's activities and the roles of other parties defined in the transaction documents. Financial instruments used by the Company for risk management purposes include derivative instruments. Such instruments are used for commercial hedging purposes only, not for trading or speculative purposes, to hedge interest rate and currency risk arising as part of the securitisation transaction. The principal derivative instruments used by the Company in managing its risk are cross currency swaps. The maturity profile of derivative instruments reflects the nature of exposures arising from underlying business activities. All of the Company's derivatives activity is contracted with financial institutions.

(a) Credit risk

Credit risk is the potential for financial loss caused by a party failing to meet an obligation as it becomes due. The Company is exposed to credit risk via amounts due from the loans to Group undertaking, derivative counterparties and deposits with third party banks.

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

13 Financial risk management (continued)

(a) Credit risk (continued)

The Company's ability to meet payments under the floating rate notes relies on the receipt of funds on the loans to Group undertaking, which in turn is dependent on receipt of payments on the mortgage portfolio held in trust. To minimise risk, any mortgage included in the portfolio is required to meet a number of criteria as determined in the transaction documentation. Credit risk also exists on the derivative contracts entered into. The swap counterparties are required to have minimum credit ratings as outlined in the transaction documentation and where appropriate the Company holds collateral in respect of derivatives (see note 9).

The maximum credit risk exposure at the Balance Sheet date before taking account of any collateral netting and other enhancements was as follows :

	At 31 March 2014 £000	At 31 December 2012 £000
Cash and cash equivalents	217,714	178,146
Derivative financial instruments	134,390	150,934
Loans to Group undertakings	1,176,919	1,274,539
Total on-Balance Sheet and maximum exposure to credit risk	1,529,023	1,603,619

No impairment has been recognised in respect of any financial asset, and no financial assets were past due.

Credit enhancements

Credit enhancement is provided to the securitisation structure in a number of ways. The mortgage pool assets are significantly greater than the notes which have been issued by the subsidiaries of Aire Valley Holdings Limited. This over-collateralisation as well as the reserve fund are available to make good any reductions in the principal balance of the mortgage pool as a result of defaults by customers.

At 31 March 2014 the cash and cash equivalents were deposited with a counterparty which had a credit rating of AA- (31 December 2012: AA-).

	At 31 March 2014 £000	At 31 December 2012 £000
Mortgages	9,772,466	10,402,949
Notes in issue	(7,056,459)	(7,667,634)
Over collateralisation	2,716,007	2,735,315
Reserve fund	380,000	380,000
Total credit enhancements	3,096,007	3,115,315

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

13 Financial risk management (continued)

(a) Credit risk (continued)

Credit enhancements (continued)

The Company is exposed to credit risk on the 'loans to Group undertaking'. This comprises a loan to Aire Valley Funding 1 Limited, which used the proceeds to purchase an interest in a portfolio of residential mortgages from B&B. The credit risk associated with the mortgage portfolio is continually monitored by the B&B group and external rating agencies. A significant increase in the arrears and/or repossession losses associated with this mortgage portfolio could result in Aire Valley Funding 1 Limited being unable to make all repayments of interest and principal due to the Company in respect of the loans. This in turn could mean that the Company is unable to make all repayments of interest and principal due in respect of the loan notes. It should be noted however, that the Company is only obliged to make repayments of interest and principal in respect of the loan notes to the extent that the repayments received from the loans to Aire Valley Funding 1 Limited allow.

(b) Liquidity risk

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due. The ability of the Company to meet payments under the floating rate notes relies on the receipt of funds on the loans to Group undertaking, which is in turn dependent on the receipt of payments on the mortgage portfolio held in trust.

There is a liquidity reserve fund provided by Aire Valley Funding No.1 Limited in the event that the Company is unable to meet its financial commitments, on a temporary basis, in certain circumstances and subject to certain criteria. This fund was not drawn upon during the current period or preceding year or in 2014 up to the date of authorisation of these Financial Statements.

The contractual undiscounted cash flows associated with financial liabilities were as follows:

31 March 2014	On demand £000	Within three months £000	After three months but within one year £000	After one year but within five years £000	After five years £000	Total £000
Debt securities in issue	-	25,652	83,357	572,356	688,395	1,369,760
Amounts due to banks	217,697	-	-	-	-	217,697
Total	217,697	25,652	83,357	572,356	688,395	1,587,457

31 December 2012	On demand £000	Within three months £000	After three months but within one year £000	After one year but within five years £000	After five years £000	Total £000
Debt securities in issue	-	31,675	117,149	856,287	461,120	1,466,231
Amounts due to banks	178,129	-	-	-	-	178,129
Total	178,129	31,675	117,149	856,287	461,120	1,644,360

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

13 Financial risk management (continued)

(b) Liquidity risk (continued)

The cash flows above assume that the loan notes are redeemed on the earliest possible date that the Company could be compelled to redeem them. As described in note 8, on 10 May 2012 a non-asset trigger event occurred. This has affected the timing of future redemptions of the loan notes.

These differ from Balance Sheet values due to the effects of discounting on certain Balance Sheet items and due to the inclusion of contractual future interest flows.

Prepayment risk

'Prepayment risk' arises when it is possible that the assets may be realised earlier than it is possible to redeem the liabilities. Following the advent of the pass-through arrangements on 10 May 2012, this risk is fully mitigated because all available principal receipts are utilised to make repayments on the loan notes. There is no restriction on the amount which can be repaid on any given payment date as was the case when scheduled amortisation was applicable.

(c) Market risk

Foreign currency risk

The Company has floating rate notes in issue denominated in Euros and US Dollars. The Company's policy is to eliminate all exposures arising from movements in exchange rates by the use of cross currency swaps to economically hedge payments of interest and principal on the notes. All other assets, liabilities and transactions are denominated in Sterling. Consequently, at 31 March 2014 and 31 December 2012 the Company had no net material exposure to foreign exchange fluctuations or changes in foreign currency interest rates. The impact on the Company's profit and equity of reasonably possible changes in exchange rates compared to actual rates would not have been material at 31 March 2014; the movement in value of the floating rate notes would be offset by movement in value of derivatives.

The table below summarises the Company's exposure to foreign currency exchange rate risk at the Balance Sheet date :

	Euro	US \$	Total
At 31 March 2014	£000	£000	£000
Financial assets			
Cash and cash equivalents	217,697	-	217,697
Derivative financial instruments	407,075	359,407	766,482
Total financial assets	624,772	359,407	984,179
Financial liabilities			
Debt securities in issue	407,075	359,407	766,482
Amounts due to banks	217,697	-	217,697
Total financial liabilities	624,772	359,407	984,179
Net currency gap	-	-	-

Aire Valley Mortgages 2007 - 1 plc

Notes to the Financial Statements for the 15 months to 31 March 2014 (continued)

16 Ultimate controlling party

The Company's immediate parent undertaking is Aire Valley Holdings Limited, a private limited liability company incorporated and domiciled in the United Kingdom.

The Company's ultimate parent undertaking is SFM Corporate Services Limited, a private limited liability company incorporated and domiciled in the United Kingdom, which holds the shares of Aire Valley Holdings Limited on a discretionary trust basis for the benefit of certain charities.

Copies of the financial statements of Aire Valley Holdings Limited and SFM Corporate Services Limited may be obtained from the Company Secretary at 35 Great St. Helen's, London, EC3A 6AP.

Under IFRS, the Company's controlling party during the period and previous year was B&B a public limited company incorporated and domiciled in the United Kingdom. B&B heads the smallest group of companies into which the Financial Statements of the Company are consolidated. Copies of the financial statements of B&B may be obtained from the Company Secretary at Croft Road, Crossflatts, Bingley, West Yorkshire BD16 2UA.

The ultimate parent undertaking of B&B is UKAR, a private limited company incorporated and domiciled in the United Kingdom, which is wholly owned by the Treasury Solicitor as nominee for HM Treasury. UKAR heads the largest group of companies into which the Financial Statements of the Company are consolidated. Copies of the financial statements of UKAR may be obtained from the Company Secretary at Croft Road, Crossflatts, Bingley, West Yorkshire BD16 2UA. The Company considers Her Majesty's Government to remain its ultimate controlling party.

17 Events after the reporting period

The Directors are of the opinion that there have been no significant events which have occurred since 1 April 2014 to the date of this report that are likely to have a material effect on the Company's financial position as disclosed in these Financial Statements.