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# B.A.T. INTERNATIONAL FINANCE p.l.c.

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## 2012 Annual Report

# B.A.T. INTERNATIONAL FINANCE p.l.c.

## ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2012

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### Notice of Meeting

Notice is hereby given that the Annual General Meeting of B.A.T. International Finance p.l.c. will be held at Globe House, 4 Temple Place, London, WC2R 2PG on 5 April 2013 at 10am for the transaction of the following business:

1. To receive the financial statements for the year ended 31 December 2012 and the reports of the Directors and the Auditors thereon.
2. To reappoint Directors.
3. To reappoint the Auditors.
4. To authorise the Directors to determine the Auditors' remuneration.

By Order of the Board

Ann Griffiths, Assistant Secretary  
3 April 2013

#### Note:

A member entitled to attend and vote is entitled to appoint a proxy to attend and vote instead of him. Such proxy need not be a member of the Company.

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### Secretary and Registered Office

Nicola Snook  
Globe House  
4 Temple Place  
London WC2R 2PG

### Registered Number 1060930

### Auditors

PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
1 Embankment Place, London WC2N 6RH

## Directors' Report for the year ended 31 December 2012

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### Introduction

The Directors present their Annual Report and the audited Financial Statements for B.A.T. International Finance p.l.c. ('the Company') and its subsidiaries ('the Group') for the year ended 31 December 2012.

### Board of Directors

The names of the persons who served as Directors of the Company during the period 1 January 2012 to the date of this report are as follows:

John Benedict Stevens  
Kenneth John Hardman  
Robert Lee Allen (resigned 29 February 2012)  
Michael Scott Hayes (resigned 21 March 2012)  
Robert James Casey  
Christopher John McAllister (appointed 10 February 2012)  
Tadeu Luiz Marroco (appointed 10 February 2012)

Mr R.J. Casey and Mr K.J. Hardman are subject to retirement by rotation and, being eligible, offer themselves for reappointment at the forthcoming Annual General Meeting.

### Business Review for the year ended 31 December 2012

The Group's profit for the financial year amounted to **£164 million** (2011: £83 million). Total equity has increased by **£135 million** (2011: increased by £97 million). The Directors do not recommend payment of a dividend for the year (2011: £nil).

At 31 December 2012 no commercial paper was outstanding (2011: £85 million).

In June 2012 the Group repaid a €337 million bond due in June 2012.

In June 2012 the Group issued new US\$2 billion bonds: US\$500 million with a maturity of June 2015; US\$600 million with a maturity of June 2017; and US\$900 million with a maturity of June 2022.

The Directors expect the Company's activities to continue on a similar basis in the foreseeable future.

### Post balance sheet events

In March 2013 the Group issued new US\$300 million bonds with a maturity of March 2016, and €650 million bonds with a maturity of March 2025.

### Principal activities, risks and uncertainties

The principal activities of the Group and the Company comprise the raising of finance for British American Tobacco p.l.c. and its subsidiaries ('the BAT Group'), the management of financial risks arising from the BAT Group's underlying operations and the management of the BAT Group's cash resources. The Group's treasury operations and management of financial risks are described fully in note 12 on pages 22-26. All these activities are carried out under defined policies, procedures and limits. It is intended that the Group will continue to undertake business relating to these activities.

Given the nature of the Group's activities, the Group's capital base is managed within the overall framework of the BAT Group and the Company's Directors consider that key performance indicators based solely on the Group's results are not necessary or appropriate for an understanding of the Group's specific development, performance or position of its business. However, key performance indicators relevant to the BAT Group, and which may be relevant to the Group, are disclosed in the Business Review of British American Tobacco p.l.c. and do not form part of this report.

The Board of British American Tobacco p.l.c. reviews and agrees the overall treasury policies and procedures, delegating appropriate authority to the Company. The British American Tobacco p.l.c. Finance Director is a member of the Board of the Company and any significant change to agreed policies is subject to prior approval by the Board of British American Tobacco p.l.c.

## Directors' Report continued

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Clear parameters have been established, including levels of authority, on the type and use of financial instruments to manage the financial risks facing the Group. Such instruments are only used if they relate to an underlying exposure; speculative transactions are expressly forbidden under the BAT Group's treasury policy. The Group's treasury position is monitored by the BAT Group Corporate Finance Committee ('CFC'), which meets regularly and is chaired by the British American Tobacco p.l.c. Finance Director. Regular reports are provided to senior management and treasury operations are subject to periodic independent reviews and audits, both internal and external.

### **Directors' indemnities**

Throughout the period from 1 January 2012 to the date of this report, an indemnity has been in force under which Mr J. B. Stevens, as a Director of the Company, is, to the extent permitted by law, indemnified by British American Tobacco p.l.c., the ultimate parent undertaking, in respect of all costs, charges, expenses or liabilities which he may incur in or about the execution of his duties to the Company or as a result of things done by him as a Director on behalf of the Company.

Throughout the period from 1 January 2012 to the date of this report, indemnities have been in force for each of the remaining Directors under which they, as Directors of the Company, are, to the extent permitted by law, indemnified in respect of all costs, charges, expenses or liabilities which they may incur in or about the execution of their duties to the Company or as a result of things done by them as Directors on behalf of the Company since their appointment.

### **Directors' responsibilities in relation to the financial statements**

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 prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, and the Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). 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 Group and the Company and of the profit or loss of the Group for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether IFRSs as adopted by the European Union and applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Group and Company financial statements respectively; 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 the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

### **Directors' declaration in relation to relevant audit information**

Having made enquiries of fellow Directors and of the Company's auditors, each of the Directors confirms that:

- to the best of his knowledge and belief, there is no relevant audit information of which the Company's auditors are unaware; and
- he has taken all steps that a Director might reasonably be expected to have taken in order to make himself aware of relevant audit information and to establish that the Company's auditors are aware of that information.

### **Directors' responsibilities statement**

The Directors confirm to the best of their knowledge and belief that:

- the financial statements, prepared in accordance with the applicable accounting standards identified above, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and Company; and
- the Directors' Report includes a fair review of the development and performance of the business and the position of the Group and the Company, together with a description of the principal risks and uncertainties that they face.

## Directors' Report continued

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The names of the Directors are listed in this Directors' Report on page 2. Neither the Company nor the Directors accept any liability to any person in relation to this Annual Report except to the extent that such liability could arise under English law. Accordingly, any liability to a person who has demonstrated reliance on any untrue or misleading statement or omission shall be determined in accordance with section 90A of the Financial Services and Markets Act 2000.

### **Auditors**

A resolution to reappoint PricewaterhouseCoopers LLP as auditors to the Company will be proposed at the Annual General Meeting.

### **Going concern**

After reviewing the Group's annual budget and plans, the Directors consider that the Group and Company have adequate resources to continue in operational existence for the foreseeable future and that it is therefore appropriate to continue to adopt the going concern basis in preparing the financial statements.

By Order of the Board



C.J. McAllister, Director  
3 April 2013

B.A.T. International Finance p.l.c.  
Registered Number 1060930

## Group Income Statement for the year ended 31 December

	2012	2011
	£m	£m
Interest income (note 3)	575	504
Interest expense (note 4)	(424)	(499)
Net fee income (note 5)	1	3
Net fair value gains on derivatives and exchange differences (note 6)	<u>17</u>	<u>84</u>
<b>Net finance income</b>	<b>169</b>	<b>92</b>
Other operating expenses (note 7)	<u>(1)</u>	<u>(1)</u>
<b>Profit before taxation</b>	<b>168</b>	<b>91</b>
Taxation on ordinary activities (note 8)	<u>(4)</u>	<u>(8)</u>
<b>Profit for the year</b>	<b><u>164</u></b>	<b><u>83</u></b>

All the activities during both years are in respect of continuing operations.

The accompanying notes are an integral part of the Group financial statements.

## Group Statement of Comprehensive Income for the year ended 31 December

	2012	2011
	£m	£m
<b>Profit for the year</b>	<b>164</b>	<b>83</b>
<b>Other comprehensive income</b>		
Differences on exchange	<b>(43)</b>	<b>18</b>
Cash flow hedges		
- net fair value (losses)		(2)
- reclassified and reported in profit for the year	<b>1</b>	<b>1</b>
Net investment hedges		
- foreign exchange gains on forward exchange contracts	<b>10</b>	
- differences on exchange on borrowings	<u><b>3</b></u>	<u><b>(3)</b></u>
Total other comprehensive income for the year	<u><b>(29)</b></u>	<u><b>14</b></u>
<b>Total comprehensive income for the year</b>	<b><u>135</u></b>	<b><u>97</u></b>

The accompanying notes are an integral part of the Group financial statements.

## Group Statement of Changes in Equity for the year ended 31 December

	Share capital £m	Hedging reserve £m	Translation reserve £m	Retained earnings £m	2012 Total equity £m
Balance at 1 January 2012	231	(2)	220	765	1,214
Total comprehensive income for the year (page 5)		1	(30)	164	135
<b>Balance at 31 December 2012</b>	<b>231</b>	<b>(1)</b>	<b>190</b>	<b>929</b>	<b>1,349</b>
					2011
	Share capital £m	Hedging reserve £m	Translation reserve £m	Retained earnings £m	Total Equity £m
Balance at 1 January 2011	231	(1)	205	682	1,117
Total comprehensive income for the year (page 5)		(1)	15	83	97
Balance at 31 December 2011	231	(2)	220	765	1,214


The accompanying notes are an integral part of the Group financial statements.

## Group Balance Sheet at 31 December

	2012 £m	2011 £m
<i>Assets</i>		
Cash and cash equivalents (note 9)	509	641
Amounts due on demand from fellow subsidiaries (note 10)	799	433
Derivative financial instruments (note 11)	485	513
Other receivables (note 13)	12	13
Loans due from parent undertaking (note 14a)	3,633	3,630
Loans due from fellow subsidiaries (note 14b)	21,478	17,692
<b>Total assets</b>	<b>26,916</b>	<b>22,922</b>
<i>Liabilities</i>		
Bank overdrafts (note 15)	86	94
Amounts repayable on demand to parent undertaking (note 16a)	7,750	6,348
Amounts repayable on demand to fellow subsidiaries (note 16b)	9,344	6,354
Derivative financial instruments (note 11)	392	389
Other payables (note 17)	2	15
Term deposits repayable to fellow subsidiaries (note 18)	1,211	2,505
Issued debt (note 15)	6,782	6,003
<b>Total liabilities</b>	<b>25,567</b>	<b>21,708</b>
<i>Equity</i>		
Share capital (note 19)	231	231
Hedging reserve (note 19)	(1)	(2)
Translation reserve (note 19)	190	220
Retained earnings (note 19)	929	765
<b>Total equity</b>	<b>1,349</b>	<b>1,214</b>
<b>Total equity and liabilities</b>	<b>26,916</b>	<b>22,922</b>

The accompanying notes are an integral part of the Group financial statements.

On behalf of the Board



J.B. Stevens  
3 April 2013



## Group Cash Flow Statement for the year ended 31 December 2012

	2012 £m	2011 £m
<i>Cash flows from operating activities</i>		
Interest receipts	138	248
Interest payments	(368)	(375)
Net inflow on fees	4	6
Other (payments)/ receipts	(5)	1
	<b>(231)</b>	<b>(120)</b>
<i>(Decrease / Increase in operating assets and liabilities:</i>		
Net short-term funds (outflow) from fellow subsidiaries and parent undertaking	(1,771)	(506)
Proceeds from external debt	1,272	594
Repayment of external debt	(332)	(567)
Movements relating to derivative financial instruments	79	162
Net cash inflow on loans to fellow subsidiaries	2,244	48
Net cash (outflow)/ inflow on borrowings from fellow subsidiaries	(1,346)	251
Net cash outflow from operating activities	(85)	(138)
Differences on exchange	(39)	44
<b>Net decrease in cash and cash equivalents</b>	<b>(124)</b>	<b>(94)</b>
<b>Net cash and cash equivalents at 1 January</b>	<b>547</b>	<b>641</b>
<b>Net cash and cash equivalents at 31 December (note 9)</b>	<b>423</b>	<b>547</b>

The accompanying notes are an integral part of the Group financial statements.

Notes are shown on pages 9 to 33.

## Group Notes on the Accounts

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### 1. Accounting policies

#### **Basis of accounting**

The Group financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The financial statements have been prepared under the historical cost convention except as described in the accounting policy below on financial instruments. The presentation of the Group balance sheet is based on liquidity.

None of the new and amended IFRSs and IFRIC interpretations adopted by the Group with effect from 1 January 2012 had any significant effect on reported profit or equity or on the disclosures in the financial statements.

The preparation of the Group financial statements requires management to make estimates and assumptions that affect the reported amounts of income, expenses, assets and liabilities, and the disclosure of contingent liabilities at the date of the financial statements. The key estimates and assumptions relate to calculation of fair value assets and liabilities using exchange rates and market expectations of future interest rates as at the balance sheet date. These are set out in the accounting policies below, together with the related notes to the accounts.

#### **Basis of consolidation**

The consolidated financial information includes the financial statements of B.A.T. International Finance p.l.c. and its subsidiary undertakings.

A subsidiary is an entity controlled by the Group, where control is the power to govern the financial and operating policies of the entity so as to obtain benefit from its activities.

Intercompany balances and transactions, and any unrealised gains arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

As permitted by section 408(3) of the Companies Act 2006, the Company individual Profit and loss account and related notes have not been included in these financial statements. The Company profit was **£668 million** (2011: £25 million).

#### **Foreign currencies**

The functional currency of the Company is sterling and this is also the presentation currency of the Group.

The income and cash flow statements of Group undertakings expressed in currencies other than sterling are translated to sterling at average rates of exchange in each year provided that the average rate approximates the exchange rate at the date of the underlying transactions. Assets and liabilities of Group undertakings are translated at rates of exchange at the end of each year.

The differences between retained profits of foreign currency subsidiary undertakings translated at average and closing rates of exchange are taken to reserves, as are differences arising on the retranslation to sterling (using closing rates of exchange) of foreign currency net assets at the beginning of the year. Any differences that have arisen since 1 January 2004 are presented as a separate component of equity. As permitted under IFRS 1, any differences prior to that date are not included in this separate component of equity. Where a disposal of an investment in a Group undertaking results in a loss of control of a subsidiary undertaking, the cumulative amount of the related foreign exchange differences deferred in the separate component of equity are recognised in the income statement when the gain or loss on disposal is recognised. These related exchange differences comprise the exchange differences on all amounts deemed to be part of the net investment in the undertaking, which are recycled to the income statement when a disposal occurs.

Foreign currency transactions are initially recognised in the functional currency of each entity in the Group at the exchange rate ruling at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of foreign currency assets and liabilities at year end rates of exchange are recognised in the income statement, except when deferred as qualifying cash flow hedges in the hedging reserve, on intercompany net investment loans and qualifying net investment hedges in the translation reserve.

#### **Accounting for income**

As a financing vehicle, the Group's primary sources of income comprise interest on loans to fellow subsidiaries and net fee income. These are recognised on an effective interest rate method, and all income is only recognised to the extent that it is considered to be collectable.

Net fee income comprises commitment fees received in respect of undrawn revolving credit facilities provided to fellow subsidiaries, and commitment fees paid in respect of revolving credit facilities provided by external banks.

## Group Notes on the Accounts

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### 1. Accounting policies continued

#### Taxation

Taxation is that chargeable on the profits for the period, together with deferred taxation.

The current income tax charge is calculated on the basis of tax laws enacted or substantially enacted at the balance sheet date in the countries where the Group operates and generates taxable income.

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more taxation in the future or a right to pay less taxation in the future have occurred at the balance sheet date.

A net deferred taxation asset is recognised as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which to recover carried forward taxation losses and from which the future reversal of underlying timing differences can be deducted.

Deferred taxation is measured at the average taxation rates that are expected to apply in the periods in which the timing differences are expected to reverse based on taxation rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred taxation is measured on an undiscounted basis.

Tax is recognised in the income statement except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case it is recognised in other comprehensive income or changes in equity.

#### Financial instruments

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the relevant instrument and derecognised when it ceases to be a party to such provisions.

Financial assets and financial liabilities are initially recognised at fair value, plus directly attributable transaction costs where applicable, with subsequent measurement as set out below.

Non-derivative financial assets are classified on initial recognition as either loans and receivables or cash and cash equivalents as follows:

- Loans and receivables: these are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market; and
- Cash and cash equivalents: cash and cash equivalents include cash in hand and deposits held on call, together with other short-term highly liquid investments including investments in certain money market funds. Cash equivalents normally comprise instruments with maturities of three months or less at date of acquisition. In the cash flow statement, cash and cash equivalents are shown net of bank overdrafts, which are shown as a separate category in the liabilities section on the Balance Sheet.

Non-derivative financial assets are stated at amortised cost using the effective interest method, subject to reduction for allowances for estimated irrecoverable amounts. These estimates for irrecoverable amounts are recognised when there is objective evidence that the full amount receivable will not be collected according to the original terms of the asset. Such evidence might include financial difficulties of the counterparty, defaults of payment or significant overdue balances. For interest-bearing assets, their carrying value includes accrued interest receivable.

Non-derivative financial liabilities are stated at amortised cost using the effective interest method. For borrowings, their carrying value includes accrued interest payable, as well as unamortised issue costs.

Derivative financial assets and liabilities are initially recognised, and subsequently measured, at fair value, which includes accrued interest receivable and payable where relevant. Changes in their fair values are recognised as follows:

- For derivatives that are designated as cash flow hedges, the changes in their fair values are recognised directly in other comprehensive income, to the extent that they are effective, with the ineffective portion being recognised in the income statement. The accumulated gains and losses are reclassified to the income statement in the same period as the hedged item;

## Group Notes on the Accounts

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### 1. Accounting policies continued

#### Financial instruments continued

- For derivatives that are designated as fair value hedges, the carrying value of the hedged item is adjusted for the fair value changes attributable to the risk being hedged, with the corresponding entry being made in the income statement. The changes in fair value of these derivatives are also recognised in the income statement;
- For derivatives that are designated as hedges of net investments in foreign currency operations, the changes in their fair values are recognised directly in other comprehensive income, to the extent that they are effective, with the ineffective portion being recognised in the income statement. Where non-derivatives such as foreign currency borrowings are designated as net investment hedges, the relevant exchange differences are similarly recognised. The accumulated gains and losses are recognised in the income statement when the foreign currency operation is disposed of; and
- For derivatives that do not qualify for hedge accounting or are not designated as hedges, the changes in their fair values are recognised in the income statement in the period in which they arise.

In order to qualify for hedge accounting, the Group is required to document prospectively the relationship between the item being hedged and the hedging instrument. The Group is also required to demonstrate an assessment of the relationship between the hedged item and the hedging instrument, which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at each reporting date to ensure that the hedge has remained, and is expected to remain, highly effective.

Hedge accounting is discontinued when a hedging instrument is derecognised (e.g. through expiry or disposal) or no longer qualifies for hedge accounting. Where the hedged item is a highly probable forecast transaction, the related gains and losses remain in equity until the transaction takes place, when they are reclassified to the income statement in the same manner as for cash flow hedges as described above. When a hedged future transaction is no longer expected to occur, any related gains and losses, previously recognised in other comprehensive income, are immediately reclassified to the income statement.

#### Segmental analysis

Senior management of the BAT Group Treasury function, including the BAT Group Treasurer, who is also a Director of the Company, are identified as the chief operating decision maker (CODM), and are responsible for managing within an overall policy framework, the BAT Group's exposure to funding and liquidity, interest rate, foreign exchange and counterparty risks. The Group is the central vehicle used by BAT Group Treasury for managing these risks. The Group does not report segment information internally as the Group is managed by senior management of the BAT Group Treasury function as a single segment entity in the context of the BAT Group as a whole.

The prices agreed between Group companies, and with BAT Group entities, for intra-BAT Group loans and borrowings, and charges for such are based on normal commercial practices which would apply between independent businesses.

#### Dividends

Dividend distributions are recognised as a liability in the financial statements in the period in which the dividends are paid.

#### Future changes to Group accounting policies

Certain changes to IFRS will be applicable for the Group financial statements in future years. Set out below are those which are considered to affect the Group.

IFRS 9 Financial Instruments has been issued. This standard represented the first phase of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement, and has mandatory application for accounting periods beginning on or after 1 January 2015. In its current form, it sets out the classification and measurement criteria for financial assets and financial liabilities. It requires all financial assets, including assets currently classified under IAS 39 as available-for-sale, to be measured at fair value through profit and loss unless the assets can be classified as held at amortised cost. Qualifying equity investments held at fair value may have their fair value changes taken through other comprehensive income by election. Where the fair value option for certain financial liabilities is applied, the portion of fair value changes representing own credit risk would be recognised through other comprehensive income rather than the income statement. The Group does not use the fair value option for financial liabilities. The effect of applying the standard in its current form is not considered to have a material impact on the Group's reported profit or equity. The impact on the Group of further changes to IFRS 9 and the impact of the second and third phases of the project, covering impairment and hedge accounting respectively, will be assessed when the IASB has finalised the proposed requirements. IFRS 9 has not been endorsed by the EU and will only become applicable once that endorsement has occurred.

## Group Notes on the Accounts

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### 1. Accounting policies continued

#### Future changes to Group accounting policies continued

IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities have been issued along with revised versions of IAS 27 Separate Financial Statements and IAS 28 Associates; additionally IAS 31 Joint Ventures has been withdrawn. These standards form a single package of proposals with mandatory application in the EU from 1 January 2014. The aim of these standards is to improve the quality of reporting in relation to the consolidation of subsidiaries, special purpose vehicles and accounting for joint arrangements. The Group intends to early adopt these new and revised standards with effect from 1 January 2013. While the requirements of IFRS 12 will potentially lengthen certain disclosures in respect of Group entities, the requirements of these standards are not expected to materially affect the Group in its present form.

An amendment to IAS 1 Presentation of Financial Statements has been issued. This amendment changes the disclosure of items presented in other comprehensive income grouping them into items which recycle to profit and loss and items which will not. Apart from the change in disclosure, this amendment will have little impact on the Group financial statements. Mandatory application is for accounting periods beginning on or after 1 July 2012.

IFRS 13 Fair Value Measurement has been issued. This standard aims to provide a single source of fair value measurement and disclosure requirements for use across IFRS. The implementation of IFRS 13 does not change where fair value is or is not applied under IFRS and will not require a restatement of historical transactions. Mandatory application is from 1 January 2013.

In addition, a number of other interpretations and revisions to existing standards have been issued which will be applicable to the Group financial statements in future years and which will have no material effect on reported profit or equity or on the disclosures in the financial statements.

## Group Notes on the Accounts

### 2. Segmental reporting

As the Company is the central financing vehicle for the BAT Group and is domiciled in the UK, all income other than interest on cash and cash equivalents is earned from counterparties within the BAT Group. Interest on cash and cash equivalents of **£1 million** (2011: £4 million) comprises **£0.5 million** (2011: £3 million) from money market funds and **£0.5 million** (2011: £1 million) from bank current accounts.

Interest income from cash and cash equivalents attributable to the UK is **£1 million** (2011: £4 million) and **£nil** (2011: £nil) attributable to foreign countries.

IFRS 8 considers a group of entities under common control as a single customer. **£84 million** (2011: £65 million) of interest income is generated from the parent undertaking and **£490 million** (2011: £435 million) from fellow subsidiaries controlled directly or indirectly by the parent undertaking, British American Tobacco p.l.c.

### 3. Interest income

	2012 £m	2011 £m
Interest income		
From the parent undertaking	84	65
From fellow subsidiaries	490	435
Cash and cash equivalents	1	4
	<u>575</u>	<u>504</u>

### 4. Interest expense

	2012 £m	2011 £m
Interest expense		
Commercial paper	3	4
Bank borrowings	5	3
Issued debt	351	347
	<u>359</u>	<u>354</u>
To the parent undertaking	18	9
To fellow subsidiaries	47	136
	<u>424</u>	<u>499</u>

### 5. Net fee income

	2012 £m	2011 £m
Fee income		
Commitment fees on undrawn revolving credit facilities to fellow subsidiaries	6	8
Fee expense		
Fees charged on committed borrowing facilities	(5)	(5)
	<u>1</u>	<u>3</u>

Two-thirds of the fees charged on the committed borrowing facility in 2012 and 2011 are borne by the Group, with one-third being borne by fellow subsidiaries.

### 6. Net fair value gains on derivatives and exchange differences

	2012 £m	2011 £m
Fair value changes on derivatives comprise:		
Cash flow hedges transferred from equity	(1)	(1)
Fair value hedging instruments – exchange related movements	(15)	(15)
Fair value hedging instruments – net interest income	41	41
Fair value hedging instruments – interest related movements	23	33
Fair value changes on hedged items	(34)	
Instruments held-for-trading	(14)	5
Net fair value gains on derivatives	<u>17</u>	<u>63</u>
Exchange differences	17	21
	<u>17</u>	<u>84</u>

## Group Notes on the Accounts

### 6. Net fair value gains on derivatives and exchange differences continued

Included within exchange differences above is a gain of **£15 million** (2011: £15 million) in respect of items subject to fair value hedges and **£nil** gain (2011: £1 million gain) in respect of items subject to cash flow hedges.

The net gains on fair value of derivatives and exchange differences of **£17 million** (2011: £84 million) include a loss of **£11 million** (2011: £12 million gain) due to the ineffective portion of fair value hedges and **£nil** (2011: £21 million gain) from the release of fair value basis adjustments to debt.

Most foreign currency assets and liabilities are maintained in US dollars and euros, which have been translated to sterling at the closing rates on 31 December 2012 of **US\$1.6255** and **€1.2329** (2011: US\$1.55410 and €1.19720).

### 7. Other operating expenses and employee information

	2012 £m	2011 £m
Other operating expenses	<u>1</u>	<u>1</u>

Other operating charges include remuneration of **£191,000** (2011: £136,000) payable to the Company's auditors for the audit of the Group and Company annual financial statements and **£170,000** (2011: £25,000) for the supply of other assurance services to the Company (of which **£140,000** has been capitalised).

The Group has no directly employed employees (2011: nil) and consequently utilises the services of a number of employees whose contracts of service are with fellow subsidiaries, and their remuneration is included in the financial statements of these subsidiaries. An annual management charge is levied from two of these fellow subsidiaries in respect of the cost of employees in the Asia Pacific Treasury Service Centre (Singapore), and in the British American Shared Service Centre (Romania). These charges are included in 'other operating charges' above.

### 8. Taxation on ordinary activities

#### a) Summary of tax

	2012 £m	2011 £m
UK corporation tax		
Comprising:		
- current tax at <b>24.5%</b> (2011: 26.5%)	4	8
- double tax relief	(4)	(8)
Overseas tax comprising:		
- tax on current income	<u>4</u>	<u>8</u>
Total current tax expense ( <i>note 8b</i> )	<u>4</u>	<u>8</u>

The Group has not recognised deferred tax assets in respect of deductible temporary differences of **£2 million** (2011: £4 million).

## Group Notes on the Accounts

### 8. Taxation on ordinary activities continued

#### b) Factors affecting the tax charge

The standard rate of corporation taxation in the UK changed from 26.0 per cent to 24.0 per cent with effect from 1 April 2012. Accordingly the Company's profit for this accounting period is taxed at an effective rate of 24.5 per cent. The taxation charge differs from the standard 24.5 per cent rate of corporation tax in the UK. The major causes of this difference are listed below:

	2012 £m	2011 £m
Profit before taxation	168	91
UK corporation tax at <b>24.5%</b> (2011: 26.5%)	<u>41</u>	<u>24</u>
<b>Factors affecting the tax rate:</b>		
Temporary timing differences	(2)	(1)
Overseas taxation	4	8
Double tax relief	(4)	(8)
BAT Group loss relief claimed for no consideration	<u>(35)</u>	<u>(15)</u>
Total current tax expense ( <i>note 8a</i> )	<u>4</u>	<u>8</u>

### 9. Cash and cash equivalents

	2012 £m	2011 £m
Cash and bank balances	75	62
Cash equivalents	<u>434</u>	<u>579</u>
	<u>509</u>	<u>641</u>

Cash equivalents comprise short-term deposits and investments in money market funds with an original maturity of three months or less. The carrying value of cash and cash equivalents approximates their fair value.

As part of its short-term cash management, the Company invests in a range of cash and cash equivalents, including money market funds, which are regarded as highly liquid and are not exposed to significant changes in fair value. These are kept under continuous review as described in the credit risk section below. At 31 December 2012, cash and cash equivalents include **£434 million** invested in money market funds (2011: £558 million).

The currency in which cash and cash equivalents are held, are as follows:

	2012 £m	2011 £m
US dollar	434	549
UK sterling		30
Euro		9
Australian dollar	33	21
Romanian Leu	25	
Other	<u>17</u>	<u>32</u>
	<u>509</u>	<u>641</u>



## Group Notes on the Accounts

### 9. Cash and cash equivalents continued

In the Group cash flow statement, net cash and cash equivalents are shown after deducting bank overdrafts (note 15) and accrued interest, where applicable:

	2012	2011
	£m	£m
Cash and cash equivalents as above	509	641
Less: bank overdrafts	(86)	(94)
Net cash and cash equivalents	423	547

### 10. Amounts due on demand from fellow subsidiaries

Amounts due on demand from fellow subsidiaries comprise unsecured current accounts and cash pooling accounts referred to as In House Cash accounts (IHC) between fellow subsidiaries and the Group. These are denominated in the following currencies:

	2012	2011
	£m	£m
UK sterling	35	182
US dollar	33	25
Swiss franc	27	24
Hong Kong Dollar	109	
Euro	461	180
Singapore Dollar	73	
Other	61	22
	799	433

Amounts due on demand from fellow subsidiaries include amounts of £nil (2011: £0.3 million) of interest receivable. There is no material difference between the book value and fair value for amounts due on demand from fellow subsidiaries.

### 11. Derivative financial instruments

The fair values of derivatives are determined based on market data (primarily yield curves and exchange rates) to calculate the present value of all estimated flows associated with each derivative at the balance sheet date. In the absence of sufficient market data, fair values would be based on the quoted market price of similar derivatives. The classification of these assets and liabilities under the IFRS 7 fair value hierarchy is given in note 12.

	2012		2011	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Fair value hedges				
Interest rate swaps	122		133	
Cross-currency swaps	10		6	12
Held-for-trading*				
Cross-currency swaps	12	12	30	30
Interest rate swaps	142	142	76	76
Forward foreign currency contracts	199	237	259	268
Others		1	9	3
	485	392	513	389

All balances above relate to derivatives with external parties other than those disclosed in note 21.

\* Some derivative financial instruments are not designated as hedges and are required to be classified as held-for-trading.

## Group Notes on the Accounts

### 11. Derivative financial instruments continued

The maturity dates of all derivative financial instruments as recognised in the balance sheet are as follows:

	2012		2011	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Within one year	209	187	265	248
Between one and two years	61	28	53	45
Between two and three years			43	1
Between three and four years	17	17		
Between four and five years	45	83	35	30
Beyond five years	153	77	117	65
	<b>485</b>	<b>392</b>	<b>513</b>	<b>389</b>

Derivative liabilities above include certain interest rate swaps and cross-currency swaps maturing in 2016 and 2017 with a combined fair value of **£50 million**, where the contracting parties hold the right to exercise mutual break-up clauses on 29 June 2015, 7 July 2015, and 15 March 2016.

The tables below set out the maturities of the Group's derivative financial instruments on an undiscounted contractual basis, based on spot rates.

The maturity dates of all gross-settled derivative financial instruments are as follows:

	2012			
	Assets		Liabilities	
	Inflow £m	Outflow £m	Inflow £m	Outflow £m
Within one year				
- Cross-currency swaps	22	(29)	18	(4)
- Forward foreign exchange contracts	7,567	(7,388)	5,806	(5,979)
Between one and two years				
- Cross-currency swaps	22	(29)	18	(4)
- Forward foreign exchange contracts	619	(594)	760	(783)
Between two and three years				
- Cross-currency swaps	24	(31)	18	(6)
Between three and four years				
- Cross-currency swaps	407	(357)	343	(389)
Between four and five years				
- Cross-currency swaps	18	(16)		
Beyond five years				
- Cross-currency swaps	575	(616)		
- Forward foreign exchange contracts			1,379	(1,452)
	<b>9,254</b>	<b>(9,060)</b>	<b>8,342</b>	<b>(8,617)</b>

## Group Notes on the Accounts

### 11. Derivative financial instruments continued

	2011			
	Assets		Liabilities	
	Inflow £m	Outflow £m	Inflow £m	Outflow £m
Within one year				
- Cross-currency swaps	8	(18)	36	(20)
- Forward foreign exchange contracts	7,805	(7,573)	8,663	(8,900)
- Other	1,188	(1,175)		
Between one and two years				
- Cross-currency swaps	7	(18)	36	(19)
- Forward foreign exchange contracts	657	(630)	630	(657)
Between two and three years				
- Cross-currency swaps	11	(18)	36	(26)
- Forward foreign exchange contracts	60	(61)	61	(60)
Between three and four years				
- Cross-currency swaps	12	(18)	36	(27)
Between four and five years				
- Cross-currency swaps	406	(343)	361	(422)
Beyond five years				
- Cross-currency swaps	19	(15)	592	(634)
	<u>10,173</u>	<u>(9,869)</u>	<u>10,451</u>	<u>(10,765)</u>

The maturity dates of net-settled derivative financial instruments are as follows:

	2012		2011	
	Assets	Liabilities	Assets	Liabilities
	Inflow/ (Outflow) £m	Inflow/ (Outflow) £m	Inflow/ (Outflow) £m	Inflow/ (Outflow) £m
Within one year	63	(12)	65	(27)
Between one and two years	63	(11)	66	(33)
Between two and three years	31	(6)	41	(14)
Between three and four years	24	(15)	17	(7)
Between four and five years	20	(12)	13	(5)
Beyond five years	17	(6)	17	2
	<u>218</u>	<u>62</u>	<u>219</u>	<u>(84)</u>

The above maturity analysis primarily comprises the Group's interest rate swaps.

## Group Notes on the Accounts

### 11. Derivative financial instruments continued

In summary by type, the fair values of derivative financial instruments are as follows:

	2012		2011	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Interest rate swaps	264	142	209	76
Cross-currency swaps	22	12	36	42
Forward foreign currency contracts	199	237	259	268
Other		1	9	3
	<b>485</b>	<b>392</b>	<b>513</b>	<b>389</b>

#### (a) Interest rate swaps

	Note	Maturity date	Principal Currency	m	£m	Interest rate		2012	
						Original	Swapped	Assets £m	Liabilities £m
Fixed – floating		2013	EUR	400	324	5.1	<i>Note (a)</i>	<b>14</b>	
	A	2013	GBP	150	150	5.8	<i>Note (a)</i>	<b>6</b>	
	A	2014	GBP	500	500	6.0	<i>Note (a)</i>	<b>26</b>	
	A	2014	GBP	250	250	6.0	<i>Note (a)</i>	<b>18</b>	
	A	2017	USD	600	369	2.1	<i>Note (a)</i>	<b>4</b>	
		2017	EUR	600	487	3.7	<i>Note (a)</i>	<b>45</b>	
	A	2019	GBP	250	250	6.4	<i>Note (a)</i>	<b>68</b>	
		2020	EUR	600	487	4.0	<i>Note (a)</i>	<b>65</b>	
		2023	EUR	750	608	2.4	<i>Note (a)</i>	<b>8</b>	
		2023	EUR	750	608	2.8	<i>Note (a)</i>	<b>10</b>	
Floating – fixed		2013	EUR	400	324	<i>Note (a)</i>	5.1		<b>14</b>
		2017	EUR	600	487	<i>Note (a)</i>	3.7		<b>45</b>
		2020	EUR	600	487	<i>Note (a)</i>	4.0		<b>65</b>
		2023*	EUR	750	608	<i>Note (a)</i>	2.8		<b>10</b>
		2023	EUR	750	608	<i>Note (a)</i>	2.4		<b>8</b>
									<b>264</b>

\* The €750 million euro interest rate swap maturing in 2023 has a start date of 2015.

	Note	Maturity date	Principal Currency	m	£m	Interest rate		2011	
						Original	Swapped	Assets £m	Liabilities £m
Fixed – floating	A	2012	EUR	337	289	3.6	<i>Note (a)</i>	7	
		2013	EUR	400	343	5.1	<i>Note (a)</i>	24	
	A	2013	GBP	150	150	5.8	<i>Note (a)</i>	11	
	A	2014	GBP	500	500	6.0	<i>Note (a)</i>	29	
	A	2014	GBP	250	250	6.0	<i>Note (a)</i>	22	
		2017	EUR	600	514	3.7	<i>Note (a)</i>	22	
	A	2019	GBP	250	250	6.4	<i>Note (a)</i>	64	
		2020	EUR	600	514	4.0	<i>Note (a)</i>	30	
Floating – fixed		2013	EUR	400	343	<i>Note (a)</i>	5.1		24
		2017	EUR	600	514	<i>Note (a)</i>	3.7		22
		2020	EUR	600	514	<i>Note (a)</i>	4.0		30
								<b>209</b>	<b>76</b>

*Note (a)*: The floating rate interest rates in 2012 and 2011 are based on LIBOR or EURIBOR plus a margin ranging between 35 and 268 basis points.

## Group Notes on the Accounts

### 11. Derivative financial instruments continued

In both 2012 and 2011, Swaps denoted with **A** were used to manage the interest rate profile of external borrowings and are reflected in the repricing table in note 15 on page 29. All other swaps were not designated as hedging instruments

#### (b) Cross-currency swaps

									2012	
	Note	Maturity date	Interest rate (%)	Original Currency (m)	Principal £m	Interest rate (%)	Swapped Currency (m)	Principal £m	Assets £m	Liabilities £m
Fixed – floating		2016	5.5	GBP 325	325	<i>Note (b)</i>	EUR 473	384		12
	B	2019	4.6	EUR 20	16	<i>Note (b)</i>	USD 22	12	7	
	B	2021	3.6	EUR 600	487	<i>Note (b)</i>	GBP 518	518	3	
Floating – fixed		2016	<i>Note (b)</i>	EUR 473	384	5.5	GBP 325	325	12	
										22
									2011	
	Note	Maturity date	Interest rate (%)	Original Currency (m)	Principal £m	Interest rate (%)	Swapped Currency m	Principal £m	Assets £m	Liabilities £m
Fixed – floating		2016	5.5	GBP 325	325	<i>Note (b)</i>	EUR 473	395		30
	B	2019	4.6	EUR 20	17	<i>Note (b)</i>	USD 22	14	6	
	B	2021	3.6	EUR 600	501	<i>Note (b)</i>	GBP 518	518		12
Floating – fixed		2016	<i>Note (b)</i>	EUR 473	395	5.5	GBP 325	325	30	
										36

*Note (b)*: The floating interest rates in 2012 and 2011 are based on LIBOR, EURIBOR, SOR or BBSW plus a margin ranging between 82 and 154 basis points (2011: 82 and 154 basis points).

In both 2012 and 2011 swaps denoted with **B** have been used to manage the interest rate profile of external borrowings) and are reflected in the repricing table in note 15 on page 29.

All other swaps have been entered into in order to manage the interest rate risk of debt held by fellow subsidiaries, and are therefore not reflected in the repricing table in note 15 on page 29.

## Group Notes on the Accounts

### 11. Derivative financial instruments continued

#### (c) Forward foreign currency contracts

Forward foreign currency contracts have been used to hedge both internal and external forecast transactions as well as the hedging of internal and external assets and liabilities

Forward foreign currency contracts are denominated in the following currencies:

	2012	2012	2011	2011
	Asset	Liability	Asset	Liability
	£m	£m	£m	£m
GBP/EUR	17	7	46	2
GBP/AUD	9	2		28
GBP/ZAR	2	1	19	4
GBP/CHF	10		12	2
GBP/USD	32		2	49
EUR/USD	23	1		27
EUR/GBP	6	58		30
EUR/PLN		7	9	
USD/EUR	3	24	28	
USD/GBP		29	40	2
USD/JPY	57		1	41
ZAR/GBP	1	1	4	19
Others	39	107	98	64
	<b>199</b>	<b>237</b>	<b>259</b>	<b>268</b>

Certain contracts were used to manage the currency profile of external borrowings and are reflected in the currency table in note 15 on page 29, and their nominal values are as follows:

	2012		2011	
	Sell	Purchase	Sell	Purchase
	£m	£m	£m	£m
Forward contracts to purchase GBP, sell CHF	221	(221)	86	(89)
Forward contracts to purchase GBP, sell AUD			1,121	(1,092)
Forward contracts to purchase GBP, sell CAD	287	(292)	294	(290)
Forward contracts to purchase GBP, sell USD			272	(268)
Forward contracts to purchase GBP, sell EUR	362	(362)		
Forward contracts to purchase EUR, sell DKK	344	(344)	390	(390)
Forward contracts to purchase EUR, sell NOK	166	(166)	162	(160)
Forward contracts to purchase EUR, sell SEK	131	(131)	130	(126)
Forward contracts to purchase EUR, sell GBP	1,452	(1,379)	77	(75)
Forward contracts to purchase NOK, sell GBP	164	(166)		

## Group Notes on the Accounts

### 11. Derivative financial instruments continued

#### (d) Others

	2012		2011	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Bund forwards (note i)			9	
Interest derivative (note ii)		1		3
		<u>1</u>	<u>9</u>	<u>3</u>

Notes:

- Forward contracts to purchase and sell German government securities with a nominal value of **€nil** (2011: €1.4 billion), taken out to manage the BAT Group's financing arrangements.
- Remaining impact of an interest derivative with a nominal value of €1 billion maturing in 2013.

### 12. Management of financial risks

One of the principal responsibilities of the Company is to manage the financial risks arising from the BAT Group's underlying operations. Specifically, Treasury manages, within an overall policy framework set by the BAT Group's Main Board and Corporate Finance Committee ('CFC'), the BAT Group's exposure to funding and liquidity, interest rate, foreign exchange and counterparty risks. The overall BATIF Group treasury position is monitored by the CFC which meets regularly throughout the year and is chaired by the BAT Group Finance Director.

Given the nature of the Group's activities, the Group is managed in accordance with BAT Group treasury policies and procedures. These policies and procedures include a set of financing principles including the monitoring of credit ratings, interest cover and liquidity. These provide a framework within which the Group's capital base is managed. The Group defines capital as equity (see note 19) and net debt which is defined as external borrowings, including derivatives in respect of debt, less cash and cash equivalents. The Group's net debt balances, which are managed as part of the BAT Group's net debt, are as follows:

	2012 £m	2011 £m
Borrowings - bank overdrafts and issued debt (note 15)	6,868	6,097
Derivatives in respect of debt:		
- Assets	(301)	(170)
- Liabilities	206	70
Cash and cash equivalents (note 9)	(509)	(641)
	<u>6,264</u>	<u>5,356</u>

The Group manages its financial risks in line with the classification of its financial assets and liabilities in the Group's balance sheet and related notes.

The Group's management of specific risks is dealt with as follows:

#### Liquidity risk

It is the policy of the Group to maximise financial flexibility and minimise refinancing risk by issuing debt with a range of maturities, generally matching the projected cash flows of the BAT Group, and to obtain this financing from a wide range of providers. The BAT Group has a target average centrally managed debt maturity of at least 5 years with no more than 20 per cent of centrally managed debt maturing in a single rolling year. The debt held by the Group is part of the BAT Group's centrally managed debt and is therefore not managed to separate targets. As at 31 December 2012, the average centrally managed debt maturity was **7.2 years** (2011: 7.0 years) and the highest proportion of centrally managed debt maturing in a single rolling year was **19.3 per cent** (2011: 18.3 per cent). As at 31 December 2012, the average debt to maturity of the Group was **7.9 years** (2011: 8.8 years) and the highest proportion of total issued debt maturing in a single rolling year was **21.1 per cent** (2011: 18.3 per cent). As noted the Group is part of the BAT Group's centrally managed debt and is therefore not managed to separate targets, therefore the 21.1 per cent does not breach 20 per cent of centrally managed debt rolling in one year.

At 31 December 2012 **£nil** of commercial paper was outstanding. (2011: £85 million).

In June 2012, the Group repaid a €337 million bond due in June 2012.

In June 2012, the Group issued new US\$2 billion bonds: US\$500 million with a maturity of June 2015; US\$600 million with a maturity of June 2017; and US\$900 million with a maturity of June 2022.

## Group Notes on the Accounts

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### 12. Management of financial risks continued

The Group ensures that there is flexibility in funding arrangements with fellow subsidiaries by providing short-term facilities or early prepayment rights. To ensure that the Group can maintain its liquidity at all times, the Group is a borrower under the BAT Group's central banking facility of £2 billion. The new central banking facility of £2 billion has a final maturity date of December 2015 and was undrawn at both 31 December 2012 and 31 December 2011.

In July 2012, the Group established a US\$150 million bilateral facility with Sumitomo Mitsui Banking Corporation which matures in 2017 and was undrawn as at 31 December 2012.

In June 2011, the Group established a US\$2 billion commercial paper programme. It is Group policy that short-term sources of funds (including drawings under both the US\$ programme and the existing Group £1 billion euro commercial paper (ECP) programme) are backed by undrawn committed lines of credit and cash.

As the Group is the principal central financing vehicle for the BAT Group, it is used to mobilise cash for the BAT Group through participation in cash pooling and zero balancing bank account structures with fellow subsidiaries.

As part of its short-term cash management, the Company invests in a range of cash and cash equivalents, including money market funds, which are regarded as highly liquid and are not exposed to significant changes in fair value. These are kept under continuous review as described in the credit risk section below. At 31 December 2012, cash and cash equivalents include **£434 million** (2011: £558 million) invested in money market funds.

Although term deposits repayable to fellow subsidiaries as shown in note 18 fall due within one year, they are typically renewed subject to the funding requirements of the counterparty. Loans to fellow subsidiaries, subsidiary companies and the parent undertaking are made on commercial terms. All contractual borrowing covenants have been met and none of them are expected to inhibit the Group's operations or funding plans.

#### Currency risk

The Group is subject to exposure on the translation of the net assets of foreign currency subsidiaries into its reporting currency, sterling. Lending and borrowing activity with fellow subsidiaries is usually in the currency of the counterparty resulting in primary balance sheet translation exposures to the US dollar, Euro, Canadian dollar, Australian dollar, Singapore dollar, Danish krone, Norwegian krone and Swedish krona. These exposures are kept under continuous review and the Group's policy is to minimise all balance sheet translation exposure where it is practicable and cost effective to do so through matching of currency assets with currency borrowings. At 31 December 2012, the currency profile of the Group's gross issued debt, after taking into account derivative contracts, was **27 per cent** (2011: 16 per cent) US dollar, **7 per cent** (2011: 29 per cent) euro, **52 per cent** (2011: 19 per cent) sterling, **4 per cent** (2011: 5 per cent) Canadian dollar, **nil per cent** Australian dollar (2011: 19 per cent), **5 per cent** Danish krone (2011: 6 per cent), and **5 per cent** (2011: 6 per cent) other currencies.

The Group faces currency exposures arising from the translation of profits earned in foreign currency subsidiaries; these exposures are not normally hedged.



## Group Notes on the Accounts

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### 12. Management of financial risks continued

#### Currency risk continued

IFRS 7 requires a sensitivity analysis that shows the impact on the income statement and on items recognised directly in equity of hypothetical changes of exchange rates in respect of non-functional currency financial assets and liabilities held by the Group. All other variables are held constant although, in practice, market rates rarely change in isolation. All financial assets and liabilities held in the functional currency of the Group's subsidiaries, as well as non-financial assets and liabilities and translation risk, are not included in the analysis. The Group considers a 10 per cent strengthening or weakening of the functional currency against the non-functional currency of its subsidiaries as a reasonably possible change. The impact is calculated with reference to the financial asset or liability held as at the year end, unless this is unrepresentative of the position during the year.

A 10 per cent strengthening of functional currencies against non-functional currencies would result in pre-tax profit being **£7 million** lower (2011: no material change). A 10 per cent weakening of functional currencies against non-functional currencies would result in pre-tax profit being **£8 million** higher (2011: no material change).

A 10 per cent change in exchange rates would have no impact on items recognised directly in other comprehensive income for the current and prior year.

The currency sensitivity of pre-tax profit is principally due to the impact from forward foreign currency contracts hedging forecast dividend cash flows from fellow subsidiaries on behalf of British American Tobacco p.l.c. These contracts provide cash flow certainty and are designated as net investment hedges in the Group financial statements of British American Tobacco p.l.c. As the Group does not have the underlying investments, the contracts are not designated as hedges in these financial statements and changes in their fair value are recognised through the income statement.

Excluding the impact of these contracts, a 10 per cent strengthening of functional currencies against non-functional currencies would result in pre-tax profit being **£3 million** lower (2011: no material change). A 10 per cent weakening of functional currencies against non-functional currencies would result in pre-tax profit being **£3 million** higher (2011: no material change).

A 10 per cent change in exchange rates would have no impact on items recognised directly in other comprehensive income for the current and prior year

#### Interest rate risk

The objectives of the Group's interest rate risk management policy are to lessen the impact of adverse interest rate movements on earnings, cash flow and economic value of the Group and to safeguard against any possible breach of its financial covenants. Additional objectives are to minimise the cost of hedging and the associated counterparty risk.

## Group Notes on the Accounts

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### 12. Management of financial risks continued

#### Interest rate risk continued

The BAT Group has an externally imposed capital requirement in respect of its centrally managed banking facilities, which requires a gross interest cover of 4.5 times. Although the Company is a joint borrower under these central banking facilities, the requirement is based on the audited group financial statements of British American Tobacco p.l.c.

In order to manage its interest rate risk, the Group maintains both floating rate and fixed rate debt. The Group's ratio of fixed to floating rate debt forms part of overall BAT Group debt for which targets are set for the desired ratio of floating to fixed rate debt on both a gross basis and net basis (at least 50 per cent fixed on a net basis in the short to the medium-term) as a result of regular reviews of market conditions and strategy by the CFC and the Board of the Company. At 31 December 2012, the relevant ratios of floating to fixed rate external borrowings were **37:63** (2011: 31:69) on a gross basis and **29:71** (2011: 21:79) on a net basis. Underlying borrowings are arranged on both a fixed rate and a floating rate basis and, where appropriate, the Group uses derivatives, primarily interest rate swaps, to vary the fixed and floating mix. The interest rate profile of liquid assets is taken into account in determining the net interest rate exposure.

IFRS 7 requires a sensitivity analysis that shows the impact on the income statement and on items recognised directly in other comprehensive income of hypothetical changes of interest rates in respect of interest-bearing financial assets and financial liabilities of the Group. All other variables are held constant although, in practice, market rates rarely change in isolation. For the purposes of this sensitivity analyses, financial assets and liabilities with fixed interest rates are not included. The Group considers a 100 basis point change in interest rates as a reasonably possible change except where rates are less than 100 basis points. In these instances it is assumed that the interest rates increase by 100 basis points and decrease to zero for the purpose of performing the sensitivity analysis. The impact is calculated with reference to the financial asset or liability held as at the year end, unless this is unrepresentative of the position during the year.

A 100 basis point increase in interest rates would result in pre-tax profit being **£35 million** higher (2011: £36 million higher). A 100 basis point decrease in interest rates, or less where applicable, would result in pre-tax profit being **£110 million** lower (2011: £57 million lower).

A 100 basis point change in interest rates would have no impact on items recognised directly in other comprehensive income for the current and prior year.

#### Credit risk

The Group has no significant concentrations of counterparty credit risk in respect of its external financial assets. As the central financing vehicle for the BAT Group, concentrations of credit risk arise from financial assets due from fellow subsidiaries and the parent undertaking. All loans to fellow subsidiaries, subsidiary companies and the parent are priced on an arm's length basis. To determine the appropriate risk premium, the Group consults, where appropriate, with independent financial institutions who assess the asset base and sovereign risk specific to the relevant counterparty.

Intercompany counterparties have appropriate capital structures to meet their obligations as they fall due. All loans to fellow subsidiaries, subsidiary companies and the parent undertaking are therefore between parties which have been individually reviewed and are considered to be in a position to continue to meet their obligations. The Group recognises that the sovereign risk of a fellow subsidiary can be the determining factor of default.

All external derivatives are subject to ISDA documentation.

## Group Notes on the Accounts

### 12. Management of financial risks continued

#### Credit risk continued

Cash deposits and other financial instruments give rise to credit risk on the amounts due from the related counterparties. Generally, the Group targets a long term counterparty credit rating of at least A-/A3. From time to time, the Group may invest in short dated corporate commercial paper. For this, the Group has identified specific counterparties with a minimum short-term rating of A1/P1.

External counterparty credit risk is managed on a global basis by limiting the aggregate amount and duration of exposure to any one counterparty, taking into account its credit rating. The credit ratings of bank counterparties are reviewed regularly. The Group ensures that it has sufficient counterparty credit capacity of requisite quality to undertake all anticipated transactions.

The maximum exposure to credit risk of financial assets at the balance sheet date is reflected by the carrying values included in the Group balance sheet. In addition, the Group provides committed credit facilities to certain fellow subsidiaries. The undrawn portion of these committed facilities at 31 December 2012 is **£720 million** (2011: £508 million). Guarantees provided to third parties are shown in note 20 on page 32.

#### Price risk

At 31 December 2012 and 31 December 2011, the Group's financial instruments are not sensitive to price risk.

#### Hedge accounting

In order to qualify for hedge accounting, the Group is required to document prospectively the relationship between the item being hedged and the hedging instrument. The Group is also required to demonstrate an assessment of the relationship between the hedged item and the hedging instrument, which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed periodically to ensure that the hedge has remained and is expected to remain highly effective.

#### Fair value estimation

The fair values of financial assets and liabilities with maturities of less than one year, other than derivatives, are assumed to approximate their book values. For other financial instruments which are measured at fair value in the balance sheet, the basis for fair values is described below.

#### Fair value hierarchy

In accordance with the IFRS 7 classification hierarchy all derivatives held by the Group at 31 December 2012 and 31 December 2011, fall within Level 2. Level 2 financial instruments are not traded in an active market but the fair values are based on quoted market prices, broker dealer quotations or alternative pricing sources with reasonable levels of price transparency. Level 2 financial instruments include certain money market securities and most OTC derivatives.

### 13. Other receivables

	2012 £m	2011 £m
Prepayments and accrued income:		
Due from fellow subsidiaries	3	4
Other	9	9
	<u>12</u>	<u>13</u>

Within the 'other' category of other receivables are prepaid facility fees of **£5 million** (2011: £7 million) which relate to periods which fall beyond one year.

The currency profile of other receivables is **£11 million** (2011: £10 million) UK sterling, **£nil** (2011: £1 million) euros, **£1 million** (2011: £nil) US dollar, **£nil** Australian dollar (2011: £1 million) and **£nil** (2011: £1 million) in other currencies.

All amounts are unsecured and interest free. Due to their short-term nature, there is no material difference between the book values and fair values of all amounts due from fellow subsidiaries included above.

## Group Notes on the Accounts

### 14a. Loans due from parent undertaking

Loans due from parent undertaking at 31 December 2012 of **£3,633 million** fall due within four to five years (2011: £3,630 million within two years) are unsecured and reprice within one year (2011: £3,630 million within one year). This loan is in UK Sterling.

Loans due from parent undertaking include **£16 million** of interest receivable at 31 December 2012 (2011: £13 million). There is no material difference between the book value and fair value for loan due from the parent undertaking.

### 14b. Loans due from fellow subsidiaries

Unsecured loans due from fellow subsidiaries are denominated in the following currencies:

	2012	2011
	£m	£m
UK sterling	16,092	8,424
Euro	1,360	3,462
US dollar	3,016	3,195
Singapore dollar		1,191
Danish krone	345	396
Canadian dollar	288	357
Swiss franc	221	86
Norwegian krone		168
Hong Kong dollar		142
Swedish krona	136	135
Polish zloty	20	41
Hungarian forint		51
New Zealand dollar		25
Mexican peso		19
	21,478	17,692

There is no material difference between the book value and fair value for loans due from fellow subsidiaries.

The maturity dates of loans due from fellow subsidiaries as recognised in the balance sheet are as follows:

	2012	2011
	£m	£m
Within one year	16,300	5,258
Between one and two years	995	7,353
Between two and three years	714	1,204
Between three and four years	370	958
Between four and five years	662	370
Beyond five years	2,437	2,549
Total	21,478	17,692

The timing exposure to interest rate changes when loans reprice is as follows:

	Total	Within 1 year	Between 1 and 2 years	Between 2 and 3 years	Between 3 and 4 years	Between 4 and 5 years	Greater than 5 years
	£m	£m	£m	£m	£m	£m	£m
As at 31 December 2012	21,478	18,074	488	479			2,437
As at 31 December 2011	17,692	17,308	294				90

Interest rate risk on loans due from fellow subsidiaries is not hedged by the Group.

Loans due from fellow subsidiaries include **£58 million** of interest receivable (2011: £68 million).

## Group Notes on the Accounts

### 15. Borrowings - bank overdrafts and issued debt

	Currency	Maturity dates	Interest rates	2012 £m	2011 £m
<b>Issued debt</b>					
Eurobonds	Euro	2013-2021	3.6 to 5.9%	2,646	2,973
	UK sterling	2013-2040	5.8 to 7.3%	2,296	2,302
Other bonds issued pursuant to Rule 144A and RegS under the US Securities Act	US dollar	2013-2022	1.4 to 9.5%	1,840	643
Commercial paper					85
				<b>6,782</b>	6,003
<b>Bank overdrafts</b>					
				<b>86</b>	94
				<b>6,868</b>	6,097

In June 2012, the Company repaid a €337 million bond due in June 2012.

In June 2012, the Company issued new US \$2,000 million bonds: US\$500 million with a maturity of June 2015; US\$600 million with a maturity of June 2017; and US\$900 million with a maturity of June 2022.

Included within borrowings of **£6,782 million** (2011: £6,003 million) above are **£1,995 million** (2011: £1,923 million) where the amortised cost has been adjusted as part of a fair value hedge. The carrying value of borrowings subject to fair value hedges has been increased by **£143 million** at 31 December 2012 (2011: increased by £109 million) shown in the table above.

Bank overdrafts are all repayable within one year, and are denominated in Czech krona, Euro, Hong Kong dollar, Singapore dollar, Turkish lira, New Zealand Dollar, Danish krona, UK Sterling and US dollar (2011: Czech krona, Euro, Swedish krona, Singapore dollar, Turkish lira, UK sterling, US dollar and South African rand).

#### Borrowings are repayable as follows:

	Per balance sheet		Contractual gross maturities	
	2012 £m	2011 £m	2012 £m	2011 £m
Within one year	584	625	693	803
Between one and two years		353	332	678
Between two and three years	1,317		1,652	308
Between three and four years		1,041	269	1,352
Between four and five years	1,373		1,666	247
Beyond five years	3,594	4,078	4,972	5,686
Total	<b>6,868</b>	6,097	<b>9,584</b>	9,074

The contractual gross maturities in each year include the borrowings maturing in that year, together with forecast interest payments on all borrowings which are outstanding for all or part of the year.

Issued debt repayable within one year includes interest payable of **£157 million** (2011: £162 million).

## Group Notes on the Accounts

### 15. Borrowings - bank overdrafts and issued debt continued

Issued debt is denominated in the following currencies:

	Total £m	GBP £m	USD £m	EUR £m	CHF £m	AUD £m	CAD £m	DKK £m	SEK £m	NOK £m
<b>As at 31 December 2012</b>										
Total issued debt	6,782	2,296	1,840	2,646						
Effect of derivative financial instruments										
Cross-currency swaps	28	518	13	(503)						
Forward foreign exchange contracts	66	741		(1,658)	221		287	344	131	
	<b>6,876</b>	<b>3,555</b>	<b>1,853</b>	<b>485</b>	<b>221</b>		<b>287</b>	<b>344</b>	<b>131</b>	
<b>As at 31 December 2011</b>										
Total issued debt	6,003	2,302	694	3,007						
Effect of derivative financial instruments										
Cross-currency swaps	14	518	14	(518)						
Forward foreign exchange contracts	42	(1,662)	272	(751)	86	1,121	294	390	130	162
	<b>6,059</b>	<b>1,158</b>	<b>980</b>	<b>1,738</b>	<b>86</b>	<b>1,121</b>	<b>294</b>	<b>390</b>	<b>130</b>	<b>162</b>

Details of the derivative financial instruments included in these tables are given in note 11 on pages 16-22.

The timing exposure to interest rate changes when borrowings are repriced is as follows:

	Total £m	Within 1 year £m	Between 1 and 2 years £m	Between 2 and 3 years £m	Between 3 and 4 years £m	Between 4 and 5 years £m	Beyond 5 years £m
<b>At 31 December 2012</b>							
Total issued debt	6,782	498		1,317		1,373	3,594
Effect of derivative financial instruments							
Interest rate swaps		1,369	(750)			(369)	(250)
Cross-currency swaps	28	531					(503)
	<b>6,810</b>	<b>2,398</b>	<b>(750)</b>	<b>1,317</b>		<b>1,004</b>	<b>2,841</b>
<b>At 31 December 2011</b>							
Total issued debt	6,003	531	353		1,041		4,078
Effect of derivative financial instruments							
Interest rate swaps		1,150	(150)	(750)			(250)
Cross-currency swaps	14	532					(518)
	<b>6,017</b>	<b>2,213</b>	<b>203</b>	<b>(750)</b>	<b>1,041</b>		<b>3,310</b>

Details of the derivative financial instruments included in these tables are given in note 11 on pages 16-22.

British American Tobacco p.l.c. has provided guarantees for all of the Group's public indebtedness. As at 31 December 2012, the amount of these guarantees was **£5,938 million** (2011: £5,708 million).

The fair value of issued debt is **£7,862 million** (2011: £6,843 million) and has been determined using quoted market prices.

## Group Notes on the Accounts

### 16a Amounts repayable on demand to parent undertaking

Amounts repayable on demand to parent undertaking of **£7,750 million** (2011: £6,348 million) are unsecured and comprise current account borrowings from the parent. These are denominated in sterling. There is no accrued interest repayable in the current or prior year.

There is no material difference between the book value and fair value for amounts repayable on demand to parent undertaking.

### 16b Amounts repayable on demand to fellow subsidiaries

Amounts repayable on demand to fellow subsidiaries comprise fellow subsidiary current accounts and cash pooling accounts held with the Group. These are unsecured, are denominated in the following currencies:

	2012	2011
	£m	£m
UK sterling	8,029	5,420
Euro	435	552
US dollar	470	176
Swiss franc	35	36
New Zealand dollar		6
Norwegian krona	48	
Australian dollar	135	26
Hong Kong dollar	19	20
Romanian Leu	103	
Other	70	118
	<u>9,344</u>	<u>6,354</u>

Amounts repayable on demand to fellow subsidiaries include **£nil** of interest repayable at 31 December 2012 (2011: £0.5 million). There is no material difference between the book value and fair value for amounts repayable on demand to fellow subsidiaries.

### 17. Other payables

	2012	2011
	£m	£m
Accrued charges		
Due to fellow subsidiaries		13
Other	2	2
	<u>2</u>	<u>15</u>

The currency profile of other payables is **£2 million** (2011: £15 million) UK sterling.

All amounts are unsecured and interest free. There is no material difference between the book values of other payables and their fair values.

## Group Notes on the Accounts

### 18. Term deposits repayable to fellow subsidiaries

Term deposits repayable to fellow subsidiaries are unsecured, are denominated in the following currencies:

	2012	2011
	£m	£m
UK sterling	473	1,972
Euro	553	115
US dollar	62	267
Norwegian krone		51
Swiss franc	15	19
Hong Kong dollar	5	12
Danish krone		30
Bulgarian lev		6
Singapore dollar	33	33
Japanese Yen	68	
Romanian leu	2	
	1,211	2,505

Term deposits repayable to fellow subsidiaries include **£0.3 million** of interest payable at 31 December 2012 (2011: £0.7 million) and repriced within one year (2011: £2,505 million within one year).

In 2012 and 2011, term deposits repayable to fellow subsidiaries fall due within one year.

There is no material difference between the above amounts for term deposits repayable to fellow subsidiaries and their fair values.

### 19. Total shareholders' equity

	Share capital	Hedging reserve	Translation reserve	Retained earnings	Total equity
	£m	£m	£m	£m	£m
<b>1 January 2012</b>	<b>231</b>	<b>(2)</b>	<b>220</b>	<b>765</b>	<b>1,214</b>
<b>Comprehensive income</b>					
Profit for the year				164	164
Differences on exchange			(43)		(43)
Cash flow hedges					
net fair value losses					
reclassified and reported in profit and loss		1			1
Net investment hedges					
net fair value gains					
differences on exchange on borrowings			13		13
<b>31 December 2012</b>	<b>231</b>	<b>(1)</b>	<b>190</b>	<b>929</b>	<b>1,349</b>
	Share capital	Hedging reserve	Translation reserve	Retained earnings	Total equity
	£m	£m	£m	£m	£m
1 January 2011	231	(1)	205	682	1,117
Comprehensive income					
Profit for the year				83	83
Differences on exchange			18		18
Cash flow hedges					
net fair value losses		(2)			(2)
reclassified and reported in profit and loss		1			1
Net investment hedges					
net fair value gains					
differences on exchange on borrowings			(3)		(3)
31 December 2011	231	(2)	220	765	1,214



## Group Notes on the Accounts

### 19. Total shareholders' equity continued

Details relating to the allotted and issued share capital, and movements therein, are included on page 41, note 14 to the company financial statements.

The translation reserve is as explained in the accounting policy on foreign currencies on page 9. The hedging reserve is as explained in the accounting policy on financial instruments on pages 10-11.

### 20. Contingent liabilities

The Group is one of the three entities in the BAT Group which have jointly guaranteed borrowing facilities available to B.A.T. Capital Corporation of **£25 million** (US\$40 million) and to B.A.T. Holdings (The Netherlands) B.V. of **£2,855 million** (€2,369 million and £325 million). The Group has guaranteed a borrowing facility available to B.A.T Colombia SAS of **£15 million** (US\$25 million). All such facilities have been utilised at the balance sheet date.

The full fair value of the above guarantees is recognised in the financial statements of the ultimate parent undertaking, British American Tobacco p.l.c.

Contingent liabilities mature as follows:

	2012	2011
	£m	£m
Within one year	436	444
Between one and two years	487	810
Between two and three years		501
Between three and four years	325	
Between four and five years		325
Beyond five years	1,647	1,070
Total	<u>2,895</u>	<u>3,150</u>

The Group has guaranteed a cross currency swap issued out of B.A.T Colombia SAS, receive variable Dollars, pay fixed Colombian Peso, as at 31 December 2012 this cross currency interest rate swap had a liability fair value of **£19 million** (2011: £4 million)

### 21. Related party disclosures

The Group has a number of transactions and relationships with related parties, as defined in IAS 24, all of which are undertaken in the normal course of the Group's business as a primary financing vehicle for the BAT Group.

Transactions and balances with fellow subsidiaries and the parent undertaking relate mainly to the provision of finance to companies within the BAT Group.

Details of these transactions in the Group Balance Sheet are set out in notes 10, 13, 14, 16, 17, and 18. In addition, outstanding balances with fellow subsidiaries are included within note 11 as follows:

	2012		2011	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Derivative financial instruments				
Cross-currency swaps	12		30	
Interest rate swaps	55	87	22	53
Forward foreign currency contracts	48	181	130	98
	<u>115</u>	<u>268</u>	<u>182</u>	<u>151</u>

Details of these transactions in the Group Income Statement are set out in notes 3, 4 and 5. In addition, balances with fellow subsidiaries are included within note 6 as follows:

	2012	2011
	Income/(Expense) £m	Income/(Expense) £m
Derivative financial instruments		
Cross-currency swaps	(29)	(3)
Interest rate swaps	(14)	(18)
Forward foreign currency contracts	(145)	11
	<u>(188)</u>	<u>(10)</u>

### 21. Related party disclosures continued

The key management of the Company consist of the members of the Board of Directors and no such person had any material interest during the year in a contract of significance with the Group. The term key management in this context includes the respective members of their households.

### 22. Post balance sheet events

In March 2013, the Group issued new US\$300 million bonds with a maturity of March 2016, and €650 million bonds with a maturity of March 2025.

### 23. Principal subsidiary undertakings

The Company holds the entire issued share capital of BATIF Dollar Limited, and of B.A.T Finance B.V. - finance companies incorporated in England and Wales and the Netherlands respectively.

### 24. Directors' remuneration

None of the Directors received any remuneration in respect of their services to the Group during the year (2011: £nil).

### 25. Parent undertaking

The Company's immediate and ultimate parent undertaking and ultimate controlling party is British American Tobacco p.l.c., being incorporated in the United Kingdom and registered in England and Wales and registered as an external company in the Republic of South Africa. Consolidated group financial statements are prepared by British American Tobacco p.l.c. and are publicly available.

### 26. Copies of the report and accounts

Copies of the report and accounts of British American Tobacco p.l.c. may be obtained from the Company Secretary, Globe House, 4 Temple Place, London WC2R 2PG.

## **Independent Auditors report to the members of B.A.T. International Finance p.l.c. - Group Financial Statements**

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We have audited the group financial statements of B.A.T. International Finance p.l.c. for the year ended 31 December 2012 which comprise the Group Income Statement, the Group Statement of Comprehensive Income, the Group Statement of Changes in Equity, the Group Balance Sheet, the Group Cash Flow Statement and the Group Notes on the Accounts. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### **Respective responsibilities of Directors and auditors**

As explained more fully in the Directors' responsibilities statement as set out on pages 3-4, the Directors are responsible for the preparation of the Group 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 Group financial statements in accordance with applicable law and International Standards on Auditing (UK and 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.

### **Scope of the audit of the financial statements**

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 Group'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. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### **Opinion on financial statements**

In our opinion the Group financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2012 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the Group financial statements are prepared is consistent with the Group financial statements.

### **Matters on which we are required to report by exception**

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

- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

### **Other matters**

We have reported separately on the Parent Company financial statements of B.A.T. International Finance p.l.c. for the year ended 31 December 2012.



Paul Cragg (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
1 Embankment Place, London

4 April 2013

**Balance Sheet – B.A.T. International Finance p.l.c.**  
**at 31 December 2012**  
**Registered Number 1060930**

	2012 £m	2011 £m
<b>Assets</b>		
<i>Fixed assets</i>		
Investments in subsidiaries (note 2)	718	1,160
Loans due from parent undertaking (note 3a)	3,633	3,630
Loans due from subsidiary and fellow subsidiaries (note 3b)	<u>20,703</u>	<u>14,497</u>
	<u>25,054</u>	<u>19,287</u>
<i>Current assets</i>		
Amounts due on demand from subsidiaries (note 4)		1,443
Amounts due on demand from fellow subsidiaries (note 5)	799	433
Prepayments and accrued income (note 6)	12	13
Derivative financial instruments (note 7)	485	513
Short-term deposits and cash (note 9)	<u>509</u>	<u>641</u>
	<u>1,805</u>	<u>3,043</u>
<b>Total assets</b>	<u>26,859</u>	<u>22,330</u>
<b>Liabilities</b>		
<i>Creditors</i>		
Issued debt (note 10)	6,782	6,003
Bank overdrafts (note 10)	86	94
Amounts payable on demand to parent undertaking (note 11a)	7,750	6,348
Amounts payable on demand to fellow subsidiaries (note 11b)	9,344	6,354
Borrowings from fellow subsidiaries (note 12)	1,211	2,505
Derivative financial instruments (note 7)	392	389
Accruals and deferred income (note 13)	<u>2</u>	<u>15</u>
	<u>25,567</u>	<u>21,708</u>
<i>Capital and reserves</i>		
Called up share capital (note 14)	231	231
Hedging reserve (note 14)	(1)	(3)
Retained earnings (note 14)	<u>1,062</u>	<u>394</u>
Total shareholders' equity	<u>1,292</u>	<u>622</u>
<b>Total equity and liabilities</b>	<u>26,859</u>	<u>22,330</u>

On behalf of the Board

  
 John Benedict Stevens  
 3 April 2013

The accompanying notes are an integral part of the Company financial statements. Notes are shown on pages 37-42.

## Notes on the Accounts – B.A.T. International Finance p.l.c.

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### 1. Accounting policies

#### **Basis of accounting**

The Company financial statements have been prepared on the going concern basis under the historical cost convention except as described in the accounting policy below on financial instruments and in accordance with the Companies Act 2006 and UK Generally Accepted Accounting Principles.

The preparation of the Group's financial statements under International Financial Reporting Standards has led to the use of the 'liquidity format' for the balance sheet in those financial statements. In order to aid comparability between the Group and Company, the format of the Company balance sheet has been presented within the limits of the Companies Act 2006, to match as closely as possible the 'liquidity format' in order to present a true and fair view of the state of affairs of the Company.

Accounting policies of the Company are consistent with the respective policies of the Group's financial statements unless otherwise stated and thus the disclosures in the Company financial statements are referenced to the Group's financial statements where appropriate.

#### **Cash flow statement**

The cash flows of the Company are included in the Group cash flow statement on page 8. Consequently, the Company is exempt under the terms of FRS 1 (Revised) from publishing a cash flow statement.

#### **Foreign currencies**

Transactions arising in currencies other than sterling are translated at the rate of exchange ruling on the date of the transaction. Assets and liabilities expressed in currencies other than sterling are translated at rates of exchange ruling at the end of the financial year. All exchange differences are taken to the profit and loss account in the year.

#### **Accounting for income**

As a financing vehicle, the Company's primary sources of income comprise interest on loans to fellow subsidiaries and net fee income. These are recognised on the effective interest rate method, and all income is only recognised to the extent that it is considered to be collectable.

Net fee income comprises commitment fees received in respect of undrawn revolving credit facilities provided to fellow subsidiaries, and commitment fees paid in respect of revolving credit facilities provided by external banks.

#### **Taxation**

Taxation provided is that chargeable on the profits of the year, together with deferred taxation.

The current income taxation charge is calculated on the basis of taxation laws enacted or substantially enacted at the balance sheet date.

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more taxation in the future or a right to pay less taxation in the future have occurred at the balance sheet date.

A net deferred taxation asset is recognised as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which to recover carried forward taxation losses and from which the future reversal of underlying timing differences can be deducted.

Deferred taxation is measured at the average taxation rates that are expected to apply in the periods in which the timing differences are expected to reverse based on taxation rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred taxation is measured on an undiscounted basis.

#### **Investments in subsidiaries**

Investments in subsidiaries are stated at cost, together with subsequent capital contributions, less provision for any impairment in value.

#### **Financial instruments**

Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the relevant instrument and derecognised when it ceases to be a party to such provisions.

### 1. Accounting policies continued

#### Financial instruments continued

Non-derivative financial assets are stated at amortised cost using the effective interest method, subject to reduction for allowances for estimated irrecoverable amounts. Financial assets measured at amortised cost are reviewed for impairment at each balance sheet date, or whenever events indicate that the carrying amount may not be recoverable. An impairment for irrecoverable amounts is recognised when there is objective evidence that the full amount receivable will not be collected according to the original terms of the asset. Such evidence might include financial difficulties of the counterparty, defaults of payment or significant overdue balances. For interest-bearing assets, their carrying value includes accrued interest receivable.

Short-term deposits and cash include cash in hand and deposits held on call, together with other short-term highly liquid investments including investments in certain money market funds. Short-term deposits normally comprise instruments with maturities of three months or less at date of acquisition.

Non-derivative financial liabilities are stated at amortised cost using the effective interest method. For borrowings, their carrying value includes accrued interest payable, as well as unamortised issue costs.

Derivative financial assets and liabilities are stated at fair value, which includes accrued interest receivable and payable where relevant. Changes in their fair values are recognised as follows:

- For derivatives that are designated as cash flow hedges, the changes in their fair values are recognised directly in equity, to the extent that they are effective, with the ineffective portion being recognised in the income statement. The accumulated gains and losses are recognised in the income statement in the same period as the hedged item; and
- For derivatives that are designated as fair value hedges, the carrying value of the hedged item is adjusted for the fair value changes attributable to the risk being hedged, with the corresponding entry being made in the income statement. The changes in fair value of these derivatives are also recognised in the income statement.

For derivatives that do not qualify for hedge accounting or are not designated as hedges, the changes in their fair values are recognised in the income statement in the period in which they arise.

In order to qualify for hedge accounting, the Company is required to document prospectively the relationship between the item being hedged and the hedging instrument. The Company is also required to demonstrate an assessment of the relationship between the hedged item and the hedging instrument, which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at each reporting date to ensure that the hedge has remained, and is expected to remain, highly effective.

Hedge accounting is discontinued when a hedging instrument is derecognised (for example through expiry or disposal), or no longer qualifies for hedge accounting.

#### Segmental analysis

The Company's internal reporting systems are not arranged on a geographical basis. As SSAP 25 requires a segmental analysis, geographical segmentation based on location of counterparty has been provided in note 15. The Company is a single product business providing finance services.

#### Related parties

The Company has taken advantage of the exemption under paragraph 3(c) of FRS 8 from disclosing transactions with related parties that are wholly owned subsidiaries of the BAT Group.

#### Dividends

Dividend distributions are recognised as a liability in the financial statements in the period in which the dividends are paid.

### 2. Investments in subsidiaries

The Company holds the entire issued share capital of BATIF Dollar Limited and of B.A.T Finance B.V. - finance companies incorporated in England and Wales and the Netherlands respectively. The cost of these investments as at 31 December 2012 was **£718 million** (2011: £1,160 million).

During the year a capital reduction in BATIF Dollar Limited took place resulting in a **£442 million decrease** on the carrying value of this investment.

The Directors are of the opinion that the individual investments in the subsidiary undertakings have a value of not less than the amount at which they are shown in the balance sheet.

## Notes on the Accounts – B.A.T. International Finance p.l.c.

### 3a. Loans due from parent undertaking

Loans due from parent undertaking of **£3,633 million** (2011: £3,630 million) comprise exactly the same balances and disclosures as Loans due from parent undertaking, detailed in Group note 14a.

### 3b. Loans due from subsidiary and fellow subsidiaries

Unsecured loans due from subsidiary and fellow subsidiaries are denominated in the following currencies:

	2012	2011
	£m	£m
UK sterling	16,092	8,424
Euro	1,360	3,462
Singapore dollar		1,191
Danish krone	345	396
Canadian dollar	288	357
Swiss franc	221	86
Norwegian krone		168
Hong Kong dollar		142
Swedish krona	136	135
Polish zloty	20	41
Hungarian forint		51
US dollar*	2,241	
Mexican peso		19
New Zealand dollar		25
	20,703	14,497

There is no material difference between the book value and fair value for loans due from subsidiary and fellow subsidiaries.

The maturity dates of loans due from subsidiary and fellow subsidiaries as recognised in the balance sheet are as follows:

	2012	2011
	£m	£m
Within one year*	15,770	5,072
Between one and two years	995	7,191
Between two and three years	2,906	906
Between three and four years	370	958
Between four and five years	662	370
Greater than five years		
Total	20,703	14,497

\* Loans due from subsidiary of £2,241 million (2011: £nil) fall due in 2015 are unsecured and reprice within one year. The loan is in US dollar.

Loans due from subsidiary and fellow subsidiaries repayable within one year are expected to be renewed upon maturity and accordingly are classified as fixed assets in the Company balance sheet.

The timing exposure to interest rate changes when loans reprice is as follows:

	Total	Within 1 year	Between 1 and 2 years	Between 2 and 3 years	Between 3 and 4 years	Between 4 and 5 years
	£m	£m	£m	£m	£m	£m
<b>As at 31 December 2012</b>	20,703	19,743	481	479		
As at 31 December 2011	14,497	14,203	294			

Interest rate risk of loans to subsidiary and fellow subsidiaries is not hedged.

Loans to subsidiary and fellow subsidiaries include **£40 million** of interest receivable at 31 December 2012 (2011: £65 million).

Loans totalling **€nil** (2011: €1.4 billion) due from a fellow subsidiary will be settled by delivery of German government securities. Forward sale contracts are in place to hedge the value of these securities (Group note 11).

## Notes on the Accounts – B.A.T. International Finance p.l.c.

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### 4. Amounts due on demand from subsidiaries

Amounts due on demand from subsidiaries of **£nil** (2011: £1,443 million) comprise current accounts held with the Company. These are denominated in US dollars.

There is no material difference between the book value and fair value for amounts due on demand from subsidiaries.

### 5. Amounts due on demand from fellow subsidiaries

Amounts due on demand from fellow subsidiaries of **£799 million** (2011: £433 million) for the Company comprise the same balances and disclosures as Amounts due on demand from fellow subsidiaries for the Group, detailed in Group note 10. Consequently no additional information is presented here.

### 6. Prepayments and accrued income

Prepayments and accrued income of **£12 million** (2011: £13 million) for the Company comprise exactly the same balances and disclosures as other receivables, detailed in Group note 13. Consequently no additional information is presented here.

### 7. Derivative financial instruments

Derivative financial instruments comprise the same balances as derivative financial instruments, detailed in Group note 11.

Under FRS 29, the disclosures required are the same as under IFRS 7. Consequently no additional information is presented in this note.

### 8. Management of financial risks

The disclosures provided by Group note 12 under IFRS 7 are the same as the disclosures required by FRS 29. Consequently no additional information is presented here except for interest rate risk and credit risk.

#### Interest rate risk

FRS 29 requires a sensitivity analyses that shows the impact on the income statement and on items recognised directly in equity of hypothetical changes of interest rates in respect of interest-bearing financial instruments recognised in the balance sheet at 31 December 2012. All other variables are held constant although, in practice, market rates rarely change in isolation. For the purposes of the sensitivity analyses, financial assets and liabilities with fixed interest rates are not included. Interest sensitivity in respect of foreign exchange forward contracts is not included in the analysis for 2012 as it is considered as fixed rate interest. The Company considers a 100 basis point change in interest rates as a reasonably possible change except where rates are less than 100 basis points. In these instances it is assumed that the interest rates increase by 100 basis points and decrease to zero for the purpose of performing the sensitivity analysis. The impact is calculated with reference to the financial asset or liability held as at the year end, unless this is unrepresentative of the position during the year.

A 100 basis point increase in interest rates would result in pre-tax profit being **£29 million** higher (2011: £19 million higher). A 100 basis point decrease in interest rates, or less where applicable, would result in pre-tax profit being **£92 million** lower (2011: £41 million lower).

A 100 basis point change in interest rates would have no impact on items recognised directly in other comprehensive income for the current and prior year.



### 8. Management of financial risks continued

#### Credit risk

The maximum exposure to credit risk of financial assets at the balance sheet date is reflected by the carrying values included in the Company balance sheet. In addition, the Company provides committed credit facilities to certain fellow subsidiaries. The undrawn portion of these committed facilities at 31 December 2012 is **£663 million** (2011: £399 million). Guarantees provided to third parties are shown in note 17 page 41.

### 9. Short-term deposits and cash

Short-term deposits and cash for the Company comprise the same balances and disclosures as cash and cash equivalents, detailed in Group note 9. Consequently no additional information is presented here.

### 10. Borrowings - bank overdrafts and issued debt

Bank overdrafts and issued debt for the Company comprise the same balances and disclosures as Bank overdrafts and Issued debt, detailed in Group note 15. Consequently no additional information is presented here.

### 11a. Amounts payable on demand to parent undertaking

Amounts payable on demand to parent undertaking of **£7,750 million** (2011: £6,348 million) comprise the same balances and disclosures as Amounts repayable on demand to parent undertaking, detailed in Group note 16a. Consequently no additional information is presented here.

### 11b. Amounts payable on demand to fellow subsidiaries

Amounts payable on demand to fellow subsidiaries of **£9,344 million** (2011: £6,354 million) comprise the same balances and disclosures as Amounts repayable on demand to fellow subsidiaries, detailed in Group note 16b. Consequently no additional information is presented here.

### 12. Borrowings from fellow subsidiaries

Borrowings from fellow subsidiaries of **£1,211 million** (2011: £2,505 million) for the Company comprise the same balances and disclosures as Term deposits repayable to fellow subsidiaries, detailed in Group note 18. Consequently no additional information is presented here.

### 13. Accruals and deferred income

Accruals and deferred income of **£2 million** (2011: £15 million) for the Company comprise the same balances and disclosures as Other payables, detailed in Group note 17. Consequently no additional information is presented here.

## Notes on the Accounts – B.A.T. International Finance p.l.c.

### 14. Total shareholders' equity

	Called up share capital	Hedging reserve	Retained earnings	Total equity
	£m	£m	£m	£m
1 January 2012	231	(3)	394	622
Profit for the financial year			668	668
Cash flow hedges				
Reclassified and reported in net profit		2		2
31 December 2012	231	(1)	1,062	1,292

As permitted by Section 408(3) of the Companies Act 2006, the profit and loss account of the Company has not been presented in these Company financial statements. The profit for the financial year ended 31 December 2012 was **£668 million** (2011: £25 million).

Share capital consists of 231 million ordinary shares of £1 each, allotted, issued and fully paid.

The hedging reserve is explained in the accounting policy on financial instruments on pages 36-37.

Details of the audit fee in respect of the company are included in Group note 7 on page 14.

### 15. Segmental reporting

	Total		Western Europe		EEMEA*		Americas		Asia Pacific	
	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Net assets/ (liabilities)	1,292	622	1,931	(650)	(105)	81	(325)	95	(209)	1,096

\* Eastern Europe, Middle East and Africa

### 16. Directors' remuneration

None of the Directors received any remuneration in respect of their services to the Company during the year (2011: £nil).

### 17. Contingent liabilities

Contingent liabilities of **£2,895 million** (2011: £3,150 million) for the Company in relation to guarantees provided to fellow subsidiaries comprise the same balances and disclosures as Contingent liabilities, detailed in Group note 20. Consequently no additional information is presented here.

### 18. Related parties

As explained in the accounting policies on note 1, the Company has taken advantage of the exemption under paragraph 3(c) of FRS 8 from disclosing transactions with related parties that are wholly owned subsidiaries of the BAT Group. Details of balances and transactions with related parties that are not wholly owned by the BAT Group are disclosed below.

As at 31 December 2012, total assets on the balance sheet included **£nil** (2011: £nil) of loans due from related parties that are not wholly owned by the BAT Group (2011: £nil). Total liabilities included amounts repayable on demand of **£4 million** (2011: £8 million).

The Company did not earn any material income or incur any material expenses in transactions with related parties that are not wholly owned by the BAT Group.

**18. Related parties continued**

Cash flows for the year ended 31 December 2012, included net cash flows of **£nil** (2011: **£nil**) in respect of loans advanced to fellow subsidiaries that are not wholly owned by the BAT Group and net outflows of **£1 million** (2011: **£1 million inflows**) in respect of net borrowings obtained.

**19. Post balance sheet events**


In March 2013, the Group issued new US\$300 million bonds with a maturity of March 2016, and €650 million bonds with a maturity of March 2025.

**20. Parent undertaking**

The Company's immediate and ultimate parent undertaking and ultimate controlling party is British American Tobacco p.l.c., being incorporated in the United Kingdom and registered in England and Wales and registered as an external Company in the Republic of South Africa. Consolidated Group financial statements are prepared by British American Tobacco p.l.c. and are publicly available.

**21. Copies of the report and accounts**

Copies of the report and accounts of British American Tobacco p.l.c. may be obtained from the Company Secretary, Globe House, 4 Temple Place, London WC2R 2PG.

  
For and on behalf of PricewaterhouseCoopers LLP,  
Chartered Accountants and Statutory Auditors  
1 Lombard Street, London  
4 April 2013

## Independent Auditors report to the members of B.A.T. International Finance p.l.c. –Parent Company Financial Statements

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We have audited the Company financial statements of B.A.T. International Finance p.l.c. for the year ended 31 December 2012 which comprise the Balance Sheet and the Notes on the Accounts. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

### Respective responsibilities of Directors and auditors

As explained more fully in the Directors' responsibilities statement in relation to the financial statements as set out on pages 3-4, the Directors are responsible for the preparation of the Parent Company 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 Parent Company financial statements in accordance with applicable law and International Standards on Auditing (UK and 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.

### Scope of the audit of the financial statements

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 Parent 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 Directors' report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on financial statements

In our opinion the Parent Company financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2012;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the Parent Company financial statements are prepared is consistent with the Parent Company financial statements.

### Matters on which we are required to report by exception

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

- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

### Other matters

We have reported separately on the Group financial statements of B.A.T. International Finance p.l.c. for the year ended 31 December 2012.



Paul Cragg (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
1 Embankment Place, London  
4 April 2013