

British-American Tobacco (Holdings) Limited
Registered Number 262254

Directors' Report and Accounts

For the year ended 31 December 2006

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British-American Tobacco (Holdings) Limited

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British-American Tobacco (Holdings) Limited

Directors' report

The Directors present their report together with the audited accounts for the year ended 31 December 2006

Principal activities

The Company is a holding company of a group of companies, which includes a number of subsidiaries, the principal business activities of which are the marketing and manufacture of tobacco products

Review of the year to 31 December 2006

The profit for the year attributable to British-American Tobacco (Holdings) Limited shareholders after deduction of all charges and the provision of tax amounted to £908,367,000 (2005 restated £927,665,000)

Key performance indicators

The Directors of British American Tobacco plc, the ultimate parent company, manage the operations of the British American Tobacco Group (the "Group") on a regional basis. For this reason, and given the nature of the Company's activities, the Company's Directors believe that key performance indicators are not necessary or appropriate for an understanding of the Company's specific development, performance or the position of its business. However, key performance indicators relevant to the Group, and which may be relevant to the Company, are disclosed under the Operating and Financial Review section in the Annual Review of British American Tobacco plc and do not form part of this report.

Principal risks and uncertainties

The principal risks and uncertainties of the Company are integrated with the principal risks of the Group and are monitored by audit committees to provide a framework for identifying, evaluating and managing risks faced by the Group. Accordingly, the key group risk factors that may be relevant to the Company are disclosed in the Annual Review of British American Tobacco plc, and do not form part of this report.

Change in accounting policy

The Company has adopted FRS20 "Share-based payment" in these financial statements. In accordance with the transitional provisions of FRS20, the requirements of FRS20 have been applied to all equity-settled grants that were unvested at 1 January 2006. FRS20 has also been applied to all cash-settled grants not settled as at 1 January 2006. For share-based payments for which the requirements of FRS20 have not been applied, the Company has continued to account for such awards in accordance with UITF Abstract 17. The comparative figures for 2005 have been adjusted accordingly in respect of this accounting policy change.

The Company has both equity-settled and cash-settled compensation plans. With the adoption of FRS20, equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed over the vesting periods, based on the Company's estimate of awards that will eventually vest, with a corresponding credit to reserves.

For cash-settled share based payments, a liability equal to the portion of the services received is recognised at its current fair value determined at each balance sheet date. Fair value is measured by the use of Black-Scholes and Monte-Carlo option pricing models.

British-American Tobacco (Holdings) Limited

Directors' report

Change in accounting policy (continued)

The expected life used in the models has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations. Under UITF Abstract 17, the cost of awards is calculated by reference to the fair value of the shares at the date of the award.

The share scheme expense for the year ended 2006 on adoption of FRS20 was £48,184,898 (2005 £53,047,251). The charge would have been £58,747,960 (2005 £50,451,061) under UITF Abstract 17. Shareholders' funds at 31 December 2005 were increased by £49,862,000 as a result of applying FRS20. In addition, the effect of the change in accounting policy was to reduce provisions for liabilities and charges for share schemes by £17,820,994 and correspondingly increase shareholders' funds at 31 December 2004 by the same amount.

Dividends

During the year, the Company paid dividends amounting to £750,000,000 (2005 £618,000,000). The retained profit for the financial year after dividends of £158,367,000 will be transferred to reserves (2005 restated £309,665,000).

Board of Directors

The names of the persons who served as Directors of the Company during the period 1 January 2006 to the date of this report are as follows:

Rudi Kindts

Antonio Monteiro de Castro

Paul Ashley Rayner

Nicola Snook

(appointed 14 December 2006, resigned 22 December 2006)

Peter Henry Taylor

Neil Robert Withington

Directors' indemnities

As at the date of this report, an indemnity is in force under which Messrs P A Rayner and A Monteiro de Castro, 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.

Employees

The Company utilises a range of initiatives to actively encourage employee involvement in the Group's business including individual discussions, team briefings, employee surveys, publications and regular meetings with employee representatives.

The Company actively encourages employee share ownership through participation in the employee share plans, the most recent of which are the Partnership Share Scheme and the Share Reward Scheme.

The Company has Employment Policies which are committed to providing a work environment that is free from harassment, bullying and discrimination – these policies are available to all staff on the Company's intranet. There is no discrimination against people with disabilities who apply to join the Company and anyone within the Company with disability is awarded the same opportunities for promotion, training and career development as other staff. We aim to establish and maintain a safe working environment for all staff, including those with disabilities.

British-American Tobacco (Holdings) Limited

Directors' report

Tangible fixed assets

The movement of fixed assets is shown in note 6 to the accounts

Creditor payment policy

The Company follows the Better Payment Practice Code* and therefore for both the current and the next financial year aims to settle the terms of payment with its suppliers when agreeing the terms of each transaction, in any case within the supplier's own standard payment period, and also aims to pay all of its suppliers within a reasonable period of their invoices being received

In respect of all of its suppliers, it is the Company's policy to

- agree the terms of payment with those suppliers when agreeing the terms of each transaction,
- ensure that those suppliers are made aware of the terms of payment,
- abide by the terms of payment,
- avoid any delays when legitimately questioning invoices

Payment of creditors is carried out by a fellow Group undertaking

* Details of the Better Payment Practice Code are available on the website <http://www.payontime.co.uk>

Statement of Directors' responsibilities

The following Statement sets out the responsibilities of the Directors in relation to the financial statements. The report of the independent auditors, shown on page 7, sets out their responsibilities in relation to the financial statements

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company as at the end of the financial year and of the profit or loss for the financial year. In preparing those financial statements, the Directors are required to

- select appropriate accounting policies and apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether applicable UK accounting standards have been followed, subject to any material departures being disclosed and explained, and
- prepare the financial statements on the going concern basis, unless they consider that to be inappropriate

The Directors are responsible for ensuring that the Company keeps sufficient accounting records to disclose with reasonable accuracy the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for taking reasonable steps to safeguard the assets of the Company and in that context to have proper regard to the establishment of appropriate systems of internal control with a view to the prevention and detection of fraud and other irregularities

The Directors are required to prepare the financial statements and to provide the auditors with every opportunity to take whatever steps and undertake whatever inspections the auditors consider to be appropriate for the purpose of enabling them to give their audit report

The Directors consider that they have pursued the actions necessary to meet their responsibilities as set out in this statement

British-American Tobacco (Holdings) Limited

Directors' report

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

- (1) to the best of his knowledge and belief, there is no relevant audit information of which the Company's auditors are unaware, and
- (2) 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

On behalf of the Board



G C W Cunningham

Assistant Secretary

30 October 2007

Report of the independent auditors to the members of British-American Tobacco (Holdings) Limited

We have audited the financial statements of British-American Tobacco (Holdings) Limited for the year ended 31 December 2006 which comprise the profit and loss account, the balance sheet, the statement of total recognised gains and losses and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of Directors and auditors

The Company's Directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, 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.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements. We also report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2006 and of its profit for the year then ended, the financial statements have been properly prepared in accordance with the Companies Act 1985, and the information given in the Directors' Report is consistent with the financial statements.



PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors
1 Embankment Place
London
WC2N 6RH

30 October 2007

British-American Tobacco (Holdings) Limited

Profit and loss account for the year ended 31 December 2006

		2006	2005
	Note	£'000	Restated £'000
Operating income	2	179,340	222,317
Operating charges	3	(278,202)	(259,393)
Operating loss		(98,862)	(37,076)
Income from shares in subsidiary undertakings		1,016,000	989,000
Investment income from group undertakings		34,744	7,894
Interest payable to group undertakings		(41,317)	(30,427)
Other financing costs	15	(2,089)	(1,641)
Profit on ordinary activities before taxation		908,476	927,750
Taxation on ordinary activities	5	(109)	(85)
Profit for the financial year		908,367	927,665
Dividends paid on equity shares		(750,000)	(618,000)
Increase in reserves		158,367	309,665

All the activities during the year are in respect of continuing operations

There is no difference between the profit on ordinary activities before taxation and the profit for the financial year stated above and their historical cost equivalents

The profit and loss account for the comparative year has been restated following the introduction of FRS 20 as described in note 1(11) to the financial statements

Statement of total recognised gains and losses for the year ended 31 December 2006

	2006	2005
	£'000	Restated £'000
Profit for the year	908,367	927,665
Actuarial gain/(loss) on pension scheme	2,728	(10,805)
Total recognised gains relating to the year	911,095	916,860
Change in accounting policy FRS 20 (note 1(11))	49,862	
Total gains recognised since last annual report	960,957	

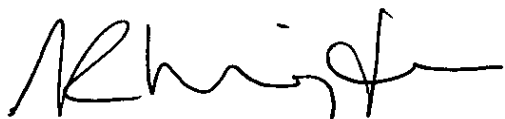
Notes are shown on pages 10 to 25

British-American Tobacco (Holdings) Limited

Balance sheet – 31 December 2006

		2006	2005
	Note	£'000	Restated £'000
Fixed assets			
Tangible assets	6	62,503	62,032
Investments in subsidiary undertakings	7	563,389	629,641
		625,892	691,673
Current assets			
Debtors	8	3,904,449	3,011,601
Creditors amounts falling due within one year	9	(1,787,494)	(2,879,602)
Net current assets		2,116,955	131,999
Total assets less current liabilities		2,742,847	823,672
Creditors amounts falling due after more than one year	10	(2,003,132)	(250,233)
Provisions for liabilities and charges	11	(22,741)	(23,873)
Net assets excluding pensions deficit		716,974	549,566
Pensions deficit	11 & 15	(45,550)	(45,824)
Net assets		671,424	503,742
Capital and reserves			
Called up share capital	12	84,630	84,630
Share premium	13	744	744
Profit and loss account	13	586,050	418,368
Total equity shareholders' funds	14	671,424	503,742

The financial statements on pages 8 to 25 were approved by the Directors on 30 October 2007 and signed on behalf of the Board



N R Withington

Director

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

1 Accounting policies

A summary of the principal accounting policies is set out below

(1) Basis of accounting

The financial statements have been prepared under the historical cost convention and in accordance with UK Generally Accepted Accounting Principles

(2) Cash flow statement

The Company is a wholly-owned subsidiary of British American Tobacco p l c The cash flows of the Company are included in the consolidated cash flow statement of British American Tobacco p l c which is publicly available Consequently the Company is exempt under the terms of Financial Reporting Standard 1 (Revised) from publishing a cash flow statement

(3) Foreign currencies

Transactions arising in currencies other than sterling are translated at the rate of exchange ruling on the date of the transaction Monetary assets and liabilities expressed in currencies other than sterling are translated at rates of exchange ruling at the end of the financial year Non monetary assets expressed in currencies other than sterling which are hedged by a foreign currency liability are translated at rates of exchange ruling at the end of the financial year All exchange differences on non monetary assets hedged by a matching liability are offset in reserves Other exchange differences are taken to the profit and loss account in the year

(4) Accounting for income

Income is included in the profit and loss account when all contractual or other applicable conditions for recognition have been met Provisions are made for bad and doubtful debts, including where delays are anticipated in the receipt of monies from overseas

(5) Taxation

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

Deferred taxation is provided in full on timing differences between the recognition of gains and losses in the financial statements and their recognition in tax computations As allowed by FRS 19 the Group has chosen not to discount deferred tax assets and liabilities

(6) Tangible fixed assets

Tangible fixed assets are stated at cost less depreciation Depreciation is calculated on a straight-line basis to write off the cost of tangible fixed assets over their useful lives Depreciation is charged pro rata based on the month of acquisition and disposal

The rates of depreciation used are

	%
Plant and machinery	7
Motor vehicles	25
Process control and computer equipment	20
Other equipment and fittings	10-20
Leasehold assets	short leases
	Over the period of the lease

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

1 Accounting policies (continued)

(7) Fixed asset investments

Fixed asset investments are stated at cost less provisions for any impairment in value

(8) Leased assets

The annual payments under operating leases are charged to the profit and loss account

(9) Financial instruments

The Company utilises cross-currency swaps as part of its exchange rate management. These cross-currency swaps are revalued at the balance sheet date and used to adjust the book values of the related foreign currency borrowings.

(10) Accounting for pensions

Pension surpluses/deficits as of the balance sheet date are recognised in full as an asset/liability for all pension funds where the Company is the major participant or where it is possible to identify the Company's individual share of the underlying assets and liabilities in the scheme.

The Company participates in several pension schemes, the largest of which, the British American Tobacco UK Pension Fund, is a multi-employer scheme. Under FRS 17, where more than one employer participates in a defined benefit scheme the individual participating employers should account for the scheme as a defined contribution scheme if they are unable to identify their individual shares of the underlying assets and liabilities in the scheme.

The Company is unable to identify its share of the underlying assets and liabilities of the multi-employer British American Tobacco group funded defined benefit scheme and therefore, does not recognise any share of any surplus or deficit in respect of these.

Details of those defined benefit schemes where the Company is the major participator are shown in Note 15.

(11) Change in accounting policy - FRS 20 Employee share schemes

The Company has adopted FRS20 "Share-based payment" in these financial statements. In accordance with the transitional provisions of FRS20, the requirements of FRS20 have been applied to all equity-settled grants that were unvested at 1 January 2006. FRS20 has also been applied to all cash-settled grants not settled as at 1 January 2006. For share-based payments for which the requirements of FRS20 have not been applied, the Company has continued to account for such awards in accordance with UITF Abstract 17. The comparative figures for 2005 have been adjusted accordingly in respect of this accounting policy change.

The Company has both equity-settled and cash-settled compensation plans. With the adoption of FRS20, equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed over the vesting periods, based on the Company's estimate of awards that will eventually vest, with a corresponding credit to reserves.

For cash-settled share based payments, a liability equal to the portion of the services received is recognised at its current fair value determined at each balance sheet date. Fair value is measured by the use of Black-Scholes and Monte-Carlo option pricing models. The expected life used in the models has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

(11) Change in accounting policy - FRS 20 Employee share schemes (continued)

Under UITF Abstract 17, the cost of awards is calculated by reference to the fair value of the shares at the date of the award

The share scheme expense for the year ended 2006 on adoption of FRS20 was £48,184,898 (2005 £53,047,251) The charge would have been £58,747,960 (2005 £50,451,061) under UITF Abstract 17 Shareholders funds at 31 December 2005 were increased by £49,862,000 as a result of applying FRS20 In addition, the effect of the change in accounting policy was to reduce provisions for liabilities and charges for share schemes by £17,820,994 and correspondingly increase shareholders' funds at 31 December 2004 by the same amount

2 Operating income

Operating income comprises technical and advisory fees receivable

3 Operating charges

	2006	2005
	£'000	Restated £'000
Operating leases – buildings	12,266	11,811
Staff costs	166,610	133,164
Depreciation	14,022	17,915
Auditors' fees	1,515	1,672
Other operating charges	83,789	94,831
	278,202	259,393

	2006	2005
	£'000	Restated £'000
Staff costs		
Wages and salaries	87,585	72,174
Social security costs	7,651	7,688
Unfunded defined benefit scheme pension costs	4,957	2,465
Defined contribution scheme costs	299	352
Other pension costs	683	-
Defined benefit scheme treated as defined contribution scheme	66,720	45,000
Contributions from other group undertakings re pension costs	(19,167)	(20,063)
Share based payments expense	48,185	53,047
Contributions from other Group undertakings re share based payments	(30,303)	(27,499)
	166,610	133,164

The average weekly number of persons employed by the Company during the year was

	2006	2005
	Number	Number
Administration	591	635

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

3 Operating charges (continued)

The Company has annual commitments in respect of operating leases as follows

	2006 Building £'000	2005 Building £'000
Beyond 5 years	10,582	10,491
	10,582	10,491

4 Directors' emoluments

The aggregate emoluments of the Directors payable by the Company or its subsidiary undertakings in respect of their services to those companies while Directors of the Company were

	2006 £2,104,760	2005 £1,798,845
Aggregate emoluments		
Amounts (excluding shares) receivable under long term incentive schemes	-	-

	Number	Number
Directors exercising share options during the year	3	3
Directors entitled to receive shares under a long term incentive scheme	3	3
Directors retirement benefits accruing under a defined benefit scheme	3	3

The above figures do not include Messrs P A Rayner and A Monteiro de Castro on the basis that they are paid for their services by the ultimate holding company, British American Tobacco p l c , and details of their remuneration can be found in that Company's annual report and accounts

Highest paid Director	2006	2005
Aggregate emoluments	£779,445	£691,734
Amounts (excluding shares) receivable under long term incentive schemes	-	-
Defined benefit pension scheme		
Accrued pension at the end of the year	£66,458	£79,056
Accrued lump sum at the end of the year	£50,747	£49,331

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

5 Taxation on ordinary activities

(a) Summary of tax on ordinary activities

	2006 £'000	2005 £'000
UK Corporation Tax		
Comprising		
- current tax at 30.00% (2005 30 00%)	-	-
Overseas tax	109	85
Total current taxation <i>note 5(b)</i>	109	85

(b) Factors affecting the tax charge

The current taxation charge differs from the standard 30 00 per cent rate of Corporation Tax in the UK
The major causes of this difference are listed below

	2006 £'000	2005 Restated £'000
Profit on ordinary activities before taxation	908,476	927,750
Corporation Tax at 30.00% (2005 30 00%) on profit on ordinary activities	272,543	278,325
Factors affecting the tax rate		
Group loss relief (claimed)/surrendered for nil consideration	(4,422)	2,364
Permanent differences	36,679	16,011
Overseas withholding taxes	109	85
Corporate income tax relief on intra-group dividends	(304,800)	(296,700)
Total current taxation charge <i>note 5(a)</i>	109	85

An amount of £58,732,000 (2005 £19,850,599) (tax amount of £17,619,600 (2005 £5,955,180)) included in permanent differences above represents tax adjustments in respect of UK to UK transfer pricing

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

6 Tangible fixed assets

	Short leasehold land and buildings £'000	Plant, machinery and equipment £'000	Assets in the course of construction £'000	Total £'000
Cost				
At 1 January 2006	41,924	94,207	10,886	147,017
Additions	2	3,131	16,168	19,301
Reallocation	-	1,448	(1,448)	-
Disposals	-	(1,752)	(4,541)	(6,293)
At 31 December 2006	41,926	97,034	21,065	160,025
Depreciation				
At 1 January 2006	15,900	69,085	-	84,985
Charge for the year	2,466	11,556	-	14,022
Disposals	-	(1,485)	-	(1,485)
At 31 December 2006	18,366	79,156	-	97,522
Net book value				
At 31 December 2006	23,560	17,878	21,065	62,503
At 31 December 2005	26,024	25,122	10,886	62,032

The Company had no capital commitments at 31 December 2006 (2005 £nil)

7 Investments in subsidiary undertakings

(1) Shares in subsidiaries

<u>Unlisted – registered in England</u>	% equity shares held
British American Tobacco (Investments) Limited	100
Louisville Securities Limited	100
South Western Nominees Limited	100

The Company has taken advantage of the exemption under s231(5) of the Companies Act 1985 by providing information only in relation to subsidiary undertakings whose results or financial position, in the opinion of the Directors, principally affected the figures shown in the financial statements

(2) Shareholdings at cost less provisions

	£'000
1 January 2006	629,641
Exchange translation difference	(65,452)
Disposal	(800)
31 December 2006	563,389

The disposal of £800,000 relates to the liquidation of Companhia Continental de Cigarros Limited

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

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

8 Debtors

	2006 £'000	2005 £'000
Amounts due from group undertakings	3,873,859	2,972,474
Other debtors	614	498
Prepayments and accrued income	29,976	38,629
	3,904,449	3,011,601

Amounts due from group undertakings include £348.1m of interest bearing amounts. The interest rate for the year was variable between 4.5% and 4.8%. Also included in amounts due from group undertakings are loans of \$429.6m and \$915m which are both due after more than one year, interest free and unsecured. All other amounts are unsecured, interest free and repayable on demand.

9 Creditors: amounts falling due within one year

	2006 £'000	2005 Restated £'000
Amounts due to group undertakings	1,748,935	2,841,843
Accrued charges and deferred income	38,559	37,759
	1,787,494	2,879,602

Amounts due to group undertakings are unsecured, interest free and repayable on demand.

10 Creditors: amounts falling due after more than one year

	2006 £'000	2005 £'000
Loans from group undertakings	2,003,132	250,233

The loans from group undertakings include a US dollar borrowing of \$429.6m which is repayable in 2008 with interest calculated at USD 6 month LIBOR plus 0.625% and a US dollar borrowing of \$915m which is repayable in 2011 with interest calculated at USD 6 month LIBOR plus 1.4%. Also included are borrowings of \$915m and £577.5m which are repayable in 2011, and borrowings of £271.1m which are repayable in 2008, all of which are unsecured and interest free.

11 Provisions for liabilities and charges

	Share Schemes £'000	Pensions £'000
1 January 2006 – as previously reported	72,316	45,824
Change in accounting policy FRS 20 (note 1(11))	(48,443)	-
1 January 2006 - as restated	23,873	45,824
Provided in respect of the year	11,378	2,212
Transfers from fellow group undertakings (note 15)	-	242
Utilised during the year	(12,510)	-
Other movements	-	(2,728)
31 December 2006	22,741	45,550

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

12 Called up share capital

Ordinary shares of £1 each	2006	2005
Authorised - value	£84,630,700	£84,630,700
- number	84,630,700	84,630,700
Allotted, called up and fully paid		
- value	£84,630,122	£84,630,122
- number	84,630,122	84,630,122

13 Reserves

	Share premium account £'000	Profit and loss account £'000	Total £'000
1 January 2006 – as previously reported	744	368,506	369,250
Change in accounting policy FRS 20 (Note 1(11))	-	49,862	49,862
1 January 2006 – as restated	744	418,368	419,112
Profit for the financial year	-	908,367	908,367
Actuarial gain on pension scheme	-	2,728	2,728
Exercise of equity-settled shares	-	(34,547)	(34,547)
Equity share scheme expense	-	41,134	41,134
Dividends - interim paid	-	(750,000)	(750,000)
31 December 2006	744	586,050	586,794

14 Reconciliation of movements in shareholders' funds

	2006 £'000	2005 £'000
Profit for the year – as previously reported		930,261
Change in accounting policy FRS 20 (Note 1(11))		(2,596)
Profit for the year – as restated	908,367	927,665
Actuarial gain/(loss) on pension scheme	2,728	(10,805)
Exercise of equity-settled shares	(34,547)	-
Equity share scheme expense	41,134	34,637
Dividends paid	(750,000)	(618,000)
Net transfer to/(offset against) shareholders' funds	167,682	333,497
Opening shareholders' funds – as previously reported	453,880	152,424
Change in accounting policy FRS 20 (Note 1(11))	49,862	17,821
Opening shareholders' funds – as restated	503,742	170,245
Closing shareholders' funds	671,424	503,742

British-American Tobacco (Holdings) Limited

Notes to the accounts - 31 December 2006

15 Pensions

The Company participates in several pension schemes, the largest of which, the British American Tobacco UK Pension Fund is a multi-employer scheme. Under FRS 17, where more than one employer participates in a defined benefit scheme the individual participating employers should account for the scheme as a defined contribution scheme if they are unable to identify their individual shares of the underlying assets and liabilities in the scheme. The Company is unable to identify its share of the underlying assets and liabilities of the multi-employer British American Tobacco group funded defined benefit schemes and therefore, does not recognise any share of any surplus or deficit in respect of these.

The last full actuarial valuation of the British American Tobacco UK Pension Fund was carried out as at 31 March 2005 by a qualified independent actuary. This has been updated to 31 December 2006 and a net deficit on this fund of £209,965,000 (2005 £359,617,000) was identified.

On 1 April 2005 the UK defined benefit schemes were closed to new employees who are now eligible to join a defined contribution pension scheme, the cost to Company for which was £299,000 (2005 £352,000).

Under FRS 17 the Company is required to report its liabilities in respect of certain unfunded defined benefit pension schemes where the Company is the major participator. At 31 December 2006 these amounted to £45,550,000 (2005 £45,824,000) as shown below.

The total operating pension cost to the Company, including charges in respect of unfunded defined benefit pensions, was £53,492,000 (2005 £27,754,000).

In respect of the unfunded scheme the major assumptions used by the actuary were

	2006	2005	2004
Rate of increase in salaries	5.1%	5.0%	4.8%
Rate of increase in deferred and pensions in payment	3.1%	3.0%	2.8%
General inflation	3.1%	3.0%	2.8%
Discount rate	5.1%	4.7%	5.3%

The liabilities of the schemes were

	2006 £'000	2005 £'000	2004 £'000
Present value of scheme liabilities	(45,550)	(45,824)	(32,449)
Net deficit in scheme	(45,550)	(45,824)	(32,449)
Related deferred tax assets	-	-	-
Net pension liabilities	(45,550)	(45,824)	(32,449)

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

15 Pensions (continued)

The movements in the net recognisable deficit were as follows

	2006 £'000	2005 £'000	2004 £'000
Net recognisable deficit as at 1 January	(45,824)	(32,449)	(27,327)
Current service cost	(4,957)	(2,465)	(1,839)
Settlements and curtailments	3,170	-	-
Transfers from other group companies	(242)	-	-
Interest on scheme liabilities	(2,089)	(1,641)	(1,476)
Benefits paid	1,664	1,536	1,549
Actuarial gain/(losses)	2,728	(10,805)	(3,356)
Net recognisable deficit as at 31 December	(45,550)	(45,824)	(32,449)

Analysis of amount charged to the profit and loss	2006 £'000	2005 £'000
Operating profit		
– current service cost	(4,957)	(2,465)
– Total operating charge	(4,957)	(2,465)
Other financing costs		
– interest on scheme liabilities	(2,089)	(1,641)
– Net return	(2,089)	(1,641)

Analysis of amounts recognised in statement of total recognised gains and losses	2006 £000	2005 £000	2004 £000	2003 £000	2002 £000
Experience gains/(losses) on scheme liabilities	533	(2,005)	(2,491)	751	(377)
Changes in assumptions underlying present value of scheme liabilities	2,195	(8,800)	(865)	(1,503)	(97)
Actuarial gain/(loss) recognised in statement of total recognised gains and losses	2,728	(10,805)	(3,356)	(752)	(474)

Details of experience gains and losses for the year to 31 December

	2006 £'000	%	2005 £'000	%	2004 £'000	%
Experience gains/(losses) on scheme liabilities	533		(2,005)		(2,491)	
– percentage of present value of scheme liabilities		1		4		8
Net actuarial gain/(loss)	2,728		(10,805)		(3,356)	
– percentage of present value of scheme liabilities		6		24		10

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

16 Share Based Payments

During the period ended 31 December 2006, the following share-based payment arrangements existed, which are described below

Type of arrangement	Long Term Incentive Plan	Deferred Share Bonus Scheme	Sharesave Scheme	Share Option Scheme	Share Reward Scheme
Timing of grant	Annually in March (2005 - May)	Annually in March	Annually in November	See note (a)	Annually in April
Number of options granted in 2006	2,533,526	1,716,736	3 year - 126,844/ 5 year - 154,664	n/a	334,738
Number of options granted in 2005	3,334,893	2,192,747	3 year - 224,885/ 5 year - 190,160	n/a	305,888
Fair value per share for 2006 grant	£10 10	£13 00	3 year - £3 65/ 5 year - £3 91	n/a	£13 85
Fair value per share for 2005 grant	£7 29	£8 12	3 year - £3 12/ 5 year - £3 33	n/a	£9 31
Method of settlement	Both equity and cash-settled grants	Both equity and cash-settled grants	Equity	Both equity and cash-settled grants	Equity
Contractual life	10 years	3 years	3 5 or 5 5 years	10 years	3 years
Vesting conditions	See note (b)	See note (c)	See note (d)	See note (e)	See note (f)

Notes

(a) The granting of options under this scheme ceased with the last grant made in March 2004. Eligible individuals are entitled to participate in the Long Term Incentive Plan and Deferred Share Bonus Scheme.

(b) Nil-cost options in British American Tobacco p l c shares exercisable three years from date of grant, with payout subject to performance conditions based on earnings per share relative to inflation (50 per cent of grant) and total shareholder return, combining the share price and dividend performance of the British American Tobacco p l c by reference to two comparator groups (50 per cent of grant). Participants are not entitled to dividends from British American Tobacco p l c prior to the exercise of the options. For grants made in 2005 and thereafter, a cash equivalent dividend will accrue through the vesting period and will be paid on vesting.

(c) Free shares in British American Tobacco p l c released three years from date of grant and may be subject to forfeit if participant leaves employment before the end of three year holding period. Participants receive a separate payment equivalent to a proportion of the British American Tobacco p l c dividend during the holding period.

(d) Options in British American Tobacco p l c shares granted at invitation at a 20 per cent discount to the market price. Options are exercisable at the end of a three or five year savings contract. Participants are not entitled to British American Tobacco p l c dividends prior to the exercise of the options.

(e) Options in British American Tobacco p l c exercisable three years from date of grant and subject to earnings per share performance condition relative to inflation. Participants are not entitled to receive British American Tobacco p l c dividends in the period prior to the exercise of the options.

(f) Free British American Tobacco p l c shares granted (maximum £3,000 in any year) subject to three year holding period and may be subject to forfeit if employee leaves within this period. Participants are entitled to receive British American Tobacco p l c dividends during the holding period, which are re-invested to buy further shares.

During the period, the Company operated a Partnership Share Scheme, which was open to all eligible employees, where employees can allocate part of their pre-tax salary to purchase shares in British American Tobacco p l c. The maximum amount that can be allocated in this way to any individual is £1,500 in any tax year. The shares purchased are held in a UK-based trust and are normally capable of transfer to participants tax free after a five year holding period.

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

16 Share Based Payments (continued)

Further details on the operation of share-based payment arrangements can be found in the Remuneration Report in the 2006 Annual Review for the British American Tobacco Group

Share Option Schemes

Details of the movements for equity-settled share option schemes during the years ended 31 December 2006 and 31 December 2005 covering the Share Option and Sharesave schemes were as follows. The last of the former B A T Industries Employee Share "E" Option Scheme shares were exercised in 2005.

	2006		2005	
	Number of options	Weighted average exercise price per share (£)	Number of options	Weighted average exercise price per share (£)
Outstanding at start of year	12,648,695	6.39	17,352,182	5.97
Granted during the period	281,508	11.52	415,045	9.77
Exercised during the period	(4,234,650)	5.75	(4,864,295)	5.20
Forfeited during the period	(245,872)	7.01	(254,237)	5.89
Outstanding at end of year	8,449,681	6.86	12,648,695	6.39
Exercisable at end of year	3,626,882	5.55	3,267,697	5.19

In addition to the above options, the movement in nil-cost equity-settled options from the Long Term Incentive Plan was as follows:

	2006	2005
	Number of options	Number of options
Outstanding at start of year	9,403,252	9,851,735
Granted during the period	2,224,313	3,099,082
Exercised during the period	(2,478,316)	(2,078,722)
Forfeited during the period	(1,040,994)	(1,468,843)
Outstanding at end of year	8,108,255	9,403,252
Exercisable at end of year	922,014	744,082

The weighted average British American Tobacco plc share price at the date of exercise for share options exercised during the period was £13.94 (2005 £10.05). A detailed breakdown of the range of exercise prices for options outstanding for the years ended 31 December 2006 and 31 December 2005 is shown in the table below:

Range of exercise prices	2006			2005		
	Number outstanding at end of year	Weighted average remaining contractual life (in years)	Weighted average exercise price per share (£)	Number outstanding at end of year	Weighted average remaining contractual life (in years)	Weighted average exercise price per share (£)
Nil cost	8,108,255	7.8	n/a	9,403,252	8.0	n/a
£2.53 to £4.99	389,805	2.0	3.19	966,689	1.8	3.46
£5.00 to £6.99	3,908,880	4.1	5.74	7,330,469	5.5	5.81
£7.00 to £8.99	3,488,622	6.4	7.83	3,936,492	7.4	7.83
£9.00 to £12.50	662,374	3.9	10.51	415,045	4.4	9.77
Total	16,557,936	6.4	3.50	22,051,947	6.7	3.66

The weighted average fair value of equity-settled Share Option Schemes' granted during 2006 were £9.39 (2005 £6.81).

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

16 Share Based Payments (continued)

Assumptions used in the Black-Scholes models to determine the fair value of share options at grant date were as follows

	2006		2005	
	Long Term Incentive Plan	Sharesave Schemes*	Long Term Incentive Plan	Sharesave Schemes*
Share price at date of grant (£)	14 34	14 40	10 37	12 21
Exercise price (£)	Nil cost	11 52	Nil cost	9 77
Volatility (%)	23	21	27	24
Average expected term to exercise (yrs)	3 5	3 2/5 2	3 5	3 2/5 2
Risk free rate (%)	4 4	4 9/4 8	4 3	4 2/4 2
Expected dividend yield (%)	3 3	3 4	4 0	3 5

*Where two figures have been quoted for the Sharesave schemes, the first number represents the assumptions for the three-year savings contract and the second number for the five-year savings contract

Market condition features were incorporated into Monte-Carlo models for the total shareholder return elements of the Long Term Incentive Plan, in determining fair value at grant date. Assumptions used in these models were as follows

	2006 %	2005 %
Average share price volatility FTSE 100 comparator group	31	34
Average share price volatility FMCG comparator group	23	26
Average correlation FTSE 100 comparator group	26	24
Average correlation FMCG comparator group	18	16

The expected British American Tobacco p l c share price volatility was determined taking account of the daily share price movements over a five year period. The respective FMCG and FTSE 100 share price volatility and correlations were also determined over the same periods. The average expected term to exercise used in the models has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural conditions, forfeiture and historical experience.

The risk free rate has been determined from market yield curves for government gilts with outstanding terms equal to the average expected term to exercise for each relevant grant. The expected British American Tobacco p l c dividend yield was determined by calculating the yield from the last two declared dividends divided by the grant share price.

For grants containing earnings per share performance conditions, the payout calculation is based on the average of expectations published in analysts' forecasts.

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

16 Share Based Payments (continued)

Other equity share-based payment arrangements (other than share options)

Details of the movements of other equity share-based payment arrangements during the years ended 31 December 2006 and 31 December 2005, covering the Deferred Share Bonus and Share Reward Schemes, were as follows

	2006	2005
	Number of shares	Number of shares
Outstanding at start of year	7,001,271	7,284,592
Granted during the period	1,959,868	2,310,273
Exercised during the period	(3,037,981)	(2,461,386)
Forfeited during the period	(89,287)	(132,208)
Outstanding at end of year	5,833,871	7,001,271
Exercisable at end of year	383,294	643,825

The shares outstanding for the year ended 31 December 2006 had a weighted average contractual life of 1.1 years (2005 1.1 years)

The fair value for other equity share-based payment arrangements granted during the period was determined using the Black-Scholes model with the following input assumptions at their grant date

	2006		2005	
	Deferred Share Bonus Scheme	Share Reward Scheme	Deferred Share Bonus Scheme	Share Reward Scheme
Grant price (£)	14.34	13.85	9.29	9.31
Expected volatility (%)	23	23	30	30
Average expected term to exercise (yrs)	3	5	3	5
Risk free rate (%)	4.4	4.5	4.8	4.7
Expected dividend yield (%)	3.3	3.4	4.5	4.5

The weighted average fair value of other equity share-based payment arrangements granted during 2006 were £13.14 (2005 £8.27)

Cash-settled share-based payment arrangements

The Company issues to certain employees cash-settled share-based payments that require the Company to pay the intrinsic value of these share-based payments to the employee at the date of exercise. The Group has recorded liabilities at the end of 2006 of £11,660,579 (2005 £12,664,895) of which £3,456,071 (2005 £2,698,902) was in respect of vested grants. Fair value was determined from the Black-Scholes and Monte-Carlo models, using assumptions revised at the balance sheet date for cash-settled share-based payment arrangements. The Company recorded total expenses of £2,619,127 in 2006 (2005 £8,971,389).

Details of movements for cash-settled arrangements in respect of the Share Option scheme, during the years ended 31 December 2006 and 31 December 2005, are as follows

	2006		2005	
	Number of options	Weighted average exercise price per share (£)	Number of options	Weighted average exercise price per share (£)
Outstanding at start of year	1,057,496	6.40	1,859,995	6.35
Granted during the period	n/a	n/a	n/a	a/a
Exercised during the period	(605,634)	6.19	(774,940)	6.28
Forfeited during the period	(20,582)	6.69	(27,559)	6.21
Outstanding at end of year	431,280	6.69	1,057,496	6.40
Exercisable at end of year	313,101	6.17	375,833	6.38

British-American Tobacco (Holdings) Limited

Notes to the accounts – 31 December 2006

16 Share Based Payments (continued)

In addition to the above, the movement in other nil-cost cash-settled arrangements during the years ended 31 December 2006 and 31 December 2005, covering the Long Term Incentive Plan and Deferred Share Bonus Scheme, are as follows

	2006	2005
	Number of shares	Number of shares
Outstanding at start of year	1,000,264	1,030,400
Granted during the period	400,819	424,173
Exercised during the period	(238,566)	(408,380)
Forfeited during the period	(56,683)	(45,929)
Outstanding at end of year	1,105,834	1,000,264
Exercisable at end of year	63,934	16,190

Assumptions used to determine the fair value of cash-settled share-based payment arrangements at date of grant, can be found in the sections relating to Share Option schemes and other equity share-based payment arrangements

The weighted average British American Tobacco share price at the date of exercise for cash-settled share-based arrangements exercised during the period was £14.05 (2005 £10.05). A detailed breakdown of the range of exercise prices for cash-settled share-based payment arrangements outstanding at the end of 31 December 2006 is shown in the table below

	2006			2005		
Range of exercise prices	Number outstanding at end of year	Weighted Average Remaining Contractual Life (in years)	Weighted average exercise price per share (£)	Number outstanding at end of year	Weighted Average Remaining Contractual Life (in years)	Weighted average exercise price per share (£)
Price						
Nil cost	1,105,834	6.1	n/a	1,000,264	5.4	n/a
£5.60 to £5.98	163,481	6.1	5.97	546,929	7.1	5.98
£6.39 to £8.09	267,799	6.0	7.14	510,567	6.7	6.86
Total	1,537,114	6.1	1.88	2,057,760	6.2	3.29

Share-based payment expense

The amounts recognised in the income statement in respect of share-based payments were as follows

	2006	2005
	£	£
Equity-settled share-based payments	41,133,860	34,636,566
Cash-settled share-based payments	2,619,126	8,971,389
UITF Abstract 17 (revised 2003)	-	4,083,484
Employers NI Charge	4,431,912	5,355,812
Total amount recognised in profit and loss account on page 8	48,184,898	53,047,251

In addition to the above share-based payment expense, for the year ending 31 December 2006, BAT Holdings Limited recharged £30,303,681 (2005 £27,498,583) to other Group companies, for share scheme related costs based on the fair value calculated at award date, for awards granted during the year

British-American Tobacco (Holdings) Limited

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17 Related parties

Transactions with related parties have been aggregated by nature of transaction and were as follows

	2006 £'000	2005 £'000
Transactions with associates and joint ventures of the British American Tobacco p l c Group		
Other charges	(1,822)	-
Other income	-	-

The associates referred to are

Reynolds American Inc

The Company has taken advantage of the exemption under paragraph 3(c) of FRS 8 from disclosing transactions with other subsidiary undertakings of the British American Tobacco p l c Group

18 Parent undertakings

The Company's ultimate parent undertaking is British American Tobacco p l c being incorporated in the United Kingdom and registered in England and Wales. Its immediate parent undertaking is B A T Industries p l c. Group accounts are prepared only at the British American Tobacco p l c level.

19 Copies of the Report and Accounts

Copies of the Report and Accounts of British American Tobacco p l c may be obtained from

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