

**Nicoventures Limited**

**Registered Number 07412694**

**Directors' report and financial statements**

**For the year ended 31 December 2012**



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## Directors' report

The Directors present their report together with the audited financial statements of the Company for the year ended 31 December 2012

### Principal activities

The Company focuses exclusively on the development and commercialisation of innovative regulatory approved nicotine products that provide a consumer-acceptable alternative to cigarettes

### Review of the year ended 31 December 2012

The loss for the financial year attributable to Nicoventures Limited shareholders after deduction of all charges and the provision of taxation amounted to £12,609,000 (19 October 2010 to 31 December 2011 £9,750,000)

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

### Going concern

The Directors believe that preparing the financial statements on the going concern basis is appropriate due to the continued financial support of its immediate parent undertaking British American Tobacco (1998) Limited. This support is expected to continue for the foreseeable future. The Directors confirm that they have complied with the above requirements in preparing the financial statements

### Key performance indicators

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 Business Review section in the Annual Report 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, including financial risk management, 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 Report of British American Tobacco plc, and do not form part of this report

### Dividends

The Directors do not recommend the payment of a dividend for the year (19 October 2010 to 31 December 2011 £nil)

## Directors' report

### 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 signing this report are as follows

	Appointed	Resigned
Charl Erasmus Steyn		9 February 2013
Steven Glyn Dale		8 February 2013
Michael Charles Terrell Prideaux		8 February 2013
Adrian John Anthony Marshall		28 June 2013
Roy Duncan Chambers		28 August 2013
Steven James Burton		28 August 2013
Kevin Arthur Bridgman	8 February 2013	
Peter Simon Charles Cleverly	28 August 2013	
Douglas James Lafferty	28 August 2013	
Desmond John Naughton	28 August 2013	
Philippe Zell	28 August 2013	

### Research and development

The Company is currently undertaking development into innovative regulatory nicotine products that provide a consumer acceptable alternative to cigarettes without the real and serious health risks of smoking

### 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, and
- avoid any delays when legitimately questioning invoices

The proportion which the amount owed to trade creditors at 31 December 2012 in relation to the amounts invoiced by suppliers during the year equated to a 37 days proportion of 366 days (19 October 2010 to 31 December 2011 39 days)

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

## Directors' report

### Statement of Directors' responsibilities

The Directors are responsible for preparing the Directors' report and the financial statements in accordance with applicable law and regulations

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the financial statements in accordance with 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 Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to

- Select suitable accounting policies and then apply them consistently,
- Make judgements and accounting estimates that are reasonable and prudent,
- State whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

The Directors confirm that they have complied with the above requirements in preparing the financial statements

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

### 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

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

(b) 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

By order of the Board



S. Ellis  
Secretary

23 September 2013

## **Independent auditors' report to the members of Nicoventures Limited**

We have audited the financial statements of Nicoventures Limited for the year ended 31 December 2012 which comprise the Profit and loss account, the Balance sheet and the related notes. 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 Statement of Directors' responsibilities set out on page 4, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and 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 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 financial statements

- Give a true and fair view of the state of the Company's affairs as at 31 December 2012 and of its loss for the year then ended,
- 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 financial statements are prepared is consistent with the financial statements.

Nicoventures Limited

## Independent auditors' report to the members of Nicoventures Limited

### 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, or returns adequate for our audit have not been received from branches not visited by us, or
- The financial statements are not in agreement with the accounting records and returns, 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



James Parker

Senior Statutory Auditor

For and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

1 Embankment Place

London

25 September 2013

## Profit and loss account for the year ended 31 December 2012

			19 October 2010 to 31 December
		2012	2011
Continuing operations		£'000	£'000
	Note		
Other operating charges	2	(12,593)	(9,800)
<b>Operating loss</b>		<b>(12,593)</b>	<b>(9,800)</b>
Interest receivable and similar income	3	11	50
Interest payable and similar charges	4	(27)	-
<b>Loss on ordinary activities before taxation</b>		<b>(12,609)</b>	<b>(9,750)</b>
Tax on loss on ordinary activities	5	-	-
<b>Loss for the financial year</b>	10	<b>(12,609)</b>	<b>(9,750)</b>

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

There are no recognised gains or losses other than the loss for the financial year and therefore no Statement of total recognised gains or losses has been presented

The accompanying notes are an integral part of the financial statements

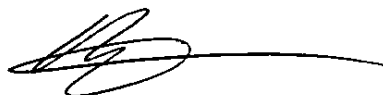


Nicoventures Limited

**Balance sheet at 31 December 2012**

	Note	<b>2012</b> <b>£'000</b>	2011 £'000
<b>Fixed assets</b>			
Tangible assets	6	<b>2,020</b>	-
		<b>2,020</b>	-
<b>Current assets</b>			
Debtors amounts falling due within one year	7a	<b>886</b>	8,382
Debtors amounts falling due after one year	7b	<b>2,000</b>	-
Creditors amounts falling due within one year	8	<b>(12,265)</b>	(3,132)
<b>Net current (liabilities)/assets</b>		<b>(9,379)</b>	5,250
<b>Total assets less current liabilities</b>		<b>(7,359)</b>	5,250
<b>Capital and reserves</b>			
Called up share capital	9	<b>15,000</b>	15,000
Profit and loss account	10	<b>(22,359)</b>	(9,750)
<b>Total shareholders' (deficit)/funds</b>	11	<b>(7,359)</b>	5,250

The financial statements on pages 7 to 19 were approved by the Directors on 23 September 2013 and signed on behalf of the Board



D J Lafferty  
Director

**Registered number 07412694**

The accompanying notes are an integral part of the financial statements

## Notes to the financial statements for the year ended 31 December 2012

### 1 Accounting policies

#### Basis of accounting

The financial statements are prepared on the going concern basis, under the historical cost convention, and in accordance with the Companies Act 2006 and applicable accounting standards in the United Kingdom

The principal accounting policies have been applied consistently throughout the year and a summary is set out below

#### 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 has taken advantage of the exemption from preparing a cash flow statement under the terms of FRS1 (revised 1996) 'Cash flow statements'

#### 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. All exchange differences are taken to the profit and loss account in the year.

#### 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.

## Notes to the financial statements for the year ended 31 December 2012

### 1 Accounting policies (continued)

#### Tangible assets

Tangible assets are stated at cost less accumulated depreciation. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Depreciation is calculated on a straight-line basis to write off the cost of tangible assets over their useful lives. Depreciation is charged pro rata based on the month of acquisition and disposal.

Assets in the course of construction are not depreciated until brought into operational use.

#### Operating leases

The annual payments under operating leases are charged to the profit and loss account on a straight line basis over the length of the lease term.

#### Employee share schemes

The Company is recharged by British-American Tobacco Holdings Limited, a fellow group company, for the cost of share schemes to which its employees belong. This recharge is expensed in the year incurred. The recharge in the year ended 31 December 2012 was £457,000 (19 October 2010 to 31 December 2011: £nil) as disclosed in note 2 other operating charges. The fellow Group company, which administers the share schemes on behalf of other group companies, calculates and reflects the charge for the share schemes, provides the relevant disclosures required under FRS 20.

#### Retirement benefits

The Company participates in several pension schemes, the largest of which, the British American Tobacco UK Pension Fund, is a multi-employer pension 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.

The Company also operates a defined contribution scheme. Payments in respect of defined contribution schemes are charged to the profit and loss account as they fall due.

#### Research and development

Research and development expenditure is charged to the profit and loss account as incurred.

## Notes to the financial statements for the year ended 31 December 2012

### 2 Other operating charges

	2012	19 October 2010 to 31 December 2011
	£'000	£'000
<b>Other operating charges comprise:</b>		
Staff costs	4,117	1,885
Exchange (gains)/losses	(2)	1
Operating lease charges		
- buildings	128	-
Research and development costs	1,992	5,614
Other	6,358	2,300
	<b>12,593</b>	<b>9,800</b>

#### Staff costs:

Wages and salaries	2,729	1,556
Other staff costs	286	13
Social security costs	370	212
Share-based payments (note 13)	457	-
Defined contribution scheme costs (note 12)	146	34
Other pension costs (note 12)	129	70
	<b>4,117</b>	<b>1,885</b>

Auditors' fees of £2,500 were borne by a fellow Group undertaking (19 October 2010 to 31 December 2011 £2,500)

The average monthly number of persons (including Directors) employed by the Company was

	2012	19 October 2010 to 31 December 2011
	Number	Number
Administration	12	5

The aggregate emoluments of the Directors payable by the Company in respect of their services to the Company were as follows

	2012	19 October 2010 to 31 December 2011
	£'000	£'000
Aggregate emoluments	414	373
	Number	Number
Directors exercising share options during the year	1	1
Directors entitled to receive shares under a long term incentive scheme	1	1
Directors retirement benefits accruing under a defined benefit scheme	1	1

## Notes to the financial statements for the year ended 31 December 2012

### 2 Other operating charges (continued)

#### Highest paid Director

	19 October 2010 to 31 December	
	2012	2011
	£'000	£'000
Aggregate emoluments	414	373
Defined benefit pension scheme		
Accrued pension at the end of year	139	54

During 2012 and 2011, the highest paid Director was entitled to receive shares under a long term incentive scheme and exercised share options during the year

At 31 December, the Company had annual commitments in respect of non-cancellable operating leases expiring as follows

	Land and buildings	
	2012	2011
	£'000	£'000
2 – 5 years	129	-

### 3 Interest receivable and similar income

	19 October 2010 to 31 December	
	2012	2011
	£'000	£'000
Interest receivable from Group undertakings	11	50

### 4 Interest payable and similar charges

	19 October 2010 to 31 December	
	2012	2011
	£'000	£'000
Interest payable to Group undertakings	27	-

# Notes to the financial statements for the year ended 31 December 2012

## 5 Tax on loss on ordinary activities

### (a) Summary of taxation on loss on ordinary activities

	2012 £'000	19 October 2010 to 31 December 2011 £'000
<b>Current taxation.</b>		
UK corporation taxation on loss of the year		
Comprising		
- current taxation at 24.5% (19 October 2010 to 31 December 2011 26.74%)	-	-
Total current taxation note 5(b)	-	-

### (b) Factors affecting the taxation charge

The standard rate of corporation taxation in the UK changed from 26.0% to 24.0% with effect from 1 April 2012. Accordingly the Company's loss for this accounting period is taxed at an effective rate of 24.5%.

The current taxation charge differs from the standard 24.5% (19 October 2010 to 31 December 2011 26.74%) rate of corporation taxation in the UK. The major causes of this difference are listed below.

	2012 £'000	19 October 2010 to 31 December 2011 £'000
Loss on ordinary activities before taxation	(12,609)	(9,750)
Corporation taxation at 24.5% (2011 26.74%) on loss on ordinary activities	(3,089)	(2,607)
<b>Factors affecting the taxation rate:</b>		
Permanent differences	3	-
Group loss relief surrendered at less than full consideration	3,086	2,607
Total current taxation note 5(a)	-	-

# Notes to the financial statements for the year ended 31 December 2012

## 6 Tangible assets

	Assets in the course of construction £'000	Total £'000
<b>Cost</b>		
1 January 2012	-	-
Additions	2,020	2,020
<b>31 December 2012</b>	<b>2,020</b>	<b>2,020</b>
<b>Accumulated depreciation</b>		
1 January 2012	-	-
<b>31 December 2012</b>	<b>-</b>	<b>-</b>
<b>Net book value</b>		
1 January 2012	-	-
<b>31 December 2012</b>	<b>2,020</b>	<b>2,020</b>

## 7 Debtors

### (a) Amounts falling due within one year

	2012 £'000	2011 £'000
Amounts owed by Group undertakings	-	7,938
Other debtors	749	444
Prepayments and accrued income	137	-
	<b>886</b>	<b>8,382</b>

Included within amounts owed by Group undertakings is an amount of £nil (2011 £7,612,000) which is unsecured, interest bearing and repayable on demand. The interest rate is based on LIBOR. Other amounts owed by Group undertakings are unsecured, interest free and repayable on demand.

### (b) Amounts falling due after one year

	2012 £'000	2011 £'000
Other debtors	2,000	-

Other debtors are unsecured, interest bearing and repayable over a period of more than one year. The interest rate is fixed at 10% per annum.

# Notes to the financial statements for the year ended 31 December 2012

## 8 Creditors: amounts falling due within one year

	2012 £'000	2011 £'000
Trade creditors	758	1,418
Amounts owed to Group undertakings	10,665	946
Accruals and deferred income	842	768
	<b>12,265</b>	<b>3,132</b>

Included within amounts due to Group undertakings is an amount of £9,474,000 (2011 £nil) which is unsecured, repayable on demand and incurs interest based on LIBOR. Other amounts owed to Group undertakings are unsecured, interest free and repayable on demand.

## 9 Called up share capital

Ordinary shares of £1 each	2012	2011
Allotted, called up and fully paid		
- value	£15,000,002	£15,000,002
- number	15,000,002	15,000,002

## 10 Reserves

	Profit and loss account £'000
1 January 2012	(9,750)
Loss for the financial year	(12,609)
<b>31 December 2012</b>	<b>(22,359)</b>

## 11 Reconciliation of movements in shareholders' (deficit)/funds

	2012 £'000	19 October 2010 to 31 December 2011 £'000
Loss for the financial year	(12,609)	(9,750)
Net proceeds of issue of ordinary share capital	-	15,000
Net movement in shareholders' (deficit)/funds	(12,609)	5,250
Opening shareholders' funds	5,250	-
<b>Closing shareholders' (deficit)/funds</b>	<b>(7,359)</b>	<b>5,250</b>



## Notes to the financial statements for the year ended 31 December 2012

### 12 Pensions

The Company participates in the British American Tobacco UK Pension Fund, which is a multi-employer scheme, in respect of certain employees. Employees are not required to contribute. Details of the latest actuarial valuation of this defined benefit scheme are contained in the financial statements of British-American Tobacco (Holdings) Limited. The last full tri-annual actuarial valuation, calculated using the projected unit basis, of the British American Tobacco UK Pension Fund was carried out as at 31 March 2011 by a qualified independent actuary. The valuation showed that the fund had a deficit of £516,000,000. As at 31 December 2012 the Group valuation of the deficit on an IAS 19 basis was £340,743,000 (2011: £400,251,000). The valuation is not completed on an FRS 17 basis therefore the IAS 19 value is disclosed in accordance with requirements of FRS 17.

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 only participates in multi-employer schemes and the Company is unable to identify its share of the underlying assets and liabilities of the schemes. Therefore, under FRS 17 the Company does not recognise any share of any surplus or deficit in respect of the joint pension schemes.

The defined benefit pension scheme cost was £129,000 (19 October 2010 to 31 December 2011: £70,000) for the year.

The Company also participates in a defined contribution scheme. Payments in respect of defined contribution schemes are charged as an expense as they fall due. The defined contribution pension cost for the company was £146,000 (19 October 2010 to 31 December 2011: £34,000).

There are no amounts prepaid or outstanding in respect of defined benefit or defined contribution schemes in the current financial year or the prior financial period.

### 13 Share-based payments

Employees of the Company participate in the British American Tobacco share schemes arrangements. The Group operates a number of share-based payment arrangements of which the two principal ones are:

#### Long-Term Incentive plan (LTIP)

Nil-cost options exercisable after three years from date of grant with a contractual life of ten years. Payout is 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 Company by reference to two comparator groups (50 per cent of grant). Participants are not entitled to dividends prior to the exercise of the options. A cash equivalent dividend accrues through the vesting period and is paid on vesting. Both equity and cash-settled LTIPs are granted in March each year. In 2012 the Management Board LTIP award was made in May.

#### Deferred Share Bonus Scheme (DSBS)

Free ordinary shares released three years from date of grant and may be subject to forfeit if participant leaves employment before the end of the three year holding period. Participants receive a separate payment equivalent to a proportion of the dividend payment during the holding period. Both equity and cash-settled grants are granted in March each year.

# Notes to the financial statements for the year ended 31 December 2012

## 13 Share-based payments (continued)

The Group also has the following arrangement which is not material for the Group and the Company

### Share Reward Scheme (SRS)

Free shares granted in April each year (maximum £3,000 in any year) under the equity-settled scheme are subject to a three year holding period. Participants receive dividends during the holding period which are reinvested to buy further shares.

### Share-based payment expense

The expense is calculated using the fair value and the shares expected to vest at grant date. However, these conditions and any transfers, early exercises or lapses are not taken into account after this date as they would be under FRS 20 principles. This is due to the cost implications and additional administration required to monitor the movement of Group employees between fellow Group undertakings.

Please refer to the Annual Report of British American Tobacco p.l.c. for full disclosures under IFRS 2.

The amounts recognised in the profit and loss account in respect of share-based payments and the number of options granted in relation to the expense were as follows:

	2012		19 October 2010 to 31 December 2011	
	Equity-settled £000's	Number of shares / options granted	Equity-settled £000's	Number of shares / options granted
LTIP	163	8,533	-	-
DSBS	277	9,709	-	-
SRS	17	527	-	-
Total recognised in the profit and loss account (note 2) / total number of grants	457	18,769	-	-

### Valuation assumptions

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

	2012		19 October 2010 to 31 December 2011	
	LTIP	DSBS	LTIP	DSBS
Expected volatility (%)	25.7	25.7	25.0	25.0
Average expected term to exercise (years)	3.5	3.0	3.5	3.0
Risk-free rate (%)	0.7	0.6	2.0	1.8
Expected dividend yield (%)	3.9	3.9	4.8	4.8
Share price at date of grant (£)	32.08	32.08	23.77	23.77
Fair value at grant date (£)	21.79	28.50	15.60	20.58

## Notes to the financial statements for the year ended 31 December 2012

### 13 Share-based payments (continued)

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

	2012	2011
	%	%
Average share price volatility FTSE 100 comparator group	39.0	40.0
Average share price volatility FMCG comparator group	26.0	26.0
Average correlation FTSE 100 comparator group	38.0	39.0
Average correlation FMCG comparator group	36.0	35.0

Fair values determined from the Black-Scholes and Monte-Carlo models use assumptions revised at the end of each reporting period for cash-settled share-based payment arrangements

The expected British American Tobacco plc share price volatility was determined taking account of the return index, (the share price index plus the dividend reinvested) 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 dividend yield was determined by calculating the yield from the last two declared dividends divided by the grant share price.

In addition to these valuation assumptions, LTIP awards contain earnings per share performance conditions. As these are non-market performance conditions they are not included in the determination of fair value of share options at the grant date, however they are used to estimate the number of awards expected to vest. This payout calculation is based on expectations published in analysts' forecasts.

## Notes to the financial statements for the year ended 31 December 2012

### 14 Related party disclosures

As a wholly owned subsidiary 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

### 15 Contingent liabilities

The Company's ultimate parent undertaking British American Tobacco p l c has guaranteed the liabilities of the British American Tobacco UK Pension Fund, on behalf of the Company and the other participating employers of the scheme. The fund had a deficit according to the last formal tri-annual actuarial valuation in March 2011 of £516,000,000. As at 31 December 2012 the Group valuation of the deficit on an IAS 19 basis was £340,743,000 (2011 £400,251,000). The valuation is not completed on an FRS 17 basis, therefore the IAS 19 value is disclosed in accordance with requirements of FRS 17.

### 16 Parent company support

The intermediate parent undertaking British American Tobacco (1998) Limited has indicated its willingness to continue to provide support to allow the Company to continue at its current level of operations for the foreseeable future.

### 17 Parent undertakings

The Company's 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. The Company's immediate parent undertaking is British American Tobacco (1998) Limited. Group financial statements are prepared only at the British American Tobacco p l c level and may be obtained from

The Company Secretary  
Globe House  
4 Temple Place  
London  
WC2R 2PG