



BRITISH AMERICAN TOBACCO 1999



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Annual Review and Summary Financial Statement

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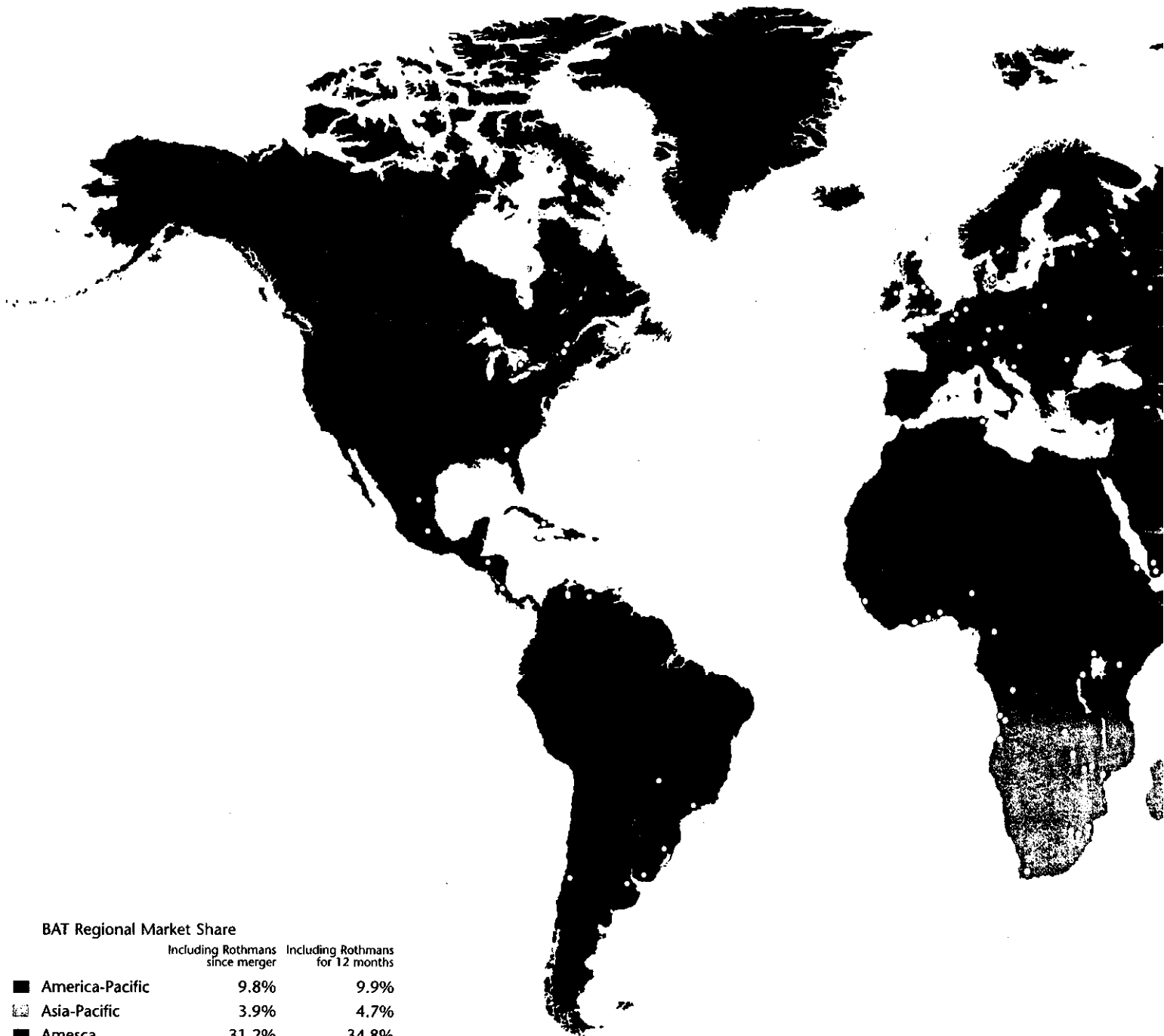
COMPANY NO.: 3407696

Our vision is to become the world's leading international tobacco company.

Since 1994, the Group has grown global market share from 10.7% to 15.4%.

This Annual Review and Summary Financial Statement does not contain sufficient information to allow for a full understanding of the results of the Group and the state of affairs of the Company or of the Group. For further information the full Annual Accounts, the Auditors' Report on those accounts and the Directors' Report should be consulted (see page 30).

The combined British American Tobacco has 97 factories, operating in 66 countries, more than 700 million kilos of tobacco and have 24 growing programmes and 28 le with expertise in Virginia and Blended cigarettes. We have leadership in over 50 mar £13 billion per annum to national exchéquers worldwide through excise duties and t profit after tax.



BAT Regional Market Share

	Including Rothmans since merger	Including Rothmans for 12 months
■ America-Pacific	9.8%	9.9%
■ Asia-Pacific	3.9%	4.7%
■ Amesca	31.2%	34.8%
■ Europe	13.9%	16.0%
■ Latin America	50.1%	50.3%
■ Canada	70.4%	70.4%

Plant Locations

Highlights of the Year



**BRITISH AMERICAN
TOBACCO**

Pre-tax profit	£1,371m	+86%
Earnings per share	25.25p	+14%
Adjusted earnings per share	52.33p	+13%
Dividends per share	26.20p	+9%

- Completion of the Rothmans merger resulting in a major advance in achieving our vision.
- Operating profit before goodwill and exceptional items up 30 per cent to £2,022 million.
- Results benefited from the merger with Rothmans, combined with a good underlying performance.

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Chairman's Statement



Martin Broughton, Chairman and
Kenneth Clarke, Non-executive Deputy Chairman

AS A RESULT OF THE ROTHMANS MERGER, WE MADE A MAJOR ADVANCE IN ACHIEVING OUR VISION DURING 1999. WE ALSO SUCCEEDED IN MANAGING THE BUSINESS ON STRATEGY IN A DIFFICULT ENVIRONMENT, A TASK MADE MORE COMPLEX BY THE MERGER. WE ARE DISAPPOINTED THAT THE REAL PROGRESS WE HAVE MADE HAS NOT BEEN REFLECTED IN OUR SHARE PRICE.

The Group's operating profit before exceptional items grew by 30 per cent to £2,022 million, reflecting seven months' benefit from the merger with Rothmans, combined with a good underlying performance. Pre-tax profit rose 86 per cent to £1,371 million, while adjusted fully diluted earnings per share, probably the best indication of the true improvement, advanced by 13 per cent to 52.3p.

Your Board is recommending a final dividend of 17.9p per share, payable on 3 May. This will take the total dividend growth for the year to 9 per cent, in line with our policy of paying out at least 50 per cent of sustainable earnings.

The major strategic achievements were plainly the Rothmans merger and the highly complex acquisition of our Canadian associate company, Imasco, including the subsequent sale of its non-tobacco businesses on a tax efficient basis. The transaction, which will enable us to integrate Imperial Tobacco of Canada into our operations, was completed in February 2000 and it will materially improve our cash flow this year.

Complexity was also a feature of the Rothmans merger, especially when it came to securing regulatory approval with limited disposals and undertaking corporate restructurings in a number of key markets. The outcome was better than we expected when we announced the merger, except in Canada where the forced sale of the Rothmans business reflected the exceedingly depressed level of tobacco assets. The anticipated £250 million of synergies per annum will be achieved ahead of schedule.

I should like to take this opportunity to welcome Bill Ryan, as Deputy Managing Director, and Johann Rupert and Jan du Plessis, as non-

executives, to the Main Board, where their experience is proving invaluable. We also welcome Tony Jones and Chris Bischoff to the Management Board.

For the tobacco industry, a difficult environment does not, of course, confine itself to the trading conditions covered in the Managing Director's Review. Our two principal legal and regulatory concerns at the moment are the three phase Engle class action in Florida and the World Health Organization's Framework Convention on Tobacco Control (FCTC).

The latter is a potential threat, despite the fact that it represents a developed world obsession being foisted on to the developing world. There are, however, encouraging signs that some significant countries are in favour of a broad convention, allowing governments to take account of their own circumstances, rather than a binding treaty.

We have been analysing the potential impact of the FCTC and believe that it has fundamental

We will build on the **SUCCESS** of the Rothmans merger

flaws. In particular, the proposals conflict with the established principles of good public policy formation and risk undermining governments' sovereignty over tobacco regulations and excise.

Because of the way the Engle class action is being run by the Judge, who is himself a member of the class, investors expect a headline-grabbing punitive damages award in the next month or so and this has affected the share price. We are confident that, in the event of a loss, the companies involved will be able to appeal successfully, without having to post a bond. Despite the blatant pressure applied by the Judge, Brown & Williamson has no intention of settling.

It is also worth stressing that Engle is really something of an exception as, elsewhere on the litigation front, class actions and medical reimbursement cases are consistently being dismissed, despite increasingly novel claims being filed, not least by the US Federal Government.

In terms of creativity, pride of place in a crowded field probably goes to the US plaintiffs' lawyers

who have been able to persuade various Latin American countries and states, as well as Thailand, to sue the tobacco industry in the US, rather than in their own courts. The Guatemala and Thailand cases have already been dismissed and we expect the others to follow suit.

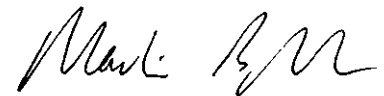
The pressure from regulators and governments who, it must be remembered, make over ten times as much from the sale of cigarettes as we do, seems set to continue. As this new century begins, we are determined to find a constructive way forward, instead of remaining trapped with them in the sterile arguments of the past.

We have, for example, recently presented the UK Government with a coherent set of proposals called "partnership for change", the details of which can be found on the inside back cover.

In a further initiative to improve our ability to communicate directly with all our stakeholders, this Annual Review's publication coincides with the launch of our website. Please visit us at www.bat.com

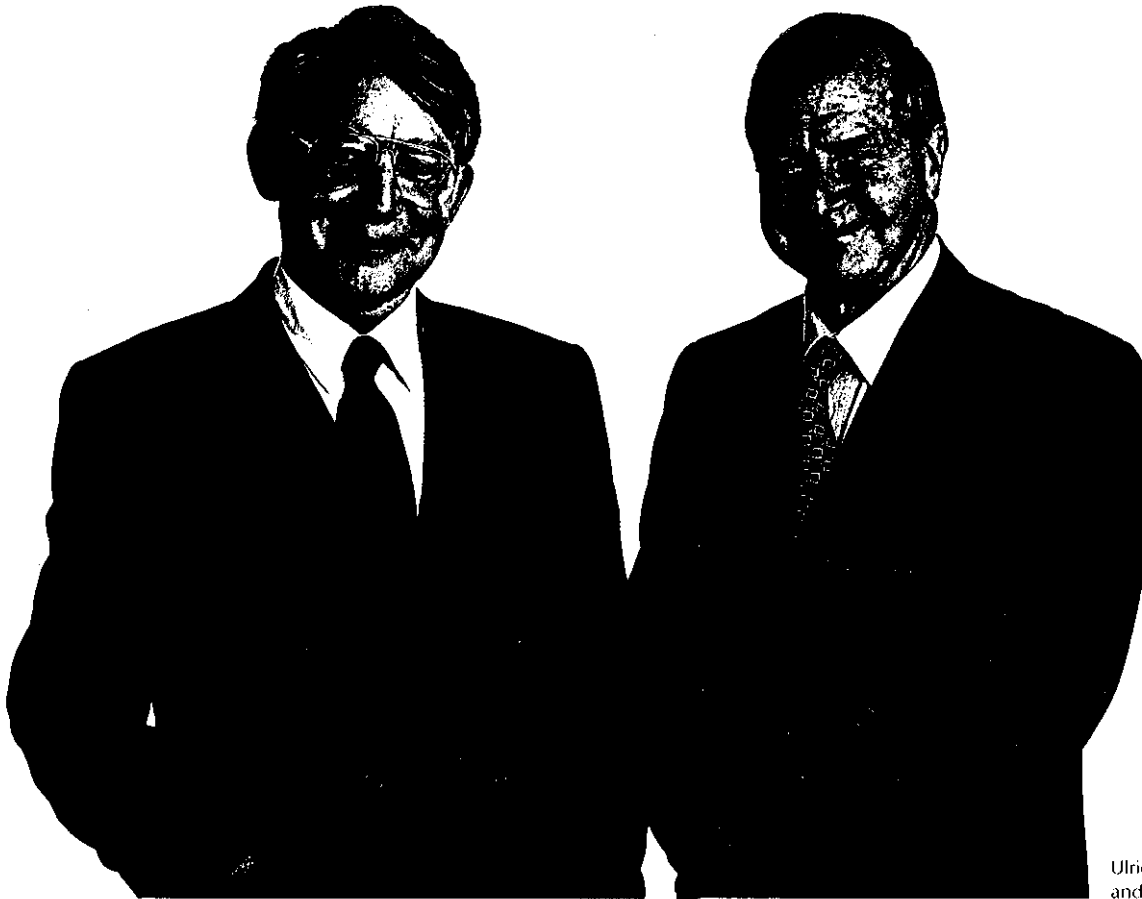
On behalf of the Board, I would like to thank our management teams and employees, around the world and at our headquarters here in the UK, for their unstinting efforts during a momentous year in the Company's development. The way that so many people have risen to additional challenges is an impressive tribute to their commitment.

While we recognise that traditional businesses are currently out of favour with the stock market, our task for 2000 is to work on ensuring that the value we are building for shareholders is actually reflected in the value of our shares. Apart from market share and financial growth targets, our broader objectives include continuing to build on the success of the Rothmans merger, starting to capitalise on the benefits that e-Commerce can offer and making progress in becoming recognised as a responsible company in an industry seen as controversial.



Martin Broughton

Managing Director's Review



Ulrich Herter, Managing Director
and Bill Ryan, Deputy Managing Director

THE FOLLOWING PAGES WILL PROVIDE SHAREHOLDERS WITH A BETTER UNDERSTANDING OF OUR PROGRESS IN 1999 AND HOW WE ARE POSITIONING OURSELVES FOR THE FUTURE, AS WE WORK ON BUILDING THE VALUE OF THE BUSINESS.

Just how difficult conditions were in 1999 can clearly be seen from our early reading of the world market, which is estimated to show a decline of between 2 and 3 per cent. While our volumes rose 5 per cent to 753 billion, there was a 9 per cent decline excluding the Rothmans business, a similar position to our main international competitors. We were hit by a continuing fall in exports to Asia-Pacific, the imposition of an export tax in Brazil and the impact of settlement related price increases in the US. The position there was further exacerbated by grey market imports and cigarettes supplied by manufacturers who did not participate in the Attorneys General Settlement.

We expect the world market to be more stable in 2000. It is also worth noting that British American

Tobacco has now overtaken Philip Morris in volume outside the US, an important milestone in achieving our vision of becoming the world's leading international tobacco company.

In a group as diverse as ours, it is always invidious to single out particular markets for comment but there were a number of important wins. The European region will be much stronger as a result of the Rothmans merger. The success of Lucky Strike in Germany and the volume growth in Russia, thanks to Yava and Pall Mall, is especially encouraging.

An additional element in the merger has been the formation of a smoking tobacco and cigars business, bringing together Rothmans' non-cigarette businesses in Europe with British American Tobacco's smaller Roll Your Own interests. As a result, this business is receiving real focus in British American Tobacco for the first time.

The merger has also changed the shape of our business in Asia-Pacific. Now that Australia and

Malaysia are such significant domestic markets, we are no longer so dependent on exports to the region. It is also worth highlighting the 15 per cent volume growth in Indonesia.

Amesca becomes a greater contributor as a result of the immensely strong Rothmans business in South Africa. The merger has had least impact in Latin America, other than providing us with market leadership in Jamaica, and in America-Pacific, apart from providing us with a better competitive platform in South Korea.

Since the year end, the Group has announced the signing of a Memorandum of Understanding with the Sumitomo Corporation, providing for the acquisition of their Japanese cigarette import and sales subsidiary. We expect to complete the transaction by the end of March.

In general, economic conditions made 1999 a very tough year for premium brands but the merger provided us with valuable additions to our portfolio and increases our share of the

Premium international brands that will continue to **grow**

premium international brands segment from 11.3 per cent to 17.6 per cent. We expect the pattern of consumers trading up to premium brands to resume, as their living standards rise, but progress will not always be smooth.

In order to capitalise on this important trend, we will concentrate on improving, upgrading and modernising our international brands, especially in the lights and ultra lights segments. We also intend to make the development of innovative new products even more of a priority.

Following the merger, we have made rapid progress in simplifying and clarifying our long term brand portfolio. Dunhill, State Express 555, Kent, Lucky Strike, Benson & Hedges, Rothmans and Pall Mall will be our main international drive brands and we expect to grow their volume significantly in the years ahead.

If the integration of the two brand portfolios was one challenge, another vital task, as with any merger, has been ensuring that we secured

the best of both companies in terms of people. We take pride from the fact our advisors were able to say that they "have rarely seen such a complex merger achieved with such a combination of speed and relative harmony". About 30 per cent of the new Group's management population of some 10,000 and 35 per cent of our general managers and country managers come from Rothmans. In addition, 90 per cent of the managers valued most highly by Rothmans have stayed with British American Tobacco.

A further major highlight of 1999 has been the ability of our manufacturing operations to keep product costs below the previous year, despite the 9 per cent fall in our volumes. We closed or announced the closure of 10 factories during the year. We obviously very much regret the need to close factories, especially when it is difficult to provide alternative employment, but we take every care to ensure that the employees who are affected receive fair compensation as well as advice and assistance.

In order to secure additional efficiencies, we will be doing everything we can to reduce any unnecessary complexity in our products, recipes, materials and specifications, as well as working to increase our flexibility.

Looking to the future, one of the most important areas for us to focus on is the whole subject of e-Business. We are examining not just the contribution that 'e' could make to our business, whether to the supply chain or to marketing and distribution, but also whether there are aspects of our business, such as our unique global infrastructure, that we ourselves could contribute to 'e'. We are fully prepared to adopt different or alternative business models in order to work the new technology to best advantage.



Ulrich Herter

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PREMIUM



Review of the Year

FOLLOWING THE ROTHMANS MERGER, BRITISH AMERICAN TOBACCO'S WORLD MARKET SHARE INCREASED TO 15.4% WITH OUR SHARE IN THE KEY PREMIUM INTERNATIONAL BRAND SEGMENT RISING FROM 11.3% TO 17.6% THUS IMPROVING OPERATING MARGINS FROM 16.8% TO 18.1%.

Although the past year has been a difficult period for the global tobacco industry, as premium brand volumes continued to be affected by downtrading, we have remained committed to our long term strategy. We have therefore reviewed our combined portfolio rigorously to develop our brands and ensure that we drive our progress in the key premium and lights segments. We will continue to focus support on our leading brands to increase premium brand share.

Lucky Strike now vies with State Express 555 as our best selling premium international brand. Its key regions are Europe, Japan, Latin America and the US, supported by some markets in Asia-Pacific.

Whilst the difficult trading environment in Asia-Pacific continued to depress volumes, State Express 555 managed to strengthen its competitive position within its major segments. Benson & Hedges increased market share in Australia, Arabia and South Africa, where Rothmans Special Mild also grew strongly.

Dunhill volumes were depressed by difficult trading conditions in Malaysia, although there were volume and share increases in a number of markets. Peter Stuyvesant grew share in South Africa, although the sale of the brand in New Zealand and Australia affected total volumes.

Including Rothmans brands, our share of the lights segment improves to 21.0 per cent. A number of our key brands within this segment achieved good progress.

Kent continued to increase share in Japan, although economic difficulties in some Asian markets affected total volumes. Lucky Strike Lights made significant gains in Germany and

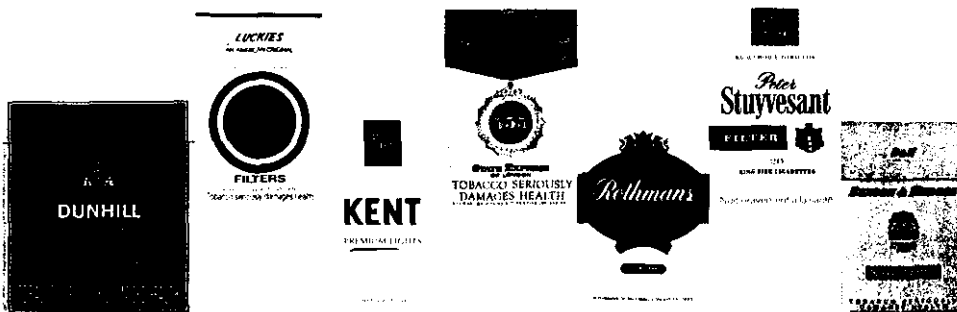
the US, and progress was maintained for Lucky Strike Menthol Lights in Japan.

We continue to identify and develop consumer segments and analyse the contestable space in the strategic markets that provide the key to future volume and profit growth. We position our differentiated brand portfolio on both a market and a regional basis and tailor it to consumers' requirements. This offers smokers a broader brand selection from which to trade upwards.

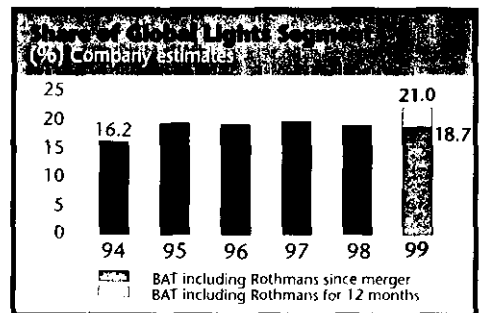
It is worth noting that the international value-for-money segment, in which we have a strong position, has traditionally been seen as the first stepping up point for consumers shifting from low priced domestically produced product to premium priced international brands.

In this context, it is encouraging that Pall Mall progressed well during the year. Both Pall Mall Lights and Viceroy Lights saw double-digit growth and we expect further success as we integrate the Rothmans Pall Mall trademark into our brand family.

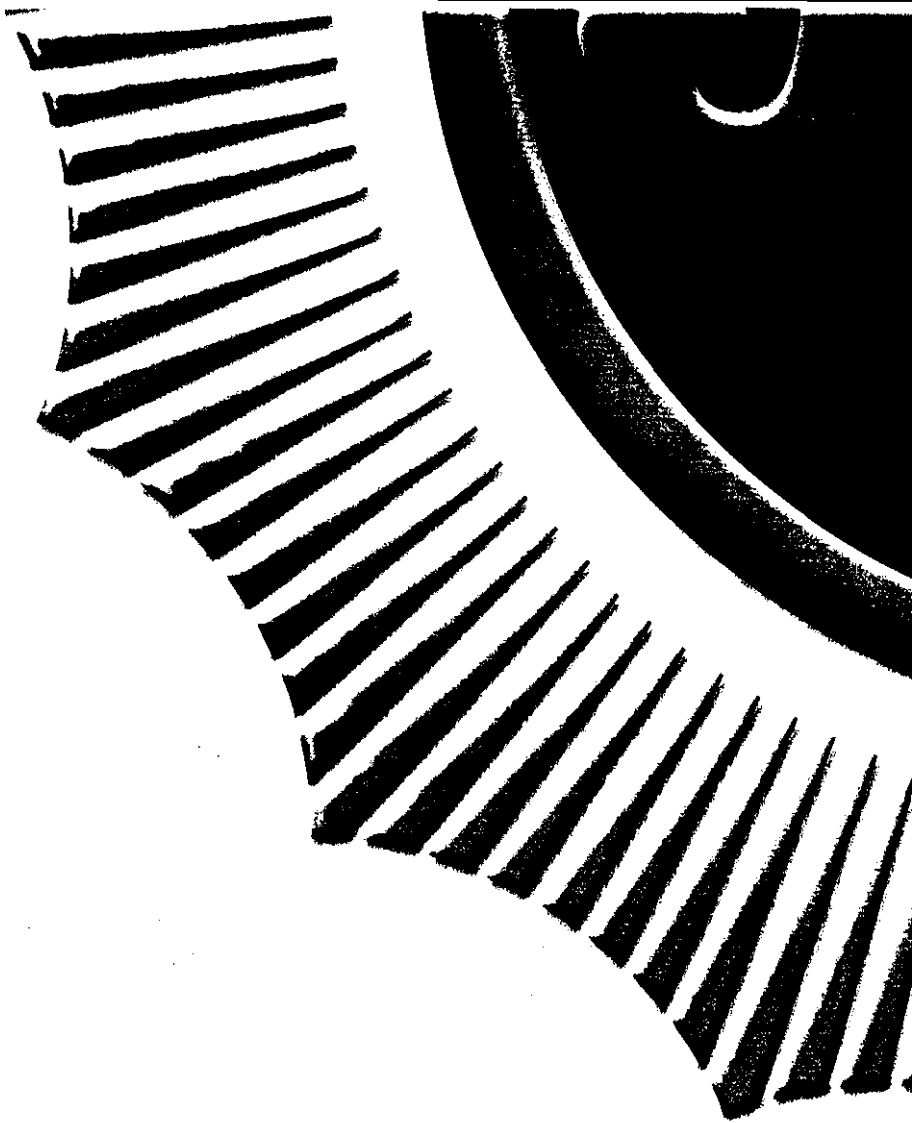
brands



Our premium international brand portfolio.



Kent is the key lights brand in our international portfolio. Launched in America in 1954, Kent is now sold in over 70 countries as diverse as Japan, Chile, Azerbaijan and Israel.



S STATE

Review of the Year continued



Quantum and MaxFli deliver immediate business benefits.



Point of purchase is a key arena for brand image.

CHANGES IN CONSUMER PURCHASING BEHAVIOUR HAVE LED TO NEW MEDIA OPPORTUNITIES, AS TRADITIONAL ADVERTISING LOSES ITS IMPACT.

Over recent years, we have strategically managed our marketing budget to focus on developing areas such as more interactive point of sale and Horeca (hotels, restaurants and cafés) events and programmes. This becomes more important as restrictions on communication increase and it becomes progressively more challenging to reach our consumers.

In many markets, the point of purchase has become the key arena in which we interact with our consumers, making it important for us to build brand image in the retail environment.

We continue to develop and apply our world class research techniques to provide insight into consumers' lifestyles and values and to understand our smokers better. This, in turn, leads to more efficient investment and improves the communication of brand images at the retail level.

This unique way of segmenting consumers, matching their values to our brand profiles, is coordinated with the retailer's own consumer proposition. By working in partnership, we maximise the effectiveness of promotions, increasing the volume and profit of the tobacco category and improving the overall performance of our trade partners. Our aim is to become the benchmark FMCG supplier to the trade, to be regarded as the experts in the tobacco category and, therefore, the supplier that wholesalers and retailers naturally turn to for advice.

Quantum and MaxFli, our proprietary integrated marketing and sales systems, have been centrally developed with Siebel's world-leading software, to enable our sales forces to build a better understanding of an outlet's consumer profile and improve relationships with individual retailers. These systems can be tailored to specific market requirements, assisting the sales force by holding stock and promotional information on each outlet so helping retailers to sell British American Tobacco's brands more effectively.

This enables us to integrate all our marketing activities from the sales representative to the brand manager, making it possible to analyse retail sales trends throughout the business. Following the successful implementation of Quantum in 11 markets, we expect to roll out the system to a further 20 markets around the world by the end of 2000.

Technology is also having an impact in operations, where our policy of defining the best approach for each factory, together with growing standardisation, has enabled a record level of more than one hundred items of significant machinery to be redeployed within the Group, avoiding new investment of some £44 million in 1999.

New capital investment has focused on high productivity machinery and product innovation, a key feature of which has been the installation of additional round corner box capacity, to meet growing consumer demand. Significant investment in equipment and new initiatives has resulted in a 6 per cent increase in the Group's key product quality index over the past year.

of the art



Launched in 1895, State Express 555 is now sold in more than 55 countries and is popular amongst smokers in China, Taiwan, Bangladesh and Vietnam.

ORIGINAL



Review of the Year continued

thinking

AT BRITISH AMERICAN TOBACCO WE TAKE AN ORIGINAL APPROACH TO THE WAY IN WHICH WE DO BUSINESS.

In November 1999, Nick Brookes, CEO of Brown & Williamson Tobacco Corporation, answered participants' questions and discussed a variety of issues facing the tobacco industry, as hundreds of users logged on to their website during the first on-line internet chat session with a tobacco CEO.

The structure of the British American Racing investment was another innovative idea and marked our return to Formula One motor racing at the start of the 1999 championship season. We were the first title sponsor to create a new team via an equity partnership, with chassis designer, Adrian Reynard and motorsport entrepreneur, Craig Pollock. Although the team had a disappointing opening year, the new alliance with Honda, as engine provider, together with drivers Jacques Villeneuve and Ricardo Zonta, gives us optimism for future seasons.

Observers and researchers estimate that within the course of the next few years the value of goods and services traded through the internet could approach US\$3 trillion, with approximately 75 per cent being business-to-business transactions. In 2000, we are likely to see some exciting advances as British American Tobacco drives forward initiatives to capitalise on these emerging e-Business opportunities.

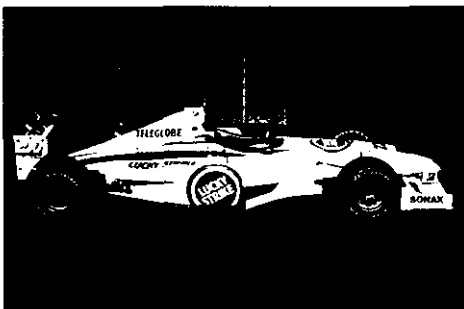
We are already working on new business models; for example with Ernst & Young on a concept called MarkITing Inc where we aim to deliver our cutting edge Trade Marketing and Distribution solutions to our end markets and subsequently make them available, on a commercial basis, to non-tobacco FMCGs.

As one of the world's largest trademark owners, British American Tobacco uses a bespoke, networked, intellectual property management system, to protect our brand rights globally. Our work with government enforcement agencies in pursuing counterfeiters, seizing and destroying imitation goods, has saved the Group some

US\$30 million in recent years by protecting brand sales. British American Tobacco leads the industry cooperation with key governments in this field.

Across the world, we work with more than 250,000 farmers, providing advice on planting, growing and harvesting tobacco, as well as information on crop rotation. This vertical integration results in greater security of supply for our business and the rapid integration of the Rothmans businesses and their leaf purchases into this system has already created synergies.

In terms of new product development, the Group's US subsidiary, Brown & Williamson is working with Star Tobacco to make cigarettes which are low in tobacco-specific nitrosamines. Star Tobacco has developed a process for curing tobacco which inhibits the formation of these nitrosamines. Brown & Williamson is currently exploring the best way to use this tobacco within its brands.



We are an equity partner, rather than just a sponsor.



Lucky Strike Ultra was successfully launched in Germany.



We work with over 250,000 tobacco farmers.



Launched in 1871, Lucky Strike is one of the oldest trademarks in the world and is now sold in some 90 countries. Key markets include Germany, Spain, Japan and the United States.

STYAB

STYAB

& scale

FOLLOWING THE MERGER WITH ROTHMANS, OUR OBJECTIVE IS TO LEVERAGE OUR SIZE AND SCALE TO DEVELOP AND DELIVER EXCELLENT QUALITY PRODUCTS AT MINIMUM SUPPLY CHAIN COST.

The merger has provided an opportunity to build on the success of existing initiatives and our progress in reducing product complexity has continued. Economies of scale have already produced significant cost savings in tobacco leaf, packaging materials and manufacturing overheads.

On a comparable basis, and despite a decline in Group volumes, unit product cost fell by 7 per cent. The process of building alliances with strategic suppliers continued, with global agreements established for tow, board and film materials. Factories in Singapore, Spain, Suriname, Papua New Guinea, Nicaragua and parts of operations in Belgium and Brazil were closed. Our New Zealand plant was sold to

Imperial Tobacco plc and announcements were made about further plant closures in Switzerland, Australia, Malaysia, South Africa and the UK.

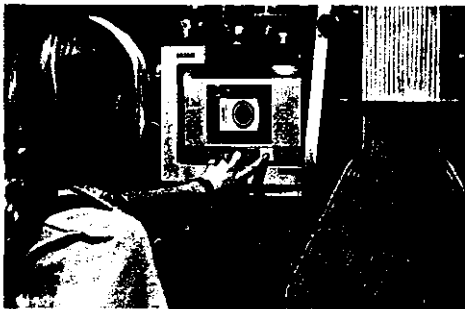
Productivity, measured in terms of cigarettes per man hour on a pre-merger basis, improved 7 per cent over the year, reflecting the success of technology cascading, combined with selective investment and factory rationalisation. A comprehensive programme of product harmonisation, involving tobacco leaf grades, blend recipes, packaging materials and manufacturing processes is currently underway.

Our regional supply chain initiatives have resulted in significant efficiency gains and through central coordination we are now able to achieve additional global synergy benefits by further developing our supply chain strategy.

Size and scale is not just about our worldwide manufacturing footprint. For many years, our

direct distribution programme in Latin America has provided a significant competitive advantage. Hundreds of thousands of retailers are visited by our distribution sales force at varying frequencies, geared to the needs of each outlet. This ensures that our brands are also available in outlets not usually serviced by traditional distribution channels and we can increasingly take advantage of this strength to maximise consumer communication at the point of sale.

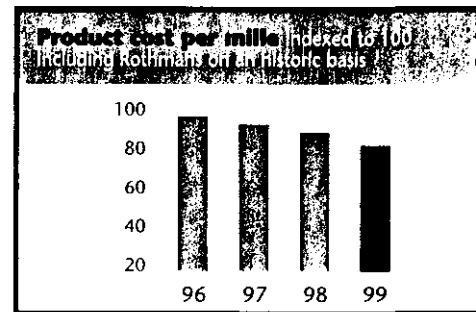
Over recent years, we have rolled out this distribution model to numerous markets in Eastern Europe, Asia and Africa. In many developing markets, British American Tobacco, either directly or via exclusive distributors, reaches more retailers than any other company in the world.



Productivity on a pre-merger basis improved by 7 per cent.



A world class distribution network.



Launched in 1890, Rothmans is now sold in approximately 115 countries and its key markets include South Africa, France, New Zealand and Saudi Arabia.

International

20

London · Paris · New York

Regional Review

reach

Regional Data

	Cigarette volumes		Net revenue		Operating profit	
	1999 bns	1998 bns	1999 £m	1998 £m	1999 £m	1998 £m
America-Pacific	84	93	3,204	2,491	544	535
Asia-Pacific	85	71	1,208	959	257	179
Latin America	167	196	1,461	1,671	333	309
Europe	171	132	2,359	1,552	316	164
Amesca	214	190	1,350	913	268	110
Imasco	32	32	1,600	1,662	304	253
	753	714	11,182	9,248	2,022	1,550
Initial US tobacco settlements					(24)	(613)
Integration costs					(357)	
Goodwill amortisation					(162)	
Sales tax recovery						74
					1,479	1,011
Operating profit, before goodwill and exceptional items, restated at comparable rates of exchange					2,025	1,550

THE IMPROVED GEOGRAPHICAL BALANCE OF OUR BUSINESSES IS REFLECTED BY THE FACT THAT THE GROUP HAS THE LEADERSHIP POSITION IN OVER 50 COUNTRIES AROUND THE WORLD. THROUGHOUT THE INTEGRATION OF ROTHMANS INTO THE BUSINESS, WE HAVE REMAINED FOCUSED ON ACHIEVING GLOBAL LEADERSHIP OF THE TOBACCO BUSINESS BY DEVELOPING BRANDS AND GROWING STRONG POSITIONS IN THE PREMIUM AND LIGHTS SEGMENTS.

Operating profit, before goodwill amortisation and exceptional items, was 31 per cent higher in local currency as a result of the inclusion of Rothmans since June 1999. On a pre-merger basis, profit is estimated to be around 4 per cent higher than last year.

Profit in the fourth quarter, before exceptional items, was 101 per cent higher than the comparable period last year. This increase reflects the contribution from Rothmans, cost reduction initiatives and last year being affected by the one-off cost of factory closures.

Group volumes increased by 5 per cent. Excluding Rothmans, Group volumes declined by 9 per cent, in line with our major international competitors.

America-Pacific

Operating profit from the America-Pacific region was £544 million, an increase of £9 million from 1998. These figures exclude the initial payments and liquidated legal fees on the US tobacco settlements. Total volume for 1999 was 11 per

cent lower than 1998, due to conditions in the US market.

US domestic market contribution, before reduced common overheads of £259 million, was £601 million, a fall of 7 per cent compared to 1998. This decrease is attributable to lower volumes, partially offset by higher pricing net of settlement costs.

Total industry shipments for the year declined 9 per cent due to trade inventory adjustment, the emergence of grey market product and list price increases in excess of 60 per cent. Brown & Williamson's volume fell 13 billion units to 56 billion and overall market share slipped to 13.4 per cent. This was principally due to GPC, which was affected by the rise in grey market

Launched in 1939, Dunhill cigarettes are now sold in 120 countries around the world. Dunhill's key markets include Malaysia, South Africa, Australia and France.

Regional Review continued

brands, preferential treatment allowed to certain small manufacturers under the MSA agreement and aggressive competitive discounting. Although Kool's market share was slightly down, image building programmes did register sizeable share gains in specific segments, while Lucky Strike Filters and Lights distribution was expanded. In the premium sector, Capri slightly increased its share of the market and Carlton's repositioning has helped slow its share decline.

The Group's operations in Japan show higher sales volumes in a reduced total market. The Group's market share rose to 7.4 per cent, with further growth from Kent and Kool. Despite the 23 per cent increased contribution in local currency, the contribution in US dollars decreased slightly due to the unfavourable US\$/Yen exchange rates.

Asia-Pacific

In Asia-Pacific, profits rose to £257 million, reflecting the merger with Rothmans as a result of which the Group now has a much stronger balance of businesses. The merger has also created significant opportunities for synergy benefits in the region. Actions to secure these savings, through factory rationalisation and

distribution changes, are now well underway following corporate restructurings in Malaysia, Singapore, Australasia, and Indonesia.

The Australasian markets showed strong profit growth (excluding the divested brands as described on page 22), driven by cost control and improved margins. Following the excise change in November, market share in Australia increased as a result of the strength of Benson & Hedges, Winfield and Dunhill.

In Malaysia, improvements in financial performance were constrained by lower total market volume, market penetration by kreteks and excise increases in 1998. Indonesia continued the good performance in difficult market conditions, despite excise tax changes that reduced margins, with volumes and profits well up. Profits in Singapore increased following the closure of the factory in 1998. Vietnam has seen strong growth in Craven 'A' volume.

On a comparable basis, regional volumes were 9 per cent lower at 85 billion, principally due to weak export volumes impacted by macro-economic conditions and a significant increase in counterfeit products.

Latin America

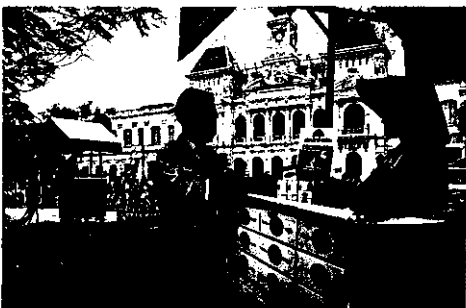
In Latin America, profit was slightly higher at £333 million, if the benefit from the recovery of sales tax of £74 million in Brazil is excluded from the comparative figures. Despite the difficult economic situation in Latin America, there were good performances in Mexico, Venezuela, Central America and the Caribbean. The regional volumes decreased by 15 per cent to 167 billion, due mainly to the lower exports from Brazil following the introduction of a cigarette export tax.

Souza Cruz maintained their share of the duty paid market in Brazil, with Free increasing its share although smuggling and tax evasion posed a growing threat. However, despite good performances from the leaf business and cost reduction initiatives, profit for the year was lower as export volumes fell significantly.

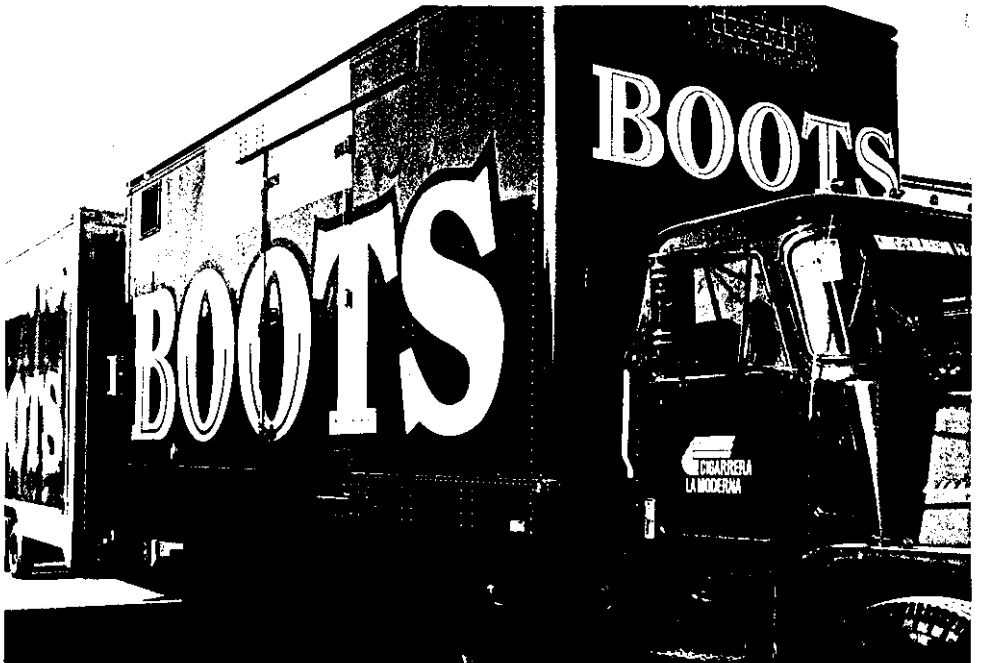
In Venezuela and Central America, profits rose as a result of price increases and cost savings, with volume growth in Venezuela. Despite the slight decrease in our market share in Mexico due to aggressive competitor activities, profits were helped by price rises, cost savings and firmer exchange rates. In Chile, profits were severely



Market share in Japan has risen to 7.4 per cent.



Craven 'A' has seen strong growth in Vietnam.



Boots is a leading brand in Mexico, where profits rose.



Yava Gold sales grew significantly in Russia.

impacted by swingeing excise increases that resulted in downtrading, as well as lower leaf export volumes, while profits in Argentina were affected by the strong recession.

Europe

The regional profit for the enlarged group almost doubled from £164 million to £316 million. The growth in profit is due to the merger (including the smoking tobacco and cigars operations) and higher contributions from Russia, Germany and Romania. These were partly offset by the discontinuation of intra-EU duty free and the adverse affects of the change in the local excise structure in Hungary and difficult trading conditions in Ukraine and Poland.

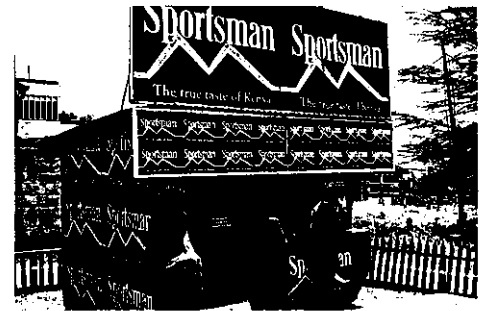
A step change was achieved in our competitive position in Europe where the reported volume grew 30 per cent to 171 billion. We increased volumes in both the largest market in Eastern Europe, Russia, and the largest market in Western Europe, Germany. In Russia, this was driven by significantly higher sales of Yava Gold and Pall Mall and in Germany, Lucky Strike and Pall Mall. There were also improved volumes in Romania. However, these successes were offset by small declines in a number of other markets.

Amesca

Total regional profit was £268 million, up £158 million, benefiting from the merger and improved profits in India and South Africa. Group volumes grew to 214 billion cigarettes. On a comparable basis, volumes were 6 per cent lower than last year largely due to civil war in the Congo and some depressed economies in Africa and South Asia.

In South Africa, profit grew despite a declining market, benefiting from price increases and a reduction in costs. Benson & Hedges, Rothmans Special Mild and Peter Stuyvesant grew market share. In Uzbekistan, volumes were well ahead resulting in higher market share and profitability. In India, good profit growth was achieved from tobacco principally through a combination of improved mix and price increases, although there was a loss on disposal of certain non-tobacco interests.

The Middle East achieved profit growth with rising sales in the premium sector of the market. In particular, results in Arabia were strong, as the sales mix improved with John Player Gold Leaf showing steady growth in share. In Sri Lanka, excellent results were generated



Sportsman grew market share in Kenya.



Player's is a leading brand in Canada.

through a combination of cost reductions, improved margins and the sale of the CTC Eagle insurance operations.

Imasco

Imasco in Canada, which was equity accounted in 1999, contributed £304 million to the Group profits, up 18 per cent in local currency. In the tobacco business, profits rose 8 per cent to £149 million as a result of higher prices and cost efficiencies. In a slightly reduced total market, a higher market share was again achieved. The total profits from financial services increased by 25 per cent to £103 million. This is the result of the growth in revenues together with strong cost control and higher productivity. Profit from other trading activities was substantially higher at £52 million.

Non-trading Items

These comprise goodwill amortisation and exceptional items which are described on page 21.



Launched in 1954, Peter Stuyvesant is now sold in around 55 countries. It is popular in South Africa, France, Greece and the Netherlands.



ESTABLISHED
OLD BOND S
LONDO

Special

Community and Environment



Afforestation programmes replace depleted woodlands.



Kanichole (Nikki) Taylor is one of B&W's first S.E.E.D. Scholars.



Our initiatives in Kenya promote existing small businesses.

THROUGH PROJECTS AND INITIATIVES AROUND THE WORLD, BRITISH AMERICAN TOBACCO IS COMMITTED TO HELP PROTECT AND IMPROVE THE ENVIRONMENT, SUPPORT LOCAL EMPLOYMENT AND TERTIARY EDUCATION, PROMOTE ARTISTIC AND CULTURAL ACTIVITIES AND ASSIST WITH DISASTER AID.

In 1999, Group payments for charitable purposes, amounted to £6.1 million, £0.5 million of which was paid in the UK.

Over time, our target is to focus 80 per cent of the Group's worldwide charitable support and community involvement on three key areas; the environment, tertiary education and support for small businesses. Our intention is that the balance should principally be dedicated to cultural causes although we will always endeavour to respond to a market's appeal for assistance in the face of a natural disaster.

Our current involvement in these areas includes afforestation and environmental programmes in countries such as Sri Lanka and Bangladesh, and the potential yield from our afforestation programmes around the world exceeds our wood

fuel usage. In addition, Brown & Williamson's S.E.E.D. Scholars Programme provides financial assistance to African-American students who would not otherwise anticipate attending college. There are also, for example, initiatives in Germany and Kenya promoting new businesses and existing small businesses respectively, which both result in enhanced local employment prospects.

Our operating companies have a strong track record of responding quickly and positively to emergencies in their communities. For example, in August 1999, British American Tobacco donated US\$100,000 to the National Disaster Fund for humanitarian relief following the earthquake in north-west Turkey and, a month later, gave US\$78,000 to the Taiwanese Government, becoming involved in the relief efforts after the island's worst earthquake in the last hundred years.

We accept that, like all businesses, we have an impact on the environment, one which we are working hard to minimise. We are committed to following the best international standards of environmental protection globally and also to the principles of sustainable development. We endorse global initiatives such as the convention on bio-

diversity and the international Kyoto agreement to halt climate change, through rigorous energy and materials conservation programmes.

Environmental management is embedded into our business systems. For example, a new fully integrated crop management system was rolled out to all leaf growing programmes, resulting in a 21 per cent reduction in agrochemical usage. Our environmental management systems conform to international standards such as ISO 14001. In the most recent survey of corporate environmental engagement of the FTSE 100 companies, conducted by Business in the Environment in 1998, British American Tobacco was rated as one of the very best performing companies.

We have a duty to our employees and the countries and communities in which we operate to demonstrate leadership on health and safety in the workplace. We have the best safety performance record in the tobacco industry and, in 1999, reduced lost workday case accidents by a further 37 per cent. We also work actively within local communities to improve awareness of the steps that can be taken in the prevention of infectious diseases.

care



Launched in 1873, Benson & Hedges is now available in more than 80 countries. This premium brand is popular in Australia, South Africa, Malaysia and New Zealand.

Finance Director's Review



Keith Dunt, Finance Director

ON 7 JUNE 1999 WE COMPLETED THE MERGER WITH ROTHMANS, WHICH HAS CLEARLY HAD A MAJOR IMPACT ON THIS YEAR'S PERFORMANCE.

The transaction was financed by the issue of 604.3 million ordinary shares and 241.7 million convertible redeemable preference shares, as a result of which Compagnie Financière Richemont AG and Rembrandt Group Limited together indirectly own 35 per cent of the fully diluted share capital of the Company. This led to an increase in shareholders' funds of £5,089 million and goodwill of £5,171 million. The global merger was followed by subsequent local restructurings in Singapore, Malaysia, Australasia and South Africa. These involved a cash outflow of £434 million, net of the sale of certain Rothmans brands, and gave rise to further goodwill of £403 million.

Goodwill arises on this transaction as it is necessary under UK requirements to account for it as an acquisition. The goodwill will be amortised over 20 years and the charge for 1999 was £162 million. In the future the annual

charge in respect of this transaction will be around £275 million.

The integration of the businesses is now well advanced, with most of them being managed on a unified basis. During 1999 we incurred £357 million of costs which relate to the integration of Rothmans into British American Tobacco. While this indicates that the final total for such costs will be somewhat higher than the £400 million estimate referred to in the circular to shareholders issued for the merger, we are also ahead of schedule in achieving the £250 million of annual synergy benefits.

For the seven months of 1999 that the Rothmans' businesses were part of the Group, their net revenue and operating profit is estimated at £1,626 million and £427 million respectively.

As the intention to dispose of the Canadian interests of Rothmans was announced at the outset of the merger, their results were not consolidated. On 3 February 2000 this business was sold for Can\$314 million and the goodwill on the Rothmans transaction reflects this

disposal value. Therefore the transaction will not result in any profit or loss in 2000, but there will be a reduction in net debt as a result of the sale.

Notice has been given to the Company by the holder of the preference shares, under the terms of the Merger agreement with Rothmans, of their intention to redeem the half of the convertible preference shares, redeemable in June 2000. The cost of the redemption would be £695 million. The preference shares which remain after June 2000 are redeemable in June 2004 at 675p per share.

The Group's results for 2000 will be affected by a change in structure in respect of Imasco in Canada. With the completion of this transaction on 1 February 2000, the Group's interests in Canada are focused on Imperial Tobacco rather than through a 42 per cent stake in a diversified holding company. The transaction will be reflected in our first quarter results for 2000 and is expected to result in goodwill of around £2.1 billion with a significant increase in shareholders' funds. The Group's share of Imasco's results for

A year of excellent progress across the Group

January 2000 will include an exceptional charge of around Can\$147 million for severance and similar payments consequent upon the change of control. The increase in net debt, including Imasco's own debt, is approximately £900 million, which will be reduced from the proceeds of the Genstar sale which is well underway. This restructuring of the Group's investment in Canada will materially improve our cash flow in 2000.

Accounting policies

During 1998 the principal financial services businesses of B.A.T Industries p.l.c. were demerged and British American Tobacco p.l.c. became the listed parent company for the retained businesses. To comply with company law and accounting standards the Group accounts for 1998 included the results of the financial services businesses up to the date of demerger. However, to provide information which is helpful to shareholders of British American Tobacco p.l.c., the Directors also presented financial information prepared as if the demerger had taken effect prior to 1998. As this financial information is the basis which more clearly reflects the ongoing operations of

British American Tobacco p.l.c., it is used for the comparatives on pages 28 and 29.

In the segmental analyses published for 1998 the costs of the headquarters for B.A.T Industries were shown separately. To provide 1998 comparatives on a more consistent basis with the segmental results for 1999, the comparatives have been restated to allocate these costs within the regional results.

During the year two new accounting standards were implemented, being FRS12 on provisions and FRS13 on financial instruments. While these standards have resulted in some additional disclosures they have not affected profit or shareholders' equity.

Group results

The Group has made significant progress in a year when a number of markets have been affected by adverse trading conditions. Operating profit, before goodwill and exceptional items, was 30 per cent ahead following the merger. On a pre-merger basis, profit is around 4 per cent ahead of last year which is better than we had indicated at the half year.

Details of the Group's operating performance can be found on pages 4 to 17.

Operating profit after goodwill amortisation, exceptional items and the impact of exchange is 46 per cent higher at £1,479 million. As explained above, the goodwill amortisation and integration costs in 1999 arose from the Rothmans merger.

The other exceptional item in 1999 was £24 million for one-off US tobacco settlement compliance costs and liquidated legal fees. US tobacco settlements constituted the principal exceptional item in 1998 with a charge of £613 million, comprising £463 million for the US cigarette companies' agreement with the Attorneys General in 46 US States and £150 million resulting from the earlier agreement with the State of Minnesota and Blue Cross and Blue Shield of Minnesota.

Other settlement costs are charged as ongoing costs. Operating profit before exceptional items in 1999 was after charging costs of £746 million compared to £106 million in the prior year.

Finance Director's Review continued

Profit and Loss Account

	1999 £m	1998 £m
Operating profit	1,479	1,011
Sale of brands	88	
Demerger and restructuring costs		(46)
	1,567	965
Net interest	(196)	(227)
Profit before tax	1,371	738
Taxation	(673)	(277)
Profit after tax	698	461
Minority interests	(142)	(115)
Profit for the year	556	346
Dividends from demerged businesses		123
Dividends	(620)	(377)
Retained (loss)/profit	(64)	92

The other exceptional item in 1998 was £74 million for a sales tax recovery in Brazil.

Below operating profit a gain of £88 million arose on the sale of certain British American Tobacco brands in Australasia. This sale was required by regulatory authorities as a consequence of the restructuring of the local businesses and was implemented on a tax efficient basis.

The demerger and restructuring costs of £46 million in 1998 comprised advisory and legal fees for the restructuring of the B.A.T Industries group.

The Group is now able to recover interest on the amounts which form the basis for the sales tax recovery in Brazil (see above). The reduction in net interest in 1999 includes £25 million in respect of this item, as well as gains on cancellation of swap contracts and the benefits of restructuring the Group's debt.

The impact of all the above was to leave profit before tax at £1,371 million, compared to £738 million in 1998. The effective tax rate increases to 49.1 per cent in 1999 as a result of goodwill amortisation and charges accrued in the year for certain of the US tobacco settlements not being relieved for tax until the following year. As future years are expected to show the same pattern for such payments and tax relief, under UK accounting standards there is a distortion to the tax rate shown in the accounts for 1999. While the settlement payments will not materially distort the tax rate after 1999, there will be a continuing distortion from goodwill amortisation.

With the various distortions to the profit and effective tax rate in 1999, earnings per share is best viewed on the basis of an adjusted fully diluted earnings per share. This removes the impact of exceptional items and goodwill amortisation, as well as reflecting the impact of the potential conversion of the preference shares. On this basis the earnings per share is 52.3p, a 13 per cent increase on 1998.

Dividends

Details of the dividends are given on page 32. As well as the amounts payable on the ordinary and preference shares, the table also includes the amortisation of discount on the preference shares. This reflects the difference between the share price at the date of the Rothmans transaction and the redemption price in 2004, which is being amortised over the period to the redemption date.

With the recommended final dividend of 17.9p, the total dividends per share are 26.2p for 1999, up 9 per cent on the prior year. Our policy is to continue to pay out at least 50 per cent of long term sustainable earnings, excluding the impact of goodwill. As an indication of this, the total dividend per share would represent 50 per cent of adjusted fully diluted earnings per share in 1999 and 52 per cent in 1998.

The Group has also acted to accelerate the payment of dividends. The interim and final dividends for 1998 were paid on 5 January 1999 and 1 July 1999 respectively. For 1999 dividends, the interim had all been paid by 27 September 1999 and the final is being brought forward to 3 May 2000.

The last dividend paid as a foreign income dividend (FID) was the interim for 1998, as FIDs were abolished with effect from 6 April 1999. Also, for presentation in the profit and loss account on page 28, dividends received from the demerged businesses are shown as a separate item below profit for the year.

Shareholders' funds

The reserve movements are summarised below. As regards the impact of exchange, the weakening of a number of currencies against sterling during 1999 led to an adverse movement of £268 million. However, the main impact in 1999 was the share issues in respect of the Rothmans merger described above. The ACT written back of £96 million in 1998 arose because of the utilisation of ACT which had been written off to reserves in prior years.

Shareholders' Funds

	1999 £m	1998 £m
1 January	64	(97)
Retained (loss)/profit	(64)	92
Differences on exchange	(268)	(69)
Share issues	5,092	42
ACT written back		96
Other	(3)	
31 December	4,821	64

Cash flow

The table opposite summarises the Group cash flow but the comparison of 1999 with 1998 is distorted by a number of events.

Operating cash flows were significantly higher at £2,255 million. This principally reflected the inclusion of Rothmans for seven months and a one-off timing benefit as certain ongoing US tobacco settlement payments are not made until early in 2000.

Cash flow also benefits as net interest and capital expenditure are lower despite the inclusion of Rothmans operations for the first time. The material reduction in net interest is partly due to one-off timing benefits from the restructuring of Group debt.

As the bulk of the initial payments in respect of US tobacco settlements were paid over in 1998, the outflow is only £170 million in 1999 compared to £546 million in the previous year.

In 1999 investing activities were significant, unlike 1998, with a net impact on cash of £216 million mainly as a result of the merger related transactions in Singapore, Malaysia, Australasia and South Africa less the proceeds on sale of BAT brands noted above.

Even though the 1999 cash flow reflects the acceleration of Group dividend payments, total dividend payments were down as 1998 included payments which were in respect of B.A.T Industries. The last two items in the table which benefited 1998 reflect the settlement of inter company balances and other transactions with the demerged financial services businesses.

As a result of the above the net cash inflow is £518 million. However, the Group's net debt position rose by £480 million to £3,055 million, reflecting the inclusion of Rothmans debt as well as exchange movements.

Treasury operations

The role of Treasury is to raise finance and to manage the financial risks arising from underlying operations. Both the financing and risk management functions are carried out under defined policies, procedures and limits.

The Board reviews and agrees the overall treasury policies and procedures, delegating appropriate authority to Treasury, the Finance Director and the boards of the central finance companies. The Group Finance Director chairs the boards of both major central finance companies. Any significant departure from agreed policies is subject to prior approval of the Board.

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. Transactions are only undertaken if these relate to underlying exposures and cannot be viewed as speculative. Regular reports are provided to senior management and treasury operations are subject to periodic independent reviews and audits, both internal and external.

The Rothmans merger provided Treasury with the opportunity to reassess limits in the light of the activities of the enlarged Group, but the general policy framework for managing each financial risk remains the same.

Management of financial risks: One of the principal responsibilities of Treasury is to manage the financial risk arising from its underlying operations. Specifically, Treasury manages, within an overall policy framework, the Group's exposure to interest rate and foreign exchange risks, funding and liquidity. Derivative contracts are entered into only to facilitate the management of these risks.

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 Group, and obtaining this financing from a wide range of debt providers. Furthermore it is the policy that short term sources of funds (including US and Euro Commercial

Paper Programmes) are backed by undrawn committed lines of credit or cash.

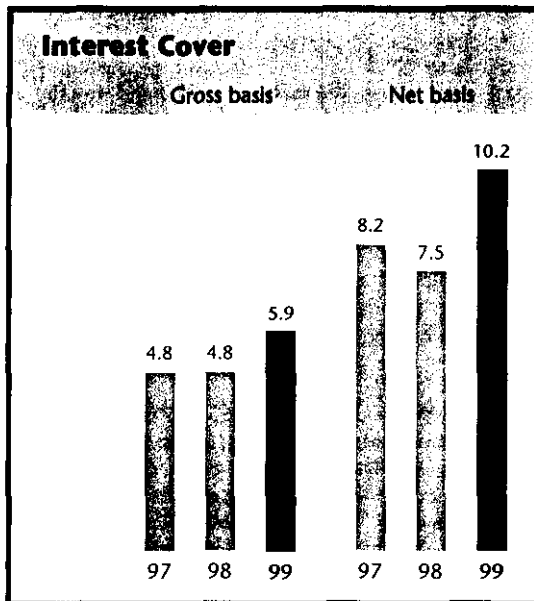
As foreshadowed in last year's review, the maturity profile and investor base of the Group's debt have been extended during 1999 with a number of issues in the international capital markets. These have substantially improved the financial flexibility of the Group. In February 1999 the Group issued a single tranche euro 1,700 million eurobond with a ten year maturity. This very large transaction in the new euro currency was greeted as a landmark issue and was subsequently recognised as one of the deals of the year. In March, this issue was followed by an euro 1,000 million five year bond which was increased to euro 1,500 million in May. A further transaction raised euro 700 million with a three year maturity.

These public debt issues, together with a six year US\$ 400 million bond and several smaller private placements brought total issuance in 1999 to the equivalent of over £3.0 billion. This has allowed bank commitments to the enlarged Group to be reduced substantially. In particular, over half of the US\$ 8 billion facility arranged in 1997 was cancelled. Upon the merger with Rothmans, bond market debt of £568 million equivalent with maturities of four, six, and nine years was assumed.

As a result, the maturity profile of the Group's debt has improved significantly. The Group had £2,621 million in cash and short term investments at year end as a result of the proceeds of the bond issues and strong cash flow from operations. As well as underwriting several of the transactions associated with the merger with Rothmans, this liquidity has also served the Group well in closing the acquisition of the majority of Imasco at the beginning of February 2000. Although in cash terms the cost of that investment was matched by the proceeds from the sale of the Imasco non-tobacco businesses, the Group used its liquidity in the initial acquisition of Imasco shares. Some of these cash resources would be available to meet the potential redemption of the convertible preference shares noted above.

Cash Flow		
	1999 £m	1998 £m
Net operating cash flows	2,255	1,728
Investment returns/finance costs	(206)	(282)
Taxation	(334)	(281)
Capital expenditure	(281)	(351)
	1,434	814
Initial US tobacco settlements	(170)	(546)
Acquisitions and disposals	(216)	(16)
Dividends paid	(530)	(696)
Dividends from demerged businesses		242
Cash flow with demerged businesses		668
Net cash flows before financing activities	518	466

Finance Director's Review continued



Subsidiary undertakings are funded by share capital and retained earnings, loans from the central finance companies on commercial terms, or through local borrowings by the subsidiaries in appropriate currencies.

All contractual borrowing covenants have been met and none of these 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 overseas subsidiaries into its reporting currency, sterling. The Group's primary balance sheet translation exposure is to the US dollar and the euro. These exposures are kept under continuous review and the Group's policy is to minimise all balance sheet translation exposure. Where practicable and cost effective, the exposures are managed by matching currency assets with currency borrowings. Hedging is undertaken using direct borrowings, cash and short term investments, cross currency swaps and forward foreign currency contracts. The currency profile of the Group's gross debt, after taking into account derivative contracts was 61 per cent US dollar, 19 per cent euro, 11 per cent sterling and 9 per cent other currencies.

The Group also faces currency exposures on the translation of profits earned in overseas subsidiaries and on trading transactions undertaken by all subsidiaries in foreign currencies. These exposures, comprise anticipated and known flows and are netted and offset wherever possible. The remaining exposures are hedged with forward foreign exchange contracts and options. The decision to hedge is influenced by the size of the exposure, its certainty and the prevailing exchange rate.

Interest rate risk: The objective of the Group's interest rate risk management policy is to protect the earnings, cash flow and the economic value of the Group from the impact of interest rate fluctuations, at acceptable costs, and to safeguard against the breach of financial covenants. In applying this policy action is taken to minimise counterparty credit risk.

In order to manage its interest rate risk the Group maintains both floating rate and fixed rate debt. The desired ratio of fixed to variable rate debt is determined as a result of regular reviews of market conditions and strategy by Treasury and the board of the main central finance company. Changes

in strategy are approved at Board level. At 31 December 1999 there was a 45:55 ratio (1998 65:35) between floating and fixed rate gross debt. 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.

Counterparty risk: Cash deposits and other financial instruments give rise to credit risk on the amounts due from counterparties. 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. Counterparty credit ratings are reviewed regularly.

Financial resources

The Group assesses its financial capacity by reference to cash flow and interest cover. The unadjusted figures for interest cover are distorted by the goodwill amortisation and exceptional items in operating profit, the profit on sale of brands and the demerger and restructuring costs. The table opposite shows the cover, adjusting for these items, on the basis of both profit over interest paid (gross) and profit over net interest paid (net). As can be seen, even on a gross basis the interest cover is strong at 5.9 (1998 4.8).

European Monetary Union

The Company, as a matter of policy, actively supports Economic and Monetary Union as a means of delivering increased stability and prosperity. Each operating subsidiary has prepared a business impact plan assessing the risks, uncertainties and opportunities associated with the euro. Costs incurred in 1999 on the euro programme had no material effect on the Group's business performance.

Millennium

Throughout 1999, the millennium programme remained a top business priority and a Millennium Transition Office monitored the rollover of Group companies worldwide. In the event, all operations returned to business as usual shortly after 1 January 2000. The final estimate for expenditure to tackle this issue across the merged Group is £72 million.

Going concern

After reviewing the Group's annual budget and plans, the Directors consider that the Group has 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 accounts.

Keith Dunt

Corporate Governance

British American Tobacco continues to apply the Principles of the London Stock Exchange's Combined Code and considers that, with only one exception, relating to notice periods under the service contracts of executive Directors, it has complied with all applicable provisions of that Code. Our auditors have conducted a limited review of our compliance with specific provisions of the Code and have not identified any issues which require reporting. Key aspects of our approach to corporate governance are set out below.

The Board of Directors

The Board meets at least six times a year, with one meeting being a two-day strategy discussion. Responsibility for implementing the Group's strategy is delegated to the Management Board, which meets at least eight times a year.

The Board is responsible for the overall system of internal control for the Company and its subsidiaries and for reviewing the effectiveness of these controls. The system is designed to manage risks that may impede the achievement of the Company's business objectives rather than to eliminate these risks. The internal control system can therefore only provide reasonable assurance, not absolute assurance, against material misstatement or loss.

Board Committees (see pages 26 and 27 for details of membership).

The Audit Committee is chaired by Rupert Pennant-Rea. It meets regularly with internal and external auditors, as well as management, to review the effectiveness of internal controls, any matters raised in regular reports to the Committee and the full year financial statements prior to their submission to the Board.

The Remuneration Committee is chaired by Kenneth Clarke. It makes recommendations to the Board on the terms of employment of executive Directors and members of the Management Board and decides their specific remuneration.

Directors' Remuneration and Interests

	Remuneration/ fees in 1999 (£)	Ordinary shares as at 31.12.99	Share options* at 31.12.99
M F Broughton	1,355,701	176,115	608,385
K H Clarke	100,000	4,091	-
U G V Herter	957,582	26,902	327,226
W P Ryan	571,154	20,000	-
K S Dunt	618,645	7,686	213,381
H Einsmann	26,250	-	-
W A Owens	41,796	-	-
R L Pennant-Rea	33,750	3,023	-
J P du Plessis	17,077	-	-
J P Rupert	19,923	-	-
K S Wong	35,000	-	-

*Includes awards of shares under the Long Term Incentive Plan. These options and awards are exercisable until 2009 subject to fulfilment of performance conditions (apart from options granted by B.A.T Industries p.l.c. prior to the listing of the Company in September 1998).

Martin Broughton, Ulrich Herter and Keith Dunt are members of the B.A.T Pension Scheme. Further details of executive Directors' pensions are given on page 8 of the Directors' Report and Accounts.

The Nominations Committee is chaired by Martin Broughton. It recommends to the Board candidates for appointment to the Board and the Management Board.

Social responsibility

British American Tobacco has adopted a coherent structured approach to environmental, health and safety management across all its international operations, the Company's objectives being to exceed current environmental and occupational health and safety standards wherever feasible and to be at the forefront of international developments.

Details of our community affairs programme are available on page 19.

Payments for charitable purposes in 1999 amounted to £6.1 million, £0.5 million of which was paid in the UK.

No money was given for political purposes in the UK.

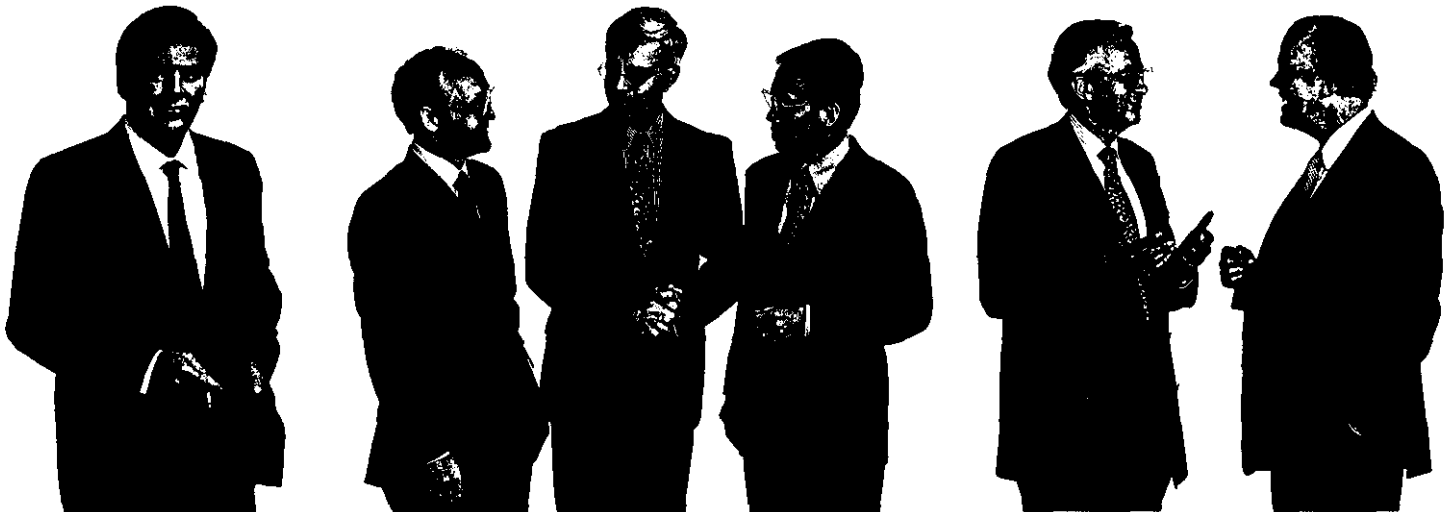
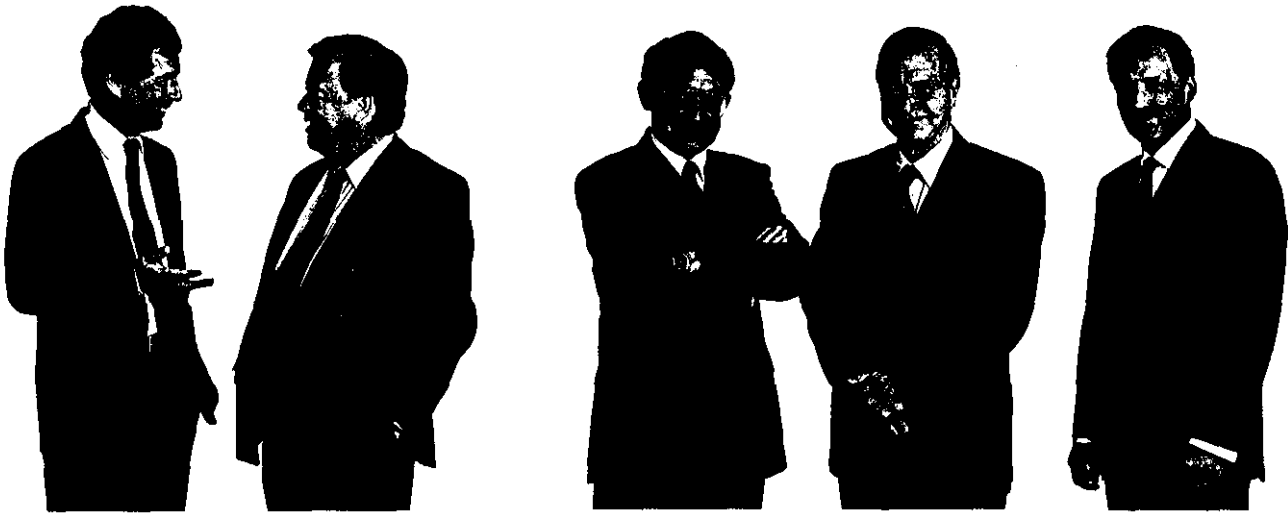
Employees

British American Tobacco actively encourages employee involvement in the Group's business via publications, team briefings and regular meetings with employee representatives. The Company established a European Employee Council ahead of the European Works Council Directive becoming effective in the UK and is presently taking steps to create a combined European Employee Council following the Rothmans merger.

Through savings-related share option schemes and share participation schemes, many of the Group's employees have become shareholders in the Company. The Company intends to further employee share ownership by taking authority at the forthcoming Annual General Meeting to establish a scheme based on the Government's proposals for new all-employee share plans.

The Company's employment policy includes commitments to recruit people on the basis of their ability, to equal opportunities and to the employment of disabled people. Depending on their skills and abilities, disabled people are given the same consideration as others when applying for jobs and in career prospects.

Main Board



This page pictured left to right
Top tier

Martin Broughton (52), Chairman #
Joined the British American Tobacco Group in 1971. Appointed to the Board of B.A.T Industries p.l.c. in 1988, he was Group Chief Executive and Deputy Chairman at the time of the merger in 1998. He is a member of the Financial Reporting Council, and a non-executive Director of Whitbread PLC and the British Horseracing Board Ltd.

The Rt. Hon. Kenneth Clarke QC MP (59), Non-executive Deputy Chairman # + *
Appointed a Director and Chairman of the Remuneration Committee in 1998. Appointed Queen's Counsel in 1980 and from 1993 until May 1997, he was Chancellor of the Exchequer. He is Chairman of Alliance UniChem Plc and a Director of Foreign and Colonial Investment Trust PLC and Independent News & Media (UK) Limited.

Ulrich Herter (58), Managing Director #
Joined the British American Tobacco Group in Germany in 1984, becoming a Director of B.A.T Industries p.l.c. in 1990. He was appointed Managing Director, Tobacco in 1992 and a Director of British American Tobacco in 1998.

Bill Ryan (64), Deputy Managing Director
Appointed a Director in June 1999, he was formerly Chief Executive of Rothmans International and a director of Compagnie Financière Richemont AG.

Keith Dunt (52), Finance Director
Joined the British American Tobacco Group in 1975 and held various positions including Director for Latin America and Finance and IT Director. He joined the Board in 1998.

Lower tier

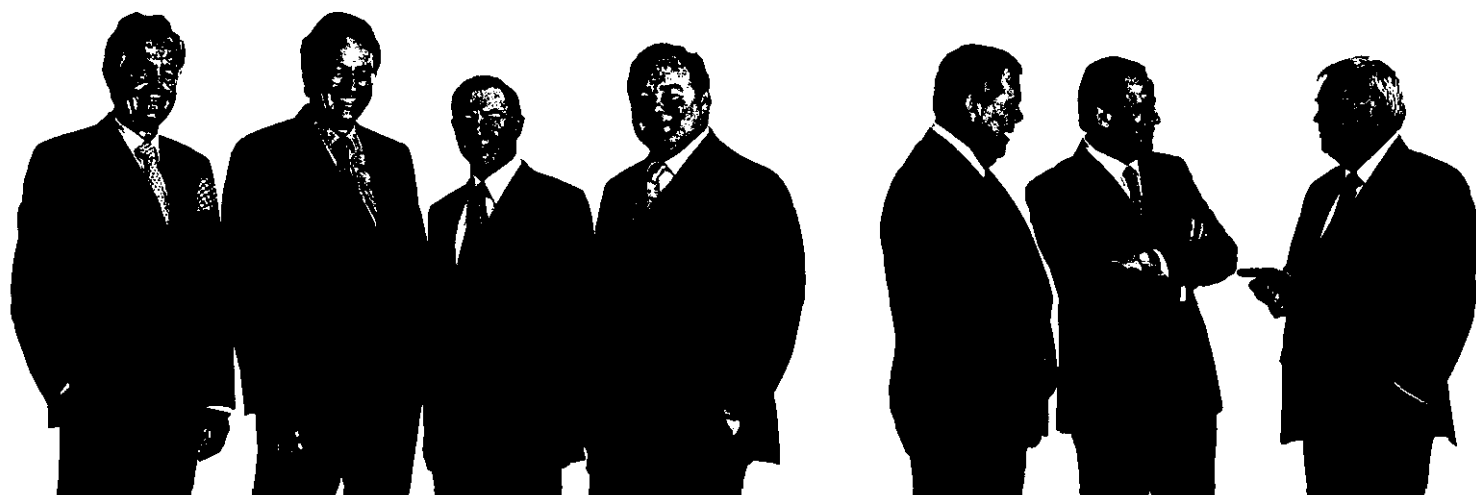
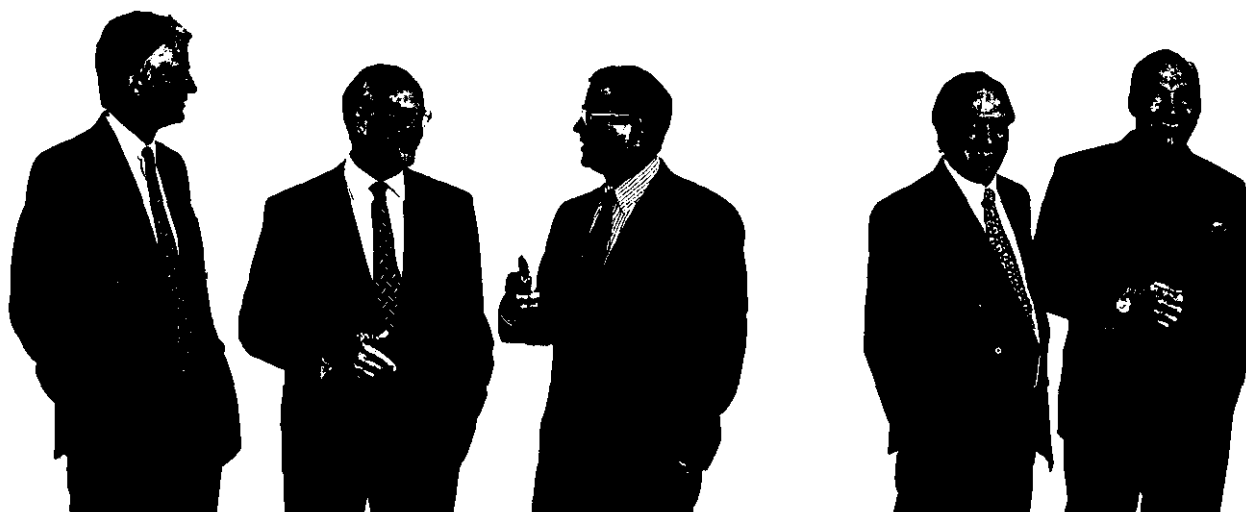
Johann Rupert (49), Non-executive Director # *
A Director since June 1999, he is Chief Executive of Compagnie Financière Richemont AG and Chairman of Rembrandt Group Limited and Gold Fields of South Africa. He was formerly a Director of Rothmans International.

Jan du Plessis (46), Non-executive Director # + *
Joined the Board in June 1999. He is Finance Director of Compagnie Financière Richemont AG and a Director of Hanover Direct. He was formerly Finance Director of Rothmans International.

Admiral William Owens (59), Non-executive Director # + *
Appointed a Director in 1998, Admiral Owens is Co-Chief Executive Officer of Teledesic of the USA which he joined in 1998. He had a distinguished career in the US Navy which included the appointments of Vice Chairman of the Joint Chiefs of Staff, Deputy Chief of Naval Operations and Commander of the Sixth Fleet.

Management Board

The Management Board comprises the executive Directors of British American Tobacco p.l.c. together with the following executives:



Wong Kok Siew (53), Non-executive Director # + *
Appointed a Director in 1998. He is President and Chief Executive Officer of SembCorp Industries, a leading Singapore engineering and technology group, and holds various non-executive appointments including Nomura (Singapore) and Brierley Investments (New Zealand). He is also Deputy Chairman of the Singapore Trade Development Board.

Dr Harald Einsmann (65), Non-executive Director # + *
Appointed a Director in 1999, Dr Einsmann was a main board Director of Procter & Gamble Co. from 1991 to 1999. He is also a non-executive Director of EMI Group plc, Tesco PLC and Stora Enso AB in Sweden.

Rupert Pennant-Rea (52), Non-executive Director # + *
Formerly Editor of the Economist and Deputy Governor of the Bank of England. He is Chairman of The Stationery Office Holdings Limited, Plantation & General Investments PLC and Key Asset Management (UK) Limited. He was appointed a non-executive Director of B.A.T Industries p.l.c. in 1995, becoming a Director of British American Tobacco in 1998. He chairs the Audit Committee.

Board Committees
Committee membership is indicated by the following symbols
Nominations Committee
+ Audit Committee
* Remuneration Committee

This page pictured left to right
Top tier

Michael Prideaux (49), Corporate and Regulatory Affairs Director
Stuart Chalfen (59), Legal Director and General Counsel
Dr John Jewell (50), Operations Director
David Stevens (58), Human Resources Director
Jimmi Rembiszewski (49), Marketing Director

Lower tier

Chris Bischoff (57), Director, Smoking Tobacco and Cigars
Nick Brookes (49), Regional Director, America-Pacific
Tony Johnston (52), Regional Director, Asia-Pacific
Paul Adams (46), Regional Director, Europe
Dick Green (56), Regional Director, Mesca
Antonio Monteiro de Castro (54), Regional Director, Latin America
Tony Jones (52), Regional Director, Africa

Summary Group Profit and Loss Account for the year ended 31 December

(excluding demerged businesses)

	1999 £m	1998 £m
Revenue		
Subsidiary undertakings	18,798	14,584
Share of associates	2,873	2,792
	21,671	17,376
Profit		
Subsidiary undertakings operating profit	1,099	676
after charging: US tobacco settlements	(24)	(613)
integration costs	(357)	
goodwill amortisation	(162)	
after crediting: sales tax recovery		74
Share of associates and joint venture	380	335
Total operating profit	1,479	1,011
Sale of brands	88	
Demerger and restructuring costs		(46)
Profit on ordinary activities before interest	1,567	965
Subsidiary undertakings: investment income	195	147
interest payable	(365)	(351)
Share of associates interest paid less received	(26)	(23)
Profit on ordinary activities before taxation	1,371	738
Taxation on ordinary activities	(673)	(277)
Profit on ordinary activities after taxation	698	461
Minority interests	(142)	(115)
Profit for the year	556	346
Dividends from demerged businesses		123
Dividends and other appropriations: ordinary shares	(546)	(377)
convertible redeemable preference shares	(74)	
Retained (loss)/profit	(64)	92
Earnings per share: basic	25.25p	22.17p
adjusted fully diluted	52.33p	46.12p

Statement of Total Recognised Gains and Losses for the year ended 31 December

	1999 £m	1998 £m
Profit for the year <i>above</i>	556	346
Differences on exchange	(268)	(69)
Total recognised gains related to the year <i>page 29</i>	288	277

Summary Group Balance Sheet at 31 December

	1999 £m	1998 £m
Assets		
Fixed assets		
Intangible assets	5,338	
Tangible assets	2,456	2,048
Investments in associates and joint venture	636	472
Other investments and long term loans	210	119
	8,640	2,639
Current assets		
Stocks	2,850	2,165
Debtors	2,000	1,493
Acquired businesses awaiting disposal	123	
Current investments	768	185
Short term deposits and cash	1,853	970
	7,594	4,813
Total assets	16,234	7,452
Liabilities		
Capital and reserves		
Share capital	605	393
Share premium account	4	1
Merger reserves	4,726	
Other reserves	503	483
Profit and loss account	(1,017)	(813)
Shareholders' funds (including non-equity interests of £1,474 million – 1998 £nil)	4,821	64
Minority shareholders' equity interest	455	323
	5,276	387
Other liabilities		
Provisions for liabilities and charges	1,251	741
Borrowings	5,676	3,730
Creditors	4,031	2,594
	10,958	7,065
Total funds employed	16,234	7,452

Interest of British American Tobacco's Shareholders for the year ended 31 December

	1999 £m	1998 £m
Balance 1 January	64	(97)
Total recognised gains related to the year <i>page 28</i>	288	277
Issue of shares	5,092	42
Dividends from demerged businesses		123
Dividends and other appropriations	(620)	(377)
Other	(3)	96
Balance 31 December	4,821	64

This summary financial statement was approved by the Board of Directors on 7 March 2000 and signed on its behalf by Martin Broughton, Chairman.



Summary Financial Statement and Notes

Summary Financial Statement

The Summary Financial Statement on pages 28 to 32 is a summary of information in the Directors' Report and Accounts and should be read with the Managing Director's Review (pages 4 to 17) and the Finance Director's Review (pages 20 to 24). The Chairman will comment on the current year in his speech at the Annual General Meeting on 27 April 2000. Copies of the speech may be obtained from the Secretary after the meeting.

The Annual Review and Summary Financial Statement does not contain sufficient information to allow for a full understanding of the results of the Group and the state of affairs of the Company or of the Group as would be provided by the full annual accounts and reports. Shareholders requiring more detailed information have the right to obtain free of charge, a copy of the full annual Group accounts and Directors' report for 1999, or for future years, by writing to the Company's Registrar whose details are given on page 32.

As explained in the Finance Director's Review on page 21 it is necessary to consider the comparatives for the Group's financial information on two bases. The statements on pages 28 and 29 provide additional information prepared as if the demerger by B.A.T Industries of its principal financial services businesses had taken effect prior to 1 January 1998. This more clearly reflects the continuing operations of the Group and is on a basis consistent with the Listing Particulars published in 1998. The statement on page 31 provides the financial information required by law, where the comparatives are different as a result of including the results of the demerged businesses for part of 1998.

Report of the auditors

The auditors' report on the full annual accounts of the Group for the year ended 31 December 1999 is unqualified and does not contain any statement concerning accounting records or failure to obtain necessary information and explanations.

Contingent liabilities

There are contingent liabilities in respect of litigation, overseas taxes and guarantees in various countries. Group companies, notably Brown & Williamson Tobacco Corporation ('B&W') as well as other leading cigarette manufacturers, are defendants, principally in the United States, in a number of product liability cases, including a substantial number of new cases filed in 1999, although a number of cases were discontinued by claimants (without payment by any defendants) in the year.

Legal matters outside the United States

At year end, there were no active claims against Group companies (including those of the former Rothmans group) in respect of health-related claims outside Argentina, Australia, Brazil, Canada, Chile, Eire, Finland, France, Germany, Israel, the Netherlands, Pakistan, the Philippines and Sri Lanka.

US litigation

The total number of US product liability cases pending at year end involving Group companies was 537 (31 December 1998, 678 cases).

UK Group companies were named as co-defendants in 161 of those cases (1998, 238 cases). Since many of these pending cases seek unspecified damages, it is not possible to determine the total amount of claims pending. The cases fall into three principal categories:

(1) **Medical reimbursement cases.** These civil actions seek to recover amounts spent by government entities and other third party providers on health care and welfare costs claimed to result from illnesses associated with smoking. Despite the almost uniform success of the industry's defence to these to date, the US Federal Government has filed a suit, which will probably not come to trial until 2003.

(2) **Class actions.** As at 31 December 1999, B&W was named as a defendant in some 38 (31 December 1998, 55) separate actions attempting to assert claims on behalf of classes of persons allegedly injured by smoking. Despite the almost uniform success of the industry's defence to these to date, there is one case (Engle, Florida) currently in trial.

(3) **Individual cases.** Approximately 421 cases were pending against B&W at 31 December 1999 (31 December 1998, 497), filed by or on behalf of individuals in which it is contended that diseases or deaths have been caused by cigarette smoking or by exposure to environmental tobacco smoke (ETS). While the industry continues not to have paid any damages to date, two decisions adverse to Philip Morris are currently under appeal.

Conclusion

While it is impossible to be certain of the outcome of any particular case or of the amount of any possible adverse verdict, the Company believes that the defences of the Group companies to all these various claims are meritorious both on the law and the facts, and a vigorous defence is being made everywhere. If an adverse judgement were entered against any of the Group companies in any case, an appeal would be made. Such appeals could require the posting of appeal bonds or substitute security by the appellants for the amounts of such adverse judgements. At least in the aggregate and despite the quality of defences available to the Group, it is not impossible that the results of operations or cash flows of the Group in particular quarterly or annual periods could be materially affected by this and by the final outcome of any particular litigation.

Having regard to all these matters, the Directors (i) do not consider it appropriate to make any provision in respect of any pending litigation and (ii) do not believe that the ultimate outcome of all this litigation will significantly impair the financial condition of the Group.

Post balance sheet events

As explained in the Finance Director's Review on page 20 the Group has received notice from the holder of the convertible preference shares of their intention to redeem half the shares, while the holding in Imasco was restructured in February 2000.

Profit and Loss Account for the year ended 31 December

(including demerged businesses)

	Revenue		Operating profit	
	1999 £m	1998 £m	1999 £m	1998 £m
Retained businesses	18,798	14,584	1,099	676
Demerged businesses		3,800		504
Subsidiary undertakings	18,798	18,384	1,099	1,180
Share of associates	2,873	2,792	380	335
	21,671	21,176	1,479	1,515
			1999 £m	1998 £m
Profit on ordinary activities before interest			1,567	1,440
Net interest			(196)	(227)
Profit on ordinary activities before taxation			1,371	1,213
Taxation on ordinary activities			(673)	(453)
Profit on ordinary activities after taxation			698	760
Minority interests			(142)	(123)
Profit for the year			556	637
Capital reserve transfer				76
Dividends: equity and non-equity demerger			(620)	(377)
				(6,689)
Retained loss			(64)	(6,353)
Earnings per share			25.25p	27.04p

The aggregate emoluments of the Directors were £3,776,878.

Auditors' statement to the members of British American Tobacco p.l.c.

We have examined the summary financial statement set out on pages 28 to 31.

Respective responsibilities of Directors and auditors

The Directors are responsible for preparing the Annual Report and Summary Financial Statement. Our responsibility is to report to you our opinion on the consistency of the summary financial statement within the Annual Review and Summary Financial Statement with the full annual accounts and directors' report, and its compliance with the relevant requirements of Section 251 of the Companies Act 1985 and the regulations made thereunder. We also read the other information contained in the Annual Review and Summary Financial Statement and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the summary financial statement.

Basis of opinion

We conducted our work in accordance with Bulletin 1999/6 'The auditors' statement on the summary financial statement' adopted by the Auditing Practices Board.

Opinion

In our opinion the summary financial statement is consistent with the full annual accounts and directors' report of British American Tobacco p.l.c. for the year ended 31 December 1999 and complies with the applicable requirements of Section 251 of the Companies Act 1985, and the regulations made thereunder.

PricewaterhouseCoopers
PricewaterhouseCoopers

Chartered Accountants and Registered Auditors, London
7 March 2000

Shareholder Information

Financial Calendar

Dividends on Ordinary Shares and CRP Shares

The Directors will be recommending to the shareholders at the Annual General Meeting to be held on 27 April 2000, the payment on 3 May 2000, of a final dividend for the year of 17.9p per ordinary share of 25p and convertible redeemable preference share of 25p. Valid transfers received by the Registrar up to 17 March 2000, will be in time to rank for payment of this dividend. The ex-dividend date is 13 March 2000.

Dividends	1999		1998	
	Pence per share	£m	Pence per share	£m
Ordinary shares				
Special Interim paid 1 July 1999	4.0	62		
Interim 1999 paid 27 September 1999				
– ordinary	4.3	94		
– FID			8.0	125
Final 1999 payable 3 May 2000	17.9	390	16.0	252
	26.2	546	24.0	377
Convertible redeemable preference shares				
Interim 1999 paid 27 September 1999	4.3	10		
Final 1999 payable 3 May 2000	17.9	44		
Amortisation of discount		20		
	22.2	74		

Annual General Meeting

Thursday 27 April 2000 at 11.30am, The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE.

Results

First quarter – 27 April 2000

Second quarter – 1 August 2000

Registrar

Enquiries concerning holdings of the Company's ordinary shares and notification of a holder's change of address should be referred to Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA, Tel: +44 (0) 870 600 3983; www.lloydstsb-registrars.co.uk. A text phone facility for those with hearing difficulties is available by contacting Tel: +44 (0) 870 600 3950. Copies of the British American Tobacco Annual Review and Summary Financial Statement and Directors' Report in alternative formats such as braille, audio tape and large print are available by contacting Tel: +44 (0) 20 7845 1925.

Low Cost Share Dealing Facility

A postal facility, which provides a simple, low cost method of buying and selling British American Tobacco ordinary shares is available through Lloyds TSB Registrars, Tel: +44 (0) 870 606 0302.

Individual Savings Accounts (ISAs)

British American Tobacco has introduced a sponsored ISA managed by The Share Centre, Tel: +44 (0) 1442 890 844; www.share.co.uk

Share Price Information

The latest British American Tobacco share price is available on Ceefax and Teletext and also on the Financial Times Cityline Service, Tel: +44 (0) 906 843 1770 (calls charged at 60p per minute).

Capital Gains Tax

For the purposes of UK capital gains tax, the market value at 31 March 1982 of an ordinary share of B.A.T Industries p.l.c. was £4.075. For British American Tobacco shares arising out of B.A.T Industries shares held and retained since that date the adjusted price is £0.15282. This takes account of the 3 for 1 capitalisation issue in 1983, the two demergers in 1990, the 1 for 1 capitalisation in 1993 and the Allied Zurich demerger in September 1998.

American Depositary Receipts

The Company sponsors an American Depositary Receipt (ADR) programme in the United States. ADRs, which each represent two ordinary shares of the Company, are publicly traded in the US on the American Stock Exchange under the symbol BTI with a CUSIP number 110448107. A dividend re-investment plan (DRIP) is available for ADR holders. ADR holders may instruct the authorised depository, The Bank of New York how the ordinary shares represented by their ADRs should be voted at the Company's Annual General Meeting by completing and returning a voting card which will be sent to them. All enquiries regarding ADR holder accounts and payment of dividends should be directed to The Bank of New York, ADR Department, 101 Barclay Street, 22W, New York, NY10286, USA, Tel: +1 212 815 5981; www.adrbony.com

Registered Office

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Secretary

Philip Cook

General Counsel

Stuart Chalfen

Investor Relations

Enquiries should be directed to:
Ralph Edmondson (UK), Tel: +44 (0) 20 7845 1180 and
Robert Caputo (USA), Tel: +1 212 351 5006.

Press Office

Enquiries should be directed to:
Fran Morrison, Tel: +44 (0) 20 7845 2888.

Internet

Information on British American Tobacco is available on www.bat.com

Auditors

PricewaterhouseCoopers
1 Embankment Place, London WC2N 6NN.

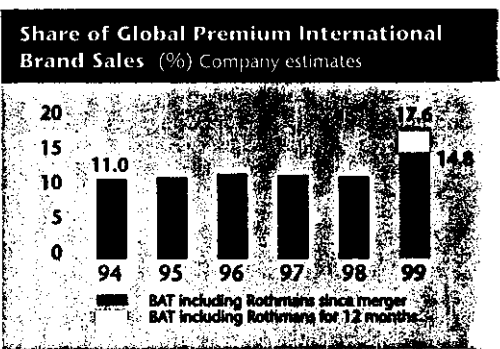
Producing over 800 billion cigarettes per year. We use
 processing plants. We have four major R&D centres
 etc. British American Tobacco companies contribute
 etc, more than ten times as much as the Group's



World's most respected food/ beverages companies Copyright Financial Times

Rank 1999	Rank 1998	Company	Country
1	(2)	Coca-Cola	US
1	(1)	Nestle	Switzerland
3		Heineken	Netherlands
4	(3)	Procter & Gamble	US
5		British American Tobacco	UK
6	(5)	Philip Morris	US
7		Unilever	Netherlands/UK
7	(6)	Cargill	US
9		Danone	France
9		PepsiCo	US

December 1999 Financial Times global survey covering 750 Chief Executives



Global Market Volumes (billions)
 Company estimates of market consumption

1 China	1,632	11 Poland	88
2 USA	420	12 Spain	86
3 Japan	329	13 France	84
4 Russia	249	14 Philippines	81
5 Germany	141	15 Ukraine	79
6 Turkey	114	16 United Kingdom	62
7 India	98	17 Egypt	60
8 Brazil	97	18 Vietnam	51
9 Italy	96	19 Mexico	49
10 South Korea	94	20 Pakistan	48

Partnership change

Proposals for the UK Government, the tobacco industry and public health groups

An adult choice

British American Tobacco recognises that along with the pleasures of smoking come real risks of serious diseases. In the past we have worked closely with governments and public health bodies on these issues. Over the past few years this cooperation has been more difficult, primarily due to the efforts of those wishing to damage our reputation as a means to promoting a 'smoke-free' society. We are seeking a return to dialogue and cooperation on the following areas:

Responsible marketing

We are committed to responsible marketing. We recognise society's changing expectations, and the need to establish a forum where the industry, Government, public health groups and consumer advocacy groups can reach consensus on what constitutes responsible marketing of tobacco products. We believe in our right to provide adult smokers with brand choice and information, alongside our responsibility to ensure that our marketing does not undermine efforts to prevent children from smoking. We expect our actions to be influenced by independent research and to include a comprehensive review of codes governing tobacco marketing.

Ensure that only adults smoke

The decision to smoke should be exclusively an adult choice. We have proposed a summit meeting amongst Government, public health groups, educationalists, tobacco companies and retailers, to develop an action plan on the prevention of under age smoking. We expect this to result in a range of initiatives, based on independent research into teenage behaviour, that may include raising the legal age for tobacco sales to 18, supporting retailers through young persons identity cards and funding a teenage action group, where teenagers themselves can develop messages to their peers on how to deal with adult products such as cigarettes and alcohol.

Ensure that smokers are informed of the varying levels of risk

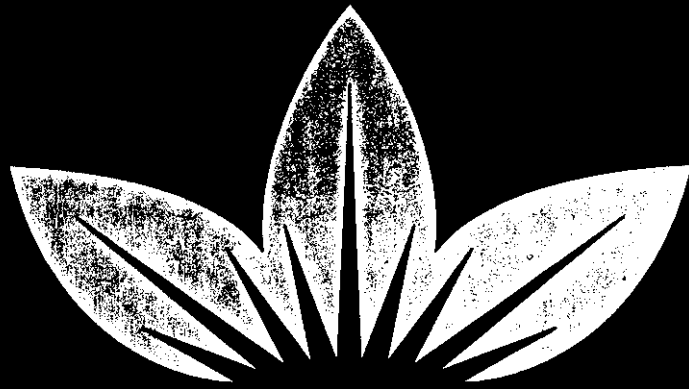
We believe that after decades of public education, people are well aware of the health risks associated with smoking. However, we also believe that public health messages could address the steps that smokers could take to reduce their exposure to risk. Government, public health bodies and tobacco companies could work together on such messages to smokers and innovative ways to deliver them. We expect the actions to include independent research on low tar cigarettes.

Ensure that the concerns of non-smokers are accommodated

We recognise that tobacco smoke is a significant annoyance to some non-smokers, and we believe that Government, public health bodies and the tobacco industry can work together on practical solutions. These could include investigating cost-effective devices for reducing environmental tobacco smoke in public spaces and support for campaigns which provide solutions for the hospitality sector.

Ensure that the ability to communicate about potentially lower risk cigarettes is unencumbered by opportunistic criticism

We consider the development of lower risk tobacco products a priority and are currently working on three strands of research aimed at product modifications that might be accepted as reducing risks. These are the continued development of very low tar cigarettes acceptable to consumers, lower tar cigarettes with certain smoke constituents reduced further, and novel designs that significantly change the composition of smoke. Our proposals include promoting a scientific forum to discuss which product changes would be supported by public health groups and might gain consumer acceptability, and how new products might be tested and promoted.



BRITISH AMERICAN TOBACCO

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BRITISH AMERICAN
TOBACCO

Directors' Report and Accounts 1999

COMPANY NO. : 3407696

British American Tobacco p.l.c.

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Financial Statements of British American Tobacco p.l.c.

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This document contains the Directors' Report, the annual accounts and the Report of the Auditors for the year ended 31 December 1999. The Chairman's Statement, the Managing Director's Review and the Finance Director's Review are contained in a separate booklet – the Annual Review and Summary Financial Statement.

The Annual Review and Summary Financial Statement together with the Directors' Report and Accounts comprise the full annual report and accounts of British American Tobacco p.l.c. for 1999 in accordance with the Companies Act 1985.



Directors' Report

The Directors present their Report together with the audited Group accounts for the year ended 31 December 1999.

British American Tobacco p.l.c. (the 'Company') is a holding company which owns, directly or indirectly, investments in the numerous companies constituting the British American Tobacco Group of companies. The principal subsidiaries, associates and joint venture are listed on pages 50 to 52.

The Chairman's Statement on pages 2 and 3 of the Annual Review and Summary Financial Statement reports the progress made in the financial year under review and outlines future developments.

Details of the Group's overall performance are given on pages 4 to 24 of the Annual Review and Summary Financial Statement.

Changes in the Group

Rothmans

On 11 January 1999 the Company announced that it had reached agreement on the terms of a proposed merger with Rothmans International B.V. ('Rothmans'). Under the terms of a Transaction Agreement entered into between the Company and Compagnie Financière Richemont AG ('Richemont'), Rembrandt Group Limited ('Rembrandt') and Rothmans International Holdings S.A. (now 'R & R Holdings S.A.') the Company was to acquire the Rothmans issued share capital and, in consideration, would issue ordinary shares of 25p ('ordinary shares') and convertible redeemable limited voting participating preference shares of 25p each ('convertible preference shares') to R & R Holdings S.A., a holding company of Rothmans jointly indirectly owned by Richemont and Rembrandt.

The merger was subject to various regulatory clearances detailed in the Company's listing particulars dated 15 March 1999 and to the approval by the shareholders of the Company and Rembrandt, which approval was given at shareholder meetings of both companies on 8 April 1999.

Following these approvals the merger was completed on 7 June 1999 whereupon the Company issued to R & R Holdings S.A. 604,336,627 ordinary shares and 241,734,651 convertible preference shares. The new shares accounted for approximately 35 per cent of the fully diluted ordinary share capital of the Company, 25 per cent in ordinary shares and 10 per cent in convertible preference shares, whilst the voting interest is limited to a maximum of 25 per cent, as set out in note 1 on page 4. Further information about changes to the Company's share capital during the year is set out in note 44 on page 74.

The impact of this acquisition is more fully described on page 20 of the Annual Review and Summary Financial Statement and note 21 (page 39) of this Directors' Report and Accounts.

R & R Holdings S.A. has given notice under the Articles of Association of the Company, of its intention to redeem one half of the convertible preference shares in June 2000 at a price of 575p per share. The total cost of the redemption would be £695 million.

On the fifth anniversary of the completion of the transaction (7 June 2004), the Company will be required to redeem all the convertible preference shares not previously redeemed at a price of 675p each.

Rothmans Inc., Canada

On 3 February 2000, the Group sold its entire shareholding in Rothmans Inc., Canada in a public offering on the Toronto Stock Exchange for C\$13.35 per share.

Imasco

On 3 August 1999, the Company announced that it had entered into an agreement with Imasco Limited ('Imasco') to acquire for cash all Imasco common shares not already owned by the Group, representing approximately 58 per cent of the Imasco common shares in issue, through a wholly-owned Canadian subsidiary (British American Tobacco (Canada) Limited ('British American Tobacco (Canada)').

The agreement with Imasco dated 2 August 1999 provided for a minimum cash consideration of C\$40 per Imasco common share which could be increased depending on the outcomes of sales processes for Imasco's retailing business, Shoppers Drug Mart ('Shoppers') and its Genstar land development company ('Genstar'). On 18 November 1999 the Company announced that it had agreed with Imasco a final price of C\$41.60 per Imasco common share and that it had accepted an offer from an investor group led by Kohlberg Kravis Roberts & Co. ('KKR') to purchase Shoppers for C\$2.55 billion in cash conditional upon completion of the acquisition of Imasco.

Concurrently with the Imasco agreement dated 2 August 1999, the Company entered into an agreement with Toronto Dominion Bank ('TD Bank'), under which TD Bank made an offer (the 'Offer') of C\$67 per share for all of the issued common shares of CT Financial Services Inc. ('CT') owned by Imasco. The Company also agreed to cause British American Tobacco (Canada) to deposit all of the common shares in the capital of CT currently owned by Imasco to the Offer.

Directors' Report continued

The acquisition of Imasco was completed on 1 February 2000, at which time Imasco was amalgamated with British American Tobacco (Canada) to form Imperial Tobacco Canada Limited ('Imperial Tobacco'). The offer by TD Bank for CT was completed immediately following the Group's acquisition of the Imasco common shares and the proceeds to the Group of C\$7.85 billion were used in part to satisfy the consideration of C\$10.4 billion payable for the Imasco common shares. The sale of Shoppers to KKR was completed on 4 February 2000.

The sale process for Genstar is continuing. The Company will retain the full net proceeds from a future sale of Genstar. Once Genstar is sold, the British American Tobacco Group's only business in Canada will be the tobacco business operated by Imperial Tobacco, the leading Canadian tobacco company with a market share of approximately 69 per cent of the Canadian cigarette market.

Accounting policies

During 1998 the principal financial services businesses of B.A.T Industries p.l.c. were demerged and British American Tobacco p.l.c. became the listed parent company for the retained businesses. The Group accounts are presented as if British American Tobacco p.l.c. had been the Group's parent company for each year presented.

To comply with company law and accounting standards the Group accounts for 1998 included the results of the financial services businesses up to the date of demerger. The Group accounts for 1999 are set out on pages 16 to 71 of this Directors' Report and Accounts, with the primary statements (including demerged businesses in 1998) on pages 58 to 62.

However, to provide information which is helpful to the Company's shareholders, in 1998 the Directors also presented financial information prepared as if the demerger had taken effect prior to 1998. As this is the basis which more clearly reflects the ongoing operations of the Company, the Directors believe it is necessary to include financial information with comparatives prepared on this basis. This additional information has been presented, together with the related accounting policies and notes, on pages 16 to 47 and 50 to 54, with the primary statements on pages 18 to 21.

In the segmental analyses published for 1998 the costs of the headquarters for B.A.T Industries p.l.c. were shown separately. To provide 1998 comparatives on a more consistent basis with the segmental results for 1999, the comparatives have been restated to allocate these costs within the regional results.

During the year two new accounting standards were implemented, being FRS12 on provisions and FRS13 on financial instruments. While these standards have resulted in some additional disclosures they have not affected profit or shareholder's equity.

Directors

The names of the current Directors of the Company are shown on pages 26 and 27 of the Annual Review and Summary Financial Statement.

Directors' interests

The interests (all of which are beneficially held) of the Directors of the Company in the issued share capital of the Company, according to the register maintained under Section 325 of the Companies Act 1985 (which is open to inspection at the registered office) are shown below. Their interests in share options are shown on page 11 of the Remuneration Report.

The following table shows their interests over ordinary shares for the period 1 January (or their date of appointment, if later) to 31 December 1999.

British American Tobacco p.l.c.

Ordinary Shares of 25p

	At 1 January 1999*	At 31 December 1999	At 6 March 2000
M F Broughton	146,667	176,115	176,115
K H Clarke	2,192	4,091	4,091
U G V Herter	26,282	26,902	26,902
W P Ryan	—	20,000	20,000
K S Dunt	7,066	7,686	7,686
H Einsmann	—	—	—
W A Owens	—	—	—
R L Pennant-Rea	1,023	3,023	3,023
J P du Plessis	—	—	—
J P Rupert	—	—	—
K S Wong	—	—	—

* Or date of appointment, if later.



In addition, on 31 December 1999 and at the date of this report, the Group's employee share ownership trusts referred to on page 10 of the Remuneration Report held a total of 15,581,616 ordinary shares in the Company. All employees, including the executive Directors (but with the exception of Bill Ryan), are deemed to have a beneficial interest in these shares.

No Director has had any material interest in a contract of significance (other than service contracts) with the Company or with any subsidiary company during the year.

Directors proposed for reappointment

In accordance with the Articles of Association, the Directors named below retire from the Board at the forthcoming Annual General Meeting and, being eligible, offer themselves for reappointment. Of these, Bill Ryan, Jan du Plessis and Johann Rupert were appointed to the Board of Directors on 7 June 1999 upon completion of the merger with Rothmans. Biographical information on each of these Directors is set out on pages 26 and 27 of the Annual Review and Summary Financial Statement and is also contained in the Secretary's letter which accompanies the Notice of Annual General Meeting of the Company.

Name

M F Broughton
H Einsmann
R L Pennant-Rea
J P du Plessis
J P Rupert
W P Ryan

Annual General Meeting

The next Annual General Meeting of the Company will be held on 27 April 2000. Details of the business to be proposed at the meeting are contained in the Notice of Annual General Meeting.

New All Employee Share Plan

The Government has proposed a new all employee share plan to encourage wider share ownership. Full details of the new plan are expected to be published with the Finance Bill 2000 and will become law later this year. The Directors are reviewing the proposals and wish to obtain approval from the shareholders at the forthcoming Annual General Meeting to establish the new plan based upon the proposals as they currently stand. The Directors will wait until the final details of the new plan are published before taking any decision to either implement or operate it.

Further information about the new plan is contained in the Secretary's letter which accompanies the Notice of Annual General Meeting.

Dividends

Details of dividends in respect of 1999 are given on page 27 note 6.

The Board has recommended to shareholders a final dividend of 17.9p per ordinary share for the year to 31 December 1999. This dividend will be paid on 3 May 2000 to shareholders registered in the books of the Company on 17 March 2000.

Analyses of shareholders

At 31 December 1999 there were 2,176,902,616 ordinary shares in issue held by 99,067 shareholders.

These shareholdings are analysed as follows by category of shareholder and size of shareholding:

Category of shareholder	Number of holders	Percentage of total holders	Number of ordinary shares	Percentage of issued share capital
Individuals	79,751	80.50	107,821,625	4.95
Banks	79	0.08	478,145	0.02
Nominee companies	16,262	16.42	1,387,442,510	63.73
Insurance companies	18	0.02	31,381,767	1.44
Pension funds	20	0.02	4,079,816	0.19
Other corporate holders	2,936	2.96	41,362,126	1.90
R&R Holdings S.A.	1	-	604,336,627	27.77
	99,067	100.00	2,176,902,616	100.00

Size of shareholding	Number of holders	Percentage of issued share capital
1 - 1,999	76,906	2.25
2,000 - 9,999	19,130	3.23
10,000 - 199,999	2,365	4.34
200,000 - 499,999	309	4.48
500,000 and over	357	85.70
	99,067	100.00

Directors' Report continued

Substantial shareholdings

At 6 March 2000, the following persons held an interest in the ordinary shares of the Company that is required to be recorded in the register of substantial interests maintained pursuant to Section 211 of the Companies Act 1985.

Size of shareholding	Number of ordinary shares	Percentage of issue
R & R Holdings S.A. 1 2	604,336,627	27.77
Brandes Investment Partners, L.P.	122,183,850	5.60

Notes:

1. Pursuant to the Standstill Agreement dated 11 January 1999 entered into between the Company and R & R Holdings S.A. (then named Rothmans International Holdings S.A.), Compagnie Financière Richemont AG and Rembrandt Group Limited (together 'the R and R Parties') the R and R Parties gave certain undertakings to the Company including the following: (a) that the R and R Parties and persons acting in concert with any of them will not exercise at any general meeting of the Company more than 25% of the voting rights attached to shares of a class carrying rights to vote in all circumstances at general meetings of the Company and (b) the interests of the R and R Parties and persons acting in concert with any of them in the issued ordinary share capital of the Company will not exceed 27.8% except in certain specified circumstances e.g. the Company making a purchase of its own shares or otherwise having reduced its issued share capital.

2. Compagnie Financière Richemont AG, Rembrandt Group Limited, British American Tobacco p.l.c. and R&R Holdings S.A. (then named Rothmans International Holdings S.A.) are parties to an agreement dated 11 January 1999 ('the Agreement') to which Section 204(2) of the Companies Act 1985 applies by virtue of the acquisition on 7 June 1999 of shares in British American Tobacco p.l.c. The number of such shares is 604,336,627 ordinary shares and 241,734,651 preference shares as defined in the Agreement.

Purchase of own shares

At the Annual General Meeting of the Company held on 29 April 1999 the Company was given authority to purchase up to 157,000,000 of its ordinary shares. This authority will expire at the Annual General Meeting to be held on 27 April 2000. Although no ordinary shares have been purchased by the Company during the period from 29 April 1999 to the date of this report, the Directors at the Annual General Meeting will be seeking fresh authority for the Company to purchase its ordinary shares.

Stock Market listings

The Company's ordinary shares are listed on the London Stock Exchange. They are also traded on the American Stock Exchange, New York, in the form of American Depositary Receipts.

Auditors

A resolution will be proposed at the Annual General Meeting for the reappointment of PricewaterhouseCoopers as auditors and to authorise the Directors to determine their remuneration.

Charitable and political contributions

Details of payments for charitable purposes made by the Group during the year ended 31 December 1999 are given on page 25 of the Annual Review and Summary Financial Statement.

The Company and its subsidiaries gave no money for political purposes in the UK during the period under review.

Employees

Details of the Group's employment policies are given on page 25 of the Annual Review and Summary Financial Statement.

Research and development

The Group's research and development activities are concentrated on the development of new products, new processes, quality improvement of existing products and cost reduction programmes in the tobacco industry.

Research is also undertaken into various aspects of the science and behavioural science related to smoking, and the Group continues to provide significant funding for independent studies.

Millennium

Throughout 1999, the Millennium Programme remained a top business priority. By the final quarter remediation activities were complete for over 99 per cent of systems, business continuity plans had been put in place throughout the organisation and detailed arrangements for the transition period around the critical date change were in place.

A Millennium Transition Office monitored the rollover of Group companies worldwide. In the event, all operations returned to business as usual as scheduled shortly after 1 January 2000. The Company remained vigilant for further date changes, for example 29 February 2000, and reports that all businesses performed as usual.

The final estimate for expenditure to tackle the issue of the millennium date change across the merged group is £72 million. This reduction from the £90-100 million reported for the third quarter of 1999 reflects reduced contingency costs and more rapid programme closure as a result of the smooth transition.



Creditor payment policy

Given the international nature of the Group's operations, there is not a Group standard code in respect of payments to suppliers. Operating subsidiaries are responsible for agreeing terms and conditions for their business transactions when orders for goods and services are placed, ensuring that suppliers are aware of the terms of payment and including the relevant terms in contracts where appropriate. These arrangements are adhered to provided that suppliers meet their contractual commitments.

Creditor days have not been calculated for the Company as it is an investment holding Company and had no trade creditors at 31 December 1999.

OECD Guidelines

The Group recognises its responsibilities to the countries in which it operates and supports the OECD Guidelines for Multinational Enterprises in their current form, which seek to encourage the positive contributions multinational enterprises can make to economic and social progress in OECD member countries and elsewhere in the world.

Intra Group pricing

The prices agreed between Group companies for international sales of materials and manufactured goods are based on normal commercial practices which would apply between independent businesses. Intra group charges for royalties, commissions, services and fees are also based on the principles of normal commercial practice between independent businesses.

European Monetary Union

The Company, as a matter of policy, actively supports Economic and Monetary Union as a means of delivering increased stability and prosperity. The Group's European companies including those in the UK have been capable of transacting business in the euro following its introduction in eleven European countries on 1 January 1999. The ability of the Group to conduct business in national currencies will be retained as long as necessary. The decision as to when to adopt the euro as a subsidiary's functional currency will be a local decision for each subsidiary in the European Union, having regard to the speed of transition to the euro in the individual economy.

Each operating subsidiary has prepared a business impact plan assessing the risks and uncertainties associated with the euro, with all end-market activity in the euro being coordinated through a European Regional Support Team. Costs incurred in 1999 on the euro programme had no material effect on the Group's business performance and the Company is still finalising estimates of costs expected for 2000.

On behalf of the Board
Philip Cook, Secretary
7 March 2000

Remuneration Report

This report has been prepared by the Board in accordance with the requirements of the Combined Code adopted by the London Stock Exchange. It covers the level and make-up of Directors' remuneration, the remuneration policy and a number of formal disclosures relating to individual Directors' remuneration.

The Remuneration Committee

The Remuneration Committee is responsible for the following key areas:

- Recommending to the Board the Company's policy on the terms of employment, including remuneration, of executive Directors and other members of the Management Board and their specific remuneration packages;
- Reviewing the overall performance of the Chairman and the Managing Director on an annual basis.

The Committee currently comprises all the non-executive Directors and is chaired by Kenneth Clarke. Harald Einsmann became a member on 1 April 1999 and Johann Rupert joined the Committee on completion of the merger with Rothmans on 7 June 1999. Jan du Plessis joined the Committee on 3 March 2000.

The Board considers that all the non-executive Directors on the Remuneration Committee are independent of management and are free from any business or other relationship which could materially interfere with the exercise of their independent judgement.

The Chairman and the Managing Director may be invited to attend meetings of the Committee when their own remuneration is not under consideration and the Secretary to the Committee is the Company Secretary. The Chairman and the Managing Director are consulted in respect of the remuneration of the Deputy Managing Director, the Finance Director and other members of the Management Board. The Committee has access to professional advice from both internal and external sources in order to develop the Company's policy.

Remuneration policy

The remuneration policy is designed to reflect the highly international and competitive nature of the Group's operations so that high quality executives with proven business experience can be recruited, motivated and retained. This is fundamental to the Group's declared vision to be the world's leading international tobacco group. The Company aims to follow

best practice in relation to its remuneration policy and, in particular, complies with the relevant Principles set out in the Combined Code.

The implementation of this policy has resulted in a structured and balanced remuneration package for each executive Director and member of the Management Board, the main elements of which are as follows:

- The establishment of base salary levels for each of the executive Directors and members of the Management Board having regard to the market levels paid for equivalent positions in other leading international companies based in the UK. In arriving at its conclusions on these matters, the Committee takes account of the performance of the business and the performance of the individual executive in the geographical or functional area for which he is responsible. The Committee recognises that the requirements of recruitment or retention may on occasion justify the payment of a salary outside the range regarded as appropriate to a particular position;
- The award of bonuses which are specifically linked to measured performance against demanding objectives set annually;
- The award of ordinary shares in the Company under the Long Term Incentive Plan;
- The provision of retirement benefits through the Group's pension plans.

Further details on the individual elements of the remuneration packages of the executive Directors are given on the next page.

Executive Directors' service contracts

With the exception of Bill Ryan details of whose service contract with the Company are set out below, each service contract for the executive Directors can be terminated by the Company on giving two years' notice. However, the Company has reserved the right to terminate without notice provided it makes a severance payment equivalent to one year's salary, bonus and benefits. Executive Directors are entitled to refuse such a payment and instead demand a payment based upon strict notice rights, in which event the Director concerned will be expressly required to



mitigate his loss. Accordingly, the Company would not expect to pay the full value of the two year notice period in the event of the termination of a Director's employment.

Bill Ryan joined the Board as Deputy Managing Director on 7 June 1999 following completion of the merger with Rothmans. His contract of employment is for a fixed period of two years from that date unless terminated by either the Company or Bill Ryan prior to 7 June 2000. In such circumstances either party may elect that a severance payment be made to Bill Ryan equal to 12 months pay, including accrued bonus and benefits.

Directors' remuneration

An audited analysis of the remuneration paid by the Group in respect of 1999 to the Directors of British American Tobacco p.l.c. is shown in table 1 below:

Table 1. Directors' remuneration

	Salary/fees £	Performance related pay and deferred bonus £	Benefits in kind £	1999 Total £	1998 Total £
M F Broughton	696,171	639,000	20,530	1,355,701	1,017,394
K H Clarke	100,000	-	-	100,000	67,820
U G V Herter	520,620	420,000	16,962	957,582	642,971
W P Ryan	256,154	315,000	-	571,154	-
K S Dunt	323,550	280,000	15,095	618,645	104,983
H Einsmann	26,250	-	-	26,250	-
W A Owens	41,796	-	-	41,796	23,842
R L Pennant-Rea	33,750	-	-	33,750	30,000
J P du Plessis	17,077	-	-	17,077	-
J P Rupert	19,923	-	-	19,923	-
K S Wong	35,000	-	-	35,000	23,333
Total remuneration	2,070,291	1,654,000	52,587	3,776,878	1,910,343

Notes:

1. The remuneration shown for Bill Ryan, Harald Einsmann, Jan du Plessis and Johann Rupert is for the period since the date of appointment.
2. The remuneration shown in the table above for 1998 in respect of Keith Dunt is for his qualifying services as a Director of the Company which commenced on 8 September 1998. The remuneration shown for 1998 in respect of Martin Broughton, Ulrich Herter and Rupert Pennant-Rea includes the remuneration paid to them as Directors of B.A.T Industries p.l.c. prior to the demerger in September 1998.
3. Deferred bonus includes an exceptional deferred share bonus referred to on page 8 of the Remuneration Report.

Remuneration Report continued

The remuneration paid to the executive Directors was totally in relation to their services as managers.

Executive Directors' performance related bonus plans

The executive Directors participate in the Directors' Incentive Bonus Scheme. Under the scheme, a Director's bonus depends on the performance of the business. Demanding targets are set at the beginning of each year and are measured in terms of both financial and business performance. The financial element includes, amongst others, profit, cash flow and earnings per share. The business elements are related to a variety of strategic goals, most of which are normally of a long term nature although for 1999 they related specifically to a variety of marketing objectives and to the integration of Rothmans. Bonus entitlements are determined by the Remuneration Committee and carry a value which, under the scheme, may range from nil to a maximum of 75 per cent of base salary for the Chairman and to 50 per cent of base salary for the other executive Directors. Bonus payments are charged in the year to which they relate, and provision is made accordingly.

In addition, the Remuneration Committee has decided to award an exceptional bonus of 40 per cent of basic salary to members of the Group's senior management who participate in the Company's executive share schemes in order to reward them for their contribution to the success of the merger with Rothmans. These bonuses will be held in the form of ordinary shares in the Company and normally remain in trust for three years. Participants will normally forfeit the shares if they resign in this period.

Executive Directors' pensions benefits

The executive Directors with the exception of Bill Ryan are, like other employees, eligible for membership of the B.A.T Pension Scheme which covers employees in the UK. Upon completion of the merger with Rothmans, Bill Ryan elected to take an early retirement pension from the Rothmans International UK Pension Fund. The B.A.T Pension Scheme is a non-contributory defined benefit scheme and includes provision for spouse benefits on death in service or after retirement equal to half of the member's pension.

The early retirement rules in the Pension Scheme permit payment of the accrued retirement pension from age 55 without actuarial reduction subject to the Company's agreement.

Accrual rates differ according to individual circumstances but do not exceed one-fortieth of salary for each year of pensionable service. Pensionable pay covers base salary only with bonus awards and the value

of benefits in kind not being pensionable. Ulrich Herter joined the Pension Scheme after 1989 and is subject to the Inland Revenue cap on earnings (currently £90,600) which may be pensioned through an approved scheme. Accordingly, he has an unfunded promise of a supplemental pension benefit from the Company on an equivalent basis in respect of earnings above the cap. He also has an unfunded preserved pension benefit in respect of his service with British-American Tobacco (Germany) GmbH prior to his moving to the UK in January 1992. As a former employee of Rothmans in Germany, he also has a retained promise from Rothmans Germany GmbH, which became part of the British American Tobacco Group on 7 June 1999 following completion of the merger. The annual value of that promise is fixed until retirement at DM 49,479 (£15,758) and therefore no further entitlements accrued during the year, nor was there any increase for inflation. The unfunded commitments are included in the provisions referred to on page 44 note 24 to the accounts.

Table 2. Executive Directors' pension entitlements

	Age at 31 Dec 1999	Pension p.a. accruing during 1999 ¹ £	Total accrued pension p.a. as at 31 Dec 1999 ² £
M F Broughton	52	47,186	448,537
U G V Herter ³	57	13,846	258,785
K S Dunt	52	62,173	185,551

Notes:

1. The increase in accrued pension during the year excluding any increase for inflation.
2. The pension entitlement shown is that which would be paid annually on retirement based on service to the end of the year.
3. Ulrich Herter's pension entitlement includes the effect of the relative exchange rate movement between sterling and the deutschemark/euro. It also includes pension accruing under the unfunded promise of a supplemental pension benefit referred to above.
4. Members of the B.A.T Pension Scheme have the option of paying additional voluntary contributions; neither the contributions nor the resulting benefits are included in the table.
5. The normal retirement age for Martin Broughton and Keith Dunt is 59. The normal retirement age for Ulrich Herter is 60.

Share options and share incentive schemes

The executive Directors are eligible to participate in the following employee share schemes which are designed to incentivise employees of the Group: the Share Participation Scheme, the Sharesave Scheme, the Share Option Scheme and the Long Term Incentive Plan. Under his service contract Bill Ryan is only entitled to participate in the Sharesave Scheme



and the Share Participation Scheme. The Board and/or the Remuneration Committee selects from time to time which of these schemes will be operated. The Remuneration Committee determines whether executive Directors and members of the Management Board are eligible to participate in the Long Term Incentive Plan or the Share Option Scheme. Individuals who receive awards under the Long Term Incentive Plan in any year do not normally also receive options under the Share Option Scheme. All benefits under the employee share schemes are non-transferable and non-pensionable.

It is the policy of the Board that in future executive Directors and other members of the Management Board will normally participate in the Long Term Incentive Plan rather than the Share Option Scheme.

Share Participation Scheme

All UK employees, including executive Directors, benefit from the Company's Share Participation Scheme which is an approved profit-sharing scheme under Schedule 9 of the Income and Corporation Taxes Act 1988. An appropriation of shares was made on 1 April 1999 up to a maximum value of £3,200 to each UK-based employee under the Scheme.

Sharesave Scheme

Eligible employees, including UK-based executive Directors, have been granted employee savings-related share options to subscribe for ordinary shares in the Company.

Prior to the demerger of B.A.T Industries p.l.c. in 1998, options were granted under the B.A.T Industries Savings-Related Share Option Scheme (the 'ESRO Scheme').

The Company established the British American Tobacco Sharesave Scheme (the 'Sharesave Scheme') in 1998 which allows for options granted to be exercisable in conjunction with either a three-year or five-year savings contract. The first grant of options under the Sharesave Scheme took place in November 1998 and a further grant was made in November 1999.

Options are normally granted at a discount of 20 per cent to the market price at the time of the invitation, as permitted under the rules of the Sharesave Scheme.

Share Option Scheme

The Company established a share option scheme, the British American Tobacco Share Option Scheme (the 'Scheme') in 1998. The Scheme comprises an Inland Revenue Approved part and an Unapproved part. Under the Approved part of the Scheme, options may be granted over

ordinary shares up to a total market value of £30,000 on the date of the grant whilst any amount over and above that limit would be made under the Unapproved part of the Scheme. All employees, including the executive Directors (but with the exception of Bill Ryan), are eligible to participate in the Scheme. The Scheme is operated by the Remuneration Committee in relation to the grant of options to Martin Broughton, Ulrich Herter and Keith Dunt and the remaining members of the Management Board although options are not normally granted in any year to individuals who receive an award under the Long Term Incentive Plan referred to below. Under normal circumstances, the Remuneration Committee considers whether to make a grant of options once a year. The value of options which may be granted on each occasion is limited to a percentage of base salary.

Options granted under the Scheme are not issued at a discount to the market price at the time of grant. Options are normally exercisable after the third anniversary of the date of the grant and lapse ten years after the date of their original grant, subject to a performance condition based on earnings per share growth. For options to be exercisable, the Company's published adjusted earnings per share growth has to exceed inflation by an average of 3 per cent per annum over any consecutive three-year period during the ten-year life of the options.

Long Term Incentive Plan

The Long Term Incentive Plan (the 'Plan') was established in 1998 by the Company and provides for awards of free ordinary shares to senior employees, including the executive Directors (but with the exception of Bill Ryan), provided certain demanding performance conditions are met. The Plan is operated each year by the Remuneration Committee in relation to awards to the executive Directors and members of the Management Board. The value of the award which may be granted on each occasion is limited to a percentage of base salary which cannot exceed 100 per cent for any single award. The first awards were made under the Plan in March 1999 based upon a market price of 526.5p and the percentage of salary applied ranged from 75 per cent to 100 per cent for the executive Directors and other members of the Management Board.

There are two performance measures attaching to the award of ordinary shares made in March 1999. These conditions are measured over a three year period which began on 1 January 1999 and ends on 31 December 2001:

- The first measure applies to 50 per cent of the award and relates to earnings per share growth relative to inflation. 50 per cent of the award will vest if earnings per share growth over the three year

Remuneration Report continued

performance period is an average of at least 9 per cent per annum in excess of inflation; 10 per cent will vest if the same figure is at least 3 per cent in excess of inflation and an award will vest on a pro rata basis between these two points.

- The second measure is based upon Total Shareholder Return ('TSR'). TSR performance combines both the share price and dividend performance of the Company during the performance period by reference to two comparator groups. The first of these is the constituents of the London Stock Exchange's FTSE100 index at the beginning of the performance period whilst the second is a peer group of international 'FMCG' (fast-moving consumer goods) companies. 25 per cent of the total award is based upon each of these two separate measures. 25 per cent of the total award vests in full in the event of upper quartile performance by the Company relative to one of the comparator groups, 7.5 per cent of the total award will vest in the event of median performance and then pro rata between these two points.

To the extent that the performance conditions have been satisfied, awards are normally exercisable between three and ten years after they have been granted. It is possible for some of the shares in an award to be released if one of the performance conditions has been met, even if the other performance conditions have not been met. An award of shares lapses to the extent that the performance conditions are not satisfied in accordance with the measures set out above at the end of the three year performance period.

B.A.T Industries Employee Share 'E' and 'D' Option Schemes

Prior to the demerger, options were granted under the B.A.T Industries Share 'E' Option Scheme (the 'E' Scheme). Options granted under the 'E' Scheme, as with the B.A.T Industries Employee Share 'D' Option Scheme (the 'D' Scheme) which it replaced in 1994, were not issued at a discount to the market price at the time of grant.

Options granted under the 'E' Scheme and the 'D' Scheme are normally exercisable between the third and the tenth anniversary of the date of grant.

At the time of the demerger, British American Tobacco p.l.c. made an offer of replacement options of equivalent value over ordinary shares in the Company to continuing employees of the Group, including the executive Directors of the Company, who did not exercise their 'E' or 'D' Options. The replacement option price and associated number of replacement options were calculated to ensure that the total monetary value of the replacement options was equal (as nearly as possible) to the total monetary value of the ordinary shares in B.A.T Industries p.l.c.

Replacement options continue to be governed under the rules of the 'E' or 'D' Schemes, as applicable.

Options and awards outstanding

To satisfy the future exercise of options or awards under the Group's employee share schemes, ordinary shares are acquired in the market by two separate Employee Share Ownership Trusts ('ESOTs'). New ordinary shares are issued by the Company only in relation to the ESRO Scheme, the Sharesave and the 'D' Option schemes.

Under the ESRO Scheme and Sharesave Scheme, a total of 7,403,509 options over ordinary shares in the Company were outstanding at 31 December 1999. These options are exercisable until May 2004 at option prices ranging from 218.34p to 418p.

Under the 'D' Option Scheme, a total of 126,179 options over ordinary shares in the Company were outstanding at 31 December 1999. These options are exercisable until September 2004 at prices ranging from 173.8p to 315.6p.

The first ESOT, the B.A.T Industries Employee Share Ownership Plan, was set up with an interest-free loan from B.A.T Industries p.l.c. to satisfy the future exercise of options under the 'E' Scheme. The loan from B.A.T Industries p.l.c. amounted to £26.5 million at 31 December 1999 (1998 £28 million).

The second ESOT, The British American Tobacco Group Employee Trust, was set up with an interest-free loan from the Company in September 1998 to satisfy the future exercise of options under the Scheme. In addition, this trust was set up to satisfy the exercise of awards of ordinary shares made under the Plan. As the exercise of an award under the Plan does not involve a payment from the participant to the Company, the Company funds the purchase of ordinary shares by the trust by way of a gift in accordance with the terms of the Trust Deed. The loan to the trust amounted to £37.3 million at 31 December 1999 (1998 £21 million). Both loans will be repaid from the proceeds of the exercise of options or, if the options lapse, ordinary shares may be sold by the ESOTs to cover the loan repayment. The ESOTs waive dividends on the ordinary shares held by them. As at 31 December 1999, the two ESOTs held 15,581,616 ordinary shares (1 January 1999 10,700,826 ordinary shares). Both ESOTs waived payment of the interim dividend for 1998 of £554,841 in January 1999, the final dividend for 1998 and the special interim for 1999 of £2,869,333 in July 1999 and the second interim dividend of £603,139 in September 1999.



Executive Directors' options and awards

Audited information in respect of options and awards, held by the executive Directors of British American Tobacco p.l.c. during the year ended 31 December 1999 is contained in the following table:

The table shows the options and awards held by, or granted to, executive Directors of the Company over ordinary shares in the Company during the period from 1 January to 31 December 1999. No options or awards over ordinary shares lapsed or were exercised during that period by the executive Directors.

Table 3 – Executive Directors' options and awards over ordinary shares of 25p

	At 1 Jan 1999	Weighted average grant price	Granted in 1999		At 31 Dec 1999	Weighted average grant price	Expiry dates
			Number	Weighted average grant price			
M F Broughton							
E	328,269	333.9p	–	–	328,269	333.9p	2002-2005
ESRO	6,960	247.6p	–	–	6,960	247.6p	2001-2002
Share Option Scheme	149,700	434.2p	–	–	149,700	434.2p	2008
LTIP	–	–	123,456	526.5p	123,456	526.5p	2009
U G V Herter							
E	121,839	330.8p	–	–	121,839	330.8p	2003-2005
ESRO	3,671	265.4p	–	–	3,671	265.4p	2001
Share Option Scheme	110,548	434.2p	–	–	110,548	434.2p	2008
LTIP	–	–	91,168	526.5p	91,168	526.5p	2009
K S Dunt							
E	103,058	327.8p	–	–	103,058	327.8p	2002-2005
ESRO	7,397	232.9p	–	–	7,397	232.9p	2000-2002
Sharesave Scheme	–	–	1,920	316.4p	1,920	316.4p	2005
Share Option Scheme	55,274	434.2p	–	–	55,274	434.2p	2008
LTIP	–	–	45,732	526.5p	45,732	526.5p	2009

The closing mid-market price of ordinary shares in British American Tobacco p.l.c. on 30 December 1999, the last day of dealing in the Company's shares in 1999, was 351.75p and ranged from 335p to 675p from 1 January 1999 to 31 December 1999. The market price on 30 December 1999, did not in all cases, exceed the grant price of all the options detailed in table 3 above.

Corporate Governance Statement

The Company has continued to commit itself to the achievement of high standards of corporate governance. This has been defined as "the system by which companies are directed and controlled" and the Board is accountable for it to shareholders.

Each company listed on the London Stock Exchange is obliged to inform its shareholders how it has performed in relation to a set of corporate governance criteria called the Combined Code. This is in two parts - Principles and Provisions. A company must state how it has applied the Principles, giving enough explanation to enable shareholders to evaluate the statement, and whether it has complied with the Provisions. If not, it must provide an explanation.

The ways in which the Company has applied the Principles set out in the Code are described in this statement and in the Remuneration Report. With the exception of the notice periods under the service contracts of executive Directors, the Company has fully complied with the Provisions throughout the year.

Directors

The Board of the Company currently has eleven Directors, comprising the Chairman, three other executive Directors and seven non-executive Directors. The key functions of Chairman and Managing Director are clearly defined. The majority of the non-executive Directors are independent as set out in the Code. In this context, two of the non-executive Directors, Jan du Plessis and Johann Rupert, are not considered to be independent for all purposes because of the shareholdings they represent. All the non-executive Directors provide a considerable depth of knowledge and experience collectively gained from a variety of public and private companies. As non-executive Deputy Chairman, Kenneth Clarke acts as the senior independent director as envisaged by the Code Provisions.

The Board meets at least six times during the year and has reserved to itself key matters on which it alone may make decisions. Responsibility for implementing the Group's strategy is delegated to the *Management Board*, which meets at least eight times a year. This comprises the executive Directors and twelve senior Group executives. The Board has also established three Board Committees, each of which has clear terms of reference. These are:

The *Remuneration Committee*, whose composition and terms of reference are set out in the Remuneration Report on page 6.

The *Audit Committee* is comprised of all the non-executive Directors (with the exception of Johann Rupert) and is chaired by Rupert Pennant-Rea. The Managing Director and Finance Director attend meetings of the

Committee but are not members. The Committee meets regularly with management and with the internal and external auditors to review the effectiveness of internal controls, other matters raised in regular reports to the Committee and the full year financial statements prior to their submission to the Board. The Audit Committee receives reports from the Group's regional audit committees which monitor the effectiveness of business and financial controls across the Group. The Audit Committee is satisfied that the Company's auditors, PricewaterhouseCoopers, continue to be objective and independent of the Company. The auditors do perform non-audit services for the Company but the Audit Committee is satisfied that such work is best handled by the auditors because of their knowledge of the Group and that their objectivity is not impaired by reason of this further work.

The *Nominations Committee* is responsible for nominating, for approval by the Board, candidates for appointment to the Board and the Management Board. It is chaired by Martin Broughton and its other members are Ulrich Herter and all of the non-executive Directors.

There is open communication between senior executive management and Board members. The Board and its committees are supplied with high quality, up-to-date information for review prior to each meeting to enable them to discharge their responsibilities. All Directors have access to the advice and services of the Company Secretary and a procedure is in place for Directors to take independent professional advice, should this be required.

The Company's articles of association provide that one-third of directors must submit themselves for re-election each year at the Annual General Meeting. Further, any Director appointed during the year also has to seek re-election at the Annual General Meeting. In this way, each Director of the Board is required regularly to submit himself for re-election. Having regard to the size of the current Board, the period for submission for re-election for each Director would be every three or four years. In practice, the Company will require that each Director submits himself for re-election at intervals of not more than three years. The Directors who retire and offer themselves for re-election at this year's Annual General Meeting are set out on page 3.

In accordance with the Code, each new non-executive Director is appointed for a fixed term, being an initial period to the next Annual General Meeting after appointment and, subject to reappointment at that meeting, for a further three years. Subsequent reappointment will be subject to the approval of shareholders. Directors are given appropriate training on appointment and subsequently as necessary.



Directors' remuneration

The Remuneration Committee, which is comprised exclusively of non-executive Directors, has responsibility for executive remuneration. The remuneration of the non-executive Directors is determined by the Board. Information about the Company's remuneration policies and, in particular, the Directors' service contracts are found in the Remuneration Report on pages 6 and 7.

The Code states that there is a case for service contracts to be for one year or less. The contractual position of the Company's four executive Directors is explained in the Remuneration Report as above. The Remuneration Committee is unanimous that, in the context of a truly multinational group seeking to attract the best talent from around the world, this contractual position is appropriate to meet the interests of shareholders, the Company and the individual Directors concerned.

Relations with shareholders

The Principles encourage dialogue with institutional shareholders and use of the Annual General Meeting to encourage participation by private investors. The Company has regular dialogue with institutional shareholders where it believes this to be in the interests of shareholders generally. The Annual General Meeting provides a useful interface with shareholders and procedures at such meetings are in compliance with the Code. The availability of information about the Company to its shareholders has been improved by the development of its newly launched internet website at www.bat.com

Accountability and audit

The Board has reviewed in detail the contents of the Annual Review and Summary Financial Statement and the Directors' Report and Accounts in order to satisfy itself that the presentation is balanced and that the Company's position and prospects are understandable by shareholders.

A summary of the Directors' responsibilities in respect of the financial statements is given on page 14. The system of internal control designed to safeguard shareholders' investment and the Company's assets is set out below. The Audit Committee, whose composition and functions are described above, has considered in conjunction with the external auditors, the accounting policies adopted in the Group Accounts and has examined the internal controls which have been put in place in the Group.

Internal control

At the time of the publication of the Combined Code, the Institute of Chartered Accountants in England & Wales agreed with the London Stock Exchange that it would provide guidance to assist listed companies to implement the requirements in the Code relating to internal control. In

September 1999, the Turnbull Report was adopted by the London Stock Exchange to provide this necessary guidance for full compliance with the Combined Code.

Set out below is the Group Statement on internal control in accordance with the guidance provided by the Turnbull Report.

The Board is responsible for the overall system of internal control for the Company and its subsidiaries and for reviewing the effectiveness of these controls. The system is designed to manage risks that may impede the achievement of the Company's business objectives rather than to eliminate these risks. The internal control system can therefore only provide reasonable assurance, not absolute assurance, against material misstatement or loss.

There is and has been an ongoing process for identifying, evaluating, and managing the significant risks faced by the Company and its subsidiaries. This process has been in place throughout 1999 and is regularly reviewed by the Board. The Board includes on its agenda matters relating to significant risks that may impede meeting business objectives. In addition, internal control and business risk issues have been regularly reviewed by the six regional audit committees (chaired by either the Managing Director or Finance Director) and the Audit Committee as set out above. Regional and end market management, along with internal audit, support the Board in its role of ensuring a sound internal control environment.

British American Tobacco representation on the respective boards of significant associated companies provides the venue for addressing risk and control issues in these businesses.

The Board with advice from the Audit Committee has completed its annual review of the system of internal control in accordance with the Turnbull Report for the period since 1 January 1999 to the date of this report and is satisfied that it is in accordance with that guidance. The assessment included consideration of the effectiveness of the Board's ongoing process for identifying, evaluating, and managing the risks of the business and review of the work of regional audit committees in examining annual reports of internal control and business risks completed by operating companies.

Rothmans

The operations of Rothmans joined the Group on completion of the merger in June 1999. Consequently, although Rothmans had appropriate internal controls in place prior to the merger, the process described above was not in place throughout 1999 for those former Rothmans operations. However, implementation of this process is now in place for the whole Group and will be operational for the entire year 2000.

Statement of Directors' Responsibilities

The following Statement sets out the responsibilities of the Directors in relation to the financial statements. The report of the auditors, shown on page 15, sets out their responsibilities in relation to the financial statements.

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group 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, subject to any material departures being disclosed and explained;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed;
- 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 the Group 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 the Group, 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 they 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

Report of the Auditors to the members of British American Tobacco p.l.c.

We have audited the financial statements on pages 16 to 47 and 50 to 76. As explained in note 1 on page 16, the accounts include additional comparative financial information for the Group as if the demerger of the principal financial services businesses ('the demerged businesses') had taken effect prior to 1 January 1998.

Respective responsibilities of Directors and Auditors

The Directors are responsible for preparing the Annual Report. As described on page 14, this includes responsibility for preparing the financial statements, in accordance with applicable United Kingdom accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the London Stock Exchange and our profession's ethical guidance.

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 United Kingdom Companies Act. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the Company or Group 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 or the Listing Rules regarding Directors' remuneration and transactions is not disclosed.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts.

We review whether the statements on pages 12 and 13 reflect the Company's compliance with the seven provisions of the Combined Code specified for our review by the London Stock Exchange, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Company's or Group's corporate governance procedures or its risk and control procedures.

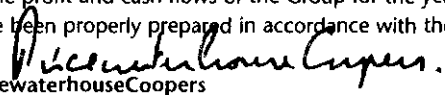
Basis of audit opinion

We conducted our audit in accordance with Auditing Standards 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 judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and Group'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 accounts 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 of the state of affairs of the Company and the Group at 31 December 1999 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.


PricewaterhouseCoopers
Chartered Accountants and Registered Auditors
1 Embankment Place
London
WC2N 6NN
7 March 2000

Accounting Policies

Group Accounts – excluding demerged businesses

1 Basis of accounting

On 7 September 1998 B.A.T Industries completed the demerger of its financial services businesses and their merger with Zurich Insurance Company. The remaining businesses were retained within British American Tobacco p.l.c., which became the new parent for B.A.T Industries p.l.c. and its subsidiaries on 8 September 1998, prior to which it had not commenced trading or made any profit or losses. The Company's acquisition of the entire share capital of B.A.T Industries p.l.c. has been accounted for as a merger and consequently these consolidated accounts have been presented as if it had been the parent company of the Group for each year presented.

As explained in the Directors' Report and in the accounting policies on page 55 it is necessary to provide accounts including the results of the demerged businesses in the comparatives. However, additional comparative financial information is provided on the Group as if the demerger had taken effect prior to 1 January 1998 and prepared on a basis consistent with the Listing Particulars for British American Tobacco p.l.c. issued in May 1998. This additional information has been presented, together with the related accounting policies and notes, on pages 16 to 47 and 50 to 54. It has been prepared as if the Group's interest in the share capital of the demerged businesses had been distributed by way of dividend prior to 1 January 1998 and reflects the amounts recorded in the accounts of the companies remaining after the demerger. As a result all central management and other similar costs of B.A.T Industries have been borne by the retained businesses. In addition the net amounts owed by demerged businesses to retained businesses include interest-free current accounts and therefore the net interest payable included in 1998 is not necessarily representative of the retained businesses as a separate Group. The accounts also include dividends from demerged businesses, shown after the profit for the year in the profit and loss account.

2 Basis of consolidation

The consolidated financial information includes the accounts of British American Tobacco and its subsidiary undertakings together with the Group's share of the results of its associated undertakings. Associates comprise investments in undertakings, which are not subsidiary undertakings, where the Group's interest in the equity capital is long term and over whose operating and financial policies the Group exercises a significant influence. They are accounted for using the equity method.

The results of subsidiary undertakings acquired during the period are included from the date of acquisition of a controlling interest at which date, for the purposes of consolidation, the purchase consideration is allocated between the underlying net assets acquired, other than goodwill, on the basis of their fair value.

The results of subsidiary undertakings, which have been sold during the period, other than demerged businesses, are included up to the date of disposal. The profit or loss on sale is calculated by reference to the net asset value at the date of disposal, adjusted for purchased goodwill previously written off to reserves on acquisition.

3 Goodwill on acquisitions prior to 1 January 1998 has been eliminated during the year of purchase against reserves. Goodwill on acquisitions from 1 January 1998 is capitalised and amortised over its useful economic life. Adjustments to provisional fair values of assets acquired in the preceding period are reflected as adjustments to goodwill.

4 Foreign currencies

Turnover, profits and cash flows expressed in currencies other than sterling are translated to sterling at average rates of exchange in each year. Assets and liabilities are translated at rates of exchange at the end of each year. For high inflation countries, the translation from local currencies to sterling makes allowance for the impact of inflation on the local currency results.

The differences between retained profits of overseas subsidiary and associated 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 overseas net assets at the beginning of the year, after taking into account related foreign currency borrowings. Other exchange differences, including those on remittances, are reflected in profit.

5 Revenue represents turnover of subsidiary undertakings and the Group's share of associates' turnover. Group turnover comprises sales to external customers and includes duty, excise and other taxes.

6 Pensions and post retirement benefits

The costs of providing pensions and post retirement health care benefits, calculated by reference to actuarial valuations, are charged against profits on a systematic basis with surpluses and deficits arising allocated over the expected average remaining service lives of current employees. Differences between the amounts charged in the profit and loss account and payments made to pension schemes are treated as assets or liabilities in the balance sheet.

7 Research and development revenue expenditure is charged against profits as incurred.



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

The Group's deferred tax is calculated as indicated below:

- (a) Deferred taxation is provided for on timing differences using the liability method to the extent that it is probable that the liability will crystallise. Timing differences arise on items of income and expenditure that are recognised for tax purposes in different periods from those in which they are recognised in the profit and loss account.
- (b) No account is taken of tax which may be payable on the realisation of investments held by Group companies. Deferred taxation is not provided on the undistributed profits retained by subsidiary and associated undertakings as such profits are considered to be permanently invested in those businesses.

9 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. Freehold and long leasehold land and buildings are depreciated at rates between 2.5 per cent and 4 per cent per annum, and plant, machinery and equipment at rates between 7 per cent and 25 per cent per annum. No depreciation is provided on freehold land.

10 Other investments are stated at cost less provisions, consistent with the concept of prudence.

11 Stocks are valued at the lower of cost and net realisable value. The method used in calculating cost, which includes raw materials, direct labour and overheads where appropriate, is average cost.

12 Leased assets

Assets held under finance leases are included under tangible fixed assets at their capital value and depreciated over their estimated useful lives. Leasing payments consist of capital and finance charge elements and the finance element is charged to the profit and loss account. The annual payments under operating leases are charged to the profit and loss account.

13 Geographical analyses are based on the five Regions through which the Group operates. The Group's principal associated company, Imasco Limited ('Imasco') which is incorporated in Canada, is shown separately.

Royalty income, less related expenditure, is included in the Region in which the licensor is based.

14 Financial instruments

The Group utilises a number of differing derivative instruments as part of its interest rate and exchange rate risk management. These instruments include interest rate swaps, swaptions, caps and collars and forward rate agreements as well as cross-currency swaps, tax equalisation swaps and forward foreign currency contracts.

Interest rate risk management

Interest differentials are recognised on an accrual basis and adjusted against interest payable. Initial premiums and discounts are amortised over the lives of the instruments. Where instruments are terminated early, gains and losses are amortised over their original lives if the underlying exposure remains in place or otherwise recognised immediately.

Exchange rate risk management

Cross-currency swaps are revalued at the balance sheet date and utilised to adjust the book values of the related foreign currency borrowings. Where forward foreign currency contracts are used to hedge existing assets and liabilities, the contract rates are used to value the related assets and liabilities. Gains and losses arising on hedges of future transactions are not recognised until the transactions occur.

Group Profit and Loss Account – excluding demerged businesses

for the year ended 31 December

	Notes	1999 £m	1998 £m
Revenue			
Subsidiary undertakings		18,798	14,584
Share of associates <i>page 53</i>		2,873	2,792
		21,671	17,376
Profit			
Subsidiary undertakings			
Turnover including duty, excise and other taxes		18,798	14,584
Duty, excise and other taxes		(9,726)	(7,464)
Turnover excluding duty, excise and other taxes		9,072	7,120
Other operating income	1	150	250
Operating charges	1	(8,123)	(6,694)
Operating profit		1,099	676
after charging: US tobacco settlements	1	(24)	(613)
integration costs	1	(357)	
goodwill amortisation	1	(162)	
after crediting: sales tax recovery	1		74
Share of associates and joint venture <i>page 53</i>		380	335
Total operating profit		1,479	1,011
Sale of brands	2	88	
Demerger and restructuring costs	2		(46)
Profit on ordinary activities before interest		1,567	965
Subsidiary undertakings: investment income	3	195	147
interest payable	4	(365)	(351)
Share of associates' interest paid less received <i>page 53</i>		(26)	(23)
Profit on ordinary activities before taxation		1,371	738
Taxation on ordinary activities	5	(673)	(277)
Profit on ordinary activities after taxation		698	461
Minority interests		(142)	(115)
Profit for the year <i>page 19</i>		556	346
Dividends from demerged businesses	28		123
Dividends and other appropriations: ordinary shares	6	(546)	(377)
convertible redeemable preference shares	6	(74)	
Retained (loss)/profit		(64)	92
Earnings per share: basic – unadjusted	7	25.25p	22.17p
diluted – unadjusted	7	27.02p	21.98p
– adjusted	7	52.33p	46.12p

As explained on page 39 note 21 the results for 1999 include the acquired Rothmans businesses for the period from 7 June 1999 to 31 December 1999. There is no difference between the profits on ordinary activities before taxation and the retained profits for the year stated above and their historical cost equivalents.

The retained profit with the exception of income from the non-tobacco businesses of Imasco (detailed on page 54) and (in 1998 only) dividends from demerged businesses, arises entirely from continuing operations.

Notes are shown on pages 23 to 47.



BRITISH AMERICAN
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Statement of Total Recognised Gains and Losses – excluding demerged businesses

for the year ended 31 December

	Notes	1999 £m	1998 £m
Profit for the year <i>page 18</i>		556	346
Differences on exchange	15	(268)	(69)
Total recognised gains related to the year <i>below</i>		288	277

Interest of British American Tobacco's Shareholders – excluding demerged businesses

for the year ended 31 December

	Notes	1999 £m	1998 £m
Balance 1 January	15	64	(97)
Total recognised gains related to the year <i>above</i>		288	277
Issue of shares:			
share options		3	42
Rothmans merger <i>page 39 note 21</i>		5,089	
Dividends from demerged businesses <i>page 18</i>			123
Dividends and other appropriations: <i>page 18</i>			
ordinary shares		(546)	(377)
convertible redeemable preference shares		(54)	
amortisation of discount on preference shares <i>page 74 note 44</i>		(20)	
Utilisation of ACT			96
Other		(3)	
Balance 31 December	15	4,821	64

Notes are shown on pages 23 to 47.

Group Balance Sheet – excluding demerged businesses

31 December

	Notes	1999 £m	1998 £m
Assets			
Fixed assets			
Intangible assets	8	5,338	
Tangible assets	9	2,456	2,048
Investments in associates and joint ventures	10	636	472
Other investments and long term loans	11	210	119
		8,640	2,639
Current assets			
Stocks	12	2,850	2,165
Debtors	13	2,000	1,493
Acquired business awaiting disposal	21	123	
Current investments	14	768	185
Short term deposits and cash		1,853	970
		7,594	4,813
Total assets		16,234	7,452
Liabilities			
Capital and reserves			
Share capital		605	393
Share premium account		4	1
Merger reserves		4,726	
Other reserves		503	483
Profit and loss account		(1,017)	(813)
Shareholders' funds:	15	4,821	64
equity		3,347	64
non-equity		1,474	
Minority shareholders' equity interest		455	323
		5,276	387
Other liabilities			
Provisions for liabilities and charges	16	1,251	741
Borrowings	17	5,676	3,730
Creditors	19	4,031	2,594
		10,958	7,065
Total funds employed		16,234	7,452

Notes are shown on pages 23 to 47.



Group Cash Flow Statement – excluding demerged businesses

for the year ended 31 December

	Notes	1999 £m	1998 £m
Net operating cash flow from subsidiary undertakings	27	1,995	1,096
Dividends from associates		90	86
Net cash inflow from operating activities		2,085	1,182
Returns on investments and servicing of finance	28	(206)	(282)
Taxation		(334)	(281)
Capital expenditure and financial investment	28	(281)	(351)
Net cash generation		1,264	268
Acquisitions less disposals	28	(216)	(16)
Equity dividends paid		(530)	(696)
Dividends from demerged businesses	28		242
Cash flow with demerged businesses	28		668
Cash flow before use of liquid resources and external financing		518	466
Management of liquid resources	28	(1,340)	459
Financing – proceeds from issue of shares		3	42
– increase/(decrease) in debt	28	853	(845)
		856	(803)
Increase in cash in the year <i>below</i>		34	122
Reconciliation of net cash flow to movement in net debt	29		
Increase in cash in the year <i>above</i>		34	122
(Increase)/decrease in debt		(853)	845
Increase/(decrease) in liquid resources		1,340	(459)
Change in net debt resulting from cash flow		521	508
Net debt acquired on purchase of subsidiaries		(754)	
Net funds disposed of on sale of subsidiaries		(23)	
Other changes		(33)	(45)
Differences on exchange		(191)	52
Movement in net debt in the year		(480)	515
Net debt at 1 January		(2,575)	(3,090)
Net debt at 31 December		(3,055)	(2,575)

Notes are shown on pages 23 to 47.



Notes on the Accounts

Segmental Analyses

(a) Turnover excluding duty, excise and other taxes analysis for subsidiaries is based on location of manufacture. Figures based on external sales in each region are as follows:

	1999 £m	1998 £m
America-Pacific	3,204	2,491
Asia-Pacific	1,207	959
Latin America	1,460	1,664
Europe	2,044	1,216
Amesca	1,157	790
	9,072	7,120

(b) Revenue including Group's share of associates is as follows:

	1999 £m	1998 £m
Including duty, excise and other taxes	21,671	17,376
Duty, excise and other taxes	(10,489)	(8,128)
Excluding duty, excise and other taxes	11,182	9,248

(c) The operations of subsidiaries are almost entirely related to tobacco. The Group's share of the operations of associates comprise the following businesses:

	Turnover excluding duty, excise and other taxes		Operating profit	
	1999 £m	1998 £m	1999 £m	1998 £m
Tobacco	824	721	225	217
Financial services	761	693	103	81
Other trading activities	525	714	52	37
	2,110	2,128	380	335

(d) Operating assets

	1999 £m	1998 £m
Total assets <i>page 20</i>	16,234	7,452
Less: goodwill	(5,338)	
investments in associates and joint venture	(636)	(472)
non-operating assets <i>note (e)</i>	(2,723)	(1,213)
operating creditors <i>note (f)</i>	(3,013)	(1,855)
<i>page 22</i>	4,524	3,912

(e) Non-operating assets

Acquired businesses awaiting disposal	123	
Other investments and long term loans	210	119
Current investments	768	185
Short term deposits	1,403	504
Taxation recoverable	131	394
Interest	88	11
<i>note (d)</i>	2,723	1,213

(f) Operating creditors

Total creditors	4,031	2,594
Less: dividends payable	(433)	(377)
UK and overseas taxation on profits	(248)	(198)
interest	(337)	(164)
<i>note (d)</i>	3,013	1,855

Notes on the Accounts

Profit and Loss Account

1 Operating profit

Other operating income in 1998 includes £74 million in respect of a sales tax recovery, following a favourable decision taken by a Regional Federal Court in Brazil. This is receivable in respect of amounts previously paid to the Government as social contributions assessed on the basis of sales. The amount is shown as additional information on the face of the profit and loss account.

	1999 £m	1998 £m
Operating charges comprise:		
Raw materials and consumables	1,980	1,887
Changes in stocks of finished goods and work in progress	69	(41)
Staff costs <i>note (a)</i>	1,251	996
Depreciation <i>note (c)</i>	350	297
US tobacco settlements – initial costs <i>note (d)</i>	24	613
– ongoing costs <i>note (d)</i>	746	106
Goodwill amortisation <i>note (e)</i>	162	
Other	3,541	2,836
Other operating charges <i>note (f)</i>	4,473	3,555
	8,123	6,694
<hr/>		
(a) Staff costs comprise:		
Wages and salaries	998	771
Social security costs	147	130
Other pension and post retirement benefit costs <i>note (b)</i>	106	95
	1,251	996
<hr/>		
(b) Other pension and post retirement benefit costs comprise:		
Funded plans – defined contribution	28	22
– defined benefit	24	28
Unfunded plans – defined benefit	54	45
	106	95
<hr/>		
(c) Depreciation includes:		
Depreciation in respect of assets held under finance leases	26	21
<hr/>		
(d) To the extent that payments arising under settlements reached in the USA in respect of litigation against the major tobacco companies are not subject to future sales, Brown & Williamson's share of the industry payments is charged as initial costs in the year of settlement. Other costs are shown as ongoing costs in the year to which they relate.		

(c) Depreciation includes:

Depreciation in respect of assets held under finance leases

(d) To the extent that payments arising under settlements reached in the USA in respect of litigation against the major tobacco companies are not subject to future sales, Brown & Williamson's share of the industry payments is charged as initial costs in the year of settlement. Other costs are shown as ongoing costs in the year to which they relate.

During the fourth quarter of 1998 agreement was reached with Attorneys General in 46 US states ('the Settling States') to settle the outstanding Medicaid recovery suits. The initial costs in respect of this agreement amounted to £463 million, principally comprising a £260 million up front payment and £130 million for plaintiffs' legal fees. The remaining £150 million of the initial costs in 1998 arises from the earlier settlement between the US cigarette companies and the State of Minnesota and Blue Cross and Blue Shield of Minnesota. This included initial payments to those parties, together with legal fees, and also included the impact of Most Favoured Nation clauses which increased amounts due under previous state settlements and advances on legal fees. During 1999 there was a further charge of £24 million in respect of one-off settlement compliance costs and liquidated legal fees.

These initial costs are shown as additional information on the face of the profit and loss account.



1 Operating profit *continued*

The US tobacco industry will incur ongoing costs under the agreement with the Settling States. The US tobacco manufacturers who entered into the agreement ('the settling companies') have agreed to make payments to the Settling States in perpetuity. The nominal value of payments by the four original settling companies over the first twenty five years of the agreement is approximately US\$219 billion. The actual payments will be adjusted annually to reflect changes in industry volume, inflation and other factors. Additionally the settling companies will pay fees of the Settling States' attorneys, and the amounts payable will be set by arbitration (with a US\$500 million annual cap for the first five years which rises to US\$750 million in years six to ten inclusive, less amounts previously paid as liquidated fees) or by agreement.

These payments will be allocated among the settling companies based on their relative annual market share in each year, which in 1999 was approximately 13.9 per cent for Brown & Williamson 1998, 15.4 per cent.

- (e) Goodwill has mainly arisen on the initial acquisition of Rothmans and subsequent local restructurings of the enlarged Group's publicly listed subsidiaries in Singapore, Australia and South Africa (see page 39 note 21). The goodwill arising on these of £5,574 million is being amortised over a period of twenty years. The amortisation charge is shown as additional information on the face of the profit and loss account and for 1999 includes £153 million in respect of the initial acquisition of Rothmans and £9 million on the subsequent restructurings.

	1999 £m	1998 £m
(f) Other operating charges include:		
Research and development expenses	58	45
Rent of machinery and equipment (operating leases)	39	25
Rent of land and buildings (operating leases)	65	58
Finance charges in respect of finance leases	5	4
Auditors' fees	6	4
Fees paid to PricewaterhouseCoopers for advisory and consultancy services		
– UK	3.0	3.0
– Overseas	3.7	2.6
(g) Operating charges include integration costs which are the costs incurred in integrating the Rothmans businesses into the British American Tobacco Group and the consequential restructuring of the enlarged Group. These costs are shown as additional information on the face of the profit and loss account and comprise:		
Staff costs	180	
Depreciation	74	
Other	103	
	357	

2 Sales of brands and demerger and restructuring costs

(a) Profit on sale of brands

This comprises the £88 million profit on the sale of certain British American Tobacco brands in Australasia. This profit has no effect on the taxation charge but increases the minority interests by £36 million. The cash inflow associated with this transaction is included within Acquisitions less disposals (see page 47 note 28).

(b) Demerger and restructuring costs

The charge of £46 million in 1998 comprised advisory and legal fees for restructuring the B.A.T Industries group in 1998, involving the demerger of its principal financial services businesses and the formation of British American Tobacco p.l.c. as the parent company for the retained businesses. These costs reduced the taxation charge by £6 million and there was no impact on minority interests.

Notes on the Accounts

Profit and Loss Account

3 Investment income

	1999 £m	1998 £m
Long term loans	4	29
Current investments	55	20
Short term deposits	86	94
Gain on cancellation of swap contracts	18	4
Dividends from business awaiting disposal	7	
Interest on Brazil sales tax recovery	25	
	195	147
Comprising:		
Third parties	195	121
Loans to demerged businesses		26
	195	147

4 Interest payable

	1999 £m	1998 £m
Bank loans and overdrafts	119	116
Other loans	246	235
	365	351
Comprising:		
Third parties	365	334
Loans from demerged businesses		17
	365	351

5 Taxation on ordinary activities

	1999 £m	1998 £m
UK Corporation Tax at 30.25% 1998 31.00%	62	307
Double taxation relief	(77)	(164)
ACT written back <i>page 27 note 7</i>		(5)
UK taxation	(15)	138
Overseas taxation	434	132
Current taxation	419	270
Deferred taxation	114	(110)
	533	160
Share of associates and joint venture	140	117
	673	277



6 Dividends and other appropriations

	1999 pence per share	1999 £m	1998 pence per share	1998 £m
(a) On ordinary shares:				
Interim				
– special 1999 paid 1 July 1999	4.00	62		
– ordinary 1999 paid 27 September 1999	4.30	94		
– FID 1998 paid 5 January 1999			8.00	125
Final				
– 1999 payable 3 May 2000	17.90	390		
– 1998 paid 1 July 1999			16.00	252
	26.20	546	24.00	377
(b) On convertible redeemable preference shares:				
Interim 1999 paid 27 September 1999	4.30	10		
Final 1999 payable 3 May 2000	17.90	44		
Amortisation of discount <i>page 74 note 44</i>		20		
	22.20	74		

The 1998 interim dividend paid on 5 January 1999 was paid as a Foreign Income Dividend. This reduced the ACT by £31 million which is taken up in the comparatives within these accounts.

7 Earnings per share

Basic earnings per share are based on equity earnings of **£482 million** 1998 £346 million (net basis) and **£482 million** 1998 £341 million (nil basis) and **1,910 million** 1998 1,561 million ordinary shares of 25p each, being the average number of shares in issue during the year. To comply with FRS14 the average number of shares in issue excludes shares held by British American Tobacco and B.A.T Industries Employee Share Ownership Trusts.

For diluted earnings per share the average number of shares in issue is increased to **2,058 million** 1998 1,574 million to reflect the potential dilution effect of the convertible redeemable preference shares and the exercise of employee share options. The earnings are correspondingly adjusted to the amount of earnings prior to charging dividends and the amortisation of discount on the convertible redeemable preference shares.

For the periods prior to the demerger, the average number of shares in issue is based on 50 per cent of the average number of B.A.T Industries ordinary 25p shares in issue, reflecting the issue of one ordinary share in British American Tobacco p.l.c. for every two ordinary shares of B.A.T Industries.

The earnings have been affected by a number of exceptional items. To illustrate the impact of the principal distortions, as well as the effect of goodwill amortisation and ACT shown on page 26 note 5, an alternative net earnings per share is shown below:

	Diluted		Basic	
	1999 pence per share	1998 pence per share	1999 pence per share	1998 pence per share
Unadjusted earnings per share	27.02	21.98	25.25	22.17
Adjustment from net to nil basis		(0.32)		(0.32)
Effect of goodwill amortisation	7.82		8.43	
Effect of US tobacco settlements	0.73	23.89	0.79	24.08
Effect of integration costs	11.27		12.15	
Effect of sales tax recovery	(0.63)	(2.35)	(0.68)	(2.37)
Effect of sale of brands	(2.53)		(2.72)	
Effect of demerger and restructuring costs		2.92		2.95
Effect of US tobacco settlements on effective tax rate	8.65		9.32	
Adjusted earnings per share	52.33	46.12	52.54	46.51

Notes on the Accounts

Balance Sheet

8 Intangible assets

	£m
Cost	
1 January 1999	
Additions:	
The Rothmans group page 39 note 21	5,574
Other	7
Differences on exchange	(83)
31 December 1999	5,498
Amortisation	
1 January 1999	
Charge for year	160
31 December 1999	160
Net book value 31 December 1999	5,338
Net book value 31 December 1998	

9 Tangible fixed assets

	Freehold land and buildings £m	Leasehold land and buildings £m	Plant machinery and equipment £m	Assets in course of construction £m	Total £m
Cost					
1 January 1999	690	122	2,904	186	3,902
Differences on exchange	(22)	(11)	(11)	(2)	(46)
Expenditure	13	9	215	141	378
Acquisitions	235	52	751	26	1,064
Reallocations	22		146	(168)	
Disposals	(35)	(11)	(284)	(15)	(345)
31 December 1999	903	161	3,721	168	4,953
Depreciation					
1 January 1999	247	32	1,575		1,854
Differences on exchange	(9)	(3)	1		(11)
Acquisitions	60	11	479		550
Charge for year	35	6	307		348
Adjustments on disposals	(23)	(10)	(211)		(244)
31 December 1999	310	36	2,151		2,497
Net book values 31 December 1999	593	125	1,570	168	2,456
Net book values 31 December 1998	443	90	1,329	186	2,048

	1999 £m	1998 £m
Cost of land on which no depreciation is provided	96	79
Leasehold land and buildings comprise:		
Net book value of long leasehold	77	50
Net book value of short leasehold	48	40
	125	90
Net book value of assets held under finance leases	72	55
Contracts placed for future expenditure	47	82



10 Investments in associates and joint venture pages 52 to 54

	£m	
1 January 1999 (including loans of £4 million)	472	
Differences on exchange	30	
Acquisitions	13	
Retentions	116	
Other movements	5	
31 December 1999 (including loans of £32 million)	636	
	1999	1998
	£m	£m
Listed overseas (market value £3,906 million 1998 £3,184 million)	594	438
Unlisted	42	34
	636	472

As at 31 December 1999, the Group's share of the gross assets and liabilities of the joint venture are not material to the Group and are disclosed here rather than on the face of the balance sheet. They totalled **£11 million** 1998 **£13 million** and **£43 million** 1998 **£22 million** respectively. In addition, during 1999 the Group subscribed for **£28 million** convertible loan stock.

11 Other investments and long term loans

	Listed equity £m	Unlisted equity £m	Unlisted loans £m	Long term loans £m	Total £m
1 January 1999	49	29	38	3	119
Differences on exchange		(2)	1		(1)
Acquisitions	59	9	1	1	70
Additions and advances	29			1	30
Disposals and repayments	(3)	(4)		(1)	(8)
31 December 1999	134	32	40	4	210
				1999	1998
				£m	£m
Market value of listed investments				108	56

The listed equity investments include **£76 million** 1998 **£49 million** of shares in the Company owned by the British American Tobacco and B.A.T Industries Employee Share Ownership Trusts. Details are shown in the Remuneration Report on pages 6 to 11.

Notes on the Accounts

Balance Sheet

12 Stocks

	1999 £m	1998 £m
Raw materials and consumables	1,898	1,550
Finished goods and work in progress	694	495
Goods purchased for resale	258	120
	2,850	2,165
Current replacement cost of stocks	2,896	2,171

13 Debtors

	Total		Receivable within one year		Receivable beyond one year	
	1999 £m	1998 £m	1999 £m	1998 £m	1999 £m	1998 £m
Trade debtors	945	532	945	532		
Other debtors	302	267	267	241	35	26
Prepayments and accrued income	753	694	366	501	387	193
	2,000	1,493	1,578	1,274	422	219

Prepayments and accrued income include **£33 million** 1998 **£40 million** deferred consideration in respect of an exchange of brands in 1993. The amounts are receivable up to the year 2003 and are related to Benson & Hedges sales in certain European markets.

Prepayments and accrued income also include a deferred tax asset of **£100 million** 1998 **£225 million**, and pension prepayments of **£230 million** mainly resulting from the fair valuing of certain Rothmans pension schemes (see page 39 note 21).

14 Current Investments

	1999 £m	1998 £m
Listed – UK	19	9
Listed – overseas	105	100
Unlisted – equity	40	45
Unlisted – other	604	31
	768	185
Market value of listed investments	276	255



15 Shareholders' funds

	Share capital £m	Share premium account £m	Merger reserves £m	Other reserves £m	Profit and loss account £m	Total £m
1 January 1999	393	1		483	(813)	64
Differences on exchange					(268)	(268)
Increase in share capital:						
Share options		3				3
Other <i>page 39 note 21</i>	212		4,877			5,089
Transfers from profit and loss account					556	556
Dividends and similar appropriations:						
Ordinary shares					(546)	(546)
Convertible redeemable preference shares <i>below</i>					(54)	(54)
Amortisation of discount on preference shares <i>below</i>					(20)	(20)
Other movements			(151)	20	128	(3)
31 December 1999	605	4	4,726	503	(1,017)	4,821

	1999 £m	1998 £m
Shareholders' funds comprise:		
Equity	3,347	64
Non-equity <i>below</i>	1,474	
	4,821	64
Non-equity interests comprise:		
Convertible redeemable preference shares	61	
Amortisation of the discount arising on the issue of these shares	20	
Applicable merger reserve	1,393	
	1,474	

For further information in respect of the convertible redeemable preference shares see page 74 note 44.

Included in differences on exchange are exchange gains of **£73 million** 1998 £11 million loss arising on borrowings denominated in, or swapped into, foreign currencies designated as hedges of net investments overseas.

Cumulative goodwill written-off as at 31 December 1999 (in respect of acquisitions up to 1 January 1998) amounted to **£1,854 million** 1998 £1,793 million, this movement arises from exchange differences only.

Notes on the Accounts

Balance Sheet

16 Provisions for liabilities and charges

	Unfunded pensions £m	Other post retirement benefits £m	Deferred taxation £m	Reorganisation of acquired business £m	Other provisions £m	Total £m
1 January 1999	351	188	47	15	140	741
Differences on exchange	(30)	6	(3)		(4)	(31)
Acquisitions	270	1	122		95	488
Provided in respect of the year	26	14	(2)	87	50	175
Utilised during the year	(36)	(24)		(1)	(58)	(119)
Other movements			6	1	(10)	(3)
31 December 1999	581	185	170	102	213	1,251

The provisions in respect of unfunded pensions largely relate to the pension arrangements in Germany and these, together with the provisions in respect of other post retirement benefits are discussed further in note 24 on page 43.

The deferred taxation balances are further analysed in note 20 on page 38.

Provisions in respect of the reorganisation of acquired businesses mostly relate to those set up to cover the integration of the Rothmans businesses.

Other provisions comprise other balances set up in the ordinary course of general business that cannot be classified within the other categories. This includes provisions for staff costs and the reorganisation of existing businesses.



17 Borrowings

	Currency	1999 £m	1998 £m
6¼% Notes due 2003	US dollar	17	16
Medium term notes 2000/2029	US dollar	408	392
7¼% Notes due 1999	US dollar		13
US commercial paper	US dollar		713
Euro commercial paper	Various		126
Acceptance credits	UK sterling		35
5¾% Eurobonds 2006	Deutschmark	236	268
Eurobonds 2004/2009	Euro	591	
Eurobonds 2002/2009	US dollar	1,671	82
Eurobonds 2004/2009	UK sterling	584	
Euro medium term notes 2000/2019	Various	115	102
Syndicated bank loan	US dollar	611	1,354
6¼% Notes due 2008	US dollar	188	
6¼% Notes due 2003	US dollar	188	
5½% Notes due 2005	Swiss franc	163	
7¼% and 7% Notes due 2004/2009	Malaysian ringgit	122	
Other bank loans	Various	533	370
Finance leases	Various	74	55
Miscellaneous	Various	65	91
Term borrowings		5,566	3,617
Overdrafts	Various	110	113
Total		5,676	3,730
Amounts secured on Group assets including finance leases		120	101

Included in the finance leases above are obligations of **£26 million** 1998 £20 million payable within one year, **£19 million** 1998 £16 million payable between one and two years and **£29 million** 1998 £19 million payable between two and five years.

Medium term notes have been issued in a number of currencies. Certain of these borrowings have been swapped into sterling and US dollars and have been accounted for accordingly.

	1999 £m	1998 £m (a)	1998 £m (b)
The borrowings are repayable as follows:			
Due beyond 5 years (non-instalment)	1,931	376	376
Due between 2 and 5 years	2,506	1,219	2,178
Due between 1 and 2 years	206	540	540
Due beyond 1 year	4,643	2,135	3,094
Due within 1 year	1,033	1,595	636
	5,676	3,730	3,730

As explained on pages 23 and 24 of the Annual Review and Summary Financial Statement, the maturity profile of the Group's borrowings has lengthened as a result of several medium and long dated issues in the Eurobond market in 1999. For the 1998 maturity profiles above, column (a) includes borrowings on the basis of their maturity dates and column (b) includes certain short term debt that was backed by a banking facility on the basis of that facility's maturity dates. For 1999 no such short term debt was outstanding.

Notes on the Accounts

Balance Sheet

17 Borrowings continued

	1999 £m	1998 £m
Borrowings facilities		
Undrawn committed facilities expiring:		
within one year	385	532
beyond one year and within two years	1,879	709
beyond two years and within five years	1	2,803
beyond five years	50	13
	2,315	4,057

As explained on pages 23 and 24 of the Annual Review and Summary Financial Statement, the facilities include undrawn amounts in respect of the syndicated bank loan facility of US\$3 billion (£1.86 billion), reduced from US\$8 billion in the previous year.

18 Financial Instruments

The objectives and policies for holding or issuing financial instruments and similar contracts, the strategies for achieving the objectives, and the role that financial instruments have had during the year in creating or changing the risks faced by the British American Tobacco Group in its activities are set out on pages 23 and 24 of the Annual Review and Summary Financial Statement.

Financial liabilities

The currency and interest rate exposure of financial liabilities, excluding finance leases, as at 31 December 1999 was as follows:

Currency	Total £m	Non-interest bearing £m	Floating rate £m	Fixed rate £m	Fixed rate	
					Weighted average interest rate %	Weighted average time for which rate is fixed years
US dollar	3,529	89	1,653	1,787	6.5	6.3
UK sterling	2,090	1,474	316	300	7.7	0.4
Euro	1,037		258	779	4.4	5.5
Others	509		305	204	6.5	5.3
	7,165	1,563	2,532	3,070	6.1	5.5
1998	3,729	54	2,398	1,277		

The above analysis takes account of interest rate, cross currency swap and forward foreign currency contracts.

Floating rate financial liabilities principally bear interest at rates based on relevant national LIBOR equivalents.

The average interest rate for total borrowings is estimated to be **6.8 per cent 1998 7.4 per cent**.

Non-interest bearing financial liabilities comprise the convertible redeemable preference shares (details of which are set out on page 74 note 44) and certain creditors due after more than one year. The weighted average period until maturity for these creditors is 3.0 years.



18 Financial instruments continued

Financial assets

The currency and interest rate exposure of financial assets, at 31 December 1999 was as follows:

Currency	Total £m	Non-interest bearing £m	Floating rates £m	Fixed rates £m	Fixed rate	
					Weighted average interest rate %	Weighted average time for which rate is fixed years
US dollar	989	105	849	35	6.1	4.5
UK sterling	191	42	118	31	6.9	6.3
Euro	949	209	740			
Others	835	342	492	1	7.6	3.2
	2,964	698	2,199	67	6.5	5.3
1998	1,285	374	800	111		

Non-interest bearing financial assets comprise certain cash balances, equity investments, debtors falling due after more than one year and the business awaiting disposal. The latter was realised in February 2000. Of the remainder, £501 million have no fixed date of repayment, and for £74 million the average period to maturity is 11.9 years.

Floating rate financial assets principally earn interest based on relevant national LIBID equivalents or government bond rates.

Monetary assets

The currency exposure of net monetary assets, at 31 December 1999 was as follows:

Functional currency of the Group's operations:	Net foreign currency monetary assets/ (liabilities)			
	US dollar £m	UK sterling £m	Euro £m	Others £m
US dollar		(21)	(3)	3
UK sterling	36		(79)	(10)
Euro		(7)		1
Others	15	(24)		(28)
	51	(52)	(82)	(34)

Notes on the Accounts

Balance Sheet

18 Financial Instruments continued

Fair values	Book value		Fair value	
	1999 £m	1998 £m	1999 £m	1998 £m
Primary financial instruments held or issued to finance the Group's operations:				
Borrowings	(5,479)	(3,682)	(5,211)	(3,690)
Other financial liabilities	(1,563)	(54)	(1,553)	(54)
Other investments and long term loans	134	70	151	70
Current investments	768	185	879	218
Other financial assets	209	60	209	60
Short term deposits and cash	1,853	970	1,853	970
Derivative financial instruments held to manage the interest rate and currency profile:				
Interest rate swaps	(8)		(35)	(64)
Cross currency swaps	(84)	7	(106)	8
Forward foreign currency contracts	(39)		(39)	
Others	2	2	(3)	4
Derivative financial instruments held or issued to hedge the currency exposure on expected future sales:				
Forward foreign currency contracts			(114)	(43)

Other financial assets comprise loans to associates and the joint venture, the business awaiting disposal and certain long term debtors.

Other financial liabilities comprise the convertible redeemable preference shares and certain long term creditors.

Under the Group's accounting policy, foreign currency assets and liabilities that are hedged using forward foreign currency contracts or currency swaps are translated at the forward rate inherent in the contracts. Consequently, the book value of the relevant asset or liability effectively includes the fair value of the hedging instrument. For the purpose of the above table, the book value of the relevant asset or liability is shown gross of the effect of the hedging instrument.

Summary of methods and assumptions

Interest rate swaps, caps, collars, currency swaps and forward foreign currency contracts

Fair value is based on market price of comparable instruments at the balance sheet date.

Fixed rate borrowings and loans and deposits

The fair value has been estimated using either market prices of comparable instruments at the balance sheet date or discounted cash flow analysis.

Other investments and current investments

The fair value is based on quoted market prices, market prices of comparable instruments at the balance sheet date or discounted cash flow analysis.

Business awaiting disposal

The expected proceeds.

Convertible redeemable preference shares

The fair value has been estimated by discounted cash flow analysis, assuming total redemption in June 2004.



18 Financial Instruments continued

Hedges

As explained on pages 23 and 24 of the Annual Review and Summary Financial Statement, the Group's policy is to hedge the following exposures:

Interest rate risk	Using interest and cross currency swaps and interest rate agreements such as caps and collars.
Currency risk	Using cross currency swaps and forward foreign currency contracts to manage the currency risk on borrowings in order to hedge net investments overseas. Forward foreign currency contracts are also used for currency exposures on unsettled trading transactions and future sales.

The table below shows the extent to which the Group has off-balance sheet (unrecognised) and on-balance sheet (deferred) gains and losses in respect of financial instruments used as hedges at the beginning and end of the year. It also shows the amount of such gains and losses which have been included in the profit and loss account for the year and those gains and losses which are expected to be reflected in next year's or later profit and loss accounts.

Unrecognised gains and losses	Gains £m	Losses £m	Total net gains/(losses) £m
Balances 1 January 1999	18	(122)	(104)
Differences on exchange		(3)	(3)
Brought forward balance recognised in current year	(4)	73	69
Brought forward balance not recognised in current year	14	(52)	(38)
Current year items not recognised in current year	24	(154)	(130)
Balances 31 December 1999	38	(206)	(168)
Expected to be dealt with next year based on 31 December 1999 exchange and interest rates	7	(55)	(48)

The above balances reflect the value at 31 December of the derivatives which are being used to manage the financial risks arising from the underlying operations. Such valuations of derivatives will tend to be volatile and, by way of example, the swap contracts cancelled during the year which resulted in a gain of £18 million were showing unrecognised losses of £29 million at 1 January 1999.

Deferred gains and losses

Balances 1 January 1999	7		7
Brought forward balance recognised in current year	(1)		(1)
Brought forward balance not recognised in current year	6		6
Current year items not recognised in current year	1	(12)	(11)
Balances 31 December 1999	7	(12)	(5)
To be recognised in the profit and loss account for next year	1	(1)	

Other financial assets and financial liabilities

Certain short term assets and liabilities, as well as finance lease liabilities are excluded from interest rate and fair value analysis. The fair value of such items is considered to approximate to their book values. There are no interest rates applicable to such items, with the exception of finance leases which are not considered to be material in the context of the Group's borrowings.

Notes on the Accounts

Balance Sheet

19 Creditors

	Total		Payable within one year		Payable beyond one year	
	1999 £m	1998 £m	1999 £m	1998 £m	1999 £m	1998 £m
Trade creditors	456	368	456	368		
Duty, excise and other taxes	1,030	573	1,026	567	4	6
Accrued charges and deferred income	910	582	790	479	120	103
Dividends payable	434	377	434	377		
Taxation on profits – UK	12	67	12	67		
– overseas	236	131	229	131	7	
Other taxation and social security	47	59	47	59		
Sundry creditors	906	437	873	387	33	50
	4,031	2,594	3,867	2,435	164	159

Sundry creditors include **£483 million** 1998 **£250 million** for tobacco settlements (page 24 note 1).

20 Deferred taxation

	Provided		Unprovided	
	1999 £m	1998 £m	1999 £m	1998 £m
Stock relief in respect of overseas stocks	22	16	184	170
Excess of capital allowances over depreciation	44	19	150	138
Losses available for set off against future taxable profit	(34)	(48)	(10)	(12)
Capital gains	61	60	4	11
Other timing differences	(23)	(225)	(220)	(4)
	70	(178)	108	303

The deferred tax provision above is net of a deferred tax asset shown on page 30 note 13. Other timing differences include short term timing differences as well as an asset of **£36 million** 1998 asset of **£91 million** in respect of pensions and other post retirement benefits.



BRITISH AMERICAN
TOBACCO

Notes on the Accounts

Other financial information

21 The Rothmans group

(a) The acquisition

On 7 June 1999 British American Tobacco p.l.c. issued 604,336,627 ordinary shares and 241,734,651 convertible redeemable preference shares for the acquisition of the Rothmans International B.V. group. This combination has been reflected in these accounts using the acquisition method of accounting. It was announced before the completion of the initial acquisition, that the Canadian interests of Rothmans would be disposed of in due course. In accordance with this decision, the results and assets of that business are not consolidated in these accounts. The dividend payments are included in the Group's investment income and the investment is shown as a current asset.

The provisional goodwill arising on this acquisition and the subsequent local restructurings of the enlarged Group's publicly listed subsidiary undertakings in Singapore, Australia and South Africa comprises:

	1999 £m
Goodwill arising on the initial acquisition	5,171
Goodwill arising on subsequent local restructurings	403
	5,574

The goodwill arises as follows:

	Book value £m	Reclassification £m	Revaluations £m	Accounting policy alignment £m	Provisional fair value £m
Tangible fixed assets	494	(13)	47		528
Investments in associates	78	(65)			13
Other investments and long term loans	50		15		65
Stocks	874	(83)	(6)		785
Debtors	710	(22)	168	(16)	840
Current investments	59	112	1		172
Short term deposits and cash	321	27			348
Business awaiting disposal		44	79		123
Provisions for liabilities and charges	(417)	1	(124)	(3)	(543)
Borrowings	(1,102)	26	(20)		(1,096)
Creditors	(1,029)	3	(22)		(1,048)
Minority interests	(223)	(27)	2	8	(240)
Net (liabilities) acquired	(185)	3	140	(11)	(53)
Subsequent local restructurings <i>below</i>					40
Goodwill					5,574
Consideration					5,561
Consideration satisfied by:					
Shares issued (net of issue costs of £0.3 million)					5,089
Cash (£471 million net of £37 million received – <i>below</i>)					434
Acquisition costs					38
					5,561

The main provisional element of the fair value attributable to the Rothmans businesses relates to the provisions which were held by the former Rothmans businesses in Australia against potential franchise fee claims brought by retailers. If the retailers are unsuccessful in their appeals against prior legal decisions in favour of the company, the write-back of the Rothmans provisions included above will be credited against goodwill.

The book value of the net liabilities acquired has been revalued to fair value as at the acquisition date, the major effects being the recognition of pension scheme surpluses, additional provisions in respect of deferred taxation after considering the enlarged Group as a whole, and deferred taxation arising on the fair value adjustments made. The accounting policy alignment reflects the restatement of deferred taxation balances to comply with the Group's accounting policy. The reclassification is of certain investments held by the Rothmans group which are now either subsidiary or associated undertakings in the enlarged Group, as well as the deconsolidation of the Canadian business.

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21 The Rothmans group continued

The subsequent local restructurings largely relate to various publicly-listed companies within the enlarged Group resulting in the goodwill of £403 million noted above. The main components being:

- (a) In Australia the purchase of the interests of the minority shareholders (32.7 per cent) in W.D. & H.O. Wills Holdings Limited, and the merger with Rothmans Holdings Limited.
- (b) In Singapore the purchase of the interests of the minority shareholders in British-American Tobacco Co. (Singapore) Limited (20 per cent), and Rothmans Industries Limited (50 per cent).
- (c) In South Africa the purchase of the interests of the minority shareholders (36.38 per cent) in British American Tobacco Holdings (South Africa) Limited.

The cash element of the consideration above relates to restructuring and largely comprises cash paid to acquire minority shareholdings net of cash received following the divestment of certain of the Rothmans' Australasian brands.

(b) Results

The integration of the acquired businesses is well advanced, with many being managed on a unified basis from an early stage. For this reason it is only possible to estimate the post-acquisition results of the Rothmans businesses. The turnover excluding duty, excise and other taxes attributable to the Rothmans businesses during the period since acquisition on 7 June 1999 to 31 December 1999 is estimated at £1,626 million and the corresponding operating profit is estimated at £427 million. However, given the integration, it is not practical to estimate the cash flow impact of the acquired businesses since acquisition.

The estimated regional analysis of the contribution of the Rothmans businesses to turnover excluding duty, excise and other taxes is: America-Pacific £78 million, Asia-Pacific £426 million, Latin America £29 million, Europe £740 million and Amesca £353 million.

The estimated regional analysis of the contribution to operating profit is: America-Pacific £14 million, Asia-Pacific £115 million, Latin America £18 million, Europe £145 million and Amesca £135 million.

In the periods prior to the acquisition, the consolidated results of Rothmans International B.V. prepared on the basis of their accounting policies were as follows:

	1 April 1999 to 6 June 1999 £m	1 April 1998 to 31 March 1999 £m
Turnover excluding duty, excise and other taxes	427	3,022
Operating profit	72	720
Profit before taxation	67	673
Taxation and minority interest	(45)	(331)
Profit attributable to shareholders	22	342
Exchange adjustments and other movements	20	(51)
Total recognised gains for the period	42	291

22 Group employees

The average number of persons employed by the Group during the year was **107,620** 1998 101,081.

	1999	1998
America-Pacific	7,440	7,433
Asia-Pacific	10,502	6,542
Latin America	16,442	18,005
Europe	16,884	10,690
Amesca	16,024	15,214
Subsidiary undertakings	67,292	57,884
Associates	40,328	43,197
	107,620	101,081

Details of Directors' remuneration and share options are given in the Remuneration Report on pages 6 to 11.



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23 Contingent liabilities and financial commitments

There are contingent liabilities in respect of litigation, overseas taxes and guarantees in various countries.

Group companies, notably Brown & Williamson Tobacco Corporation ("B&W") as well as other leading cigarette manufacturers, are defendants, principally in the United States, in a number of product liability cases, including a substantial number of new cases filed in 1999, although a number of cases were discontinued by claimants (without payment by any defendants) in the year. Significant compensatory and punitive damages are being sought by a number of plaintiffs.

US Litigation

The total number of US product liability cases pending at year end involving Group companies was 537 (31 December 1998 678 cases). Group companies were named as co-defendants in 161 of those cases (1998 238 cases). Only perhaps a couple of dozen cases or fewer will actually come to trial in 2000. Since many of these pending cases seek unspecified damages, it is not possible to determine the total amount of claims pending, but the aggregate amounts involved in such litigation are significant. The cases fall into four broad categories:

(1) Medical reimbursement cases. These civil actions seek to recover amounts spent by government entities and other third party providers on health care and welfare costs claimed to result from illnesses associated with smoking.

The United States Department of Justice has filed suit against the leading US cigarette manufacturers, certain affiliated companies (including parent companies), and others seeking reimbursement for Medicare and other health expenses incurred by the US federal government as well as various equitable remedies, including paying over of proceeds from alleged unlawful acts. The court has indicated that, if the case is not dismissed, it is not likely to be tried for several years. At 31 December 1999, similar reimbursement suits were pending against B&W amongst others by eight Indian tribes and by seven county or other political subdivisions of certain states. The settlement of the states' suits includes a credit for any amounts paid in suits brought by the states' political subdivisions; nevertheless, B&W intends to defend these cases vigorously.

At 31 December 1999, B&W was named as defendant in seven US cases brought by non-US government entities seeking reimbursement of medical costs which they incurred for treatment for persons in their own countries who are alleged to have smoked imported cigarettes including those manufactured by B&W. The five foreign government cases pending in US federal court have been consolidated before a single judge in the District of Columbia. On 30 December 1999, that judge dismissed the first of these cases (Guatemala) to be argued before him. One foreign government case (Marshall Islands) is set for trial in 2000.

Based on somewhat different theories of claim are some 48 non-governmental medical reimbursement cases and health insurers claims, the majority of which were filed by labour union health and welfare funds on behalf of their members. To date, five federal appellate courts have issued decisions dismissing this type of case entirely and some but not all state courts to date have issued similar decisions. Only one union health fund case (Ohio Iron Workers) has been tried, resulting in a verdict for defendants in March 1999. Seven third party reimbursement cases are currently scheduled for trial in 2000.

2) Class actions. As at 31 December 1999, B&W was named as a defendant in some 38 (31 December 1998 55) separate actions attempting to assert claims on behalf of classes of persons allegedly injured by smoking. While nine courts refused to do so, eight courts have certified classes of tobacco claimants in cases involving B&W but four of these classes have subsequently been decertified. Even if the classes remain certified and the possibility of class-based liability is eventually established, it is likely that individual trials will still be necessary to resolve any actual claims. If this happens, many of the defences that have contributed to more than 600 individual cases being successfully disposed of over the years by the US industry without, to date, monetary loss, will be available.

One class action in Florida (Engle) is currently being tried. In the first phase of the trifurcated trial, the jury returned a verdict that included general findings that smoking causes several specified diseases and other findings including that the defendants conduct rose to a level that would permit a potential award of punitive damages. The second phase of the trial includes two parts; the first is the trial of three named class representatives' claims. If the jury returns a verdict in favour of any of these individuals, the jury is expected to be instructed to determine a single sum by way of punitive damages to be eventually split between all successful claimants in the class. Both parts of phase two are expected to be completed by Spring of 2000. This will be the first opportunity where B&W will actually have the right to appeal in this case. The claims of all the remaining individuals in the class for compensatory and for entitlement to participate in any punitive damages award sum, are to be determined on a case-by-case basis in the third phase of the trial – a process that is expected to take many years.

Although jury verdicts are inherently unpredictable and although it is considered that manifest appealable errors already exist concerning the conduct of this trial, in light of all the events of this trial to date, adverse jury verdicts on both compensatory and punitive damages may be likely in phase two of this case. The amount of any such award is unpredictable. B&W believes that Florida law would not authorise the court to render a punitive damage award enforceable before the completion of phase three. Under Florida law and federal constitutional law, B&W should be permitted to appeal such an award if

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23 Contingent liabilities and financial commitments continued

made and avoid enforcement on such a judgement without posting a bond (or by posting a bond in an amount less than the entire award). If the trial court judge makes contrary rulings, these will be vigorously challenged.

(3) **Individual cases.** Approximately 421 cases were pending against B&W at 31 December 1999 (31 December 1998 497) filed by or on behalf of individuals in which it is contended that diseases or deaths have been caused by cigarette smoking or by exposure to environmental tobacco smoke (ETS). In 1999, in four individual smoker cases, juries found for the industry, in one case the jury found that the smoker's fault outweighed defendants' fault resulting in no award of damages and there was a verdict for the industry in an ETS case. In two cases not involving B&W, juries awarded judgement against Philip Morris, Inc., of \$51,500,000 (Henley, February 1999) and \$80,300,000 (Williams, March 1999). The trial courts later reduced these verdicts to \$26,500,000 and \$32,800,000 respectively. Philip Morris, Inc. is appealing these decisions.

(4) **Other claims.** Eight cases are pending on behalf of asbestos companies. Those companies seek reimbursement from the US industry for costs and judgements paid in litigation brought by third parties against them. These companies claim that but for the smoking of the successful third parties the damages awarded against them would have been lower. In addition, conduct-based claims, including antitrust and RICO claims, have been filed and also threatened in the US but none of these recent cases is considered to be meritorious or material.

B.A.T Industries has been named as a co-defendant in the US in most of the medical reimbursement cases, in a quarter or fewer of the class actions and even fewer of the individual cases. They are contesting the jurisdiction of the US courts since they are 'holding' companies not transacting business in the United States. In the 45 cases that have decided this issue to date, 27 courts have dismissed them prior to trial. In the balance of 18 cases, there has been no adverse ruling on the issue of jurisdiction affirmed through appeal: merely, the courts involved have said that the issue is, in their court system, not sufficiently beyond doubt to prevent the question even coming into a trial. Some 125 plaintiffs have voluntarily agreed to drop the Company (or B.A.T Industries) and substitute the Company's indirectly held subsidiary British American Tobacco (Investments) Limited (formerly called British-American Tobacco Company Ltd.), as a co-defendant.

Legal Matters Outside the United States

At year end, there were no active claims against Group companies (including those of the former Rothmans Group) in respect of health-related claims outside Argentina, Australia, Brazil, Canada, Chile, Eire, Finland, France, Germany, Israel, the Netherlands, Pakistan, the Philippines and Sri Lanka.

Conclusion

While it is impossible to be certain of the outcome of any particular case or of the amount of any possible adverse verdict, the Company believes that the defences of the Group companies to all these various claims are meritorious both on the law and the facts, and a vigorous defence is being made everywhere. If an adverse judgement were entered against any of the Group companies in any case, an appeal would be made. Such appeals could require the posting of appeal bonds or substitute security by the appellants for the amounts of such adverse judgements: at least in the aggregate and despite the quality of defences available to the Group, it is not impossible that the results of operations or cash flows of the Group in particular quarterly or annual periods could be materially affected by this and by the final outcome of any particular litigation.

Having regard to all these matters, the Directors (i) do not consider it appropriate to make any provision in respect of any pending litigation and (ii) do not believe that the ultimate outcome of all this litigation will significantly impair the financial condition of the Group.



23 Contingent liabilities and financial commitments continued

Guarantees

Performance guarantees given to third parties in respect of Group companies were **£76 million** 1998 **£49 million**.

	1999 £m	1998 £m
Operating leases		
Annual commitments under operating leases comprise leases which expire:		
Land and buildings		
Within 1 year	10	13
Between 2 and 5 years	20	23
Beyond 5 years	12	9
	42	45
Others		
Within 1 year	11	6
Between 2 and 5 years	24	19
Beyond 5 years	12	
	47	25

24 Post employment schemes

The Group's subsidiary undertakings operate over 100 active retirement benefit arrangements worldwide. The majority of employees belong to defined benefit schemes, most of which are funded externally. In some countries, however, separate provisions are made, covered by assets retained within the companies concerned. The remaining employees belong to defined contribution schemes providing benefits based upon contributions paid plus interest.

Pension commitments are financed according to accepted current practices in each country.

Defined benefit scheme costs are determined following valuations by qualified independent actuaries, who generally use either the attained age or projected unit credit method. All the schemes are formally valued at least every three years.

In total, taking the major retirement schemes summarised in detail below with all other schemes, the actuarial value of assets in externally funded defined benefit schemes was £3.1 billion at the respective dates of the last actuarial valuations. This exceeded the total value of projected accrued benefits at the same dates. Any deficit or surplus in these schemes are being eliminated by increased or reduced company contributions, enhancement of scheme benefits or a combination of both. Certain schemes show deficits on a current funding level basis but these are not material in the context of the whole Group.

The total market value of scheme assets, including the most significant schemes summarised below, at the dates of the most recent actuarial valuations was £3.3 billion which was not less than the value of the accrued obligations.

Of the approximately 90 defined benefit schemes those in the UK and US represent some 69 per cent of the total obligations. The main actuarial assumptions used for accounting purposes, asset values, funding level and pension costs for the period for the main schemes in the UK and US are summarised in the following tables:

Country	BAT Pension Scheme UK	Rothmans International Pension Scheme UK	Brown & Williamson Scheme US
Actuarial method	Projected unit credit	Projected unit credit	Projected unit credit
Main actuarial assumptions:			
Investment return	8.0%	8.0%	7.0%
Salary increases	5.5%	5.5%	5.5%
Pension increases	3.5%	3.5%	0.0%
Asset value on market (US)/ market related (UK) basis	£450 million	£600 million	US\$1,805 million
Funding level	101.6%	137.9%	122.0%
Amortisation method	Percentage of salary	Percentage of salary	Straight line
Period over which surplus amortised	13 years	10 years	13 years
Date of last valuation	31 March 1999	31 March 1999	31 October 1999

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Other financial information

24 Post employment schemes continued

The next most significant pension arrangements, representing a further 14 per cent of the total obligations, are the unfunded schemes in Germany covering employees of BAT Germany and Rothmans International Germany. A total provision of £418 million was held in the balance sheet at the end of the period (£265 million at the end of 1998 for BAT Germany) in respect of these schemes. The annual cost was £33 million for the period. The liabilities and annual costs for the schemes have been determined using a 6 per cent investment return with allowances for salary and pension increases, being in line with or more conservative than normal local practice.

For the remaining schemes, typical assumptions used for accounting purposes are that real investment returns will be 3 per cent to 5 per cent per annum, and that real salary increases will be 1 per cent to 3.5 per cent per annum. Pension increases are generally assumed to be in line with inflation.

Following completion of the acquisition of the Rothmans International Group its pension schemes have been brought into the balance sheet on a fair value basis, which has been reflected in the figures summarised above (see page 39 note 21).

Other post employment schemes

The Group also operates two major plans in the United States, as well as two plans in South Africa which provide employees with certain post-retirement benefits other than pensions. The liabilities in respect of these benefits are assessed by qualified independent actuaries, applying the projected unit credit method. The current year and prior year provisions are shown on page 32 note 16.

The assumptions which have the most significant effects on the valuations of the schemes are those relating to the discount rate for obligations, assumed to be 7 per cent in the United States and 14 per cent in South Africa, and healthcare cost inflation, which is assumed to range from 5.5 per cent to 8 per cent reducing by 0.5 per cent per annum to 5.5 per cent for all beneficiaries in the United States, and assumed to be 10 per cent in South Africa.

	1999 £m	1998 £m
Total post-employment (non-pension) benefit costs	13	17
Total pension costs	93	78
Total pension and post employment benefit costs	106	95
Regular annual cost of pension schemes	123	108

Of the 1999 total pension and post employment benefit cost £13 million relates to the Rothmans pension schemes. The total regular annual cost for 1999 includes £21 million for the Rothmans pension schemes.

25 Related party disclosures

The Group has a number of transactions and relationships with related parties, as defined in FRS8 on Related Party Disclosures, all of which are undertaken in the normal course of trading. Details of these are set out below.

Transactions and balances with associates relate mainly to sale and purchase of cigarettes and tobacco leaf.

	1999 £m	1998 £m
Transactions – Revenue	9	12
– Purchases and sponsorship fees	(73)	(88)
– Other net income	8	8
Amounts receivable at 31 December	4	6
Amounts payable at 31 December	(3)	(1)

In addition, the Group made a further investment of US\$45 million in the form of Convertible Loan Stock in British American Racing, in which the Group has a 50% interest.

The Directors of British American Tobacco p.l.c. had no material transactions with the Group. The term Director in this context includes members of their households.

Other than the transactions undertaken in connection with the acquisition of Rothmans, and subsequently in their capacity as shareholders, there have been no material transactions with Compagnie Financière Richemont AG and the Rembrandt Group Limited, who together indirectly own 35 per cent of the fully diluted ordinary share capital of British American Tobacco p.l.c. Between 1 January 1999 and the date of the acquisition, there were no material transactions between the British American Tobacco Group and the Rothmans International B.V. Group.



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26 Post balance sheet events

(a) Acquisition of Imasco

On 3 August 1999, the Company announced that it had entered an agreement with Imasco Limited ('Imasco') to acquire for cash all Imasco shares not already owned by the Group, representing approximately 58 per cent of the Imasco shares in issue through a wholly owned subsidiary British American Tobacco (Canada) Limited ('British American Tobacco Canada').

The agreement with Imasco of 2 August provided for a minimum cash consideration of C\$40 per Imasco share which could be increased depending on the outcomes of sales processes for Imasco's retailing business, Shoppers Drug Mart ('Shoppers') and its Genstar land development company ('Genstar'). On 18 November the Company announced that it had agreed with Imasco a final price of C\$41.60 per Imasco share and that it had accepted an offer from an investor group led by Kohlberg Kravis Roberts & Co ('KKR') to purchase Shoppers for C\$2.55 billion in cash conditional upon completion of the acquisition of Imasco.

Concurrently with the 2 August agreement with Imasco, the Company entered into an agreement with Toronto Dominion Bank ('TD Bank') whereby TD Bank agreed to make an offer ('the Offer') of C\$67 per share for all of the issued common shares of CT Financial Services Inc ('CT') owned by the Imasco Group and the Company agreed to cause British American Tobacco Canada to deposit all of the common shares in the capital of CT owned by the Imasco Group to the Offer.

The acquisition of Imasco was completed on 1 February 2000, at which time Imasco was amalgamated with British American Tobacco (Canada) Limited to form Imperial Tobacco Canada Limited. The offer by TD Bank for CT was completed immediately following the Group's acquisition of the Imasco shares and the proceeds to the Group of C\$7.85 billion were used in part to satisfy the consideration of C\$10.4 billion payable for the Imasco shares. The sale of Shoppers to KKR was completed on 4 February 2000.

The sale process for Genstar is continuing. The Company will retain the full net proceeds from a future sale of Genstar. Once Genstar is sold, the British American Tobacco Group's only business in Canada will be the tobacco business operated by Imperial Tobacco, the leading Canadian tobacco company with a share of approximately 69 per cent of the Canadian cigarette market.

(b) Notice of intention to redeem the convertible redeemable preference shares

See page 74 note 44.

(c) Acquisition of S.C.A. Tobacco Corporation

On 1 February 2000 the Group announced the signing of a Memorandum of Understanding with the Sumitomo Corporation. Under this the Group would acquire Sumitomo Corporation's Japanese tobacco importing and sales subsidiary S.C.A. Tobacco Corporation.

(d) Disposal of Rothmans Inc.

On 6 February 2000 the Group announced the agreement to dispose of its 71.2 per cent interest in Rothmans Inc., representing the Canadian interests of Rothmans. The proceeds amounted to C\$314.3 million and the sale was completed on 3 February 2000. The disposal proceeds have been included within the calculation of the goodwill arising on the acquisition of Rothmans given that the intention to dispose had been announced at the time of the acquisition (see page 39 note 21).

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Cash Flow Statement

27 Net operating cash flow from subsidiary undertakings

	1999 £m	1998 £m
Operating profit	1,099	676
Depreciation	350	297
Goodwill amortisation	162	
Decrease/(Increase) in stocks	31	(36)
Decrease/(Increase) in debtors	82	(131)
Increase in creditors	180	291
Increase in provisions	83	10
Other	8	(11)
Net operating cash flow from subsidiary undertakings	1,995	1,096

Operating profit includes charges for US settlement costs and integration costs, as well as a credit for sales tax recovery, referred to in note 1 on page 24. These are also reflected in the movements in debtors, creditors and provisions above. The cash outflow in respect of US settlement costs was **£543 million** (including **£373 million** ongoing costs) 1998 **£643 million** (including **£97 million** ongoing costs). The cash outflow in respect of integration costs was approximately **£105 million** in 1999. The cash inflow for the sales tax recovery in 1998 was **£35 million**.

28 Analysis of items netted in the cash flow statement

	1999 £m	1998 £m
Investment income	193	150
Interest paid	(256)	(319)
Non-equity dividends paid	(10)	
Interest element of finance lease rental payments	(4)	(4)
Demerger and restructuring costs		(31)
Dividends paid to minorities	(129)	(78)
Returns on investments and servicing of finance	(206)	(282)
Capital expenditure	(340)	(363)
Sale of fixed assets	87	35
Other investments – purchases	(30)	(30)
– sales	2	7
Capital expenditure and financial investment	(281)	(351)
Subsidiary and associated undertakings – purchases	(278)	(152)
– sales	2	136
Sale of brands	88	
Loan to joint venture	(28)	
Acquisitions less disposals note (a)	(216)	(16)
Short term deposits	(841)	467
Current investments	(499)	(8)
Management of liquid resources note (c)	(1,340)	459



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28 Analysis of items netted in the cash flow statement continued

	1999 £m	1998 £m
Unsecured loan stock		(397)
Commercial paper	(864)	424
Medium term notes	140	(709)
Bonds	2,780	(814)
Acceptance credits	(35)	(40)
Syndicated bank loans	(782)	660
Bank and other loans	(360)	52
Capital element of finance lease rental payments	(26)	(21)
Financing – increase/(decrease) in debt	853	(845)

In 1999 medium term notes comprise issues of £242 million and repayments of £102 million and Bank and other loans includes repayment of £400 million of debt acquired with Rothmans. In 1998 medium term notes and bonds include issues of £101 million and £343 million respectively (page 33 note 17).

(a) Acquisitions less disposals

The net cash outflow in respect of the purchase of subsidiary and associated undertakings principally reflects the effect of the local restructurings resulting from the acquisition of the Rothmans group, as described on page 39 note 21. The outflow of £509 million (including the £38 million acquisition costs) is reduced by £37 million disposal proceeds for certain Rothmans' Australasian brands. It is further reduced by the cash within the Rothmans group on acquisition of £200 million.

The cash outflow in 1998 mainly comprises £116 million in relation to the settlement of a prior year creditor in respect of the acquisition of Cigarrera La Moderna and £24 million in respect of the purchase of additional shares in the Group's subsidiary undertaking in Poland.

The cash inflow in 1998 mainly comprises £98 million in relation to the Group's participation in the share buy back scheme of Imasco in Canada and £37 million in respect of the sale of Companhia de Papel Pirahy, in Brazil, in 1997.

(b) Dividends and cash flow related to demerged businesses

The dividends received from demerged businesses of £123 million in the Group profit and loss account comprises dividends received of £242 million less amount reinvested in demerged businesses of £119 million.

Cash flow with demerged businesses of £668 million comprises cash inflows at the date of demerger of £820 million less movements on investment loan and current accounts of £152 million.

(c) Net cash flow from liquid resources

Liquid resources include current investments, together with short term deposits and cash other than cash and deposits repayable on demand.

(d) Cash flow attributable to Rothmans

See page 39 note 21.

29 Analysis of net debt

	1 Jan 1999 £m	Cash flow £m	Net debt acquired £m	Disposals £m	Other changes £m	Differences on exchange £m	31 Dec 1999 £m
Cash and bank balances	466						450
Overdrafts	(113)						(110)
	353	34				(47)	340
Term borrowings	(3,562)	(879)	(1,045)		(8)	2	(5,492)
Finance lease obligations	(55)	26			(43)	(2)	(74)
		(853)					
Short term deposits	504	841	133		3	(78)	1,403
Current investments	185	499	158	(23)	15	(66)	768
		1,340					
	(2,575)	521	(754)	(23)	(33)	(191)	(3,055)

Five Year Summary – excluding demerged businesses

For the years ended 31 December	1999 £m	1998 £m	1997 £m	1996 £m	1995 £m
Revenue					
Continuing operations	21,671	17,376	17,834	18,762	17,690
Discontinued operations				25	135
	21,671	17,376	17,834	18,787	17,825
Profit					
Operating profit (before goodwill amortisation and exceptionals)	2,022	1,550	1,591	1,714	1,646
Operating profit – continuing operations	1,479	1,011	1,303	1,714	1,646
Operating profit – discontinued operations				2	82
Operating profit	1,479	1,011	1,303	1,716	1,728
Profit on ordinary activities before interest	1,567	965	1,094	1,798	1,668
Profit before taxation	1,371	738	875	1,626	1,460
Profit after taxation	698	461	518	1,106	970
Profit for the year	556	346	412	988	860
	pence	pence	pence	pence	pence
Earnings per share – basic unadjusted	25.25	22.17	26.59	63.87	55.75
– diluted unadjusted	27.02	21.98	26.32	63.21	55.09
– diluted adjusted	52.33	46.12	49.07	58.36	53.67
At 31 December	1999 £m	1998 £m	1997 £m	1996 £m	1995 £m
Balance Sheet					
Fixed assets	8,640	2,639	2,645	2,366	2,596
Current assets	7,594	4,813	5,905	5,726	5,464
Total assets	16,234	7,452	8,550	8,092	8,060
Shareholders' funds (including non-equity interests)	4,821	64	(97)	701	503
Interest of minority shareholders	455	323	342	327	364
	5,276	387	245	1,028	867
Borrowings	5,676	3,730	4,566	3,393	3,523
Provisions and other creditors	5,282	3,335	3,739	3,671	3,670
	10,958	7,065	8,305	7,064	7,193
Total funds employed	16,234	7,452	8,550	8,092	8,060

The information included in the five year summary has been restated, where applicable, to reflect changes in accounting policy.



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Quarterly Analyses of Profit – excluding demerged businesses

The figures shown below have been produced using average rates of exchange for the years ended 31 December 1999 and 1998 respectively, with the previously reported figures for 1999 restated using average rates for the full year.

	3 months to			
	31.3.99 £m	30.6.99 £m	30.9.99 £m	31.12.99 £m
Subsidiary undertakings	244	322	400	133
after charging: US tobacco settlements	(13)	(9)	5	(7)
integration costs			(81)	(276)
goodwill amortisation			(91)	(71)
Share of associates	96	73	113	98
Operating profit	340	395	513	231
Sale of brands			88	
Profit on ordinary activities before interest	340	395	601	231
Net interest – subsidiary undertakings	(27)	(37)	(45)	(61)
Share of associates' net interest	(5)	(7)	(4)	(10)
Profit before taxation	308	351	552	160

	3 months to			
	31.3.98 £m	30.6.98 £m	30.9.98 £m	31.12.98 £m
Subsidiary undertakings	303	261	375	(263)
after charging: US tobacco settlements		(150)		(463)
after crediting: sales tax recovery		74		
Share of associates	75	84	85	91
Operating profit	378	345	460	(172)
Demerger and debt restructuring costs	(7)	(19)	(17)	(3)
Profit on ordinary activities before interest	371	326	443	(175)
Net interest – subsidiary undertakings	(56)	(49)	(54)	(45)
Share of associates' net interest	(4)	(6)	(5)	(8)
Profit before taxation	311	271	384	(228)

Principal Subsidiary Undertakings

	% equity shares held		% equity shares held
Europe		Russia	
Great Britain		British American Tobacco – STF	99
B.A.T Industries p.l.c.	100	OJSC British American Tobacco – Yava	88†
British-American Tobacco (Holdings) Ltd.	100	Spain	
British American Tobacco (1998) Ltd.	100*	B.A.T Espana S.A.	100
British American Tobacco (Investments) Ltd.	100	Switzerland	
B.A.T (U.K. and Export) Ltd.	100	BAT (Suisse) SA	100
B.A.T. International Finance p.l.c.	100	F J Burrus SA	100
BATMark Ltd.	100	Rothmans of Pall Mall Ltd.	100
British American Tobacco (Brands) Ltd.	100	Ukraine	
Rothmans International Tobacco (UK) Ltd.	100	A/T B.A.T – Prilucky Tobacco Co.	65
Rothmans Finance p.l.c.	100	America-Pacific	
BAT (CI) Finance Ltd.	100	United States of America	
Weston Investment Co. Ltd.	100	BATUS Holdings Inc.	100
Tobacco Insurance Co. Ltd.	100	British American Tobacco (Brands) Inc.	100
Belgium		B.A.T Capital Corporation	100
British American Tobacco Belgium SA	100	Brown & Williamson Tobacco Corporation	100
Tabacofina-Vander Elst NV	100	Asia-Pacific	
Bulgaria		Australia	
British American Tobacco Bulgaria Eood	100	British American Tobacco Australasia Ltd.	59
Cyprus		Cambodia	
B.A.T (Cyprus) Ltd.	100	British American Tobacco Cambodia Ltd.	51
Finland		China	
British American Tobacco Nordic Oy	100	B.A.T China Ltd.	
Germany		(incorporated in the United Kingdom)	100
BATIG Gesellschaft fur Beteiligungen m.b.H.	100	British-American Tobacco Co. (Hong Kong) Ltd.	100
British-American Tobacco (Germany) G.m.b.H.	100	Indonesia	
British American Tobacco Industrie GmbH	100	PT BAT Indonesia Tbk.	70
Rothmans Germany GmbH	100	PT Rothmans of Pall Mall Indonesia	100
Hungary		Malaysia	
BAT Pecci Dohanygyar Kft	100	British American Tobacco (Malaysia) Berhad	50
British American Tobacco Magyarorszag		New Zealand	
Dohany Kereskedelmi Kft	100	British American Tobacco (New Zealand) Ltd.	100 (59)
Netherlands		Papua New Guinea	
B.A.T Finance BV	100	British American Tobacco (PNG) Ltd.	100 (59)
British American Tobacco International (Holdings) BV	100	Singapore	
British American Tobacco The Netherlands BV	100	British-American Tobacco Co. (Singapore) Ltd.	100
British American Tobacco Holdings		Rothmans Industries Ltd.	100
(The Netherlands) BV	100	Vietnam	
British American Tobacco Manufacturing BV	100	B.A.T Vietnam Ltd.	
British American Tobacco Exports BV	100	(incorporated in the United Kingdom)	100
Rothmans Central & Eastern Europe BV	100	Latin America	
Rothmans Far East BV	100	Argentina	
Theodorus Niemeyer BV	100	Nobleza-Piccardo SAICyF	70
Poland			
British-American Tobacco Polska SA	96		
Republic of Ireland			
P J Carroll & Co. Ltd.	100		
Hamburg Investment & Trading Co.	100		
Romania			
British-American Tobacco (Romania) Trading SRL	100		



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	% equity shares held		% equity shares held
Barbados		Cameroon	
British-American Tobacco Co. (Barbados) Ltd.	100	British American Tobacco Cameroun SA	99
Brazil		Congo	
Souza Cruz SA	75	British American Tobacco Congo SARL	100
Souza Cruz Trading SA	100 (75)	Ghana	
Chile		British American Tobacco Ghana Ltd.	55
Compania Chilena de Tabacos SA	70	Kenya	
Costa Rica		British American Tobacco Kenya Ltd.	60
Republic Tobacco Co.	80	La Reunion	
El Salvador		B.A.T La Reunion SARL	100
Cigarrera Morazan SA de CV	75	Malawi	
Guatemala		B.A.T (Malawi) Ltd.	75
Tabacalera Nacional SA	94	Mauritius	
Guyana		British-American Tobacco (Mauritius) p.l.c. (incorporated in the United Kingdom)	100
Demerara Tobacco Co. Ltd.	70	Nigeria	
Honduras		Nigerian Tobacco Co. p.l.c.	59
Tabacalera Hondurena SA	80	Pakistan	
Jamaica		Pakistan Tobacco Co. Ltd.	65
Carreras Group Ltd. ○	50	Sierra Leone	
Mexico		Aureol Tobacco Co. Ltd.	86
Cigarrera La Moderna SA de CV	100	South Africa	
Nicaragua		British American Tobacco Holdings South Africa (Pty) Ltd.	100
Tabacalera Nicaraguense SA	60	Sri Lanka	
Panama		Ceylon Tobacco Co. Ltd.	84
Tabacalera Istmena SA	100	Uganda	
Surinam		British American Tobacco Uganda Ltd.	90
Tobacco Company of Suriname NV	100	Uzbekistan	
Trinidad & Tobago		UZBAT AO	95
The West Indian Tobacco Co. Ltd.	50	Zimbabwe	
Venezuela		British American Tobacco Zimbabwe Ltd.	85
CA Cigarrera Bigott Sucs	100	Export Leaf Tobacco Co. of Africa (Pvt) Ltd.	100
Amesca		Rothmans of Pall Mall (Zimbabwe) Ltd.	50
Bangladesh		Tobacco Processors Zimbabwe (Pvt) Ltd.	70
British American Tobacco Bangladesh Co. Ltd.	65		

Subsidiary undertakings held directly by British American Tobacco p.l.c. are indicated as thus *, all other subsidiary undertakings are held by sub-holding companies and British American Tobacco p.l.c.'s interest is shown in brackets where this differs from that of the sub-holding company. The country of incorporation is stated and, unless otherwise stated, is also the country of operation. Subsidiary undertakings are involved in activities related to the manufacture, distribution and sale of tobacco products.

All companies' shares are ordinary shares or common stock except for those indicated as thus †, which include preference shares.

Subsidiary undertakings indicated as thus ○, have a financial year different from 31 December, typically being 31 March. These companies are former Rothmans International B.V. companies, and are in the process of changing to 31 December.

In addition, and as described in note 21 on page 39, the Canadian businesses of Rothmans have not been consolidated.

A complete list of investments in subsidiary and associate undertakings will be attached to the British American Tobacco p.l.c. Annual Return made to the Registrar of Companies.

Associates and Joint Venture

Principal Investments

Associates

		Latest published information	Total issued capital £m	% shares held
Canada				
Imasco Ltd.*	○ Ordinary	31.12.99	352	42
<i>tobacco retailing financial services</i>				
Europe				
Denmark				
Skandinavisk Tobakskompagni AS	Class I Ordinary	30.6.99	1	
<i>tobacco</i>				
	Class II Ordinary		30	26
Amesca				
India				
ITC Ltd.	○ Ordinary	31.12.99	35	32
<i>tobacco paper and packaging hotels</i>				
VST Industries Ltd.	○ Ordinary	31.12.99	2	32
<i>tobacco</i>				

Joint Venture

		Latest published information	Total issued capital £m	% shares held
Great Britain				
British American Racing (Holdings) Ltd.	Class A shares	30.11.99	11	100
<i>Formula One Grand Prix racing car team</i>				
	Class B shares		3	
	Class C shares		8	

○ Listed overseas

* Subsequent to 31 December 1999 restructured to become a subsidiary of the Group as of 1 February 2000. See note 26 on page 45 for further details.



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Associates and Joint Venture

results for the year ended 31 December

	Total 1999 £m	Group's share 1999 £m	Total 1998 £m	Group's share 1998 £m
Turnover				
Commercial activities	6,073	2,112	5,622	2,099
Financial services life and investment business <i>below</i>	1,793	761	1,645	693
Turnover including duty, excise and other taxes	7,866	2,873	7,267	2,792
Duty, excise and other taxes	(2,358)	(763)	(1,898)	(664)
Turnover excluding duty, excise and other taxes	5,508	2,110	5,369	2,128
Profit				
Commercial activities	756	277	675	254
Financial services life and investment business <i>below</i>	243	103	192	81
Operating profit <i>page 18</i>	999	380	867	335
Interest paid less received	(62)	(26)	(60)	(23)
Profit before taxation	937	354	807	312
Taxation	(361)	(140)	(299)	(117)
Profit after taxation	576	214	508	195
Attributable to minority shareholders		(8)		(8)
Attributable to British American Tobacco's shareholders		206		187
Dividends – listed investments		(68)		(59)
– unlisted investments		(22)		(27)
Retentions		116		101

The operating profit above includes losses of £20 million 1998 £9 million in respect of the joint venture.

Associates and Joint Venture

results for the year ended 31 December

The amounts shown above for the Group's share include the following amounts relating to Imasco:

	1999 £m	1998 £m
Turnover	1,857	1,910
Operating profit	304	253
Profit before taxation	287	235
Taxation	(108)	(88)
Profit after taxation	179	147
The segmental analysis of the operating profit of Imasco is as follows:		
Tobacco	149	135
Financial services <i>below</i>	103	81
Other <i>below</i>	52	37
Total	304	253

Following the completion of the restructuring of Imasco, from 1 February 2000 Imasco will no longer be included in the results of the Group's associated companies. As explained in note 26(a) on page 45, the tobacco operations will become a wholly owned subsidiary of the Group while the non-tobacco interests will be sold. The discontinued non-tobacco operations contributed £1,286 million of turnover and £155 million of operating profit to Group results in 1999.

Statement of total recognised gains and losses	1999 £m	1998 £m
Attributable profit	206	187
Differences on exchange	30	(34)
Total recognised gains related to the year	236	153

Share of net assets	1999 £m	1998 £m
The Group's share of net assets, mainly represented by Imasco, comprises:		
Fixed assets	689	374
Current assets	9,415	8,346
Liabilities due within one year	(5,483)	(5,486)
Liabilities due beyond one year	(4,017)	(2,766)
	604	468



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Accounting Policies

Group Accounts – including demerged businesses

1 Basis of accounting

On 7 September 1998 B.A.T Industries completed the demerger of its financial services businesses and their merger with Zurich Insurance Company. The remaining businesses were retained within British American Tobacco p.l.c.

The accounts which follow are presented on the basis necessary to comply with company law and accounting standards and comprise the results of the Group, including as part of the 1998 comparatives the trading results of the demerged businesses up to 30 June 1998 and transactions between the retained and demerged businesses after that date. The accounting policies applicable to this financial information comprise those set out below, together with accounting policies 2 to 13 on pages 16 and 17. Similarly the financial information comprises pages 55 to 71, together with the relevant notes on pages 23 to 47 and 50 to 54.

As explained in the Directors' Report the financial information on pages 16 to 47 and 50 to 54 comprise additional information to show the results of the Group as if the demerger had taken effect prior to 1 January 1998.

2 The Group accounts have been prepared in accordance with the Companies Act 1985 (Schedule 4) and applicable accounting standards. They combine the accounts of Group undertakings at 31 December and, as permitted by that Act, the accounts formats have been adapted, as necessary, to give a true and fair view of the state of affairs and profit of the Group. The accounts are on an historical cost basis as modified to include certain insurance assets at market value.

Prior to the demerger, the Group had two main businesses and the accounts formats had been developed to reflect most appropriately the operations of the Group. Given the differences between the two main businesses and the constraints of the regulatory environment within which insurance companies operate, separate cash flow statements were prepared for the two businesses, instead of the consolidated cash flows envisaged by FRS1, as the regulatory environment in insurance limits the availability of cash flows between businesses. Where appropriate, information relating to the financial services activities had been prepared in a manner consistent with the provisions of the Companies Act applicable to insurance companies and the guidance on accounting for insurance business issued by the Association of British Insurers prior to the date of the demerger which is the basis consistent with that adopted by B.A.T Industries in previous years.

The Directors are of the opinion that this approach, where it differs from the Companies Act 1985 and applicable accounting standards was

necessary to present a true and fair view of the Group. Consequently this approach has been continued for this set of accounts, which include results for the demerged financial services businesses.

Depreciation is not provided in respect of freehold and leasehold investment properties for the demerged businesses although the requirement of the Companies Act 1985 is to depreciate all properties. That requirement conflicts with SSAP19 which states that investment properties should not be subject to depreciation. The Directors consider it is necessary to adopt SSAP19 in order to give a true and fair view and in their opinion, depreciation would not be significant on the basis of expected future residual values.

3 Revenue is the summation of turnover of the demerged and retained businesses together with the Group's share of associates. For financial services it comprises gross premium income, excluding insurance premium tax where appropriate, of insurance subsidiary undertakings and management fees from Farmers' exchanges together with unit trust sales, sales of mutual funds and sales of Open Ended Investment Schemes.

4 Profit on ordinary activities before interest comprises profit before taxation from demerged businesses, trading profit from retained businesses and the Group's share of associates' profit before taxation.

5 General business

The balance on the general business technical account is determined after taking account of:

- (a) Premiums that relate to business incepted during the year and include an estimate of pipeline premiums, less an allowance for cancellations.
- (b) Unearned premiums which are the proportion of premiums written in the current year which relate to cover provided in following periods. For financial insurances business unearned premiums are determined having regard to the expected emergence of claims.
- (c) Unexpired risks – provision is made for the estimated amount required over and above unearned premiums and related future investment return to meet aggregate estimated future claims and related expenses on business in force at the period end.
- (d) Movements in equalisation reserves comprise amounts set aside to mitigate exceptional loss experience in future years for classes of business displaying a high degree of claims volatility. These reserves are in addition to the provisions required to meet the anticipated

Accounting Policies

ultimate cost of settlement of outstanding claims at the balance sheet date and are included within technical provisions.

- (e) Deferred acquisition expenses that represent commission and other acquisition costs relating to unearned premiums.
- (f) Claims incurred, which include provisions for the estimated ultimate cost of claims and the related handling expenses in respect of incidents up to period end, including those which had not been notified by that date. Provision for claims for UK employers and public liability and certain lines of excess of loss and facultative business are discounted at a rate appropriate to the income earned on matching assets.

Provision for claims in respect of domestic mortgage indemnity are included from the date of repossession. Potential claims, where repossession has not yet taken place, are included in the unexpired risk calculation.

Within the investment returns, Eagle Star's investment appreciation is the appreciation in its general business funds of listed and unlisted investments, property and mortgages in the year. It includes profits and losses on realisations and the movement in market value of investments held during the year and is stated after offsetting exchange differences on currency liabilities and matching currency investments. Credit is taken in the profit and loss account for one fifth of this appreciation and of the appreciation in the previous four years. Balances not yet credited to the profit and loss account less related deferred taxation are carried forward as deferred investment gains.

The transfer between the profit and loss account and the capital reserve includes the Group's net unrealised element of Eagle Star's investment appreciation.

6 Life (long term) business

- (a) Premiums and consideration for annuities are included when due; for premiums in respect of unit-linked policies, the due date is taken as when the associated units are created.
- (b) Expenses relating to the acquisition and maintenance of business are charged to the technical account. Costs of acquiring new business are deferred to the extent they are recoverable out of future revenue margins and amortised accordingly.
- (c) All claims, except for those in respect of unit-linked policies, are

charged against revenue on notification of death or on expiry of the term of endowment. Surrenders are charged against revenue in the year payment is made or the bonus applied; annuities are charged against revenue in the year in which payment becomes due. Benefits payable under unit-linked policies are charged against revenue in the year such policies cease to participate in the relevant investment fund. Claims incurred include reversionary and terminal bonuses payable during the year. Claims include related handling costs.

- (d) Reassurance premiums, recoveries and related commission and expenses are charged when payable or receivable.
- (e) The long-term business provision is determined by annual actuarial valuation, and includes provision for vested bonuses where applicable. For Allied Dunbar and Eagle Star the long term business provision is determined in accordance with the actuarial principles laid down in the EC Third Life Framework Directive. For Farmers the provision is determined in accordance with United States Generally Accepted Accounting Principles.
- (f) Technical provisions for linked liabilities in the case of unit-linked policies represent the value of the outstanding units in force at the balance sheet date, and for other linked business are determined on the same basis as the long term business provision in (e) above.
- (g) The fund for future appropriations incorporates amounts that have yet to be allocated to either participating policyholders or shareholders. Transfers to, or from, the fund reflect the excess or deficiency of revenues over expenditure to the extent that these have not been allocated to participating policyholders by way of reversionary or terminal bonus, or to shareholders.
- (h) Realised and unrealised gains and losses arising on assets held in respect of the life funds and Farmers' business are included in the technical account; those on other investments are reflected in the unallocated investment return.

7 Taxation provided is that chargeable on the profits of the period, including the grossing up of the life technical account, together with deferred taxation.

For the life funds in Eagle Star, Allied Dunbar and Farmers the transfer from the life technical account is grossed up using the effective taxation rate applicable to the period.



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In the demerged businesses, deferred taxation is provided for on the realisation of investments to the extent that it is probable that the liability will crystallise. However, as noted in accounting policy 8 on page 17, no account is taken of tax which may be payable on the realisation of investments held by retained businesses.

8 Tangible fixed assets

For financial services subsidiary undertakings, all land and buildings are included as investment assets.

9 Interest in underwriting associations is stated at the fair value at the date of acquisition of Farmers Group, Inc. derived from an aggregation of the surpluses in the insurance exchanges, as amended by subsequent changes in certificates in the surplus. The surpluses at acquisition were the amounts shown by the exchanges' financial statements prepared for state insurance regulators. The value is reviewed annually by the Directors and the cost would be written down where a permanent diminution in value was deemed to have occurred.

10 Investments held by financial services subsidiary undertakings have been included on the following bases:

General business – properties at open market values as determined by qualified valuers. Listed investments at middle market values, less accrued interest, or amortised cost which is not materially different to market value. Other investments at Directors' valuations.

Life business – other than where attributable to unit-linked funds, properties and listed investments are at middle market values, amortised cost which is not materially different to market value, or Directors' valuations. Investments of unit-linked funds are at lowest offered dealing price or middle market values.

11 Interest in life businesses is the value attributed by the Directors to the in-force business of life operations at the date of their acquisition by the Group together with subsequent investments in the life funds. Each year the Directors review this value plus the current book value of the other net assets of the life businesses, compared to the value of the Group's equity interest in the life businesses. Any permanent diminution in value would be reflected by a write down of the cost of the interest in the life businesses.



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Statement of Total Recognised Gains and Losses – including demerged businesses for the year ended 31 December

	Notes	1999 £m	1998 £m
Profit for the year <i>page 58</i>		556	637
Differences on exchange	15	(268)	(100)
Total recognised gains related to the year below		288	537

Interest of British American Tobacco's Shareholders – including demerged businesses for the year ended 31 December

	Notes	1999 £m	1998 £m
Balance 1 January	15	64	4,751
Total recognised gains related to the year <i>above</i>		288	537
Issue of shares:			
share options		3	42
Rothmans' merger <i>page 39 note 21</i>		5,089	
Dividends and other appropriations: <i>page 58</i>			
ordinary shares		(546)	(377)
convertible redeemable preference shares		(54)	
amortisation of discount on preference shares		(20)	
demerger			(6,689)
Deferred investment gains			97
Utilisation of ACT			96
Goodwill reinstated on demerger			1,607
Other		(3)	
Balance 31 December	15	4,821	64

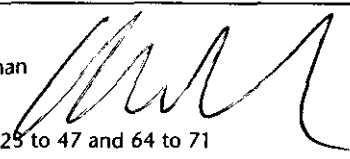
Notes are shown on pages 23 to 47 and 64 to 71.

Group Balance Sheet – including demerged businesses

31 December

	Notes	1999 £m	1998 £m
Assets			
Fixed assets			
Intangible assets	8	5,338	
Tangible assets	9	2,456	2,048
Investments in associates and joint venture	10	636	472
Other investments and long term loans	11	210	119
		8,640	2,639
Current assets			
Stocks	12	2,850	2,165
Debtors	13	2,000	1,493
Acquired business awaiting disposal	21	123	
Current investments	14	768	185
Short term deposits and cash		1,853	970
		7,594	4,813
Total assets		16,234	7,452
Liabilities			
Capital and reserves			
Share capital		605	393
Share premium account		4	1
Merger reserves		4,726	
Other reserves		503	483
Profit and loss account		(1,017)	(813)
Shareholders' funds:	15	4,821	64
equity		3,347	64
non-equity		1,474	
Minority shareholders' equity interest		455	323
		5,276	387
Other liabilities			
Provisions for liabilities and charges	16	1,251	741
Borrowings	17	5,676	3,730
Creditors	19	4,031	2,594
		10,958	7,065
Total funds employed		16,234	7,452

On behalf of the Board
Martin Broughton, Chairman
 7 March 2000



Notes are shown on pages 25 to 47 and 64 to 71



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Group Cash Flow Statements

for the year ended 31 December

	Notes	1999 £m	1998 £m
Retained businesses			
Net operating cash flow from subsidiary undertakings	27	1,995	1,096
Dividends from associates		90	86
Dividends from demerged businesses	28		242
Net cash inflow from operating activities		2,085	1,424
Returns on investments and servicing of finance	28	(206)	(282)
Taxation		(334)	(281)
Capital expenditure and financial investment	28	(281)	(351)
Net cash generation		1,264	510
Acquisitions less disposals – demerger	40		820
– other	28	(216)	(16)
		(216)	804
Equity dividends paid		(530)	(696)
Cash flow with demerged businesses	40		(152)
Cash flow before use of liquid resources and external financing		518	466
Management of liquid resources	28	(1,340)	459
Financing – proceeds from issue of shares		3	42
– increase/(decrease) in debt	28	853	(845)
		856	(803)
Increase in cash in the year below		34	122
Reconciliation of net cash flow to movement in net debt	29		
Increase in cash in the year above		34	122
(Increase)/decrease in debt		(853)	845
Increase/(decrease) in liquid resources		1,340	(459)
Change in net debt resulting from cash flows		521	508
Net debt acquired on purchase of subsidiaries		(754)	
Net funds disposed of on sale of subsidiaries		(23)	
Other changes		(33)	(45)
Differences on exchange		(191)	52
Movement in net debt in the year		(480)	515
Net debt at 1 January		(2,575)	(3,090)
Net debt at 31 December		(3,055)	(2,575)

Notes are shown on pages 23 to 47 and 64 to 71.

Group Cash Flow Statements

for the year ended 31 December

	Notes	1999 £m	1998 £m
Demerged businesses			
Net cash flow from operating activities excluding investment gains	39		431
Finance costs	40		(67)
Taxation			(142)
Capital expenditure	40		(22)
Equity dividends paid			(242)
Other cash flow with retained businesses and demerged businesses	40		(232)
Financing – increase in debt	40		342
			68
Cash flow was invested as follows:			
Decrease in cash in the year			(42)
Net portfolio investment (excluding long term business)	40		
Share and other variable yield securities			(130)
Debt securities and other fixed income securities			440
Investment properties			(1)
Other investments			(199)
			110
Net investment of cash flow			68
Movement in opening and closing portfolio investments net of financing			
Net cash flow for the year			(42)
Cash flow			
Net portfolio investments			110
Increase in debt			(342)
			(232)
Movement arising from cash flow			(274)
Change in market values			248
Other changes			(300)
Changes in life funds			556
Differences on exchange			(30)
			200
Portfolio investments net of financing at 1 January			17,009
Portfolio investments net of financing on demerger			17,209

The life business cash flow above excludes flows of the Allied Dunbar, Eagle Star, and Threadneedle Asset Management life funds.

Notes are shown on pages 23 to 47 and 64 to 71.



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Segmental Analyses – including demerged businesses
of revenue, profit and assets for the year ended 31 December

	General		Life		Total	
	1999 £m	1998 £m	1999 £m	1998 £m	1999 £m	1998 £m
Revenue						
Demerged businesses						
UK		862		1,554		2,416
Rest of Europe		106		218		324
North America		666		142		808
Latin America				44		44
Asia		28		81		109
Africa		96		3		99
		1,758		2,042		3,800
Retained businesses page 22					11,182	9,248
See note below					11,182	13,048

Operating profit

Demerged businesses						
UK		(15)		147		132
Rest of Europe		8		2		10
North America		284		68		352
Latin America						
Asia		(4)				(4)
Africa		14				14
		287		217		504
Retained businesses page 22					1,479	1,011
					1,479	1,515

Operating assets

Retained businesses page 22					10,498	4,384
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Notes relating to retained businesses are shown on page 23.

Analysis of revenue

		1999 £m	1998 £m
Total revenue page 58		21,671	21,176
Less duty, excise and other taxes of retained businesses page 23 note (b)		(10,489)	(8,128)
Total revenue		11,182	13,048

Notes on the Accounts

Profit and Loss Account

30 Turnover and operating profit – retained businesses

	1999 £m	1998 £m
(a) Subsidiary undertakings		
Turnover including duty, excise and other taxes	18,798	14,584
Duty, excise and other taxes	(9,726)	(7,464)
Turnover excluding duty, excise and other taxes	9,072	7,120
Other operating income	150	250
Operating charges	(8,123)	(6,694)
Operating profit	1,099	676

(b) Operating profit is stated		
after charging: US tobacco settlements	(24)	(613)
integration costs	(357)	
goodwill amortisation	(162)	
and crediting: sales tax recovery		74

Operating profit is described more fully in note 1 on pages 24 and 25, and as stated there, the above charges and credit are shown as additional information on the face of the profit and loss account.

31 Turnover and operating profit – financial services general business

	1999 £m	1998 £m
Turnover		
Gross premiums written		1,395
Management fees from Farmers' exchanges		363
		1,758
Operating profit		
Balance on general business technical account <i>note (a)</i>		(113)
Management of underwriting associations <i>note (b)</i>		217
Unallocated investment return <i>note (c)</i>		181
Other income		6
Other charges		(4)
Profit from financial services general business		287



31 Turnover and operating profit – financial services general business continued

	1999 £m	1998 £m
(a) Balance on general business technical account:		
Gross premiums written		1,395
Outward reinsurance premiums		(89)
Net premiums written		1,306
Change in provision for unearned premiums – gross		(58)
– reinsurers' share		10
– net		(48)
Earned premiums, net of reinsurance		1,258
Allocated investment return <i>note (c)</i>		37
		1,295
Claims paid – gross		(1,038)
– reinsurers' share		68
– net		(970)
Change in provision for claims – gross		7
– reinsurers' share		(20)
– net		(13)
Claims incurred, net of reinsurance		(983)
Net operating expenses:		
Acquisition costs arising in the year		(245)
Change in deferred acquisition costs		8
Administrative expenses		(192)
Reinsurance commissions and profit participation		11
Change in equalisation provision		(7)
		(1,408)
		(113)
(b) Management of underwriting associations:		
Management fees from Farmers' exchanges		363
Management expenses		(146)
		217

Notes on the Accounts

Profit and Loss Account

31 Turnover and operating profit – financial services general business continued

	1999 £m	1998 £m
(c) Unallocated investment return:		
Income from:		
– Loans to retained businesses subsidiary undertakings		16
– Land and buildings		5
– Listed investments		115
– Other investments		59
		195
Interest payable on loans from retained businesses subsidiary undertakings		(26)
Interest payable on other loans		(39)
Net realised gains on investments		176
Net unrealised gains on investments		45
Investment expenses and charges		(6)
		345
Net investment return		345
Transfer to technical account <i>note (a)</i>		(37)
Transfer to deferred investment gains		(127)
		181

(d) As described in accounting policy 5(f) on page 56, the Group uses a five-year moving average to measure investment returns. If profit were measured including all realised and unrealised investment gains and losses as they arise with no averaging, operating profit for 1998 for general business would have been £414 million and £221 million for life business. If 1998 profit were measured excluding unrealised investment gains and losses operating profit for the general business would have been £369 million and £216 million for the life business. For the life business the adjustments relate only to certain investments held outside life funds.

32 Turnover and operating profit – financial services life business

	1999 £m	1998 £m
Turnover		
Gross premiums written		1,764
Sales of unit trusts, OEIC and mutual funds		278
		2,042
Operating profit		
Balance on long term business technical account <i>note (a)</i>		141
Tax attributable to shareholders' profits from life funds		45
Tax attributable to Farmers' long term business		24
		210
Unallocated investment return <i>note (b)</i>		4
Unit trust, OEIC and mutual fund sales		239
Unit trust, OEIC and mutual fund creations and repurchases		(220)
Other income		17
Other charges		(33)
Profit from financial services life business		217

32 Turnover and operating profit – financial services life business continued

	1999 £m	1998 £m
(a) Balance on long term business technical account:		
Gross premiums written		1,764
Outward reinsurance premiums		(15)
Earned premiums, net of reinsurance		1,749
Allocated investment return <i>note (b)</i>		3,189
Other technical income		2
		4,940
Claims paid – gross		(1,353)
– reinsurers' share		10
– net		(1,343)
Change in provision for claims – gross		(7)
– reinsurers' share		1
– net		(6)
Claims incurred, net of reinsurance		(1,349)
Change in long term business provision – gross		(408)
– reinsurers' share		6
– net		(402)
Change in technical provisions for linked liabilities, net of reinsurance		(2,359)
Net operating expenses:		
Acquisition costs		(248)
Change in deferred acquisition costs		31
Administrative expenses		(119)
Tax attributable to life funds		(336)
Tax attributable to Farmers' long term business		(112)
Transfer to the fund for future appropriations		(24)
		(217)
		(4,799)
		141

Notes on the Accounts

Profit and Loss Account

32 Turnover and operating profit – financial services life business continued

	1999 £m	1998 £m
(b) Unallocated investment return		
Income from:		
Loans to retained businesses subsidiary undertakings		1
Land and buildings		73
Listed investments		550
Other investments		164
		788
Interest payable on loans repayable within 5 years		(7)
Net realised gains on investments		647
Net unrealised gains on investments		1,818
Investment expenses and charges		(49)
		3,197
Net investment return		3,197
Transfer to technical account <i>note (a)</i>		(3,189)
Transfer to deferred investment gains		(4)
		4

(c) The total amount of bonuses and rebates charged to the long term business technical account in 1998 was £76 million.

33 Financial services operating profit – general and life businesses

	1999 £m	1998 £m
Operating profit is stated after charging:		
Staff costs <i>note (a)</i>		306
Depreciation – plant and machinery		37
Rent of machinery and other equipment (operating leases)		6
Rent of land and buildings (operating leases)		27
Auditors' fees		1
Fees paid to PricewaterhouseCoopers in the UK for advisory and consultancy services		1.2
(a) Staff costs comprise:		
Wages and salaries		261
Social security costs		26
Other pension costs <i>note (b)</i>		19
		306
(b) Other pension costs comprise:		
Funded plans – defined contribution		16
– defined benefit		2
Unfunded plans – defined benefit		1
		19



Notes on the Accounts

Profit and Loss Account and Other Financial Information

34 Demerger and debt restructuring costs

	1999 £m	1998 £m
Demerged businesses		(29)
Retained businesses <i>note 2(b) page 25</i>		(46)
		(75)

The charge in the demerged businesses represents the initial provisions for reorganising the financial services operations in the UK in preparation for the merger with Zurich Group.

The tax effect of these costs was to reduce the 1998 taxation charge by £14 million.

35 Taxation on ordinary activities

	1999 £m	1998 £m
UK Corporation Tax at 30.25% 1998 31.00%	62	396
Double taxation relief	(77)	(190)
Tax attributable to UK dividends receivable		3
ACT written back		(5)
UK taxation	(15)	204
Overseas taxation	434	280
Current taxation	419	484
Deferred taxation	114	(148)
	533	336
Share of associates and joint venture	140	117
	673	453

36 Earnings per share

Basic earnings per share is based on equity earnings of **£482 million** 1998 **£637 million** and **1,910 million** 1998 **2,356 million** ordinary shares, being the weighted average number of British American Tobacco and B.A.T Industries shares in issue during the year. For 1998 the average number of shares is based on the average of the shares of B.A.T Industries for the period for which the results of the demerged businesses have been recognised and of British American Tobacco thereafter.

For diluted earnings per share the average number of shares in issue is increased to **2,058 million** 1998 **2,365 million** to reflect the potential dilution effect of the convertible redeemable preference shares and the exercise of employee share options.

37 Group employees

The average number of persons employed by the Group during the year was **107,620** 1998 **112,973**.

	1999	1998
UK		6,277
Rest of Europe		1,012
North America		3,681
Latin America		37
Asia		219
Africa		666
Demerged businesses		11,892
Retained businesses <i>note 22 page 40</i>	107,620	101,081
	107,620	112,973

Details of Directors' remuneration and share options are given in the Remuneration Report on pages 6 to 11.

Notes on the Accounts

Other financial information

38 Demerger of financial services businesses

In September 1998 the demerger of B.A.T Industries' financial services businesses and their merger with Zurich Insurance Company was completed. The demerged businesses included all of the principal financial services subsidiaries, including Farmers, Eagle Star, Allied Dunbar and Threadneedle Asset Management.

Under the agreement the financial services businesses, together with those of Zurich, were transferred into Zurich Financial Services, a new Swiss company with headquarters in Zurich. Shareholders in a UK-based company, Allied Zurich p.l.c. ('AZ'), have a 43 per cent interest in this new company and the shareholders of Zurich have a 57 per cent interest.

The remaining businesses of B.A.T Industries were retained within a separately listed company, British American Tobacco p.l.c.

As a result of the demerger B.A.T Industries' shareholders received one share in British American Tobacco p.l.c. and one share in AZ for every two B.A.T Industries' shares held.

The share capital of the demerged business was distributed by way of a dividend in specie and the demerger dividend represents their net assets after reinstating goodwill previously eliminated against reserves, leaving the Group for nil proceeds. It is calculated as follows:

	£m
Interest in underwriting associations	1,539
Interest in life businesses	686
Investments	18,935
Assets held to cover linked liabilities	21,431
Reinsurers' share of technical provisions	705
Other assets	3,963
Insurance funds	(37,725)
Borrowings	(2,111)
Other liabilities	(2,257)
	5,166
Minority interests	(84)
	5,082
Goodwill previously eliminated against reserves	1,607
Demerger dividend	6,689

39 Reconciliation of operating profit to net cash flow from operating activities

	General		Life		Total	
	1999 £m	1998 £m	1999 £m	1998 £m	1999 £m	1998 £m
Operating profit – general business <i>page 64 note 31</i>		287				287
Operating profit – life business <i>page 66 note 32</i>				217		217
Depreciation		28		6		34
Exclusion of investment gains		(94)		(5)		(99)
Increase in technical provisions		51		47		98
Increase in other assets		(174)		(22)		(196)
Increase in other liabilities		68		23		91
Taxation attributable to shareholders' profits						
from life funds				(45)		(45)
Other		38		6		44
Net cash inflows from operating activities						
excluding investment gains <i>page 62</i>		204		227		431



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Notes on the Accounts

Cash Flow Statements

40 Analysis of items netted in the cash flow statement

	General		Life		Total	
	1999 £m	1998 £m	1999 £m	1998 £m	1999 £m	1998 £m
Finance costs: interest paid		(66)		(1)		(67)
Capital expenditure		(20)		(11)		(31)
Sale of fixed assets		7		2		9
Capital expenditure		(13)		(9)		(22)
Investments		(4)		174		170
Loans and current accounts – to date of demerger		(8)		(10)		(18)
Cash flows – retained businesses <i>page 61</i>		(12)		164		152
Loans and current accounts – on demerger		(386)				(386)
Cash flows with the life funds				2		2
Other cash flows with retained and demerged businesses <i>note (a)</i>		(398)		166		(232)
Surplus notes		386				386
Other loans		(55)		11		(44)
Financing – increase in debt		331		11		342
Purchases of share and other variable yield securities		(328)		(9)		(337)
Sales of share and other variable yield securities		466		1		467
Purchases of debt securities and other fixed income securities		(1,826)		(238)		(2,064)
Sales of debt securities and other fixed income securities		1,474		150		1,624
Purchases of investment properties		(2)		(3)		(5)
Sales of investment properties		6				6
Purchases of other investments		(1,400)		(65)		(1,465)
Sales of other investments		1,654		10		1,664
Net portfolio investment		44		(154)		(110)

(a) Retained businesses

In the retained businesses cash flow dividends from the demerged businesses are included in the net cash flow from operating activities, as this is consistent with the presentation in the other primary statements.

The cash inflow of £820 million in 1998 arising on the demerger comprises the outflow of £386 million in the demerged businesses cash flow noted above together with other inflows to the retained businesses of £434 million.

The total Group increase in cash in the year including retained businesses (see page 47 note 29) was **£34 million** 1998 £80 million. However as explained in accounting policy 2 on page 55, the Directors are of the opinion that the separate disclosure of assets and liabilities for each business and of the cash flows for each business is necessary to present a true and fair view of the Group.

Balance Sheet – British American Tobacco p.l.c.

31 December

	Notes	1999 £m	1998 £m
Assets			
Fixed assets			
Investments in Group companies	41	393	393
Other investments	42	49	21
		442	414
Current assets			
Debtors	43	2,045	647
		2,045	647
Total assets		2,487	1,061
Liabilities			
Capital and reserves			
Share capital		605	393
Share premium account		4	1
Other reserves		20	
Profit and loss account		1,368	257
Shareholders' funds:	44	1,997	651
equity		1,916	651
non-equity		81	
Other liabilities			
Creditors	45	490	410
Total funds employed		2,487	1,061

On behalf of the Board
Martin Broughton, Chairman
7 March 2000



Notes are shown on pages 73 to 76

Notes on the Accounts

Balance Sheet

41 Investments in Group companies

The Company's directly owned subsidiary at 31 December 1999 was British American Tobacco (1998) Limited. On 7 June 1999 the Company acquired the entire issued share capital of Rothmans International B.V. This was subsequently disposed of on 30 November 1999 at book value to a wholly-owned subsidiary.

The Directors are of the opinion that the investment in the subsidiary undertaking has a value not less than the amount at which it is shown in the balance sheet.

42 Other investments

Other investments are listed equity investments being shares in the Company owned by the British American Tobacco Employee Share Ownership Trust. The market value of these shares at 31 December 1999 was **£34 million** 1998 **£23 million**.

43 Debtors

	1999 £m	1998 £m
Amounts due from subsidiary undertakings	2,004	613
Taxation recoverable	31	31
Other debtors	5	
Prepayments and accrued income	5	3
	2,045	647

All the above amounts are due within one year except for £31 million in 1998 in respect of taxation recoverable.

Notes on the Accounts

Balance Sheet

44 Shareholders' funds

	Ordinary share capital £m	Share premium account £m	Other reserves £m	Profit and loss account £m	Total £m
1 January 1999	393	1		257	651
Increase in share capital	212	3			215
Transfer from profit and loss account				1,728	1,728
Dividends and other appropriations:					
Ordinary shares				(546)	(546)
Convertible redeemable preference shares <i>below</i>				(54)	(54)
Amortisation of discount on preference shares <i>below</i>				(20)	(20)
Other movements			20	3	23
31 December 1999	605	4	20	1,368	1,997
				1999 £m	1998 £m
Shareholders' funds comprise:					
Equity				1,916	651
Non-equity <i>below</i>				81	
				1,997	651
Non-equity interests comprise:					
Convertible redeemable preference shares				61	
Amortisation of the discount arising on the issue of these shares				20	
				81	

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the Company has not been presented in these financial statements. The Company was incorporated on 23 July 1997 with the name Measureprofit Public Limited Company. Its name was changed to British American Tobacco p.l.c. on 24 April 1998. The profit for the year ended 31 December 1999 was £1,728 million. The profit from the date of incorporation to 31 December 1998, dealt with in the accounts of the Company, was £634 million.



44 Shareholders' funds continued

Share capital	Ordinary No. of shares	Convertible redeemable preference No. of shares	£m
Authorised			
1 January 1999	2,000,000,000		500.00
Changes in the authorised share capital were as follows:			
8 April 1999 – ordinary shares of 25p each	858,265,349		214.57
8 April 1999 – convertible redeemable preference shares of 25p each		241,734,651	60.43
	2,858,265,349	241,734,651	775.00
Allotted, called up and fully paid			
1 January 1999	1,571,233,101		392.81
Changes during the year were:			
7 June 1999 – ordinary shares of 25p each	604,336,627		151.09
7 June 1999 – convertible redeemable preference shares of 25p each		241,734,651	60.43
Share option schemes	1,332,888		0.33
	2,176,902,616	241,734,651	604.66

Share premium

The increase in the year of £3 million relates solely to ordinary shares issued under the Company's share option schemes. No share premium has been recorded in respect of the shares issued as consideration for the acquisition of Rothmans International B.V. as the Company has taken advantage of the provisions of Section 131 Companies Act 1985.

Convertible redeemable preference shares

On 7 June 1999 the Company issued, 604,336,627 ordinary shares of 25p each and 241,734,651 convertible redeemable preference shares of 25p each in consideration for the acquisition of the entire issued share capital of Rothmans International B.V.

Each convertible redeemable preference share will automatically convert into an ordinary share on a one for one basis on any disposal of such a share to a third party not under the control of the shareholders. The holders of convertible redeemable preference shares may at any time require the Company to convert such shares into ordinary shares on a one for one basis, provided that such conversion will not result in such holders having an aggregate holding of more than 25 per cent of the entire issued ordinary share capital of the Company.

The shares will rank uniformly with ordinary shares for distribution of profits. On a return of capital on a winding-up, the assets will be applied in priority to a payment to the holders of any other class of shares in paying the holders of convertible redeemable preference shares the sum of 575p per share until the first anniversary of their issue and 675p per share thereafter.

Holders of convertible redeemable preference shares will only be entitled to vote at general meetings on a resolution for the winding-up of the Company; on any resolution varying, modifying, or abrogating any of the rights or provisions attaching to their shares.

On the first anniversary of the date of issue of the convertible redeemable preference shares, the holders may require the Company to redeem up to 50 per cent of the total number of such shares issued at a cost of 575p per share. The holders must give the Company six months' notice of their desire to redeem up to half of the shares eligible for redemption and three months' notice of their desire to redeem the other half. Notice of the intention to redeem was given in respect of the first half of the shares eligible for redemption on 2 December 1999 and for the second half on 6 March 2000.

On the fifth anniversary of the date of issue of the convertible redeemable preference shares, the Company will be required to redeem all such shares not previously redeemed or converted into ordinary shares. The redemption price will be 675p per share.

The amortisation of discount on convertible redeemable preference shares reflects the difference between the share price at 7 June 1999 and the redemption price in 2004, which is being amortised over the period to the redemption date.

Notes on the Accounts

Balance Sheet and Profit and Loss Account

45 Creditors

	1999 £m	1998 £m
Dividends payable	434	377
Amounts due to subsidiary undertakings	55	
Taxation on profits – UK		31
Sundry creditors	1	2
	490	410

All the above amounts are due within one year.

46 Audit fees

	1999	1998
Auditors' fees	£30,000	£30,000
Fees paid to PricewaterhouseCoopers for advisory and accountancy services – UK	£nil	£nil

47 Contingent liabilities and financial commitments

British American Tobacco p.l.c. has guaranteed borrowings by subsidiary undertakings of **£4,707 million** 1998 £3,089 million and total borrowing facilities of **£10,886 million** 1998 £10,748 million. In addition, on completion of the acquisition of Imasco (details of which are set out on page 45 note 26 (a)), the Company has guaranteed indebtedness of Imperial Tobacco Canada Limited. As at 1 February 2000 this amounted to C\$2,091 million (£894 million) comprising debentures, medium term notes, drawn bank credit facilities and commercial paper outstandings. In addition, the Company guaranteed a US\$1 billion (£617 million) undrawn committed revolving credit facility.

Performance guarantees given to third parties in respect of Group companies were **£49 million** 1998 £21 million.