B.A.T CAPITAL CORPORATION

Financial Statements

December 31, 2019 and 2018

(With Independent Auditors' Report Thereon)

B.A.T CAPITAL CORPORATION

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KPMG LLP
Suite 400
300 North Greene Street
Greensboro, NC 27401

Independent Auditors' Report

The Board of Directors
B.A.T Capital Corporation:

We have audited the accompanying financial statements of B.A.T Capital Corporation, which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of operations, shareholder's deficit, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of B.A.T Capital Corporation as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG LLP

Greensboro, North Carolina
March 25, 2020

B.A.T CAPITAL CORPORATION

Balance Sheets

December 31, 2019 and December 31, 2018

(Dollars in thousands)

Assets	**2019**	**2018**
Current assets:		
Cash and cash equivalents	$ 16,664	$ 11,288
Due from affiliates	1,574,214	913,221
Guarantee fee receivable from affiliates	38,671	31,856
Accrued interest receivable from affiliates	250,575	240,270
Loan receivable from affiliates	2,225,903	1,200,000
Other amounts due from affiliates	192,712	492
Total current assets	4,298,739	2,397,127
Long-term assets:		
Loan receivable from affiliate	20,199,198	19,932,536
Derivative financial instruments	173	—
Deferred income tax assets, net	143,822	86,374
Total assets	$ 24,641,932	$ 22,416,037
Liabilities and Shareholder's Deficit		
Current liabilities:		
Due to affiliates	$ 3,018,503	$ 2,184,056
Guarantee fee payable to affiliate	38,661	31,856
Accounts payable and accrued liabilities	115	503
Accrued interest payable	237,349	218,800
Derivative financial instruments	357,260	188,471
Current portion of long-term debt	999,575	—
Income taxes payable	42,883	10,143
Total current liabilities	4,694,346	2,633,829
Long-term liabilities:		
Long-term debt	20,093,601	19,873,430
Total liabilities	24,787,947	22,507,259
Shareholder's deficit:		
Common shares, $1 par value (2,000 shares authorized, issued and outstanding)	2	2
Additional paid-in capital	29,499	29,499
Accumulated other comprehensive loss	(310,569)	(98,727)
Retained Earnings (Accumulated deficit)	135,053	(21,996)
Total shareholder's deficit	(146,015)	(91,222)
Total liabilities and shareholder's deficit	$ 24,641,932	$ 22,416,037

See accompanying notes to financial statements

B.A.T CAPITAL CORPORATION

Statements of Operations

Years ended December 31, 2019 and December 31, 2018

(Dollars in thousands)

		2019		2018
Interest income	$	1,809	$	281
Interest income from affiliates		812,544		739,708
Guarantee fee reimbursement from affiliates		195,974		191,266
Other reimbursement income from affiliates		215,947		8,896
Total income		**1,226,274**		**940,151**
Interest expense		662,214		625,149
Interest expense to affiliates		132,720		91,481
Guarantee fees to affiliate		195,974		191,266
Net loss on derivatives		50,390		143,735
Foreign exchange gains		(24,293)		(134,855)
Loss on early extinguishment of debt		6,457		—
General and administrative and other expenses		4,016		303
Total expenses		1,027,478		917,079
Income before income taxes		198,796		23,072
Income tax expense		41,747		12,805
Net income	$	**157,049**	**$**	**10,267**
Other comprehensive loss:				
Loss on interest rate swaps, net of tax benefit (2019 - $18,854; 2018 - $26,244)		(70,929)		(98,727)
Loss on pre-hedge settlement, net of tax benefit (2019 - $37,459)		(140,913)		—
Comprehensive loss	$	**(54,793)**	**$**	**(88,460)**

See accompanying notes to financial statements.

B.A.T CAPITAL CORPORATION

Statements of Shareholder's Deficit

Years ended December 31, 2019 and December 31, 2018

(Dollars in thousands)

	Common shares										
	Shares		Amount		Additional paid-in capital		Accumulated other comprehensive loss		Accumulated earnings (deficit)		Total
Balance at December 31, 2017	2,000	$	2	$	334,999	$	—	$	(32,263)	$	302,738
Net income	—		—		—		—		10,267		10,267
Derivative, net of $26,244 tax benefit							(98,727)				(98,727)
Return of capital	—		—		(305,500)		—		—		(305,500)
Balance at December 31, 2018	2,000		2		29,499		(98,727)		(21,996)		(91,222)
Net income	—		—		—		—		157,049		157,049
Derivative, net of $56,313 tax benefit	—		—		—		(211,842)		—		(211,842)
Balance at December 31, 2019	2,000	$	2	$	29,499	$	(310,569)	$	135,053	$	(146,015)

See accompanying notes to financial statements.

B.A.T CAPITAL CORPORATION

Statements of Cash Flows

Years ended December 31, 2019 and December 31, 2018

(Dollars in thousands)

	2019	2018
Cash flows from operating activities:		
Net income	$ 157,049	$ 10,267
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of loan fees received from affiliate	(8,985)	(8,896)
Amortization of debt issuance costs and discounts and termination of derivatives	16,421	8,722
Loss on early extinguishment of debt	6,457	—
Foreign exchange gains	(24,293)	(134,855)
Derivative losses, net	50,390	143,735
Deferred income tax (income) expense	(1,135)	2,662
Other changes that provided (used) cash:		
Accrued interest receivable from affiliate	(10,305)	(5,646)
Other amounts due from affiliates	(192,230)	305,009
Accounts payable and accrued liabilities	(388)	356
Accrued interest payable	18,549	2,609
Income taxes payable	32,740	(99,655)
Interest payable on derivative financial instruments	28,209	2,373
Other, net	1,751	(36)
Net cash flows from operating activities	74,230	226,645
Cash flows (used in) from investing activities:		
Net proceeds from cash agreements with affiliates	173,454	1,124,389
Loans to affiliates	(1,285,580)	(1,200,000)
Net cash flows used in investing activities	(1,112,126)	(75,611)
Cash flows from (used in) financing activities:		
Return of capital to parent	—	(305,500)
Proceeds from issuance of notes	3,500,000	—
Payment of debt issuance costs	(16,000)	—
Repayments of long-term debt	(2,250,000)	—
Payment for early extinguishment of debt	(6,457)	—
Proceeds (payment) on termination of derivative contracts	(184,271)	665
Net cash flows from (used in) financing activities	1,043,272	(304,835)
Net increase (decrease) in cash	5,376	(153,801)
Cash and cash equivalents – beginning of year	11,288	165,089
Cash and cash equivalents – end of year	$ 16,664	$ 11,288
Supplemental cash flow information:		
Interest paid	$ 626,796	$ 613,813
Income taxes paid	$ 2,350	$ 109,798

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

(a) Basis of Presentation

The accompanying financial statements present the financial position, results of operations and cash flows of B.A.T Capital Corporation, referred to as the Company, an indirect wholly owned subsidiary of British American Tobacco p.l.c., referred to as BAT, a company incorporated under the laws of England and Wales. Until December 7, 2016, the Company was a direct subsidiary of BAT. On December 7, 2016, following a sale of the Company by BAT to Louisville Securities Limited, referred to as LSL, the Company was purchased by BATUS Holdings Inc., referred to as BHI, from LSL pursuant to a stock purchase agreement and BHI became the sole stockholder and parent of the Company. Both LSL and BHI are indirect wholly-owned subsidiaries of BAT. The sale and purchase were at carrying value as the entities were under common control. The Company, incorporated in Delaware, has 2,000 common shares authorized, issued and outstanding with a par value of one dollar per share. The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America.

(b) Nature of Business

The Company is a U.S. finance company that has historically been an issuer and a guarantor under the BAT Euro Medium Term Note Programme, referred to as the EMTN Program, (see note 2 and note 7) and has provided financing and cash management services to BAT companies in the U.S. Other than its role as a guarantor, the Company had been inactive for several years prior to 2017. On July 24, 2017, the Company borrowed $20 billion from a syndicate of third party banks under a bridge facility agreement and loaned the proceeds to BHI to fund a portion of the acquisition price paid to purchase the remaining 58% of Reynolds American Inc., referred to as RAI, not already owned by the BAT group, referred to as the RAI merger. On August 15 and August 16, 2017, the Company repaid the borrowings under the bridge facility agreement and issued approximately $20 billion of notes denominated in US dollars (USD), British pounds sterling (GBP) and euros (EUR) with tenors ranging from 3 years to 30 years.

Subsequent to the merger, in addition to the financing provided to BHI, the Company is providing financing and cash management services to RAI and guarantees certain debt of B.A.T. International Finance p.l.c., referred to as BATIF, an affiliated subsidiary of BAT. BATIF serves as the primary financing and cash management company for the BAT group.

(c) Cash and Cash Equivalents

Cash and cash equivalents may include money market funds, commercial paper and time deposits in major institutions to minimize investment risk. As short-term, highly liquid investments readily convertible to known amounts of cash, with remaining maturities of three months or less at the time of purchase, cash equivalents have carrying values that approximate fair values.

As of July 1, 2019, the Company’s cash is swept into a cash pooling structure managed by B.A.T. Operating Finance Limited, referred to as BATOF, previously managed by BATIF. The Company has an In-House Cash, or IHC, account which represents its interest in the cash pooling structure and amounts in the Company’s IHC account are due on demand and earn interest. As further discussed below in note 4, the IHC agreement provides the Company with a $900.0 million overdraft facility.

(d) Fair Value Measurement

The Company determines the fair value of assets and liabilities using a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity, and the reporting entity's own assumptions about market participant assumptions based on the best information available in the circumstances.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, essentially an exit price.

The levels of the fair value hierarchy are:

Level 1: inputs are quoted prices, unadjusted, in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2: inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. A Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: inputs are unobservable and reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability.

(e) Derivative Financial Instruments

The Company uses derivative instruments to manage certain interest rate and foreign currency risks. All derivative contracts entered into by the Company are with BATIF as the counterparty.

Derivatives are recognized on the Company's balance sheets at fair value and are classified according to their asset or liability position and the expected timing of settlement. Changes in the fair values of derivatives are recorded in net income (loss) or other comprehensive income (loss) based on whether the instrument is designated and effective as a hedge transaction and, if so, the type of hedge transaction.

(f) Revenue Recognition

The Company applies ASU 2014-09, Revenue from Contracts with Customers (Topic 606), together with its related supplemental implementation guidance. This accounting standard establishes principles for reporting information about the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. Substantially all of the Company's net revenues are from transactions with BHI and RAI and consist of interest income and reimbursements of guarantee fees and other related financing expenses incurred by the Company. Loan and reimbursement agreements provide the terms and conditions for these transactions. Interest income is recognized as earned in accordance with the interest provisions in the underlying loan agreements. Reimbursement income is recognized when qualified expenses under the reimbursement agreements are incurred by the Company.

(g) Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Interest and penalties related to uncertain tax positions are accounted for as tax expense.

For federal income tax purposes, the Company's results are included in the consolidated United States federal income tax return of BHI. For state income tax purposes, the Company's results are included in 28 combined state income tax returns that include members of the consolidated United States federal income tax return of BHI. For financial reporting purposes, the Company's current and deferred income taxes are calculated using the separate return method. All current and deferred tax expense and current and deferred tax liabilities are calculated as if the Company files separate federal and state income tax returns that exclude the income, deductions and tax attributes of BHI.

The Company accounts for uncertain tax positions which require that a position taken or expected to be taken in a tax return be recognized in the financial statements when it is more likely than not (a likelihood of more than 50%) that the position would be sustained upon examination by tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. The Company did not have any uncertain tax positions for 2019 or 2018. The federal statute of limitations remains open for tax years 2016 through 2019.

(h) ***Accounting Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts in the financial statements and accompanying notes. Actual results could differ from those estimates.

(i) ***Contingencies***

In accordance with ASC 450, *Contingencies*, the Company records any loss related to a contingency at the time that likelihood of a loss becomes probable and the amount of the loss can be reasonably estimated. When the reasonable estimate is a range, the best estimate within that range will be recorded. When no amount within the range is more likely, the lowest amount within the range will be recorded. No such amounts were recorded for the years ended December 31, 2019 and 2018.

(j) ***Subsequent Events***

Subsequent events have been evaluated through March 25, 2020, the date the financial statements were issued.

(k) ***Recently Issued Accounting Pronouncementss***

In June 2016, the Financial Accounting Standards Board issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*, which replaces the current incurred loss impairment methodology for recognizing credit losses for financial instruments with a methodology that reflects expected credit losses and requires consideration for a broader range of reasonable and supportable information for estimating credit losses. The amended guidance is effective for fiscal years beginning after December 15, 2022. The amended guidance is not expected to have a material impact on the Company's results of operations, cash flows and financial position.

(2) Long-Term Debt

Revolving Credit Facillity

In connection with the RAI acquisition, the Company, along with other subsidiaries of BAT and with BAT as Guarantor, entered into a two-tranche £6.0 billion forward starting revolving credit facility, which consists of a £3.0 billion 364-day revolving credit facility (with a one-year extension option and a one-year term-out option) and a £3.0 billion revolving credit facility, maturing in 2021. The Company had no amounts outstanding under either revolving credit facility as of December 31, 2019 or December 31, 2018.

On March 12, 2020, the Company, along with other subsidiaries of BAT, entered into a new two-tranche £6.0 billion revolving credit facility, consisting of a £3.0 billion 364-day revolving credit facility (with two extension options and a term-out option) and a £3.0 billion revolving credit facility (with two extension options), maturing in 2025.

Long-term Notes

On August 15, 2017 and August 16, 2017, the Company issued approximately $20 billion in notes consisting of $17.25 billion in USD denominated notes, referred to as the USD notes, $2.2 billion equivalent in EUR denominated notes, and $0.6 billion equivalent in GBP denominated notes, in the aggregate referred to as the BATCAP Notes. The USD notes were issued in a private offering exempt from, or not subject to, the registration requirements of the federal securities laws and were subject to a registration rights agreement. The USD notes maturities range from 2020 to 2047. The notes denominated in GBP and EUR were sold to investors under the existing EMTN Program. The maturities for the EUR denominated notes are 2021 and 2023, and the maturity date for the GBP denominated notes is 2025. Under the terms of the EMTN Program, the notes were guaranteed by BAT, BATIF and certain other BAT affiliates. The BATCAP Notes were issued net of discounts of $4.2 million and the Company paid $79.8 million in fees and expenses. The discounts and debt issuance costs are being amortized, using the effective interest rate method, as interest expense over the life of the respective notes.

In July 2019, BAT filed a registration statement on Form F-3 with the U.S. Securities and Exchange Commission, referred to as the SEC, to allow BATCAP and BATIF to offer and sell from time to time debt securities up to an aggregate amount of $10.0 billion over the next three years. Debt securities issued under this facility are guaranteed by BAT, BATIF and certain other BAT affiliates. On September 6, 2019, the Company issued $3.5 billion of USD denominated notes under this facility, referred to as the USD 2019 Notes, with maturities ranging from 2024 to 2049. Upon issuance of these notes, the Company paid $16.0 million in fees that are being amortized, using the effective interest rate method, as interest expense over the life of the respective notes.

With a portion of the proceeds from this debt offering, the Company prepaid a $2.25 billion USD note bearing fixed interest at 2.297% that was due August 14, 2020. The Company incurred a $6.5 million loss on the early extinguishment of this debt.

The Company recognized interest expense of $662.2 million, including $6.1 of amortization related to terminated derivatives, and $625.1 million in 2019 and 2018, respectively and, as of December 31, 2019 and 2018, had accrued $237.3 million and $218.8 million in accrued interest payable related to the BATCAP Notes and the USD 2019 Notes.

Details of the BATCAP Notes and the USD 2019 Notes at carrying value, including a schedule of maturities, included in the Company's long-term debt is as follows (in thousands):

	For the years ended December 31,	
	2019	**2018**
USD notes:		
2.297% notes due 08/14/2020	$ -	$ 2,250,000
3 month LIBOR plus 0.59% notes due 08/14/2020	1,000,000	1,000,000
3 month LIBOR plus 0.88% notes due 08/15/2022	750,000	750,000
2.764% notes due 08/15/2022	2,250,000	2,250,000
3.222% notes due 08/15/2024	2,500,000	2,500,000
2.789% notes due 09/6/2024	1,000,000	-
3.215% notes due 09/6/2026	1,000,000	-
3.557% notes due 08/15/2027	3,500,000	3,500,000
3.462% notes due 09/6/2029	500,000	-
4.390% notes due 08/15/2037	2,500,000	2,500,000
4.540% notes due 08/15/2047	2,500,000	2,500,000
4.758% notes due 09/6/2049	1,000,000	-
EUR notes:		
3 month EURIBOR plus 0.5% notes due 08/16/2021, face value €1,100,000,000	1,233,320	1,261,370
1.125% notes due 11/16/2023, face value €750,000,000	840,900	860,025
GBP notes:		
2.125% notes due 08/15/2025, face value £450,000,000	596,565	573,930
Total principal	21,170,785	19,945,325
Unamortized discount	(2,874)	(3,386)
Unamortized debt issuance costs	(74,735)	(68,509)
Total long-term debt at carrying value	21,093,176	19,873,430
Less current maturities of long-term debt at carrying value	999,575	-
Total long-term debt (less current maturities) at carrying value	$ 20,093,601	$ 19,873,430

The EUR denominated debt and GBP denominated debt is valued using the foreign denominated face value and the related spot rate for the respective currency at the respective measurement date. Accordingly, in 2019, the Company recognized a gain of $24.5 million from the revaluation of the carrying value of the EUR denominated debt and GBP denominated debt to the December 31, 2019 spot rate. In 2018, the Company recognized a gain of $134.9 million for the revaluation of the carrying value of the EUR denominated debt and GBP denominated debt to the December 31, 2018 spot rate.

As of December 31, 2019, the maturities of the BATCAP Notes and the USD 2019 Notes, excluding unamortized discount and debt issuance costs, for the next five years and thereafter are as follows:

Year	Total
2020	$ 1,000,000
2021	1,233,320
2022	3,000,000
2023	840,900
2024	3,500,000
2025 and thereafter	11,596,565
	$ 21,170,785

Fair Value of Debt

The estimated fair value of the Company's outstanding debt, in the aggregate, was $21.5 billion as of December 31, 2019 and $18.2 billion as of December 31, 2018. The fair value is derived from a third-party pricing source and is classified in Level 2 of the fair value hierarchy.

Registration of USD Notes and Subsequent Exchange Offer

In October 2018, the Company, as issuer of the USD notes, filed a Form F-4 with the SEC, to register notes, referred to as Registered Notes, under the Securities Act of 1933, referred to as the 1933 Act. The Registered Notes contained terms and conditions substantially identical to the $17.25 billion in privately placed USD notes, referred to as the Exchange Notes, issued in August 2017. On October 22, 2018, upon the Form F-4 being declared effective by the SEC, the Company launched an exchange offer to exchange any and all (to the extent held by eligible holders) Exchange Notes for its Registered Notes. On November 20, 2018, the Company completed the exchange offer, and of the total $17.25 billion in Exchange Notes outstanding, approximately $17.2 billion, or 99.7%, were exchanged for Registered Notes. Each series of Registered Notes is substantially identical to the Exchange Notes of the corresponding series, except that the Registered Notes are registered under the 1933 Act and do not bear any legends restricting transfer, and except that the registration rights pertaining to the Exchange Notes do not apply to the Registered Notes.

The Company remains the principal obligor of the remaining $47 million in Exchange Notes that were not tendered in the exchange offer. Both the Registered Notes and the Exchange Notes have been guaranteed by BAT and RAI.

(3) Income Taxes

The components of the provision for income taxes for the years ended December 31 were as follows:

	2019	2018
Current:		
Federal	$ 42,883	$ 10,143
State and other	—	—
	42,883	10,143
Deferred:		
Federal	(1,136)	2,662
State and other	—	—
	(1,136)	2,662
Provision for income taxes	$ 41,747	$ 12,805

Significant components of deferred tax assets and liabilities for the years ended December 31 included the following:

	2019	2018
Deferred tax assets:		
Losses on derivatives	$ 161,770	$ 99,589
Unrealized foreign exchange losses	(18,368)	(13,215)
Other	420	—
Net deferred tax asset	$ 143,822	$ 86,374

As of December 31, 2019 and 2018, the Company has no valuation allowance recorded against deferred tax assets.

The differences between the provision for income taxes and income taxes computed at statutory U.S. federal income tax rates for the years ended December 31 were as follows:

	2019	2018
Income taxes computed at the statutory U.S. federal income tax rate	$ 41,747	$ 4,845
BEAT	—	7,960
Provision for (benefit from) income taxes	$ 41,747	$ 12,805
Effective tax rate	21.0%	55.5%

The effective tax rate for 2018 was impacted by the BEAT provisions of the Tax Reform act. Excluding the impact of the BEAT in 2018, the effective tax rate was 21.0%.

The Company recognized a deferred tax benefit of $56.3 million and $26.2 million in accumulated other comprehensive loss at December 31, 2019 and 2018. In 2019, the deferred income tax benefit related to the loss from the change in the fair value of the forward starting pay-fix interest rate swaps entered into in October 2018 and the forward starting floating-to-fixed interest rate swaps entered into in February 2019, less the amortization of the starting pay-fix interest rate swaps that settled during September 2019. In 2018, the deferred income tax benefit related to the loss from the change in the fair value of the forward starting pay-fix interest rate swaps entered into in October 2018.

All of the derivative transactions, as discussed in note 4, with exception of the Foreign Currency Forward Contracts have been properly identified as hedging transactions for U.S. federal income tax purposes and are therefore being accounted for as hedging transactions for U.S. federal income tax purposes under the relevant sections of the Internal Revenue Code and underlying regulations.

The Company is included in the consolidated United States federal income tax return of BHI since December 7, 2016 when BHI became its sole shareholder in the transaction discussed in note 1. For state income tax purposes, the Company's results are included in 28 combined state income tax returns that include members of the consolidated United States federal income tax return of BHI. For financial reporting purposes, the company's current and deferred income taxes are calculated using the separate return method under ASC 740-10-30-27. All current and deferred tax expense and current and deferred tax liabilities are calculated as if the Company files separate federal and state income tax returns that exclude the income, deductions and tax attributes of BHI.

(4) Related Party Transactions

As a U.S. finance company, the Company enters into transactions with multiple BAT affiliates, including its direct parent, BHI. The following is a summary of balances and transactions with BAT and its affiliates.

Loan Receivable

On August 15, 2017 and August 16, 2017, the Company issued approximately $20 billion in notes (see note 2). The proceeds from those notes were loaned to BHI in a series of term loans that consisted of eleven separate term loans denominated in U.S. dollars with amounts and maturity dates that matched the corresponding notes issued by the Company. BHI paid the Company $83.9 million in upfront fees related to the loans and the Company is amortizing those fees over the life of the respective notes using the effective interest method. Related to the BHI loans receivable, the Company recognized $715.5 million and $707.0 million in interest income in 2019 and 2018, respectively, and had $236.8 million and $239.6 million accrued as interest receivable at December 31, 2019 and December 31, 2018, respectively.

In September 2018, the Company entered into a one-year term loan agreement with RAI for a principal amount of $1.2 billion. The term loan bore a floating interest rate based on three-month U.S. dollar LIBOR plus a margin of 1.14%. Interest was payable on the term loan quarterly. On May 31, 2019, the term loan to RAI was extended to May 1, 2020 and an additional $1.2 billion was advanced to RAI under this agreement. The Company also entered into a term loan agreement with R. J. Reynolds Tobacco Company, an indirect subsidiary of RAI, on May 31, 2019 for a principal amount of $82 million due on May 1, 2020. Each respective loan bears interest of three-month U.S. dollar LIBOR plus a margin of 1.36%. The terms of the term loan to R. J. Reynolds Tobacco Company are the same as the RAI loan agreement.

On December 20, 2019, the Company entered into separate installment term loans with BHI and RAI, respectively, with each effective on January 2, 2020 and having a maturity date of September 2049. The installment term loan with BHI was for $20.0 billion and effectively refinanced, in total, the eleven separate term loans made to BHI in August 2017 into a single term loan. The installment term loan made to RAI was for $1.25 billion. Each installment term loan bears an interest rate of 3.582% and is payable semi-annually. The interest rate for each respective term loan may be adjusted from time to time to reflect changes to the Company's weighted average cost of borrowing as defined in the agreements.

Installments under the new term loans are due and payable per the terms of an installment schedule in each respective agreement. Not less than ten business days prior to the installment due date, BHI and RAI have the ability to request the payable date of a term loan installment be extended. The Company, in its sole discretion, may accept or decline the extension request.

On December 30, 2019, RAI provided a written notice to the Company of its intent to prepay $1.25 billion of its $2.4 billion outstanding term loan. RAI subsequently made the prepayment on January 2, 2020.

On July 19, 2019, the Company entered into a $5.5 million three-year amortizing term loan agreement, due July 2022, with VapeWild Holdings, LLC, an indirect subsidiary of RAI. This term loan is drawable in one or more tranches and bears a floating interest rate based on the three-month U.S. dollar LIBOR plus a margin of 2.12%, per annum. The total amount outstanding at December 31, 2019 was $1.6 million, net of a $2 million reserve related to collectability.

Related to these total RAI loan receivables, the Company recognized $71.4 million and $11.2 million in interest income in 2019 and 2018, respectively, and had $13.8 million and $0.7 million accrued as interest receivable at December 31, 2019 and December 31, 2018, respectively.

Details of the loans receivable at carrying value is as follows at December 31, 2018:

	2018
Fixed rate loans:	
BHI	
2.417% note due 08/14/2020	$ 2,250,000
2.937% note due 08/15/2022	2,250,000
3.219% note due 11/16/2023	880,755
3.385% note due 08/15/2024	2,500,000
3.372% note due 08/15/2025	584,735
3.840% note due 08/15/2027	3,500,000
4.462% note due 08/15/2037	2,500,000
4.699% note due 08/15/2047	2,500,000
Variable rate loans:	
BHI	
Three-month LIBOR plus 0.59% note due 08/14/2020	1,000,000
Three-month LIBOR plus 0.87% note due 08/16/2021	1,288,969
Three-month LIBOR plus 0.88% note due 08/15/2022	750,000
RAI	
Three-month LIBOR plus 1.14% note due 09/27/2019	1,200,000
Total principal	21,204,459
Facility commitment fees	(71,923)
Total loan receivable from affiliate	$ 21,132,536

Details of the loans receivable at carrying value is as follows at December 31, 2019:

	2019
BHI	
3.582% installment term note due 09/06/2049	20,004,459
RAI	
Three-month LIBOR plus 1.14% note due 05/01/2020	1,150,000
3.582% installment term note due 09/06/2049	1,250,000
RJRT	
Three-month LIBOR plus 1.36% note due 05/01/2020	82,000
VapeWild	
Three-month LIBOR plus 2.12% note due 07/19/2022	1,580
Total principal	22,488,039
BHI Facility commitment fees	(62,938)
Total loan receivable from affiliates	$ 22,425,101

As of December 31, 2019, the maturities of these loans receivable from affiliates, excluding facility commitment fees, were as follows:

Year	Total
2020	$ 2,232,000
2021	1,288,969
2022	3,001,580
2023	880,755
2024	3,500,000
2025 and thereafter	11,584,735
	$ 22,488,039

Due from (to) affiliates

As of July 1, 2019, the Company's excess cash balances are swept into a cash pooling arrangement managed by BATOF, previously managed by BATIF. The Company's interest in the cash pooling structure is represented by its balances in its IHC account. Excess cash advances on deposit at BATOF are payable to the Company on demand and bear interest at a rate of 0.275% under LIBOR. If necessary, the Company has the ability to overdraft its IHC account at BATOF up to $900.0 million in the aggregate. Overdraft positions bear interest at 0.75% over LIBOR. At December 31, 2019, the Company had advanced $1.6 billion on its IHC account with BATOF and at December 31, 2018, the Company had advanced $913.2 million on its IHC account with BATIF. These amounts are classified as Due from affiliates in the Company's balance sheet.

The Company provides cash management services to RAI. On July 25, 2017, upon competion of the RAI merger, the Company entered into a zero balance account credit agreement and revolving note with RAI. Under the zero balance credit agreement, RAI's cash balances were transferred daily to the Company. These excess cash advances were payable to RAI on demand and bore interest at a rate of 0.275% under one-month LIBOR. Under the credit agreement and revolving note, if RAI was not in a position where it had advances outstanding with the Company, RAI was permitted to borrow, on a revolving basis, up to $900 million at any one time from the Company. Borrowings bore interest at a rate of 0.75% over one-month LIBOR. The zero balance account credit agreement and revolving note were terminated in November 2018.

In September 2018, the Company entered into separate IHC agreements with RAI and certain of its subsidiaries which replaced the zero balance account credit agreement and revolving note. Under the terms of these IHC agreements, excess daily cash balances in RAI and its subsidiaries bank accounts are advanced to the Company. Excess cash balances on deposit with the Company are payable to each respective entity on demand and bear interest at a rate of 0.275% under the overnight LIBOR rate. Certain IHC agreements provide a separate overdraft facility that provides for advances that may not exceed the overdraft limits set forth in each respective agreement. Overdraft advances bear interest at a rate of 0.75% over the overnight LIBOR rate. Any outstanding advances and interest are due and payable no later than the maturity date of May 1, 2020. The net amount on deposit in the IHC accounts for the benefit of RAI and its subsidiaries was $3.0 billion at December 31, 2019 and $2.2 billion at December 31, 2018 and is classified as Due to affiliates in the Company's balance sheet.

In 2019 and 2018, the Company recognized $56.4 million and $27.2 million, respectively, in interest expense and $25.7 million and $20.3 million, respectively, in interest income related to IHC accounts.

Guarantee Fees

The Company entered into an agreement with BAT whereby BAT would provide an unconditional guarantee of the Company's notes issued in August 2017 and September 2019 in exchange for a guarantee fee based on a fee rate and the nominal amount of the notes issued. At December 31, 2019 and December 31, 2018, the Company has a payable to BAT for $38.7 million and $31.9 million, respectively. In 2019 and 2018, the Company recognized guarantee fee expense of $196.0 million and $191.3 million, respectively.

In August 2017, upon lending the proceeds from the note issuance to BHI, BHI agreed to reimburse the Company for the guarantee fees in the same amount as the Company was paying BAT. In December 2019, RAI agreed to reimburse the Company for the guarantee fees on a proportionate share of the notes benefitting RAI. Accordingly, at December 31, 2019 and 2018, the Company recognized a reimbursement receivable for $38.7 million and $31.9 million, respectively, for guarantee fees. In addition, in 2019 and 2018, the Company has recognized guarantee fee income of $196.0 million and $191.3 million, respectively.

Revolving Credit Facility with Affiliate

On December 7, 2016, the Company entered into a $50 million Uncommitted Revolving Credit Facility, referred to as the RCF, with Brown & Williamson Holdings, Inc., referred to as BWH, a BHI affiliate, that matured on December 7, 2018. The RCF agreement contained standard terms and conditions including, at the option of the borrower, the ability to prepay advances and to select a variable interest rate based on a one-month, three-month or six-month USD LIBOR, plus 0.425%. No advances were made under the RCF in 2018 prior to its maturity.

Derivatives

(a) Cross-Currency Interest Rate Swaps

In order to manage currency fluctuation risk on the EUR and GBP denominated notes, the Company entered into cross currency interest rate swaps pursuant to which it swapped the EUR and GBP denominated principal amounts bearing fixed or floating interest rates, as applicable, for a USD denominated principal amount bearing a corresponding fixed or floating interest rate, as applicable. The objective of these cross-currency swaps is to reduce volatility of cash flows associated with the underlying debt from changes in foreign currency exchange rates. Under the terms of these contracts, the Company will make interest payments in U.S dollars and receive interest in British pounds sterling or euros, as applicable. Upon the maturity of these contracts, the Company will pay the principal amount of the loans in U.S dollars and receive British pounds sterling or euros, as applicable. BATIF is the counterparty in these contracts. The key terms for the cross-currency swaps were as follows (USD/EUR/GBP amounts in thousands):

Cross currency swaps	Number of Contracts	Inception Date	Maturity Date	Pay Notional Amount	Interest Rate (Pay USD)	Receive Notional Amount	Interest Rate (Receive EUR/GBP)
EUR-USD	5	8/16/2017	8/16/2021	$ 1,288,969	3M Libor+86.7 bp	€ 1,100,000	3M Euribor+50 bp
EUR-USD	4	8/16/2017	11/16/2023	880,755	3.220%	€ 750,000	1.125%
GBP-USD	3	8/16/2017	8/15/2025	584,735	3.370%	£450,000	2.125%
				$ 2,754,459			

The Company recognized a net liability of $103.1 million plus associated accrued interest payable of $9.3 million at December 31, 2019 for the cross-currency swaps. At December 31, 2018, the Company had recognized a net liability of $52.6 million plus associated accrued interest payable of $10.9 million.

The change in fair value of the cross-currency interest rate swaps was a loss of $50.5 million in 2019 and a loss of $144.5 million in 2018 and is reported in Net loss on derivatives in the accompanying statements of operations. In addition, the Company recognized net interest expense of $68.7 million and $64.3 million, respectively, in 2019 and 2018 related to the cross-currency swaps.

(b) Foreign Currency Forward Contracts

The Company will enter into foreign currency exchange contracts with BATIF to minimize the financial impact from exposure to changes in the exchange rates for GBP and EUR on certain liabilities denominated in those currencies. At December 31, 2019 and December 31, 2018, the Company had a liability recorded of $224,000 and $31,000, respectively, for the fair value of forward exchange contracts. In 2019 and 2018, the Company recognized $99,000 and $753,000, respectively, as income related to foreign currency forward contracts recorded in Net loss on derivatives. Changes in the fair value are recognized as either income or expense, as applicable, as derivative (gains) losses, net in the accompanying statements of operations.

In addition, the Company has entered into offsetting immaterial foreign currency exchange contracts with BATIF and RAI Services Company, a subsidiary of RAI, related to certain liabilities denominated in GBP.

(c) Forward Starting Interest Rate Swaps and Treasury Locks

In October 2018, in anticipation of highly probable future note issuances to be used to refinance certain note maturities, the Company entered into forward starting pay-fix interest rate swaps, referred to as forward swaps, for a notional amount of $3.4 billion to lock in the five and ten year forward swap rates. The forward swaps anticipated note issuances in 2019 and 2020. The counterparty exposure under these forward swaps is with BATIF with BATIF entering into identical swaps with external banks. The Company is utilizing cash flow hedge accounting for these forward swaps.

In August 2019, the Company terminated forward swaps with a notional amount of $1.35 billion associated with the anticipated issuance of the notes in September 2019 and incurred a loss of $158.6 million, before tax, which the Company settled with a cash payment. Concurrent with the termination of the forward swaps, the Company entered into treasury locks with a notional amount of $1.35 billion that the Company subsequently terminated on the date of the note issuance at a loss of $25.9 million before tax and was settled with a cash payment. These losses were recognized in accumulated other comprehensive loss and, accordingly, will be amortized to interest expense over the life of the related debt. In 2019, the Company amortized $6.1 million to Interest expense.

For the forward swaps associated with an anticipated debt issuance in 2020, at December 31, 2019, the Company had recognized a liability of $211.9 million for the fair value of the forward swaps with a corresponding balance for the same amount, before tax, in accumulated other comprehensive loss. If the highly probably future note issuances occur on the anticipated issue dates or within the following two months, the amount recorded in accumulated other comprehensive loss that is considered to be effective shall be reclassified as interest expense in the statement of operations in the same periods during which the interest expense on the anticipated debt is recognized. If the forecast transaction does not occur within the specified time period, any amounts in accumulated other comprehensive loss will be reclassified as interest expense in the statement of operations immediately.

At December 31, 2018, the Company had recognized a liability of $125.0 million for the fair value of the forward swaps with a corresponding balance for the same amount, before tax, in accumulated other comprehensive loss.

(d) Floating to Fixed Interest Rate Swaps

In February 2019, the Company entered into three forward starting, floating to fixed interest rate swaps with BATIF as the counterparty. These swaps cover an aggregate notional amount of approximately $3.0 billion with fixed rates ranging from 3.22% to 3.53% and are effective from May 2019 to February 2020. The Company is using cash flow hedge accounting for these floating to fixed interest rate swaps. At December 31, 2019, the Company had recognized a net liability of $2.8 million plus associated accrued interest payable of $29.7 million for the fair value of the forward swaps. A corresponding balance for the net liability, before tax, was recorded in accumulated other comprehensive loss. In addition, the Company recognized interest expense of $7.6 million in 2019.

Other income – affiliates

Pursuant to an agreement with BHI, certain expenses of the Company are reimbursed by BHI related to the financing transactions that occurred in 2017. On December 20, 2019, the Company entered into a similar agreement with BHI and RAI related to the financing transactions that occurred in 2019. In 2019 and 2018, the Company recognized $215.9 million and $8.9 million, respectively, as other income from affiliates for these reimbursements as follows (dollars in thousands):

	2019	2018
Losses on debt pre-hedges	$ 184,505	$ —
Fees related to early extinguishment of debt	6,457	—
Debt issuance fees	16,000	—
Other	8,985	8,896
	$ 215,947	$ 8,896

General and administrative services

The Company had no direct employees in 2019 and 2018. The Company has a services agreement with Louisville Corporate Services Inc., a direct subsidiary of BHI, for the provision of general and adminstrative services to the Company consisting primarily of administrative, accounting, income tax and other support services.

(5) Fair Value

The Company records its derivative contracts at their fair value as of the balance sheet date. All derivatives held by the Company at December 31, 2019 and December 31, 2018, are categorized in Level 2 of the fair value hierarchy. Level 2 financial instruments are not traded in an active market but rather the fair values are determined based on market data, primarily yield curves and exchange rates, to calculate the present value of all estimated flows associated with each derivative contract at the balance sheet date. In the absence of sufficient market data, fair values would be based on the quoted market price of similar derivatives.

(6) Shareholder's Equity

Return of Capital to BHI

In July 2018, the Board of Directors for the Company approved a cash distribution of $305.5 million in the form of a return of capital be made to BHI.

Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss, net of $56.3 million in tax benefit in 2019, were as follows:

	Forward Starting Pay-Fix Interest Rate Swaps	Floating to Fixed Interest Rate Swaps	Pre-hedge Settlement	Total
Balance at December 31, 2018	$ (98,727)	$ -	$ -	$ (98,727)
Net current period other comprehensive loss	(68,689)	(2,240)	(140,913)	(211,842)
Balance at December 31, 2019	$ (167,416)	$ (2,240)	$ (140,913)	$ (310,569)

(7) Contingent Liabilities

On December 9, 2011, the Company ceased to be a party to the EMTN Program under which the issuers, that also include BATIF, B.A.T. Netherlands Finance B.V. and British American Tobacco Holdings (The Netherlands) B.V., can from time to time issue notes in amounts not to exceed the EMTN Program limits or its equivalent in other currencies. The payments of all amounts in respect of any notes issued under the EMTN Program prior to December 9, 2011 are unconditionally and irrevocably guaranteed by BAT, the Company and each of the other issuers (except where it is the relevant issuer).

On May 31, 2017, the EMTN Program was amended and restated to increase the size of the EMTN Program from £15.0 billion to £25.0 billion and to add the Company as an issuer and a guarantor. At December 31, 2019 and December 31, 2018, the Company had issued $2.7 billion and $2.7 billion, respectively, equivalent of notes under the EMTN Program at the related spot rate for the respective currency at the respective measurement date.

Effective February 13, 2018, the Company became an additional guarantor of the notes issued pursuant to the EMTN Program that it was not already a guarantor of during the period since it ceased participation. With the additional guarantees in place, as of December 31, 2019 and December 31, 2018, the Company was a guarantor in the amount of approximately $14.4 billion and $16.6 billion, respectively, plus accrued interest which represents the maximum potential exposure (at applicable year-end exchange rates) had the relevant issuers defaulted.

The Company's guarantee of the notes issued under the EMTN is unconditional and irrevocable, joint and several with the other guarantors and is triggered when the issuer of the EMTN securities defaults on its payment obligations. If the Company is required by law to withhold any U.S. taxes (or taxes of any of its political subdivisions) from payments it makes under its guarantee, the Company is required to pay additional amounts so that security holders receive the same payment they would receive absent such withholding, subject to exceptions. The Company does not maintain a guarantee liability related to its guarantees with respect to the EMTN Program.