

BAA (SP) Limited

For the year ended  
31 December 2008

Registered number: 06458621

# **BAA (SP) Limited**

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# **BAA (SP) Limited**

## **Officers and Professional Advisors**

### **Directors**

L Sanchez Salmeron (appointed 20 December 2007)  
J Leo (appointed 20 December 2007)  
S J K Nelson (appointed 20 December 2007 and resigned 31 March 2008)

### **Secretary**

Shu-Mei Ooi (appointed 28 November 2008)  
S Welch (appointed 20 December 2007 and resigned 28 November 2008)

### **Registered Office**

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London  
SW1V 1LQ

### **Independent Auditors**

PricewaterhouseCoopers LLP  
Chartered Accountants and Registered Auditors  
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WC2N 6RH

### **Bankers**

Royal Bank of Scotland  
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# BAA (SP) Limited

## Business Review

BAA (SP) Limited ('BAA SP' or 'the Group') is the holding company for the Security Group that owns the Designated Airports comprising the UK Regulated Airports of Heathrow, Gatwick and Stansted and operates the Heathrow Express rail between Heathrow and Paddington, London. BAA (SP) Limited is also the holding company of BAA Funding Limited, which is the company that is the bond issuer for the Security Group. BAA (SP) Limited is an indirect subsidiary of BAA Limited (formerly Airports Development and Investment Limited) ('BAA').

The Company was incorporated on 20 December 2007 and on 31 January 2008, the Company entered into a sale and purchase agreement to purchase the entire issued capital of BAA (AH) Limited from BAA. At the time of this transaction, BAA (AH) Limited was the owner of the Designated Airports described above.

The financial statements of BAA (SP) Limited have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice ('UK GAAP'). The accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements. In order to present a true and fair view of the BAA (SP) Limited Group the abovementioned sale and purchase transaction or group reorganisation, has been merger accounted. Comparative financial information has been provided as if the Group had always existed in its current form.

On 17 September 2008, BAA announced plans to sell Gatwick airport given the Competition Commission's ('CC') provisional findings in its investigation into BAA Limited Group ownership of UK airports. The sale process is progressing on schedule with initial bids received during January 2009. The process is expected to be completed in the first half of 2009. Under UK GAAP, Gatwick is described as a continuing operation as the sale process is not expected to be completed within three months of the year end, as is required for classifying an operation as discontinued.

On 7 August 2008, Heathrow Airport Limited ('HAL') acquired from BAA Airports Limited, a fellow group company, ownership of Heathrow Express Operating Company Limited ('HEX'). As this transaction is not deemed to be part of the group reorganisation process referred to above, the Group has applied acquisition accounting in relation to this transaction.

This business review is presented under three sections:

**Management review and outlook** – overview of the year ended 31 December 2008, along with the key factors likely to impact the Group in 2009.

**Financial performance** – presentation and explanation of the key drivers behind the adjusted financial performance reported for the year ended 31 December 2008 and analysis of the financial position of the Group as at that date. The Group's accounting and reporting policies and procedures are also considered.

**Risk management** – outline of the Group's approach to risk management, sources of assurance and highlight of the key business risks identified by the Group Executive Committee.

## Management review and outlook

### Review of 2008

#### *Transforming BAA SP's airports*

BAA SP's strategy is to deliver sustained improvements in passengers' experience and airlines' operations through a combination of substantial investment in modern airport facilities and improved service standards. It also intends to deliver further investment targeted at enhancing capacity to meet the expected continued growth in air travel.

This strategy will ensure that its airports provide customers with superior facilities relative to competitors in the UK and elsewhere, particularly in Europe, encouraging greater utilisation of BAA SP's airports by passengers and supporting the Group's long term growth ambitions.

# BAA (SP) Limited

## Management review and outlook (continued)

### Review of 2008 (continued)

#### *Developing modern airport facilities*

In 2008, the most significant development in BAA SP's airport facilities was the opening of Terminal 5 at Heathrow, the first new terminal at the airport for over 20 years. Despite the difficulties around its opening, Terminal 5 is now providing airlines and passengers with a world-class service. Independent surveys rank it as the best airport terminal facility in Europe in overall passenger satisfaction.

The opening of Terminal 5 has also provided the spare capacity at Heathrow to enable the Group to invest in improving service across the whole airport in the next few years. Over the period to 31 March 2013, BAA expects to invest a further £4.3 billion (at 2007/08 prices) at Heathrow, with the most significant investment relating to construction of the new Terminal 2A and its satellite Terminal 2B, which will replace the existing Terminal 2 and deliver facilities of equivalent standard to Terminal 5. Terminals 3 and 4 will also be extensively refurbished to raise standards to similar levels to Terminal 5. There will also be substantial investment in improving baggage connections across the airports. This investment programme has been agreed with airlines and the CAA.

This investment programme will strengthen Heathrow's position as a leading global hub airport and on completion will result in:

- 70% of Heathrow's passengers travelling through new or recently constructed terminals with the remaining 30% of passengers using significantly refurbished terminals
- Joint location of members of the major global airline alliances, providing a unique platform for BAA SP's airline customers to enhance efficiency and profitability

The recent confirmation by the Secretary of State for Transport of the UK government's support for the development of a third runway with additional terminal facilities is a key step towards ensuring Heathrow plays a key role in meeting long term aviation demand in the UK and the development of the wider UK economy.

BAA SP is committed to transforming other airports in its portfolio. For example, in 2008 £99 million was invested at Stansted which included in particular the completion of the extension to its arrivals area to provide additional capacity and enhanced retail layout. Plans for the longer term growth of Stansted were supported by approval in October 2008 by the Secretary of State for Transport and Communities and Local Government to increase passenger traffic levels at the airport, using existing facilities, from 25 million to 35 million per annum. In addition, following the submission of a planning application in 2008, a public inquiry relating to a second runway and terminal at the airport, that would enable growth beyond 35 million passengers per annum, is due to commence shortly.

#### *Service standards*

Consistent delivery of high service standards is a key strategic priority for BAA SP, underpinning the experience of passengers and airlines and supporting the Group's long term growth ambitions. Major service improvements in 2008 included the impact of Terminal 5's commissioning and occupation and the benefit of operating at Heathrow and Gatwick under the strengthened service quality rebate schemes applying from 1 April 2008.

Following the initial difficulties immediately after its opening in March 2008, service at Terminal 5 has improved substantially with overall passenger satisfaction, as measured by Airline Council International's Airport Service Quality ('ASQ') survey for the third quarter of 2008, rated amongst the best European airports terminal facilities. In the same survey, Heathrow overall has moved above several competing major European hub airports in overall passenger satisfaction compared to its position a year earlier. Gatwick's rating has also improved relative to the prior year.

The service quality rebate schemes applying at Heathrow and Gatwick from 1 April 2008 were strengthened to include new elements, higher standards for existing parts of the schemes, increased penalties for not achieving standards and bonuses where out-performance is achieved consistently across an airport.

Further evidence of improving service standards can be seen from the rapid reduction in rebates paid by Heathrow and Gatwick following the introduction of these stricter schemes. The level of rebates (net of bonuses earned) in the nine months to 31 December 2008 was £7.8 million with the level of rebates declining from £4.7 million in the 3 months to 30 June 2008 to just £2.3 million and £0.8 million in the two subsequent quarterly periods.

One of the most visible service standards relates to security queuing times. These have improved significantly and security queues for direct passengers were below five minutes for 98.6% and 95.2% of the time at Heathrow and Gatwick respectively in the nine months to 31 December 2008 compared with the required 95.0% service standard.

# BAA (SP) Limited

## Management review and outlook (continued)

### Review of 2008 (continued)

#### Passenger traffic trends

Trends in passenger traffic for 2008 across all three of BAA SP's airports as well as by market served for its airports are compared against performance in 2007 in the table below.

	Year ended 31 December 2008	Year ended 31 December 2007	Change (%) <sup>1</sup>
<b>Passengers by airport</b>			
Heathrow <sup>2</sup>	66.9	67.9	(1.4)
Gatwick	34.2	35.2	(2.8)
Stansted	22.3	23.8	(6.0)
<b>Total passengers<sup>1</sup></b>	<b>123.4</b>	<b>126.8</b>	<b>(2.6)</b>
<b>Passengers by market served</b>			
UK	11.7	12.3	(5.6)
Europe	68.5	70.5	(2.9)
Long haul	43.3	43.9	(1.5)
<b>Total passengers<sup>1</sup></b>	<b>123.4</b>	<b>126.8</b>	<b>(2.6)</b>

(1) These numbers have been calculated on un-rounded numbers.

(2) These numbers do not include rail passengers of Heathrow Express which increased by 0.3% to 5.42 million passengers during the year (2007: 5.40 million)

Traffic performance across all BAA SP's airports softened as the year progressed reflecting the increasingly difficult global economic environment, with performance earlier in the year also affected by the aviation industry's need to adjust to surging fuel prices. Across the European aviation industry, long haul traffic maintained its recent trend of outperforming other market segments and continued growing despite the difficult market conditions. BAA SP benefited from this trend particularly at Heathrow, where long haul traffic increased, reflecting its position as a major global hub airport for long haul services. This is also beneficial for BAA SP's financial performance as long haul traffic generates higher levels of aeronautical and retail income. However, other market segments were more affected, including the charter market, domestic and other short haul services.

At Heathrow, BAA SP's largest airport, long haul passenger numbers increased 3.5% to 35.0 million (2007: 33.8 million), reflecting both the transfer of some US traffic from Gatwick due to the EU-US Open Skies Agreement and growth on other long haul routes. Transfer traffic increased to 36% of Heathrow's total traffic (2007: 34%). Long haul growth partially offset weaker domestic and other short haul services with Heathrow's total passenger traffic declining 1.4% to 66.9 million (2007: 67.9 million).

Gatwick saw passenger numbers decline 2.8% to 34.2 million (2007: 35.2 million) reflecting the loss, starting in April 2008, of approximately 40% of its US services to Heathrow. It also lost traffic later in the year as a result of the collapse of three carriers (XL Airways, Zoom Airlines and Sterling Airlines). These losses were in part offset by a surge in new services to Ireland and the take up of vacated slots by existing low cost airlines. At Stansted, passenger numbers declined 6.0% to 22.3 million (2007: 23.8 million) due to major airlines reducing operations in the face of weakening demand and high fuel prices and the collapse of carriers such as Maxjet and Eos Airlines.

Across BAA SP's airports, long haul traffic declined just 1.5% to 43.3 million passengers (2007: 43.9 million), with North Atlantic routes seeing a 1.7% reduction and other long haul destinations performing slightly better, with a 1.3% decline. The strongest growing regional markets were the Middle East and South America which were up 4.0% and 5.1% respectively on 2007. European passenger traffic declined 2.9% to 68.5 million (2007: 70.5 million) due particularly to weakness in the charter market. Domestic traffic declined 5.6% to 11.7 million passengers (2007: 12.3 million).

# BAA (SP) Limited

## Management review and outlook (continued)

### Review of 2008 (continued)

#### *Retail activities*

BAA SP's retail activities have proved resilient to the worsening economic environment reflecting a number of factors specific to BAA SP's airports.

These include the significant recent expansion and upgrade of BAA SP's retail facilities. In particular, Heathrow Terminal 5 has 23,000m<sup>2</sup> of the highest quality retail space at Heathrow out of the airport's total of 66,000m<sup>2</sup>. Terminal 5 has only welcomed its full complement of passengers since October 2008 when British Airways completed its planned moves from other terminals. Elsewhere at Heathrow, the launch of Terminal 1's common user lounge in June 2008 (providing domestic passengers with access to the same retail offer as international passengers) also helped to support retail performance. Other recent increases and improvements to retail facilities across BAA SP's airports has resulted from the completion of the South Terminal departure lounge extension at Gatwick and the new arrivals area at Stansted.

The principal drivers of retail spend in BAA SP's airports are time spent in departure lounge areas and passenger propensity to spend. Improvements to the end-to-end passenger experience (including security queuing) have led to a better propensity to spend and recent exchange rate movements have increased the attractiveness of product pricing to non-UK based passengers. The change in the passenger mix towards more long haul passengers, who tend to have earlier check in times and combined with more efficient check in procedures, giving more time in lounges have contributed to the increased retail spend. These factors, taken with the significant improvements to the catering and retail offer, led by Terminal 5, have led to increases in participation (proportion who buy) and spend per passenger amongst both UK and foreign passengers.

#### *Regulatory developments*

##### *Competition Commission inquiry into BAA Limited Group's ownership of UK airports*

On 17 December 2008, the Competition Commission ('CC') issued its Provisional Decision on Remedies in relation to its ongoing investigation of BAA Limited Group's ownership of UK airports, which includes BAA SP's airports. These include structural and behavioural remedies as well as recommendations on regulatory and policy matters for consideration by other governmental bodies.

The provisional structural remedies include the disposal of Gatwick and Stansted to different owners. These remedies are subject to further consultation on the timing of the Stansted disposal particularly in relation to the forthcoming public inquiry concerning its potential second runway.

Suggested behavioural remedies include strengthening consultation processes and provisions on non-discrimination and quality of service at Heathrow. The CC has also recommended that the Department for Transport ('DfT') consider adopting a licence based regime of economic regulation of UK airports and allowing terminals to be separately owned from runways.

The CC is expected to publish its final report, and the appropriate remedies, in March 2009. BAA will then have two months in which to decide to lodge a legal appeal.

##### *Gatwick disposal*

Given the CC's findings earlier in its investigation, on 17 September 2008, BAA announced plans to sell Gatwick airport. The sale process is progressing on schedule with initial bids received during January 2009. The process is expected to be completed in the first half of 2009. The regulatory asset base of Gatwick airport at 31 December 2008 was £1,578 million and it is forecast to be £1,624 million at 30 June 2009.

# BAA (SP) Limited

## Management review and outlook (continued)

### Review of 2008 (continued)

*Department for Transport ('DfT') review of UK airport economic regulation*

The DfT is currently conducting a review of the economic regulation of all UK airports with a 3 month formal consultation process likely to commence shortly. This is expected to be followed by the issue of the DfT's final decision on the new regulatory proposals in the autumn of 2009. Implementation of the final proposals will require changes in law which could occur as early as mid-2010 although this timing will be subject to parliamentary time being found to enact the necessary legislative changes.

The DfT has indicated that the key policy objectives of the review will include improving the passenger experience (particularly a stronger focus on putting the passenger first across the whole journey). It will also seek to encourage appropriate and timely investment in additional capacity to help deliver economic growth in line with wider Government policy and address the wider environmental impacts of aviation and airport development.

It is anticipated that the regulatory review will result in the introduction of a licensing regime similar to that operating in many regulated industries. Other key concepts that are expected to feature in the consultation are the introduction of a regime that more explicitly supports the financial profile of airport operators and of a special administration regime. These concepts are common in other regulated industries.

Whilst there may be a change in law prior to the end of the price control periods in 2013 for Heathrow and Gatwick and 2014 for Stansted, the DfT has made clear that the tariff arrangements for these periods will not be re-opened.

### *Aeronautical charges at Heathrow and Gatwick for 5 years to 31 March 2013 ('fifth quinquennium' or 'Q5')*

In March 2008, the Civil Aviation Authority ('CAA') published its price control review for both Heathrow and Gatwick for the five years to 31 March 2013 ('quinquennium 5'). In its proposals, a pre-tax real cost of capital of 6.2% at Heathrow and 6.5% at Gatwick was assumed. It set the maximum growth in aeronautical charges per passenger for Heathrow at RPI+23.5% for the year to 31 March 2009 and RPI+7.5% per annum for the remainder of Q5. For Gatwick, the corresponding figures are RPI+21.0% and RPI+2.0% per annum respectively.

The resulting impact on the maximum allowable yield per passenger (in 2007/08 prices) is as follows:

	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
Heathrow	£10.36	£12.80	£13.72	£14.76	£15.84	£16.99
Gatwick	£5.61	£6.79	£6.92	£7.06	£7.20	£7.34

The significant one-off increase in the aeronautical charges reflects the major capital programmes being undertaken by BAA SP at Heathrow and Gatwick in addition to the increased expenditure required to meet the new security regime. Further, between 2007/08 and 2008/09 this reflects a rebasing of tariffs to include costs previously charged to airlines by NATS for aerodrome navigation services and by BAA SP separately from the aeronautical charges for both baggage infrastructure services and fuel levy. The total amount included in the new tariffs for these services is £1.08 and £0.70 per passenger at Heathrow and Gatwick respectively.

The higher charges for Q5 are being phased in during the first regulatory year to 31 March 2009, meaning that in the year to 31 December 2008 the full benefit was not enjoyed.

### *Proposed aeronautical charges at Stansted for 5 years to 31 March 2014*

On 9 December 2008, following CC recommendations, the CAA issued final proposals, subject to a further round of consultation, on aeronautical charges to apply at Stansted Airport for the five year period to 31 March 2014. Key features of the CAA's proposals include a permitted real pre-tax return on capital of 7.1%. It has also recommended that maximum allowable aeronautical charges remain flat at £6.05 per passenger for 2 years and increase at RPI+1.63% after 2010/11.

The CAA's recommendations are based on a capital plan of approximately £90 million, in 2007/08 prices, primarily on Stansted's existing facilities over the 5 years to 31 March 2014 that has been agreed with Stansted's airline community.

Further, the CAA supports the need for Stansted Generation 2 ('SG2'), that involves the construction of a new terminal and runway. However, it has suggested a later opening date than currently planned. It has also indicated that in the event that circumstances change, such as planning approval being received during the five year period to 31 March 2014, it would be open to Stansted to seek approval to re-set the tariffs for the remainder of the quinquennium.

The CAA is expected to issue its final decision regarding pricing for Stansted's next quinquennium in the first half of March 2009.



# BAA (SP) Limited

## Management review and outlook (continued)

### Review of 2008 (continued)

#### *Approval for increased traffic at Stansted*

On 9 October 2008, BAA SP's planning application to increase the number of air transport movements ('ATMs') permitted at Stansted was approved by the Secretary of State for Transport and for Communities and Local Government. The new limit has been increased by 9.5% to 264,000 ATMs per year from 241,000. BAA expects this approval to allow annual passenger throughput to grow from around 25 million to around 35 million if all available ATMs are utilised by airlines operating at Stansted.

### Refinancing

In August 2008, BAA Limited completed a permanent refinancing of the acquisition financing originally put in place at the time of the Ferrovial-led consortium's acquisition of the former BAA Limited Group in 2006. Details of the refinancing, and the nominal amounts involved, are described below:

- A corporate reorganisation occurred to enable separate ownership and financing of the three London airports (the 'Designated Airports') of Heathrow, Gatwick and Stansted.
- The Designated Airports became indirect wholly-owned subsidiaries of BAA (SP) Limited, forming a sub-group in which a ring fenced investment grade long term financing platform was established.
- The financing established within this sub-group included £4.4 billion of drawn bank facilities ('Refinancing Facility'), £2.75 billion of capital expenditure and working capital facilities ('Initial Credit Facility'), £0.4 billion of drawn loan facilities from the European Investment Bank, and £4.5 billion of bonds assumed by BAA Funding Limited ('BAA Funding Limited Bonds') in exchange for bonds previously issued by BAA Airports Limited (formerly BAA Limited and prior to that, at the date of the issue of the bonds, the former BAA plc). BAA Funding Limited is the vehicle for future bond issuance (the 'Issuer').
- BAA (SP) Limited became a direct wholly-owned subsidiary of BAA (SH) Limited to which a subordinated debt facility of £1.566 billion (£1.966 billion prior to the refinancing) was migrated from BAA Limited (formerly Airport Development and Investment Limited). BAA (SH) Limited is itself an indirect wholly-owned subsidiary of BAA Limited and its ultimate parent company in the United Kingdom is FGP Topco Limited.

### Development since beginning of 2009

#### *Heathrow third runway*

On 15 January 2009, the Secretary of State for Transport confirmed the UK government's support for the addition of a third runway at Heathrow with additional terminal facilities. It is expected that this will allow maximum air transport movements at Heathrow to increase from 480,000 currently to 605,000 by around 2020 subject to achieving noise and air quality standards. The next step in the process for the potential development of the third runway and additional terminal facilities is to prepare appropriate plans with a view to obtaining the necessary planning permissions and other consents.

#### *2009 traffic trends*

In January 2009, BAA SP's total passenger traffic was 8.1 million, a fall of 5.9% compared to 8.6 million in January 2008. This performance continued the moderation in the rate of decline in monthly passenger numbers relative to the prior year seen in December 2008. Heathrow maintained its recent resilience with a 2.1% decline. In February 2009, passenger traffic versus 2008 will be impacted by both weather disruption early in the month and the fact that February 2008 contained 29 days.

# BAA (SP) Limited

## Management review and outlook (continued)

### Outlook for 2009

2009 is expected to be a challenging year with the economic environment expected to have a continued impact on passenger traffic. Despite the forecast fall in passenger numbers in 2009, BAA SP's financial performance is expected to improve relative to 2008 as it earns a return on the substantial agreed investments it continues to make in its airports on behalf of its airline customers. In particular, aeronautical charges per passenger at Heathrow, Gatwick and Stansted are expected to average over 10% higher than in 2008. Retail performance is expected to remain resilient, reflecting the full year benefits of recent significant retail space additions such as Terminal 5 and the common user lounge at Terminal 1 at Heathrow. In addition, actions have been identified to deliver further efficiencies and cost savings.

BAA SP Group expects to invest a total of £1.2 billion across its airports, assuming ownership of Gatwick for the first half of 2009 only.

In the coming weeks there are expected to be a number of regulatory developments of significance to BAA SP's future including:

- The Department for Transport publishing proposals for consultation on the future economic regulation of UK airports. Its final proposals are expected to be issued in autumn 2009
- The Competition Commission publishing its Report on Remedies relating to its investigation of BAA Limited Group ownership of UK airports
- The Civil Aviation Authority publishing its final price control determination for Stansted for the 5 years to 31 March 2014

The sale of Gatwick will be an important milestone in the development of the business during 2009 and is expected to be completed in the first half of the year.

# BAA (SP) Limited

## Financial performance

### Introduction

The following financial review, based on the consolidated financial statements of BAA (SP) Limited, provides commentary on performance of the Designated Airports during 2008. Whilst the Group represented by BAA (SP) Limited and its subsidiaries did not exist until 2008, its accounts have been prepared under UK GAAP including the adoption of merger accounting in relation to the group reorganisation that occurred in January 2008 and the refinancing completed in August 2008. This has enabled comparative financial information for 2007 to be provided as if the group always existed. Under UK GAAP, the Gatwick operations are included in the continuing business.

In order to provide a better understanding of the results of BAA (SP) Limited and its subsidiaries, the following business commentary is on the adjusted performance which excludes the impact of exceptional items.

### Statutory operating profit

Statutory operating profit fell by £71 million to £364 million (31 December 2007: £435 million).

### Basis of preparation of statutory results

Some of the significant events and programmes that are highlighted in this Business Review have particular impacts on the way in which the financial results have been presented. The main areas of impact are:

- Exceptional items (refer to Note 5) relating to:
  - Accumulated past service pension costs
  - Reorganisation costs - including 'Simplifying the Organisation' restructuring programme
  - Heathrow Terminals 1 and 2 accelerated depreciation
  - Heathrow Terminal 5 launch/operational readiness costs

### Summary of adjusted performance

	Year ended 31 December 2008	Year ended 31 December 2007	Change <sup>1</sup> %
Adjusted turnover (£ million)	2,292	1,976	16.0
Adjusted EBITDA <sup>2</sup> (£ million)	916	904	1.3
Adjusted operating profit <sup>3</sup> (£ million)	472	615	(23.3)
Passenger traffic (million)	123.4	126.8	(2.6)

<sup>1</sup> Percentage change calculated using un-rounded numbers.

<sup>2</sup> Adjusted EBITDA is earnings before interest, tax, depreciation, amortisation and exceptional items. Refer to Note 2 in notes to the financial statements for the reconciliation of adjusted EBITDA and statutory operating profit.

<sup>3</sup> Adjusted operating profit is stated before exceptional items.

# BAA (SP) Limited

## Financial performance (continued)

### Summary statutory results for the period

	Year ended 31 December 2008	Year ended 31 December 2007	Change <sup>1</sup> %
Turnover (£ million)	2,292	1,976	16.0
Operating profit (£ million)	364	435	(16.3)
(Loss)/profit before tax (million)	(324)	213	(252.3)
Net retail income (NRI) <sup>2</sup> (£ million)	554	553	0.2
NRI per passenger <sup>3</sup> (£)	4.5	4.4	2.3
Cash generated from operations (£ million)	831	817	1.7
Capital expenditure <sup>4</sup> (£ million)	1,015	1,076	(5.7)
Net debt (£ million) <sup>5</sup>	11,226	10,042	11.8

<sup>1</sup> Percentage change calculated using un-rounded numbers.

<sup>2</sup> Defined as revenues received directly from third-party retail operators and concession fees paid to BAA SP's airports by World Duty Free ('WDF').

<sup>3</sup> Defined as net retail income divided by the number of passengers.

<sup>4</sup> Capital expenditure excludes capitalised interest.

<sup>5</sup> Excluding interest payable.

### Reconciliation of statutory results to adjusted operating profit performance

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m	Change <sup>1</sup> %
Statutory turnover – (a)	2,292	1,976	16.0
<b>Adjusted turnover (d)</b>	<b>2,292</b>	<b>1,976</b>	<b>16.0</b>
Operating costs			
Statutory (b)	1,928	1,541	25.1
Net exceptional costs	108	180	(40.0)
<b>Adjusted operating costs (e)</b>	<b>1,820</b>	<b>1,361</b>	<b>33.7</b>
Operating profit			
Statutory (a – b)	364	435	(16.3)
Adjusted operating profit (d – e)	472	615	(23.3)

<sup>1</sup> Percentage change calculated using un-rounded numbers.

# BAA (SP) Limited

## Adjusted performance

The commentary below, in respect of operating costs and operating profit, is based on the adjusted performance of the Group. The commentary on all other aspects of the Group's results are based on the statutory financial information.

## Turnover

Turnover during the year increased 16.0% to £2,292 million (2007: £1,976 million). This increase reflects a 28.8% rise in aeronautical income, a 2.6% increase in gross retail income and 6.7% increase in other income compared to 2007, despite a 2.6% reduction in passengers.

	Year ended 31 December 2008	Year ended 31 December 2007	Change <sup>1</sup>
	£m	£m	%
Aeronautical income	1,209	939	28.8
Retail income	591	576	2.6
Other income	492	461	6.7
<b>Total<sup>1</sup></b>	<b>2,292</b>	<b>1,976</b>	<b>16.0</b>

<sup>1</sup> Percentage change and total calculated using un-rounded numbers

## Aeronautical charges summary (by airport)

	Aeronautical charges			Per passenger		
	Year ended 31 December 2008	Year ended 31 December 2007	Change <sup>1</sup> %	Year ended 31 December 2008	Year ended 31 December 2007	Change <sup>1</sup> %
Heathrow	835	634	31.8	12.48	9.34	33.7
Gatwick	228	178	28.6	6.68	5.05	32.4
Stansted	145	127	14.2	6.50	5.34	20.8
<b>Total<sup>1</sup></b>	<b>1,209</b>	<b>939</b>	<b>28.8</b>	<b>9.79</b>	<b>7.40</b>	<b>32.4</b>

<sup>1</sup> Percentage change and total calculated using un-rounded numbers

Growth in aeronautical income was driven by revised tariff proposed by the CAA for Heathrow and Gatwick for the five year regulatory period commencing on 1 April 2008. As a result, aeronautical income at these airports increased by 31.1% to £1,063 million (2007: £812 million). A significant element of the increase in aeronautical income at Heathrow and Gatwick reflected the inclusion in the regulatory settlement of the costs of the heightened security regime in place since 2006. At Stansted, aeronautical income increased by 14.2% to £145 million (2007: £127 million) partly reflecting the fact that certain discounts on its aeronautical charges ceased to apply from 1 April 2007.

In addition, £49 million of the increase in aeronautical income across the three London airports reflected a rebasing of tariffs to include costs previously charged to airlines by NATS for aerodrome navigation services (ANS). The tariffs at Heathrow and Gatwick were also rebased to include services previously charged by BAA separately from the aeronautical charges for both baggage infrastructure services and fuel levy.

## Retail income

The Group's gross retail income increased 2.6% to £591 million (2007: £576 million). On a comparable basis, derived by deducting cost of sales from gross income to adjust principally for changes in car parking contractual arrangements, net retail income ('NRI') increased 0.2% to £554 million (2007: £553 million) with an increase of 2.3% per passenger largely offset by a 2.6% reduction in passenger numbers.

# BAA (SP) Limited

## Financial performance (continued)

### Reconciliation of net retail income and net retail income per passenger

	Year ended 31 December 2008	Year ended 31 December 2007	Change <sup>1</sup>
	£m	£m	%
Retail revenue	591	576	2.6
Less cost of sales	(37)	(23)	60.9
Net retail income	554	553	0.2
Passengers (million)	123.4	126.8	(2.6)
Net retail income per passenger <sup>2</sup>	4.5	4.4	2.3

<sup>1</sup> Percentage change calculated using un-rounded numbers.

<sup>2</sup> Based on un-rounded numbers.

### Analysis of net retail income

	Year ended 31 December 2008	Year ended 31 December 2007	Change
	£m	£m	%
Airside specialist shops	79	74	6.8
Landside shops and bookshops	42	41	2.4
Catering	53	52	1.9
Bureaux de change	51	53	(3.8)
Duty Free	127	124	2.4
Car parking	128	134	(4.5)
Car rental	16	16	0.0
Advertising (media sales)	34	32	6.3
Other retail	24	27	(11.1)
<b>Total</b>	<b>554</b>	<b>553</b>	<b>0.2</b>

Retail performed solidly with a 3% uplift in net retail income per passenger across all BAA SP's airports. This resilience at a time of weak retail performance on the High Street reflects a number of factors specific to BAA SP's airports.

These include the significant recent expansion and upgrade of BAA SP's retail facilities. In particular, Heathrow Terminal 5 has 23,000m<sup>2</sup> of the highest quality retail space at Heathrow out of the airport's total of 66,000m<sup>2</sup>. Terminal 5 has only welcomed its full complement of passengers since October 2008 when British Airways completed its planned moves from other terminals. Elsewhere at Heathrow, Terminal 1's common user lounge launched in June 2008 (providing domestic passengers with access to the same retail offer as international passengers) also helped to support retail performance. Other recent increases and improvements in retail facilities across BAA SP's airports include the South Terminal departure lounge extension at Gatwick and the new arrival areas at Stansted.

The principal drivers of retail spend in BAA's airports are time spent in departure lounge areas and passenger propensity to spend. Improvements to the end-to-end passenger experience (including security queuing) have led to a better propensity to spend and recent exchange rate movements have increased the attractiveness of product pricing to non-UK based passengers. The change in the passenger mix towards more long haul passengers, who tend to have earlier check in times and combined with more efficient check in procedures, giving more time in lounges have contributed to the increased retail spend. These factors, taken with the significant improvements to the catering and retail offer, led by Terminal 5, have led to increases in participation (proportion who buy) and spend per passenger amongst both UK and foreign passengers.

#### Other income

Other income increased 6.7% in the year to 31 December 2008 to £492 million (2007: £461 million). This increase reflected in particular £12 million in income resulting from the introduction of services provided for passengers with restricted mobility ('PRM') which was previously directly sourced by the airlines. In addition, compared to 2007, rail income from Heathrow Express increased 8.3% from £80 million to £86 million and property rental income increased by 6.4% from £116 million to £124 million.

# BAA (SP) Limited

## Financial performance (continued)

### Operating costs

The Group's adjusted operating costs for the year ended 31 December 2008 were £1,820 million (31 December 2007: £1,361 million).

### Adjusted Group operating costs

	Year ended 31 December 2008	Year ended 31 December 2007	Change
	£m	£m	%
Staff costs	445	361	23.3
Rent and rates	130	100	30.0
Utilities	120	103	16.5
Maintenance	170	125	36.0
Retail costs	37	23	60.9
Depreciation and amortisation	444	289	53.6
Other costs	507	393	29.0
Capitalised costs	(33)	(33)	0.0
<b>Group operating costs</b>	<b>1,820</b>	<b>1,361</b>	<b>33.7</b>

There was a 23.3% increase in staff costs to £445 million (2007: £361 million) concentrated primarily at Heathrow, which in addition to the opening of Terminal 5 was related to the costs of increased numbers of security personnel that were required to achieve the security service standards under the new Service Quality Rebate ('SQR') schemes. The increases in rent and rates, utilities and maintenance costs reflects the opening of Terminal 5, higher unit costs for utility services and increased maintenance costs partly driven by the new SQR schemes. Retail costs increased due to increased expenditure relating to changes in the contractual structure for car parking contracts. Other costs include an additional £74 million in costs relating to aerodrome navigation services ('ANS') and services for passengers with reduced mobility ('PRM') which were sourced previously directly by the airlines. These are reimbursed through aeronautical charges for ANS and other income for PRM, as mentioned above. Other costs also reflect increases in cleaning costs of £13 million, due principally to the inclusion of Terminal 5 operations in 2008 in addition to running the other four terminals.

# BAA (SP) Limited

## Financial performance (continued)

### Adjusted EBITDA

Adjusted EBITDA for the year was £916 million (31 December 2007: £904 million) representing an increase of 13.3%.

### Performance by segment

On a segmental basis, revenue and adjusted EBITDA performance:

### Adjusted segmental analysis

	Year ended 31 December 2008		Year ended 31 December 2007		Change <sup>1</sup>	
	Revenue £m	Adjusted EBITDA <sup>2</sup> £m	Revenue £m	Adjusted EBITDA <sup>2</sup> £m	Revenue %	Adjusted EBITDA %
Heathrow <sup>3,4</sup>	1,568	635	1,324	636	18	-
Gatwick	465	159	410	154	13	3.2
Stansted	259	117	242	114	7	2.6
Others <sup>5</sup>	-	5	-	-	-	-
<b>Total</b>	<b>2,292</b>	<b>916</b>	<b>1,976</b>	<b>904</b>	<b>16</b>	<b>1.3</b>

<sup>1</sup> Percentage change calculated using un-rounded numbers.

<sup>2</sup> Adjusted EBITDA is earnings before interest, tax, depreciation, amortisation and exceptional items. Refer to Note 2 in notes to the financial statements for the reconciliation of adjusted EBITDA and statutory operating profit.

<sup>3</sup> Heathrow Express and Heathrow Connect rail services are included within the Heathrow Airport segment. The rail contribution to Heathrow's revenue and operating profit for the year was £86 million (31 December 2007: £80 million) and £5million (31 December 2007: £21 million) respectively.

<sup>4</sup> This amount excludes £8 million intercompany revenue received from HEX as it is eliminated at Heathrow Airport Limited level since HEX was acquired by Heathrow Airport Limited during the year.

<sup>5</sup> Others consist of other entities are Heathrow Express Operating Company Limited (HEX), BAA Funding Limited, BAA (AH) Limited and BAA (SP) Limited, parent entity as well as inter-company elimination.

The key drivers in Adjusted EBITDA remaining at similar levels to the prior year, whilst revenues increased by 16.0% were:

- Significant additional employment and other costs associated with operating Terminal 5
- Increased general and maintenance expenses to achieve higher service standards
- Increased employment costs driven by an increase in security personnel to reflect and achieve enhanced service standards and security requirements
- Increased aeronautical charges approved by CAA to reflect the higher cost structure, including those highlighted above, only applying from 1 April 2008
- The higher aeronautical charges applying at Heathrow and Gatwick from 1 April 2008 being phased such that only by 31 March 2009 will the full amounts have been recovered
- Part of the increased revenues being a pass through at nil margin of aerodrome air navigation services, previously charged directly to airlines by NATS, and services for passengers with restricted mobility

## Statutory results

### Exceptional items

Exceptional items are based on statutory results rather than adjusted results. Exceptional items include a total of £108 million in net pre-tax exceptional charges to the profit and loss account in 2008 (2007: £180 million). This is mainly due to £84 million of accelerated depreciation relating to the shortened asset lives of Terminals 1 and 2 at Heathrow given the Terminal 2A development, £22 million of T5 operational readiness costs, £17 million of exceptional pension costs and £15 million of reorganisation income. Please refer to Note 5 for details.

### Derivatives

Financial derivatives recognised in finance costs have given rise to a net fair value loss through the profit and loss account of £74 million (31 December 2007: £nil) (Note 6). This loss related primarily to index-linked swaps which are internally designated to hedge the BAA Funding bonds but do not achieve hedge accounting under UK GAAP. The index-linked swaps also provide a commercial hedge of future RPI linked revenue.



# BAA (SP) Limited

## Financial performance (continued)

### Net finance costs - ordinary

The Group's net finance costs before fair value gain on financial instruments were £619 million (31 December 2007: £222 million), after capitalised interest of £100 million (31 December 2007: £256 million) (Note 6). The higher annualised year on year net finance cost is primarily due to a lower capitalised interest charge. Capitalised interest reflects the Group's ongoing capital investment programme and related assets under construction, particularly Heathrow T5. Net interest paid for the year amounts to £101 million (31 December 2007: £nil).

### Taxation

The tax credit for the period was £123 million (31 December 2007: £159 million).

A tax credit of £48 million (31 December 2007: £33 million) for exceptional items (Note 5) has been recognised within the above tax credit. In addition, a deferred tax credit of £125 million on fair value losses (Note 21) has been recognised through statement of group total recognised gains and losses.

The accounting impact of the abolition of IBA's in the financial statements of BAA (SP) Group, prepared under UK GAAP, is significantly different to that disclosed in the consolidated financial statements of BAA Limited, which were prepared under IFRS. Under UK GAAP the accounting impact of the abolition of IBA's resulted in the release of a deferred tax liability of £170.9 million in the year ended 31 December 2007.

### Dividend

The Company paid an interim dividend of 13.4p (2007: Nil) per ordinary share, amounting to £705 million on 18 August 2008. No final dividends were paid or proposed during the year.

### Summary cash flow

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
Net cash inflow from operating activities	831	817
Net interest paid	(101)	-
Net capital expenditure	(1,015)	(1,076)
Acquisition of Heathrow Express Operating Company Limited	(4)	-
Dividend paid	-	(151)
Movement in liquid resources	(157)	-
Net cash inflow in financing activities	471	410
<b>Increase in cash</b>	<b>25</b>	<b>-</b>

### Balance sheet

At 31 December 2008, the Group had net assets of £1,138 million (31 December 2007: £2,556 million).

### Balance sheet position

	31 December 2008 £m	31 December 2007 £m
Total assets	14,470	13,868
Net assets	1,138	2,556
Gross debt <sup>1</sup>	11,408	10,042
Cash and liquid resources <sup>2</sup>	182	-
<b>Net debt<sup>1</sup></b>	<b>11,226</b>	<b>10,042</b>
Undrawn committed facilities	2,500	-

<sup>1</sup> Excluding interest payable

<sup>2</sup> Represented by both current asset investments of £157 million and cash at bank and in hand of £25 million.

# BAA (SP) Limited

## Financial performance (continued)

### Capital expenditure

In 2008, BAA SP incurred £1,016 million in capital expenditure (2007: £1,076 million) with £793 million at Heathrow, £124 million at Gatwick and £99 million at Stansted.

The major projects at Heathrow included the building of a tunnel between the main Terminal 5 building and its new satellite terminal ('T5C') for a connected baggage system, continued work on T5C and the purchase of an old control tower, which was the last part of land within the Central Terminal Area that was not owned by BAA SP and is key for future transformation plans. There were various other projects in the rest of the Heathrow campus, such as the Terminal 1 check-in refurbishment and creation of a common departure lounge in Terminal 1 for bmi and Aer Lingus.

At Gatwick major developments included completing the South Terminal departure lounge extension and starting the upgrade of the transit system that operates between the North Terminal and South Terminal.

At Stansted there was £61 million of expenditure on the existing infrastructure including the extension of the arrivals area to provide a better layout for capacity and retail. In addition, there was £38 million of expenditure for the Stansted second runway project.

### Regulatory Asset Base

The Regulatory Asset Base ('RAB') of BAA SP's airports is provided to the CAA and published as at 31 March each year in the regulatory accounts of Heathrow, Gatwick and Stansted airports. The RAB is also determined at 31 December each year for the purposes of calculating BAA SP's Regulatory Asset Ratio (the ratio of net debt to RAB) under its financing arrangements. The RAB is rolled forward between each date according to a formula set out by the CAA. Set out below are historic RAB figures for the three airports at 31 March 2008 from their regulatory accounts together with historic figures at 31 December 2008 and forecast figures at 31 December 2009 for Heathrow and Stansted. No forecast RAB at 31 December 2009 is provided for Gatwick as it is expected to be sold prior to that date but at 30 June 2009 it is forecast to have a RAB of £1,624 million.

	Heathrow	Gatwick	Stansted	Total
<b>31 March 2008</b>	9,232	1,560	1,185	11,977
<b>31 December 2008</b>	9,661	1,578	1,222	12,461
<b>31 December 2009</b>	10,510	-	1,265	11,775

### Financing –excluding interest payable

Gross debt at 31 December 2008 was £11,408 million (31 December 2007: £10,042 million). At 31 December 2008, net debt had increased to £11,226 million (31 December 2007: £10,042 million). The Group had outstanding interest rate swaps of £4.4 billion, index linked swaps of £2.2 billion and cross-currency swaps of £1.7 billion (in respect of €1 billion 2012, €750 million 2014 and €750 million 2018 bonds). The mark to market valuation of these derivatives at 31 December 2008 implied a net asset of £302 million (31 December 2007: a net asset of £nil million).

### Movement in gross debt – excluding interest payable

Below is a table summarising movements in gross debt in the period:

	£m
<b>Gross debt 31 December 2007</b>	<b>10,042</b>
Repayment of intercompany loans	(8,442)
Increase in bonds	4,499
Increase in bank loans	4,817
Increase in capex facilities	250
Repayment of SP Debenture	(34)
Fair value revaluation <sup>1</sup>	387
Issue fees	(145)
Amortisation of transaction costs, premiums and discounts	34
<b>Gross debt 31 December 2008</b>	<b>11,408</b>

<sup>1</sup> Foreign exchange revaluation of Euro denominated bonds

Please refer to Note 26(b) for explanation of the cash and non-cash movement in gross debt.

# BAA (SP) Limited

## Financial performance (continued)

### Liquidity

As at 31 December 2008, the Group had cash and liquid resources of £182 million (31 December 2007: nil) and undrawn committed facilities of £2,500 million (31 December 2007: nil).

### Security and Guarantees

Heathrow Airport Limited, Gatwick Airport Limited, Stansted Airport Limited, Heathrow Express Operating Company Limited, BAA (SP) Limited and BAA (AH) Limited (together, the Obligors) have granted security over their assets to secure their obligations to the Borrower Secured Creditors under the August 2008 refinancing documents and to the Subordinated Creditors under the Subordinated Facility Agreement which is held at the immediate parent entity of BAA (SP) Limited for £1.566 billion with maturity in 2011. Each Obligor has also provided a guarantee in respect of the obligations of the other Obligors.

BAA Pension Trustee Company Limited (the BAA Pension Trustee) is a Borrower Secured Creditor and has a right to receive up to £300 million out of the proceeds of enforcement of the security granted by the Obligors, such right ranking *pari passu* with the Class A creditors of the Obligors.

BAA Airports Limited (formerly BAA Limited) has provided a guarantee to the Deutsche Trustee Company Limited (the Bond Trustee) for itself and on behalf of the BAA Guaranteed Bondholders in respect of bonds with a final legal maturity of no later than 2018 issued by BAA Funding Limited.

BAA Funding Limited has provided security to the Bond Trustee (as trustee for the Issuer Secured Creditors).

BAA (DSH) Limited (intermediate parent entity of BAA (SP) Limited) and its subsidiaries (other than BAA Funding Limited and Heathrow Airport Community Board insulation Limited), plus ADI Finance 2 Limited, BAA Limited, BAA Airports Holdco Limited and BAA Airports Limited are guarantors under the Subordinated Facility Agreement. All the guarantors, apart from ADI Finance 2 Limited, are party to transaction security which secures liabilities arising under the Subordinated Facility Agreement.

Heathrow Airport Limited, Gatwick Airport Limited, Stansted Airport Limited and Heathrow Express Operating Company Limited have provided a guarantee in favour of The Royal Bank of Scotland plc as Borrower Account Bank in respect of the liabilities of those companies under the Borrower Account Bank Agreement.

### Covenants

The BAA Funding Limited Bonds, Refinancing Facilities and the Initial Credit Facilities are required to comply with the covenants under the Common Terms Agreement ('CTA') of the designated Group. There are certain covenant threshold requirements under the CTA which must be maintained:-

		Forecasting event	Trigger event	Financial covenant <sup>1</sup>
Senior Interest Cover Ratio	to be greater than	1.60	1.40	1.05
Junior Interest Cover Ratio	to be greater than	1.40	1.20	N/A
Senior Net Indebtedness to Total RAB (RAR)	to be less than	0.70	0.70	0.925
Junior Net Indebtedness to Total RAB (RAR)	to be less than	0.85	0.85	N/A

<sup>1</sup> Three year period average for Interest Cover Ratio from the three year period ending 31 December 2012.

Following the occurrence of a Trigger Event (as defined above) which is continuing, the Obligors are prohibited from making certain payments ("Restricted Payments"), mainly in relation to payments in respect of subordinated debt and payments to other BAA group companies outside of the security group, and are obliged to make repayments of amounts outstanding under the senior debt facilities of the security group, equivalent to the amount of restricted payments that would otherwise have been made.

# BAA (SP) Limited

## Financial performance (continued)

### Covenants (continued)

Following the occurrence of a Forecasting Event (as defined above) which is continuing, the Investor Report issued under the CTA shall disclose information of all forward looking ratios until the end of the current regulatory period, rather than just the 12 month forward looking ratio. In addition, the Investor Report and Compliance Certificate issued under the CTA shall disclose the forecast restricted payments which are to be made within the 90 days commencing from the delivery of such report.

All covenants have been tested and complied with as at 31 December 2008.

Additional disclosures on risk management and hedging of borrowings are included in Note 17.

### Contingent liabilities

The Group has external contingent liabilities, comprising letters of credit, performance/surety bonds, performance guarantees and other items arising in the normal course of business amounting to £325 million at 31 December 2008 (31 December 2007: £123 million).

Included in the above, in July 1998, BAA Airports Ltd and Heathrow Airport Limited entered into a cross-border lease and leaseback in relation to the Heathrow Express rolling stock owned by Heathrow Airport Limited. The companies guarantee payments that are decreased by a deposit of US\$59.4 million with Rabobank and US\$15 million in US Government securities. In addition, they guarantee early termination payments. The cross border lease transaction was terminated on 13th January 2009 with Heathrow Airport Limited making a termination payment of US\$3.3 million.

easyJet have obtained leave to bring a judicial review of the CAA's price cap determination for Gatwick Airport for Q5. The easyJet challenge relates principally to the amount of operating expenditure allowed. They maintain the CAA has not had sufficient regard to the recommendations of the Competition Commission and has unfairly and unlawfully allowed security cost submitted at a late stage of the review. The case is expected to be heard in the High Court from the 16th March 2009. If easyJet are successful it is likely the issue will be remitted to the CAA for their reconsideration. Should the CAA determine that the airport charges cap should be lower Gatwick Airport Limited would be required to rebate the amount of airport charges levied in excess of the amended cap. On the basis of legal advice received the Board is confident no such rebate will arise.

Under the Shared Service Agreement (Note 1) hedging costs properly incurred by BAA Airports Limited in relation to the Employee Share Ownership Plan (ESOP) may be recharged to BAA Limited's subsidiaries which includes entities within the Group. At 31 December 2008, the ESOP swap held in BAA Airports Limited had a fair value loss of £117 million. The Group may be obligated to settle its share of these amounts in the future, depending on a number of factors, including the number of options vesting, the number of options being exercised and the Ferrovial share price at exercise date. Accordingly, this is disclosed as contingent liability.

# BAA (SP) Limited

## Risk management

Risk management is a key element of the BAA Limited Group's ('Group') operations. Risk is centrally managed for the whole Group (including BAA (SP) Group) as part of corporate services provided to the businesses under the Shared Service Agreement (Note 1). The Executive Committee and Board referred in the notes below relates to Executive Committee and Board of the Group.

Risk management in the Group facilitates the identification, evaluation and effective management of the threats to the achievement of the Group's purpose, vision, objectives, goals and strategies. The vision of risk management is to embed the awareness of risk at all levels of the organisation, in such a way that all significant business decisions are risk-informed. Particular emphasis is given to safety and security, environmental, commercial, financial, reputational and legal risks with the framework ensuring that the Group's financial aspirations are not pursued at the expense of risk management, thus delivering a balanced control of risk, using formal risk management processes.

A key element of the risk management process is the risk-profiling methodology. This determines the threats to the achievement of business objectives and day to day operations in terms of likelihood and consequence at both inherent and residual level, after taking account of mitigating and controlling actions. Details are maintained in a hierarchy of risk registers used as the basis for regular review of risk management at Executive Committee and Board level. The risk registers are also used to inform decisions relating to the procurement of insurance cover.

The risk management process is also aimed at defining and implementing clear accountabilities, processes and reporting formats that deliver efficient and effective management assurance to the Board to ensure statutory compliance whilst supporting business units to successfully manage their operations and properly embed risk management within these operations. The operation of the process and the individual registers are subject to review by the Group's Business Assurance function, whose primary responsibility is to provide independent assurance to the Board that the controls put in place by management to mitigate risks are working effectively.

The principal corporate risks as identified by the Executive Committee are:

### Safety and security risks

Safety and security risks are regarded as an important risk to manage throughout the Group. The Group mitigates this risk by adopting and enforcing rigorous policies and procedures supported by professional training and by investment in leading-edge security technology. The Group works closely with government agencies, police and the Armed Forces to match security measures to a level commensurate with the current raised threat environment.

Assurance is provided through management reporting processes and a specialist compliance audit function, reporting directly to the Health, Safety, Security and Environment Committee.

### Regulatory environment, legal and reputational risks

#### CAA regulation

As noted previously, the Group's operations at Heathrow, Gatwick and Stansted airports are subject to regulatory review by the CAA and CC every five years. The risk of an adverse outcome from the five-yearly review is mitigated as far as possible by a dedicated project team which ensures full compliance with formal regulatory requirements, establishes a sound relationship with the regulator and advises the Executive Committee and Board on regulatory matters.

Part of the regulatory framework is the Group's involvement in constructive engagement with the airlines. In order to manage the risk of adverse airline relations, all airlines have been invited to participate at all stages and to be represented on all fora – eg joint steering groups. When feedback was sought or processes measured, independent third parties have been utilised for data gathering and analysis to ensure confidentiality and neutrality of interpretation. In addition, key stakeholders are engaged on a joint planning basis which provides the airlines with the opportunity of airing views and sharing plans, thereby ensuring their ongoing requirements are articulated and understood.

#### Competition rules

The penalties for failing to comply with the 1998 Competition Act and relevant EU law are recognised as risks to manage within the Group, given its position in certain markets. Clear policy direction, which includes compulsory awareness training and close support from the internal legal department, has reduced the likelihood of the Group breaching these regulations. Refer to the 'Outlook for 2009' section for details on the regulatory process and OFT investigation on competition.

# BAA (SP) Limited

## Risk management (continued)

### Capacity shortfall

Failure to secure necessary planning permissions would lead to the Group having insufficient capacity to meet the expected demands of the industry resulting in increased congestion and declining passenger service. The Group mitigates this risk through extensive consultation with community groups and authorities at a local level and active participation in Government consultations and other advisory groups. However, it should be noted that, despite the mitigating action taken by management and a planned capital investment programme, which will provide additional capacity, it is anticipated that demand will continue to exceed available capacity in London throughout the next ten years. In addition, the investment in additional capacity at the airports is dependent on the outcome of the regulatory settlements in 2013 for Heathrow and Gatwick and 2014 for Stansted.

Existing planning approvals provide for approximate passenger traffic growth at Heathrow (including T5) to 90 million, Gatwick to around 40 million and Stansted to around 35 million. BAA has announced details of its development proposal for Stansted Generation 2 ('SG2'). This proposal includes the provision of a second runway and terminal and will have an initial capacity for about 10 million passengers per annum. This proposal is subject to a separate planning inquiry which is due to commence shortly.

The UK Government's Aviation White Paper '*The Future of Air Transport*' (the White Paper) was published in December 2003 and clarified the Government's policies regarding airport expansion for the whole of the country. It emphasised the need for airport operators to invest in delivering new capacity. The Group recognises a need to manage airport development following the White Paper in a way that does not lead to a loss of public or political confidence in BAA. To mitigate this risk, separate dedicated project teams (with relevant expertise and disciplines) for Heathrow and Stansted have been established to work closely with local communities, airlines and other interested parties.

### Environment

Environmental risks need to be managed throughout the Group as they have the potential to impact the Group's reputation, and our licence to operate and to grow. The Group mitigates these risks at a number of levels, including environmental management systems and training programmes embedded with operations, clear environmental strategies, resource conservation initiatives, proactive and progressive influencing of third parties, stakeholder engagement and community relations programmes. The Group works closely with a range of stakeholders to ensure that the Group reacts effectively to the challenges posed by the environmental agenda.

### Commercial and financial risks

#### Capital projects

The Group recognises that failure to control key capital project costs and delivery could damage its financial standing and reputation. The Group mitigates this risk through adherence to a continually enhanced project process and by systems of project reviews before approval, during construction and after project completion. In addition, specific additional controls for Heathrow T5 were introduced, including the strengthening of the project management team and the commitment of dedicated specialist internal audit and risk management resources to reinforce assurance to the Board. Similar controls will also be adopted for the Stansted Generation 2 and Heathrow East terminal developments. All projects include an allowance for risk and opportunity.

#### Changes in demand

The risk of unanticipated long-term changes in passenger demand for air travel could lead to misaligned operational capacity within the Group. Since it is not possible to identify the timing or period of such an effect, the Group carries out evaluations through a series of scenario planning exercises.

#### Industrial relations

The risk of industrial action by key staff that affects critical services, curtails operations, and has an adverse financial and reputational impact on the Group is recognised. The Group has a range of formal national and local consultative bodies to discuss pay, employment conditions and business issues with the Trade Unions. A three year Pay Agreement was reached in August 2006 covering negotiated grades within the Group and new negotiations are taking place in 2009 for the next pay deal. The Group could also be exposed in the short term to the effect of industrial action at key clients (i.e. airlines).

# BAA (SP) Limited

## Risk management (continued)

### Treasury

The Board approves prudent treasury policies and delegates certain responsibilities to senior management who directly control day-to-day treasury operations.

Treasury operates on a centralised non-speculative risk basis. The treasury function is not permitted to speculate in financial instruments. Its purpose is to identify, mitigate and hedge treasury related financial risks inherent to the Group's business operations. To achieve this, the Group enters into interest rate swaps, cross currency interest rate swaps, index linked swaps and foreign exchange spot and forward/swap transactions to protect against interest rate risk, foreign currency risk and future RPI related revenue. The primary treasury related financial risks faced by the Group which are the focus of treasury policies, summarised as:

#### (a) Interest rates

The Group maintains a mix of fixed and floating rate debt. At the period end, the level of fixed rate debt after hedging as at 31 December 2008 was 88%.

#### (b) Foreign currency

For debt raised in foreign currencies, the Group uses cross-currency swaps to hedge the related interest and principal payments. In cases where debt is raised in foreign currencies, 100% of the exposure is hedged in this way, subject to a de minimus limit. The Group uses foreign currency forward contracts to hedge material capital expenditure in foreign currencies once a project is certain to proceed. As at 31 December 2008, there were no significant unmatched exposures.

#### (c) Funding and liquidity

To ensure continuity of funding and flexibility, debt maturities are spread over a range of dates, thereby ensuring that the Group is not exposed to excessive refinancing risk in any one year. In August 2008, BAA Limited completed a permanent refinancing of the acquisition financing originally put in place at the time of the Ferrovial-led consortium's acquisition of the Group in 2006. The refinancing comprise of the following key elements in relation to BAA SP Group:

- A corporate reorganisation to enable separate financing of the 3 London airports of Heathrow, Gatwick and Stansted.
- The establishment of an investment grade long term financing platform for the 3 London airports including £7.59 billion of bank facilities (comprising term loans, capital expenditure and working capital facilities) and the exchange of £4.5 billion of bonds previously issued by BAA Airports Limited (the previous BAA plc at the original date of issue) for bonds issued by BAA Funding Limited

#### (d) Covenants

Covenants are standardised wherever possible and are monitored on an ongoing basis with formal testing reported to the Board and Executive Committee. The Group continues to comply with all borrowing obligations and financial covenants.

#### (e) Counterparty credit

The Group maintains a prudent split of cash and liquid resources across a range of market counterparties in order to mitigate counterparty credit risk. Board approved investment policies and relevant debt facility agreements provide counterparty investment limits, based on short and long term credit ratings. Investment activity is reviewed on a regular basis and no cash or liquid resources are placed with counterparties with credit ratings lower than A- / A-1. The Group monitors the credit rating of the derivative counterparties on a daily basis and ensures no positions are held with counterparties with a credit rating of below BBB+ / A.

By order of the Board



**Jose Leo**  
Director

# BAA (SP) Limited

## Report of the Directors

### BAA (SP) Limited Annual Report 31 December 2008

The directors present their report and the audited financial statements for the year ended 31 December 2008.

#### Principal Activities

The principal activity of BAA (SP) Limited ('BAA SP') is as the holding company of BAA (AH) Limited, owner of the Designated airports (Heathrow, Gatwick and Stansted airports) and BAA Funding Limited, the bond issuer of the Security Group.

#### Review of Business and Future Developments

On 20 December 2007, the Company was incorporated as a direct subsidiary of BAA Limited (formerly known as Airport Development and Investment Limited) with nominal share capital of £2. The entity was subsequently transferred to BAA Airports Limited (formerly known as BAA Limited) for the same consideration.

On 31 January 2008, the Company carried out a share for share exchange and issued a debenture to BAA Airports Limited in order to acquire BAA (AH) Limited, the holding company for Heathrow, Gatwick and Stansted airports.

On 29 February 2008, part of the total consideration above in the form of shares were issued to BAA Airports Limited in exchange for the transfer of the additional shares issued by BAA (AH) Limited to BAA Airports Limited on the same date.

On 23 April 2008, the High Court of Justice approved the special resolution, passed on 26 March 2008, requesting the reduction in the nominal value of each ordinary share issued. The share capital for the Company reduced from £9,000,000,000 divided into 9,000,000,000 ordinary shares at £1 each to £17,100,000 divided into 9,000,000,000 ordinary shares at £0.0019 each. The capital reduction was necessary to create distributable reserves to make dividend payments to BAA (SH) Limited, the immediate parent.

#### Results and Dividends

The results for the period are set out on page 28. The Company paid an interim dividend of 13.4p (2007: Nil) per ordinary share, amounting to £705 million on 18<sup>th</sup> August 2008. No final dividends were paid or proposed during the year.

#### Board of Directors

The directors who served during the period and since the period end are as follows:

L Sanchez Salmeron	(appointed 20 December 2007)
J Leo	(appointed 20 December 2007)
S J K Nelson	(appointed 20 December 2007 and resigned 31 March 2008)

#### Directors' Interests

None of the directors had any interests in the ordinary shares of the Company at the end of the period or had interests in any of the Company's subsidiaries at any time during the period. None of the directors had a material interest in any contract of significance with the Company or any of its subsidiary undertakings during the year.

#### Employees

The Company has no direct employees. However all staff costs which are borne by BAA Airports Limited (the Company's intermediate parent entity in the UK) on behalf of BAA SP are recharged directly to the airports.



# BAA (SP) Limited

## Report of the directors

### BAA (SP) Limited Annual Report 31 December 2008

#### Donation

The Group's charitable donations for the year amounted to £0.4 million (31 December 2007: £0.4 million).

The amount contributed to and purpose for each major category of charitable donation is as follows:

Heathrow Travel care	£0.1 million	Crisis social work
Green corridor	£0.1 million	Environmental charity

#### Payment Practice

The Company complies with the UK Government's Better Payment Practice Code which states that responsible companies should:

- Agree payment terms at the outset of a transaction and adhere to them
- Provide suppliers with clear guidance on payment procedures
- Pay bills in accordance with any contract agreed or as required by law
- Advise suppliers without delay when invoices are contested and settle disputes quickly.

The Company's trade payables balance during the year was £nil (31 December 2007: £nil).

#### Financial Risk Management Objectives and Policies

The Group's financial risk management objectives and policies, including hedging policies along with the Group's exposure to risk can be found on pages 19 to 21 of the Risk Management section of the Business Review.

#### Directors' Indemnity

The Company's Articles of Association provide that, subject to the provisions of the Companies Act, but without prejudice to any indemnity to which the person concerned might otherwise be entitled, every director of the Company shall be indemnified out of the assets of the Company against any loss or liability incurred by him in defending any proceedings in which judgment is given in his favour, or in which he is acquitted or in connection with any application in which relief is granted to him by the court for any negligence, default, breach of duty or breach of trust by him in relation to the Company or otherwise in connection with his duties or powers or office.

#### Disclosure of information for auditors

The directors are satisfied that the auditors are aware of all information relevant to the audit of the Company's Consolidated Financial Statements for the period ended 31 December 2008 and that they have taken all steps that they ought to have taken as directors in order to make them aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

# BAA (SP) Limited

Report of the directors

BAA (SP) Limited Annual Report 31 December 2008

## Auditors

Pursuant to Section 487 of the Companies Act 2006, the auditors will be deemed to be re-appointed and PricewaterhouseCoopers LLP therefore will continue in office.

By order of the Board



Shu Mei Qor  
Company Secretary  
25 February 2009

Registered Office:  
130 Wilton Road  
London  
SW1V 1LQ

# BAA (SP) Limited

## Statement of Directors' Responsibilities in respect of the Annual Report and the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom generally accepted standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the Group and of the profit or loss of the Group for that period.

In preparing those consolidated financial statements, the directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State that the Company's financial statements comply with applicable UK GAAP, subject to any material departures disclosed and explained in the financial statements;
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business, in which case there should be supporting assumptions or qualifications as necessary. This statement should cover both the parent company and group as a whole.

The directors confirm that they have complied with the above requirements in preparing the consolidated financial statements.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The maintenance and integrity of the BAA website which includes information related to BAA (SP) Limited Group is the responsibility of the directors. The work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board



Shu Mei Ooi  
Company Secretary  
25 February 2009

## **Independent auditors' report to the members of BAA (SP) Limited**

We have audited the Group financial statements ("the financial statements") of BAA (SP) Limited for the year ended 31 December 2008 which comprise the consolidated profit and loss account, the consolidated balance sheet, the consolidated cash flow statement, the statement of total recognised gains and losses, the reconciliation of movements in group shareholder's funds, the note of group historical cost profits and losses and the related notes. These financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of BAA (SP) Limited for the year ended 31 December 2008.

### **Respective responsibilities of directors and auditors**

The directors' responsibilities for preparing the Group financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the Group financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the Group financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Report of the Directors is consistent with the Group financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited Group financial statements. The other information comprises only the Report of the Directors, the Statement of Directors Responsibilities and the Business Review. We consider the implications for our report if we become aware of any apparent misstatements with the Group financial statements. Our responsibilities do not extend to any other information.

### **Basis of audit opinion**

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

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

## **Independent auditors' report to the members of BAA (SP) Limited (continued)**

### **Opinion**

In our opinion:

- The Group financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Group's affairs as at 31 December 2008 and of its loss and cash flows for the year then ended;
- The Group financial statements have been properly prepared in accordance with the Companies Act 1985; and
- The information given in the Report of the Directors is consistent with the Group financial statements.

A handwritten signature in cursive script that reads "PricewaterhouseCoopers LLP".

**PricewaterhouseCoopers LLP**

Chartered Accountants and Registered Auditors

London

25 February 2009

# BAA (SP) Limited

## Consolidated profit and loss account For the year ended 31 December 2008

	Note	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
Turnover – continuing operations	2	2,292	1,976
Operating costs – ordinary	3	(1,820)	(1,361)
Operating costs – exceptional	5	(108)	(180)
Total operating costs		(1,928)	(1,541)
<b>Operating profit – continuing operations</b>		<b>364</b>	<b>435</b>
Interest receivable	6(a)	111	39
Interest payable and similar charges – ordinary	6(b)	(656)	(261)
Interest payable and similar charges – exceptional	5	(143)	-
Total net interest payable and similar charges		(688)	(222)
(Loss)/profit on ordinary activities before taxation		(324)	213
Tax credit on (loss)/profit on ordinary activities	7	123	159
<b>(Loss)/profit on ordinary activities after taxation</b>	22	<b>(201)</b>	<b>372</b>

The notes on pages 32 to 63 form an integral part of these financial statements.

All profit and loss recognised during the current and prior year is from continuing operations.

## BAA (SP) Limited

### Statement of total recognised gains and losses For the year ended 31 December 2008

	Note	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>(Loss)/profit for the financial year</b>	22	(201)	372
Unrealised (loss)/gain on revaluation of investment properties	20	(192)	19
Losses on cash flow hedges taken directly to equity	21	(445)	-
Deferred tax arising on cash flow hedge losses	21	125	-
		(512)	19
<b>Total recognised (losses)/gains relating to the financial year</b>		(713)	391

### Reconciliation of movements in group shareholder's funds For the year ended 31 December 2008

	Note	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>(Loss)/profit for the financial year</b>	22	(201)	372
Dividends on shares classified in shareholder's funds	8	(705)	(151)
Retained profit		(906)	221
Other recognised gains and losses relating to the year (net)		(512)	19
Net movement in shareholder's funds		(1,418)	240
<b>Opening shareholder's funds</b>		2,556	2,316
<b>Closing shareholder's funds</b>		1,138	2,556

### Note of group historical cost profits and losses For the year ended 31 December 2008

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>Reported (loss)/profit on ordinary activities before taxation</b>	(324)	213
Adjusted for:		
Fair value gains and losses on derivatives contracts:		
- Interest rate swaps	50	-
- Cross currency interest rate swaps	(35)	-
- Index linked swaps	(81)	-
- Foreign exchange contracts	(7)	-
Amortisation of fair value of derivative contracts at novation	10	-
Amortisation of the accretion on the RPI leg of index-linked swaps	(42)	-
<b>Historical cost (loss)/profit on ordinary activities before taxation</b>	(429)	213
<b>Historical cost (loss)/profit on ordinary activities after taxation</b>	(306)	372

# BAA (SP) Limited

## Consolidated balance sheet at 31 December 2008

	Note	31 December 2008 £m	31 December 2007 £m
<b>Fixed assets</b>			
Tangible fixed assets	9	12,910	12,493
Financial assets – derivative financial instruments	17	830	-
<b>Total fixed assets</b>		<b>13,740</b>	<b>12,493</b>
<b>Current assets</b>			
Stocks	10	8	8
Debtors: due within one year	11	402	793
due after more than one year	11	-	574
Financial assets – derivative financial instruments	17	138	-
Current assets investment	12	157	-
Cash at bank and in hand	13	25	-
<b>Total current assets</b>		<b>730</b>	<b>1,375</b>
<b>Current liabilities</b>			
Creditors: amounts falling due within one year	14	(1,064)	(8,751)
<b>Net current liabilities</b>		<b>(334)</b>	<b>(7,376)</b>
<b>Total assets less current liabilities</b>		<b>13,406</b>	<b>5,117</b>
<b>Creditors: amounts falling due after more than one year</b>	15	<b>(11,714)</b>	<b>(1,829)</b>
<b>Provisions for liabilities and charges</b>	18	<b>(554)</b>	<b>(732)</b>
<b>Net assets</b>		<b>1,138</b>	<b>2,556</b>
<b>Capital and reserves</b>			
Called up share capital	19	10	5,274
Revaluation reserve	20	2,035	2,227
Merger reserve	21	(5,630)	(5,630)
Fair value reserve	21	(320)	-
Profit and loss account	22	5,043	685
<b>Total shareholder's funds</b>		<b>1,138</b>	<b>2,556</b>

These financial statements were approved by the board of directors on 25 February 2009 and were signed on its behalf by:

  
 Jose Leo  
 Director



# BAA (SP) Limited

## Consolidated cash flow statement For the year ended 31 December 2008

	Note	Year ended 31 December 2008 £m	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m	Year ended 31 December 2007 £m
<b>Net cash inflow from operating activities</b>	26		831		817
<b>Return on investment and servicing of finance</b>					
Interest received	6	111		39	
Interest paid	6	(830)		(517)	
Bond cost amortisation		13		-	
Fees amortised on bank facilities		23		-	
Hedge prepayment amortisation		63		-	
Unwinding of discount on provision	18	15		5	
Movement in accruals during the year		45		-	
Non-cash movement of intercompany interest		459		473	
Net cash outflow from returns on investments and servicing of finance			(101)		-
<b>Capital expenditure and financial investment</b>					
Purchase of tangible fixed assets	9	(1,016)		(1,076)	
Sale of tangible fixed assets		1		-	
Net cash outflow for capital expenditure and financial investment			(1,015)		(1,076)
<b>Acquisition</b>					
Purchase of subsidiary undertaking	23	(4)		-	
Net cash outflow for acquisition			(4)		-
<b>Equity dividends paid to shareholders</b>					(151)
Net cash outflow before use of liquid resources and financing			(289)		(410)
<b>Management of liquid resources</b>					
Increase in short term deposits	12	(157)		-	
Net cash outflow from management of liquid resources			(157)		-
<b>Financing</b>					
Drawdown of refinancing facility	16	4,400		-	
Drawdown in capex facility	16	250		-	
Drawdown of EIB facility		435		-	
Repayment of EIB facility		(18)		-	
Payment of loan arrangement fees		(15)		-	
(Decrease)/increase in amounts owed to group		(4,581)		410	
Net cash inflow from financing			471		410
<b>Increase in net cash</b>	13		25		-
<b>Reconciliation to net debt</b>					
Net debt at 1 January	26		(10,042)		-
<b>Increase in net cash</b>	13		25		-
Movement in liquid resources	12		157		-
Movement in borrowings			(5,052)		-
Movement in intercompany borrowings			4,264		(10,042)
Other non-cash changes			(143)		-
Exchange adjustments	26		(435)		-
<b>Net debt at 31 December</b>	26		(11,226)		(10,042)

# BAA (SP) Limited

## Notes to the financial statements

### 1 Accounting policies

These financial statements have been prepared under historical cost convention, as modified by the revaluation of certain tangible fixed assets and financial instruments in accordance with the Companies Act 1985 and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) except as set out within the accounting policies note.

The directors have prepared the financial statements on a going concern basis which requires the directors to have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future.

Consequently the directors have reviewed the cashflow projections of the Group taking into account:

- the forecast passenger numbers, revenue and operating cashflows from the underlying operations;
- the forecast level of capital expenditure; and
- the Groups funding structure following the refinancing in August 2008 and the significant committed facilities that are available to the Group (see note 16).

As a result of the review, having made appropriate enquiries of management and allowing for headroom to accommodate a reasonable downside scenario (including a fall in passenger numbers), the directors have a reasonable expectation that sufficient funds will be available to meet the Group's funding requirement over the coming twelve month period. All of the Group's financial covenants (see note 17) have been met and are forecast to be met for the foreseeable future.

Gatwick Airport Limited will not be disclosed as a discontinued operation as the expected completion date of the sale process does not meet the criteria of a discontinued operation under UK GAAP. Under UK GAAP the sale process needs to be completed within 3 months of the financial year end.

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements.

#### **Basis of consolidation**

The Company was incorporated on 20 December 2007. On 31 January 2008, the Company entered into sale and purchase agreement to purchase the entire issued capital of BAA (AH) Limited from BAA Limited. The consideration was satisfied by:

- a) the allotment and issue by the Company to BAA Limited of 4,588,184,000 ordinary shares of £1 each credited as fully paid in the capital of the Company; and
- b) the issue by the Company to BAA Limited of a loan note with a principal amount of £1,600,000,000.

Subsequently, on 29 February 2008, the Company purchased additional shares of BAA (AH) Limited and was satisfied by the allotment and issue by the Company of 685,371,176 ordinary shares of £1 each credited as fully paid in the capital of the Company. At the time of this transaction, BAA (AH) Limited was the owner of the Designated Airports.

In order to present a true and fair view of the BAA (SP) Limited Group the abovementioned transaction (the "Transaction") has been accounted for in accordance with FRS6 and the principles of merger accounting. This represents a departure from the provision of the United Kingdom Companies Act 1985 which sets out the conditions for merger accounting based on the assumption that a merger is effected through the issue of equity shares.

Schedule 4A to the Companies Act 1985 and FRS 6 'Acquisition and Mergers' require that acquisition accounting be adopted where all the conditions laid down for merger accounting are not satisfied. These conditions were not all satisfied because the fair value of the non-equity element of the consideration (the loan note) given by the Company for the shares in BAA (AH) Limited exceeded 10% of the nominal value of the share element of the consideration.

However, in the opinion of the directors, the Transaction was a group reconstruction rather than an acquisition, since the shareholders of the Company are the same as the former shareholders of BAA (AH) Limited and the rights of each shareholder, relative to the others, are unchanged and no minority interest in the net assets of the Group is altered. In addition, the purpose of the transaction was not to move value out of the Group and return to shareholders, but rather to reorganise the assets and liabilities within the existing group. Therefore the directors consider that to record the Transaction as an acquisition by the Company, attributing fair values to the assets and liabilities of the Group and reflecting only the post transaction results within these financial statements, would fail to give a true and fair view of the Group's results and financial position.

# BAA (SP) Limited

## 1 Accounting policies (continued)

### Basis of consolidation (continued)

Accordingly, having regard to the overriding requirement under section 227(6) of the Companies Act 1985 for the financial statements to give a true and fair view of the Group's results and financial position, the directors have adopted merger accounting principles in drawing up these financial statements. The main consequence of adopting merger rather than acquisition accounting is that the balance sheet of the merged group includes the assets and liabilities of each of the groups subsidiaries at their carrying values prior to the merger, subject to any adjustments to achieve uniformity of accounting policies, rather than at their fair values at the date of the merger.

Had merger accounting not been adopted in the preparation of these financial statements goodwill of approximately £3.5 billion, with an useful economic life of 20 years would have been recorded in the consolidated balance sheet, with an associated amortisation charge for the period from merger to 31 December 2008 of £152 million. These approximations have been made based on the fair value of the underlying airport assets and goodwill recognised at the June 2006 acquisition of BAA Limited by Grupo Ferrovial, the Company's ultimate parent entity having adjusted the goodwill recorded under IFRS to add back the intangible assets recognised separately under IFRS that would have been subsumed into goodwill under UK GAAP.

Whilst the group represented by BAA (SP) Limited and its subsidiaries did not exist until 2008, the adoption of merger accounting results in comparative information for 2007 being provided as if the group has always been in existence.

However, the Group applied acquisition accounting on the acquisition of Heathrow Express Operating Company Limited (HEX) which took place on 7 August 2008 as this is not deemed a part of the initial Group reconstruction process. Please refer to Note 23 for details.

### Turnover

Turnover is recognised in accordance with Financial Reporting Standard (FRS) 5 'Reporting the substance of transactions', net of VAT, and comprises primarily:

- Airport and other traffic charges
  - Passenger charges based on the number of departing passengers on departure
  - Aircraft landing charges levied according to weight on landing
  - Aircraft parking charges based on a combination of weight and time parked
  - Other charges levied for passenger and baggage handling when these services are rendered
- Property and operational facilities
  - Property letting sales, recognised on a straight-line basis over the term of the rental period
  - Usage charges made for operational systems (eg check-in-desks), recognised as each service period is provided
  - Proceeds from the sale of trading properties, recognised on the unconditional completion of the sale
  - Other invoiced sales, recognised on the performance of the service.
- Retail
  - Concession fee based upon turnover certificate supplied by concessionaires.
- Other
  - Turnover from ticket sales, recognised at the time of travel.

### Exceptional items

Exceptional items are material items of income and expense that, because of the unusual nature and expected infrequency of the events giving rise to them, merit separate presentation to allow an understanding of the Group's financial performance.

Such events may include gains or losses on disposal of businesses or assets, major reorganisation of business, closure or mothballing of terminals and those costs incurred in bringing new airport terminal complexes and airfields to operational readiness that are not able to be capitalised as part of the project.

Additional details of items disclosed as exceptional are provided in note 5.

# BAA (SP) Limited

## 1 Accounting policies (continued)

### Fixed assets

#### (i) Operational assets

Terminal complexes, airfield assets, plant and equipment, rail assets and Group occupied properties are stated at cost less accumulated depreciation. Assets in the course of construction are stated at cost less provision for impairment. Assets in the course of construction are transferred to completed assets when substantially all the activities necessary to get the asset ready for use are complete. Where appropriate, cost includes borrowing costs capitalised, own labour costs of construction-related project management, and directly attributable overheads. Projects that are in the early stages of planning are capitalised where the directors are satisfied that it is probable the necessary consents will be received and the projects will be developed to achieve a successful delivery of an asset such that future commercial returns will flow to the Group. The Group reviews these projects on a regular basis, and at least every six months, to determine whether events or circumstances have arisen that may indicate that the carrying amount of the asset may not be recoverable, at which point the asset would be assessed for impairment.

#### (ii) Investment properties

Investment property, which is property held to earn rentals and/or capital appreciation, is valued at the balance sheet date at open market value. All investment properties are revalued annually by the directors and at least once every five years by external valuers. Any surplus or deficit on revaluation is transferred to the revaluation reserve with the exception of deficits below original cost which are expected to be permanent, which are charged to the profit and loss account.

Profits or losses arising from the sale of investment properties are calculated by reference to book value and treated as exceptional items. Profits are recognised on completion.

In accordance with Statement of Standard Accounting Practice (SSAP) 19, 'Accounting for Investment Properties', no depreciation is provided in respect of freehold or long leasehold investment properties. This is a departure from the Companies Act 1985 which requires all properties to be depreciated. Such properties are not held for consumption but for investment and the directors consider that to depreciate them would not give a true and fair view. Depreciation is only one amongst many factors reflected in the annual valuation of properties and accordingly the amount of depreciation which might otherwise have been charged cannot be separately identified or quantified. The directors consider that this policy results in the accounts giving a true and fair view.

#### (iii) Depreciation

Depreciation is provided on operational assets, other than land, to write off the cost of the assets less estimated residual value, by equal instalments over their expected useful lives as follows:

#### Terminal complexes

Terminal building, pier and satellite structures	20–60 years
Terminal fixtures and fittings	5–20 years
Airport plant and equipment:	
- baggage systems	15 years
- screening equipment	7 years
- lifts, escalators and travelators	20 years
- Other plant and equipment, including runway lighting and building plant	5–20 years
Tunnels, bridges and subways	50–100 years

#### Airfields

Runway surfaces	10–15 years
Runway bases	100 years
Taxiways and aprons	50 years

#### Rail

Railways:	
- Rolling stock	8–40 years
- Tunnels	100 years
- Track metalwork	5–10 years
- Track bases	50 years
- Signals and electrification work	40 years

# BAA (SP) Limited

## 1 Accounting policies (continued)

### Fixed assets (continued)

#### Plant and Equipments

Motor vehicles	4–8 years
Office equipment	5–10 years
Computer equipment	4–5 years
Computer software	3–7 years

#### Other land and buildings

- Short leasehold properties	Over period of lease
------------------------------	----------------------

### Impairment of assets

The Group assesses, at each reporting date, whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. Where the asset does not generate cash flows that are independent of other assets, the recoverable amount of the income-generating unit to which the asset belongs is estimated. Recoverable amount is the higher of an asset's net realisable value and its value in use. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses of continuing operations are recognised in the profit and loss account in those expense categories consistent with the function of the impaired assets.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been change in the estimates used to determine the asset's recoverable amount since the latest impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. After such reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount less any residual value, on a straight-line basis over its remaining useful life.

### Capitalisation of interest

Interest payable is charged as incurred except where the borrowing finances tangible fixed assets in the course of construction. Such interest is capitalised once planning permission has been obtained and a firm decision to proceed has been taken until the asset is complete and ready for use. It is then charged to the profit and loss account as depreciation over the life of the relevant asset.

### Leases

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

#### (i) Group as lessor

Leases where the Group retains substantially all the risks and benefits of ownership are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying value of the leased asset and recognised over the lease term on the same basis as the income.

#### (ii) Group as lessee

Rental costs under operating leases are charged to the profit and loss account in equal annual amounts over the period of the lease.

### Stocks

Raw materials and consumables consist of engineering spares and other consumable stores and are valued at the lower of cost and net realisable value.

# BAA (SP) Limited

## 1 Accounting policies (continued)

### Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are measured at the best estimate of the expenditure required to settle the obligation at the balance sheet date and are discounted to present value where the effect is material.

### Deferred taxation

In accordance with FRS 19, 'Deferred Tax', deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax is not provided on timing differences arising from the revaluation of investment properties where there is no commitment to sell the asset.

Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

### Shared Services Agreement

All employees of BAA SP's airports are employed directly by BAA Airports Limited which also acts as the provider of corporate and administrative services to BAA (SP) Limited. BAA Airports Limited is the administrator of the related defined benefit and defined contribution pension plans and grant all employee benefits.

On 18 August 2008, the airports entered a Shared Services Agreement with BAA Airports Limited by which the latter becomes the shared services provider for the BAA (SP) Group's airports providing the airports with operational staff and corporate services.

#### *Operational staff*

BAA Airports Limited charges the airports for the provision of services in relation to staff costs, including wages and salaries, superannuation costs, medical costs and redundancy payments, as well as any other of its associated expenses properly incurred by the employees of BAA Airports Limited in providing the services. These costs include the cost of purchase of any shares in relation to share options granted and any hedging costs related to the employee share options. All of the amounts included in the abovementioned costs are settled in cash except for superannuation costs or costs related to hedging of share options, which are only settled when the cash outflow is requested by BAA Airports Limited.

#### *Corporate and centralised services*

BAA Airports Limited also provides centralised airport support including IT applications, general business services, procurement and financial accounting. These services are charged in accordance with the shared service agreement with a mark-up of 7.5% except for IT applications where full costs were recharged to the airports. The total mark-up charged to BAA SP's airports amounted to £8.9 million during the year (2007: £8.2 million).

#### *Pension costs*

Under the shared service agreement the current period service cost for the BAA Airports Limited pension schemes are recharged to the BAA (SP) Limited Group's airports. Cash contributions are made directly to the pension trustee of the BAA Airports Limited defined benefit scheme on behalf of BAA Airports Limited. The airports also have a legal obligation to fund any pension deficit related to BAA Airports Limited pension plans under the shared service agreement. In the period to 31 December 2008 an amount of £17 million has been recorded as a one-off exceptional past-service cost in the profit and loss account relating to unfunded pension schemes existing at BAA Airports Limited. However, these amounts will not be settled until the cash outflows are required by BAA Airports Limited and are accordingly recorded as long term provisions.

### Dividend distribution

A dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the shareholders' right to receive payment of the dividend is established by approval of the dividend at the Annual General Meeting. Interim dividends are recognised when paid.

# BAA (SP) Limited

## 1 Accounting policies (continued)

### Cash and liquid resources

Cash, for the purpose of the cash flow statement, comprises cash in hand and deposits repayable on demand, less overdrafts payable on demand.

Liquid resources are current asset investments which are disposable without curtailing or disrupting the business and are either readily convertible into known amounts of cash at or close to their carrying values or traded in an active market. Liquid resources comprise of term deposits less than one year (other than cash) and investments in money market managed funds.

### Classification of financial instruments issued by the Group

Following the adoption of FRS 25, financial instruments issued by the Group are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

- a) they include no contractual obligations upon the Company (or Group as the case may be) to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Company (or Group); and
- b) where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company's exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the Company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of interest payable and similar charges. Finance payments associated with financial instruments that are classified as part of shareholders' funds (see dividends policy), are dealt with as appropriations in the reconciliation of movements in shareholders' funds.

The Group is exempt from reporting information under FRS 29 as its intermediate parent, BAA Limited prepared group accounts in accordance with IFRS 7.

### Foreign currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Sterling, which is the parent's functional currency.

Transactions denominated in foreign currencies are translated into the functional currency of the entity using the exchange rates prevailing at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies are translated into Sterling at the rates of exchange ruling at the period-end. Differences arising on translation are charged or credited to the profit and loss account, except when deferred in equity as qualifying cash flow hedges. Translation differences on non-monetary items, such as equities classified as available-for-sale financial assets, are recognised in equity within the fair value reserve.

### Issue costs and arrangement fees

Immediately after issue debt is stated at the fair value of the consideration received on the issue of the capital instrument after deduction of issue costs. The finance cost of the debt is allocated to periods over the term of the debt at a effective interest on the carrying amount.

Issue costs are those that are incurred directly in connection with the issue of a capital instrument, that would not have been incurred had the instruments not been issued. These are accounted for as a deduction from the fair value of consideration received and amortised under the effective interest rate method.

Facility and arrangement fees resulting from the negotiation of finance that do not qualify as issue costs are written off to the profit and loss account as incurred.

# BAA (SP) Limited

## 1 Accounting policies (continued)

### Derivative financial instruments and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either:

- fair value hedges, where they hedge the exposure to changes in the fair value of the hedged asset or liability; or
- cash flow hedges, where they hedge the exposure to variability in cash flows that are either attributable to a particular risk associated with any changes in the fair value of the hedged asset, liability or forecasted transaction.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flow of hedged items.

The full fair value of a hedging derivative is classified a non-current asset or liability when the remaining hedged item is more than 12 months, and as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Derivatives that do not qualify hedge accounting are classified as a current asset or liability.

#### (a) Fair value hedge

Changes in the fair value in derivatives that are designated and qualify as fair value hedges are recorded in the profit and loss account, together with any changes in the fair value of the hedged assets or liability that are attributable to the hedged risk. The Group only applies fair value hedge accounting for hedging fixed interest rate risk on borrowings.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to profit or loss over the period to maturity.

#### (b) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit and loss account.

Amounts accumulated in equity are recycled in the profit and loss account in the periods when the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit and loss account. This accounting policy also relates to the scenario where by the forecast transaction is still expected to occur. When a forecast transactions is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the profit and loss account.

#### (c) Derivatives at fair value through profit or loss

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any of these derivatives instruments are recognised immediately in the profit and loss account.

When derivatives are designated in a fair value hedge or a cash flow hedge of interest rate risk, the net interest payable or receivable on those derivatives are recorded as net against the interest on the underlying hedged item in the profit and loss account. When derivatives are not in a hedge relationship the fair value changes on these derivatives are recognised within interest payable and other similar charges in the profit and loss account. The interest payable and receivable on those derivatives are recorded at their gross amount in interest payable and interest receivable in the profit and loss account.

In August 2008 as part of the BAA refinancing, a portion of the interest payable on some of the derivatives which were novated from BAA Limited and BAA Airports Limited was paid prior to novation to the BAA (SP) Group. The prepayment forms part of the fair value of these derivatives on their initial recognition in BAA (SP) Group.



# BAA (SP) Limited

## 1 Accounting policies (continued)

### Related party disclosures

The Company is ultimately owned in the UK by FGP Topco Limited, a company registered in England and Wales. The results of the Company are included in the audited consolidated financial statements of FGP Topco Limited for the year ended 31 December 2008. The results are also included in the audited consolidated financial statements of BAA (SH) Limited for the year ended 31 December 2008 (intermediate parent entity). They are also included in the audited consolidated financial statements of BAA Limited for the year ended 31 December 2008.

The Company is also exempt under the terms of FRS 8 'Related Party Disclosures' from disclosing related party transactions with entities that are related to, or part of the FGP Topco Limited Group. However, the transactions and balances in relation to the provision of services under the shared service agreement between the BAA SP Group and subsidiaries of the FGP Topco Group are disclosed in the notes to the financial statements.

### Significant accounting judgements and estimates

In applying the Group's accounting policies management have made estimates and judgements in a number of key areas. Actual results may, however, differ from the estimates calculated and management believe that the following areas present the greatest level of uncertainty.

#### White Paper

The UK Government's Aviation White Paper *'The Future of Air Transport'* ('the White Paper'), published on 16 December 2003, sets out the Government's policy for runway development in the UK. The Government chose a second runway at Stansted as its preferred location for the first new runway in the South East of England. The development of Stansted will be the subject of a planning inquiry, and the Group submitted its planning application to Uttlesford District Council on 11 March 2008. The costs incurred to date have been capitalised as part of the runway development costs. This is based on management's belief that it is virtually certain the necessary consents will be received and the project will be developed to achieve a successful delivery of an asset such that future benefits will flow to the Group.

Additionally, the Group has promoted three voluntary schemes to compensate those people living near Stansted Airport, whose homes will be affected by the airport expansion. These costs have also been capitalised as part of the runway development costs.

#### Investment properties

Investment properties were valued at a fair value at 31 December 2008 by Drivers Jonas, Chartered Surveyors, Strutt and Parker, Chartered Surveyors and King Sturge, Valuers and Surveyors. These valuations were prepared in accordance with UK GAAP and the appraisal and valuation manual issued by the Royal Institution of Chartered Surveyors. Valuations were carried out having regard to comparable market evidence. In assessing fair value, current and potential future income (after deduction of non-recoverable outgoings) has been capitalised using yields derived from market evidence. Approximately 70 percent of the Investment properties comprise car parks and airside assets at the Group's airports and these are considered less vulnerable to market volatility than the overall market. Given recent market conditions and the decline in property prices, for the year ended 31 December 2008, independent valuations have been obtained for 100 percent of the Investment properties.

#### Taxation

Provisions for tax contingencies require management to make judgements and estimates in relation to tax issues and exposures. Amounts provided are based on management's interpretation of country specific tax law and the likelihood of settlement. Tax benefits are not recognised unless the tax positions are probable of being sustained. In arriving at this position, management reviews each material tax benefit to assess whether a provision should be taken against full recognition of the benefit on the basis of potential settlement through negotiation and/or litigation. All such provisions are included in current tax liabilities.

#### Hedge accounting

From 1 October 2008, certain interest rate swaps for £1.9 billion notional were designated in a cash flow hedge relationship to hedge the exposure to variability in cash flows of existing liabilities and forecast transactions, based on management expectation that it is highly probable these derivatives will match future sterling funding issuances which will occur to refinance existing debt. In 2008, £301 million of fair value losses on these derivatives, arising from a reduction in UK interest rates have been recognised in the cash flow hedge reserve.

Management assesses on a regular basis the extent to which terms of future financing are expected to match the profiles of the hedges, and adjusts the accounting accordingly. Any such change in the expected financing may require the recycling of the cash flow hedge reserve through the profit and loss account.

# BAA (SP) Limited

## 2 Segment information

The Group's primary reporting format is business segments. The operating businesses are primarily the individual airports, which are organised and managed separately.

The 'other entities' business segment includes Heathrow Express Operating Company (HEX), BAA Funding Limited, BAA (AH) Limited and the parent entity BAA (SP) Limited.

	Turnover <sup>1</sup>		Operating profit		Net Assets	
	Year ended 31 December	Year ended 31 December	Year ended 31 December	Year ended 31 December	Year ended 31 December	Year ended 31 December
	2008	2007	2008	2007	2008	2007
	£m	£m	£m	£m	£m	£m
Heathrow <sup>2 3</sup>	1,568	1,324	175	278	1,459	1,968
Gatwick	465	410	104	81	904	1,036
Stansted	259	242	81	76	1,012	1,152
Other entities <sup>4</sup>	-	-	4	-	(757)	-
Other adjustments	-	-	-	-	(1,480) <sup>5</sup>	(1,600) <sup>6</sup>
	<b>2,292</b>	<b>1,976</b>	<b>364</b>	<b>435</b>	<b>1,138</b>	<b>2,556</b>

<sup>1</sup> All turnover originated in the UK.

<sup>2</sup> All rail income and associated costs are included in Heathrow.

<sup>3</sup> This amount excludes £8 million inter-company revenue received from HEX as it is eliminated at Heathrow Airport Limited level since HEX was acquired by Heathrow Airport Limited during the year.

<sup>4</sup> Other entities are Heathrow Express Operating Company Limited, BAA Funding Limited, BAA (AH) Limited and BAA (SP) Limited.

<sup>5</sup> Relates to elimination of inter-company transactions and consolidation adjustments.

<sup>6</sup> Relates to the BAA (SP) Limited Debenture which has been treated as if it had been issued in the prior year as a result of the application of merger accounting.

### Reconciliation of Adjusted EBITDA<sup>1</sup> and Operating profit

For the year ended 31 December 2008	Adjusted EBITDA <sup>1</sup>	Exceptional items <sup>2</sup>	Depreciation	Operating Profit
	£m	£m	£m	£m
Heathrow	635	(114)	(346)	175
Gatwick	159	9	(64)	104
Stansted	117	(3)	(33)	81
Other entities	5	-	(1)	4
	<b>916</b>	<b>(108)</b>	<b>(444)</b>	<b>364</b>
For the year ended 31 December 2007	Adjusted EBITDA <sup>1</sup>	Exceptional items <sup>2</sup>	Depreciation	Operating Profit
	£m	£m	£m	£m
Heathrow	636	(154)	(204)	278
Gatwick	154	(17)	(56)	81
Stansted	114	(9)	(29)	76
	<b>904</b>	<b>(180)</b>	<b>(289)</b>	<b>435</b>

<sup>1</sup> Adjusted EBITDA has been used to provide clearer indication of the performance of the individual airports and to assist better comparison with the prior year. Adjusted EBITDA is earnings before interest, tax, depreciation, amortisation and exceptional items.

<sup>2</sup> Includes only exceptional items within operating profit

# BAA (SP) Limited

## 3 Operating costs - ordinary

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
Operating costs		
Staff costs <sup>1</sup>		
Wages and salaries	(343)	(268)
Social security	(27)	(21)
Pensions	(50)	(53)
Other staff related	(21)	(17)
Share Based Payments	(4)	(2)
	<b>(445)</b>	<b>(361)</b>
Retail expenditure	(37)	(23)
Depreciation	(444)	(289)
Maintenance expenditure	(170)	(125)
Rent and rates	(130)	(100)
Utility costs (including distribution fees)	(120)	(103)
Police	(55)	(47)
General expenses <sup>2</sup>	(148)	(59)
Air navigation charges <sup>3</sup>	(61)	-
Other intra - group charges <sup>4</sup>	(209)	(253)
Loss on disposal of tangible fixed assets	(1)	(1)
<b>Total operating costs - ordinary</b>	<b>(1,820)</b>	<b>(1,361)</b>

<sup>1</sup> Staff costs includes recharges from BAA Airports Limited for employee services to BAA (SP) Limited Group. Refer to Shared Services Agreement accounting policy in note 1.

<sup>2</sup> Increased in general expenses mainly contributed by £13 million in cleaning, £14 million in services quality rebates and £10.1 million and £10.5 million for noise and blight and connect/baggage respectively.

<sup>3</sup> During the year, National Air Traffic Services ceased billing the airlines for the aircraft handling within the airports landing and departure zone and now billed Heathrow Airport Limited, Gatwick Airport Limited and Stansted Airport Limited directly.

<sup>4</sup> This amount includes all costs in relation to the corporate and centralised services under the Shared Service Agreement (refer to Note 1 for detail). The reduction in other intra-group charges during the year is mainly due to the elimination of intra-group charges made by HEX as it became part of the Group during the year. Intra-group charges made by HEX in the prior year were £55 million.

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>Operating costs include:</b>		
Rentals under operating leases		
- Plant and machinery	37	31
- Other operating leases	18	11
Services provided by the Group's auditor		
- Fee payable for the audit	0.3	0.2
- tax advisory work	-	0.1

Services provided by the auditors in relation to the wider BAA Group's refinancing were borne by BAA Limited (formerly Airport Development and Investment Limited).

# BAA (SP) Limited

## 4 Employee information and Directors' emoluments

### Employee numbers

The Company has no employees. However, all staff costs for BAA SP airports are borne by BAA Airports Limited which recharges all such costs directly to the airports. Previously this was included in a management charge.

The average number of employees of BAA Airports Limited engaged in the operation of three London airports during the year was 9,308 (31 December 2007: 7,600 ).

### Directors' Remuneration

None of the directors who served BAA (SP) Limited during the year received emoluments for services to the Company.

During the year, one of the directors (31 December 2007: one) had retirement benefits accruing to them under the BAA Airports Limited's defined benefits scheme.

## 5 Exceptional items

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>Operating items</b>		
Pension cost (a)	(17)	-
Reorganisation income/(costs) (b)	15	(69)
Heathrow Terminals 1 and 2 accelerated depreciation (c)	(84)	(66)
Heathrow Terminal 5 launch / operational readiness costs (d)	(22)	(45)
	<b>(108)</b>	<b>(180)</b>
<b>Interest payable and similar charges</b>		
Refinancing fees written off (e)	(143)	-
<b>Total exceptional items before income tax</b>	<b>(251)</b>	<b>(180)</b>
Tax credit on exceptional items	48	33
<b>Total exceptional items</b>	<b>(203)</b>	<b>(147)</b>

(a) £17 million (31 December 2007: £nil) of accumulated past service pension costs not previously charged to the Group by BAA Airports Limited in relation to Unfunded Retirement Benefit Scheme and Post Retirement Medical Benefits were incurred during the year. The Group's share of these costs have been allocated on the basis of earnings before interest, tax, depreciation and amortisation for the year ended 31 December 2008.

(b) A release of £15 million was credited during the year associated with restructuring programmes (2007: charge of £69 million). The amount released resulted from higher staff turnover than historic experience, lower than expected cost for each reduction in headcount and certain headcount reduction not being made due to the decision to sell Gatwick. The charge in the year ended 31 December 2007 was in relation to severance and pension payments associated with the 'Simplifying the Organisation' programme carried out during 2008-2009.

(c) With the anticipated development of Terminal 2A, Terminals 1 and 2 at Heathrow airport will be demolished necessitating an additional depreciation charge of £84 million in the year to 31 December 2008 (2007: £66 million) to reflect the shortened useful lives of the assets.

(d) Operational readiness costs of £22 million (2007: £45 million) relating to management of the opening of Heathrow Terminal 5 were incurred during the year

(e) Fees of £143 million (31 December 2007: £nil) were incurred during the year, in relation to facility and arrangement fees that are expensed under UK GAAP. These costs are mainly upfront fees paid for the capital expenditure, working capital, liquidity, initial credit facility and costs attributed to future bond issuance. For further details of the borrowing facilities see Note 16.

# BAA (SP) Limited

## 6 Interest receivable and interest payable and similar charges

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>6(a) Interest receivable</b>		
Interest receivable on derivatives not in a hedging relationship	84	-
Interest receivable from other group undertakings <sup>1</sup>	26	39
Interest on money market and bank deposits	1	-
<b>Interest receivables</b>	<b>111</b>	<b>39</b>
<b>6(b) Interest payable and similar charges</b>		
Interest on borrowings		
Bonds and related hedging instruments	(116)	-
Bank loans and overdrafts and related hedging instruments	(150)	-
Interest payable on derivatives not in a hedging relationship	(53)	-
Facility fees	(13)	-
Interest on BAA (SP) Limited debenture	(145)	-
Interest payable to other group undertakings <sup>1</sup>	(338)	(512)
Provisions: Terminal 5 land purchase and Cross Border Lease	(15)	(5)
	<b>(830)</b>	<b>(517)</b>
<b>Fair value gain/(loss) on financial instruments</b>		
Interest rate swaps: cash flow hedges*	(24)	-
Interest rate swaps: not in hedge relationship	(26)	-
Index linked swaps: not in hedge relationship	81	-
Cross currency interest rate swaps: cash flow hedges*	35	-
Fair value re-measurements of foreign currency balances	8	-
	<b>74</b>	<b>-</b>
<b>Interest capitalised</b>	<b>100</b>	<b>256</b>
<b>Interest payable and similar charges - ordinary</b>	<b>(656)</b>	<b>(261)</b>

\* Hedge ineffectiveness on derivatives in a hedge relationship.

<sup>1</sup> These amounts relate to interest accrued on balances due from/to BAA Airports Limited prior to refinancing in August 2008. Refer to notes 11 and 14 for details.

Borrowing costs included in the cost of qualifying assets (i.e. capitalised borrowing costs) arose on the general borrowing pool and are calculated by applying an average capitalisation rate of 6.92% (31 December 2007: 5.95%) to expenditure incurred on such assets.

# BAA (SP) Limited

## 7 Tax on profit on ordinary activities

Analysis of charge in period

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>Current tax</b>		
Current tax at 28.5% (31 December 2007 30%)	(43)	52
Adjustments in respect to prior years	(19)	(29)
	<b>(62)</b>	<b>23</b>
<b>Deferred tax</b>		
Origination and reversal of timing differences	(52)	42
Release of prior year deferred tax relating to Industrial Building Allowances	-	(171)
Adjustments in respect to prior years	(9)	-
Change in tax rate – impact on deferred tax assets and liabilities	-	(53)
Tax credit on (loss)/profit on ordinary activities	<b>(123)</b>	<b>(159)</b>

### Reconciliation of tax charge

The standard rate of current tax for the year, based on the UK standard rate of corporation tax is 28.5% (31 December 2007:30%). The actual tax charge for the current period and prior period differs from the standard rate for the reasons set out in the following reconciliation:

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
(Loss)/profit on ordinary activities before tax	(324)	213
Tax calculated at the UK statutory rate of 28.5%; 2007 (30%)	(92)	64
Effect of:		
Permanent differences	(3)	2
Non taxable income	(1)	(1)
Depreciation for the year in excess of capital allowances	114	60
Capitalised interest	(28)	(71)
Impact of change in tax rate	(1)	(1)
Other short term timing differences	(32)	(1)
Adjustments in respect of deferred income tax of previous periods	(19)	(29)
<b>Current tax (credit)/charge for the year</b>	<b>(62)</b>	<b>23</b>

The standard rate of Corporation Tax in the UK changed from 30% to 28% with effect from 1 April 2008. Accordingly, the Group's loss for this accounting period are taxed at an effective rate of 28.5% and will be taxed at 28% in the future.

Other than this change, and the unprovided deferred tax discussed in Note 18, there are no items which would materially affect the future tax charge.

The accounting impact of the abolition of IBA's in the financial statements of BAA (SP) Group, prepared under UK GAAP, is significantly different to that disclosed in the consolidated financial statements of BAA Limited, which were prepared under IFRS. Under UK GAAP, the accounting impact of the abolition of IBA's resulted in a release of a deferred tax liability of £171 million in the year ended 31 December 2007.

The cash impact of the abolition of IBAs on the Group in 'quinquennium 5' is not material due to the transitional period regime applicable to 2011 and the low taxable income base of the Group. The impact of the abolition on future periods is uncertain due to the potential regulatory change to a post-tax allowed return (as is the case in other regulated industries). Under the existing regulatory framework, and assuming no further changes, the present value on the reduced cash flows for the existing assets would be approximately £370 million.

# BAA (SP) Limited

## 8 Dividends paid or proposed

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
<b>Equity dividends declared and paid during the year</b>		
Interim dividends paid (see below)	705	121
Final dividend paid (see below)	-	30
	<b>705</b>	<b>151</b>

The Company paid an interim dividend of 13.4p (2007: Nil) per ordinary share, amounting to £705 million on 18 August 2008. Prior year dividend payment relates to payment made by Heathrow Airport Limited, Gatwick Airport Limited and Stansted Airport Limited to their previous immediate parent entity amounting to £151 million.

# BAA (SP) Limited

## 9 Tangible fixed assets

	Investment properties £m	Land held for development £m	Terminal complexes £m	Airfields £m	Rail assets £m	Group occupied assets £m	Plant, equipment and other assets £m	Assets in the course of construction £m	Total £m
<b>Cost or valuation</b>									
Balance 1 January 2008	2,591	150	4,714	970	679	75	459	5,628	15,266
Additions	-	-	9	-	-	-	3	1,004	1,016
Transfers to completed assets	256	-	3,747	329	686	21	128	(5,167)	-
Interest capitalised	-	-	-	-	-	-	-	100	100
Disposals	-	-	(4)	-	(8)	-	(2)	-	(14)
Inter company transfers	-	-	-	-	-	-	(1)	23	22
Revaluation	(154)	(36)	-	-	-	-	-	-	(190)
Revaluation adjustment (Note 20)	-	-	-	-	-	(2)	-	-	(2)
<b>Balance 31 December 2008</b>	<b>2,693</b>	<b>114</b>	<b>8,466</b>	<b>1,299</b>	<b>1,357</b>	<b>94</b>	<b>587</b>	<b>1,588</b>	<b>16,198</b>
<b>Depreciation</b>									
Balance 1 January 2008	-	-	(2,003)	(247)	(182)	(24)	(317)	-	(2,773)
Charge	-	-	(386)	(43)	(36)	(4)	(58)	-	(527)
Disposals	-	-	3	-	8	-	1	-	12
<b>Balance 31 December 2008</b>	<b>-</b>	<b>-</b>	<b>(2,386)</b>	<b>(290)</b>	<b>(210)</b>	<b>(28)</b>	<b>(374)</b>	<b>-</b>	<b>(3,288)</b>
<b>Net book value 31 December 2008</b>	<b>2,693</b>	<b>114</b>	<b>6,080</b>	<b>1,009</b>	<b>1,147</b>	<b>66</b>	<b>213</b>	<b>1,588</b>	<b>12,910</b>
Net book value 31 December 2007	2,591	150	2,711	723	497	51	142	5,628	12,493



# BAA (SP) Limited

## 9 Tangible fixed assets (continued)

### Valuation

Investment properties and land held for development were valued at open market value at 31 December 2008 by Drivers Jonas, Chartered Surveyors at £2,805 million and by Strutt & Parker, Chartered Surveyors at £12 million, resulting in a total valuation of £2,817 million. These valuations were prepared in accordance with the Appraisal and Valuation Manual issued by the Royal Institution of Chartered Surveyors taking account, inter alia, of planning constraints and reflecting the demand for airport related uses. As a result of the valuation, a deficit of £190 million has been recognised in the revaluation reserve.

Remaining group occupied properties, terminal complexes, airfield infrastructure, plant and equipment, and other assets, have been shown at historical cost.

### Capitalised interest

Included in the cost of assets after depreciation are interest costs of £1,037 million (31 December: £980 million). £100 million (31 December 2007: £256 million) has been capitalised in the period at a capitalisation rate of 6.92% (31 December 2007: 5.95%) based on a weighted average cost of borrowings.

Capitalised interest of £96 million has been treated as tax deductible in the period. Subsequent depreciation of the capitalised interest is disallowed for tax purposes, consequently, the capitalised interest gives rise to a deferred tax liability, which is released each year in line with the depreciation charged on the relevant assets.

### Historical cost

The historical cost of investment properties and land held for development at 31 December 2008 was £784 million (31 December 2007: £514 million).

### BAA Group occupied properties

Group occupied properties are freehold except for certain short leasehold properties with a net book value at 31 December 2008 of £20 million (31 December 2007: £17 million).

### Assets in the course of construction

Assets in the course of construction include £167 million (31 December 2007: £129 million) in respect of the development of a second runway and related infrastructure at Stansted Airport. The costs consist of £79 million (31 December 2007: £63 million) incurred in respect of the initial planning application preparation and £88 million (31 December 2007: £66 million) in respect of the purchase of domestic properties that fall within the expanded airport boundary. This includes a provision of £5 million (31 December 2007: £4 million) for the additional 10% payable under the Home Value Guarantee Scheme (HVGS) once planning permission has been obtained. Assets in the course of construction also includes the second satellite under construction for Terminal 5 (T5C), the future satellite for Terminal 2 as well as Terminal 4 Extension and Terminal 3 refurbishment, amongst others.

### Land acquisition

Tangible fixed assets includes £179 million (31 December 2007: £179 million) for the acquisition of land for the construction of Terminal 5. The operational assets employed by the vendor of this land have been relocated and the acquisition cost represents the present value of the estimated deferred payments to be made over a period of 35 years from the date of acquisition to the vendor in compensation for relocation. The present value of the outstanding deferred consideration is included within provisions in the balance sheet (Note 18).

### Security

BAA Airports Limited granted security over the Company's assets as disclosed in BAA Airports Limited (formerly BAA Limited) Group's report and accounts as at 31 December 2007. Subsequent to the completion of the refinancing transactions the securities were released and transferred to other group companies. Details of these are provided in Note 16.

# BAA (SP) Limited

## 9 Tangible fixed assets (continued)

### Leased assets

The Group has assets rented to third parties under operating leases as follows:

	As at 31 December 2008 £m	As at 31 December 2007 £m
Cost or valuation	3,475	3,109
Accumulated depreciation	(195)	(184)
<b>Net book amount</b>	<b>3,280</b>	<b>2,925</b>

A significant proportion of freehold property is occupied by third parties under concession and management agreements.

## 10 Stocks

	As at 31 December 2008 £m	As at 31 December 2007 £m
Raw materials and consumables	8	8

The replacement cost of raw materials and consumables at 31 December 2008 and 31 December 2007 was not materially different than the amount at which they are included in the accounts.

## 11 Debtors

	As at 31 December 2008 £m	As at 31 December 2007 £m
<b>Due within one year:</b>		
Trade debtors	248	166
Less: Provision for impairment	(9)	(3)
Trade receivables – net	239	163
Prepayments	34	28
Other debtors	42	33
Amount owed by group undertakings <sup>1</sup>	65	569 <sup>2</sup>
Group relief receivable	22	-
	402	793
<b>Due after more than one year</b>		
Loan to group undertakings	-	574 <sup>2</sup>
<b>Total debtors</b>	<b>402</b>	<b>1,367</b>

<sup>1</sup> Amount owed by group undertakings largely relates to external payments received by BAA Airports Limited under the Shared Service Agreement on behalf of BAA SP's airports that will be remitted to the airports in due course. This amount is repayable on demand and accrue interest at Bank of England base rate +1.5%.

<sup>2</sup> These amounts were fully settled on refinancing in August 2008. Refer to Note 6 for interest accrued on the balance during the current year prior to settlement.

# BAA (SP) Limited

## 12 Current assets investment

	As at 31 December 2008 £m	As at 31 December 2007 £m
Short term deposits	157	-

Board approved investment policies and relevant debt facility agreements provide counterparty investment limits based on short and long term credit ratings. Of these deposits, counterparties with a short term credit rating of A-1+ held assets of £40 million and A-1 held assets of £117 million as at 31 December 2008.

## 13 Cash at bank and in hand

	As at 31 December 2008 £m	As at 31 December 2007 £m
Cash at bank and in hand	25	-

Cash at bank and in hand earns interest at floating rates based on daily bank deposit rates and is subject to interest rate risk.

## 14 Creditors: amount due within one year

	As at 31 December 2008 £m	As at 31 December 2007 £m
Deferred income	55	37
Interest accruals	171	1
Trade creditors	146	142
Corporation tax	10	10
Other tax and social security	9	-
Group relief payable	-	52
Other creditors	15	11
Amount owed to group undertakings <sup>1</sup>	39	-
Capital creditors	252	269
Borrowing (refer note 16)	43	8,229 <sup>2</sup>
Derivative financial instruments (refer to Note 17)	324	-
	<b>1,064</b>	<b>8,751</b>

<sup>1</sup> Amount owed to group undertakings largely relates to external payments made by BAA Airports Limited under the Shared Service Agreement on behalf of BAA SP's airports.

<sup>2</sup> This amount was fully settled on refinancing in August 2008. Refer to Note 6 for interest accrued on the balance during the current year prior to settlement.

Trade payables are non-interest bearing and are generally on 30-day terms.

# BAA (SP) Limited

## 15 Creditors: amount due after more than one year

	As at 31 December 2008 £m	As at 31 December 2007 £m
Deferred income	7	16
Borrowings (refer to Note 16)	11,365	1,813
Derivatives financial instruments	342	-
	<b>11,714</b>	<b>1,829</b>

## 16 Borrowings

	As at 31 December 2008 £m	As at 31 December 2007 £m
<b>Current borrowings</b>		
Amount owed to group undertakings	-	7,030
Intercompany loans	-	1,199
Secured bank loans - EIB	43	-
<b>Total current borrowings (excluding interest payable)</b>	<b>43</b>	<b>8,229</b>
<b>Non-current borrowings</b>		
Secured		
Senior Refinancing Facility	3,341	-
Junior Refinancing Facility	982	-
Initial Credit Facility	250	-
Bank loans - EIB	372	-
BAA Funding Limited bonds:		
3.975% €1,000 million due 2012	893	-
5.850% £400 million due 2013	363	-
4.600% €750 million due 2014	656	-
12.450% £300 million due 2016	387	-
4.600% €750 million due 2018	628	-
9.200% £250 million due 2021	287	-
5.225% £750 million due 2023	606	-
7.075% £200 million due 2028	197	-
6.450% £900 million due 2031	837	-
<b>Total BAA Funding Limited bonds</b>	<b>4,854</b>	<b>-</b>
Unsecured:		
BAA (SP) Limited debenture payable to BAA (SH) Limited	1,566	1,600 <sup>1</sup>
Amount owed to group undertakings	-	213
<b>Total non-current borrowings</b>	<b>11,365</b>	<b>1,813</b>
<b>Total current and non-current borrowings (excluding interest payable)</b>	<b>11,408</b>	<b>10,042</b>

<sup>1</sup> Relates to the BAA (SP) Limited Debenture which has been treated as if it had been issued in the prior year as a result of the application of merger accounting.

# BAA (SP) Limited

## 16 Borrowings (continued)

### BAA Funding bonds

In August 2008, as part of the BAA Limited refinancing, the bonds previously issued by BAA Airports Limited (formerly BAA Limited) were cancelled and replaced by new bonds issued by BAA Funding Limited.

The BAA Funding Limited bonds were recognised at initial fair value and then subsequently carried at amortised cost using the effective interest rate method. In August 2008, as part of the wider BAA refinancing, fees of £44 million were incurred and these have been included in the carrying value of the bonds above. Bonds are carried at amortised cost using the effective interest rate method and the carrying value includes amortised transaction costs, premiums and discounts. The effective interest rate on the bonds varies between 6.28% and 7.75%.

The dates listed above correspond to the maturity dates of the loans between the airport operating company of Heathrow Airport Limited and the funding vehicle, BAA Funding Limited. Failure to repay these loans on their maturity date will be an event of default allowing BAA Funding Limited to take action under its loan agreement, such as appointing an administrative receiver to Heathrow Airport Limited.

The bonds issued by BAA Funding Limited will have a legal maturity date two-years after the maturity date of its corresponding loan with Heathrow Airport Limited. If Heathrow Airport Limited fail to repay their loans to BAA Funding Limited on their maturity date then the corresponding bond of BAA Funding Limited will not be in default for at least another two years during which time the relevant bond will have a floating interest rate of Libor plus 4%.

Interest and principal payments on all Euro bonds are swapped to fixed Sterling payments through cross-currency and interest rate swaps. All BAA Sterling bonds bear fixed rate coupons.

Bonds issued under the £4.5 billion European Medium Term Note programme totalled £3,603 million. The carrying value of these bonds was £3,907 million as at 31 December 2008.

### Refinancing Facilities

In August 2008 as part of the BAA refinancing, £3,400 million Senior refinancing facility and £1,000 million Junior refinancing facilities were drawn by Heathrow Airport Limited, Gatwick Airport Limited and Stansted Airport Limited (the "Borrowers"), in order to repay the Senior Facilities as discussed below. These facilities have the following partial maturities of £1 billion in 2010, £1 billion in 2011, £1 billion in 2012 and £1.4 billion in 2013.

The interest on these facilities is based on Libor with a margin of 2.00% on the Senior Facility and 2.75% on the Junior Facility as at 31 December 2008. The interest rate decreases with the facility balances based on the following thresholds:

Senior Facility		Junior Facility	
Less than £1,200 million	1.25%	Less than £330 million	2.00%
Between £1,200 million and £3,200 million	1.50%	Between £330 million and £660 million	2.50%
Between £2,200 million and £3,200 million	1.75%	Greater than £660 million	2.75%
Greater than £3,200 million	2.00%		

In addition, the contractual margin step ups on the margin are 0.25% in August 2010 and 0.25% each six months thereafter, provided that the aggregate increase and the margin shall be limited to 1.50% per annum.

The repayment of the Senior Refinancing Facility and Junior Refinancing Facility (regardless of where the facility is held within the BAA SP Group) is based on the terms of the Refinancing Facility Agreement. This agreement requires repayment of the facilities firstly applied in repayment of the Initial Credit Facility to ensure the required capex headroom is met, then applied to Refinancing Facilities with a maturity date falling within 12 months of the date of prepayment and then applied to Refinancing Facilities in descending order of the final maturity date, until the Senior net indebtedness to total Regulated Asset Base ('RAB') is more than or equal to 0.70 and the Junior net indebtedness to total RAB is more than or equal to 0.85. Any remaining proceeds are then applied to Refinancing Facilities in ascending order of the final maturity date. On disposal of Gatwick, 100% of the net proceeds are expected to be set against the Refinancing Facility.

The balance of the designated group Initial Credit Facility used to fund capital expenditure as at 31 December 2008 was £250 million. The interest rate on this facility is based on Libor with a margin of 2.00% as at 31 December 2008. The contractual margin step ups on the margin are 0.25% in August 2010 and 0.25% each six months thereafter provided that the aggregate increase in the margin shall be limited to 1.50% per annum. If there is no balance outstanding on the Refinancing Facility the margin shall be 1.00%.

# BAA (SP) Limited

## 16 Borrowings (continued)

### Other Borrowings

Secured bank loans comprise £417 million (excluding capitalised debt costs) of European Investment Bank ('EIB') facilities split between current and non-current. The EIB facilities amortise over the period to 2019. The interest rate on these facilities is predominately floating, except for £13 million EIB principal which is fixed at 6.21%.

### BAA (SP) Limited Debenture payable to BAA (SH) Limited

The BAA (SP) Limited Debenture was issued in January 2008 to BAA Airports Limited. On refinancing in August 2008, £34.2 million was repaid and the remaining balance novated from BAA Airports Limited to BAA (SH) Limited. The current balance payable from BAA (SP) Limited to BAA (SH) Limited is used to generate interest payment to BAA (SH) Limited in order to pay the external interest on the Subordinated Facility. The interest on the BAA (SP) Limited Debenture is 0.01% above the rate of the Subordinated Facility, and has a final redemption date of May 2011.

### Amount owed to group undertakings and other intercompany loans

The amount owed to group undertakings of £7,030 million and £213 million as at 31 December 2007 accrued interest at Bank of England base rate +1.5%. The intercompany loan of £1,199 million as at 31 December 2007 were loans payable to BAA Airports Limited and London Airports 1992 Limited with fixed rates of between 5.75% to 6.58%. These loans were all settled in full as part of the refinancing in August 2008.

### Fair value of borrowings:

	As at 31 December 2008	
	Book value	Fair value
	£m	£m
Long term debt	11,365	10,232
	<b>11,365</b>	<b>10,232</b>

The fair value of short-term borrowings approximates book value. Accrued interest is included as a current borrowings balance and not in the carrying amount of non-current borrowings. The fair values of listed borrowings are based on quoted prices. For unlisted borrowings, the Group establishes fair values by using valuation techniques such as discounted cash flows analysis. The fair value of on current borrowings which have floating rate interest are assumed to equate to their current nominal value.

### Covenants

The BAA Funding bonds, Refinancing Facilities and the Initial Credit Facilities are required to comply with the covenants under the Common Terms Agreement (CTA) within the designated group. There are certain covenant threshold requirements under the CTA which must be maintained.

		Forecasting Event	Trigger Event	Financial Covenant <sup>1</sup>
Senior Interest Cover Ratio	to be greater than	1.60	1.40	1.05
Junior Interest Cover Ratio	to be greater than	1.40	1.20	-
Senior Net Indebtedness to Total RAB (RAR)	to be less than	0.70	0.70	0.925
Junior Net Indebtedness to Total RAB (RAR)	to be less than	0.85	0.85	-

<sup>1</sup> Three year period average for Interest Cover Ratio from the three year period ending 31 December 2012.

Following the occurrence of a Trigger Event (as defined above) which is continuing, the Obligors are prohibited from making certain payments ("Restricted Payments"), mainly in relation to payments in respect of subordinated debt and payments to other BAA group companies outside of the security group, and are obliged to make repayments of amounts outstanding under the senior debt facilities of the security group, equivalent to the amount of restricted payments that would otherwise have been made.

Following the occurrence of a Forecasting Event (as defined above) which is continuing, the Investor Report issued under the CTA shall disclose information of all forward looking ratios until the end of the current regulatory period, rather than just the 12 month forward looking ratio. In addition, the Investor Report and Compliance Certificate issued under the CTA shall disclose the forecasted restricted payments which are to be made within the 90 days commencing from the delivery of such report.

All covenants have been tested and complied with as at 31 December 2008. Additional disclosures on risk management and hedging of borrowings are included in Notes 17.

# BAA (SP) Limited

## 16 Borrowings (continued)

### Securities and guarantees

Heathrow Airport Limited, Gatwick Airport Limited, Stansted Airport Limited, Heathrow Express Operating Company Limited, BAA (SP) Limited and BAA (AH) Limited (together, the Obligors) have granted security over their assets to secure their obligations to the Borrower Secured Creditors under the August 2008 refinancing documents and to the Subordinated Creditors (at BAA (SH) Limited) under the Subordinated Facility Agreement dated April 2006. Each Obligor has also provided a guarantee in respect of the obligations of the other Obligors.

BAA Pension Trustee Company Limited (the BAA Pension Trustee) is a Borrower Secured Creditor and has a right to receive up to £300 million out of the proceeds of enforcement of the security granted by the Obligors, such right ranking *pari passu* with the Class A creditors of the Obligors.

BAA Airports Limited (formerly BAA Limited) has provided a guarantee to the Deutsche Trustee Company Limited (the Bond Trustee) for itself and on behalf of the BAA Guaranteed Bondholders in respect of bonds with a final legal maturity of no later than 2018 issued by BAA Funding Limited which is held at the immediate parent entity of BAA SP for £1.566 billion with maturity in 2011.

BAA Funding Limited has provided security to the Bond Trustee (as trustee for the Issuer Secured Creditors).

BAA (DSH) Limited (intermediate parent entity of BAA (SP) Limited) and its subsidiaries (other than BAA Funding Limited and Heathrow Airport Community Board insulation Limited), plus ADI Finance 2 Limited, BAA Limited, BAA Airports Holdco Limited and BAA Airports Limited are guarantors under the Subordinated Facility Agreement. All the guarantors, apart from ADI Finance 2 Limited, are party to transaction security which secures liabilities arising under the Subordinated Facility Agreement.

Heathrow Airport Limited, Gatwick Airport Limited, Stansted Airport Limited and Heathrow Express Operating Company Limited have provided a guarantee in favour of The Royal Bank of Scotland plc as Borrower Account Bank in respect of the liabilities of those companies under the Borrower Account Bank Agreement.

### Liquidity

As at 31 December 2008, the Group had cash and liquid resources of £182 million (31 December 2007: nil) and undrawn committed facilities of £2,500 million (31 December 2007: nil).

## 17 Derivative Financial Instruments

2008	Notional £m	Assets £m	Liabilities £m	Total £m
<b>Current</b>				
Forward foreign exchange contracts - no hedge accounting	45	7	-	7
Interest rate swaps – no hedge accounting	200	-	(12)	(12)
Index-linked interest rate swaps – no hedge accounting	2,206	131	(312)	(181)
Interest rate swaps – cash flow hedge	-	-	-	-
	2,451	138	(324)	(186)
<b>Non-current</b>				
Interest rate swaps – cash flow hedge	4,226	72	(342)	(270)
Cross-currency swap – cash flow hedge	1,703	758	-	758
	5,929	830	(342)	488
<b>At 31 December 2008</b>	<b>8,380</b>	<b>968</b>	<b>(666)</b>	<b>302</b>

Any derivatives that are not in qualifying hedge relationships at the reporting date are presented as current irrespective of their maturities.

As part of the BAA refinancing in August 2008, some of the derivatives previously held at BAA Airports Limited (formerly BAA Limited) and BAA Limited (formerly Airport Development and Investment Limited) were novated into the Group.

# BAA (SP) Limited

## 17 Derivative Financial Instruments (continued)

### Interest rate swaps

The fixed interest rates on the swaps vary from 4.7% to 5.5%. The floating rates for all interest rate swaps are based on three and six month Libor rates. In 2008 a £24 million loss was recognised in the profit and loss account due to ineffectiveness in relation to cash flow hedge relationship. In addition a £26 million loss was recognised in the profit and loss account in relation to the swaps that did not qualify for hedge accounting during the period.

During the period, swaps with a notional principal of £1,813 million were designated as cash flow hedge against interest rate risk on the Group's backstop facility effective 1 October 2008. A £13 million loss was recognised in the profit and loss account in relation to these swaps during the period in which the swaps did not qualify for hedge accounting.

In addition to the novated swaps, new interest rate swaps with notional amount totalling £113 million were also taken out during the period. These swaps, together with the £400 million notional amount of interest rate swaps have been designated as a cash flow hedges against currency and interest rate risk on the €750 million bond due 2014 in conjunction with a cross currency swap (see below). The fixed interest rates vary from 5.1% to 5.5% (31 December 2007: nil) and the floating rates are based on six month Libor.

The gains and losses deferred in equity on the cash flow hedges described above will be continuously released to the profit and loss account over the period of the hedged risk.

In addition to the swaps novated to the Group, new interest rate swaps with a total notional amount of £200 million have been entered into during the year. The fixed interest rates vary from 5.2% to 5.4% (31 December 2007: nil) for all the swaps and the floating rates are based on three and six month Libor. These swaps did not qualify for hedge accounting during the period. An amount of £13 million loss was recognised in the profit and loss account during the period.

Index linked swaps with a notional principal of £2,206 million (31 December 2007: nil) were entered into to economically hedge BAA Funding bonds and future RPI based revenue. The real fixed interest rates, before applying RPI accretion, vary from 2.2% to 8.4% and the receive leg of the swaps was fixed at rates varying from 2.2% to 12.4%. Index linked swaps did not qualify for hedge accounting during the period. A gain of £81 million was recognised in the profit and loss account.

### Cross currency swaps

Two cross currency swaps have been entered into by the Group to hedge currency and cash flow interest rate risk on the €1 billion bond due 2012 and the €750 million bond due 2018. Under the €1 billion (£680 million) swap, the Group receives Euro interest at a fixed rate of 4.0% and pays Sterling interest at fixed rates which vary from 5.2% to 5.4%, and under the €750 million (£510 million) swap, the Group receives Euro interest at a fixed rate of 4.6% and pays Sterling interest at fixed rates which vary from 5.5% to 5.7%. The gains and losses deferred in equity on these swaps will be continuously released to the profit and loss account over the period to maturity of the hedged bonds.

In addition, the Group entered into a €750 million (£513 million) cross currency swap. Under this swap, the Group receives Euro interest at a fixed rate of 4.6% and pays Sterling interest at a variable rate based on six month Libor. This swap together with the £400 million interest rate swap (see above) novated from BAA and the new £113m interest rate swap, were designated as a cash flow hedge against currency and cash flow interest rate risk on the €750 million bond due 2014. The gains and losses deferred in equity on this swap will be continuously released to the profit and loss account over the period to maturity of the hedged bond.

### Foreign exchange contracts

Foreign exchange forward and swap contracts have been entered into buying US\$12 million (31 December 2007: nil), €28 million (31 December 2007: nil), Swiss Fr 8million (31 December 2007: nil) and Polish PLN 1 million (31 December 2007: nil) against Sterling. The currency forwards and swaps are used to manage exposures relating to future capital expenditure although hedge accounting is not sought for these derivatives.



# BAA (SP) Limited

## 18 Provisions for liabilities

	Deferred taxation (a) £m	Obligations under land purchase (b) £m	Reorganisation costs (c) £m	Pension (d) £m	Other (e) £m	Total £m
Balance 1 January 2008	579	99	50	-	4	732
Utilised	-	(1)	(8)	-	-	(9)
Charged/(released) to profit and loss account	(61)	-	(15)	17	-	(59)
Credit to the statement of total recognised gains and losses for the year (refer Note 21)	(125)	-	-	-	-	(125)
Unwinding of discount charged and capitalised	-	13	-	-	2	15
<b>Balance as at 31 December 2008</b>	<b>393</b>	<b>111</b>	<b>27</b>	<b>17</b>	<b>6</b>	<b>554</b>

### (a) Deferred Taxation

Analysis of the deferred tax balances are as follows:

	As at 31 December 2008 £m	As at 31 December 2007 £m
Excess of capital allowances over depreciation	488	583
Other timing differences	(95)	(4)
	<b>393</b>	<b>579</b>

	Un-provided	
	As at 31 December 2008 £m	As at 31 December 2007 £m
Tax on chargeable gains if investment properties were sold at their current valuations	445	503
Tax on rolled over gains if replacement assets were sold at their current valuations	12	12
	<b>457</b>	<b>515</b>

Provision has been made for deferred taxation in accordance with FRS 19.

No provision has been made for deferred tax on gains recognised on revaluing investment properties to their market value or on the sale of properties where taxable gains have been rolled over into replacement assets. Taxable gains will crystallise only if the property were sold without it being possible to claim rollover relief. The total amount of tax unprovided for is £457 million (31 December 2007: £515 million). At present it is not envisaged that this tax will become payable in the foreseeable future.

# BAA (SP) Limited

## 18 Provisions for liabilities (continued)

### (b) Obligations under land purchase

This provision relates to the acquisition of land for the construction of Terminal 5. The operational assets employed by the vendor of this land have been relocated, and provision has been made for the present value of the estimated payments to be made over the next 29 years to the vendor in compensation for this. The provision of £111 million (31 December 2007: £99 million), net of discount, is expected to be utilised according to the following profile:

	As at 31 December 2008 £m	As at 31 December 2007 £m
Within one year	8	6
One to two years	7	6
Two to five years	22	18
Five to ten years	26	26
Over ten years	48	43
	<b>111</b>	<b>99</b>

### (c) Reorganisation costs

The Group commenced implementing its restructuring programme 'Simplifying the Organisation' in late 2007. Costs associated with this programme are for severance and pension payments only. Additional amounts provided in the year are in relation to the Group's restructuring programmes. The amount released resulted from higher staff turnover than historic experience, lower than expected cost for each reduction in headcount and certain headcount reduction not being made due to the decision to sell Gatwick. All amounts are expected to be utilised in 2009. See note 5 for further details.

### (d) Pension

A provision of £17 million (31 December 2007: £nil) for historical accumulated past service pension costs borne by BAA Airports Limited in relation to the Unfunded Retirement Benefit Scheme and Post Retirement Medical Benefits was made in the year. This provision, which was held by BAA Airports Limited in previous years has been charged to BAA SP's airports as a result of the Shared Services Agreement, as airports are committed to fund any unfunded pension plan obligation of BAA Airports Limited (refer to Note 1 for details). This provision is based on the Group's share of the unfunded scheme valuation performed for BAA Airports Limited and will only be settled when the cash outflow is requested by BAA Airports Limited.

### (e) Other

A provision of £4 million is held for the additional 10% payment due under a compensation scheme (once planning permission has been obtained) for the second runway and related infrastructure at Stansted Airport.

A provision of £2 million has been made for the early termination costs of a lease agreement entered into by the Heathrow Airport Limited ('the Company') in 1998 in relation to rolling stock owned by the Company and operated by its subsidiary company, Heathrow Express Operating Company Limited. On 13 January 2009, the lease agreement was terminated, as a result of a credit rating downgrade of a third party obligor under the lease agreement.

# BAA (SP) Limited

## 19 Called up share capital

	Ordinary shares of £0.0019 each £	Ordinary shares of £1 each £
<b>Authorised</b>		
<b>Balance as at 1 January 2008</b>	-	-
9,000,000,000 ordinary shares of £1 each	-	9,000,000,000
Re-nominalisation from ordinary shares of £1 each to ordinary shares of £0.0019 each		
	17,100,000	(9,000,000,000)
<b>Balance as at 31 December 2008</b>		
9,000,000,000 ordinary shares of £0.0019 each	17,100,000	-
<b>Allotted and fully paid</b>		
<b>Balance as at 1 January 2008</b>	-	-
Issue of 2 ordinary shares of £1 each	-	2
Issue of 5,273,555,176 ordinary shares of £1 each	-	5,273,555,176
Re-nominalisation of 5,273,555,178 ordinary shares of £1 each to ordinary shares of £0.0019 each		
	10,019,755	(5,273,555,178)
<b>In issue as at 31 December 2008</b>		
<b>5,273,555,178 ordinary shares of £0.0019 each</b>	10,019,755	-

On 31 January 2008, there was an issue of 4,588,184,000 ordinary shares of £1 each. This was followed on 29 February 2008 by a further issue of 685,371,176 ordinary shares of £1 each.

On 23 April 2008, the High Court of Justice approved the special resolution, passed on 26 March 2008, requesting the reduction in the nominal value of each ordinary share issued. The share capital for the Company reduced from £9,000,000,000 divided into 9,000,000,000 ordinary shares at £1 each to £17,100,000 divided into 9,000,000,000 ordinary shares at £0.0019 each.

## 20 Revaluation reserves

	£m
<b>At 1 January 2008</b>	<b>2,227</b>
Unrealised loss on revaluation of properties	(190)
Revaluation adjustments	(2)
<b>At 31 December 2008</b>	<b>2,035</b>

During the year, previously recognised valuation gain amounting to £2 million were released as a result of the reclassification of a number of investment properties to BAA Group occupied properties.

# BAA (SP) Limited

## 21 Reserves

	Merger reserve £m	Cash flow hedge reserve £m	Total £m
<b>At 1 January 2008</b>	<b>(5,630)</b>	<b>-</b>	<b>(5,630)</b>
Cash flow hedges			
- Fair value losses	-	(445)	(445)
- Deferred tax on fair value losses	-	125	125
<b>At 31 December 2008</b>	<b>(5,630)</b>	<b>(320)</b>	<b>(5,950)</b>

## 22 Retained earnings

	£m
<b>At 1 January 2008</b>	<b>685</b>
Loss for the year	(201)
Dividend paid during the year	(705)
Reduction of share capital	5,264
<b>At 31 December 2008</b>	<b>5,043</b>

## 23 Acquisition of subsidiary

On 7 August 2008 Heathrow Airport Limited (HAL) acquired, from BAA Airports Limited, a fellow group company, the ownership of Heathrow Express Operating Company Limited (HEX) at the deemed fair market value of £3.8 million, equivalent to the net book value of HEX. The purchase consideration was settled in cash.

In the opinion of the Directors, the aggregate value of the shares in HEX is not less than the aggregate of the amount at which they are stated in HAL's balance sheet.

As a result of the management contract between the two entities, rail income and associated costs, and the management re-charge from HEX are already recognised in the financial statements of HAL and the Group. Therefore, the only impact subsequent to acquisition is the elimination of the management re-charge which is equivalent to 10% of the costs incurred in HEX. The elimination of the HEX management charge from the date of acquisition to 31 December 2008, increased the operating profit of the Group by £4 million.

# BAA (SP) Limited

## 24 Contingent liabilities

The Group has external contingent liabilities, comprising letters of credit, performance/surety bonds, performance guarantees and other items arising in the normal course of business amounting to £325 million at 31 December 2008 (31 December 2007: £123 million).

Included in the above, in July 1998, BAA Airports Ltd and Heathrow Airport Limited entered into a cross-border lease and leaseback in relation to the Heathrow Express rolling stock owned by Heathrow Airport Limited. The companies guarantee payments that are decreased by a deposit of US\$59.4 million with Rabobank and US\$15 million in US Government securities. In addition, they guarantee early termination payments. The cross border lease transaction was terminated on 13th January 2009 with Heathrow Airport Limited making a termination payment of US\$3.3 million.

easyJet have obtained leave to bring a judicial review of the CAA's price cap determination for Gatwick Airport for Q5. Their challenge relates principally to the amount of operating expenditure allowed. They maintain the CAA has not had sufficient regard to the recommendations of the Competition Commission and has unfairly and unlawfully allowed security cost submitted at a late stage of the review. The case is expected to be heard in the High Court from the 16th March 2009. If easyJet are successful it is likely the issue will be remitted to the CAA for their reconsideration. Should the CAA determine that the airport charges cap should be lower Gatwick Airport Limited would be required to rebate the amount of airport charges levied in excess of the amended cap. On the basis of legal advice received the Board is confident no such rebate will arise.

Under the shared service agreement hedging costs properly incurred by BAA Airports Limited in relation to the Employee Share Ownership Plan (ESOP) may be recharged to the Group. At 31 December 2008, the ESOP swap held in BAA Airports Limited had a fair value loss of £117 million. The Group may be obligated to settle its share of these amounts in the future, depending on a number of factors, including the number of options vesting, the number of options being exercised and the Ferrovial share price at exercise date. Accordingly, this is disclosed as contingent liability.

# BAA (SP) Limited

## 25 Commitments

### Non-cancellable operating lease commitments – Group as a lessee

Annual commitments under non-cancellable operating leases are as follows:

	As at 31 December 2008		As at 31 December 2007	
	Land and buildings	Other	Land and buildings	Other
	£m	£m	£m	£m
Within one year	2	-	-	-
Within two to five years	3	1	4	1
After five years	10	44	5	37
	15	45	9	38

The Group leases various offices under non-cancellable operating lease agreements. The leases have various terms, escalation clauses and renewable rights. The Group also leases plant and machinery under non-cancellable operating leases.

A significant portion of the £46 million operating lease commitments classified as 'other' are electricity supply equipments at the airports under a leased 75-year agreement with London Electricity Supply.

### Group commitments for capital expenditure

	Year ended	Year ended
	31 December	31 December
	2008	2007
	£m	£m
<b>Contracted for, but not accrued:</b>		
Heathrow - Post Terminal 5 Transfer	16	-
Heathrow Airport - Terminal 4 Airline	6	-
Heathrow Airport - Eastern Apron	6	-
Heathrow Airport - Terminal 5C Phase 2 Stage 2	6	-
Heathrow - Terminal 2B North East Stands (Heathrow Eastern Campus programme)	5	-
Gatwick Landside Inter Terminal Transit System	14	20
Heathrow Airport - Terminal 5	-	38
Heathrow Airport - Passenger Search X-Ray	-	7
South Terminal extension – Stansted	-	6
Heathrow Airport - East terminal extension	-	5
	53	76
Other projects	71	88
	124	164

The figures represented in the above table are contractual commitments to purchase goods and services at balance sheet date. The Group has in place long-term capital expenditure programmes covering its regulated airports. BAA SP's submission to the CAA in respect of quinquennium 5 included capital expenditure for Heathrow and Gatwick is £4,787 million and £920 million (2007/08 prices) respectively. In line with our commitments with the regulator, capital expenditure expected for Heathrow and Gatwick during 2009 amounts to £1,016 million and £210 million respectively. Under the terms of regulation, payments are required to be made to airlines if certain key projects are not delivered by a specified date. The amount to be paid is linked to the return BAA is estimated to earn on the anticipated cost of the project.

# BAA (SP) Limited

## 25 Commitments (continued)

The White Paper sets out the Government's policy for runway development in the UK. The Government chose a second runway at Stansted as its preferred location for the first new runway in the South East of England. The development of Stansted will be the subject of a planning inquiry, and the Group submitted its planning application to Uttlesford District Council on 11 March 2008 and the public inquiry is due to commence shortly. The anticipated costs of preparing the planning applications and taking those applications up to the commencement of the inquiry were approximately £90 million. These costs are being capitalised as part of the runway and infrastructure development costs (as detailed in Note 9). Total costs incurred to 31 December 2008 are £79 million (31 December 2007: £63 million).

As part of its commitment to the Stansted development, the Group is operating three voluntary blight schemes (the Home Value Guarantee Scheme (HVGS), the Home Owners Support Scheme and the Special Cases Scheme) for those people most affected by the airport expansion. The current estimate of the net cost of the blight and compensation schemes is up to £110 million (with approximately £96 million being incurred in this regulatory period). These costs are being capitalised as part of the runway development costs (as detailed in Note 9). Total value to 31 December 2008 is £88 million (31 December 2007: £66 million), including a £5 million provision for the additional 10% payment which will become due under the HVGS blight scheme once planning permission has been obtained for the second runway at Stansted.

The White Paper also commits the Group (and other airport operators) to offering noise mitigation measures for existing airports and voluntary blight schemes for future airport activity at the larger UK airports (those with more than 50,000 air traffic movements a year). The Group carried out a detailed examination of these White Paper provisions and consulted extensively with local communities at its airports on the implementation of potential schemes. Based on the Group's evaluation, payments under the White Paper current noise schemes are estimated at £31 million spread over the five years commencing 2007. The schemes include the provision of noise insulation for community buildings and dwellings, and assistance with the costs of relocation for dwelling owners.

In June 2006, the Government announced its conclusions for the 2006-2012 night flights regime at BAA SP's London airports. The regime commits BAA to introducing a new domestic noise insulation scheme at Heathrow, Gatwick and Stansted to address the impact of night flights on local communities. Based on the Group's evaluation, payments under this scheme are estimated to total £62 million, spread over the five year period commencing 2008.

In addition, there are live blight schemes to support the market for housing in areas identified for potential future runways at Heathrow, Gatwick, Glasgow and Edinburgh airports. Obligations under these schemes will only crystallise once the Group announces its intention to pursue a planning application for a new runway. In the case of Gatwick and the Scottish airports, this is unlikely in the short-term. In respect of Heathrow, the government has announced support for the need for a third runway at Heathrow and the Group is now reviewing the implications of the announcement with the intention of reaching a point where the Group will announce an intention to submit planning application. This is likely to occur within the next eighteen months.

The January 2009 Government Announcement for Adding Capacity at Heathrow requires the Group to review existing insulation and mitigation schemes; and to consider extending its noise insulation schemes to all community buildings and households in the new 57dBA contour who will experience an increase in noise of 3dBA or more.

Until further consultation is carried out with the local communities, the consequence of the significance of the costs related to the implementation of these schemes remains uncertain. It is too early to quantify the Group's potential obligations under these schemes.

In July 2008, the wider BAA Group reached agreement with the Trustee of the BAA Airports Limited defined benefit pension scheme to contribute the lesser of £80 million per annum and the annual cost of accruing benefits (as calculated using the FRS 17 accounting standard) for a period of three years ending 31 December 2011. BAA SP expects to contribute its share of this amount to the pension plan in the year ending 31 December 2009.

# BAA (SP) Limited

## 26 Notes to the consolidated cash flow statement

### (a) Net cash inflow from operating activities

	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m
Operating profit	364	435
Depreciation (including exceptional depreciation)	528	355
Increase in stock and debtors	(101)	(20)
Increase in creditors	30	24
Loss on disposal of fixed assets	1	1
Increase in provision	9	22
	<b>831</b>	<b>817</b>

### (b) Reconciliation in net debt

	As at 1 January 2008	Cash flow	Acquisition	Other non- cash changes	Exchange movements	As at 31 December 2008
Cash at hand and in bank	-	25	-	-	-	25
Debt due within one year	(8,229)	(43)	(4)	8,233	-	(43)
Debt due after more than one year	(1,813)	(5,009)	-	(4,108)	(435)	(11,365)
Liquid resources	-	157	-	-	-	157
Net debt	<b>(10,042)</b>	<b>(4,870)</b>	<b>(4)</b>	<b>4,125</b>	<b>(435)</b>	<b>(11,226)</b>

## 27 Cash flow relating to exceptional items

Cash flow in relation to exceptional items of £8 million for re-organisation costs and £22 million for Terminal 5 operational readiness costs were paid during the year.

## 28 Major non-cash transactions

Non-cash transactions include the settlement of the outstanding intercompany debt and the novation of the former BAA Airports Limited's bonds and related derivatives into the group (refer to other non-charges in note 26(b)) as part of the refinancing in August 2008.

The consideration for the purchase of BAA (AH) Limited was satisfied by the issuance of share capital and the BAA SP debenture. Refer to the basis of consolidation for further detail.



# BAA (SP) Limited

## 29 Ultimate parent undertaking and controlling party

The immediate parent undertaking during the financial year is BAA (SH) Limited, a company registered in England and Wales.

The ultimate parent entity in the UK is FGP Topco Limited and the ultimate parent of FGP Topco Limited is Grupo Ferrovial, S.A. (Spain), which is the largest and smallest Group to consolidate these financial statements.

The Company's results are also included in the consolidated financial statements of BAA Limited (formerly known as Airport Development and Investment Limited) and FGP Topco Limited for the year ended 31 December 2008.

Copies of the financial statements of FGP Topco Limited and BAA Limited (formerly known as Airport Development and Investment Limited) may be obtained by writing to the Company Secretary at 130 Wilton Road, London, SW1V 1LQ.

## 30 Subsidiaries

The Company's subsidiaries are as follows:

### Holding Companies

BAA (AH) Limited †

### Airport owners and operators

Heathrow Airport Limited †

Gatwick Airport Limited †

Stansted Airport Limited †

### Other

BAA Funding Limited #

Heathrow Express Operating Company Limited †

Heathrow Airport Communities Insulation Board Limited †

† Held by a subsidiary undertaking

# Incorporated in Jersey

Unless otherwise indicated, all subsidiaries are wholly owned and are incorporated and operate in the United Kingdom.

BAA Airports Limited and Heathrow Airport Limited have entered into a cross-border lease and leaseback establishing a special purpose vehicle, Paddington Railcars Company Limited ('PRC'), to act as an intermediate entity under the various lease agreements. Since the activities of PRC are effectively under the direct control of Heathrow Airport Limited under the terms of the lease agreement, PRC is deemed a quasi-subsiary of the Company and its profit, assets, liabilities and cash flows have been consolidated into the Group.

## Independent auditors' report to the members of BAA (SP) Limited

We have audited the parent company financial statements of BAA (SP) Limited for the period ended 31 December 2008 which comprise the Balance Sheet, and the related notes. These financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the Group financial statements of BAA (SP) Limited for the year ended 31 December 2008.

### Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the parent company financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the parent company financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Report of the Directors is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

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

### Basis of audit opinion

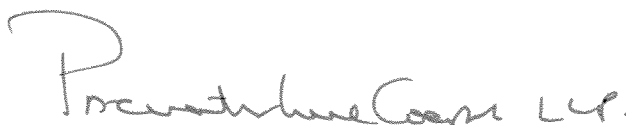
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the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

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

### Opinion

In our opinion:

- The parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2008;
- The parent company financial statements have been properly prepared in accordance with the Companies Act 1985; and
- The information given in the Report of the Directors is consistent with the parent company financial statements.



PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors

London

25 February 2009

# BAA (SP) Limited

## Balance Sheet As at 31 December 2008

	Note	31 December 2008 £m
<b>Non-current assets</b>		
Investment in subsidiaries	3	6,874
<b>Total non-current assets</b>		<b>6,874</b>
<b>Current assets</b>		
Cash and short term deposits	4	23
Debtors – due within one year	5	25
<b>Total current assets</b>		<b>48</b>
Creditors: amounts falling due within one year		
Borrowings	6	(82)
<b>Net current liabilities</b>		<b>(34)</b>
<b>Total assets less current liabilities</b>		<b>6,840</b>
Creditors: amount falling due more than one year		
	6	(2,392)
<b>Net assets</b>		<b>4,448</b>
<b>Capital and reserves</b>		
Called up share capital	7	10
Profit and loss reserve	8	4,438
<b>Total shareholder's funds</b>		<b>4,448</b>

The financial statements were approved by the Board of directors and authorised for issue on 25 February 2009 and signed on behalf of the Board.



**Jose Leo**  
Director

# BAA (SP) Limited

## Notes to the financial statements

### 1 Accounting policies

#### Basis of accounting

These financial statements have been prepared under historical cost convention, as modified by the revaluation of certain tangible fixed assets in accordance with Companies Act 1985 and applicable United Kingdom Accounting Standards.

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements.

The Company has not presented a cash flow statement or provided details of related party transactions as permitted under FRS 1 (revised) 'Cash Flow Statements' and FRS 8 'Related Party Disclosures' respectively.

#### Revenue

Revenue is recognised on an accrual basis in accordance with Financial Reporting Standard (FRS) 5 'Reporting the substance of transactions', net of VAT.

#### Interest

Interest payable is charged as incurred except where the borrowing finances tangible fixed assets in the course of construction. Such interest is capitalised once planning permission has been obtained and/or where projects are in the early stage of planning but the Directors are satisfied that the necessary consents will be received. The interest is then charged to the profit and loss account as depreciation over the life of the relevant asset.

#### Issue costs

Issue costs are those that are incurred directly in connection with the issue of a capital instrument, that would not have been incurred had the instrument not been issued. These are accounted for as a deduction from the amount of consideration received and amortised under the effective interest rate method.

#### Investments in subsidiary undertakings

Investments in subsidiary undertakings are stated at cost.

#### Deferred taxation

In accordance with FRS 19, 'Deferred Tax', deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax is not provided on timing differences arising from the revaluation of investment properties where there is no commitment to sell the asset.

Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

#### Impairment of assets

The Company assesses, at each reporting date, whether there is an indication that an asset may be impaired. If any such indication exist, or when annual impairment testing for an asset is required, the Company makes an estimate of the asset's recoverable amount. Where the asset does not generate cash flows that are independent of other assets, the recoverable amount of the cash-generating unit to which the asset belongs is estimated. Recoverable amount is the higher of an asset's fair value less costs of disposal and its value in use. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

# BAA (SP) Limited

## 1 Accounting policies

### **Impairment of assets (continued)**

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. After such reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount less any residual value, on a straight line basis over its remaining useful life.

### **Financial instruments**

#### **Trade and other receivables**

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost, using the effective interest method, less provision for impairment.

#### **Financial liabilities and equity**

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangement entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

#### **Trade and other payables**

Trade and other payables are non interest bearing and are stated at their fair value and subsequently measured at amortised cost using the effective interest method.

#### **Share capital**

Ordinary shares are classified as equity and are recorded at the par value of proceeds received, net of direct issue costs. Where shares are issued above par value, the proceeds in excess of par value are recorded in the share premium account.

# BAA (SP) Limited

## 2 Company result for the period

The Company been incorporated on 20 December 2007 and therefore the accounts have been prepared for the period from 20 December 2007 to 31 December 2008.

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the Company is not presented as part of these financial statements. The loss of the Company for the period attributable to shareholders was £121 million.

## 3 Investments

	Subsidiaries £m	Total £m
<b>Cost</b>		
Balance at incorporation	-	-
Additions	6,874	6,874
<b>Balance at 31 December 2008</b>	<b>6,874</b>	<b>6,874</b>
<b>Net book value at 31 December 2008</b>	<b>6,874</b>	<b>6,874</b>

The Company's subsidiaries are as follows:

### Holding Companies

BAA (AH) Limited

### Airport owners and operators

Heathrow Airport Limited †

Gatwick Airport Limited †

Stansted Airport Limited †

### Other

BAA Funding Limited#

Heathrow Express Operating Company Limited †

Heathrow Airport Communities Insulation Board Limited †

† Held by a subsidiary undertaking

# Incorporated in Jersey

Unless otherwise indicated, all subsidiaries are wholly owned and are incorporated and operate in the United Kingdom.

BAA Airports Limited and Heathrow Airport Limited have entered into a cross-border lease and leaseback establishing a special purpose vehicle, Paddington Railcars Company Limited ('PRC'), to act as an intermediate entity under the various lease agreements. Since the activities of PRC are effectively under the direct control of Heathrow Airport Limited under the terms of the lease agreement, PRC is deemed a quasi-subsiidiary of the Company and its profit, assets, liabilities and cash flows have been consolidated into the Group's financial statements.

## BAA (SP) Limited

### 4 Cash at bank and in hand

	As at 31 December 2008 £m
Cash at bank and in hand	23

Cash at bank and in hand earns interest at floating rates based on daily bank deposit rates and is subject to interest rate risk.

Money market funds held at 31 December 2008 total £23 million. The funds have no fixed maturity date, however the Company can withdraw its investment on demand. Returns are based on fund performance.

The fair value of cash and cash equivalents approximate to their book value.

### 5 Debtors

	As at 31 December 2008 £m
Due within one year:	
Group relief receivable	25

### 6 Borrowings

	As at 31 December 2008 £m
<b>Current</b>	
Interest payable	82
<b>Total current</b>	82
<b>Non current</b>	
Debenture payable to BAA (SH) Limited	1,566
Loans payable to subsidiary undertakings	826
	2,392
<b>Total current and non-current</b>	2,474

# BAA (SP) Limited

## 6 Borrowings (continued)

### Debenture payable to BAA (SH) Limited

The £1,600 million Debenture was issued in January 2008 to BAA Airports Limited. On refinancing in August 2008, £34.2 million was repaid and the remaining balance novated from BAA Airports Limited to BAA (SH) Limited, resulting in the carrying amount as at 31 December 2008 of £1,566 million. The current balance payable by the Company to BAA (SH) Limited is used to fund interest up to BAA (SH) Limited to pay the external interest on the Subordinated Facility owed by that company. The interest on the Debenture is 0.01% above the rate of the Subordinated Facility, and has a final redemption date of May 2011.

### Loans payable to subsidiary undertakings

The balance relates to loans payable to Heathrow Airport Limited, Gatwick Airport Limited and Stansted Airport Limited as at 31 December 2008 and bear an interest rate of 7.57% and have a final maturity date of August 2009.

Fair value of borrowings	As at 31 December 2008	
	Book value £m	Fair value £m
Non-current		
Long term debt	2,392	2,392
	<hr/>	<hr/>
	2,392	2,392

## 7 Share capital

	£
<b>Authorised</b>	
9,000,000,000 ordinary shares of £1 each	9,000,000,000
Balance at incorporation	9,000,000,000
Re-nominalisation to 9,000,000,000 ordinary shares of £0.0019 each	17,100,000
<b>Balance at 31 December 2008</b>	<b>17,100,000</b>
<b>Allotted and fully paid</b>	
In issue at incorporation: 2 ordinary shares of £1 each	2
Issue of 5,273,555,176 ordinary shares of £1 each	5,273,555,176
Capital reduction (Re-nominalisation –reduced from £1 to £0.0019 each)	(5,263,535,423)
<b>In issue at 31 December 2008: 5,273,555,178 ordinary shares of £0.0019 each</b>	<b>10,019,755</b>

On 31 January 2008, there was an issue of 4,588,184,000 ordinary shares of £1 and on 29 February 2008 there was a further issue of 685,371,176 ordinary shares of £1 each.

On 23 April 2008, the High Court of Justice approved the special resolution, passed on 26 March 2008, requesting the reduction in the nominal value of each ordinary share issued. The share capital for the Company reduced from £9,000,000,000 divided into 9,000,000,000 ordinary shares at £1 each to £17,100,000 divided into 9,000,000,000 ordinary shares at £0.0019 each.



# BAA (SP) Limited

## 8 Profit and loss reserve

	£m
Balance at incorporation	-
Retained loss for the financial period	(121)
Dividends paid	(705)
Other movements – capital reduction	5,264
<b>Balance at 31 December 2008</b>	<b>4,438</b>

## 9 Dividend paid and proposed

The Company paid an interim dividend of £70.40 (2007: Nil) per ordinary share, amounting to £705 million on 18<sup>th</sup> August 2008. No final dividend were paid or proposed during the year.

## 10 Auditor's remuneration

Auditor's remuneration paid to PricewaterhouseCoopers LLP for the performance of the statutory audit amounted to £20,000.

Details of fees for other services are provided in Note 3 of the Group financial statements.

## 11 Employee information and Directors' remuneration

### Employee numbers

The company has no employees. All staff costs are borne by BAA Airports Limited which recharges all such costs directly to the Company. Previously this was included in a management charge.

### Directors' Remuneration

None of the directors who served BAA (SP) Limited during the year received emoluments from the Company.

During the year, one of the directors (31 December 2007: one) had retirement benefits accruing to them under a defined benefits scheme.

### Registered office

BAA (SP) Limited, 130 Wilton Road, London SW1V 1LQ  
Registered in England No. 6458621