Heathrow Airport Limited
Annual report and financial statements
for the year ended 31 December 2012

Company registration number: 01991017

Heathrow Airport Limited

Contents

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Business review

Heathrow Airport Limited (the 'Company') operates Heathrow airport ('Heathrow') and Heathrow Express ('HEX'), the express rail service between Heathrow and Central London. The Company is entitled to all receipts and income relating to HEX but the day-to-day operation of HEX is undertaken by Heathrow Express Operating Company Limited on behalf of the Company.

On 15 October 2012 it was announced that the BAA name would cease being used. This change was implemented for a number of reasons including the fact that Heathrow will account for more than 95% of the former BAA Group once Stansted airport is sold. As a result, whilst the brands and related legal entity names of individual airports are being retained, the names of many of the holding companies in the business assumed the Heathrow brand.

The Company is a subsidiary of Heathrow Airport Holdings Limited (formerly BAA Limited). The Company's financial activities are aligned with Heathrow Airport Holdings Limited and the wider Heathrow Airport Holdings Limited group (the 'Heathrow Airport Holdings Group') and also with Heathrow (SP) Limited (formerly BAA (SP) Limited) group (the 'SP Group'), which is the intermediate parent undertaking of the smallest group to consolidate these financial statements.

This business review is presented in three sections:
Management review – overview of the year ended 31 December 2012, along with the key factors likely to impact the Company in 2013.
Financial review – presentation and explanation of the key drivers behind the financial performance reported for the year ended 31 December 2012 and analysis of the financial position of the Company as at that date.
Risk management – outline of the Heathrow Airport Holdings Group's approach to risk management, sources of assurance and highlights of the key business risks identified by the Heathrow Airport Holdings Group Executive Committee which are managed by the Company.

Management review
Review of 2012
Key features of the year
2012 saw significant progress across a wide range of important issues for the business. This included another year of record passenger satisfaction, as well as delivering an outstanding welcome for thousands of Olympic and Paralympic athletes. This was particularly notable as it was achieved whilst managing record passenger traffic at one of the world's busiest airports.

The year was also notable for progress in the UK hub airport capacity debate, the importance of which is underlined by the fact that in 2012 Heathrow once again operated close to its maximum permitted annual flight numbers. The hub airport model used by Heathrow and its competitors uses transfer passengers to support flights to long haul destinations which would not be viable using local demand alone. But unlike its rivals in France, Germany, the Netherlands and Dubai, Heathrow is full and its capacity constraints prevent any meaningful increase in the numbers of flights and routes. This means that the country's ability to trade with emerging economies is constrained with potential long-term consequences for UK trade, jobs and economic growth prosperity.

At the start of 2012, whilst the importance of hub airport capacity was beginning to be accepted by the UK government, a third runway at Heathrow was not one of the options under consideration. However, the year ended with the establishment of an independent commission tasked with looking at options for maintaining the UK's status as an international aviation hub. The Company will make submissions to the Airports Commission during 2013.

Work intensified through the year both within Heathrow and in consultation with its airline community and the Civil Aviation Authority on defining how the airport will develop during the next five year regulatory period (Q6), which begins on 1 April 2014. In particular, constructive engagement with Heathrow's airline community assessed key themes such as capital investment, traffic forecasts, operating costs and commercial revenue opportunities. The regulatory engagement process to date culminated with publication since the year end of Heathrow's full business plan for Q6. This period is expected to see Heathrow delivering further significant enhancements to the passenger experience, whilst delivering improved value for money through greater efficiency and productivity and driving further real growth in its commercial offering.

The Company continued to invest significantly in Heathrow's transformation with over £1 billion spent at the airport during 2012. The centrepiece of the investment programme continued to be the construction of the new Terminal 2. Work will intensify during 2013 on fit out and operational readiness with operations due to commence in little over a year from now. The scale of investment at Heathrow in recent years is underlined by Terminal 2 being the airport's second new terminal in recent years after a gap of over 20 years between the opening of Terminals 4 and 5.

The SP Group's financing position was transformed in 2012 with over £3 billion raised in multiple capital markets transactions and the successful refinancing of the SP Group's core revolving credit and liquidity facilities. This marked the culmination of a programme that has seen the SP Group raise nearly £7 billion since late 2009, enabling full repayment of loan facilities put in place in the 2008 refinancing and putting the SP Group in its strongest liquidity position for many years. In addition, the Heathrow Airport Holdings Group continued to attract investment from leading global equity investors with a 30% shareholding in the business purchased by Qatar Holding (20%) and China Investment Corporation (10%), the Qatari and Chinese sovereign wealth funds.

Management review *continued*

Review of 2012 *continued*
Key features of the year continued
At the same time as all the critical initiatives outlined above were delivered, the Company produced a robust financial performance despite the enduring challenges of subdued economic growth and continued pressure on consumer and business confidence in the world's developed economies.

It was against this background, together with the stabilisation of its financing position outlined above, that the Company was able to continue investing in the business with confidence and commence dividend payments to the Heathrow Airport Holdings Group's ultimate shareholders for the first time since it was acquired by the Ferrovial led consortium in 2006.

Passenger traffic trends
In the year ended 31 December 2012, Heathrow airport's passenger traffic increased 0.9% to 70.0 million (2011: 69.4 million), its second successive calendar year traffic record.

Heathrow's traffic in 2012 was characterised by record load factors (75.6% versus 75.2% in 2011) and more seats per passenger aircraft (197.4 versus 194.8 in 2011). These are the key drivers of the modest growth that can be expected in Heathrow's traffic for as long as it operates with its current capacity constraints where there is negligible opportunity to increase flight numbers which, whilst falling marginally to 471,341 compared to 476,197 in 2011, are very close to the cap of 480,000 flights per annum. The proportion of transfer traffic at Heathrow was 35% (2011: 35%).

Whilst underlying demand at Heathrow was firm through 2012, reported performance fluctuated through the year. There was year on year growth in the first quarter but a modest decline in the second quarter, partly reflecting issues such as the leap year and the different timing of Easter relative to 2011. In the third quarter, Heathrow's traffic was impacted in July and August by over 400,000 passengers compared to the same period of 2011 by the London 2012 Olympics, which resulted in UK based travellers staying in the country to enjoy the Games and non-UK travellers avoiding travel to the UK due to concerns over disruption caused by the Games. After that traffic growth resumed with monthly records set in September, November and December.

On a regional basis, Heathrow's performance was led by North Atlantic traffic which increased 3.2% to 16.3 million passengers (2011: 15.8 million). Traffic with other long haul destinations declined marginally, down 0.4% to 20.3 million passengers (2011: 20.4 million). Strength in services with Brazil (due to increased services), the Middle East (due partially to recovery from the unrest in the region that impacted 2011) and the Far East (due partly to recovery from 2011's Japanese tsunami) was offset particularly by weakness in African and Indian traffic due to airlines reducing or ceasing services.

Heathrow's European traffic increased modestly, up 0.5% to 28.6 million passengers (2011: 28.5 million), with significant variances in performance between markets, reflecting the macro-economic environment across Europe. There was good performance in markets such as Germany, Norway, the Netherlands and Belgium offset by weakness in markets such as Italy, Greece and Portugal. Domestic traffic was up slightly, by 0.5% at 4.7 million passengers (2011: 4.7 million).

Transforming Heathrow
The key strategic objective is for Heathrow to become the UK's direct connection to the world and Europe's hub of choice by making every journey better. A key enabler in delivering these objectives is Heathrow's continued focus on transforming passengers' and airlines' experience of using the airport through both investment in modern terminal facilities and related infrastructure and improving service standards. This will ensure customers enjoy a superior airport experience relative to competitors, encouraging greater utilisation of Heathrow and supporting its long-term growth ambitions.

Significant further progress was made in 2012 in both the transformation of Heathrow's infrastructure and further improving service standards.

The current centrepiece of Heathrow's infrastructure transformation is the construction of the new Terminal 2, which is due to open in mid-2014. Once open, more than 60% of passengers using Heathrow will enjoy some of the newest airport facilities in the world.

Alongside the transformation of Heathrow's infrastructure, there was further clear progress in improving service standards during 2012 with record overall passenger satisfaction achieved, a particularly notable achievement given the Olympics, record traffic volumes and the challenges of building the new Terminal 2 in the live operating environment of one of the world's busiest airports. In addition, Terminal 5 was voted the world's best airport terminal.

Investment in modern airport facilities
Heathrow's capital investment programme achieved a number of significant milestones in 2012 with the main projects including construction work on Terminal 2 as well as the development of baggage systems and a major refurbishment programme at Terminal 4. As expected, investment at Heathrow increased significantly in 2012 (over £1.1 billion) compared to 2011 (over £800 million). The level of investment is expected to continue at an elevated level in 2013 as progress is made towards opening Terminal 2.

Management review *continued*

Review of 2012 ***continued***

Transforming Heathrow continued

The new Terminal 2 building was made weather-tight in early 2012. This enabled significant progress on the terminal fit-out to be completed during the year. By the year end, installation of the internal walls, glass wall linings and conglomerate floor was well underway. In addition, delivery of terminal systems, including outbound baggage systems, escalators and lifts, was making good progress with commissioning of certain elements of the systems underway by year end. Installation of the information control system is now progressing, with IT systems cabling having commenced on all levels of the building and hand over of communications rooms for IT fit-out underway.

The second phase of the satellite Terminal 2B was made weather-tight in September 2012. Fit-out is progressing with the creation of internal walls, glass wall linings and the wooden linings to the arrivals corridor and installation of escalators, lifts and travelators. March 2012 saw excavation completed for the extensive basement and tunnel structures to house the tracked transit train and baggage systems that will connect the satellite to the main building once the main terminal's second phase is constructed. The passenger tunnel linking the main building with the satellite is formed with work underway on its fit out.

Good progress is being made in constructing the 'nodes' to connect the main terminal and satellite buildings to air bridges through which passengers board or leave aircraft.

There has also been significant progress on Terminal 2's multi-storey car park. The main access ramp to the car park's upper level is substantially in place, connecting the car park and existing road network. The structure of the western section of the car park is completed and the eastern section is progressing to plan. The structures for the car park's lifts and staircases as well as passenger walkways between the car park and the terminal building are under construction.

Terminal 2's construction is expected to be completed in late 2013 with operations commencing in mid-2014.

In Heathrow's baggage investment programme, the new underground automated baggage transfer system between Terminals 3 and 5 became operational. Elsewhere, the superstructure, roof and cladding for the building to house Terminal 3's new integrated baggage system are virtually complete. Baggage and IT systems are now being installed with the overall system expected to become operational in 2015.

Refurbishment works in Terminal 4's departure lounge were completed in 2012. The project has renewed floor tiling, refurbished gate areas, provided new seating, decluttered signage and provided a feature ceiling with LED lighting reducing energy consumption whilst enhancing the lounge area.

Refurbishment (including resurfacing) of Heathrow's southern runway will start in Spring 2013. The works will be carried out during night closures of the runway. The northern runway will be refurbished in 2014.

Service standards

The Company's focus on delivering transformational change in passengers' experience continues to receive significant endorsement from the travelling public, demonstrating that passengers are noticing the improvements made by Heathrow.

In April 2012 Heathrow Terminal 5 was named the world's best airport terminal in the 2012 SKYTRAX World Airport Awards. More recently, Heathrow achieved an all-time record overall passenger satisfaction score of 3.96 in the Airport Service Quality ('ASQ') survey (produced by Airports Council International) for the third quarter of 2012. This reflected in particular the success of the airport in delivering an outstanding welcome for thousands of Olympic and Paralympic athletes. Over 2012 as a whole Heathrow also achieved its highest ever average score of 3.94 (2011: 3.88) in the quarterly ASQ surveys.

In relation to individual service standards, punctuality remained at historically high levels in 2012 with 78% (2011: 79%) of aircraft departing within 15 minutes of schedule. Further, Heathrow's baggage misconnect rate was 15 per 1,000 passengers (2011: 15).

On security queuing, in 2012 passengers passed through central security within periods prescribed under service quality rebate schemes 92.8% (2011: 96.9%) of the time. This compares with 95% service standards. Whilst the reduced security queuing performance at Heathrow in 2012 reflected revised additional security procedures introduced in the fourth quarter of the year, performance has improved since the beginning of 2013.

Management review *continued*

Review of 2012 *continued*

Regulatory and governmental developments

UK aviation policy developments

The main development in UK aviation policy in the last year related to the debate on hub airport capacity, the importance of which is underlined by the fact that in 2012 Heathrow, the UK's only hub airport, once again operated close to its maximum permitted annual flight numbers. The hub airport model used by Heathrow and its competitors uses transfer passengers to support flights to long haul destinations which would not be viable using local demand alone. But unlike its rivals in France, Germany, the Netherlands and Dubai, Heathrow is full and its capacity constraints prevent any meaningful increase in the numbers of flights and routes. This means the country's ability to trade with emerging economies is constrained, with potential long-term consequences for UK trade, jobs and economic growth.

At the start of 2012, whilst the importance of hub airport capacity was beginning to be accepted by the UK government, a third runway at Heathrow was being excluded as a potential solution. However, during the year the government established the independent Airports Commission, chaired by Sir Howard Davies, which has been tasked with identifying and recommending the options for maintaining the UK's status as an international aviation hub. It is expected to do this by assessing the UK's international connectivity needs and recommending the optimum approach for meeting these.

The Commission is expected to produce an interim report by the end of 2013 which will set out its assessment of the evidence on the nature, scale and timing of the steps needed to maintain the UK's global hub status; and its recommendations for immediate actions to improve the use of existing runway capacity in the next five years consistent with credible long term options. A final report is then expected by summer 2015 which will set out the Commission's assessment of the options for meeting the UK's international connectivity needs, including their economic, social and environmental impact and its recommended solution.

The Company will make submissions to the Airports Commission during 2013.

Defining Heathrow's development for the next 5 years

Work intensified through the year within Heathrow and in consultation with its airline community and the Civil Aviation Authorirty ('CAA') on defining how the airport will develop during the next five year regulatory period (Q6), which begins on 1 April 2014.

In particular, constructive engagement with Heathrow's airline community assessed key themes such as capital investment, traffic forecasts, operating costs and commercial revenue opportunities. The regulatory process also included publication in July 2012 of the airport's initial business plan for Q6, the content of which has been superseded since the year end by the publication of an updated full business plan. Since publication of the initial business plan, Heathrow has reduced the expected cost of airlines operating at Heathrow during Q6 primarily by identifying further opportunities to enhance efficiencies and productivity. This is reflected in a proposed tariff profile, assuming no initial adjustment for the significantly lower than forecast passenger numbers at the end of the current regulatory period, of RPI+5.9% compared to RPI+6.8% in the initial business plan.

The next regulatory period is expected to see Heathrow delivering further significant enhancements to the passenger experience, whilst delivering improved value for money for example through greater efficiency and productivity and driving further real growth in its commercial offering.

Heathrow's full business plan includes a traffic forecast consistent with that in the July 2012 initial business plan showing modestly increasing passenger traffic over the next regulatory period that, after an allowance for shocks, averages around the airport's current un-shocked traffic performance. Heathrow believes it is essential to properly reflect the likely impact on passenger traffic over any medium or long-term horizon from potential shocks given that historically they have impacted its traffic by an average of close to 1.5%.

The full business plan also outlines Heathrow's proposed capital investment plan ('CIP') for 2014-2019. The CIP is aligned to Heathrow's masterplan that envisages the continuation of the process of building terminal and satellite capacity perpendicular to the airport's two runways that started with construction of Terminal 5 and is currently also being implemented in the new Terminal 2. The CIP foresees continued passenger experience improvements, ensuring there are sufficient facilities to handle expected growth in passenger numbers and aircraft size and enabling a competitive cost of operation at Heathrow based on a capital spend over the 5 years of approximately £3 billion (in 2011/12 prices).

The key elements of the CIP relate to the new Terminal 2, the Terminal 3 integrated baggage system, Heathrow's financial contribution to Crossrail (subject to regulatory approval), installation of new baggage screening technology required by 2018 and upgrades and resurfacing of runways and taxiways.

Terminal 2 is expected to open in the early months of Q6 and will involve a significant number of airline moves. In the first part of Q6, it is expected that the pier that currently connects Terminal 1 to the Terminal 2 satellite building will be demolished, opening up the taxiway between Terminal 2 and its satellite building. This will also enable two extra pier served stands to be added to the satellite building.

Management review *continued*

Review of 2012 ***continued***

Regulatory and governmental developments continued

Towards the end of Q6, the CIP assumes that work will commence on design, site clearance and enabling works for phase 2 of Terminal 2. This phase is expected ultimately to involve the demolition of Terminal 1, extension of the main terminal building, construction of a new satellite Terminal 2C, installation of a terminal baggage system and completion of tracked transit train and baggage facilities linking the main terminal building with the satellites.

Following publication of the full business plan, the next steps in the regulatory review process are for the CAA to complete its own research and analysis, following which it is expected to publish its initial price cap proposals in April 2013 for consultation. Final price cap proposals are expected to be published in October 2013.

Modernising the economic regulation of UK airports

The new Civil Aviation Act 2012 ('the Act') became law at the end of 2012 when it received Royal Assent and replaced the Airports Act 1986 as the key piece of legislation relating to the economic regulation of UK airports. The Act introduces a new single primary duty for the CAA to promote the interests of existing and future end consumers of passenger and freight services, wherever appropriate by promoting effective competition. This primary duty is supported by various supplementary duties including to ensure an efficient airport operator is able to finance the activities that are subject to the relevant licence obligations.

The Act will also bring into effect an economic licensing regime for airports similar to the regulatory framework in place in certain other regulated sectors such as water and energy. As a regulated airport, Heathrow will require a licence and initial licences will be issued by the CAA.

The licensing regime is currently being developed, with Heathrow's initial draft licence due to be published by the CAA in April 2013 for consultation alongside its publication of initial price cap proposals for Q6. The licence is expected to include scope for financial penalties, for example, in the event of a breach of certain licence conditions. Heathrow is also expected to be obliged to consult stakeholders on future plans for investment and operation of the airport, to report on environmental performance, to comply with service standards and other conditions and measures designed to ensure the effective economic regulation of the airport.

The licensing regime is also expected to include conditions relating to licensed airports' financial resilience, for example a minimum credit rating requirement, consistent with the themes proposed by the Department for Transport in 2009.

Developments since beginning of 2013

In January 2013, Heathrow's passenger traffic increased 0.3% to 5.18 million (2012: 5.17 million), an all time record for the month.

Outlook

This year is expected to see strong growth in Heathrow's turnover, Adjusted EBITDA and operating cash flow driven principally by increased aeronautical tariffs. Heathrow also intends to make significant progress in completing the new Terminal 2 with construction due to be complete by the end of 2013 and the terminal becoming operational in mid-2014.

Passenger traffic in early 2013 has been consistent with expectations with record traffic at Heathrow in January.

Financial review

The following financial review provides commentary on the performance of the Company during 2012.

Basis of presentation of financial results
The table below summarises the Company's financial performance in 2012 and includes comparative information for 2011.

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m	Change %
Turnover	**2,224.1**	2,047.2	8.6
Adjusted operating costs[1]	**(1,060.4)**	(1,008.0)	5.2
Adjusted EBITDA[2]	**1,163.7**	1,039.2	12.0
Operating costs – exceptional	**(151.2)**	(33.1)	356.8
EBITDA	**1,012.5**	1,006.1	0.6
Depreciation – ordinary	**(470.0)**	(468.3)	0.4
Depreciation and impairment – exceptional	**-**	(11.0)	100.0
Operating profit	**542.5**	526.8	3.0

[1] Adjusted operating costs are stated before depreciation, amortisation and exceptional items.
[2] Adjusted EBITDA is earnings before interest, tax, depreciation, amortisation and exceptional items.

Turnover
In the year ended 31 December 2012, the Company's turnover increased 8.6% to £2,224.1 million (2011: £2,047.2 million). This reflects increases of 11.3% and 5.7% in aeronautical and retail income respectively, and a 4.8% increase in other sources of income.

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m	Change %
Aeronautical income	**1,279.7**	1,149.6	11.3
Retail income	**460.1**	435.4	5.7
	1,739.8	1,585.0	9.8
Other sources of income:			
Operational facilities and utilities income	**162.9**	148.0	10.1
Property rental income	**102.5**	102.1	0.4
Rail income	**116.0**	111.1	4.4
Other income	**102.9**	101.0	1.9
	484.3	462.2	4.8
Total turnover	**2,224.1**	2,047.2	8.6

Aeronautical income
In the year ended 31 December 2012, aeronautical income increased by 11.3% to £1,279.7 million (2011: £1,149.6 million) and average aeronautical income per passenger increased 10.4% to £18.29 (2011: £16.57). The growth primarily reflected the headline 12.2% and 12.7% tariff increases from 1 April 2011 and 1 April 2012 respectively supported by the modest increase in passenger traffic. This has been partially offset by lower than expected yields particularly due to factors such as more quieter aircraft, a higher proportion of transfer passengers and a lower contribution from aircraft parking charges than assumed when tariffs were set. These factors led to aeronautical income being approximately £40 million lower than expected in the year ended 31 December 2012. This shortfall (or yield dilution) will be recovered through the 'K factor' true-up mechanism in the years commencing 1 April 2013 and 1 April 2014.

The headline maximum allowable yield at Heathrow will increase by 10.4% from 1 April 2013.

Financial review *continued*

Turnover *continued*
Retail income
The Company's retail income increased 5.7% to £460.1 million (2011: £435.4 million) and NRI per passenger increased 4.4% to £6.21 (2011: £5.95). The underlying growth in Heathrow's net retail income per passenger was slightly higher (around 5.5%) after adjusting for one-off benefits and Olympic-related income.

Heathrow's duty and tax-free and airside specialist shops continued to see increases in the average spend of passengers purchasing items in the in-terminal retail facilities. This was driven by factors including an increased proportion of higher spending non-EU passengers, refurbishment of Terminal 3's airside shops and enhancements to World Duty Free's stores in Terminals 3 and 4. In airside specialist shops, trading was particularly buoyant in the luxury and fashion segments.

A strong performance in bureaux de change at Heathrow was due primarily to improvements in contract terms with business partners. Catering income grew well ahead of passenger growth due to rebalancing of the portfolio towards premium outlets, enhanced contractual terms and a general focus on speed and quality of service. Finally in advertising, income growth was due to Olympic-related sales.

Reconciliation of gross retail income with net retail income and net retail income per passenger

	Year ended 31 December 2012	Year ended 31 December 2011	Change %
Gross retail income (£m)	**460.1**	435.4	5.7
Less: retail expenditure (£m)	**(25.8)**	(22.8)	13.2
Net retail income (£m)	**434.3**	412.6	5.3
Passengers (m)[1]	**70.0**	69.4	0.9
Net retail income per passenger[1,2]	**£6.21**	£5.95	4.4

[1] Percentage change calculated using un-rounded numbers.
[2] Net retail income per passenger calculated using un-rounded passenger numbers.

Other income
Income from activities other than aeronautical and retail increased 4.8% to £484.3 million (2011: £462.2 million). This was driven particularly by operational facilities and utilities income increasing 10.1% to £162.9 million (2011: £148.0 million) due mainly to higher demand, back billing and increases in tariffs for electricity. The increase in other income also reflected rail income increasing 4.4% to £116.0 million (2011: £111.1 million) and recovery of Olympics baggage related costs.

Financial review *continued*

Adjusted operating costs

Adjusted operating costs exclude depreciation, amortisation and exceptional items to provide a more meaningful comparison of the Company's operating costs.

In the year ended 31 December 2012, adjusted operating costs increased 5.2% to £1,060.4 million (2011: £1,008.0 million).

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m	Change %
Employment costs	**291.3**	262.1	11.1
Maintenance expenditure	**120.9**	110.6	9.3
Utility costs	**87.5**	89.1	(1.8)
Rents and rates	**126.3**	113.2	11.6
Other general expenses	**202.1**	188.8	7.0
Retail expenditure	**25.8**	22.8	13.2
Intra-group charges/other[1]	**207.0**	221.6	(6.6)
Profit on disposal of tangible fixed assets	**(0.5)**	(0.2)	150.0
Total	**1,060.4**	1,008.0	5.2

[1] Intra-group charges/other include HEX operating costs plus a 10% mark-up and a mark-up of 7.5% on corporate and centralised services provided by LHR Airports Limited (formerly BAA Airports Limited) in accordance with the Shared Services Agreement.

On an underlying basis, there was strong discipline in controllable costs given the impact on reported adjusted operating costs of Olympic-related activities, higher pension-related charges and the full year effect of additional infrastructure (Terminal 5C). In addition, the Company had to absorb contractual inflation adjustments to the costs of provision to the business of various services.

There were approximately £25 million in Olympic-related costs (approximately £16 million net of revenue benefits) such as the costs of Heathrow's temporary Olympic terminal, professional consultants, baggage, uniforms and staff bonuses and overtime costs.

Whilst reported employment costs were up 11.1%, adjusting for factors such as higher non-cash defined benefit pension service charges and one-off costs related to the Olympics, they increased by around 5%. Increased maintenance expenditure was mainly due to the cost of the temporary Olympic terminal at Heathrow and the impact of adverse winter weather in February 2012. Increases in rents and rates were driven primarily by inflation-linked increases in property rates and additional rateable property such as Terminal 5C that was only open for part of the comparative period. The growth in general expenses reflected increases across a range of areas including air traffic control, insurance, cleaning, service quality rebates and the Olympics. Partially offsetting these increases were reduced intra-group charges, particularly reflecting success in reducing central services costs.

The year on year increase in adjusted operating costs moderated significantly through the year with an 8.1% increase at the half year turning into a 5.2% increase for the full year. Outturn costs for the year were also lower than earlier expectations. These trends reflected particularly larger than expected reductions in intra-group charges.

Adjusted EBITDA

In the year ended 31 December 2012, Adjusted EBITDA increased 12.0% to £1,163.7 million (2011: £1,039.2 million), resulting in an Adjusted EBITDA margin of 52.3% (2011: 50.8%).

The significant increase in Adjusted EBITDA from 2011 reflects the effect of achieving turnover growth of 8.6% whilst limiting the increase in adjusted operating costs to 5.2%.

Financial review *continued*

Operating profit

The Company recorded an operating profit for the year ended 31 December 2012 of £542.5 million (2011: £526.8 million). The difference between Adjusted EBITDA and operating profit results from £470.0 million in depreciation (2011: £468.3 million) and a £151.2 million exceptional charge (2011: £44.1 million). A reconciliation between Adjusted EBITDA and statutory operating profit is provided below.

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m	Change **%**
Adjusted EBITDA	**1,163.7**	1,039.2	12.0
Depreciation	**(470.0)**	(468.3)	0.4
Exceptional items – pensions	**(151.2)**	(33.3)	354.1
Exceptional items – accelerated depreciation and impairment	**-**	(11.0)	100.0
Exceptional items – other	**-**	0.2	(100.0)
Operating profit	**542.5**	526.8	3.0

Depreciation

Depreciation for the year ended 31 December 2012, excluding exceptional charges, was 0.4% higher at £470.0 million (2011: £468.3 million).

Exceptional items: pensions

Items within operating profit include a £151.2 million non-cash pension related charge (2011: £33.3 million). This includes the Company's share of the movement in LHR Airports Limited defined benefit pension scheme deficit or surplus and Unfunded Retirement Benefit Scheme and Post-Retirement Medical Benefits pension related liabilities.

Exceptional items: accelerated depreciation and impairment

The accelerated depreciation and impairment charge of £11.0 million in 2011 was in relation to an impairment charge on the Airtrack rail project which the Company decided not to pursue.

Exceptional items: other

The £0.2 million credit in 2011 was due to the release of provisions that were no longer required.

Capital expenditure

In the year ended 31 December 2012, the cash flow impact of the Company's capital investment programme was £1,141.0 million (2011: £843.8 million).

The most significant areas of capital expenditure were on the new main Terminal 2 building, the second phase of Terminal 2's satellite building and the new integrated baggage system for Terminal 3.

Pension scheme

At 31 December 2012, the LHR Airports Limited defined benefit pension scheme had a deficit of £103.3 million as measured under FRS 17, of which £76.2 million was attributable to the Company under the Shared Services Agreement. This compares with a scheme surplus of £38.7 million at 31 December 2011 of which £26.9 million was attributable to the Company. The change from a scheme surplus to a deficit is due principally to a fall in the net discount rate applied to the scheme liabilities.

The trustees of the LHR Airports Limited defined benefit pension scheme and the Heathrow Airport Holdings Group concluded the pension scheme's 30 September 2010 triennial valuation in December 2011 and agreed a schedule of cash contributions of £97 million per annum out of which £24 million relate to the deficit recovery that became effective from 1 January 2012. Following the disposal of Edinburgh Airport Limited, the schedule of cash contributions has been reduced to £94 million per annum from January 2013 to December 2014. Approximately £71.6 million of the new annual amount will be met by the Company.

Financial review *continued*

Regulatory Asset Base ('RAB')

Set out below are RAB figures of the Company at 31 December 2011 and 31 December 2012. RAB figures are utilised in calculating gearing ratios (Regulatory Asset Ratios ('RAR')) under certain of the Heathrow Airport Holdings Group's financing agreements.

	RAB £m
31 December 2011	12,490.2
31 December 2012	13,471.0

The increase in the total RAB during the year ended 31 December 2012 reflected capital expenditure of approximately £1,158 million; inflation indexation adjustment of around £396 million; offset by regulatory depreciation of around £558 million; RAB profiling adjustments of around £15 million; and a modest amount of disposals.

Accounting and reporting policies and procedures

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain tangible fixed assets in accordance with the Companies Act 2006 and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice ('UK GAAP')). The Company's accounting policies and areas of significant accounting judgements and estimates are detailed within the Company financial statements.

Risk management

Risk management is a key element of the Heathrow Airport Holdings Group's corporate operations. Risk is centrally managed for the Heathrow Airport Holdings Group as part of the corporate services provided under the Shared Services Agreement ('SSA') (refer to the Accounting policies). In addition, the Company has a fully dedicated senior team which implements and manages risk closely. The Executive Committee, Board and Audit Committee ('AC') referred to below relate to the Executive Committee, Board and AC of Heathrow Airport Holdings Limited.

Heathrow Airport Holdings Group has updated its approach to risk management and issued a new risk management policy. The Heathrow Airport Holdings Group's risk management process is used to facilitate the identification, evaluation and effective management of the threats to the achievement of the Heathrow Airport Holdings 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 day-to-day activities are managed effectively and all significant business decisions are risk-informed.

The risk management process is evidenced in risk registers which are used as the basis for regular review of risks and their management, up to Executive Committee level. The risk registers are also used to make informed decisions relating to the procurement of insurance cover. The risk management process also supports 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.

The operation of the risk management process and the individual risk registers are subject to periodic review by the Heathrow Airport Holdings Group's Internal Audit 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.

Assurance is provided through reports to the AC, the management reporting processes and a specialist compliance audit function which reports directly to the Sustainability and Operational Risk Committee.

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

Safety risks
Health and safety is a core value of the business and the Company actively promotes the role of safety leadership in creating a safety culture that is intolerant of accidents and incidents.

The Company's Safety Management System includes risk assessment processes for all activities entailing significant risk and proportionate control measures employed to safeguard everyone impacted by the Company's business. The Company also operates robust asset management processes to ensure property and equipment remain safe. Governance, led by the senior management teams and assurance processes are used to ensure the aforementioned remain effective and to encourage continuous improvement.

Security risks
Security risks are regarded as critical risks to manage throughout the Heathrow Airport Holdings Group. The Company mitigates these risks by adopting and enforcing rigorous policies and procedures supported by professional training and by investment in leading-edge security technology. The Company works closely with government agencies, including the police and the UK Border Force building a framework to establish joint accountabilities for airport security and shared ownership of risk, thus ensuring security measures remain both flexible and proportionate to the prevailing threat environment.

Regulatory environment, legal and other reputational risks
Civil Aviation Authority ('CAA') economic regulation
As noted previously, the Company's operations are currently subject to economic regulatory review by the CAA normally every five years. The risk of an adverse outcome from these reviews is mitigated as far as possible by a dedicated project team which ensures full compliance with 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 Company's engagement with its airline customers. In order to manage the risk of adverse airline relations, all airlines are invited to be represented on engagement fora – eg joint steering groups. When feedback is sought or processes are measured, robust processes have been put in place to ensure confidentiality and neutrality of interpretation. In addition, key stakeholders are engaged on a joint planning basis which provides airlines with the opportunity to air views and share plans, thereby ensuring their on-going requirements are articulated and understood.

Risk management *continued*

Regulatory environment, legal and other reputational risks continued

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 Company, given its position in certain markets. Clear policy direction, which includes compulsory awareness training and close support from the internal legal department, reduces the risk of the Company breaching these regulations.

Capacity shortfall

Failure to secure necessary planning permissions could lead to the Company having insufficient capacity to meet the demands of the industry resulting in increased congestion. The UK government's policy on airport capacity changes has a significant influence on the Company's ability to secure necessary planning permissions and develop capacity. The Company 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. In addition, investment in additional capacity at the Heathrow airport will be partly dependent on an appropriate level of investment incentives being provided in future regulatory settlements.

Existing planning approvals provide for passenger traffic to grow to approximately 90 million at Heathrow.

Environmental risks

Environmental risk is managed throughout the Heathrow Airport Holdings Group as it has the potential to impact negatively upon the Heathrow's reputation and jeopardise its licence to operate and to grow. The Company controls and mitigates these risks at a number of levels. Proactive environmental management systems and employee training programmes are embedded within operations through clear environmental strategies and resource conservation initiatives. Progressive influencing of third parties, stakeholder engagement and community relations programmes are also established. The Company works closely with a range of stakeholders to ensure that it reacts effectively to the challenges posed by the environmental agenda.

Commercial and financial risks

Operational disruption

There are a number of circumstances that can pose short-term risks to the normal operations of Heathrow such as shocks to the macroeconomic environment, terrorism, wars, airline bankruptcies, human health scares, weather conditions and natural disasters whose cause may be remote from the location of the airport. These conditions can have a particularly significant impact on an airport such as Heathrow where, due to operating close to full capacity, there is negligible spare capacity to utilise in recovering from some of the above conditions. Where possible the Company seeks to anticipate the effects of these events on its operations and also maintains contingency plans to minimise disruption wherever possible.

Development

The Company recognises that failure to control key development costs and delivery could damage its financial standing and reputation. The Company mitigates this risk through adherence to a robust project process and by a system of assurance, consisting of project and programme reviews before approval and during construction. The process is continually improved incorporating lessons learnt and "best practice" distilled from knowledge sharing with other client programmes, expertise within its supply chain and guidance from professional bodies.

Changes in demand

The risk of unanticipated long-term changes in passenger demand for air travel could lead to misaligned operational capacity within the Company. Since it is not possible to identify the timing or period of such an effect, the Company 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 Company is recognised. The Company has a range of formal national and local consultative bodies to discuss pay, employment conditions and business issues with the Trade Unions. The Heathrow pay agreement reached in early 2011 established the pay structure for 2011, 2012 and 2013 – the next pay negotiations are planned for January 2014. The Company could also be exposed in the short-term to the effect of industrial action involving other key stakeholders in the aviation sector such as airlines, air traffic controllers, baggage handlers and the UK Border Force.

Risk management *continued*

Commercial and financial risks continued

Treasury

The Company's financial risk management objectives are aligned with Heathrow Airport Holdings Limited, and also with Heathrow (SP) Limited which is the parent undertaking of the smallest group to consolidate these financial statements and the level at which financial risks for the Company are managed. The treasury policies of the SP Group are set out below.

The Board of the Heathrow Airport Holdings Group approves prudent treasury policies and delegates certain responsibilities to senior management who directly control day-to-day treasury operations on a centralised 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 in the Heathrow Airport Holdings Group's business operations and funding. To achieve this, the Heathrow Airport Holdings Group enters into interest rate swaps, index-linked swaps, cross-currency swaps and foreign exchange contracts to protect against interest rate and currency risks.

The primary treasury related financial risks faced by the SP Group are:

(a) Interest rates
The SP Group maintains a mix of fixed and floating rate debt. As at 31 December 2012, fixed rate debt after hedging with derivatives represented 80% of the SP Group's total external nominal debt.

(b) Inflation
The SP Group mitigates the risk of mismatch between its airports' aeronautical income and regulatory asset bases, which are directly linked to changes in the retail prices index, and nominal debt and interest payments by the use of inflation linked instruments.

(c) Foreign currency
The SP Group uses cross-currency swaps to hedge all interest and principal payments on its foreign currency debt. The SP Group uses foreign exchange contracts to hedge material capital expenditure in foreign currencies once a project is certain to proceed.

(d) Funding and liquidity
The SP Group has established an investment grade financing platform for its airports. This platform supports bank term debt, bank revolving credit facilities including a revolving credit facility, bank liquidity facilities and sterling and foreign currency capital markets issuance. All debt is secured and can be issued in either senior (A-/A-) or junior (BBB/BBB) format. Covenants are standardised wherever possible and are monitored on an on-going basis with formal testing reported to the AC, the Board and Executive Committee.

Although there can be no certainty that financing markets will remain open for issuance at all times, debt maturities are spread over a range of dates, thereby ensuring that the SP Group is not exposed to excessive refinancing risk in any one year.

The SP Group has positive cash flows before capital expenditure and maintains at least 12 months' headroom under the revolving credit facility. As at 31 December 2012, cash and current asset investments were £38.1 million, undrawn headroom under revolving facilities was £1,693.0 million and undrawn headroom under liquidity facilities was £750.0 million.

Risk management *continued*

Commercial and financial risks continued
Treasury continued

(e) Counterparty credit
The SP Group's exposure to credit related losses, in the event of non-performance by counterparties to financial instruments, is mitigated by limiting exposure to any one party or instrument.

The SP Group maintains a prudent split of cash and current asset investments 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 current asset investments are placed with counterparties with short-term credit ratings lower than A-2/F1. The SP Group monitors the credit rating of derivative counterparties on a daily basis and ensures no positions are entered into with counterparties with a long-term credit rating below BBB+ (S&P)/A (Fitch).

On behalf of the Board

José Leo
Director

26 February 2013

Heathrow Airport Limited

Directors' report

The Directors present their annual report and the audited financial statements for Heathrow Airport Limited (the 'Company') for the year ended 31 December 2012.

Principal activities, review of business and future developments
The Company operates Heathrow airport ('Heathrow') and Heathrow Express ('HEX'), the express rail service between Heathrow and Central London. The Company is entitled to all receipts and income relating to HEX but the day-to-day operation of HEX is undertaken by Heathrow Express Operating Company Limited on behalf of the Company. For providing these services, the Company pays Heathrow Express Operating Company Limited a management fee and reimburses all of its operating costs.

A review of the progress of the Company's business during the year, the key performance indicators, principal business risks and likely future developments are reported in the Business review on pages 2 to 15.

No significant changes to the activities of the Company are expected in the foreseeable future.

Results and dividends
The loss after taxation for the financial year amounted to £15.1 million (2011: £114.1 million).

On 21 June 2012 the shareholders and directors of the Company approved a capitalisation of the revaluation reserve of £718,000,000 reducing the revaluation reserve and increasing share capital to enable a share capital reduction and payment of dividends.

Dividends of £150.8 million were paid during the year (2011: £nil). The statutory results for the year are set out on page 21.

Directors
The directors who served during the year are as follows:

Normand Boivin		
Neil Clark	Appointed 8 October 2012	
Emma Gilthorpe	Appointed 8 October 2012	
Clare Harbord	Appointed 8 October 2012	
John Holland-Kaye		
Carol Hui	Appointed 8 October 2012	
José Leo		
Fidel López	Appointed 8 October 2012	
Colin Matthews	Appointed 8 October 2012	
Steven Morgan	Resigned 31 October 2012	
Terence Morgan		
Jim O'Sullivan	Appointed 8 October 2012	
Fiona Rodford	Appointed 8 October 2012	Resigned 25 January 2013
Paula Stannett	Appointed 28 January 2013	

Employment policies
The Company has no direct employees. The staff are employed by LHR Airports Limited, a fellow subsidiary entity of the Heathrow Airport Holdings Group.

Supplier payment policy
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; and
- advise suppliers without delay when invoices are contested and settle disputes quickly.

The Company had 8 days purchases outstanding at 31 December 2012 (2011: 29 days) based on the average daily amount invoiced by suppliers during the year.

Directors' report *continued*

Donations
The Company's charitable donations for the year amounted to £1,105,000 (2011: £1,013,000). The main beneficiaries of charitable donations, the relevant amounts donated and the main activities of these beneficiaries are as follows:

Hillingdon Communities Trust	£1,000,000	Heathrow Airport Limited has made a 15 year commitment to make an annual grant of £1 million to the Hillingdon Communities Trust. The deed of gift to the trust carries a requirement that grants must benefit the community in the southern part of the Borough of Hillingdon including Hayes (the wards of Botwell, Townfield and Pinkwell, West Drayton, Yiewsley and the Heathrow Villages).
Independent Transport Commission	£50,000	Researches the economic, social and environmental aspects of transport and travel providing insight and analysis on the long-term strategic issues that may face the airport.
MacMillan Cancer Support	£30,600	Supports individuals in the fight against cancer providing financial and emotional support while hosting national fundraising and awareness events.
Heathrow Travel-care	£12,000	Provides counselling or assistance to passengers and airport staff.

In addition to the donations above, the Heathrow Airport Holdings Group contributes to a number of charitable causes through the Communities Trust (formerly BAA Communities Trust); in 2012, £750,000 was allotted to the fund.

The Company may incur expenditure which could be classified as political donations under the Political Parties, Elections and Referendums Act 2000 and Part 14 of the Companies Act 2006. The Company obtained a renewed shareholders' approval in February 2012 to commit up to a maximum of £60,000 of such expenditure (in aggregate) over the following four years. In the Company's view there was no expenditure in the year to 31 December 2012 (2011: £nil) that falls within this category.

Risk management
The Company actively manages all identified corporate risks. Details of the Company's risk management policies can be found on pages 12 to 15 in the Risk management section of the Business review.

Financial risk management objectives and policies
The Company's financial risk management objectives and policies, including hedging policies, can be found on pages 14 to 15 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 2006, but without prejudice to any protection from liability which might otherwise apply, 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 judgement 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.

Auditor
Pursuant to the provisions of section 485 of the Companies Act 2006, a resolution relating to the reappointment of the auditor Deloitte LLP will be proposed within the period set out in section 485 or, Deloitte LLP will be deemed re-appointed where no such resolution is proposed, following the period set out in section 485 in accordance with section 487.

Directors' report *continued*

Statement of disclosure of information to the Auditor

Each of the persons who is a director at the date of approval of this annual report confirms that:

- so far as the director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

On behalf of the Board

José Leo
Director

26 February 2013

Company registration number: 01991017

Heathrow Airport Limited

Directors' responsibilities statement

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 United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

On behalf of the Board

José Leo
Director

26 February 2013

Heathrow Airport Limited

Independent auditor's report to the members of Heathrow Airport Limited

We have audited the financial statements of Heathrow Airport Limited for the year ended 31 December 2012 which comprise the Profit and loss account, the Statement of total recognised gains and losses, the Reconciliation of movements in shareholder's funds, the Balance sheet, the Accounting policies, the Significant accounting judgements and estimates and the related notes 1 to 20. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor
As explained more fully in the Directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements
In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2012 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006
In our opinion the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception
We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

A J. Kelly

Andrew J. Kelly FCA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, UK

26 February 2013

Heathrow Airport Limited

Profit and loss account for the year ended 31 December 2012

	Note	**Year ended 31 December 2012 £m**	Year ended 31 December 2011 £m
Turnover	*1*	**2,224.1**	2,047.2
Operating costs – ordinary	*2*	**(1,530.4)**	(1,476.3)
Operating costs – exceptional: pensions	*3*	**(151.2)**	(33.3)
Operating costs – exceptional: other	*3*	**-**	(10.8)
Total operating costs		**(1,681.6)**	(1,520.4)
Operating profit		**542.5**	526.8
Impairment of fixed assets – exceptional	*3*	**(5.1)**	-
Net interest payable and similar charges	*4*	**(529.0)**	(675.9)
Profit/(loss) on ordinary activities before taxation		**8.4**	(149.1)
Tax (charge)/credit on profit/(loss) on ordinary activities	*5*	**(23.5)**	35.0
Loss on ordinary activities after taxation	*16*	**(15.1)**	(114.1)

All profits and losses recognised during the current and prior year are from continuing operations.

Heathrow Airport Limited

Statement of total recognised gains and losses for the year ended 31 December 2012

	Note	**Year ended 31 December 2012 £m**	Year ended 31 December 2011 £m
Loss for the financial year	*16*	**(15.1)**	(114.1)
Unrealised gain on revaluation of investment properties and land held for development	*6,16*	**46.8**	47.1
Unrealised loss on revaluation of fixed assets		**-**	(2.8)
Total recognised losses relating to the year		**31.7**	(69.8)

Reconciliation of movements in shareholder's funds for the year ended 31 December 2012

	Note	**Year ended 31 December 2012 £m**	Year ended 31 December 2011 £m
Loss for the financial year	*16*	**(15.1)**	(114.1)
Unrealised gain on revaluation of investment properties and land held for development	*6,16*	**46.8**	47.1
Unrealised loss on revaluation of fixed assets		**-**	(2.8)
Dividends paid	*16*	**(150.8)**	-
Realised loss on tangible fixed assets	*16*	**(0.5)**	-
Net movement in shareholder's funds		**(119.6)**	(69.8)
Opening shareholder's funds		**1,712.8**	1,782.6
Closing shareholder's funds		**1,593.2**	1,712.8

There is no material difference between the historical cost profits and losses and the profit and loss account.

Heathrow Airport Limited

Balance sheet as at 31 December 2012

	Note	31 December 2012 £m	31 December 2011 £m
Fixed assets			
Tangible fixed assets	6	**11,751.3**	10,920.4
Investments	7	**3.8**	3.8
Total fixed assets		**11,755.1**	10,924.2
Current assets			
Stocks	8	**7.2**	6.0
Debtors (including amounts due after more than one year of £1,973.5 million (2011: £1,756.5 million))	9	**2,307.9**	2,080.8
Current asset investments	10	**32.5**	21.0
Cash at bank and in hand		**1.4**	2.6
Total current assets		**2,349.0**	2,110.4
Current liabilities			
Creditors: amounts falling due within one year	11	**(1,197.1)**	(1,305.3)
Net current assets		**1,151.9**	805.1
Total assets less current liabilities		**12,907.0**	11,729.3
Creditors: amounts falling due after more than one year	12	**(11,069.1)**	(9,783.3)
Provisions for liabilities and charges	14	**(244.7)**	(233.2)
Net assets		**1,593.2**	1,712.8
Capital and reserves			
Called up share capital	15,16	**472.7**	857.6
Share premium reserve	16	**-**	23.2
Revaluation reserve	16	**429.4**	1,099.5
Profit and loss reserve	16	**691.1**	(267.5)
Total shareholder's funds		**1,593.2**	1,712.8

The financial statements of Heathrow Airport Limited (Company registration number: 01991017) were approved by the Board of Directors and authorised for issue on 26 February 2013. They were signed on its behalf by:

Colin Matthews
Director

José Leo
Director

Accounting policies for the year ended 31 December 2012

The principal accounting policies applied in the preparation of the financial statements of Heathrow Airport Limited (the 'Company') are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated.

Basis of accounting
These financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain tangible fixed assets in accordance with applicable Companies Act 2006 and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Going concern
The Directors have prepared the financial statements on a going concern basis which requires the Directors to have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. The Company forms part of the Heathrow (SP) Limited (formerly BAA (SP) Limited) group (the 'SP Group'), which is the smallest group to consolidate these financial statements, and the level at which financial risks are managed for the Company.

Consequently the Directors have reviewed the cash flow projections of the SP Group of which the Company forms part, taking into account:
- the forecast revenue and operating cash flows from the underlying operations;
- the forecast level of capital expenditure; and
- the overall SP Group liquidity position, including the remaining committed and uncommitted facilities available to it, its scheduled debt maturities, and its forecast financial ratios and ability to access the debt markets.

As a result of the review, having made appropriate enquiries of management, the Directors have a reasonable expectation that sufficient funds will be available to meet the Company's funding requirement for the next twelve months from the balance sheet signing date.

Consolidated financial statements
The Company has taken advantage of the exemption provided by section 400 of the Companies Act 2006 from the requirement to prepare consolidated financial statements as it is a wholly owned subsidiary of FGP Topco Limited and its subsidiary undertakings are included in the consolidated financial statements of that company for the year ended 31 December 2012. The results are also included in the consolidated financial statements of Heathrow (SP) Limited for the year ended 31 December 2012 (intermediate parent entity and the smallest group to consolidate these financial statements). They are also included in the audited consolidated financial statements of Heathrow Finance plc (formerly BAA (SH) plc) and Heathrow Airport Holdings Limited (formerly BAA Limited) for the year ended 31 December 2012.

The financial statements present information about the Company as an individual entity only and not as a group.

Turnover
Turnover represents amounts receivable for goods and services provided in the normal course of business, net of discounts, VAT and other sales-related taxes and consists primarily of:

Aeronautical income
- Passenger charges based on the number of departing passengers on departure.
- Aircraft landing charges levied according to noise, emissions and weight recognised on landing.
- Aircraft parking charges based on a combination of weight and time parked as provided.
- Other charges levied for passenger and baggage operation when these services are rendered.
- Other traffic charges.

Retail income
- Concession fees from retail and commercial concessionaires at or around airports are based upon turnover certificates supplied by concessionaires and are recognised in the period to which they relate.
- Car parking income is recognised at the time of exiting the car park in accordance with operator management fee arrangements.

Property and operational facilities
- Property letting rentals, recognised on a straight-line basis over the term of the rental period.
- Proceeds from the sale of trading properties, recognised on the unconditional completion of the sale.
- Usage charges made for operational systems (e.g. check-in desks), recognised as each service is provided.
- Other invoiced sales, recognised on the performance of the service.

Rail
- Turnover from ticket sales, recognised at the time of travel.

Other
- Charges related to passengers with restricted mobility and various other services, recognised at the time of delivery.

Accounting policies for the year ended 31 December 2012 *continued*

Exceptional items
The Company separately presents certain items as exceptional on the face of the profit and loss account. Exceptional items are material items of income or expense that, because of their size or incidence, merit separate presentation to allow an understanding of the Company's financial performance.

Such events may include gains or losses on the disposal of businesses or assets, major reorganisation of business, closure or mothballing of terminals and 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.

Provisions to recognise the Company's liability to fund the LHR Airports Limited (formerly BAA Airports Limited) defined benefit pension scheme deficit or surplus and Unfunded Retirement Benefit Scheme and Post-Retirement Medical Benefits pension related liabilities under the Shared Services Agreement are also treated as exceptional. Refer to the Shared Services Agreement accounting policy.

Additional details of exceptional items are provided as and when required as set out in Note 3.

Interest
Interest payable and interest receivable are recognised in the profit and loss account in the period in which they are incurred.

Tangible fixed assets
Operational assets
Terminal complexes, airfield assets, plant and equipment, rail assets and other land and buildings are stated at cost less accumulated depreciation and impairment losses.

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 and the asset is available for use. Where appropriate, cost includes borrowing costs capitalised, own labour costs of construction-related project management and directly attributable overheads. Costs associated with 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 Company. The Company 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.

Investment properties
Investment property, which is property held to earn rentals and/or for capital appreciation, is valued at the reporting date 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 in the period in which they arise.

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

In accordance with Statement of Standard Accounting Practice 19 *Accounting for Investment Properties*, no depreciation is provided in respect of freehold or long leasehold investment properties.

Capitalisation of interest
Interest payable resulting from financing tangible fixed assets that are in the course of construction is capitalised whilst projects are in progress. Where assets in the course of construction are financed by specific borrowing facilities the interest rate relating to those specific borrowing facilities is used to calculate the amount to capitalise, otherwise an interest rate based on the weighted average cost of debt is used. Capitalisation of interest ceases once the asset is complete and available for use. Interest is then charged to the profit and loss account as a depreciation expense over the life of the relevant asset.

Accounting policies for the year ended 31 December 2012 *continued*

Tangible fixed assets *continued*

Depreciation

Depreciation is provided on operational assets, other than land and assets in the course of construction, to write off the cost of the assets less estimated residual value by equal instalments over their expected useful lives as set out below:

Terminal complexes	*Fixed asset lives*
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
Airport transit systems	
Rolling stock	20 years
Track	50 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
Other land and buildings	
Short leasehold properties	period of lease
Leasehold improvements	lower of useful economic life or period of lease
Plant equipment and other assets	
Motor vehicles	4 - 8 years
Office equipment	5 - 10 years
Computer equipment	4 - 5 years
Computer software	3 - 7 years

Asset residual values and useful lives are reviewed and adjusted, if appropriate, at each reporting date.

Impairment of assets (excluding investment in subsidiaries)

The Company 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 Company estimates the asset's recoverable amount. Where the asset does not generate cash flows 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. 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. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

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 a 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.

Accounting policies for the year ended 31 December 2012 *continued*

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.

Company as a lessee

Finance leases, which transfer to the Company substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance costs are charged directly against income.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term if there is no reasonable certainty that the Company will obtain ownership by the end of the lease term.

Operating lease payments are recognised as an expense in the profit and loss account on a straight-line basis over the lease term.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Company as a lessor

Leases where the Company retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as the rental income.

Investments

Investments are held as fixed assets and are stated at cost and reviewed for impairment if there are indications that the carrying value may not be recoverable.

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 and includes all costs to bring inventories to their present location and condition.

Debtors

Debtors are recognised initially at cost less any provision for impairment.

Cash and current asset investments

Cash, for the purpose of the summary 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 term deposits of less than one year (other than cash) and investments in money market managed funds.

Creditors

Creditors are recognised at cost.

Amounts owed to group undertakings

Amounts owed to group undertakings are recognised initially at fair value, net of transaction costs incurred. Any difference between the amount initially recognised (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest rate method.

Deferred income

Contractual income is treated as deferred income and released to the profit and loss account as earned.

Accounting policies for the year ended 31 December 2012 *continued*

Borrowings
Borrowings are recognised initially at fair value, net of transaction costs incurred and are subsequently stated at amortised cost. Any difference between the amount initially recognised (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest rate method.

The borrowings from group undertakings include the balance of the Borrower Loan Agreement ('BLA') payable by the Company to Heathrow Funding Limited (formerly BAA Funding Limited). The advances under the BLA are issued on substantially the same terms as the new bonds issued by Heathrow Funding Limited, taking into consideration the related hedging instruments. The advances are carried at amortised cost with interest expense recognised using the effective interest rate method. The nominal amount of the index-linked borrowings is accreted for the RPI component recognised within interest payable in the profit and loss account.

Provisions
Provisions are recognised when the Company 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 reporting date and are discounted to present value where the effect is material.

Restructurings
A restructuring provision is recognised when the Company has developed a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement the plan or announcing its main features to those affected by it. The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring, which are those amounts that are both necessarily entailed by the restructuring and not associated with the on-going activities of the entity.

Onerous contracts
Present obligations arising under onerous contracts are recognised and measured as provisions. An onerous contract is considered to exist where the Company has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

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 an effective interest rate 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 using 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.

Derivative financial instruments
The derivative financial instruments utilised by the Company are interest rate swaps. These are used to manage the interest rate risk of borrowings. Interest receivable on the instruments is calculated using a variable interest rate whereas interest payable is based on a fixed interest rate. The purpose of the swaps is to hedge the risk that arises from the borrowings with variable interest rates.

The derivative financial instruments are accounted for on an accruals basis. 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 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, respectively. The net interest receivable or payable accrued on derivatives is included in current debtors or current creditors on the balance sheet.

Derivative financial instruments novated from other companies within the Heathrow Airport Holdings Limited group (the 'Heathrow Airport Holdings Group') are transferred at fair value prevailing on that date. Premiums payable or receivable are amortised over the term of the financial instruments.

Shared Services Agreement ('SSA')
All employees of the Company are employed directly by LHR Airports Limited which also acts as the provider of corporate and administrative services to the Company. LHR Airports Limited is the sponsor of the related defined benefit pension schemes and grants all employee benefits.

On 18 August 2008, the Company entered into a SSA with LHR Airports Limited by which the latter became the shared services provider of operational staff and corporate services.

Accounting policies for the year ended 31 December 2012 *continued*

Shared Services Agreement ('SSA') ***continued***

Operational staff

LHR Airports Limited charges the Company for the provision of services in relation to staff costs, including wages and salaries, pension costs, medical costs and redundancy payments, as well as any other of its associated expenses properly incurred by the employees of LHR 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 employee share options. All of the amounts included in the above-mentioned costs are settled in cash except for pension costs or costs related to hedging of share options, which are only settled when the cash outflow is requested by LHR Airports Limited.

Corporate and centralised services

LHR 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 SSA with a mark-up of 7.5% except for IT applications, or sub-contractor costs, where only full costs are recharged to the Company.

Pension costs

Under the SSA the current period service cost for the LHR Airports Limited pension schemes are recharged to the Company on the basis of their pensionable salaries. This charge is included within Operating costs – ordinary. Cash contributions are made directly by the company to the LHR Airports Limited pension schemes on behalf of LHR Airports Limited.

The Company has had an obligation since August 2008 to fund or benefit from their share of the LHR Airports Limited defined benefit pension scheme deficit or surplus and Unfunded Retirement Benefit Scheme and Post-Retirement Medical Benefits pension related liabilities under the SSA. These provisions or assets are based on the relevant share of the actuarial deficit or surplus and allocated on the basis of pensionable salaries. Movements in these provisions or assets are recorded as exceptional items due to their size and nature.

As more than one employer participates in the LHR Airports Limited defined benefit pension scheme and each employer is unable to identify its share of the underlying assets and liabilities in the scheme on a consistent and reasonable basis, the Company accounts for the scheme in accordance with the SSA. Additionally the Heathrow Airport Holdings Group discloses information about the total scheme surplus or deficit.

Current and deferred taxation

The tax expense for the year comprises current and deferred tax. Tax is recognised in the profit and loss account, except to the extent that it relates to items recognised directly in reserves. In this case, the tax is also recognised in reserves.

Current tax liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the balance sheet date. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation.

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.

Deferred taxation is determined using the tax rates and laws that have been enacted, or substantively enacted, by the balance sheet date and are expected to apply in the periods in which the timing differences are expected to reverse.

Share capital

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

Preference shares

Preference shares are classified as a liability where in substance the shares and related dividends have terms similar to a liability and not share capital. Features that indicate that presentation as a liability is appropriate include a dividend that is payable for a fixed or determinable amount at a fixed or determinable future date and where redemption is at a predetermined amount and date or at the option of the preference share holder. Where presentation as a liability is considered appropriate the associated dividend expense is shown within interest.

Accounting policies for the year ended 31 December 2012 *continued*

Dividend distribution
A dividend distribution to the Company's shareholder is recognised as a liability in the Company's financial statements in the period in which the shareholder's right to receive payment of the dividend is established. Interim dividends are recognised when paid.

Foreign currency
Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the entity operates. The financial statements are presented in Sterling, which is the Company's functional currency.

Transactions denominated in foreign currencies are translated into Sterling using the exchange rates prevailing at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated into Sterling at the rates of exchange ruling at the reporting date. Differences arising on translation are charged or credited to the profit and loss account.

Cash flow statement and related party transactions
The ultimate parent entity in the UK is 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 2012. The results are also included in the audited consolidated financial statements of Heathrow (SP) Limited for the year ended 31 December 2012 (intermediate parent entity and the smallest group to consolidate these financial statements). They are also included in the audited consolidated financial statements of Heathrow Finance plc and Heathrow Airport Holdings Limited for the year ended 31 December 2012. Consequently, the Company has taken advantage of the exemption from preparing a cash flow statement under the terms of FRS 1 *Cash Flow Statements (revised 1996)*. Instead, a summary cash flow statement has been provided on a voluntary basis in a note to the financial statements.

The Company is exempt under the terms of FRS 8 *Related Party Disclosures* from disclosing related party transactions with entities that are wholly owned subsidiaries of the FGP Topco Limited group.

Significant accounting judgements and estimates for the year ended 31 December 2012

In applying the Company'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 believes that the following areas present the greatest level of uncertainty.

Investment properties

Investment properties were valued at a fair value by CBRE Limited, Chartered Surveyors. The valuations were prepared in accordance with relevant accounting standards 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 81% (2011: 78%) of the investment properties comprise car parks and airside assets at Heathrow airport ('Heathrow') that are considered less vulnerable to market volatility than the overall market. Independent valuations were obtained for 100% of the investment properties.

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

1 Segment information

The directors consider the business has only one segment. All of the Company's turnover arises in the United Kingdom and relates to continuing operations. Additional details of the turnover generated by each of the Company's key activities are given below:

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Turnover		
Aeronautical income	**1,279.7**	1,149.6
Retail income	**460.1**	435.4
Operational facilities and utilities income	**162.9**	148.0
Property rental income	**102.5**	102.1
Heathrow Express rail income[1]	**116.0**	111.1
Other income	**102.9**	101.0
	2,224.1	2,047.2

[1] The Company is entitled to all receipts relating to HEX, the express rail service between Heathrow and Central London, but the day-to-day operation of HEX is undertaken by Heathrow Express Operating Company Limited on behalf of the Company for which a management fee is charged and included within 'Intra-group charges/other' in Note 2.

2 Operating costs - ordinary

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Wages and salaries	**230.8**	208.3
Social security	**20.6**	18.3
Pensions	**31.7**	24.2
Other staff related costs	**8.2**	11.3
Employment costs[1]	**291.3**	262.1
Maintenance expenditure	**120.9**	110.6
Utility costs	**87.5**	89.1
Rents and rates	**126.3**	113.2
General expenses	**119.9**	107.4
Retail expenditure	**25.8**	22.8
Intra-group charges/other	**207.0**	221.6
Police costs	**28.2**	28.8
Aerodrome navigation service charges	**54.0**	52.6
Depreciation	**470.0**	468.3
Gain on disposal of tangible fixed assets	**(0.5)**	(0.2)
	1,530.4	1,476.3

[1] Employment costs include recharges from LHR Airports Limited for employee services to the Company. Refer to the SSA in the Accounting policies.

Rentals under operating leases

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Operating costs include:		
Plant and machinery	**28.0**	26.4
Other operating leases	**16.7**	14.4

Notes to the financial statements for the year ended 31 December 2012 *continued*

2 Operating costs - ordinary *continued*

Auditor's remuneration

Audit fees and non-audit fees for the current and preceding financial years were borne by LHR Airports Limited and recharged in accordance with the SSA as described within the Accounting policies.

	Year ended 31 December 2012 £'000	Restated[1] Year ended 31 December 2011 £'000
Fees payable to the Company's auditor for the audit of the Company's annual accounts:		
Audit of the Company pursuant to legislation	**410**	422
Non audit fees payable to the Company's auditor and their associates for other services specific to the Company:		
Audit related assurance services	**157**	51
Tax compliance services	**4**	56
Other tax services	**-**	88
Other assurance services	**258**	412
Corporate finance services	**1**	-
Other services	**-**	184
Total non-audit fees	**420**	791
Total fees	**830**	1,213

[1] The presentation has been restated to be consistent with amended disclosure requirements.

Employee information

The Company has no employees (2011: nil). Staff engaged in the operation of Heathrow are employed by LHR Airports Limited which bears the related staff costs and recharges all such costs directly to the Company as a part of the SSA as described in the Accounting policies. The average number of employees of LHR Airports Limited engaged in the operation of Heathrow during the year was 5,278 (2011: 5,265). The number of employees does not include headcount related to central support functions for the Company which are rendered by LHR Airports Limited and charged as intra-group charges in accordance with the SSA.

Directors' remuneration

	Year ended 31 December 2012 £'000	Year ended 31 December 2011 £'000
Directors' remuneration		
Aggregate emoluments[1 2 3]	**2,405**	1,707
Value of company pension contributions to defined contribution scheme	**330**	131
Termination benefits	**-**	398
	2,735	2,236

[1] For the year ended 31 December 2012 aggregate emoluments includes accrued salaries, allowances, bonuses and amounts payable under Long Term Incentive Plans ('LTIP').
[2] £417,000 of bonus was paid in cash in 2012 (2011: £624,000).
[3] From October 2012 all members of Heathrow Airport Limited Executive Committee became directors of the Company.

José Leo was a director of a number of companies within the Heathrow Airport Holdings Group, including LHR Airports Limited, during the year. His remuneration for the year ended 31 December 2012 was disclosed in the financial statements of Heathrow Airport Holdings Limited (2011: BAA Limited). The directors do not believe it is possible to accurately apportion his remuneration to individual companies based on services provided.

The directors participate in various Long Term Incentive Performance Cash Plans (the 'Plans') operated by LHR Airports Limited. In respect of the Plans, a cash amount is granted which could vest in future periods contingent on achieving or surpassing EBITDA, Return on equity and other operational targets over a three year period. For the year ended 31 December 2012, the directors' remuneration includes £189,000 payable in 2013 (2011: £147,000 paid in 2012) in respect of the 2010 Plans after certain targets were met over the three year period from 2010 to 2012. As the financial performance in respect of the 2011 and 2012 Plans is uncertain at this stage, no value in relation to these awards is included above.

Notes to the financial statements for the year ended 31 December 2012 *continued*

2 Operating costs - ordinary *continued*
Directors' remuneration continued

	Year ended 31 December 2012 £'000	Year ended 31 December 2011 £'000
Highest paid director's remuneration		
Aggregate emoluments[1 2]	**563**	663
Value of pension contributions to defined contribution scheme	**58**	32
	621	695

[1] For the year ended 31 December 2012 aggregate emoluments includes accrued salary, allowances, bonus and amounts payable under LTIP.
[2] £186,000 of bonus was paid in cash in 2012 (2011: £264,000).

The highest paid director also participates in various Plans operated by LHR Airports Limited. In respect of the Plans, a cash amount is granted which could vest in future periods contingent on achieving or surpassing EBITDA, Return on equity and other operational targets over a three year period. For the year ended 31 December 2012, the highest paid director's remuneration includes £64,000 payable in 2013 (2011: £69,000 paid in 2012) in respect of the 2010 Plans after certain targets were met over the three year period from 2010 to 2012. As the financial performance in respect of the 2011 and 2012 Plans is uncertain at this stage, no value in relation to these awards is included above.

	Year ended 31 December 2012 Number	Year ended 31 December 2011 Number
Number of directors who:		
are members of a defined benefit pension scheme	**3**	1
are members of a defined contribution pension scheme	**4**	3

None of the directors (2011: none) exercised any share options during the year in respect of their services to the Company and no shares (2011: none) were received or became receivable under LTIPs.

3 Exceptional items

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Pension charge	**(151.2)**	(33.3)
Operating costs – exceptional: other	**-**	(10.8)
Total operating exceptional items	**(151.2)**	(44.1)
Non- operating exceptional impairment of fixed assets	**(5.1)**	-
Total exceptional items	**(156.3)**	(44.1)

During 2012 there was a net exceptional pension charge of £151.2 million (2011: £33.3 million). This includes the Company's share of the movement in the LHR Airports Limited defined benefit pension scheme, Unfunded Retirement Benefit Scheme and Post-Retirement Medical Benefits pension related liabilities.

For the year ended 31 December 2011 operating exceptional costs of £10.8 million were incurred, £11.0 million in relation to the Airtrack rail project which the Company has decided not to pursue and a £0.2 million reorganisation credit.

As a result of a change in the expected future use of automated immigration systems an impairment of £5.1 million has been recognised in advance of their anticipated sale. This accounting change is not expected to have an impact on those costs being included in the airport's regulatory asset base and is not expected to have a cash impact.

Notes to the financial statements for the year ended 31 December 2012 *continued*

4 Net interest payable and similar charges

	Note	**Year ended 31 December 2012 £m**	Year ended 31 December 2011 £m
Interest receivable			
Interest receivable from other group undertakings[1]		**140.9**	124.5
Interest receivable on bank deposits		**0.3**	0.2
		141.2	124.7
Interest payable			
Interest payable to other group undertakings[2]		**(622.7)**	(587.4)
Interest on bank borrowings		**(33.6)**	(79.1)
Facility fees and other charges		**(18.6)**	(21.5)
Net interest payable on derivative financial instruments		**(27.8)**	(62.6)
Dividend payable on irredeemable preference shares of £0.01 each: 5.34p per share (2011: 5.01p per share)		**(1.2)**	(1.1)
		(703.9)	(751.7)
Fair value loss on financial instruments		**(66.1)**	(75.8)
Interest capitalised[3]	*6*	**99.8**	26.9
Net interest payable and similar charges		**(529.0)**	(675.9)

1 These amounts relate primarily to interest accrued on balances due from Heathrow (SP) Limited (Note 9).
2 These amounts relate mainly to interest due on the loan from Heathrow (AH) Limited (formerly BAA (AH) Limited) and BLA with Heathrow Funding Limited (Note 13).
3 Following significant refinancing activity during the year, the Company has reassessed the applicable pool of general borrowing costs upon which interest has been capitalised. This has led to an increase in the capitalised interest rate to 4.84% compared to 2.04% for the previous year.

Notes to the financial statements for the year ended 31 December 2012 *continued*

5 Tax on profit/(loss) on ordinary activities

	Note	**Year ended 31 December 2012 £m**	Year ended 31 December 2011 £m
Current tax			
Group relief payable		**86.3**	57.9
Adjustments in respect of prior periods		**(1.2)**	(9.4)
Total current tax charge		**85.1**	48.5
Deferred tax			
Origination and reversal of timing differences:			
Current period		**(44.2)**	(68.3)
Prior period		**(1.0)**	6.1
Change in tax rate		**(16.4)**	(21.3)
Total deferred tax	*14*	**(61.6)**	(83.5)
Tax charge/(credit) on loss on ordinary activities		**23.5**	(35.0)

Reconciliation of tax charge

The standard rate of current tax for the year, based on the UK standard rate of corporation tax, is 24.5% (2011: 26.5%). The actual tax charge for the current and prior years differs from the standard rate for the reasons set out in the following reconciliation:

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Profit/(loss) on ordinary activities before tax	**8.4**	(149.1)
Tax charge/(credit) on profit/(loss) on ordinary activities at 24.5% (2011: 26.5%)	**2.1**	(39.5)
Effect of:		
Permanent differences	**37.7**	29.1
Depreciation for the year in excess of capital allowances	**43.6**	75.3
Capitalised interest	**(23.0)**	(6.7)
Other short term timing differences	**25.9**	(0.3)
Adjustments to tax charge in respect of prior periods	**(1.2)**	(9.4)
Current tax charge for the year	**85.1**	48.5

It was substantively enacted at the reporting date that the standard rate of corporation tax in the UK will change to 23% with effect from 1 April 2013. Other than this change and the unprovided deferred tax discussed at note 14, there are no items which would materially affect the future tax charge.

Notes to the Financial Statements for the year ended 31 December 2012 *continued*

6 Tangible fixed assets

	Note	Investment properties £m	Land held for development £m	Terminal complexes £m	Airfield £m	Rail assets £m	Other land and buildings £m	Plant equipment & other assets £m	Assets in the course of construction £m	Total £m
Cost or valuation										
1 January 2012		1,644.8	48.0	7,654.0	1,057.5	1,382.4	97.6	610.4	1,819.8	14,314.5
Additions at cost		9.4	-	2.0	-	-	0.1	7.1	1,140.5	1,159.1
Transfers to completed assets		(1.7)	-	395.7	4.8	2.2	10.1	35.4	(446.5)	-
Interest capitalised	*4*	-	-	-	-	-	-	-	99.8	99.8
Disposals		-	-	(27.8)	(1.0)	(4.3)	(0.1)	(17.0)	-	(50.2)
Revaluation	*16*	45.9	0.9	-	-	-	-	-	-	46.8
31 December 2012		**1,698.4**	**48.9**	**8,023.9**	**1,061.3**	**1,380.3**	**107.7**	**635.9**	**2,613.6**	**15,570.0**
Depreciation										
1 January 2012		-	-	(2,339.4)	(251.8)	(343.5)	(33.3)	(426.1)	-	(3,394.1)
Depreciation charge	*2*	-	-	(334.5)	(30.8)	(40.9)	(5.5)	(58.3)	-	(470.0)
Impairment	*3*	-	-	-	-	-	-	(3.2)	(1.9)	(5.1)
Disposals		-	-	27.8	1.0	4.3	-	17.0	-	50.1
Reclassifications		-	-	-	-	0.1	-	0.3	-	0.4
31 December 2012		**-**	**-**	**(2,646.1)**	**(281.6)**	**(380.0)**	**(38.8)**	**(470.3)**	**(1.9)**	**(3,818.7)**
Net book value 31 December 2012		**1,698.4**	**48.9**	**5,377.8**	**779.7**	**1,000.3**	**68.9**	**165.6**	**2,611.7**	**11,751.3**
Net book value 31 December 2011		1,644.8	48.0	5,314.6	805.7	1,038.9	64.3	184.3	1,819.8	10,920.4

6 Tangible fixed assets *continued*

Valuation
Investment properties and land held for development were valued at open market value by CBRE Limited, Chartered Surveyors at £1,747.3 million (2011: £1,692.8 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 surplus of £46.8 million (2011: surplus of £47.1 million) has been recognised in the revaluation reserve.

Remaining terminal complexes, airfield infrastructure, plant and equipment and other land and buildings have been shown at historical cost.

Historical cost
The historical cost of investment properties and land held for development at 31 December 2012 was £601.8 million (2011: £593.2 million).

Other land and buildings
Other land and buildings are freehold except for certain short leasehold properties with a net book value at 31 December 2012 of £14.6 million (2011: £16.9 million).

Assets in the course of construction
Assets in the course of construction primarily consist of projects for work on the new Terminal 2 and its satellite building. They also include the Terminal 3 Integrated baggage system which incorporates a new baggage facility.

Capitalised interest
Included in the net book value of fixed assets are interest costs of £934.5 million (2011: £871.9 million). £99.8 million (2011: £26.9 million) has been capitalised in the year at a capitalisation rate of 4.84% (2011: 2.04%) based on a weighted average cost of borrowings.

Following the significant refinancing activity during the year, the Company has reassessed the applicable pool of general borrowing costs upon which interest has been capitalised. This has led to an increase in the capitalised interest rate to 4.84% compared to 2.04% for the previous year.

A tax deduction of £99.8 million (2011: £26.9 million) for capitalised interest was taken in the year. 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.

Leased assets
The Company had assets rented to third parties under operating leases as follows:

	31 December 2012 £m	31 December 2011 £m
Cost or valuation	**2,388.1**	2,328.0
Accumulated depreciation	**(224.3)**	(199.1)
Net book amount	**2,163.8**	2,128.9

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

7 Investments

	£m
Cost as at 1 January and 31 December 2012	**3.8**

Subsidiary	**Nature of business**	**% of share capital held**	**Class of share**
Heathrow Express Operating Company Limited	Railway Operator	100	Ordinary shares of £1 each

In the opinion of the directors, the aggregate value of the shares in the subsidiary undertaking is not less than the aggregate of the amount at which they are stated in the Company’s Balance sheet.

Notes to the Financial Statements for the year ended 31 December 2012 *continued*

8 Stocks

	31 December 2012 £m	31 December 2011 £m
Raw materials and consumables	**7.2**	6.0

The replacement cost of raw materials and consumables at 31 December 2012 and 31 December 2011 was not materially different from the amount at which they are included in the Balance sheet.

9 Debtors

	31 December 2012 £m	31 December 2011 £m
Due within one year:		
Trade debtors	**156.1**	150.6
Amounts owed by group undertakings – interest free[1]	**10.6**	38.3
Amounts owed by group undertakings – pensions[2]	**-**	26.9
Other debtors	**34.3**	49.5
Prepayments	**39.9**	27.2
Interest receivable	**56.9**	12.0
Net interest receivable on derivative financial instruments	**19.8**	19.8
Derivative interest prepayment (Note 12)	**16.8**	-
	334.4	324.3
Due after more than one year:		
Amounts owed by group undertakings – interest bearing[3]	**1,945.6**	1,756.0
Derivative financial instruments (Note 12)	**0.4**	0.5
Derivative interest prepayment (Note 12)	**2.5**	-
Prepaid debt fees	**9.8**	-
Prepayment	**15.2**	-
	1,973.5	1,756.5
Total debtors	**2,307.9**	2,080.8

[1] Amounts owed by group undertakings – interest free largely relates to external payments received by LHR Airports Limited under the SSA on behalf of the Company which will be remitted in due course. The balance in 2011 mainly related to interest prepayment on the advances from Heathrow Funding Limited which was released during the period (Note 13).

[2] During 2012, LHR Airports Limited defined benefit pension scheme went into a deficit position (2011: surplus) and as such, its share allocated to the Company sits within Provisions (2011: Debtors – Amounts owed by group undertakings – pensions).

[3] Amounts owed by group undertakings – interest bearing represents a loan receivable from Heathrow (SP) Limited. It has a fixed interest rate of 7.57%.

10 Current asset investments

	31 December 2012 £m	31 December 2011 £m
Short-term deposits	**32.5**	21.0

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 £32.5 million as at 31 December 2012 (2011: A-1+ held assets of £21.0 million)

Notes to the Financial Statements for the year ended 31 December 2012 *continued*

11 Creditors: amounts falling due within one year

	Note	**31 December 2012 £m**	31 December 2011 £m
Bank overdraft		**23.8**	-
Trade creditors[1]		**97.3**	115.4
Capital creditors		**263.3**	245.4
Amounts owed to group undertakings – interest free[2]		**16.2**	10.2
Amounts owed to group undertakings – interest bearing[3]		**31.9**	-
Borrowings from group undertakings – interest bearing	*13*	**439.1**	691.5
External borrowings	*13*	**39.1**	39.1
Corporation tax payable		**6.4**	6.0
Group relief payable		**42.2**	32.2
Other creditors		**7.4**	16.6
Other taxes and social security costs		**5.9**	6.0
Deferred income		**31.0**	28.0
Net interest payable on derivative financial instruments		**10.2**	13.1
Interest payable		**183.3**	101.8
		1,197.1	1,305.3

1 Trade creditors are non-interest bearing and generally on 30-day terms.
2 Amounts owed to group undertakings – interest free largely relate to external payments made by LHR Airports Limited under the SSA on behalf of the Company.
3 Amounts owed to group undertakings – interest bearing represents a loan payable to Heathrow Express Operating Company Limited accruing interest at Bank of England base rate + 1.5% and a loan payable to Heathrow Funding Limited.

12 Creditors: amounts falling due after more than one year

	Note	**31 December 2012 £m**	31 December 2011 £m
Loans from Heathrow Funding Limited	*13*	**10,066.4**	**7,350.3**
External borrowings	*13*	**652.8**	**2,265.0**
Preference shares – redeemable[1]		**0.1**	**0.1**
Preference shares – irredeemable[1]		**0.2**	**0.2**
Derivative financial instruments		**345.4**	**167.2**
Deferred income		**0.1**	**0.5**
Other creditors		**4.1**	**-**
		11,069.1	**9,783.3**

1 The Company has 100,000 £1 redeemable preference shares in issue which carry an entitlement to an annual dividend fixed by reference to the prospective real redemption rate, based on projected inflation rate of 3%, of 2.5% index linked 2016 UK gilts, uplifted for movements in the RPI. The preference shares of £1 are held by the immediate parent company, Heathrow (AH) Limited (formerly BAA (AH) Limited), and are redeemable by the Company on 16 January 2016 at £1.37 per share, uplifted for movements in the RPI. On a return of capital on winding up or capital reduction, the holders of the preference shares shall be entitled to a sum calculated in accordance with the Articles of Association, in priority to any payment to the holders of any other class of shares other than the holders of irredeemable preference shares. The Company also has 21,960,014 irredeemable £0.01 preference shares in issue which carry an entitlement to an annual dividend, uplifted by reference to the RPI. The holder of the preference shares shall only be entitled to attend and vote at General Meetings at which a resolution is proposed to abrogate, vary or modify their rights, in which case preference and ordinary shares shall carry equal voting rights. Both classes of preference shares are presented within creditors.

Derivative financial instruments not included at fair value

The Company enters into derivative transactions, principally interest rate swaps and foreign exchange contracts. The purpose of these transactions is to manage interest rate and currency risks arising from the Company's operations and sources of finance.

Interest rate swaps

As at 31 December 2012, the Company had interest rate swap contracts outstanding with bank counterparties with notional values totaling £310.0 million (2011: £1,896.0 million). The swaps have fixed interest payments at rates varying from 4.6% to 5.1% and floating interest receipts based on three and six month Libor rates. At that date, these financial instruments had a mark-to-market liability of £79.8 million (2011: £300.8 million).

Heathrow Funding Limited has entered into derivative transactions with external counterparties, some of which were issued to the Company as back-to-back hedges. As at 31 December 2012, the total notional amount of these swaps was £5,199.0 million which had a mark-to-market liability of £535.9 million (2011: £4,021.8 million notional with a mark-to-market liability of £217.7 million).

The amounts recognised on the Balance sheet in relation to these financial instruments represent accrued interest and accretion and unamortised portion of interest prepayment and fair value on the date of novation. These are included in 'Net interest receivable on derivative financial instruments', 'Derivative interest prepayment' and 'Derivative financial instruments' in Note 9 'Debtors' and 'Net interest payable on derivative financial instruments (Note 11 'Creditors falling due within one year') and 'Derivative financial instruments' above.

12 Creditors: amounts falling due after more than one year *continued*

Foreign exchange contracts

Foreign exchange contracts are used to manage foreign currency exposures relating to future capital expenditure. As at 31 December 2012, the Company had various foreign exchange contracts with a total notional amount in Sterling terms of £33.6 million which had a fair value gain of £0.3million (2011: £4.3 million notional with a fair value loss of £nil).

13 Borrowings

	31 December 2012 £m	31 December 2011 £m
Current borrowings		
Secured		
Bank loans	**39.1**	39.1
Borrower Loan Agreement advances from Heathrow Funding Limited	**429.4**	677.8
Unsecured		
Loan from Heathrow (AH) Limited	**9.7**	13.7
Total current borrowings	**478.2**	730.6
Non-current borrowings		
Secured		
Borrower Loan Agreement advances from Heathrow Funding Limited	**10,066.4**	7,350.3
Capital expenditure facility	**-**	1,395.0
Revolving credit facility	**289.9**	-
Other bank loans	**362.9**	870.0
Total non-current borrowings	**10,719.2**	9,615.3
Total borrowings	**11,197.4**	10,345.9

Borrowings from group undertakings

Unsecured borrowings from group undertakings represent the loan advanced by parent, Heathrow (AH) Limited, to the Company. The loan bears an interest rate of 7.57% per annum.

During the year, following new bond issues by Heathrow Funding Limited, further advances were made to the Company for a total amount of £3,077.2 million, net of transaction costs.

The effective interest rate on the BLA advances varies between 2.64% and 7.40%.

All of the above facilities are carried at amortised cost.

The Company, together with Stansted Airport Limited, had £1,693.0 million undrawn committed borrowing facilities available as at 31 December 2012 (2011: £1,355.0 million).

In addition, as at 31 December 2012, there was a gross overdraft limit between the Company and Stansted Airport Limited up to a maximum gross overdraft balance of £75.0 million (2011: £75.0 million).

Notes to the Financial Statements for the year ended 31 December 2012 *continued*

14 Provisions for liabilities and charges

	Deferred tax (a) £m	Reorganisation Costs (b) £m	Pension costs (c) £m	Other (d) £m	Total £m
1 January 2012	204.6	3.9	17.6	7.1	233.2
Utilised in the year	-	(3.9)	-	(4.9)	(8.8)
Charged to profit and loss account	-	2.1		2.5	4.6
Released to profit and loss account	(61.6)	-	-	-	(61.6)
Movement in pensions	-	-	77.3	-	77.3
31 December 2012	**143.0**	**2.1**	**94.9**	**4.7**	**244.7**

(a) Deferred tax

Analysis of the deferred tax balances is as follows:

	31 December 2012 £m	31 December 2011 £m
Excess of capital allowances over depreciation	**161.7**	198.9
Other timing differences	**(18.7)**	5.7
	143.0	204.6

	Unprovided	
	31 December 2012 £m	31 December 2011 £m
Tax on chargeable gains if investment properties were sold at their current valuations	**201.2**	212.5
Tax on rolled-over gains if replacement assets were sold at their current valuations	**8.1**	5.0
	209.3	217.5

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

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. The total amount of tax unprovided for is £209.3 million (2011: £217.5 million). At present it is not envisaged that this tax will become payable in the foreseeable future.

The Finance Act 2012 enacted a reduction in the rate of corporation tax to 24% from 1 April 2012 and 23% from 1 April 2013. As a result the Company's deferred tax balances, which were previously provided at 25%, have been re-measured at the rate of 23%. This has resulted in a reduction in the net deferred tax liability of £16.4 million, with £16.4 million credited to the profit and loss account.

(b) Reorganisation costs

The costs associated with the Heathrow Airport Holdings Group's reorganisation programmes primarily relate to various restructuring processes designed to reduce the size and cost of the organisation. These costs are for severance and pension payments only and are expected to be utilised in early 2013.

(c) Pension costs

The closing provision is the share of the net deficit of the LHR Airports Limited defined benefit pension scheme, Unfunded Retirement Benefit Scheme and Post-Retirement Medical Benefits pension related liabilities allocated to the Company.

At 31 December 2012, £76.2 million represents the share of the LHR Airports Limited defined benefit pension scheme deficit (2011: surplus of £26.9 million classified in Debtors – Amounts owed to group undertakings – pensions). The remaining £18.7 million (2011: £17.6 million) is held for historical accumulated past service pension costs borne by LHR Airports Limited in relation to Unfunded Retirement Benefit Scheme and Post-Retirement Medical Benefits pension related liabilities. The movement in the year is mainly due to the LHR Airports Limited defined benefit pension scheme moving from a surplus to a deficit position.

(d) Other

These provisions are largely due to onerous contracts primarily relating to property leases. All amounts are expected to be utilised within two years.

15 Share capital

	£
Authorised	
31 December 2012:	
1,575,570,317 ordinary shares of £0.30 each	472,671,095
385,000,000 preference shares – redeemable of £1 each	385,000,000
500,000,000 preference shares – irredeemable of £0.01 each	5,000,000

	£
Called up, allotted and fully paid	
1 January 2012:	
857,570,317 ordinary shares of £1 each	857,570,317
100,000 preference share – redeemable of £1 each	100,000
21,960,014 preference shares – irredeemable of £0.01 each	219,600
31 December 2012:	
1,575,570,317 ordinary shares of £0.30 each	**472,671,095**
100,000 preference shares – redeemable of £1 each	**100,000**
21,960,014 preference shares – irredeemable of £0.01 each	**219,600**

Following the capitalisation, allotment and the reduction of capital (described in Note 16), the nominal value of the ordinary share capital of the Company was reduced to 30 pence per ordinary share.

16 Reserves

	Share Capital £m	Share premium reserve £m	Revaluation reserve £m	Profit and loss reserve £m	Total £m
1 January 2012	857.6	23.2	1,099.5	(267.5)	1,712.8
Capitalisation of Revaluation reserve	718.0	-	(718.0)	-	-
Reduction of Share premium	-	(23.2)	-	23.2	-
Reduction of Share capital	(1,102.9)	-	-	1,102.9	-
Dividends paid	-	-	-	(150.8)	(150.8)
Loss for the financial year	-	-	-	(15.1)	(15.1)
Unrealised gain on revaluation of investment properties	-	-	46.8	-	46.8
Realised gain on tangible fixed assets	-	-	1.1	(1.1)	-
Other Profit and loss reserve movement	-	-	-	(0.5)	(0.5)
31 December 2012	**472.7**	**-**	**429.4**	**691.1**	**1,593.2**

On 21 June 2012, the shareholders and directors of the Company approved a capitalisation of the revaluation reserve of £718.0 million by issuing 718 million of ordinary shares at £1 each. A reduction of the enhanced share capital of £1,102.9 million and a reduction of the share premium reserve of £23.2 million was then approved, which amounts to an overall capital reduction of £1,126.1 million that created positive distributable reserves to allow the Company to pay dividends.

During the year ended 31 December 2012, the Company paid dividends of £150.8 million to Heathrow (AH) Limited being £20.0 million on 21 June 2012, £21.0 million on 10 August 2012, £60.0 million on 19 September 2012 and £49.8 million on 20 December 2012.

17 Commitments

Commitments for capital expenditure

	31 December 2012 £m	31 December 2011 £m
Contracted for, but not accrued:		
Terminal 2	**624.8**	1,050.5
Western baggage product	**52.4**	45.5
Terminal restoration and modernisation	**28.9**	13.5
Capacity optimisation	**19.8**	7.5
IT projects	**14.6**	4.7
	740.5	1,121.7
Other projects	**45.2**	4.2
	785.7	1,125.9

Commitments under operating leases

At 31 December 2012, the Company was committed to making the following payments during the next year in respect of operating leases:

	31 December 2012		31 December 2011	
	Land & buildings £m	**Other leases £m**	Land & buildings £m	Other leases £m
Leases which expire:				
within one year	**0.2**	**0.1**	0.1	0.1
within two to five years	**1.9**	**0.4**	1.6	0.6
after five years	**11.5**	**31.8**	10.4	31.7
	13.6	**32.3**	12.1	32.4

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

A significant portion of the commitments classified as 'other' relates to electricity supply equipment at the airports leased on agreement with UK Power Networks Services Ltd ('UPNS'). The lease expires in 2083. The amounts disclosed are the total estimated charges under the agreement including both the actual lease commitment and the significant maintenance element of the fee payable to UPNS as neither the Company nor UPNS are able to split the base fee between a 'capital' and 'maintenance' charge. The commitment has been discounted at the Company's incremental borrowing rate.

Commitments under contractual obligations

The Company has a contractual commitment to purchase electricity that is used to satisfy physical delivery requirements for electricity usage of the Company until March 2013. Such commitments are for the normal purchase, sale or usage and hence are accounted for as ordinary purchase contracts. At 31 December 2012, the estimated minimum commitment for the future purchase of electricity under this contract totalled £4.2 million (2011: £30.5 million).

Other commitments

The Company has operated a blight compensation scheme relating to properties that might be affected by potential future runway developments. However, this scheme was closed following the change in government policy in relation to runway developments in South East England. The Company has a remaining commitment to purchase one property at 31 December 2012. All properties purchased under these schemes are included within investment properties at a value of £59.4 million as at 31 December 2012 (2011: £51.6 million).

In June 2006, the government announced its conclusions for the 2006-2012 night flights regime at the Heathrow Airport Holdings Group's London airports. The government was expected to consult on proposals for the post 2012 night flights regime during 2011. However, the government is conducting a consultation and review of aviation policy which includes reference to noise insulation and mitigation schemes. In addition they have announced that the existing night flights regime has been extended until October 2014. The process for replacing the existing night flights regime is expected to involve two stages, an initial consultation in 2012 and a further consultation in 2013 which will set out specific proposals for the new regime taking into account the revised aviation policy. Until these review processes are complete, the Company is unable to quantify potential future noise insulation and mitigation obligations.

Notes to the Financial Statements for the year ended 31 December 2012 *continued*

17 Commitments *continued*

The trustees of the LHR Airports Limited defined benefit pension scheme and the Heathrow Airport Holdings Group concluded the pension scheme's 30 September 2010 triennial valuation in December 2011 and agreed a schedule of cash contributions of £97 million per annum (out of which £24 million related to scheme deficit reduction) that became effective from 1 January 2012. Following the disposal of Edinburgh Airport Limited, the schedule of cash contributions has been reduced to £94 million per annum for 2013 and 2014. Approximately £71.6 million of the new amount will be met by the Company.

18 Contingent liabilities

The Company has contingent liabilities arising in the normal course of business amounting to £0.5 million at 31 December 2012 (2011: £205.5 million).

The Company, together with Stansted Airport Limited, Heathrow Express Operating Company Limited, Heathrow (SP) Limited and Heathrow (AH) Limited (together 'the Obligors') has granted security over their assets to secure their obligations to the Borrower Secured Creditors under their financing agreements. Each Obligor has also provided a guarantee in respect of the obligations of the other Obligors.

The Company, together with 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 their liabilities under the Borrower Account Bank Agreement.

BAA Pension Trust Company Limited has a right to receive up to approximately £289 million out of the proceeds of enforcement of the security granted by the Obligors, such right ranking pari passu with the senior (Class A) creditors to the Obligors.

19 Ultimate parent undertaking

The immediate parent undertaking of the Company is Heathrow (AH) Limited, a company registered in England and Wales.

The ultimate parent entity is FGP Topco Limited, which is the parent undertaking of the largest group to consolidate these financial statements. The shareholders of FGP Topco Limited are Hubco Netherlands B.V. (33.65%) (an indirect subsidiary of Ferrovial, S.A., Spain), Qatar Holding Aviation (20.00%) (a wholly owned subsidiary of Qatar Holdings LLC), Caisse de dépôt et placement du Québec (13.29%), Baker Street Investment Pte Ltd (11.88%) (an investment vehicle of the Government of Singapore Investment Corporation), Alinda Airports UK L.P. and Alinda Airports L.P. (11.18%) (investment vehicles managed by Alinda Capital Partners) and Stable Investment Corporation (10.00%) (an investment vehicle of the China Investment Corporation).

The Company's results are also included in the audited consolidated financial statements of Heathrow (SP) Limited for the year ended 31 December 2012, which is the parent undertaking of the smallest group to consolidate these financial statements. They are also included in the audited consolidated financial statements of Heathrow Finance plc, Heathrow Airport Holdings Limited and FGP Topco Limited for the year ended 31 December 2012.

Copies of the financial statements of FGP Topco Limited, Heathrow Airport Holdings Limited, Heathrow Finance plc and Heathrow (SP) Limited may be obtained by writing to the Company Secretarial Department at The Compass Centre, Nelson Road, Hounslow, Middlesex, TW6 2GW.

20 Summary cash flow statement

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Operating profit	**542.5**	526.8
Adjustments for:		
Depreciation (including exceptional depreciation)	**470.0**	479.2
Gain on disposal of tangible fixed assets	**(0.5)**	(0.2)
Working capital changes:		
Decrease in stock and debtors	**10.7**	18.7
(Decrease)/increase in creditors	**(9.8)**	16.8
Decrease in provisions	**(4.2)**	(6.0)
Difference between pension charge and cash contributions	**(36.9)**	(29.8)
Exceptional pension charge	**151.2**	33.3
Net cash inflow from operating activities	**1,123.0**	1,038.8
Net interest paid	**(362.7)**	(293.2)
Taxation - Group relief paid	**(74.6)**	(66.5)
Net capital expenditure	**(1,141.0)**	(843.8)
Dividends paid	**(150.8)**	-
Net cash outflow before use of liquid resources and financing	**(606.1)**	(164.7)
Management of liquid resources		
(Increase)/Decrease in short term deposits	**(11.5)**	20.0
Financing		
Drawdown of revolving credit facility	**307.0**	-
(Repayment)/drawdown of capital expenditure facility	**(1,395.0)**	95.0
Repayment of other facilities and other items	**(544.3)**	(1,338.9)
Swaps novated from Heathrow Funding Limited	**104.4**	-
Cancellation and restructuring of derivatives	**(97.8)**	(116.0)
Net movement in amounts with group undertakings	**2,298.3**	1,563.7
Settlement of accretion on index-linked instruments	**(80.0)**	(15.0)
(Decrease)/increase in cash[1]	**(25.0)**	44.1

[1] For the year ended 31 December 2012, included in Creditors: amounts falling due within one year is a bank overdraft of £23.8 million (2011: £nil).

Liquid resources are defined in the Accounting policies under 'Cash and current asset investments'.