

# **BAE Systems (Funding Two) Limited**

## **Annual report and financial statements**

**31 December 2016**

Registered number: 04333003



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## Directors' report

### Company registration

BAE Systems (Funding Two) Limited is a private company, limited by shares and registered in England and Wales with registered number 04333003.

### Review of business

The Company holds investments in group companies which are partly funded by loan notes bearing interest at floating rates. The interest payable on the loan notes is sufficiently covered by income from the investments.

There has been no change during the year in investments held.

### Principal risks and uncertainties

The management of the business and the execution of the Company's strategy are subject to a number of risks. The Company is part of the BAE Systems plc Group and the principal risks and uncertainties affecting the Group are discussed in more detail in the annual report of the Group.

Additional specific principal risks and uncertainties facing the Company concern the possible impairment of the value of its investment in BAE Systems Group subsidiary companies and changes in the US Dollar LIBOR rate.

### Results and dividends

The Company's profit for the financial year is \$139,957,831 (2015: \$139,961,787).

Dividends paid during the year comprise an interim dividend in respect of the year ended 31 December 2016 of \$139,250,000 (2015: \$140,000,000). The directors do not propose a final dividend for 2016.

### Looking forward

The directors do not expect any change in operations for the foreseeable future.

### Going concern

After making due enquiries, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.

### Directors and their interests

The directors who served during the year and at the date of this report were as follows:

B Chapman  
R Patara

The Board is not aware of any contract of significance in relation to the Company in which any director has, or has had, a material interest.

### Disclosure of information to auditor

The directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that he/she ought to have taken to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

**Directors' report** *(continued)*

**Auditor**

The auditor, KPMG LLP, has indicated its willingness to continue in office and in accordance with section 487(2) of the Companies Act 2006, has been reappointed.

**On behalf of the Board**



R Patara  
Director

24 May 2017

**Registered office:**  
Warwick House  
PO Box 87  
Farnborough Aerospace Centre  
Farnborough  
Hampshire  
GU14 6YU  
United Kingdom

## **Statement of directors' responsibilities in respect of the Directors' Report and the financial statements**

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

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 101 *Reduced Disclosure Framework*.

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; and
- make judgements and estimates that are reasonable and prudent.

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 have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

## **INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF BAE SYSTEMS (FUNDING TWO) LIMITED**

We have audited the financial statements of BAE Systems (Funding Two) Limited for the year ended 31 December 2016 set out on pages 7 to 14. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice), including FRS 101 *Reduced Disclosure Framework*.

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 set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate).

### **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 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with UK 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 is consistent with the financial statements.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and from reading the Directors' Report:

- we have not identified material misstatements in that report; and
- in our opinion, that report has been prepared in accordance with the Companies Act 2006.

### **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; or
- the directors were not entitled to take advantage of the small companies exemption from the requirement to prepare a strategic report.



**Andrew Bradshaw (Senior Statutory Auditor)**  
for and on behalf of KPMG LLP, Statutory Auditor  
*Chartered Accountants*  
KPMG LLP  
15 Canada Square  
London  
E14 5GL  
24 May 2017

**Income statement and statement of comprehensive income**  
for the year ended 31 December 2016

	Notes	2016 \$'000	2015 \$'000
Income from subsidiary companies		145,280	144,000
<b>Profit before finance costs and taxation</b>		<b>145,280</b>	<b>144,000</b>
Financial expense	2	(5,322)	(4,038)
<b>Profit before taxation</b>		<b>139,958</b>	<b>139,962</b>
Taxation expense	4	-	-
<b>Profit for the year</b>		<b>139,958</b>	<b>139,962</b>
<b>Total comprehensive income for the year</b>		<b>139,958</b>	<b>139,962</b>

The notes on pages 10 to 14 form part of the financial statements.

The results for 2016 and 2015 arise from continuing activities.

## Balance sheet

as at 31 December 2016

	Notes	2016 \$'000	2015 \$'000
<b>Non-current assets</b>			
Investments	5	3,010,000	3,010,000
<b>Current assets</b>			
Trade and other receivables	6	1,242,107	1,241,395
<b>Total assets</b>		<b>4,252,107</b>	<b>4,251,395</b>
<b>Current liabilities</b>			
Trade and other payables	7	(310,017)	(310,013)
<b>Total liabilities</b>		<b>(310,017)</b>	<b>(310,013)</b>
<b>Net assets</b>		<b>3,942,090</b>	<b>3,941,382</b>
<b>Capital and reserves</b>			
Issued share capital	8	3,701,000	3,701,000
Other reserves	8	241,032	241,032
Retained earnings / (deficit)		58	(650)
<b>Total equity</b>		<b>3,942,090</b>	<b>3,941,382</b>

Approved by the Board on 24 May 2017 and signed on its behalf by:



R Patara  
Director

Registered number: 04333003



**Statement of changes in equity**  
for the year ended 31 December 2016

	Notes	Issued share capital	Other reserves <sup>1</sup>	Retained earnings	Total equity
		\$'000	\$'000	\$'000	\$'000
At 1 January 2015		3,701,000	241,032	(612)	3,941,420
Profit for the year		-	-	139,962	139,962
Ordinary share dividends	8	-	-	(140,000)	(140,000)
At 31 December 2015		3,701,000	241,032	(650)	3,941,382
Profit for the year		-	-	139,958	139,958
Ordinary share dividends	8	-	-	(139,250)	(139,250)
<b>At 31 December 2016</b>		<b>3,701,000</b>	<b>241,032</b>	<b>58</b>	<b>3,942,090</b>

<sup>1</sup> The non-distributable portion of Other reserves is \$241,031,278 (2015: \$241,031,278).

## Notes to the financial statements

### 1 Accounting policies

#### Basis of preparation

These financial statements were prepared in accordance with Financial Reporting Standard (FRS) 101 Reduced Disclosure Framework. Amendments to FRS 101 (2014/15 cycle and other minor amendments) and Amendments to FRS 101 (2015/16 cycle) both effective for periods beginning on or after 1 January 2016 have been applied.

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards (IFRS) as adopted by the EU (EU-adopted IFRS), but makes amendments where necessary in order to comply with the Companies Act 2006 and has set out below where advantage of the FRS 101 disclosure exemptions has been taken:

- the requirements of paragraphs 10(d), 10(f), 16, 38A, 38B, 38C, 38D, 40A, 40B, 40C, 40D, 111 and 134 to 136 of IAS 1, Presentation of Financial Statements;
- the requirements of IAS 7, Statement of Cash Flows;
- the requirements of paragraphs 30 and 31 of IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors;
- the requirements of paragraphs 17 and 18A of IAS 24, Related Party Disclosures;
- the requirements in IAS 24, Related Party Disclosures, to disclose related party transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly owned by such a member; and
- the requirements of paragraphs 130(f)(ii), 130(f)(iii), 134(d) to 134(f) and 135(c) to 135(e) of IAS 36, Impairment of Assets.

The Company intends to continue to prepare its financial statements in accordance with FRS 101.

The Company is exempt under section 400 of the Companies Act 2006 from the requirement to prepare consolidated financial statements as it and its subsidiary companies are included by full consolidation in the consolidated financial statements of its ultimate parent, BAE Systems plc, a company registered in England and Wales. Accordingly, these financial statements present information about the Company as an individual company and not as a group.

The following paragraphs summarise the main accounting policies of the Company and have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of relevant financial assets and financial liabilities (including derivative instruments). The going concern basis has been applied in these financial statements. The functional currency of the Company is the US Dollar (\$), therefore the Company has adopted the US Dollar as its reporting currency.

#### Interest income and borrowing costs

Interest income and borrowing costs are recognised in the income statement in the period in which they are incurred.

#### Dividends

Dividends received and receivable are credited to the Company's income statement. Equity dividends paid on ordinary share capital are recognised as a liability in the period in which they are declared.

#### Investments

Fixed asset investments in shares in subsidiary companies and in shares in participating interests are stated at cost less provision for impairment.

#### Trade and other receivables

Trade and other receivables are stated at their cost less provision for bad debts. A provision for bad debt is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. Receivables with a short-term duration are not discounted.

A loss on provision for bad debt is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

#### Trade and other payables

Trade and other payables are stated at their cost.

## Notes to the financial statements (continued)

### 1 Accounting policies (continued)

#### Tax

Income tax expense comprises current and deferred tax. Current and deferred tax is recognised in profit or loss except to the extent that it relates to a business combination or items recognised directly in equity or other comprehensive income.

#### Current tax

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

#### Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for temporary differences:

- on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- related to investments in subsidiaries and equity accounted investments to the extent that it is probable that they will not reverse in the foreseeable future; and
- arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority and they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

### 2 Financial expense

	2016 \$'000	2015 \$'000
Net interest expense on amounts owed to group subsidiaries	(5,322)	(4,038)
<b>Financial expense</b>	<b>(5,322)</b>	<b>(4,038)</b>

### 3 Employees

The Company had no employees during the year (2015: nil)

None of the directors received any emoluments from the Company during the year. Both directors who served during the year were employed by BAE Systems plc and were remunerated through that company.

The directors did not provide any material qualifying services to the Company.

### 4 Taxation expense

	2016 \$'000	2015 \$'000
<b>Current taxation</b>		
Current tax charge	(9)	(7)
Less: double tax relief	9	12
Adjustments in respect of prior years	-	(5)
<b>Taxation expense</b>	<b>-</b>	<b>-</b>

## Notes to the financial statements (continued)

### 4 Taxation expense (continued)

#### Total Tax Reconciliation

The Company has not provided for corporation tax for the year as any profits will be covered by the surrender of losses from other Group companies, in respect of which no payment will be made.

The following reconciles the expected income tax expense, using the UK corporation tax rate, to the reported tax expense.

	2016 \$'000	2015 \$'000
<b>Profit before taxation</b>	<b>139,958</b>	<b>139,962</b>
<b>UK corporation tax rate</b>	<b>20.00%</b>	<b>20.25%</b>
Expected income tax expense on profit	(27,992)	(28,342)
Income not subject to tax	29,056	29,160
Imputed interest income	(4,588)	(5,578)
Apportioned controlled foreign company profits	(6,864)	(6,948)
Double tax relief	9	12
Losses received from Group companies	10,379	11,701
Adjustments in respect of prior years	-	(5)
<b>Taxation expense</b>	<b>-</b>	<b>-</b>

Provision for deferred tax is not required.

### 5 Investments

Carrying value	\$'000
At 1 January 2016 and 31 December 2016	3,010,000

#### Subsidiary companies at 31 December 2016

In accordance with Section 409 of the Companies Act 2006, a full list of subsidiary companies and significant holdings as at 31 December 2016 is disclosed below. Unless otherwise stated, all subsidiary companies and significant holdings are owned directly by BAE Systems (Funding Two) Limited and have a financial year end of 31 December.

Company name	Class of shares	Proportion of class (%)
<b>BAE Systems Finance (Ireland) Unlimited Company</b> Level 5, Block 4, Dundrum Town Centre Sandyford Road, Dundrum Dublin 16, D16 A4W6, Ireland	Ordinary shares of \$1	100%
<b>BAE Systems (Funding Three) Limited</b> Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hampshire, GU14 6YU, United Kingdom	Ordinary shares of \$1	100%

During the year an impairment review has been conducted of the investments held by the Company and no requirement for impairment has been identified.

Notes to the financial statements (continued)

6 Trade and other receivables

	2016 \$'000	2015 \$'000
<b>Current</b>		
Amounts owed by ultimate parent company	1,242,107	1,241,395
<b>Trade and other receivables</b>	<b>1,242,107</b>	<b>1,241,395</b>

7 Trade and other payables

	2016 \$'000	2015 \$'000
<b>Current</b>		
Amounts owed to group companies	(310,000)	(310,000)
Accruals - amounts owed to group companies	(17)	(13)
<b>Trade and other payables</b>	<b>(310,017)</b>	<b>(310,013)</b>

8 Share capital and other reserves

Share capital

	Number of \$1 Ordinary shares	Nominal value \$
<b>Issued and fully paid</b>		
At 1 January and 31 December 2016	3,701,000,100	3,701,000,100

Equity dividends

	2016 \$'000	2015 \$'000
Interim dividend paid for ordinary shares	139,250	140,000
<b>Equity dividends</b>	<b>139,250</b>	<b>140,000</b>

The directors have not proposed a final dividend for 2016.

Other reserves

	Other Reserves \$'000	Total \$'000
<b>At 1 January and 31 December 2015</b>	<b>241,032</b>	<b>241,032</b>
<b>At 31 December 2016</b>	<b>241,032</b>	<b>241,032</b>

Other Reserves

Other reserves reflects the accretion of the difference between the nominal value of the shares subscribed for by BAE Systems Holdings Inc. on 24 June 2002 and the final subscription price paid in instalments. This reserve is non-distributable. BAE Systems Holdings Inc. is a previous shareholder and all the shares in the Company have been held by BAE Systems (Holdings) Limited since 2005.

## Notes to the financial statements *(continued)*

### 9 Auditor's remuneration

The auditor's remuneration of \$3,154 (2015: \$3,851) has been borne by the ultimate parent company, BAE Systems plc.

### 10 Controlling parties

The immediate parent company is BAE Systems (Holdings) Limited and the ultimate parent company is BAE Systems plc. Both companies are incorporated in Great Britain and registered in England and Wales.

The consolidated accounts of BAE Systems plc are available to the public and may be obtained from:

6 Carlton Gardens  
London  
SW1Y 5AD

Website: [www.baesystems.com](http://www.baesystems.com)