



IMPERIAL
BRANDS

ANNUAL REPORT AND ACCOUNTS 2016

DELIVERING AGAINST **OUR STRATEGY**

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STRATEGIC REPORT

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WHO WE ARE

We are a fast-moving consumer goods company with great brands and great people.

Our name may have changed but our strategy, our values and our focus on generating sustainable shareholder returns remain the same.

Consumers around the world enjoy our Growth and Specialist Brands. These are the key assets in our portfolio, quality brands delivering quality growth.

We also have strong corporate brands. From a tobacco perspective we have Imperial Tobacco, home to most of our international tobacco operations, ITG Brands in the USA and Tabacalera, our premium cigar business.

Beyond tobacco we have Fontem Ventures, developing non-tobacco consumer experiences and currently focused on the growth of the blu e-vapour brand, and Logista, one of the largest distribution businesses in Europe.

The breadth of this brand focus is reflected in the name of our parent company: Imperial Brands perfectly captures the business we are today.

OUR VALUES

Our values express who we are and what we stand for, and capture the individual and collective behaviours we expect from everyone who works for us.

We're proud of our heritage and excited about the future.

The success of our strategy, the strength of our brands and the talents of our people will continue to generate quality growth in the years ahead.

We can



I engage



I own



We surprise



I am



We enjoy

OUR CORPORATE BRANDS

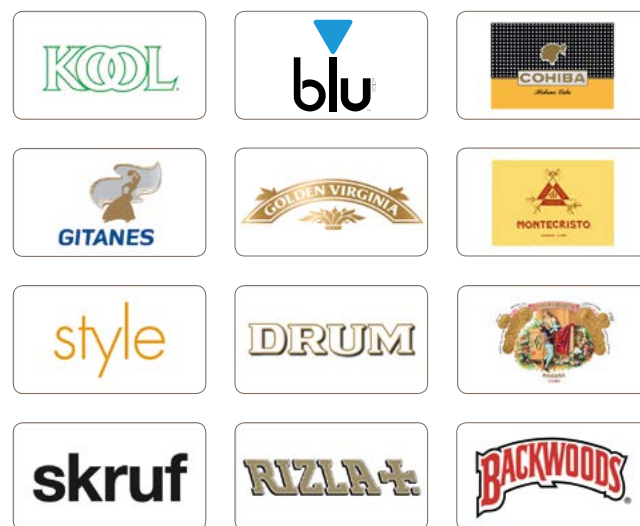


OUR CONSUMER BRANDS

GROWTH BRANDS



SPECIALIST BRANDS



OUR PERFORMANCE

DIVIDEND PER SHARE

+10%
155.2p

ADJUSTED EARNINGS PER SHARE ^{1,2}

+12%
249.6p

REPORTED EARNINGS PER SHARE

-62.7%
66.1p

GROWTH BRAND VOLUMES²

+4.3%
151bn

ADJUSTED OPERATING PROFIT¹

+10.4%
£3.5bn

REPORTED OPERATING PROFIT

+12.1%
£2.2bn

TOBACCO NET REVENUE^{1,2}

+9.7%
£7.2bn

CASH CONVERSION²

95%

ADJUSTED NET DEBT (INCLUDES THE £2.3 BILLION IMPACT OF FOREIGN EXCHANGE)

+£1.3bn
£12.9bn

ADJUSTED NET DEBT REDUCTION (AT CONSTANT CURRENCY)

£1bn

1. Changes in our adjusted results are presented on a constant currency basis.
2. KPIs used as bonus and LTIP performance criteria for Executive Directors. See Remuneration Report on page 51 for more information.

PERFORMANCE MEASURES

Measure	Explanation	Where used
Reported (GAAP)	Complies with International Financial Reporting Standards and the relevant legislation.	Throughout the report.
Adjusted (Non-GAAP)	Non-GAAP measures provide a useful comparison of performance from one period to the next. These measures are defined in the Accounting Policies on page 88.	Throughout the report.
Constant currency basis	Removes the effect of exchange rate movements on the translation of the results of our overseas operations.	Throughout the report.
Market share	Market share data is presented as a 12 month moving average weighted across the markets in which we operate. The list of markets used to compile the aggregate market share calculation has been changed for FY16 and prior periods have been restated for comparability.	Throughout the report.
Stick equivalent	Stick equivalent (SE) volumes reflect our combined cigarette, fine cut tobacco, cigar and snus volumes.	Throughout the report.



Mark Williamson
Chairman

I'm delighted to welcome you to the first Annual Report and Accounts of Imperial Brands.

Our name may have changed but our strategy and values remain the same. We continue to run a responsible and successful business that's focused on maximising sustainable returns for our shareholders.

We added to our long track record of delivery with another strong performance in 2016. The excellent results we delivered from ITG Brands in the USA were a particular highlight, as we continued to build on our enhanced position following last year's acquisition of brands and other assets.

As well as driving our operational performance we also made further progress with our transition initiatives, which continue to strengthen the business and improve our quality of growth.

None of our achievements would be possible without the energy and commitment of our people. Employees across the Imperial Brands family have worked tirelessly to deliver these results and I would like to thank them all for their commitment and support.

Imperial Brands

Shareholders voted overwhelmingly in favour of changing the name of our parent company from Imperial Tobacco Group PLC to Imperial Brands PLC at our Annual General Meeting in February.

The rationale for change was simple; Imperial Brands better reflects the brand-focused business we now are.

Consumers know us for our Growth and Specialist Brands, the key assets in our portfolio. These are quality brands, delivering quality growth and we continue to build the contribution they make to our volumes and revenues.

We also have strong corporate brands: Imperial Tobacco, home to most of our worldwide tobacco operations, ITG Brands in the USA, our international premium cigar business Tabacalera, our non-tobacco subsidiary Fontem Ventures and our European distribution business Logista.

The breadth of this brand focus is reflected in our new name and marks an exciting new chapter in our growth story.

Enhancing Shareholder Returns

The consistent execution of our strategy continues to create value by maximising sales, cost and cash opportunities.

On a constant currency basis tobacco net revenue was up 9.7 per cent, adjusted operating profit was up 10.4 per cent and we grew adjusted earnings per share by 12.0 per cent.

The Board is pleased to be recommending a total dividend for the year of 155.2 pence per share, another strong increase of 10 per cent. This is the eighth consecutive year that we have delivered dividend growth of 10 per cent and we are committed to maintaining this annual growth rate over the medium term.

Operating Responsibly

The responsible way we run our business is integral to our long-term sustainability.

We take pride in doing things the right way, living our values and adhering to our Code of Conduct.

We support community initiatives across our market footprint, provide employment for more than 30,000 people around the world and return around £17 billion a year to governments in taxes.

Governance and the Board

Imperial Brands continues to be run in an open and transparent manner. You can find out more about our governance framework and the work of the Board and its Committees in the Governance Report.

The composition of the Board changed during the year. Non-Executive Director Ken Burnett stepped down in February after completing nine years' service and I would like to thank him for the considerable contribution he made to our success.

Following Ken's departure we appointed two independent Non-Executive Directors, Steven Stanbrook in February and Therese Esperdy in July.

Between them they have held many senior executive roles over the years, Steven at a number of FMCG companies including SC Johnson & Sons Inc, and Therese in the banking sector, most notably at JP Morgan.

Both have extensive international experience, including in the USA, and are proving to be great additions to the Board.

Delivering Strong Results

2016 was another strong year of delivery for the business and we look to the future with confidence.

We have the right strategy, the right brands and the right people, and that puts us in a strong position to create further value for shareholders over the coming years.

Mark Williamson
Chairman

OUR STRATEGY AND BUSINESS MODEL

STRATEGY

Our strategy is focused on maximising sales, cost and cash opportunities to deliver sustainable shareholder returns. Building the contribution of our Growth and Specialist Brands is improving our quality of growth, while prioritising share and profit delivery in markets is key to driving performance across our balanced geographic footprint. Cost optimisation continues to enhance efficiencies and by embedding stronger capital discipline we are more effectively managing working capital and achieving high cash conversion.

MAXIMISING SHAREHOLDER RETURNS



**STRENGTHEN
PORTFOLIO**



**DEVELOP
FOOTPRINT**



**COST
OPTIMISATION**



**CAPITAL
DISCIPLINE**

HOW WE SUPPORT GROWTH

Strong Governance

High standards of governance are critical to our success.

 **Turn to page 33**
for more information

Acting Responsibly

Operating responsibly is integral to the way we do business.

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for more information

Managing Risk

We actively identify, manage and mitigate the risks facing our business.

 **Turn to page 26**
for more information

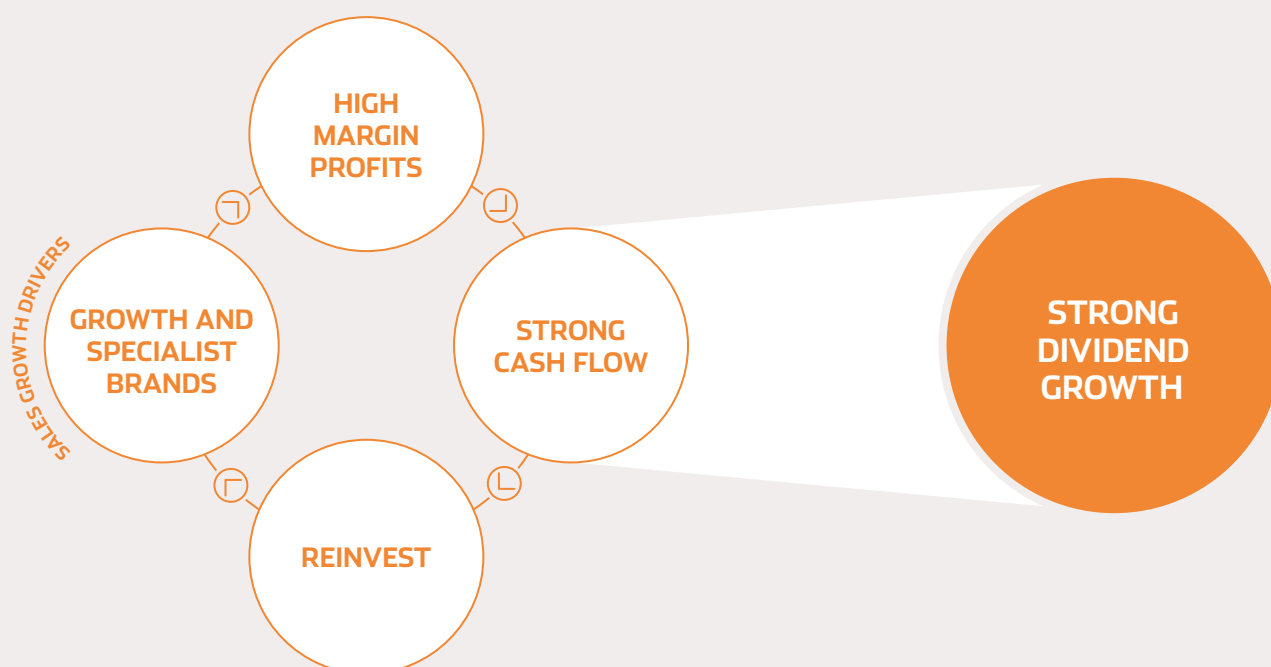
Rewarding Success

Our people are rewarded fairly and incentivised to deliver our strategy.

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for more information

BUSINESS MODEL

Our business model illustrates how we create value. Consistently applying our Sales Growth Drivers to our Growth and Specialist Brands, combined with effective cost management, delivers quality sales with high operating margins. This generates the strong cash flows that are a recognised strength of our business. We use this cash to reinvest to support growth, pay down debt or return to shareholders through dividends, which we are committed to growing by at least 10 per cent a year over the medium term.



SALES GROWTH DRIVERS

Portfolio management, innovation, customer engagement and pricing are the four Sales Growth Drivers we have selected to drive the performance of our Growth and Specialist Brands.

Through portfolio management we focus on connecting our brands with consumers to enhance brand equity and build sales.

For us, innovation means creating a drumbeat of initiatives: small, frequent innovations that keep our brands fresh and relevant. Excellence in customer engagement requires strong partnerships with retailers that support their business and maximise the impact of our brands at the point of sale.

Pricing opportunities are evaluated by brand, pack size and sales channel. We assess excise structures when making pricing decisions and focus on driving revenue growth while continuing to give consumers value for money.

HOW WE MEASURE OUR PERFORMANCE

We use key performance indicators and the supporting metrics in the Operating Review to measure the progress we make in delivering our strategy. These measures reflect our priorities and are used to monitor and drive business performance.

Return on Invested Capital (%)



Performance

Return on invested capital increased as we benefited from a full year return on our USA acquisition.

Definition

Return on invested capital measures the effectiveness of capital allocation and is calculated by dividing adjusted net operating profit after tax by invested capital. Invested capital is reported equity adding back amortisation of intangibles and adjusting back to foreign exchange rates at the time of relevant acquisitions.

Adjusted Earnings Per Share¹ (pence)



Performance

Reported adjusted earnings per share rose by 17.5 per cent. On a constant currency basis the increase was 12 per cent.

Definition

Adjusted earnings per share represents adjusted profit after tax attributable to the equity holders of the Company divided by the weighted average number of shares in issue during the period, excluding shares held to satisfy employee share plans and shares purchased by the Company and held as treasury shares.

MAXIMISING SHAREHOLDER RETURNS

STRENGTHEN PORTFOLIO

Growth Brand Volumes¹ (bn)



Performance

Our Growth Brands outperformed market trends, with volumes up 4.3 per cent compared with market declines of 0.9 per cent. Excluding Iraq and Syria, volumes were up 7.8 per cent.

Definition

Volumes are measured on a stick equivalent basis to reflect combined cigarette and fine cut tobacco volumes.

DEVELOP FOOTPRINT

Tobacco Net Revenue¹ (£bn)



Performance

Tobacco net revenue was up 9.7 per cent at constant currency and increased 14.7 per cent at actual rates.

Definition

Tobacco net revenue comprises tobacco and Fontem Ventures revenue less duty and similar items, excluding peripheral products.

1. KPIs used as bonus and LTIP performance criteria for Executive Directors. See Remuneration Report on page 51 for more information.

Dividend Per Share (pence)



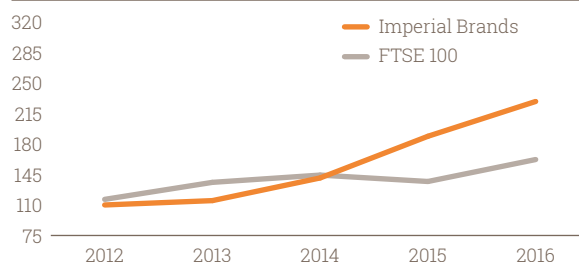
Performance

Dividend per share increased by 10 per cent for the eighth consecutive year.

Definition

Dividend per share represents the total annual dividends being the sum of the paid interim dividend and the proposed final dividend for the financial year.

Total Shareholder Return¹



Performance

In 2016 we outperformed the FTSE 100 by 2.8 per cent. With dividends reinvested, £100 invested in Imperial Brands five years ago would now be worth £228.49 compared with £161.98 if invested in the FTSE 100 index.

Definition

Total shareholder return is the total investment gain to shareholders resulting from the movement in the share price and assuming dividends are immediately reinvested in shares.

MAXIMISING SHAREHOLDER RETURNS

COST OPTIMISATION

Tobacco Operating Margin (%)



Performance

Tobacco operating margin increased by 60 basis points to 46.9 per cent.

Definition

Tobacco adjusted operating profit divided by tobacco net revenue expressed as a percentage.

CAPITAL DISCIPLINE

Cash Conversion Rate¹ (%)



Performance

Our continued focus on cash generation and working capital management delivered cash conversion of 95 per cent.

Definition

Cash conversion is calculated as cash flow from operations before interest and tax payments less net capital expenditure relating to property, plant and equipment, software and intellectual property rights as a percentage of adjusted operating profit.

OUR BRANDS AND MARKETS

We focus on maximising opportunities for our brands and markets by building the contribution from our Growth and Specialist Brands and strategically managing our markets to deliver either Growth or Returns.

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for more information

GROWTH BRANDS

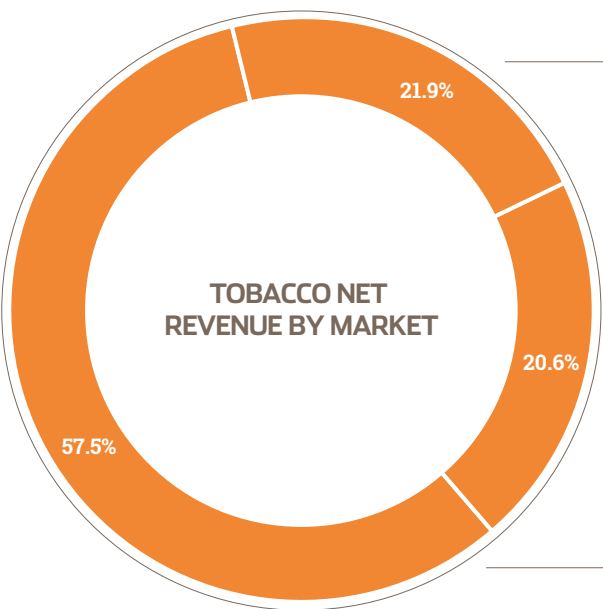
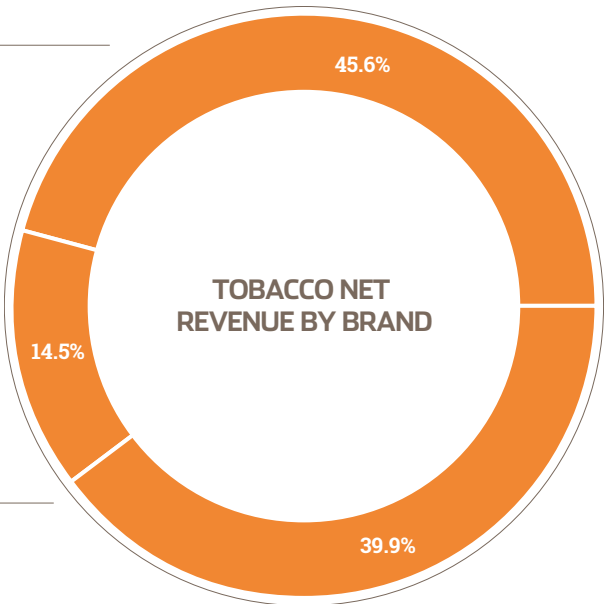
Growth Brands have broad consumer appeal and are managed to drive quality sustainable growth.

SPECIALIST BRANDS

Specialist Brands appeal to specific consumer groups and have a track record of generating strong returns.

PORTFOLIO BRANDS

Some Portfolio Brands support our volume and revenue development, while others are delisted or migrated into Growth Brands.



GROWTH MARKETS

In Growth Markets we aim to deliver long-term share and profit growth.

USA MARKET

We have a significant presence in the USA and therefore manage it as a standalone Growth Market.

RETURNS MARKETS

In Returns Markets we focus on sustainable profit delivery, while actively managing our large share positions.

More than 5,000 billion cigarettes are sold in markets around the world every year. Our operations extend across a broad spread of these markets, providing us with a balanced geographic footprint that supports our drive to deliver sustainable shareholder returns.

OUR GEOGRAPHIC FOOTPRINT

Our markets are clustered to generate either Growth or Returns.

Growth Markets have large profit and/or volume pools and include selected countries in the EU, Eastern Europe, Asia, the Middle East and the USA.

We typically have shares below 15 per cent in Growth Markets and aim to deliver both share and profit growth.

In Returns Markets, which include Australia and markets in the EU, Eastern Europe and Africa, we have larger positions and focus on generating sustainable profit, while actively managing our market share.

The macro-economic environment continues to impact consumer spending and legitimate cigarette sales in some territories. Political instability in many parts of the world, particularly in the Middle East, combined with the UK's decision to leave the EU, creates further challenges and uncertainty.

However, the strength of our strategy has enabled us to consistently develop our business in difficult conditions and we see considerable opportunities for driving quality growth in the years ahead.

REGULATING TOBACCO

Regulation is increasing, as are the costs of compliance – particularly in the EU and the USA.

Regulation is largely driven by three organisations: the World Health Organization (WHO, through the Framework Convention on Tobacco Control, the FCTC), the USA's Food and Drug Administration (FDA) and the European Commission (through the European Union Tobacco Products Directive, the EUTPD).

The EUTPD has been significantly revised to cover the appearance, production and taste of tobacco and e-cigarettes.

The revised Directive came into force in May 2014 and EU Member States had until 20 May 2016 to transpose it into national law.

From that date on, all tobacco products manufactured in the EU have had to comply with the revised Directive, although there are provisions for the sell-through of old stock which vary from Member State to Member State.

During the year, the FDA extended its authority to include the regulation of e-cigarettes and cigars and other tobacco products.

We support reasonable, proportionate and evidence-based regulation that respects adult freedom of choice and recognises that tobacco products are enjoyed by millions of people worldwide.

We oppose attempts to exclude us from regulatory debates and continue to raise concerns about the impact of extreme regulation, such as plain packaging or high excise increases, which often fuel the growth of illicit trade.

ILLICIT TRADE OF TOBACCO

Every year around 500 billion illegal cigarettes are consumed, depriving governments of around £30 billion in taxes.

The smuggling and counterfeiting of tobacco has considerably wider impacts: children can more easily obtain cigarettes, consumers are deprived of the quality they associate with their favourite brands and the livelihoods of independent retailers are threatened.

We apply stringent controls to our global network of distributors and have a dedicated team of specialists who work with governments and law enforcement agencies around the world to tackle illicit trade.

We also invest in systems and processes to improve the security of our products and share intelligence to help disrupt the supply of illegal cigarettes.

E-VAPOUR PRODUCTS

The global market for e-vapour products (EVPs) continues to expand and there is growing consensus that these products may be less risky than smoking tobacco.

E-cigarettes are the most common EVPs and we are represented in this category by blu, one of the world's leading high quality EVP brands.

The blu brand is managed by our non-tobacco subsidiary Fontem Ventures and has an established position in the USA and the UK and a growing presence in France and Italy. Between them, these four markets account for over 70 per cent of global e-vapour sales.

As well as building sales of blu, Fontem also continues to focus on developing advanced technologies to improve the consumer vaping experience, which is important for the future growth of the EVP category.

The regulation of EVPs continues to evolve. We believe a clear regulatory framework to govern the way these products are made and sold is required, and we continue to engage with key stakeholders to support the development of effective legislation.

CHIEF EXECUTIVE'S STATEMENT



Alison Cooper
Chief Executive

This was another year of strong value creation and I'd like to thank our people across the business for all their hard work and dedication. Their focus on driving quality growth, embracing new ways of working and effectively managing cost and cash has been integral to our success.

Consistently delivering against our strategy has been a hallmark of our performance in recent years and is enabling us to build a stronger, higher quality business with even greater capacity for generating sustainable shareholder returns.

Highlights in the year included further enhancing the contribution from our Growth and Specialist Brands, which now account for 60.1 per cent of the Group's tobacco net revenue. We also made excellent progress in the USA, with ITG Brands performing strongly in line with our plans.

Elsewhere, we maintained good momentum across our market footprint, with results in Growth Markets also benefiting from revenue growth from Fontem Ventures. We further emphasised our focus on quality revenue by prioritising investment in brands and markets that offer the best returns.

Our strong financials were characterised by another year of adjusted earnings per share and dividend growth. On a constant currency basis adjusted operating profit was up by 10.4 per cent and we grew adjusted earnings per share by 12.0 per cent. Return on invested capital improved to 13.9 per cent and we increased the dividend by 10 per cent for the eighth consecutive year.

Delivering Sustainable Quality Growth

Our strategic transition has created a stronger business that is generating a higher quality of growth. Like many businesses, we operate in a challenging, volatile environment and the companies that are successful in these conditions are the ones that adapt and change. In recent years we've taken decisive action to improve our results and our ways of working, and our focus on optimising our brand portfolio has been at the heart of our change agenda.

Our portfolio consists of Growth, Specialist and Portfolio Brands. Growth Brands have strong equity and broad consumer appeal; Specialist Brands also enjoy strong equity but typically appeal to more specific consumer groups. Our priority is to build the contribution these brands make to our results. Portfolio Brands are a mix of local and regional offerings. Those with strong equity support our volume and revenue progression, while weaker brands are delisted or migrated into higher quality Growth Brands.

We have a very high success rate when it comes to these migrations, with over 95 per cent of consumers completing the transition from one brand to another. During the year we completed 17 additional brand migrations across multiple markets. A total of 49 migrations have now been completed and another 15 are in progress.

We have identified significant opportunities to further simplify our brands and products and we will start driving this next phase of portfolio optimisation in 2017.

In simplifying our portfolio we are reducing complexity and cost, which reflects our approach to developing new ways of working: everything needs to be simpler and more effective than before. This is providing greater clarity on roles and responsibilities, enabling our people to prioritise and focus on work that really matters to our success.

Opportunities to enhance the way we work are identified through the continual refinement of our operating model, which involves looking at how we can change systems, processes and structures to improve performance.

In 2016 we focused on improving sales and marketing processes across 58 markets and we launched a new Customer Relationship Management solution in 19 markets. We also transitioned to a single global HR platform and introduced shared services in Finance in a number of markets.

Strengthening our Portfolio

Our drive to improve our quality of growth was reflected in the excellent results we achieved with our Growth Brands.

Growth Brands outperformed the market, with strong growth in volumes, share and net revenue.

Growth Brands continue to benefit from migrations, with multiple markets successfully migrating Portfolio Brands to JPS, West and Parker & Simpson.

We also further invested in building brand equity with marketing campaigns for JPS, West, Davidoff and Gauloises Blondes.

The excellent progress we are making with our Growth Brands was supported by strong results from our Specialist Brands, which account for almost 15 per cent of our tobacco net revenue. Net revenue increased by 44 per cent, benefiting from the contribution of the Kool and blu brands which we acquired last year.

Fontem Ventures

blu is a high quality e-vapour brand that is proving to be a tremendous addition to our portfolio. blu is managed by our non-tobacco subsidiary Fontem Ventures, which is focused on developing new consumer experiences and opportunities for sustainable revenue growth. Fontem's current priority is to capitalise on the growth in the e-vapour sector by building sales of blu and licensing a range of patented technologies.

blu sales are currently concentrated in the USA, UK, France and Italy, the four core e-vapour markets that together account for around 70 per cent of global e-vapour sales.

blu is the established number two brand in the UK and USA and has a growing presence in France and Italy.

We are investing to support growth, funding brand equity building with a new marketing campaign in the USA and UK, and allocating additional funds for technological research and development to continue to improve the blu vaping experience. During the year Fontem further enhanced revenues by licensing its first generation technology to a number of other e-vapour companies.

Developing our Footprint

Our excellent Growth and Specialist Brand performances were complemented by good results across our geographic footprint.

We delivered a positive revenue and profit performance in Growth Markets, with the benefit of additional revenue from blu and royalties from the licensing of Fontem's technology and good results in Italy, Russia, Japan and Taiwan more than offsetting declines caused by Iraq and Syria.

The integration of our US operations was completed as planned during the year and ITG Brands continued to perform strongly. We are investing to support growth, funded by the acquisition synergies, to drive long-term sustainable value. These prioritised investments have driven steady improvements in the market shares of Winston and Kool. Towards the end of the year we also launched a new pack design for Winston, coupled with a new advertising campaign, to further build brand equity. We also significantly improved the performance of our mass market cigar business as we changed our route to market to a retail focused business model, aligning it with our cigarette business.

In Returns Markets we focused on improving our quality of growth by making investment choices to underpin long-term sustainable profit growth. We have actively directed investment into markets where we see the best returns and avoided low quality or unprofitable volume. We achieved good results in Germany, Australia and Algeria, and continued to invest in the UK to defend our position in an extremely competitive environment.

Good Results from Logista

Our European distribution business Logista has a history of delivering good results and 2016 was no exception. Distribution fees and adjusted operating profit both increased and the Logista team continues to focus on cost management and new growth opportunities to further drive the profitable development of the business.

Cost Optimisation and Capital Discipline

Our current cost optimisation programme remains on track to save £300 million per annum from September 2018. A range of initiatives have been successfully deployed to optimise our cost base, realising £65 million in the year, and bringing the total annualised savings to £240 million.

Our commitment to capital discipline underpins our focus on cash generation and the effective management of our working capital.

Cash conversion remained strong at 95 per cent compared to 97 per cent last year, which benefited from one-off working capital benefits associated with the US acquisition. We reduced adjusted net debt by £1.0 billion, excluding the adverse impact of currency translation, taking the total reduction over the last two years to £2.1 billion.

For the eighth consecutive year we delivered strong dividend growth of 10 per cent and we remain committed to continuing to grow the dividend by at least 10 per cent a year over the medium term.

The Next Decade of Growth

During the year, I spent time with the Board and my senior leadership team reviewing our strategy for creating shareholder value over the next 10 years.

This reinforced the strength of our strategy and highlighted opportunities to drive even greater focus on our strategic priorities: strengthening our portfolio, developing our footprint, optimising our cost base and embedding capital discipline.

To support the delivery of further quality revenue growth in 2017 and subsequent years we will invest an additional £300 million in our Growth and Specialist Brands in the key markets that offer the best opportunities for quality growth.

Investments will be prioritised and focused on areas where we have a proven track record of generating quality revenue growth, including brand building, customer engagement and sales execution.

This increased investment will be supported by a new phase of cost optimisation, which will deliver additional savings of £300 million per annum by 2020, at a cost of £750 million.

These savings will be generated by implementing further initiatives to reduce complexity and drive operational efficiencies.

Outlook

We have a track record of consistently delivering against our strategy, which has generated significant returns to shareholders and created a strong platform for future value creation.

To further drive delivery of our strategic priorities and underpin revenue growth over the medium term, we will invest an additional £300 million, which, net of investment returns, will have a £200 million impact in 2017. This will be partly offset by £90 million of cost optimisation savings resulting in a 4 per cent net impact on 2017 constant currency earnings. However, foreign exchange translation is expected to benefit earnings by around 14 per cent based on current rates, and supports the continued delivery of our financial targets in 2017.

The phasing of the increased investment will be biased to the early part of 2017, resulting in lower revenue and profit in the first half, offset by a stronger second half performance.

We intend to sustain an increased level of investment in subsequent years and we expect a return to constant currency earnings growth in line with our medium-term guidance of 4-8 per cent from the 2018 financial year.

We continue to prioritise capital discipline and strong cash conversion to underpin our commitment to deliver dividend growth of at least 10 per cent next year and over the medium term.

We have a strong track record of delivering sustainable shareholder returns over many years and we are well-placed to build on this in 2017 and over the next decade.



Alison Cooper
Chief Executive

INVESTMENT CASE

WHY INVEST IN IMPERIAL BRANDS?

Investing for Quality Growth

Imperial Brands has an attractive portfolio of brands and markets which can deliver long-term profitable growth.

Our strategy is to strengthen our tobacco and non-tobacco portfolio by generating an increasing proportion of revenue from our strongest brands, while also prioritising our investment in those markets that offer the best returns.

We have a proven track record of achieving strong price/mix growth to offset industry volume declines and enhance profitability. We are also investing in non-tobacco products and experiences through our subsidiary, Fontem Ventures, to deliver future growth opportunities alongside our tobacco business.

Value Creation Through New Ways of Working

Our strategic agenda is changing the way we operate to strengthen the business and improve our quality of growth.

Simplification and focus are at the heart of our new ways of working, as we reduce complexity and instil a more cost-conscious culture. We are also adopting lean principles through continuous improvement in everything we do.

This provides opportunities to reduce costs, improve effectiveness and create a more agile organisation that can drive consistent returns for shareholders in an ever changing world.

**INVESTING FOR QUALITY GROWTH;
BRANDS, PRODUCTS AND MARKETS WITH
LONG-TERM PROFIT POTENTIAL**

**VALUE CREATION SUPPORTED
BY NEW AND IMPROVED WAYS
OF WORKING**

95% CASH CONVERSION

**10% DIVIDEND GROWTH PA
OVER MEDIUM TERM**

Strong Cash Generation

Our business generates strong cash flows as a result of our intrinsically high operating profit margins, coupled with our ability to convert a very high proportion of these profits to cash.

Over recent years we have improved our cash conversion by reducing our working capital and prioritising our investments more effectively. Our current focus for our cash resources are: investment in our priority brands and markets, supporting double digit dividend growth for shareholders and reducing our net debt.

Annual 10% Dividend Growth Over Medium Term

A core part of our investment proposition is our commitment to grow the dividend by at least 10 per cent per annum over the medium term. This is a commitment we have now achieved for eight consecutive years.

Our ability to improve profitability and generate strong cash flows will enable us to continue to deliver this income growth to our shareholders.

We drive the performance of our brands and markets to deliver quality growth. Our markets prioritise either Growth or Returns, depending on their strategic role, and our portfolio focus is on maximising opportunities for our Growth and Specialist Brands.

BRAND PERFORMANCES

We delivered excellent performances from our Growth and Specialist Brands. These are the most important assets in our portfolio and together they account for 60.1 per cent of our tobacco net revenue, up 320 basis points on last year, reflecting the improving quality of growth that we are consistently delivering. The rest of our portfolio consists of Portfolio Brands, which are local and regional brands that fulfil a variety of roles. Some add to our revenue momentum, while others will create more value by being migrated into Growth Brands.

Total Group tobacco volumes were 276.5 billion stick equivalents (2015: 285.1 billion), which includes an incremental 12.1 billion from our USA acquisition. Volumes were down 3.0 per cent, reflecting declines in Iraq and Syria and lower organic volumes, which offset the benefit of the contribution from ITG Brands.

GROWTH BRANDS

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Market share	%	7.7	7.2 ^R	+50bps	
Net revenue	£m	3,265	2,862	+14.1%	+10.1%
Percentage of Group volumes	%	54.7	50.9	+380bps	
Percentage of tobacco net revenue	%	45.6	45.8	-20bps	

As a result of the USA acquisition our Growth and Specialist Brands were reclassified, effective 1 October 2015. USA Gold was replaced by Winston as a Growth Brand, and instead became a Portfolio Brand, and Kool and blu joined our Specialist Brands. With the exception of market share, prior year comparatives have not been adjusted for this reclassification.

^R See Performance Measures table on page 2.

Our Growth Brands are: Davidoff, Gauloises Blondes, JPS, West, Fine, News, Winston, Bastos, Lambert & Butler and Parker & Simpson. These are quality brands with broad consumer appeal that are generating an increasing amount of our volume and revenue.

Growth Brands outperformed the market in the year, with volumes growing 4.3 per cent, against a backdrop of market volume declines in our geographic footprint of 0.9 per cent. We also grew Growth Brands net revenue by 10.1 per cent.

Excluding Iraq and Syria, underlying Growth Brand volumes increased by 7.8 per cent and underlying net revenue increased by 11.2 per cent.

We improved the share of Growth Brands from 7.2 per cent to 7.7 per cent. As part of our drive to prioritise Growth Brands and improve the quality of our growth we deliberately ceded some share in lower value Portfolio Brands, contributing to a 60 basis point decline in the Group share to 13.9 per cent.

Growth Brands now account for 54.7 per cent of total Group tobacco volumes, an increase of 380 basis points, and 45.6 per cent of overall tobacco net revenue, a decrease of 20 basis points.

Brand Chassis	Highlights
JPF (<i>JPS, Parker & Simpson and Fine</i>)	Share growth in the chassis was driven by JPS and Parker & Simpson with the continued strength of JPS in Australia and Players in the UK, as well as the ongoing success of brand migrations in a number of markets including Russia where we migrated Balkan Star. In Germany we took action to strengthen our share with the launch of larger JPS pack formats.
West (<i>West, L&B, News and Bastos</i>)	In Germany we migrated Route 66 into West and continued to grow West share in Saudi Arabia and Japan. Successful brand migrations in France have supported the growth of News and in the UK another good performance from Lambert & Butler was helped by growth in crushball.
Winston	The success of our new retailer contracts and promotional support is underpinning Winston's good results and consistent share growth. A rejuvenated pack design and new consumer marketing is further enhancing brand equity.
Davidoff	We delivered further share growth in Greece and maintained Davidoff's share position in Taiwan's premium segment with the launch of Davidoff Absolute. We also introduced Fresh Box formats in key Middle East markets, such as Saudi Arabia.
Gauloises	A successful brand campaign supported good results in Germany. An excellent performance in Algeria, supported by the launch of Gauloises L'Autre, consolidated the brand's market leading position. These positive performances more than offset the impact of Iraq and Syria.

SPECIALIST BRANDS

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Net revenue	£m	1,042	693	+50.2%	+43.6%
Percentage of tobacco net revenue	%	14.5	11.1	+340bps	

Specialist Brands appeal to specific consumer groups and include: blu (e-vapour), Style, Gitanes, Kool (cigarettes), Golden Virginia, Drum, Route 66 (fine cut tobacco), Cohiba, Montecristo, Romeo Y Julieta (premium cigars), Backwoods (cigars), Skruf (snus) and Rizla (papers).

We achieved great results with our Specialist Brands, reflected in very strong net revenue growth, enhanced by contributions from blu, Kool and Backwoods. There was also good growth from Skruf in Scandinavia and premium cigars in the USA. This more than offset the impact of Iraq and Syria, which held back Gitanes. Specialist Brands now represent a greater proportion of the business at 14.5 per cent of net revenue.

MARKET PERFORMANCES

We divide our footprint into Growth Markets, the USA Market and Returns Markets. We manage these markets based on their strategic roles, with Growth Markets and the USA Market prioritising long-term share and profit growth. In Returns Markets the focus is on sustainable profit delivery and effective management of our strong share positions.

GROWTH MARKETS

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Market share	%	6.4	6.9 ^R	-50bps	
Net revenue	£m	1,568	1,449	+8.2%	+4.3%
Adjusted operating profit	£m	443	409	+8.3%	+2.2%
Growth Brand % of net revenue	%	47.2	47.0	+20bps	
Growth Brand volume	bn SE	46.0	46.4	-0.8%	

^R See Performance Measures table on page 2.

We continued to build good momentum in Growth Markets, increasing net revenue by 4.3 per cent and adjusted operating profit by 2.2 per cent. This growth reflected an enhanced contribution from blu, the benefit of intellectual property royalties from Fontem Ventures and rising profits in key markets, offsetting increased investment in blu, transaction currency costs and the impact of Iraq and Syria.

Our overall market share decline was mainly driven by Maxim's price disadvantage in Russia in the first half. We addressed this and delivered a stronger second half performance, stabilising our share in the process.

Excluding Iraq and Syria, underlying net revenue was up 8.0 per cent and adjusted operating profit was up 8.7 per cent. We increased the proportion of net revenue generated by Growth Brands by 20 basis points.

Country	Performance
Russia	Strong pricing during the year offset share declines and supported revenue growth. Our Growth Brands achieved excellent results with growth from West and the successful launch of Parker & Simpson.
Saudi Arabia	Our share was up as we delivered consistent growth in West, with recent excise changes benefiting the lower price segment of the market. The recent launch of the Fresh Box format supported the performance of Davidoff.
Italy	We increased our share in Italy, driven by a continued strong performance with JPS.
Greece	We delivered further share growth in Davidoff to maintain the brand's positive momentum.
Sweden and Norway	We delivered good share and revenue growth in both Sweden and Norway, against a backdrop of positive pricing and a growing snus market.
Turkey	We improved profitability after restructuring our operations and continued to progress a focused growth strategy with Davidoff and West in key cities. Recent positive pricing has supported revenue growth.
Japan	We grew revenue and the share of West as we continued to invest in expanding our retailer coverage.
Taiwan	We generated further profit growth, driven by the success of Davidoff equity activations and positive pricing, although our overall market share was down as the premium segment declined.
Iraq and Syria	Continued instability in the region held back trading particularly in Gauloises and Gitanes in the first half.

USA MARKET

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Market share	%	9.2			
Net revenue	£m	1,477	707	+108.9%	+92.9%
Adjusted operating profit	£m	823	375	+119.5%	+102.4%
Growth Brand % of net revenue	%	18.6	13.7	+490 bps	
Growth Brand volume	bn SE	6.1	3.1	+99.4 %	

Group revenue and profit benefited significantly from the contribution from ITG Brands following the acquisition of assets from Reynolds American last year. The incremental contribution of the acquisition to the USA performance in the current financial year was tobacco net revenue of £682 million and volumes of 12.1 billion. Our total USA volumes for the year were 24.9 billion stick equivalents.

Adjusted operating profit more than doubled with the benefit of the acquisition. Adjusted operating margins improved 270 basis points to 55.7 per cent, despite increased brand investment.

The percentage of tobacco net revenue generated by Growth Brands increased to 18.6 per cent, as we reshaped our portfolio following the acquisition. From 1 October 2015, we reclassified our Growth and Specialist Brands, replacing USA Gold with Winston in Growth Brands and adding Kool to our Specialist Brands. USA Gold is now a Portfolio Brand.

Around 165,000 stores, representing around 90 per cent of USA cigarette volumes, have signed up to our new retailer agreements. These agreements support our new promotional arrangements, which have already delivered steady improvements in the market shares of Winston and Kool, almost offsetting the declines from our Portfolio Brands. Towards the end of the year we also launched a new pack design for Winston, coupled with a new advertising campaign, to further build brand equity.

Growth Brand volume benefited from the replacement of USA Gold with Winston, as did the percentage of net revenue generated by Growth Brands.

In addition, the action we have taken to improve our mass market cigar business, which includes the Dutch Masters and Backwoods brands, continued to strengthen our results.

RETURNS MARKETS

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Market share	%	26.1	27.0 ^R	-90bps	
Net revenue	£m	4,122	4,095	+0.7%	-2.7%
Net revenue per '000 SE	£	23.51	22.08	+6.5%	+2.9%
Adjusted operating profit	£m	2,094	2,111	-0.8%	-4.3%
Growth Brand % of net revenue	%	54.6	50.9	+370bps	

^R See Performance Measures table on page 2.

Our priority in our Returns Markets is to maximise profit while managing our share.

We grew net revenue per thousand stick equivalents by 2.9 per cent and further improved the quality of our portfolio with Growth Brands now generating 54.6 per cent of tobacco net revenue, an increase of 370 basis points.

Against a backdrop of flat industry volumes, our market share declined by 90 basis points to 26.1 per cent. Net revenue was also down. Results were impacted by share declines in Returns North, particularly Ukraine, the UK and Germany, offsetting the share growth we delivered in Returns South, particularly in Algeria.

Adjusted operating profit was down 4.3 per cent, impacted by the conclusion of the distribution contract for Philip Morris International in the UK and Morocco, adverse transaction exchange and the cost of complying with EUTPD legislation.

Excluding these impacts, adjusted operating profit for Returns Markets overall grew 0.9 per cent, with Returns North flat and Returns South up 3.1 per cent.

RETURNS MARKETS NORTH

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Market share	%	24.0	25.6 ^R	-160bps	
Net revenue	£m	2,645	2,649	-0.2%	-2.6%
Net revenue per '000 SE	£	28.01	25.76	+8.7%	+6.1%
Adjusted operating profit	£m	1,439	1,475	-2.4%	-5.1%
Growth Brand % of net revenue	%	57.2	53.6	+360 bps	

^R See Performance Measures table on page 2.

We made good progress in improving our quality of growth in Returns Markets North, increasing net revenue per thousand stick equivalents by 6.1 per cent. Growth Brands delivered 57.2 per cent of tobacco net revenue, up from 53.6 per cent.

We made a strategic decision to lower investment in Ukraine and Azerbaijan, where economic conditions and competitor discounting resulted in reduced profit opportunities. Overall profitability in Returns North was affected by the same factors outlined in the Returns Markets overview.

Country	Performance
UK	Our overall share declined, although we continued to invest to defend our position. Our fine cut tobacco share increased during the year, led by good growth from Gold Leaf, and we also grew sales of Rizla. In cigarette we generated positive momentum with JPS, Players and Lambert & Butler crushball variants, although investment to grow our share in the sub-economy segment impacted revenue and profit.
Germany	Growth in revenue and profit was supported by stable market size and the continued positive performance from Gauloises. Our success with large format variants is stabilising the share of JPS and West benefited from the migration of Route 66, which we completed in the year. Our overall share was down but strengthened in the second half, due to the actions we took.
Benelux	Brand migrations supported the good performance of JPS in fine cut tobacco, although the market size and our overall share declined following significant excise increases.
Australia	We delivered another excellent performance from JPS, resulting in further strong share, revenue and profit growth.
Ukraine	Investment was moderated in response to significant competitor discounting and currency devaluation that eroded market profitability. Our share improved in the second half as pricing conditions normalised.

RETURNS MARKETS SOUTH

		Full Year Result		Change	
		2016	2015	Actual	Constant Currency
Market share	%	29.1	29.0 ^R	+10bps	
Net revenue	£m	1,477	1,446	+2.1%	-2.9%
Net revenue per '000 SE	£	18.27	17.51	+4.3%	-0.8%
Adjusted operating profit	£m	655	636	+3.0%	-2.5%
Growth Brand % of net revenue	%	50.0	46.0	+400 bps	

^R See Performance Measures table on page 2.

Strong results in Algeria more than offset the impact of the weak operating environment in Morocco. We also saw improved market size trends in markets such as Spain and France, where the actions we have taken to strengthen performance continued to gain traction.

We improved our market share by 10 basis points, primarily due to the strong gains we made in Algeria, and we improved our market share trends in Morocco in the second half, driven by the launch of Fox. We made good progress in further building the contribution from our Growth Brands, with these brands now generating 50.0 per cent of our tobacco net revenue, up from 46.0 per cent last year. Profitability was affected by the same factors outlined in the Returns Markets overview.

Country	Performance
Spain	We continued to focus on customer engagement initiatives to strengthen our ties with retailers, while maintaining good growth momentum with West. The ongoing migration of Ducados to JPS is also enhancing the quality of our portfolio.
France	News continues to grow share following the success of the Fortuna migration and the launch of several new variants in fine cut tobacco. The next phase of portfolio simplification is generating strong initial results.
Algeria	We delivered an excellent performance, generating significant share and profit growth, driven by Gauloises, which we have established as the market-leading brand.
Morocco	Our recently launched value brand Fox reached 10 per cent share, helping to address volume declines in Marquise. Revenue and profit was affected by the conclusion of the Philip Morris International agreement.



Oliver Tant
Chief Financial Officer

We delivered another year of strong financial performance, with growth in revenue and adjusted profit and consistently high cash conversion. Our relentless focus on cost efficiencies and capital discipline is providing resources to reinvest to support growth, generate returns for shareholders and pay down debt.

When managing the performance of our business we focus on non-GAAP measures, which we refer to as adjusted measures. We believe they provide a useful comparison of performance from one period to the next. These adjusted measures are supplementary to, and should not be regarded as a substitute for, GAAP measures, which we refer to as reported measures. The basis of our adjusted measures is explained in our accounting policies accompanying our financial statements, and reconciliations between reported and adjusted measures are included in the appropriate notes to our financial statements. Percentage growth figures for adjusted results are given on a constant currency basis, where the effects of exchange rate movements on the translation of the results of our overseas operations are removed.

Group Results – Constant Currency Analysis

£ million unless otherwise indicated	Year ended 30 September 2015	Foreign Exchange	Constant currency growth	Year ended 30 September 2016	Change	Constant currency change ¹
Tobacco net revenue	6,251	307	609	7,167	14.7%	9.7%
Growth Markets net revenue	1,449	57	62	1,568	8.2%	4.3%
USA Market net revenue	707	113	657	1,477	108.9%	92.9%
Returns Markets North net revenue	2,649	64	(68)	2,645	-0.2%	-2.6%
Returns Markets South net revenue	1,446	73	(42)	1,477	2.1%	-2.9%
Tobacco adjusted operating profit	2,895	163	302	3,360	16.1%	10.4%
Growth Markets adjusted operating profit	409	25	9	443	8.3%	2.2%
USA Market adjusted operating profit	375	64	384	823	119.5%	102.4%
Returns Markets North adjusted operating profit	1,475	39	(75)	1,439	-2.4%	-5.1%
Returns Markets South adjusted operating profit	636	35	(16)	655	3.0%	-2.5%
Logistics distribution fees	749	39	21	809	8.0%	2.8%
Logistics adjusted operating profit	154	8	14	176	14.3%	9.1%
Adjusted operating profit	3,053	171	317	3,541	16.0%	10.4%
Adjusted net finance costs	(467)	(30)	(27)	(524)	12.2%	5.8%
Adjusted earnings per share (pence)	212.5	11.5	25.6	249.6	17.5%	12.0%

1. See Performance Measures table on page 2.

Excellent Track Record of Delivery

The excellent progress we are making in simplifying our brand portfolio and reducing complexity across the business is central to our cost optimisation and capital discipline agenda.

As we reduce the number of brands, we are able to align our manufacturing and supply chain to deliver operating efficiencies and optimise our working capital needs. At the same time, we are adopting new ways of working and embracing lean principles to reduce overheads and improve our effectiveness.

This is delivering tangible savings that we are able to reinvest in driving top-line growth. We have established a track record of increasing operating profit margins and adjusted earnings per share in each of the past three years. Our capital discipline has driven high cash conversion which underpins our commitment to grow dividends, repay debt and invest in the business.

Strong Financial Performance

Our results benefited from the acquisition of assets in the USA last year, with an additional volume of 12.1 billion stick equivalents and £682 million of net revenue in the year.

Outside the USA, volumes were affected by market size declines, difficult trading caused by the conflict in Iraq and Syria and by our decision to deprioritise volume in markets such as Ukraine where profitability has been affected by competitor discounting and adverse currencies. Positive price/mix and cost control initiatives mitigated these impacts. Reported tobacco net revenue was up 14.7 per cent, reflecting our market choices and the benefit of currency exposures.

Tobacco net revenue was up by 9.7 per cent at constant currency. The proportion of Group net revenue from our Growth and Specialist Brands increased to now represent 60.1 per cent, improving the quality of our revenue and strengthening our sustainability. Tobacco adjusted operating profit increased 10.4 per cent to £3.36 billion, and on a reported basis increased 12.1 per cent.

Logista again delivered an encouraging performance in a challenging environment with adjusted operating profit of £176 million compared with £154 million last year, partly as a result of foreign exchange movements; on a constant currency basis adjusted operating profit grew 9.1 per cent. The improvement was driven by the development of its non-tobacco business, particularly pharmaceutical, wholesale and transport, a stronger tobacco market, as well as the benefit of continued cost controls.

FINANCIAL REVIEW

CONTINUED

Group Earnings Performance

£ million unless otherwise indicated	Adjusted		Reported	
	2016	2015	2016	2015
Operating profit				
Tobacco	3,360	2,895	2,126	1,910
Logistics	176	154	98	74
Eliminations	5	4	5	4
Group operating profit	3,541	3,053	2,229	1,988
Net finance costs	(524)	(467)	(1,350)	(261)
Share of profit of investments accounted for using the equity method	28	29	28	29
Profit before taxation	3,045	2,615	907	1,756
Taxation	(609)	(541)	(238)	(33)
Profit for the year	2,436	2,074	669	1,723
Earnings per ordinary share (pence)	249.6	212.5	66.1	177.4

Reconciliation of Adjusted Performance Measures

£ million unless otherwise indicated	Operating profit		Net finance costs		Earnings per share (pence)	
	2016	2015	2016	2015	2016	2015
Reported	2,229	1,988	(1,350)	(261)	66.1	177.4
Acquisition costs	–	40	–	–	–	4.2
Amortisation of acquired intangibles	1,005	697	–	–	78.0	57.5
Fair value losses/(gains) on derivative financial instruments	–	–	807	(226)	76.2	(22.7)
Post-employment benefits net financing costs	–	–	19	20	1.3	1.5
Restructuring costs	307	328	–	–	23.9	24.9
Tax on unrecognised losses	–	–	–	–	5.9	(28.6)
Items above attributable to non-controlling interests	–	–	–	–	(1.8)	(1.7)
Adjusted	3,541	3,053	(524)	(467)	249.6	212.5

Adjusted net finance costs were higher at £524 million (2015: £467 million) reflecting the full year impact of the cost of the USA acquisition debt partially offset by a reduction in our all-in cost of debt.

Reported net finance costs were £1,350 million (2015: £261 million), incorporating the impact of the net fair value and exchange losses on financial instruments of £807 million (2015: gains of £226 million) and post-employment benefits net financing costs of £19 million (2015: costs of £20 million).

After tax at an effective adjusted rate of 20.0 per cent (2015: 20.7 per cent), adjusted earnings per share grew by 17.5 per cent to 249.6 pence. The effective reported tax rate is 26.2 per cent (FY15: 1.9 per cent). The effective reported tax rate for 2015 was unusually low, largely due to the recognition of previously unrecognised tax losses as a deferred tax asset, on the basis that taxable profits would arise in the relevant entities following the acquisition of assets in the USA.

The effective tax rate is sensitive to the geographic mix of profits, reflecting a combination of higher rates in certain markets such as the USA and lower rates in other markets such as the UK. The rate is also sensitive to future legislative changes affecting international businesses such as changes arising from the OECD's (Organisation for Economic Co-operation and Development) Base Erosion Profit Shifting (BEPS) work.

Reported earnings per share were 66.1 pence (2015: 177.4 pence) reflecting non-cash amortisation of £1,005 million (2015: £697 million) and restructuring costs of £307 million (2015: £328 million), as well as the effects of fair value and exchange losses in finance costs mentioned above. The difference between reported (66.1p) and adjusted earnings per share (249.6p) is materially due to the same three items.

The weakening of sterling versus the euro and US dollar positively impacted reported and adjusted measures. On a constant currency basis, adjusted earnings per share grew 12.0 per cent.

The restructuring charge for the year of £307 million (2015: £328 million) relates mainly to our cost optimisation programme announced in 2013 (£188 million) and integration costs relating to the assets acquired in FY15 (£49 million).

The total restructuring cash flow in the year ended 30 September 2016 was £268 million (2015: £256 million).

Cost Optimisation

The first phase of our cost optimisation programme is still expected to deliver savings of £300 million per annum from September 2018 and to have a cash implementation cost of in the region of £600 million. £65 million was realised in 2016 through a range of initiatives focused on reducing overheads and product cost.

As we simplify the business, optimise our manufacturing footprint and leverage our global scale through procurement we have been able to realise operational efficiencies. The cumulative savings to date are £240 million. In 2016, the cash cost of the programme was £80 million (2015: £169 million) bringing the cumulative net cash cost of the programme to £420 million.

We have identified further opportunities to extend this programme and have announced a second phase of cost optimisation that is expected to drive a further £300 million of annual savings from September 2020, at a cash cost in the region of £750 million.

Capital Discipline

Our continued focus on capital discipline is driving free cash flow that has enabled a further £1 billion of debt reduction at constant currency. Our dividend pay-out ratio of 62 per cent is among the lowest among our tobacco peers, leaving significant headroom for future dividend growth.

Reported net debt increased by £1.4 billion, with adjusted net debt increasing by £1.3 billion. The increase in adjusted net debt represents a £1.0 billion debt reduction from our continued focus on capital discipline before taking into account a £2.3 billion adverse impact of foreign exchange and fair value of derivatives.

The denomination of our closing adjusted net debt was split approximately 56 per cent euro and 44 per cent US dollar. As at 30 September 2016, the Group had committed financing in place of around £17.3 billion. Some 24 per cent was bank facilities, 6 per cent was commercial paper and 70 per cent was raised through capital markets.

Following targeted cancellation of certain bank facilities during the financial year, enabled by free cash flow generation, the outstanding syndicated acquisition facilities through which we funded our 2015 USA acquisition have been reduced to \$0.9 billion.

Our all-in cost of debt reduced 40 basis points to 3.9 per cent (2015: 4.3 per cent) as older debt matured and was repaid. Our interest cover was 7.1 times (2015: 6.3 times). We remain fully compliant with all our banking covenants and remain committed to retaining our investment grade ratings.

All of our capital allocation decisions are subject to relevant commercial analysis and hurdle rates to ensure they deliver appropriate levels of return, and potential acquisitions are judged on strict financial and commercial criteria including the ability to enhance the Group's return on invested capital (ROIC). Typically, we seek an overall internal rate of return in excess of 13 per cent across the investments we make in our existing business. This disciplined approach is supporting our investment choices and underpins returns for shareholders. Our ROIC measure increased this year to 13.9 per cent (2015: 11.0 per cent) as a result of continued discipline and the full year effect of the US acquisition.

During the financial year, we further enhanced our investment appraisal framework to even more closely align the risks and expected returns from capital allocation decisions, to ensure that investment is focused on delivering our strategic objectives whilst generating attractive returns.

Taxation Policy

Our global tax contribution through both indirect and direct taxation exceeds £17 billion annually (excluding Logistics).

Our policy is to ensure compliance with tobacco taxation and product supply legislation and to engage constructively with revenue authorities worldwide to help combat illicit trade. We also engage with revenue authorities and governments more widely on policy issues to voice opposition to aspects of regulation and excessively high tobacco taxation that are likely to increase illicit trade to the detriment of consumers, governments and the Group.

In the field of direct taxation, it is our policy to maintain a sustainably low effective tax rate in order to enhance shareholder value whilst having due regard to financial and reputational risk. Further information on income taxes is given in notes 8 and 21 to the financial statements.

In pursuing this policy it is of paramount importance that our actions comply with all national and international laws on corporate and tobacco taxation and that there is full disclosure and transparency in our dealings with all revenue authorities.

The Board is kept informed of all material developments relating to our taxation position with updates on tax matters regularly provided to the Audit Committee.

Further Strong Dividend Growth

We have delivered another year of 10 per cent growth in our dividend, demonstrating our commitment to growing shareholder returns. This is our eighth consecutive year of double digit dividend growth.

The Group has paid two interim dividends of 23.5 pence per share each in June 2016 and September 2016, in line with our quarterly dividend payment policy to give shareholders a more regular cash return.

The Board has approved a further interim dividend of 54.1 pence per share and will propose a final dividend of 54.1 pence per share, bringing the total dividend for the year to 155.2 pence per share, up 10 per cent and in line with our policy of growing dividends by at least 10 per cent per year over the medium term.

The third interim dividend will be paid on 30 December 2016 with an ex-dividend date of 17 November 2016. Subject to AGM approval, the proposed final dividend will be paid on 31 March 2017, with an ex-dividend date of 16 February 2017.

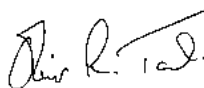
Liquidity and Going Concern

The Group's policy is to ensure that we always have sufficient capital markets funding and committed bank facilities in place to meet foreseeable peak borrowing requirements.

In reviewing the Group's committed funding and liquidity positions, the Board considered various sensitivity analyses when assessing the forecast funding and headroom requirements of the Group in the context of the maturity profile of the Group's facilities. The Group plans its financing in a structured and proactive manner and remains confident that sources of financing will be available when required.

Based on its review, and having assessed the principal risks facing the Group, the Board is of the opinion that the Group as a whole and Imperial Brands PLC have adequate resources to meet operational needs for a period of at least 12 months from the date of this report and concludes that it is appropriate to prepare the financial statements on a going concern basis.

The Board's statement on its assessment of longer-term viability is set out on page 32.



Oliver Tant
Chief Financial Officer

CORPORATE RESPONSIBILITY

We run our operations responsibly, recognising that how we behave today impacts our business tomorrow.

The responsible approach we take is integral to the success of our growth strategy and is underpinned by our values and Code of Conduct. Our policies, internal controls and risk management processes further govern the way we operate.

During the year we refreshed our Code of Conduct and reissued it to all employees across Imperial Brands. In updating the Code we took the opportunity to reinforce the links between the Code and our values

and introduced a new section on the responsible use of social media, a communication channel that has grown significantly since the Code was last published. The Code is available in 30 languages and published in full on our website: www.imperialbrandspc.com

We track our Corporate Responsibility (CR) performance against our progress in four key areas: being responsible with products, providing a rewarding workplace, respecting natural resources and reinvesting in society.

These form the basis of our Responsibility Framework and are the priorities for our business, our people and our stakeholders.

The following pages provide an overview of our CR achievements in the year. More detailed information can be found in the responsibility section of our website.

The progress we're making continues to be recognised externally, including in the 2016 Dow Jones Sustainability Index where we scored 76 per cent in the RobecoSAM assessment.

Towards the end of the year we commissioned an independent materiality assessment to identify and prioritise the most important sustainability issues for our business. The assessment involved input from a range of external stakeholders and will help to further develop our CR strategy. More details will be reported in 2017.

We measure our health and safety and environmental performance by comparing our results with our 2009 baseline year, using independently verified financial year (FY) 2015 data.



Key data reported in the Annual Report and Accounts for the year to 30 September 2016 as indicated in footnotes has been independently assured by PwC under the limited assurance requirements of the ISAE 3000 (Revised) standard.

The full assured data and PwC's assurance report are included in the Corporate Responsibility section of the website www.imperialbrandspc.com/responsibility

RESPONSIBLE WITH PRODUCTS

We ensure our products are manufactured, marketed and sold responsibly.

We recognise there are societal concerns about the health risks of smoking and acknowledge that smoking is a cause of serious disease in smokers.

Adhering to High Standards

We are rightly expected to adhere to high product standards. In rigorously testing and analysing our products we ensure that we continually build our knowledge and are able to fulfil our duty of care to consumers, as well as meet legal requirements for scientific disclosures and submissions.

We see e-vapour as a key future growth opportunity for the business and continue to invest in the next generation of e-vapour products, focusing on Fontem Venture's blu brand.

The long-term development of the e-vapour category depends on clear and consistent regulation. We support regulation that will drive high consumer safety and product quality standards.

Our research shows that the vast majority of tobacco smoke constituents are not present in e-vapour products, which means e-vapour has potential as a reduced risk product relative to tobacco.

We share our findings with regulators and other key stakeholders and intend to continue to take an active role in the ongoing debates about e-vapour.

Marketing Responsibly

Legislation that governs the way tobacco should be advertised and marketed to the public exists in most markets. We also have our own stringent International Marketing Standard (IMS), which is published on our website.

All Imperial Brands companies and employees, and the agencies who work with us around the world, must adhere to our IMS and local legislation at all times. To support IMS awareness and understanding we have developed an e-learning module that has been translated into 12 languages.

Combatting Illicit Trade

The illegal market in tobacco undermines society's efforts to ensure that tobacco products are marketed responsibly.

As well as depriving governments of valuable tax revenues, illicit trade has other adverse impacts: children can more easily obtain tobacco, adult consumers are exposed to products that have no quality controls, and retailers and tobacco companies lose legitimate sales.

We advocate a partnership approach to combatting illicit trade and seek to work with governments and customs and law enforcement agencies to tackle the problem of tobacco smuggling and counterfeiting.

Sharing our intelligence with these key stakeholders led to a number of successful operations in the year, including the disruption and closure of major counterfeiting facilities in Poland and Russia.

We have Memoranda of Understanding (MoU) with authorities around the world and continue to invest in our long-term anti-illicit trade partnership agreement with the European Commission and Member States. During the year, we renewed our MoU in Vietnam and signed new MoUs in Spain and Chad. In total, we now have 27 MoUs in place.

Working with Retailers

Tobacco products are for adults and should never be sold to children. We work with retailers to reinforce this message and encourage responsible selling. We support initiatives aimed at preventing sales of tobacco to children, including schemes that highlight the minimum age at the point of sale. For example, in the UK we provide training for independent retailers to improve their awareness and understanding of selling responsibly.

An independent report we commissioned on smoking trends last year has helped us prioritise markets for initiatives aimed at preventing children from getting access to tobacco. We produced a guide to further support these markets implement their initiatives and engage with key stakeholders.

REWARDING WORKPLACE

Our goal is to provide a great workplace for our employees. We aim to provide a safe, pleasant working environment that inspires them to do their best.

A Diverse Workforce

We employ around 34,000 people including 13,100 women, representing 39 per cent of our total workforce. At a senior leadership level, 22 per cent of the Operating Executive and 30 per cent of the Board are female, as of 30 September 2016.

We benefit enormously from our diverse workforce; our people come from different backgrounds and cultures, creating a vibrant working environment that thrives on new ideas and fresh thinking.

The importance of diversity, equality and non-discrimination is highlighted in our Code of Conduct and underpinned by our values.

For us, equal opportunity is about assessing capabilities irrespective of gender, race, disability, age, sexual orientation, religious beliefs or any other aspect which is not related to performance.

Our values capture the essence of what it's like to be part of Imperial Brands, with the 'We' and 'I' values reflecting the individual and collective behaviours we expect from employees across all our subsidiaries.

We are pleased that our efforts to provide the best possible working environment and opportunities for our people continue to be recognised externally.

During the year we received a number of Best Employer awards, including in Slovakia, Norway and Spain.

CORPORATE RESPONSIBILITY

CONTINUED

Engaging with our People

Regular engagement with our people helps motivate them to do their best. We provide regular updates on our strategic priorities and performance through a broad range of communication channels including meetings, emails, videos, intranet, social media, webinars, conferences and employee magazines.

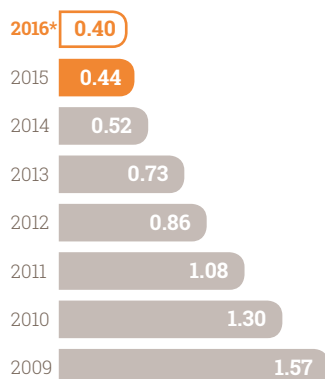
A global engagement survey is conducted every 18 months and gives employees the opportunity to tell us what it's like to work for Imperial Brands. We respond to their feedback and use it to shape action plans at both a local and global level. The 2016 survey generated an excellent response rate and showed an increase in overall engagement levels. This is encouraging, given the on-going change that is taking place in the business.

Workplace Health and Safety

The welfare of our people is of utmost importance to us. We have reduced our Lost Time Accident Frequency Rate by 72 per cent over the last six years and continue to focus on improving health and safety standards across the business.

We were saddened that a contract driver died in a road accident in the Central African Republic. We assisted the authorities with their investigation and also carried out our own. The findings have been used to further improve our employee Drive Safe programme.

Lost Time Accident Frequency Rate (per 200,000 hours)¹

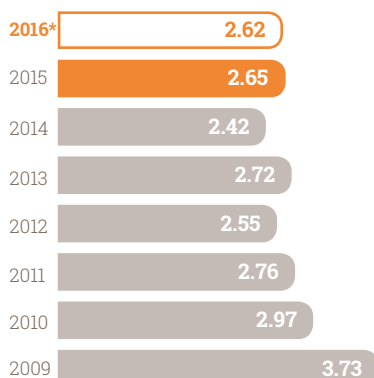


The findings of an independent health and safety review undertaken last year have formed the basis of an action plan for improving our health and safety standards.

The plan is being implemented across the business and includes initiatives aimed at enhancing our performance in three key areas: working from heights, driving safely and managing stress and resilience.

We are pleased to see a continual reduction in our sickness absence rate over the last six years. Since 2009 the rate has declined by 29 per cent.

Sickness Absence Rate (% of days worked)²



Seventy-nine per cent of our operations are now certified to the international occupational health and safety management standard OHSAS 18001.

REINVESTING IN SOCIETY

We are proud to have developed strong partnerships with a wide range of stakeholders in many different communities around the world.

Human Rights

We have a role to play in addressing human rights issues, including slavery and human trafficking. Our respect for human rights extends throughout our operations and is reflected in our Code of Conduct, our responsible leaf sourcing programme Social Responsibility in Tobacco Production (SRiTP) and our Supplier Standards, which we use to exert influence in our business and supply chain.

We have a focus on anti-discrimination and harassment, a healthy and safe working environment, responsible procurement, supplier partnerships and environmental responsibilities.

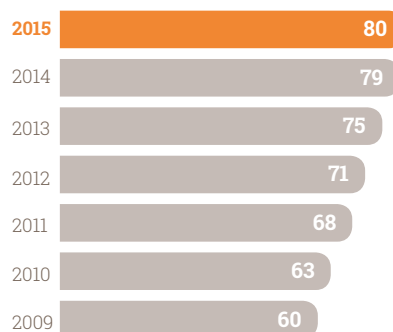
A detailed statement setting out the steps we have taken to mitigate the risk of slavery and human trafficking occurring within our business and supply chain during the financial year can be viewed on our website.

The key findings and recommendations of an independent human rights impact assessment we commissioned across our global operations and supply chains are also available on our website.

Supplier Standards

Working with supply chain stakeholders to address important issues such as leaf sustainability and child labour is a priority.

Social Responsibility in Tobacco Production Progress: Total Weighted Mean (%)³



Our leaf suppliers have been required to take part in our Social Responsibility in Tobacco Production (SRiTP) programme for many years. This programme encourages continual performance improvement in areas such as employment, health and safety, environmental management and good agricultural practices.

In April 2016 we replaced SRiTP with the Sustainable Tobacco Production (STP) programme, a common industry-wide initiative supported by all the main tobacco companies. All areas previously assessed by SRiTP are covered by STP.

1. Verified accident data is reported 12 months in arrears to allow for data collection and verification. FY15 data has been assured by PwC.

2. Sickness absence includes non-work related and work related absence.

3. All our tobacco suppliers participated in the SRiTP programme in 2015, which provides specific guidance for improvement against a variety of criteria. See our website for more information. Data for 2015 has been verified. We report 12 months in arrears to allow for the reporting and analysis of data.

* Provisional unverified FY16 data – comprising verified data for the last six months of FY15 and unverified data for the first six months of FY16 – is provided in this report. Verified data for FY16 will be published next year.

We believe STP is a more robust programme and will therefore provide an improved level of accuracy and precision in scoring the performance of leaf suppliers. As a result of this increased robustness we expect our first STP scores, which will be published next year, to be lower than previous SRiTP scores. Our SRiTP score in 2016 increased to 80 per cent.

We also have a Supplier Qualification Programme for non-tobacco material (NTM) suppliers. This is a self-assessment questionnaire that covers business conduct, environmental management, health and safety and employment practices. We conduct periodic onsite audits to confirm these assessments.

Farmer Livelihoods and Child Labour

We oppose child labour and are actively addressing the issue in our supply chains.

We are a member of the Eliminating Child Labour in Tobacco (ECLT) Foundation and have ongoing constructive dialogue with Human Rights Watch (HRW), an international non-governmental organisation that conducts research and advocacy on human rights and has a strong interest in child labour in tobacco growing. At a meeting with HRW during the year we provided more information on how we partner with our suppliers to tackle child labour.

Our Leaf Partnership Programme continues to support projects that seek to enhance the livelihoods of farmers by reducing their overall labour requirement and improving fuel efficiency. This helps secure future tobacco supplies and is essential for providing farmers with a better income and higher standards of living, reducing poverty and the potential reliance on child labour.

Supporting Communities

We fund projects that are connected to the communities in which we operate. We particularly focus on supporting the most disadvantaged communities around our factories, offices and tobacco sourcing activities.

We continue to be encouraged by the growing number of employees who volunteer to get involved in projects linked to our responsibility framework. Our global volunteering drive, entitled Mobilise for May, involved employees supporting over 160 projects in 44 countries worldwide, exceeding our global target of 55,000 hours volunteered.

RESPECTING NATURAL RESOURCES

We respect natural resources and are committed to further reducing our environmental impact by minimising waste, improving energy efficiency and reducing emissions.

Our Data Trends

We have set long-term targets for our key environmental performance indicators, energy, waste and water use. We track our progress against our 2009 baseline year. In line with other major companies, we measure our performance against the amount of tobacco net revenue we generate.

Climate Change and Energy

Our Operational Excellence Programme, aimed at improving and embedding a leaner way of working across our manufacturing sites, continues to be rolled out across the Group.

We have reduced our energy consumption by 15 per cent and our CO₂ emissions by 9 per cent over the last six years.

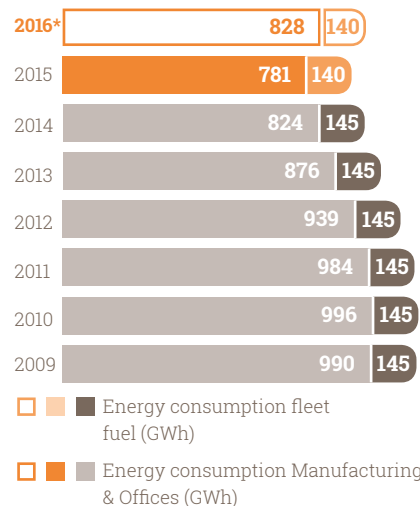
Each year we participate in the CDP Climate Change Programme, which works with organisations to measure and reduce their emissions and climate change impacts.

We continue to make improvements in this area, achieving a 'B' score from the CDP in 2016. This indicates we have a high level of environmental stewardship and are proactively managing climate change matters as they relate to our business. We are also working with the CDP to capture more information about the approach our major suppliers take to climate change and water management, through the CDP Supply Chain Programme.

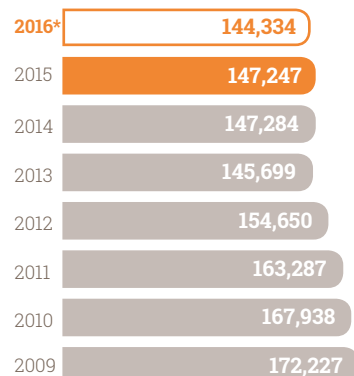
Resource Efficiency

Getting the most out of the materials and natural resources we use is good for our business and good for the environment.

Absolute Energy Consumption (GWh)¹



Energy Consumption (kWh/£million)¹



1. Environmental data is reported 12 months in arrears to allow for data collection and verification. The monetary value '£ million' is for tobacco net revenue (or logistics distribution fees, where appropriate). FY15 data has been assured by PwC; see website for more information.

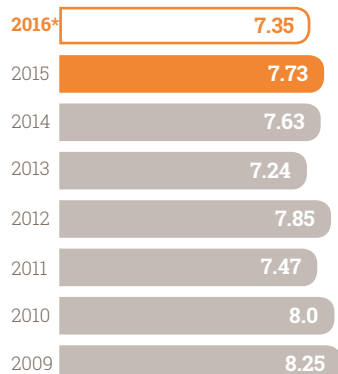
* Unverified FY16 data is estimated based on data from the last six months of FY15 and the first six months of FY16. Verified data for FY16 will be published next year.

CORPORATE RESPONSIBILITY

CONTINUED

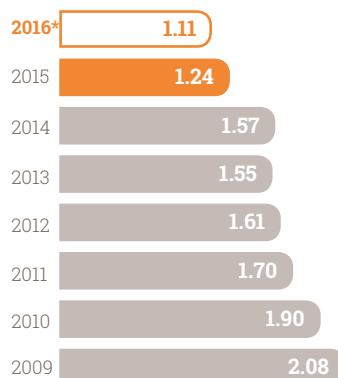
Waste

(Tonnes/£million)¹



Waste to Landfill

(Tonnes/£million)¹



Since the 2009 baseline year we have reduced waste by 6 per cent and waste to landfill by 40 per cent.

In manufacturing we are further increasing our use of environmental management systems that are independently certified to the environmental management standard ISO 14001. Ninety three per cent of our factories are now certified to this standard.

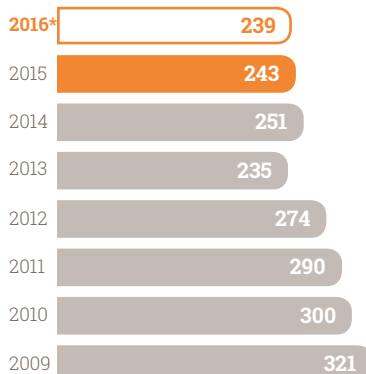
Reforestation Programmes

In Africa, where wood is the primary fuel source and the majority of tobacco farmers are smallholders, we are actively involved in protecting natural forests and reducing wood consumption.

We have continued to work with our African tobacco suppliers on a major tree planting programme that aims to achieve wood sustainability in Africa by 2022. This involved planting 1.7 million trees in Africa in 2016.

Water Consumption

(m³/£million)¹



Water Management

We have a strong track record of effectively managing water use and have reduced water consumption by 24 per cent since the 2009 baseline year. In our factories we apply environmental management systems under the international standard ISO 14001, which also help to reduce water use and manage waste water, and each location has its own local water management targets.

As part of our focus on improving water security in Africa we are funding an increasing number of projects related to water preservation.

In Malawi, for example, we are working with one of our suppliers to create three irrigation dams and six boreholes, which is expected to provide 900 farmers with access to irrigation water and 1,500 people with access to clean water.

Greenhouse Gas Emissions Reporting

We report on greenhouse gas emissions resulting from our tobacco operations which fall within our consolidated financial statements using the operational control reporting approach.

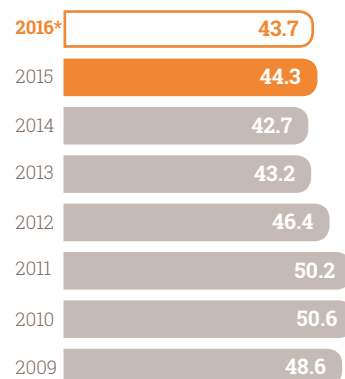
We report Scope 1 (direct) and Scope 2 (indirect) emissions for which we are responsible, using a methodology in line with the Greenhouse Gas (GHG) Protocol Corporate Accounting and Reporting Standard (revised edition).

The scope of our GHG reporting is outlined below and detailed in the 2016 non-financial Reporting & Criteria Document in the Responsibility section of our website: www.imperialbrandsplc.com

We report on the seven main greenhouse gases and report in terms of tonnes of CO₂ equivalent (CO₂e). Our relative emissions are expressed against tobacco net revenue.

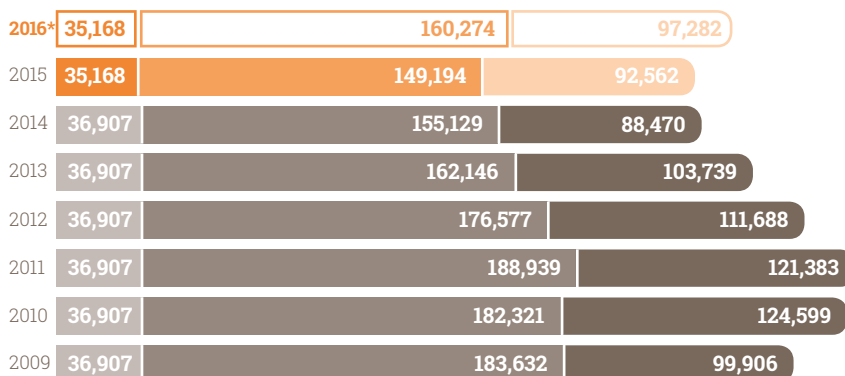
CO₂ Equivalent Emissions

(Tonnes/£million)¹



Absolute CO₂ Equivalent Emissions

(Tonnes)



■ ■ CO₂ equivalent emissions Scope 1 excl fleet fuel (Tonnes)
■ ■ CO₂ equivalent emissions Scope 2 (Tonnes)
■ ■ CO₂ equivalent emissions Scope 1 fleet fuel (Tonnes)

1. Environmental data is reported 12 months in arrears to allow for data collection and verification.
The monetary value '£million' is for tobacco net revenue (or logistics distribution fees, where appropriate).
FY15 data has been assured by PwC; see website for more information.

* Unverified FY16 data is estimated based on data from the last six months of FY15 and the first six months of FY16.
Verified data for FY16 will be published next year.

Our Scope 1 emissions comprise: emissions from stationary fuel combustion at our sites; emissions from mobile fuel combustion in our fleet of company vehicles; leakage of refrigerant gases; and process emissions from the Dry Ice Expanded Tobacco process at our tobacco expansion plant. Our Scope 2 emissions comprise the indirect emissions resulting from the use of purchased electricity, heat and steam at our sites. We report according to the GHG Scope 2 Guidance (2015), using location-based emission factors.

We use the CO₂e factors and calculation methodology for fossil fuels and electricity set out in the UK Department for Environment, Food and Rural Affairs (DEFRA) document '2014 Government GHG Conversion Factors for Company Reporting'.

Our reported emissions include all main sources from manufacturing sites over which we have operational control and our main offices (Bristol, Hamburg, Paris, Madrid and Casablanca). Operations not included, as deemed de minimis or being outside our current reporting scope, relate to small sales offices (which collectively contribute no more than 2 per cent of our total Scope 1 and 2 emissions).

Emissions for FY16 as reported here comprise unverified data for the first six months of FY16 and verified data for the last six months of FY15, except for mobile fuel consumption by our fleet vehicles which comprises complete verified data for FY15. Verified data for FY15 is reported 12 months in arrears to allow for collation, validation and external assurance.

We report separately below externally verified information provided by Logista, the Group's subsidiary transport and logistics business which is managed remotely due to commercial sensitivities. Logista has provided verified data since FY14 for absolute Scope 1, 2 and 3 emissions.

Logista

		Scope 1	Scope 2	Scope 3
CO ₂ equivalent emissions (Tonnes)	FY15	35,065	4,378	199,953
	FY14	35,731	4,455	213,081

Logista's Scope 1 emissions comprise stationary and mobile fuel combustion from transport operations for which Logista has operational control, and from the leakage of refrigerant gases at those operations. Scope 2 emissions comprise indirect emissions resulting from the use of purchased electricity at sites under Logista's operational control. Scope 3 emissions comprise transport activities for which Logista does not have operational control.

Logista's FY15 relative Scope 1 and 2 emissions comprise 52.7 tonnes (FY14: 47.4) of CO₂ equivalents per million pounds of FY15 distribution fees (our non-GAAP revenue measure for Logista). Further information on the scope of Logista's GHG reporting is available at www.grupologista.com

RISK MANAGEMENT

Our ability to achieve our strategic objectives and capitalise on growth opportunities requires effective management of the risks we face. We define “risks” as anything that could prevent the achievement of our strategic objectives.

APPROACH

Risk is an inherent part of our operating environment. The VUCA (volatile, uncertain, complex, ambiguous) world in which we operate requires effective management and monitoring of known risks, along with the identification and assessment of emerging risks, to achieve our strategic objectives. Central to this approach is the clear understanding that risk management is the responsibility of all our people.

The approach seeks to manage, rather than eliminate, the risk of failure to achieve our strategic objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

RISK MANAGEMENT FRAMEWORK

The Group's risk management framework, aligned to the operating model, is an integrated approach based upon the three lines of defence. The structure encourages the communication and escalation of risk and control related matters across the Group's diverse geographic footprint.

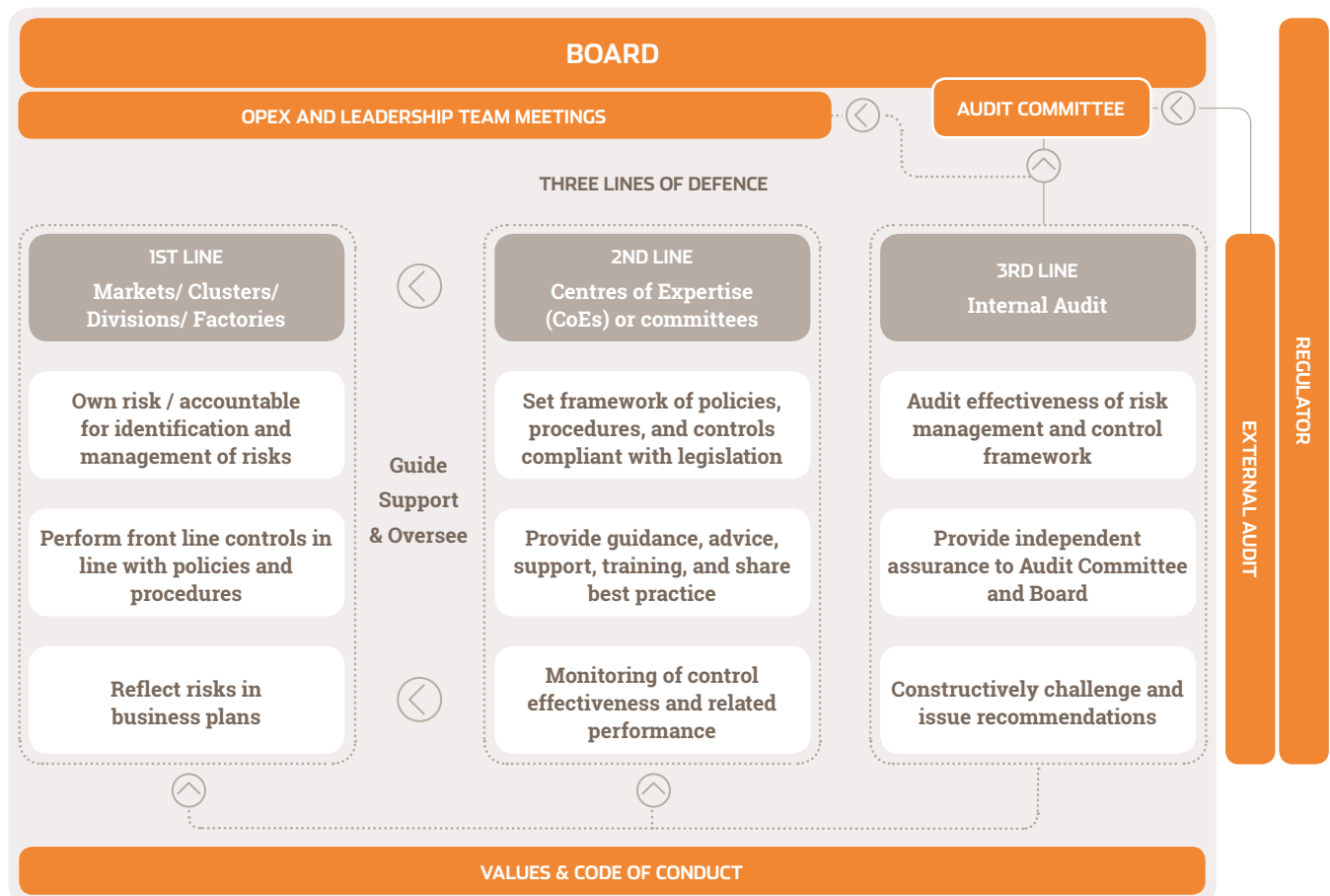
The Board has ultimate responsibility for the Group's strategy and related risk appetite. The Board is also responsible for ensuring the effectiveness of the risk management and internal control systems, with the Audit Committee assisting in the discharging of these responsibilities.

The OPEX (Operating Executive) is responsible for the operational stewardship of the business, including the ownership of the Group risks and related assurance activities. OPEX ensures the successful and effective alignment of functional business plans to the Group strategy, with business unit and functional management responsible for the delivery of operational performance and the management of the inherent risks. These management teams are responsible for ensuring that the Group's strategic objectives are achieved in line with Group policies and standards, and that we conduct business in compliance with our Code of Conduct.

The Group's functional and divisional management structures, led by our OPEX, enable a continuous process for the identification, evaluation and management of significant risks to the achievement of business objectives at both a Group and local level, enabling effective and timely identification of actual and emerging risks and responses to mitigate impacts or realise opportunities.

A key enabler of our risk management approach is the deployment of “Centres of Expertise” (2nd line). These are central functions employing technical experts with the knowledge and practical skills to develop and provide appropriate policy, process, control structures, and support to local management (1st line) within our global business to enable the consistent application of policy.

THREE LINES OF DEFENCE



An example of this is our Finance function. This has responsibility for the financial policies and standards adopted within the Group. It also manages our financial reporting processes to ensure the timely and accurate provision of information, which enables the Board to discharge its responsibilities, including the production of our half yearly and annual accounts.

The central Finance function is supported by a network of finance managers throughout the Group who have the responsibility and

accountability to provide information in keeping with our policies, procedures and internal best practices as documented in our Group Finance Manual.

The design of the Group's operating model supports the ability of our operational teams to manage commercial, legal and regulatory risk at a local level in a consistent manner. Each business unit is responsible for identifying, evaluating and monitoring the risks faced by their part of the business, and for ensuring compliance to policy and local legal requirements.

ASSESSMENT OF RISKS AND INTERNAL CONTROL COMPLIANCE

In accordance with the recommendations of the FRC's UK Corporate Governance Code (formerly known as the combined code) for Directors, the Group's systems of internal control are designed and operated to support the identification, evaluation and management of risks affecting the Group. They facilitate the effective and efficient operation of our business, provide assurance regarding the integrity of our internal reporting and are designed to comply with relevant laws and regulations, across all areas of operations. These systems are subject to continuous review as circumstances change and new risks emerge.

Risk Identification

Embedding of risk foresight within the business is facilitated by the completion of formal risk assessment updates by business units on a quarterly basis aligned to our key planning and forecasting cycles, ensuring that risks are considered on a timely and ongoing basis.

Assessment and Evaluation

Risk assessments are completed by operational management across the business, with consideration of both Group and local risks required. These are reviewed and considered by senior management as part of their monitoring of the underlying drivers of business performance.

Additionally, key Centres of Expertise provide an evaluation of the results of the assessments, and provide valuable insight into the potential impact of changes in the regulatory environment which are confirmed in local risk registers and appropriate actions planned.

The results of the bottom-up risk assessment are reviewed by, and discussed with, the OPEX. The top-down calibration of risks by the Board and OPEX ensures a consistent top-down method in the agreement, assessment and prioritisation of risks, as well as the assessment of our existing measures to manage and mitigate those risks and consideration of wider strategic impacts.

The Board receives the consolidated view of the bottom-up and top-down inputs, and confirms its acceptance of these risks, and their alignment with the Group's risk appetite.

The principal risks arising from the consolidated risk assessment are provided on pages 28 to 31.

Effective Risk Mitigation

The management of operational risk and compliance to the Group's key control requirements is the responsibility of business unit and operational management. Policies, standards, processes and related training are developed by subject matter experts in the Group's CoEs that assist in ensuring the business remains compliant with Group requirements.

As part of the communication and monitoring of internal control compliance our senior management within markets and factories



are required to complete key control assessments on a half yearly basis. The key controls highlighted within the assessment also support operational management to understand their responsibilities and accountabilities for the delivery of results in line with the Group's risk appetite, and highlight areas of best practice that can be shared across the business.

Additionally, a year end certification process is completed, under which management confirms that risk mitigation controls have operated effectively throughout the year and that entities have complied with our policies, including the Code of Conduct and anti-bribery requirements, as well as fraud prevention processes.

Monitor Commercial Impact

The results of these assessments are provided to our Centres of Expertise to enable any individual control trends to be resolved on a Group basis, to enable targeted support to individual locations, and to provide feedback on the responses provided relative to the work CoEs complete as part of their ongoing role.

The results of the control assessments are provided to our Internal Audit function. This provides the opportunity for an independent verification of the responses through the testing completed by Internal Audit as part of their annual plan and is an input to the development of that risk based plan. The results of Internal Audit reviews are shared across the business in order to provide an independent opinion on both compliance to, effectiveness and appropriate design of our internal control framework.

The risk approach embeds the assessment of risk into the Group's ongoing performance and business planning cycle. This enables the assessment of risk based root cause analysis to be performed and timely understanding of the potential future impacts and opportunities arising. By continuing to develop this foresight we seek to reduce the probability of unforeseen events.

PRINCIPAL RISKS AND UNCERTAINTIES

RISK PROFILE

The results of the risk assessment completed during the business planning process have not highlighted any significant changes from the previous year. The risks and their relative probability and impact remain materially consistent. The only significant change in the strategic risks is the reduction in the impact of mergers and acquisitions in the year resulting from the successful integration of the US business.

All principal risks identified through the risk assessment process, and agreed by the Board, have a potential impact in achieving strategic objectives in the next 12 months, with an additional impact assessment considered over a longer three year horizon.

In the following section we highlight the principal risks we face and identify the mitigations that we have in place to manage the impact of these risks upon the business. Not all of these factors are within our direct control, and the list cannot be considered to be exhaustive, as other risks and uncertainties may emerge in a changing business environment.

As is common with most large organisations, the Group is subject to general commercial risks; for example, socio-economic, cyber-security breaches, failure of our IT infrastructure, liabilities arising from defined benefit pension schemes, the impact of change programmes, the cost of our raw materials, and the impact of competition.

As a multi-national organisation, a large amount of the Group's revenue in the year was generated in markets outside the UK and the Group is therefore exposed to movements in foreign exchange rates which could impact the Group's financial results which are reported in pounds sterling. Additionally, the Group is also exposed to movements in foreign exchange rates due to its foreign subsidiaries, its commercial trading transactions denominated in foreign currencies and foreign currency cash deposits, borrowings and derivatives.

BREXIT

There are a number of uncertainties in connection with the future of the UK and its relationship with the EU.

We have considered the consequences that Brexit could have upon the business and have concluded that it does not raise any new risks but does impact a number of our existing risks on an individual basis e.g. exchange rate risk, product regulatory change, change in excise duty, illicit trade, availability of liquidity. Accordingly, the approach we have adopted is to consider the impact of Brexit in those risks.

By aligning the management of the outcomes to existing risk responsibilities this provides a more effective and operationally focused mitigation of these impacts on an ongoing and timely basis.

Reduction in size of the legitimate tobacco market

Strategic priority – Strengthening our portfolio, Developing our footprint

What affects us	Potential consequences	What we do
Product regulatory change Regulatory restrictions exist in many of our markets which impact our consumers by influencing availability, demand and freedom to use our products.	Changes in legislation can have a negative effect on consumer choice, reducing consumption levels, and revenues. Compliance with regulation has an associated cost. Changes in regulation increase compliance requirements and can therefore result in an increase in costs, potentially impacting profits.	We engage with authorities to provide informed input to unintended consequences of disproportionate changes in legislation. Regulatory changes are proactively managed to ensure that the business is commercially positioned to positively manage the risks and opportunities that such change creates. The Group's expertise and resources are prioritised according to the relevant key regulatory issues. Cross-market liaison is promoted within the Group to ensure best practice and opportunities from markets already impacted are identified, understood and applied.
Change in excise duty Adverse changes in the level or structure of excise duties as governments seek to raise public funds.	Increased cost to the consumer could potentially reduce purchase volumes. Any inability to pass on an increase in excise could result in lower product margins. The widening price differential between tobacco products in neighbouring countries increases the attractiveness to the consumer of purchasing non-domestic duty paid product.	We engage with authorities to provide informed input to unintended consequences of disproportionate changes in excise. We take commercial steps to ensure strategic price and product offerings exist in the context of the excise duty structures in each market.

Reduction in size of the legitimate tobacco market continued

Strategic priority – Strengthening our portfolio, Developing our footprint

What affects us	Potential consequences	What we do
Counterfeit and illicit non-duty paid product in market The consequence of excise and regulatory regimes is a widening gap between the price of legitimate and illegitimate product. As a result the legitimate tobacco industry continues to be subject to the significant impact and increasing threat of illicit trade.	Counterfeit and illicit trade reduces the size of the legitimate market. The sale of counterfeit product and smuggled "illicit whites" in our markets acts as a direct competitor to legitimate domestic duty paid, travel retail and duty free products, eroding our volumes and market shares. Counterfeit product is not subject to the stringent quality requirements of legitimate product. Customer perception of inferior quality could impact the reputation of genuine product and damage our brands.	Specialist teams are employed to support the business, governments, and law enforcement agencies with targeted solutions to illicit trade. We maintain strong standards and controls for our business and our first-line customers to prevent diversion of our products. We seek to partner with governments and law enforcement agencies around the world on anti-illicit trade initiatives. We work alongside the European Commission's Anti-Fraud Office (OLAF) and law enforcement agencies.
Macro-economic conditions in key markets The Group has a significant presence in mature European markets and the US. Increased economic uncertainty, related austerity measures, or geo-political pressures in those markets could lead to a reduction in consumption of legitimate product.	Any material change in the economic circumstances of, and/or our performance in, our key markets may affect our future profit development and have an adverse impact on the Group's revenue or profits.	We continually monitor and analyse consumption patterns and economic indicators in order to ensure that our current and future portfolio provides the consumer with a range of products across different price points. This analysis is completed at both a local and Group level and provides a key input to our product development, business planning and pricing strategies. Our international footprint and comprehensive portfolio provide an increasingly balanced exposure to both EU and non-EU markets.

Optimising market share

Strategic priority – Strengthening our portfolio, Developing our footprint

What affects us	Potential consequences	What we do
Brand equity Failure to maintain and grow brand equity or an inability to utilise that brand equity (as a result of disproportionate product regulatory changes such as plain packaging).	Adverse impact upon planned sales volumes and revenues resulting from a reduction in customer brand loyalty.	We have a consistent strategic marketing approach across markets, supported by monitoring of our brand equity. Brand migrations support the strategy to simplify the portfolio, reducing complexity in the supply chain and providing cost savings that can in turn be reinvested in the brand propositions. Market trends and competitor innovations are monitored in order to ensure we maintain the strength and relevance of our brand offerings. We employ experts to ensure that the intellectual property of our brands is appropriately protected.
Product quality Product fails to meet regulatory or consumer requirements.	Brand and reputational damage resulting in reduced sales volumes. Potential financial penalty and regulatory censure resulting from failure to maintain appropriate product standards.	Quality control testing and monitoring is a core part of our manufacturing and supply chain processes, with robust regulatory compliance completed on a continual basis. Customer complaints monitoring and escalation processes exist across our markets, ensuring that customer feedback is acted upon and any quality issues are managed in an effective and appropriate manner. In the event of the requirement to recall product, effective processes exist to mitigate the risks to our supply chain.
Speed of response The Group fails to respond to market dynamics in a timely manner.	Failure to maximise opportunities in markets. Reduction in sales volume or revenues resulting from failure to maintain portfolio in line with changing consumer demands.	Product innovation and customer propositions are monitored across our markets. Customer trends and choices are analysed at both a local and Group level, with effective processes in place to support innovation.

PRINCIPAL RISKS AND UNCERTAINTIES

CONTINUED

Access to funding

Strategic priority – Capital discipline

What affects us	Potential consequences	What we do
Financial market risk We have a significant level of committed debt, financed in the debt capital markets and bank loan markets. We expect any future required refinancing of this debt prior to maturity to be obtained from these markets and for us to be able to rely on funds being available from our bank counterparties when requested to be drawn.	A fall in certain of our credit ratings would raise the cost of our existing committed funding and could raise our cost of future funding and affect our ability to raise debt from the current breadth of funders. Approximately 71 per cent of the Group's net debt is currently at fixed levels of interest, and therefore the Group is exposed to movements in interest rates which could result in higher funding costs and cash outflows on the remainder. We also place cash deposits and enter into derivative financial transactions with a diversified group of financial institutions and we would be affected if those counterparties did not honour their commitments.	We have a strong focus on cash generation and the reduction in our debt over time. Our Treasury Committee (TC) oversees the operation of the Treasury function in accordance with the terms of reference set out by the Board. The TC sets out a framework for the Treasury function to operate within. The framework, which is periodically fully reviewed, covers, amongst other things, financing, liquidity and risk management, which includes interest rate, foreign exchange and counterparty risk. The TC receives regular reporting on matters covered by the framework. Cash flows, financing requirements and key rating agency metrics are regularly forecast and updated in line with business performance. This information is considered alongside conditions in the debt capital and bank loan markets to ensure we are well placed to meet the future financing needs of the Group and optimise its cost and availability. For significant acquisitions of overseas companies, borrowings are raised in the appropriate currency (or are swapped via derivatives into the appropriate currency) to minimise the balance sheet foreign exchange translation risk.

Cost optimisation and strategic change initiatives

Strategic priority – Cost optimisation, Capital discipline

What affects us	Potential consequences	What we do
Cost optimisation Failure to achieve expected cost efficiencies.	Failure to align cost base results in reduced profit and cash available for reinvestment in the business. Reduction in stakeholder confidence as a result of failure to achieve committed cost savings.	Continued focus upon cost and cash agenda embedded within the business planning and operational processes. The Group's investment appraisal process provides robust and effective assessment and challenge of investment requests. Monitoring of cost and cash form a key part of business performance reporting.
Operating model and other strategic change initiatives In order to achieve our strategic objectives, the Group may be required to undertake material initiatives, including change programmes and acquisitions.	The implementation of change initiatives could involve particular challenges and require management attention that would otherwise be devoted to running our business. We may be unable to realise the anticipated benefits of change programmes and within the timeframe contemplated. Any inability to deliver change programmes to either intended scope, cost or time could have an adverse effect on cost, cash and profit.	To support the successful delivery of material initiatives within the organisation the Group has developed and implemented a standardised project management process that provides a robust framework to enable effective change management. The majority of the Group's material change programmes are coordinated under a single umbrella programme, ensuring alignment of deliverables, management of interdependencies, and limiting the impact of change upon our operational activities. The Operating Executive receives regular reporting on the progress of key projects. This provides a continuing assessment of deliverables in changing markets, and the evaluation of interdependencies across the business.

Compliance with legal and regulatory requirements

Strategic priority – Developing our footprint

What affects us	Potential consequences	What we do
Failure to comply with legislation Failure to comply with local and international laws (including sanctions) may result in investigations.	This may cause damage to our reputation and has the potential for financial and criminal penalties for both the Group and individuals. The cost of responding to any investigations can be substantial and require significant resource and management focus.	The Group's policies and standards, including our Code of Conduct, mandate that all employees must comply with legislation relevant to a UK listed company and in the countries in which they operate. E-learning and courses are provided to management and relevant employees to ensure understanding of key regulatory and compliance requirements. Senior management certify the compliance of their area of the business with the Code of Conduct as part of an annual certification process. Exceptions are reported and mitigating actions taken. We closely monitor developments in international sanctions and actively seek external advice to ensure that we remain compliant with them. Centres of Expertise and steering groups exist for key areas of legal compliance to provide expert advice in the development of policy, process, training and monitoring of compliance.
Tobacco litigation Tobacco litigation claims are pending against the Group in a number of countries. More claims may be brought in the future, including claims for personal injury and the recovery of medical costs allegedly incurred in treating smokers. The US, the jurisdiction with the greatest prevalence of smoking and health-related litigation, is also now a key country for the Group.	To date, no tobacco litigation claim brought against the Group has been successful and/or resulted in the recovery of damages. If any claim were to be successful, it might result in a significant liability for damages and might lead to further claims against us. Regardless of the outcome, the costs of defending such claims can be substantial and may not be fully recoverable.	We employ internal and external lawyers specialising in the defence of product liability litigation to provide advice and guidance on defence strategies and to direct and manage litigation risk and monitor potential claims around the Group. The US cigarette brands have been acquired without historic product liabilities and with an indemnity from Reynolds American in respect of any liabilities relating to the period prior to acquisition.
Significant market positions Our significant market position in certain countries could result in investigations and adverse regulatory action by relevant competition authorities.	Any allegation of inappropriate market behaviour creates the risk of financial penalty, and/or regulatory censure, and negative publicity.	The Group's policies and standards, including our Code of Conduct, mandate that all employees must comply with competition laws in the countries in which we operate. We provide training and guidance to relevant employees detailing the obligations and requirements of competition laws. We employ experienced internal and external lawyers specialising in competition laws to provide advice and guidance regarding interpretation and compliance with competition laws. In the event of any investigation (which may or may not result in actions being brought against us), we cooperate fully with the relevant authority making the investigation and will continue to do so.

VIABILITY STATEMENT

The Board has assessed the prospects of the Company over a longer period than the 12 months required by the going concern requirements of the Code. This longer-term assessment process supports the Board's statements on both viability, as set out below, and going concern, made on page 19.

The Group's annual corporate planning processes include completion of a strategic review, preparation of a three-year business plan and a rolling re-forecast of current year business performance and prospects.

The plans and projections prepared as part of these corporate planning processes consider the Group's cash flows, committed funding and liquidity positions, forecast future funding requirements, banking covenants, and other key financial ratios, including those relevant to maintaining our investment grade ratings.

Where appropriate, sensitivity analysis is undertaken to stress-test the resilience of the Group and its business model to the potential impact of the Group's principal risks, or a combination of those risks. This stress-testing takes account of the availability and effectiveness of the mitigating actions that could realistically be taken to avoid or reduce the impact or occurrence of the underlying risks. In considering the likely effectiveness of such actions, the conclusions of the Board's regular monitoring and review of risk management and internal control systems, as described on page 27, are taken into account.

Whilst the Board has no reason to believe the Group will not be viable over a longer period, the period over which the Board considers it possible to form a reasonable expectation as to the Group's longer-term viability, based on the risk and sensitivity analysis undertaken, is the three-year period to September 2019. This reflects the period used for the Group's business plans and has been selected because, together with the planning process set out above, it gives management and the Board sufficient, realistic visibility on the future in the context of the industry environment. The Board has considered whether it is aware of any specific relevant factors beyond the three-year horizon and confirmed that there are none.

The Board confirms that its assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency and/or liquidity, and which are set out in the Principal Risks and Uncertainties section on pages 28 to 31, was robust.

On the basis of this robust assessment of the principal risks facing the Group, and on the assumption that they are managed or mitigated in the ways disclosed, the Board's review of the business plan and other matters considered and reviewed during the year, and the results of the sensitivity analysis undertaken and described above, the Board has a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to September 2019.



Mark Williamson
Chairman

“Our high social, environmental and ethical standards were integral to another strong performance in 2016.”

This was another year of significant achievement for the Group and I am particularly pleased with the excellent results we have achieved in the USA following last year's acquisition of brands and other assets. Following this increased exposure in the USA we appointed Steven Stanbrook and Therese Esperdy to the Board, both of whom bring extensive international experience, particularly in respect of the USA.

The Board is responsible to shareholders and other stakeholders for the long-term sustainable delivery of our strategy, activities and financial performance; this includes the efficient use of resources and ensuring we operate with high social, environmental and ethical standards.

In this report we provide an overview of our governance framework and, the work of the Board and its Committees which, together with our Code of Conduct (available on our website), set the tone for the way we work, both in respect of relationships between colleagues and with our customers and suppliers.

The standard of behaviour the Board expects from employees worldwide, together with our embedded governance framework, ensure we act with honesty and integrity. The standards of behaviour we require from our employees are often more stringent than those required by local regulations. Our policies and Code of Conduct cover key issues such as acceptable business practices, ethical and legal compliance matters, physical and data security as well as regulatory, governance and occupational health, safety and environmental issues.

More details of our governance framework, including how our sound and effective corporate governance practices support our strategy, are set out in the following sections and in the discussion on effectively managing the risks we face on page 26.

Mark Williamson
Chairman

ENSURING OUR ANNUAL REPORT IS FAIR, BALANCED AND UNDERSTANDABLE

The Audit Committee and the Board review a number of long-established and embedded processes underpinning the compilation and assurance of the Annual Report to consider whether it is fair, balanced and understandable, including:

- reviewing the use of adjusted measures and their appropriateness in aiding users of our financial statements to better understand our performance year on year;
- drafting of the Annual Report by appropriate senior management who monitor regulatory changes and have been formally briefed regarding the fair, balanced and understandable regulations. Overall coordination by the Director of Group Communications to ensure consistency of drafting both across sections of the Annual Report and with other external statements;
- extensive verification processes undertaken to ensure factual accuracy;
- comprehensive reviews of drafts of the Annual Report undertaken by members of the OPEX and other senior management;
- consideration and review of an advanced draft by Internal Audit and the Disclosure Committee;
- the Audit Committee discussing the draft Annual Report with both management and PwC and, where appropriate, challenging the content and any judgements and assumptions used;
- all Audit Committee and Board members receiving drafts of the Annual Report with sufficient time for review and comment prior to the year-end meetings in November 2016; and
- the Audit Committee reviewing the final draft at its meeting in November 2016 on which it was required to express its opinion prior to consideration by the Board.

After consideration of the above processes and review of the Annual Report, the Directors confirm that they consider, taken as a whole, it is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

BOARD OF DIRECTORS



1.

1. Mark Williamson, CA (SA)
Chairman of the Board

Skills and experience

Mark is a qualified accountant, who brings considerable financial and general managerial experience to our Board. Mark was Chief Financial Officer of International Power plc until 2012 and is experienced in managing relationships with the investor and financial communities. Prior to joining International Power plc, Mark was Group Financial Controller and Group Chief Accountant of Simon Group. He is also a former Senior Independent Non-Executive Director and Chairman of the Audit Committee of Alent PLC.

Appointment

Mark joined the Board in July 2007 and was appointed Senior Independent Non-Executive Director in February 2012. He was subsequently appointed Deputy Chairman of the Board in January 2013 before being made Chairman in February 2014.

External appointments

Senior Independent Non-Executive Director and Chairman of the Audit Committee of National Grid plc.

D N Chairman

2. Alison Cooper, BSC, ACA
Chief Executive Officer

Skills and experience

Since being appointed as Chief Executive Alison has led the development and implementation of the Group's sustainable sales growth strategy. Alison joined the Group in 1999 and, through a number of senior roles, has contributed significantly to the international expansion of the Group.

Appointment

Appointed Director in July 2007. Appointed Chief Executive in May 2010.

External appointments

Non-Executive Director, Inchcape plc since July 2009.

E



2.

3. Oliver Tant, BSc, CA (Scotland)
Chief Financial Officer

Skills and experience

Oliver held a number of senior positions in a 32-year career at KPMG, including Global Managing Director Financial Advisory and Private Equity Division and Head of UK Audit.

He was also a member of both the UK and German boards of KPMG. He brings to Imperial international experience in change management, organisational restructuring, corporate finance and mergers and acquisitions.

Appointment

Appointed to the Board of Directors in October 2013 and became Chief Financial Officer in November 2013.

External appointments

No external Director appointments.

E

4. Matthew Phillips, LLB
Chief Development Officer

Skills and experience

Matthew held a number of senior roles prior to his appointment to the Board as Corporate Affairs Director in June 2012 and has been integral to the development and implementation of the Group's strategy.

In his current role he is responsible for Fontem Ventures, corporate development and corporate, legal and regulatory affairs.

Appointment

Appointed Director in June 2012. Appointed Chief Development Officer, June 2015.

External appointments

No external Director appointments.

E



3.

5. Therese Esperdy
Non-Executive Director

Skills and experience

Therese has significant international investment banking experience having held a number of roles at JP Morgan including Global Chairman of JP Morgan's Financial Institutions Group, Co-Head of Asia-Pacific Corporate & Investment Banking, Global Head of Debt Capital Markets, and Head of US Debt Capital Markets. She began her career at Lehman Brothers and joined Chase Securities in 1997 prior to the firm's merger with JP Morgan in 2000.

Appointment

Appointed Non-Executive Director in July 2016

External appointments

Non-Executive Director and Chairman of the Finance Committee of National Grid Plc.

D A N R

6. David Haines
Non-Executive Director

Skills and experience

David brings considerable senior level board experience and was until March 2016 Chairman and Chief Executive Officer of Grohe Group Sàrl and Chief Executive Officer of Lixil Water Technology Group. He joined Grohe in 2004 from Vodafone Group PLC where he was Global Marketing Director. David is Chairman and Co-Founder of Grace Founders Sàrl, a Luxembourg-based investment company. He is also a former Chairman of Vimpelcom A/O.

Appointment

Appointed Non-Executive Director in February 2012, and Chairman of the Remuneration Committee in April 2012.

External appointments

Chairman and Co-Founder of Grace Founders Sàrl.

D A N R Chairman



7.

7. Michael Herlihy, MA (Oxon), Solicitor
Senior Independent Non-Executive Director

Skills and experience

Michael is General Counsel for Smiths Group plc. He was formerly General Counsel and Head of Mergers and Acquisitions for ICI PLC with overall responsibility for corporate acquisitions and divestments and has extensive experience with both private and public market transactions.

Appointment

Appointed Non-Executive Director in July 2007. In February 2014 he was appointed as Senior Independent Non-Executive Director.

External appointments

Serves on the board of Compass Partners International LLP and is currently General Counsel of Smiths Group plc.

DANR

8. Steven Stanbrook

Non-Executive Director

Skills and experience

Steven brings considerable international executive experience to the Board, gained in a number of FMCG companies. This includes 18 years at SC Johnson & Sons Inc., most recently as Chief Operating Officer, where he was responsible for managing their international operations. Previously, he held senior positions at Sara Lee Corporation, including as Chief Executive Officer of Sara Lee Bakery, and at CompuServe Corp. He is also a former Non-Executive Director of Chiquita Brands International, Inc. and Hewitt Associates.

Appointment

Appointed Non-Executive Director in February 2016.

External appointments

Partner of Wind Point Partners and a Director of Autism Speaks.

DANR



8.

9. Karen Witts, FCA
Non-Executive Director

Skills and experience

Karen brings significant financial and management expertise to the Board. She is currently Chief Financial Officer and Executive Director of Kingfisher plc and was previously Chief Financial Officer of the Africa, Middle East, Asia and Asia Pacific Region, at Vodafone plc. Prior to that, Karen held a number of senior positions at BT, including Chief Financial Officer of BT Retail and Managing Director Operations Openreach.

Appointment

Appointed Non-Executive Director in February 2014.

External appointments

Chief Financial Officer and Executive Director of Kingfisher plc.

DANR

10. Malcolm Wyman, CA (SA)

Non-Executive Director

Skills and experience

As a qualified accountant and former Chief Financial Officer of SAB Miller plc, with responsibility for the group's financial operations, corporate finance and development and group strategy, Malcolm brings not only a wealth of financial expertise but also considerable general management experience to the Board. Malcolm is also a former Non-Executive Director and Chairman of the Audit Committee of Serco Group plc.

He also meets the recent and relevant financial experience requirements of the UK Corporate Governance Code.

Appointment

Appointed Non-Executive Director in October 2011 and Chairman of the Audit Committee in February 2012.

External appointments

Senior Independent Non-Executive Director and Chairman of the Audit Committee of Nedbank Group Limited, listed on the Johannesburg Stock Exchange.

DA Chairman NR



9.

11. John Downing, MA, Solicitor
Company Secretary

Skills and experience

John joined Imperial in 2005 having worked for the law firm Linklaters.

He has had a number of senior legal roles in Imperial and was appointed Head of Group Legal in 2010 and played a leading role in the Altadis acquisition. He has considerable experience in managing key corporate projects related to financing, business development and other commercial matters.

Appointment

Appointed Company Secretary in June 2012.

S

Key

E Executive Director

D Non-Executive Director

S Company Secretary

N Succession and Nominations Committee

A Audit Committee

R Remuneration Committee

Skills and experience of our Board

The in-depth tobacco experience of our Executive Directors is complemented by the diverse global experience of our Non-Executive Directors, which includes FMCG, finance, mergers and acquisitions, and sales and marketing.

THE BOARD AND ITS COMMITTEES

BOARD



Mark Williamson
Chairman

“The consistent execution of our strategy continues to create sustainable shareholder returns by maximising sales, cost and cash opportunities.”

Members

Mark Williamson *Chairman*
Ken Burnett (to 3 February 2016)
Alison Cooper
Therese Esperdy (from 1 July 2016)
David Haines
Michael Herlihy
Steven Stanbrook (from 8 February 2016)

Matthew Phillips
Oliver Tant
Karen Witts
Malcolm Wyman
John Downing
Company Secretary

Focus in 2016

- continued integration of the USA business and delivery against our business plan
- investment prioritisation to generate quality growth from key brands and markets and create new opportunities for Fontem
- continued implementation of new ways of working to simplify the business and improve our effectiveness and agility
- further cost savings and capital discipline
- further investment in our people including building capabilities, succession and improving engagement

MATTERS CONSIDERED BY THE BOARD IN 2016

Six principal scheduled Board meetings were held during the year

2015	2016				
Oct	Jan	Mar	Apr	Jun	Sept
– Safety update	– Safety update	– Strategy meeting	– Safety update	– Safety update	– Safety update
– Report and accounts including period covered by viability statement	– First quarter results		– Half-Year Report	– Strategy review, including opportunities for Fontem	– Business performance
– Dividend	– Business performance		– Dividend		– Business plan
– Business performance	– Strategy review		– Business performance	– Business performance	– Corporate development
– Business planning	– AGM		– Corporate development	– Appointment of Therese Esperdy	– Board evaluation
– Corporate development	– Group funding		– Group funding including extension of debt issuance programme		– Chairman and NED fees
– EUTPD update including risks and opportunities	– Operating model		– Overseas visit to Joure factory – insight into operational excellence programme		– Risk update
– Corporate identity including change of name	– EUTPD/ plain packaging update		– ADR ratio change		
	– Appointment of Steven Stanbrook				

Focus for 2017

- continue our investment prioritisation to generate quality growth from key markets and Growth and Specialist Brands
- continue optimising our ways of working supporting our growth agenda
- support our growth agenda by further cost savings and capital discipline
- further develop our employees' capabilities and engender a growth mind-set
- enhance our governance framework to further support our sustainable growth agenda

OVERVIEW

The Directors are collectively responsible and accountable to our shareholders for the long-term sustainable success of the Group. The Board's role is to provide leadership to the Group, set its strategy and oversee its implementation.

The Board has a key role in ensuring that in achieving our strategy management operates responsibly within our governance framework whilst clearly demonstrating our values and high ethical standards. The Directors are also mindful of their legal duties to act in the way they consider, in good faith, will be most likely to promote the success of the Company for its shareholders whilst having regard to the interests of other stakeholders.

As part of the governance framework the Board has adopted a schedule of matters on which it must make the final decision. These include approving the Group's strategy, business plans, dividends and major financial announcements. The Board is also responsible for approving the acquisition or disposal of assets exceeding defined thresholds.

Within this framework the Board delegates responsibility for developing and implementing strategy and for day-to-day management to our Chief Executive, Alison Cooper, who is supported by her fellow Executive Directors and by the Operating Executive (OPEX), which she chairs. The Board also delegates matters to Board Committees. Clearly defined terms of reference and written limits support these delegations.

The OPEX consists of senior executives from across the business. It oversees operational execution and delivers our strategic and financial plans. The OPEX and Audit Committee also ensure that appropriate internal controls, which function effectively, are in place, and effective risk management processes operate throughout the Group.

SUCCESSION AND NOMINATIONS COMMITTEE



Mark Williamson
Chairman

"We have the right people and the right succession plans to deliver our strategy and build on our long track record of generating significant returns to our shareholders."

Members

Mark Williamson
Chairman¹

Ken Burnett (to 3 February 2016)
Therese Esperdy (from 1 July 2016)

David Haines

Michael Herlihy

Steven Stanbrook (from 8 February 2016)

Karen Witts

Malcolm Wyman

John Downing
Company Secretary

1. Unless dealing with the succession of the Chairman.

Executive Directors are invited to attend when appropriate.

Focus in 2016

- ongoing review of skillset and composition of the Board
- continuing business updates and education for NEDs
- Board and senior management succession planning
- appointment of Steven Stanbrook and Therese Esperdy

Focus for 2017

- ongoing Board and senior management succession planning
- review of skillset and composition of the Board's Committees
- continuing business updates and education for NEDs

OVERVIEW

Role

The Committee keeps under review and evaluates the composition of the Board and its Committees to maintain the appropriate balance of skills, knowledge, experience and independence to enable them to function effectively. Succession plans for the NEDs, Executive Directors and Group's senior management, in particular the OPEX, are also kept under review.

The Committee also retains an overview of the development plans for OPEX members together with the wider organisational structure and talent management processes.

The Committee's terms of reference are available on our website.

Boardroom Diversity

As a global business, with our products sold in over 160 countries, diversity generally is an integral part of how we do business.

To maintain the appropriate balance of skills, diversity of knowledge, professional and geographic backgrounds and experience on our Board we look ahead to upcoming retirements to identify potential gaps and appoint individuals who are best suited to fill any vacancy. The Committee is mindful of the Davies Review on gender diversity, however, appointing the best people to our Board is critical to the success of the Company; the search for candidates and any subsequent appointments are, therefore, made purely on merit regardless of gender, race, religion, age or disability. Given our commitment to appointing the best people and ensuring that all employees have an equal chance of developing their careers within the Group, we do not think it is appropriate to set targets for Board appointments.

At the year end, women, including our Chief Executive, made up 30 per cent of our Board, and 22 per cent of our OPEX.



Turn to page 21

for further details on our workforce diversity

DIRECTOR DEVELOPMENT

We are committed to the continuing development of our Directors in order to build on their expertise and develop an ever more detailed understanding of the business and the markets in which we operate.

In addition to the ongoing 'NEDucation' and training discussed on page 45, we held our April 2016 Board meeting in our Joure factory, providing NEDs with insights into our Operational Excellence Programme. They also received updates on projects focused on our world class manufacturing performance and how we are implementing global best practice across our network of factories.

During September 2016 the Board visited the headquarters and facilities of ITG Brands in Greensboro, USA. They received presentations from the USA leadership team in respect of our USA operations, including an update on the brands and assets acquired from Reynolds.

THE BOARD AND ITS COMMITTEES

SUCCESSION AND NOMINATIONS COMMITTEE

CONTINUED

SUCCESSION AND NOMINATIONS COMMITTEE IN 2016

Election and Re-election of Directors

All Directors are appointed by the Board following a rigorous selection process and subsequent recommendation by the Committee.

The performance of each Director is considered as part of the annual Board evaluation process. Following the 2016 evaluation, a review of the independence of each NED, particularly in respect of those who have served six years or more, and consideration of attendance, the Board recommends the re-election of all Directors at our 2017 AGM, with the exception of Michael Herlihy, who having served on the Board for nine years, will be retiring at the AGM.

Board Succession

Following nine years of valuable service Ken Burnett retired at the 2016 AGM. The Committee identified the profile and skillset required for NEDs to support our strategy and instructed Korn/Ferry Whitehead Mann¹ to identify appropriate candidates. Within the Company's policy of appointing the best people, Korn/Ferry Whitehead Mann was requested to give consideration to candidates who, in addition to meeting the profile and skillset, add to the overall diversity of the Board. From the list of strong candidates the Committee identified Steven Stanbrook and Therese Esperdy as best suited to oversee and continue to develop the Group's strategy.

1. Korn/Ferry Whitehead Mann also provides online assessments to our sales function with a total value in the year of £117,500.

Meetings of the Board, Board Committees and AGM

	Board	Succession and Nominations Committee	Audit Committee	Remuneration Committee	Annual General Meeting
Total number of meetings in Financial Year	6	4	4	4	1
Number of meetings attended in Financial Year					
Executive Directors					
Alison Cooper	6/6	–	–	–	1/1
Oliver Tant	6/6	–	–	–	1/1
Matthew Phillips	6/6	–	–	–	1/1
Non-Executive Directors					
Mark Williamson	6/6	4/4	–	–	1/1
Therese Esperdy ²	1/1	1/1	1/1	1/1	–
David Haines ¹	5/6	4/4	4/4	4/4	1/1
Michael Herlihy	6/6	4/4	4/4	4/4	1/1
Steven Stanbrook ³	4/4	3/3	2/2	3/3	–
Karen Witts ¹	6/6	3/4	3/4	3/4	1/1
Malcolm Wyman	6/6	4/4	4/4	4/4	1/1

1. David Haines was unable to attend one Board meeting due to being in hospital, however, he fully considered the papers before the meeting and provided his thoughts and recommendations to the Chairman. Karen Witts was unable to attend a Succession and Nominations Committee, an Audit Committee and a Remuneration Committee meeting held on the same occasion due to a conflict with a Board meeting at Kingfisher, however, she fully considered the papers before the meeting and provided her thoughts and recommendations to the Chairmen of each Committee.

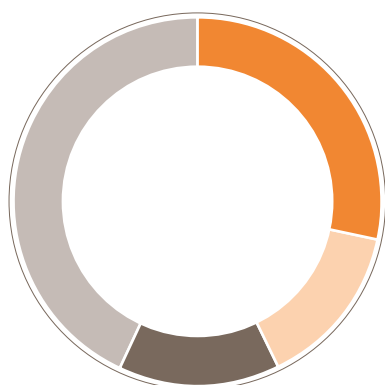
2. Therese Esperdy was appointed to the Board on 1 July 2016.

3. Steven Stanbrook was appointed to the Board on 8 February 2016.

The maximum number of meetings for each individual Director is the number which they were eligible to attend.

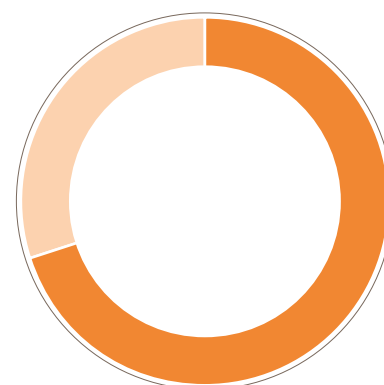
Tenure of Non-Executive Directors

- 8 years and over – 2
- 5 to 7 years – 1
- 3 to 5 years – 1
- 1 to 2 years – 3



Board Gender Balance

- Male – 7
- Female – 3



AUDIT COMMITTEE



Malcolm Wyman
Chairman

"The Committee has a key role in overseeing the Group's internal control, risk management and governance frameworks to enhance the protection of our corporate reputation, people, assets, brands, products and information."

Members¹

Malcolm Wyman ² <i>Chairman</i>	Steven Stanbrook (from 8 February 2016) Karen Witts ²
Ken Burnett (to 3 February 2016)	John Downing
Therese Esperdy (from 1 July 2016)	<i>Company Secretary</i>
David Haines	
Michael Herlihy	

Other regular attendees

Board Chairman	Director of Internal Audit ³
Chief Financial Officer	Deputy Company Secretary
Director of Finance, Planning & Reporting	Representatives from PwC, our external auditors ³
Group Financial Controller	

1. All members are independent Non-Executive Directors.
2. Malcolm Wyman and Karen Witts meet the Code's requirement of having "recent and relevant financial experience".
3. At each meeting, both the Director of Internal Audit and PwC have the opportunity to meet with the Committee without management present.

The Audit Committee report provides insight into the Committee's activities and its deliberations in respect of the 2016 financial year. During the year we continued to focus on the Group's ongoing enhancements to its risk management framework and processes and systems of internal governance and control whilst continuing to ensure the integrity of its financial statements and the quality of both the external and internal audits.

The Committee also reviewed its own performance as part of the overall Board evaluation. This review concluded that the Committee continues to carry out all of its duties effectively.

We meet four times in the year at key times within the Group's reporting cycle, with comprehensive agendas covering all significant matters to be considered by the Committee. I also meet with management on an ad-hoc basis.

Following the FRC's publication of the Revised Ethical Standard in June 2016, the Committee discussed the necessary amendments to ensure that the Group's Auditor Independence policy contained the appropriate tendering and rotation provisions, and appropriate guidance to protect the external auditors' independence. The updated policy details the prohibited non-audit services and establishes rules for hospitality between the external auditors and Group employees, including Directors. We also reviewed the report issued by the FRC's Audit Quality Review Team and the actions proposed to address the limited comments it contained. These actions should further enhance the quality of the audit PricewaterhouseCoopers (PwC) provides.

Another important aspect of our work is to critically review the detailed reports from both internal and external audit. This allows the Committee to fully understand all issues and, if required, instigate appropriate action. I meet with the Director of Internal Audit and the lead Audit Partner of our external auditors, PwC, on a regular basis between Committee meetings.

To assist the Committee in overseeing the effectiveness of controls and risk management across the business, and to assist in addressing the key matters detailed on pages 40 and 41, management prepared and presented to the Committee a wide range of papers, which provided sufficient information on each matter to facilitate discussions and enable effective decisions to be taken.

I am satisfied our activities provided the Committee with a good understanding of the key matters impacting the Group during the year and, in conjunction with its oversight of the governance and operation of the Group's significant controls and processes, enabled the Committee to draw the conclusions set out on page 41.

Malcolm Wyman
Chairman of the Audit Committee

THE BOARD AND ITS COMMITTEES

AUDIT COMMITTEE

CONTINUED

Main Objective

To assist the Board in fulfilling its corporate governance responsibilities relating to the Group's financial statements, internal control systems, risk management process and framework, the internal audit function and the external audit. During the year the Committee achieved this by:

- ensuring the integrity of our financial statements and related announcements, and assisting the Board in confirming that, taken as a whole, our Annual Report is fair, balanced and understandable, and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy (see page 33);
- monitoring and evaluating the effectiveness of our risk management and internal control systems and speaking-up process;

- maintaining appropriate oversight over the work and effectiveness of the Internal Audit department, including reviewing its audit findings and monitoring management's responses;
- scrutinising the independence, objectivity and effectiveness of PwC, including reviewing and approving the annual external audit plan, reviewing the audit findings, monitoring compliance with ethical and professional guidance and approving PwC's terms of engagement. We also reviewed and approved the Group's revised Auditor Independence policy; and
- throughout the year, considering the key matters detailed below, including taking account of PwC's views.

The Committee's terms of reference are available on our website.

AUDIT COMMITTEE MEETINGS HELD IN RESPECT OF THE 2016 FINANCIAL YEAR

Four Committee meetings were held in respect of the 2016 financial year at key times within our reporting and audit calendar and included the following matters on the agenda:

2016

Jan	Apr	Sept	Nov
– Audit planning	– Half-Year Report	– Impairment considerations	– Annual Report and Accounts
– Internal Audit and Risk Management review	– Goodwill and impairment review	– Taxation	– Goodwill and impairment review
– External auditors' effectiveness	– External auditors' report	– Internal Audit and Risk Management review	– Use of adjusted measures
– Governance and internal control	– Tax report	– External auditors' fees and independence	– FX management
– Impairment considerations	– External auditors' fees and independence	– External auditors' report and independence	– Viability and going concern statements
– Distributable reserves	– Internal Audit and Risk Management review, including consideration of cyber risk	– Viability and going concern	– External auditors' report
– Restructuring accounting policy	– Internal Audit and Risk Management review, including consideration of cyber risk	– Governance and internal control	– Internal Audit and Risk Management review
– Tax matters	– Governance and internal control	– FX management	– External auditors' fees, independence and reappointment
– Audit tendering	– Tobacco related litigation	– Distributable reserves	– Governance and internal control
		– Restructuring costs	– Tobacco related litigation
		– Treasury update	– Retirement benefits
		– Consideration of FRC's Audit Quality Review Team review	– Revenue recognition
		– Review of terms of reference	

KEY MATTERS CONSIDERED

The Committee considered the appropriateness of the following areas of significant judgement, complexity or estimation in connection with the financial statements, as set out below:

Focus area	Why this area is significant	How we as a Committee addressed this area
1 Goodwill and intangible asset impairment reviews See note 11 of the financial statements for further information.	Goodwill and intangible assets form a major part of the Group's balance sheet and their current valuations must be supported by future prospects.	We regularly received and considered detailed reports from management and challenged the methodology applied, the achievability of underlying business forecasts, and macro-economic assumptions used. For the groupings of cash generating units with the lowest headroom (Growth Division and Other Premium Cigars), we examined different scenarios and sensitivities to assess whether management's conclusions were fair and balanced. The Committee also considered detailed reporting from, and held discussions with PwC. Resulting from the above, we concluded that management's assertion that goodwill and intangible assets were not impaired was reasonable and, therefore, approved the disclosures in our financial statements and half year results.
2 Use of adjusted measures See note 1 for further information.	Non-GAAP or adjusted measures provide an appropriate and useful assessment of business performance and reflect the way in which the business is managed. They are also used in determining annual and long-term incentives for remuneration, and are widely used by our investors.	The Committee considered whether adjusted performance measures had been prepared in accordance with our policy on the use of adjusted measures set out in Note 1 to the financial statements, and discussed this with PwC. We concluded that the Group's policy continues to be applied consistently and is compatible with the ESMA guidelines on alternative performance measures. In its review of the Annual Report, the Committee has also taken account of the FRC's comments on the use of adjusted measures in its Annual Review of Corporate Reporting 2015/2016.

	Focus area	Why this area is significant	How we as a Committee addressed this area
3	Treatment of restructuring costs See note 5 for further information.	Restructuring costs is one of the main items affecting our adjusted measures. There is a risk that restructuring costs are treated or presented inappropriately within the Group's financial statements.	We periodically reviewed papers from management on actual and forecast levels of restructuring costs. The restructuring costs disclosure for inclusion within the Group's financial statements and Half-Year results were also reviewed and discussed with management and PwC. Following these detailed reviews and discussions, we concluded that determination of restructuring costs was consistently applied and that, notwithstanding the duration of some restructuring projects, costs were disclosed appropriately.
4	Going concern and viability statement See page 32 for further information.	The Directors are required to consider whether it is appropriate to prepare the financial statements on a going concern basis and explain how they have assessed the prospects of the Company over a longer period.	We examined the Group's committed funding, its ability to generate cash and its ability to raise further funding. We challenged management's cash projections and sensitivity analysis including mitigating actions. In addition, in assessing the Group's longer-term viability we considered outputs of the annual corporate planning processes including the strategic review, a three-year business plan and a rolling re-forecast of current year business performance and prospects. We also considered the resilience of the Group to the potential impact of the Group's principal risks and mitigating actions. We reviewed the period covered by the statement and concluded that three years remains the most appropriate period, being that used by the Group for its business plan. We concluded that it was appropriate to prepare the financial statements on a going concern basis and that the Board has a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to September 2019.
5	Revenue recognition See note 1 for further information.	In common with all companies, there is a risk that arrangements could be made to recognise sales that do not meet revenue recognition criteria.	Discussions were held with management and PwC and the Committee was satisfied that the Group's criteria for revenue recognition were appropriate. No breaches of the Group's revenue recognition policy were brought to the Committee's attention.
6	Taxation See notes 8 and 21 for further information.	The Group is subject to taxation in a number of jurisdictions, and significant judgement is required in relation to taxation provisions which could materially affect the Group's reported results.	We received and discussed reports from management in respect of the taxation affairs of the Group, including the tax audit in France and the potential impact on the Group of various UK and foreign taxation reform proposals. Additional tax disclosures have been included in the financial statements to provide more clarity of the basis of tax provisioning. Following consideration and discussion of management's reports and a review of reports provided by PwC, we are satisfied that the taxation provisions and their disclosure are appropriate.
7	Tobacco-related litigation See page 49 for further information.	The Group is exposed to litigation arising from claimants alleging smoking-related health effects.	We considered reports from the Group's external lawyers which confirmed that the Group continues to have meritorious defences to the actual and threatened legal proceedings and concluded that risks in respect of tobacco-related litigation are appropriately disclosed in the Annual Report and Accounts.

RISK MANAGEMENT AND INTERNAL CONTROL

The Group's risk management approach has further evolved in the year, to manage risks arising from the changing legal, regulatory, macro-economic and commercial environments in which the Group operates. The continuation of the programme to further embed risk management within our operations is enabling greater consistency in the identification, assessment and mitigation of risks at both a local and Group level.

The Committee received regular updates during the year on the continued development and implementation of the risk management framework and on the risk management systems and processes operating within the Group. Additionally, the Committee has reviewed the process for identification, assessment and reporting of the Company's principal risks set out on pages 28 to 31. The Committee has also considered and confirmed to the Board that this work is in accordance with the provisions in the 2014 UK Corporate Governance Code and the Financial Reporting Council's

(FRC) associated Guidance on Risk Management, Internal Control and Related Financial and Business Reporting.

Assurance over compliance with Group risk management policies, standards and requirements is achieved through the work of our Internal Audit department and the execution of the Audit Committee approved annual plan of reviews to be completed. Issues arising from these reviews are reported to the Committee, along with updates on the timely resolution of all issues raised in Internal Audit reports.

The Group continues to evaluate the changing risks to its information security, and has engaged subject matter experts to develop its approach to monitoring, evaluation and mitigation of the key causes of the risk. Our people have been provided with training and guidance to enable effective operational management of risks, with independent assurance of compliance to Group requirements provided by the risk-based reviews completed as part of the Internal Audit plan.

THE BOARD AND ITS COMMITTEES

AUDIT COMMITTEE

CONTINUED

The above processes and those described in the Risk Management section on pages 26 to 27 enable the Board, either directly or through the Audit Committee, to review regularly the effectiveness of the key procedures which have been established in order to provide appropriate internal controls. They also enable the Board to confirm that an ongoing process for identifying, evaluating and managing the Group's principal risks has operated throughout the year and up to the date of approval of the Annual Report and Accounts.

INTERNAL AUDIT

Internal Audit (IA) has continued to evolve and develop its practices in order to continually improve the independent challenge to the Group's activities, required by the Audit Committee and management. During the year all legacy internal auditing and assurance activities performed across the Group have been brought under the IA function. In addition, the internal audit of our new USA subsidiary, ITG Brands, has been integrated within Group IA. IA continues to perform a risk based audit programme aligned to the Group's strategic priorities.

The Audit Committee reviews the annual IA plan, including its scope and extent, and reviews reports from IA at each quarterly Audit Committee meeting to monitor the function's achievements against plan. The Audit Committee considered the results of the audits undertaken by IA and monitored management responses to the audit matters raised. IA satisfaction surveys are completed by relevant management following each audit and feedback on IA performance during the year has been positive.

IA conducted a self-assessment of effectiveness against the best practice standards of both the Institute of Internal Auditors (IIA) and the Institute of Chartered Accountants of England and Wales (ICAEW). Whilst highlighting some areas for continual improvement the self-assessment reflected an improving level of IA performance.

EXTERNAL AUDIT

During the year, the Audit Committee reviewed the external audit strategy including the key issues to be addressed. The Committee reviewed PwC's proposed audit approach, scope and materiality thresholds for the Half-Year Report and for the audit of the consolidated financial statements for the year ended 30 September 2016.

The Committee noted that PwC's identified significant audit risks were similar to previous years, but with acquisition accounting moved back to a normal level of risk following the completion of the USA acquisition in 2015.

The Audit Engagement Letter detailing the revised agreement for the provision of statutory audit and half year review services was considered and approved.

INDEPENDENCE OF OUR EXTERNAL AUDITORS

In order to ensure the independence and objectivity of PwC, the Committee maintains and regularly reviews our Auditor Independence policy. This policy provides clear definitions of services that our external auditors may and may not provide and can be found on our website. Following the FRC's publication of the Revised Ethical Standard in June 2016 the policy was updated to embed audit tendering and rotations requirements, further extend the list of prohibited services and prohibit gifts and hospitality by or to the auditors. The updated policy has been applied from 1 October 2016.

PwC, and its predecessor firms, has been the Company's auditors since 1996. In line with our Auditor Independence policy, the Group Audit Partner is required to rotate after a maximum of five years (seven years for subsidiary companies). John Maitland, our Audit Partner, has been in post since 2013.

PwC may only provide non-audit services where those services do not conflict with its independence. The policy establishes a formal authorisation process, including the tendering for individual non-audit services expected to generate fees in excess of £250,000, and pre-approval by the Committee for allowable non-audit work that they may perform. Guidelines for the recruitment of employees or former employees of PwC, and for the recruitment of our employees by PwC, are contained in the policy.

During the year PwC undertook non-audit work. This non-audit work was awarded to PwC due to its knowledge of the Group and it being deemed best placed to provide effectively the services required.

This non-audit work included:

- tax advisory and tax compliance work
- verification of our corporate social responsibility reporting and underlying processes
- agreed upon processes in respect of the performance criteria of our employee share plans

In the current year non-audit fees were 37 per cent (2015: 87 per cent) of total audit fees (see note 4 on page 92). The 2015 ratio was significantly impacted by the work undertaken in connection with the USA cigarette brands and e-cigarette acquisition. The Committee considers that the level of non-audit fees is appropriate in the light of the above activities, and is comparable with those disclosed by similar companies with international activities, and does not believe that the objectivity of the external audit has been impaired as a result of this non-audit work.

To ensure compliance with this policy, during the year the Committee carried out two auditor independence reviews including consideration of the remuneration received by PwC for audit services, audit-related services and non-audit work. The Committee also considered reports by both management and PwC which did not raise any concerns in respect of PwC's independence and confirmed that PwC maintains appropriate internal safeguards to ensure its independence and objectivity. The outcome of these reviews was that performance of the relevant non-audit work by PwC was in compliance with the policy and was the most cost-effective way of conducting our business. No conflicts of interest were found to exist between such audit and non-audit work. The Committee, therefore, confirmed that the Company and Group continue to receive an independent audit service.

AUDIT QUALITY

We place great importance on ensuring that we receive a high standard and effective external audit. To assist the Committee to assess the performance of our external auditors, during the year audit effectiveness questionnaires, covering the audit scope and planning, quality and delivery, challenge and communication and independence, were completed by members of both the Committee and Logista's Audit Committee as well as by senior managers and finance executives from across the Group. Responses indicated that, as with previous reviews, there was a consistently high perception of auditor effectiveness, with no pervasive Group-wide concerns identified.

The FRC's Audit Quality Review Team (AQRT) issued its report on PwC's audit of the Group for FY15. The Committee reviewed the findings and discussed them with PwC, and matters raised were included in the planning for the year-end audit.

Based on its consideration of the responses, together with its own ongoing assessment, for example through the quality of PwC's reports to the Committee and its interaction with the Group Audit Partner, and taking into account the AQRT inspection report, the Committee remains satisfied with the efficiency and effectiveness of the audit.

APPROACH TO AUDIT TENDER

Following the introduction of the audit tendering provisions in the Code, the Committee annually considers if the audit should be put out to tender. The result of this year's review was not to put the audit out to tender. The audit has not been put to tender since PwC were appointed as the Company's auditors in 1996.

The Committee has determined that, subject to its annual reviews, the likely timing of the audit tender will be in the year ending 30 September 2021 so that the incoming external audit firm can take up the role for the year ending 30 September 2023.

The Committee believes that this timeframe for the audit tender is in the best interests of the Company and its members given the ongoing medium-term projects involving significant changes to the Group's operating model including the migration to finance shared services.

We believe it is in the interest of both the Group and its stakeholders to ensure that the pool of major accountancy firms with the capacity to be appointed as external auditor is maximised. As part of our tender planning we have, therefore, established a number of processes including the pre-approval of any future services by appropriate accountancy firms to maintain an adequate level of independence to allow them to tender. During the auditor independence reviews detailed above, we also considered the remuneration for audit services, audit-related services and non-audit work undertaken by such accountancy firms.

There are no contractual or similar obligations restricting the Group's choice of external auditors.

The Company confirms that it has complied with the provisions of the Competition and Market Authority's Order for the financial year under review.

STATEMENT OF AUDITORS' RESPONSIBILITIES

PwC is responsible for forming an independent opinion on the financial statements of the Group as a whole and on the financial statements of Imperial Brands PLC as presented by the Directors. In addition, it also reports on other elements of the Annual Report as required by legislation or regulation and reports its opinion to members.



Turn to pages 75 and 120
for further details on PwC's opinions

AUDITORS AND DISCLOSURE OF INFORMATION TO AUDITORS

Each of the Directors in office at the date of approval of this Annual Report confirms that:

- so far as they are aware, there is no relevant audit information (that is, information needed by PwC in connection with preparing its report) of which PwC is unaware; and
- each has taken all the steps that they ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish PwC is aware of that information.

The Board accepted, at its November 2016 meeting, the Committee's recommendation to put to shareholders at the forthcoming AGM a resolution to reappoint PwC as auditors to the Company.

DIRECTORS' REPORT

APPLICATION OF THE UK CORPORATE GOVERNANCE CODE

The latest revision of the UK Corporate Governance Code (the Code) was published by the FRC in September 2014, together with Guidance on Risk Management, Internal Control and Related Financial and Business Reporting.

We are pleased to confirm that the Company has complied in full with the Code throughout this financial year. The Company has not, however, tendered for audit services in the last ten years.

We detail below how, in practice, the Company has applied the Code's principles and complied with its detailed provisions.

THE BOARD AND ITS COMMITTEES

Each of our Board Committees has specific written terms of reference issued by the Board and adopted by the relevant Committee. All Committee chairmen report on the proceedings of their Committee at the next meeting of the Board and, where appropriate, make recommendations to the Board. In addition, minutes of all Committee meetings are circulated to Board members.

To ensure Directors are kept up-to-date on developing issues and to enhance the overall effectiveness of the Board and its Committees, our Chairman and Committee chairmen communicate regularly with the Chief Executive and other Executive Directors.

Our NEDs play a key role in corporate accountability and governance through their membership of the Board's Committees. The membership and remit of each Committee are considered on pages 37 to 39 and 51. The open atmosphere at our Committee meetings enables our NEDs to use their judgement, experience and independence to review critically and, where appropriate, challenge constructively strategies proposed by management. This ensures the further development of our business, effective use of our resources and maintenance of our high standards of conduct.

Matters Reserved for the Board

In order to retain control of key decisions the Board has adopted a schedule of matters on which it must make the final decision, including approval of the Group and parent company financial statements, the Group's business strategy, the annual capital expenditure plan, major capital projects, major changes to the Group's management and control structure, material investments or disposals, risk management strategy, sustainability and environmental policies, the appointment or removal of Directors and the Company Secretary and treasury policies.

Division of Responsibilities of our Chairman and Chief Executive

Whilst retaining a close working relationship, our Chairman and Chief Executive have clearly defined and separate responsibilities divided between running the Board and the business. They speak regularly between Board meetings to ensure a full understanding of evolving issues and to facilitate swift decision making. They are responsible to our shareholders for the successful delivery of our strategy.

Board composition and roles

Chairman	Mark Williamson	Leads the Board and creates an environment that ensures there are strong links between the Board and our shareholders and management. Mark met the independence criteria of the Code on appointment and there have been no significant changes to his external commitments subsequent to his appointment.
Chief Executive	Alison Cooper	Supported by the Executive Directors and the OPEX, has day-to-day management responsibility for the Group, for recommending the Group's strategy to the Board and, once agreed, its implementation. Alison and the Executive Directors actively promote the Group's values, culture and high standards of conduct and behaviour which underpin our reputation and support the delivery of our sustainable sales growth.
Executive Directors	Oliver Tant Matthew Phillips	Support the Chief Executive in devising and implementing our strategy and overseeing the operations and development of the entire Group, in addition to specific responsibility for managing their own areas of the business.
Senior Independent Director	Michael Herlihy	Responsible for assisting the Chairman with effective shareholder communication and is available to them should they have any concerns which have not been resolved through the normal channels or if these channels are not appropriate. No such concerns were raised during the year. Michael is available to our NEDs should they have any concerns which are not appropriate to raise with the Chairman or which have not been satisfactorily resolved by the Chairman. He also acts as a sounding board for the Chairman and carries out the Chairman's performance evaluation.
Non-Executive Directors	Therese Esperdy David Haines Steven Stanbrook Karen Witts Malcolm Wyman	Evaluate information provided and challenge constructively management's viewpoints, assumptions and performance. They bring to the Board a diverse range of business and financial expertise which complements and supplements the experiences of the Executive Directors.

Conflicts of Interest and Independence

Directors are required to avoid situations where they have, or could have, a direct or indirect interest that conflicts, or possibly may conflict, with the Company's interests. In accordance with the Companies Act 2006 (the Act), our Articles of Association allow the Board to authorise potential conflicts of interest that may arise and to impose such limits or conditions as it thinks fit.

Directors are required to give notice of any potential situational and/or transactional conflicts, which are considered at the following Board meeting and, if appropriate, situational conflicts are authorised. We do not allow any Director to participate in such considerations or to vote regarding their own conflicts.

The Board has considered and authorised a number of situations all of which relate to the holding of external directorships and have been entered in our Conflicts Register. No actual conflicts have been identified. The Board considers that these procedures operate effectively.

As part of our annual review process, during the Board meeting in September 2016 we reviewed and reconsidered all situations entered in the Conflicts Register and the Board is satisfied that the independence of those Directors who have external board appointments has not been compromised. At this meeting, and taking into account the annual Board performance evaluation discussed below, the Board concluded that all our NEDs continue to contribute effectively and constructively to Board debate, demonstrate commitment to their role, challenge objectively and question management robustly and at all times have the best interests of our shareholders in mind. We confirm, therefore, that, with the exception of our Chairman who met the independence criteria of the Code on appointment, our NEDs remained independent throughout the year as defined in the Code.

External Appointments

NEDs, including the Chairman, may serve on a number of other boards provided they continue to demonstrate the requisite commitment to discharge effectively their duties. The Succession and Nominations Committee reviews the extent of the NEDs' other interests throughout the year. The Board is satisfied that each of the NEDs commits sufficient time to their duties in relation to the Company. Each of the NEDs has confirmed they have sufficient time to fulfil their obligations to the Company.

The Board is supportive of Executive Directors and members of the OPEX accepting non-executive directorships of other companies in order to widen their experience and knowledge for the benefit of the Company. Accordingly, subject to the agreement of the Board, Executive Directors and members of the OPEX are permitted to accept one external non-executive board appointment and to retain any fees received from such appointment.

Information and Training

Following their appointment to the Board, Directors are briefed on the legal and other duties they owe to the Company. Tailored induction programmes are arranged which include industry-specific training, visits to the Group's businesses and meetings with senior management. They are also briefed on internal controls at both head office and business unit level and provided with information on relevant Company policies and governance related matters.

Through its 'NEDucation' programme the Company is also committed to the continuing development of its NEDs in order that they may build on their expertise and develop their understanding of the business and the markets in which we operate.

Through this programme ongoing training is available to NEDs to meet their individual needs. We also provide regular briefings to all Directors on matters such as legislation and regulation changes and corporate governance developments. Members of our Audit and Remuneration

Committees also received briefings from PwC and New Bridge Street respectively. No specific training needs were identified in 2016.

To enable them to discharge their responsibilities, the Board and its Committees are supplied with full and timely information, including detailed financial information.

The Company Secretary is responsible for advising the Board, through the Chairman, on matters of corporate governance. In addition, all Directors have access to the advice of the Company Secretary and, where appropriate, the services of other employees for all governance and regulatory matters.

Independent professional advice is available to Directors, in appropriate circumstances, at the Company's expense.

Performance Evaluation

To enhance the effectiveness of the Board, during the year it undertook an in-house review of its performance, that of its Committees and of individual Directors.

This review considered the overall functioning of the Board and its Committees, the balance and range of Directors' skills, diversity, succession planning and how the Board works as a unit.

As part of the evaluation, the Chairman held meetings with the NEDs to consider, amongst other things, the performance of the Executive Directors.

The Senior Independent Director also held separate meetings with individual Board members and the Board as a whole, both without the Chairman present, to consider the performance of the Chairman.

The feedback obtained was collated into a report which was presented to the Succession and Nominations Committee and the Board at their September 2016 meetings and helped inform the one-to-one development discussions between the Chairman and each Director.

The evaluation showed that the Board and its Committees continue to function and perform effectively and neither significant areas for concern nor any requirement to provide extra training for our Directors were identified. The evaluation confirmed that all our Directors have sufficient time, knowledge and commitment to contribute effectively to our Board and its Committees and that they remain appropriately constituted.

Areas identified for further consideration were continued focus on succession, further discussion on the changing/emerging risks facing the Group and ensuring the use of the Board's time is optimised to ensure it focuses on where it can add the most value and make the best use of the NEDs' diverse skill set.

The Board intends to undertake an externally facilitated evaluation during 2017.

How we addressed the areas raised for consideration in the 2015 evaluation:

Area for consideration	How we addressed this area
Potentially increasing the number of NEDs on the Board	Steven Stanbrook and Therese Esperdy appointed to the Board
Increasing the NEDs' understanding of the Group's priorities within its divisions	Business planning sessions and enhanced performance and strategy presentations
Ensuring the Board has adequate time to consider appropriately all matters requiring its attention	Agendas planned to ensure Board's time focused on matters requiring its attention and an extra Board meeting held

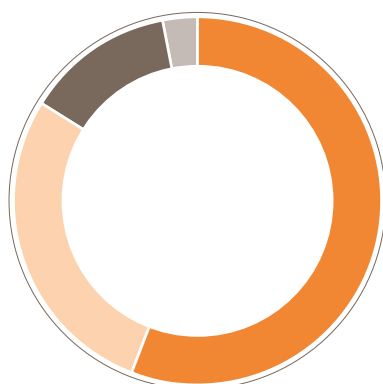
Insurance and Indemnities

We have purchased and maintain appropriate insurance cover in respect of directors' and officers' liabilities. The Company has also entered into qualifying third party indemnity arrangements for the benefit of all its Directors in a form and scope which comply with the requirements of the Act. These indemnities were in force throughout the year and up to the date of this Annual Report.

DIALOGUE WITH OUR INVESTORS

Geographical Analysis of Shareholders (as at 30 September 2016)

- UK – 56%
- USA – 28%
- Rest of Europe – 13%
- Rest of the World – 3%



We aim to provide balanced, clear and transparent communications which allow shareholders to understand how we see our prospects and the market environments in which we operate.

We maintain an active engagement with our key financial audiences, including institutional shareholders, debt stakeholders and sell-side analysts as well as potential shareholders. During the year we made regular presentations to, and had meetings with, institutional investors in the UK, Europe, Canada and the USA to communicate progress towards achieving our sales growth strategy and to answer questions. Throughout the year our senior management team presented at industry conferences organised by investor bodies and investment banks for their institutional investor bases. Our Investor Relations team managed the interaction with these audiences and provided additional regular presentations during the year.

We hosted an investor day in June 2016 at our head office which provided further details on the Group's strategy, operations and value creation opportunities. The day comprised presentations by the Chief Executive and other members of the senior management team, and focused on three themes: quality, agility and discipline. Quality – We continue to improve the quality of growth through our portfolio simplification programme and optimising our investment choices in brands and markets. Agility – Reducing complexity and streamlining the way we manage our brands and markets, combined with the changes we are making to our operating model, is creating a stronger, more agile and efficient organisation. Discipline – We maintain a disciplined approach to resource allocation and the efficient management of our cost and capital base. This underpins the effective deployment of cash to reinvest in the business, pay down debt and deliver returns to shareholders.

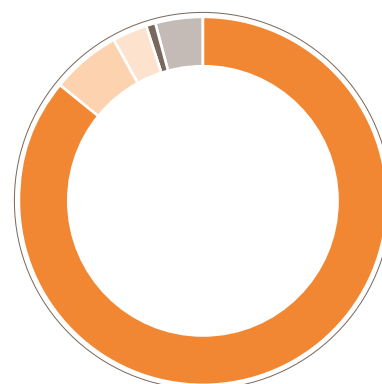
The primary means of communication with the majority of our shareholders is via our Annual Report and Accounts, Half-Year Report and website. These were supported by a combination of presentations, conference calls, one-to-one and group investor meetings.

NEDs, including our Senior Independent Director, were available throughout the year to meet with major shareholders if requested and are kept up-to-date with investor opinion.

We offer our shareholders the choice of submitting proxy votes, including abstentions, either electronically or in paper format and ensure our Annual Report and Accounts and Notice of the AGM are made available at least 20 working days prior to the meeting to allow shareholders time to consider them fully before submitting their proxy votes.

Shareholder Composition (as at 30 September 2016)

- Institutional – 86%
- Non-institutional – 6%
- Retail – 3%
- Employees – 1%
- Miscellaneous – 4%



At the AGM our Chairman and Chief Executive give presentations on our performance and current business activities and all Directors make themselves available to meet shareholders after the conclusion of the formal business of the AGM.

To ensure compliance with the Code, at all general meetings separate resolutions are proposed on each subject and all resolutions are put to a poll. At the AGM the number of proxy votes for, against and abstentions for each resolution are provided. Votes received at the AGM are added to the proxy votes and the final results published through a Regulatory Information Service, on our website and via OTCQX.

At our 2016 AGM we received votes representing approximately 78 per cent of our issued share capital (excluding shares held in treasury at the date of the meeting).

Our next AGM will be held on Wednesday 1 February 2017, full details of which are contained in the Notice of Meeting available on our website and, where applicable, posted with this Report.

OTHER INFORMATION – INTRODUCTION

One of the Board's primary responsibilities is to ensure the Company is run in the best long-term interests of its shareholders and wider stakeholders. We believe this can only be achieved if the activities of the Group are supported by appropriate governance processes applied across the Group.

These processes are illustrated below and in the individual Committee reports.

In accordance with the UK Companies Act 2006 (the Act) the following items have been included in other sections of this Annual Report:

- a fair review of the business, as required by the Act, is included in the Strategic Report. The information in our Governance Report is included in this Directors' Report by reference;
- future developments in the business are included in the Chief Executive's Statement;
- information relating to our people is included in the Rewarding Workplace section;
- our principal risks are detailed on pages 28 to 31; and
- the Directors of the Company during the financial year are listed on pages 34 and 35.

SHARE CAPITAL

Details of our share capital are shown in note 24 to the financial statements. All shares other than those held in treasury are freely transferable and rank *pari passu* for voting and dividend rights.

At our AGM on 3 February 2016 shareholder authority for the buyback of up to 95,709,000 shares was obtained.

As at 30 September 2016 we held 77,289,137 shares in treasury, which represented 7.46 per cent of issued share capital and had an aggregate nominal value of £7,728,914.

We have not cancelled these shares but hold them in a treasury shares reserve within our profit and loss account reserve and they represent a deduction from equity shareholders' funds.

At 30 September 2016 we had been notified of the following interests in 3 per cent or more of our shares and there have been no changes to this information up to the date of this Annual Report.

	Number of ordinary shares (millions)	Percentage of issued share capital
BlackRock Inc.	53	5.59 ¹
Capital Group Companies Inc.	48	5.00 ¹
Invesco Limited	47	4.94 ²
Morgan Stanley Investment Management Limited	42	4.44 ²
Franklin Resources Inc.	41	4.30 ¹

1. Indirect holding.

2. Direct holding.

We have not received notification that any other person holds 3 per cent or more of our shares.

The share interests of the Directors, their families and any connected persons are shown on page 67. Other than as disclosed on page 59, there are no agreements between the Company and its Directors or employees providing for compensation for loss of office or employment due to a takeover.

Information concerning employees and their remuneration is given in note 6 to the financial statements and in the Directors' Remuneration Report.

FINANCIAL RESULTS AND DIVIDENDS

We include a review of our operational and financial performance, current position and future developments in our Strategic Report: Strategy, Risks, Performance and Governance sections.

The profit attributable to equity holders of the Company for the financial year was 631 million, as shown in our Consolidated Income Statement. Note 3 to the financial statements gives an analysis of revenue and operating profit.

An analysis of net assets is provided in the Consolidated Balance Sheet and the related notes to the financial statements.

We pay quarterly dividends. The first and second dividends for financial year 2016 were paid on 30 June 2016 and 30 September 2016 respectively. The third dividend will be paid on 30 December 2016 and, subject to AGM approval, the final dividend will be paid on 31 March 2017 to our shareholders on the Register of Members at the close of business on 17 February 2017. The associated ex-dividend date will be 16 February 2017.

The Directors have declared and proposed dividends as follows:

£ million	2016	2015
Ordinary Shares		
Interim paid – June 2016, 23.5p per share	225	204
Interim paid – September 2016, 23.5p per share	225	204
Proposed interim – December 2016, 54.1p per share	516	468
Proposed final – March 2017, 54.1p per share	516	468
Total ordinary dividends, 155.2p per share (2015: 141.0p)	1,482	1,344

RELATIONS WITH OTHER STAKEHOLDERS

Charitable and Political Donations

As part of our responsible approach and commitment to reinvesting in society, we continued to support a number of communities in which we operate by allocating a central budget of £3.06 million (2015: £2.55 million) to partnership and community investments, in addition to in-kind activities including management time, volunteering, gifts in-kind and localised activities. The central budget was greater than in 2015, as a number of scheduled partner payments from the previous year were made during this financial year. Although difficult to quantify in monetary terms, our in-kind activities also increased in 2016 with the second year of our global volunteering initiative, which achieved some 55,000 hours of employees' time in support of charitable activities.

Through the UK Charities Aid Foundation we apportioned £1.86 million to registered charities, supporting the Eliminating Child Labour in Tobacco Growing Foundation, our Altadis Foundation and a small number of UK charities.

We also apportioned £1.2 million to our leaf sustainability partnerships which seek to help rural tobacco growing communities, predominantly in sub-Saharan Africa. In addition to our central budget our local entities donated some £0.45 million to charitable and community endeavours.

More information on our approach to supporting community livelihoods can be found on our website.

All charitable donations and partnership investments are subject to the requirements of our Code of Conduct.

No political donations were made to EU political parties, organisations or candidates (2015: Nil). This approach is aligned with our Group Policy and Code of Conduct.

Pension Fund

Our main pension fund, the Imperial Tobacco Pension Fund, is not controlled by the Board but by a trustee company, the board of which consists of five directors nominated by the Company, one director nominated by employee members and two nominated by current and deferred pensioners. This trustee company looks after the assets of the pension fund, which are held separately from those of the Group and are managed by independent fund managers. The pension fund assets can only be used in accordance with the fund's rules and for no other purpose.



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Further details are contained in our Remuneration Report.

Articles of Association

The Company's Articles of Association do not contain any entrenchment provisions and, therefore, may be altered or added to or completely new articles may be adopted by special resolution subject to the provisions of the Companies Act 2006.

Significant Agreements That Take Effect, Alter or Terminate on Change of Control

The agreements summarised below are those which we consider to be significant to the Group as a whole and which contain provisions giving the other party a specific right to terminate them if we are subject to a change of control following a takeover bid.

The Group has ten credit facility agreements that provide that, unless the lenders otherwise agree, if any person or group of associated persons acquires the right to exercise more than 50 per cent of the votes at a general meeting of the Company, the respective borrowers must repay any outstanding utilisation made by them under the respective facility agreement and the total commitments under that facility agreement will be cancelled.

The ten credit agreements are:

- a credit facilities agreement dated 15 July 2014 under which certain banks and financial institutions make available to Imperial Brands Finance PLC and Imperial Brands Enterprise Finance Limited: (a) committed acquisition credit facilities originally across three tranches of \$4,100 million, \$1,500 million and \$1,500 million, for a maximum period of up to three years, four years and six years respectively; (b) committed credit facilities originally of €1,000 million for a period of up to three years; and (c) committed credit facilities in two tranches of €2,835 million and €500 million for a period of five years. The Group has subsequently either repaid, cancelled or extended certain of these facilities, such that as at 30 September 2016 the following remained outstanding: \$900 million acquisition credit facilities until 12 June 2018, and committed credit facilities of, respectively, €350 million until 15 July 2017, €2,835 million until 15 July 2021 and €500 million until 15 July 2021;
- eight deeds of counter-indemnity each dated 3 June 2014 made on substantially the same terms under which certain insurance companies and financial institutions each make available to Imperial Tobacco Limited a surety bond, in each case issued on a standalone basis but in aggregate forming an amount of £400 million, until 3 December 2019; and
- a credit facility agreement dated 9 June 2015 in which Bank of America Merrill Lynch Limited makes available to Imperial Brands Finance PLC and Imperial Brands Enterprise Finance Limited a committed credit facility of \$300 million for a maximum period of up to five years.

In the event that any of the listed credit facility agreements are subject to any such repayment and cancellation, we would expect to replace these agreements with similar arrangements in order to satisfy the Group's existing funding commitments, ongoing working capital and similar requirements, as well as its long-term and strategic plans.

Imperial Brands Finance PLC (the Issuer) has issued bonds under a Euro Medium Term Notes (EMTN) Debt Issuance Programme (as noted below). The Company acted as guarantor.

The final terms of this series of notes contain change of control provisions under which the holder of each note will, subject to any earlier exercise by the Issuer of a tax call, have the option to require the Issuer to redeem or, at the Issuer's option, purchase that note at its nominal value if: (a) any person, or persons acting in concert or on behalf of any such person(s) becomes interested in: (i) more than 50 per cent of the issued or allotted ordinary share capital of the Company; or (ii) such number of shares in the capital of the Company carrying more than 50 per cent of the voting rights normally exercisable at a general meeting of the Company; and (b) as a result of the change of control, there is either: (i) a reduction to a non-investment grade rating or withdrawal of the investment grade rating of the notes which is not raised again, reinstated to or replaced by an investment grade rating during the change of control period specified in the final terms; or (ii) to the extent that the notes are not rated at the time of the change of control, the Issuer fails to obtain an investment grade credit rating of the notes within the change of control period as a result of the change of control.

The bonds issued in such manner are as follows:

- 15 September 2008 £600,000,000 8.125 per cent guaranteed notes due 2024;
- 17 February 2009 £1,000,000,000 9 per cent guaranteed notes due 2022;
- 24 June 2009 £500,000,000 7.75 per cent guaranteed notes due 2019;
- 5 July 2011 €850,000,000 4.5 per cent guaranteed notes due 2018;
- 26 September 2011 £500,000,000 5.5 per cent guaranteed notes due 2026;

- 1 December 2011 €750,000,000 5 per cent guaranteed notes due 2019;
- 28 February 2014 €1,000,000,000 2.25 per cent guaranteed notes due 2021;
- 28 February 2014 €650,000,000 3.375 per cent guaranteed notes due 2026; and
- 28 February 2014 £500,000,000 4.875 per cent guaranteed notes due 2032.

Imperial Brands Finance PLC has also issued bonds in the United States of America under the provisions of Section 144a and Regulation S respectively of the US Securities Act (1933). The Company acted as guarantor.

The final terms of this series of notes contain change of control provisions under which the holder of each note will, subject to any earlier exercise by the Issuer of a tax call, have the option to require the Issuer to redeem or, at the Issuer's option, purchase that note at 101 per cent of its nominal value if: (a) (i) any person (as such term is used in the US Securities Exchange Act of 1934 (the Exchange Act)) becomes the beneficial owner of more than 50 per cent of the Company's voting stock; or (ii) there is a transfer (other than by merger, consolidation or amalgamation) of all or substantially all of the Company's assets and those of its subsidiaries to any person (as such term is used in the Exchange Act); or (iii) a majority of the members of the Company's Board of Directors is not continuing in such capacity; and (b) as a result of the change of control, there is either: (i) a reduction to a non-investment grade rating or withdrawal of the investment grade rating of the notes which is not raised again, reinstated to or replaced by an investment grade rating during the change of control period specified in the final terms; or (ii) to the extent that the notes are not rated at the time of the change of control, the Issuer fails to obtain an investment grade credit rating of the notes within the change of control period as a result of the change of control.

The bonds issued in such manner are as follows:

- 11 February 2013 \$1,250,000,000 2.05 per cent guaranteed notes due 2018;
- 11 February 2013 \$1,000,000,000 3.50 per cent guaranteed notes due 2023;
- 21 July 2015 \$500,000,000 2.05 per cent guaranteed notes due 2018;
- 21 July 2015 \$1,250,000,000 2.95 per cent guaranteed notes due 2020;
- 21 July 2015 \$1,250,000,000 3.75 per cent guaranteed notes due 2022; and
- 21 July 2015 \$1,500,000,000 4.25 per cent guaranteed notes due 2025.

Update on Tobacco-Related Litigation Ireland

In the Republic of Ireland, the number of tobacco-related claims has fallen to only five. In four of these cases, the claimants are deceased and their solicitors have been unsuccessful in their efforts to contact their families. The fifth case has been inactive since 2003 and can be assumed to have been abandoned. If any of these claims reactivate, it is very likely that they would be struck out on grounds of delay.

Italy

We are currently facing two claims in Italy. The first is against Logista, which is the subject of a challenge on grounds of jurisdiction and the admission of evidence. This challenge was heard in 2006 but judgement is still awaited.

The second claim has been brought in the Court of Messina against Imperial Tobacco Italia and Reemtsma by two individuals claiming €800,000 in total. We have denied liability. The parties have filed their pleadings. A hearing is scheduled in February 2017 where the Judge will hear the parties' arguments regarding their requests for oral and expert evidence.

Morocco

In June 2015, a claim was filed in the Casablanca Court by the heirs of a deceased individual against our Moroccan subsidiary, Société Marocaine des Tabacs (SMT). The total amount of compensation sought was not specified. On 9 February 2016, the Casablanca Court found in favour of SMT and dismissed the claim. No appeal has been filed.

Argentina

SEITA has been notified of a claim filed in the Court of Buenos Aires against Nobleza Piccardo by an individual smoker. Nobleza Piccardo has denied liability. Nobleza Piccardo manufactures and distributes two brands of cigarettes owned by SEITA in Argentina under the terms of a Licence Agreement. Nobleza Piccardo has sought to invoke an indemnity contained in the Licence Agreement, pursuant to which SEITA is responsible for any product liability to third parties. The amount claimed is AR\$8,980,200.

The Netherlands

Reports in the public media indicate that a complaint has been lodged with the Public Prosecutor in the Netherlands directed at the four major tobacco manufacturers, including Imperial Brands. Neither Imperial Brands nor any of its subsidiaries or employees has been charged by the Public Prosecutor in the Netherlands, but Imperial Brands is monitoring developments.

To date, no action has been successful or settled in favour of any claimant in any tobacco-related litigation against Imperial Brands or any of its subsidiaries. Imperial Brands has been advised by its lawyers that it has meritorious defences to the legal proceedings set out above. We will continue vigorously to contest all such litigation against us.

Update on E-Vapour-Related Litigation

We are currently defending two e-vapour-related claims in the USA. The first is a consolidation of two purported class actions (Diek and Whitney) seeking to recover unquantified damages, including punitive damages. This action is subject to a pending motion to dismiss. On 1 November 2016, in response to a motion to dismiss all claims, the Court granted the motion in part dismissing with prejudice all but one remaining claim. After a response to the single remaining claim is filed, all further proceedings in the action will be stayed until further order of the Court. Therefore, at this stage, the value of the action is unquantifiable.

The second claim has been brought by the Center for Environmental Health alleging violations of the California Safe Drinking and Toxic Enforcement Act. We answered the claim in December 2015 and intend to defend it vigorously.

OTHER INFORMATION – LISTING RULES

For the purposes of LR 9.8.4R, the information required to be disclosed by LR 9.8.4R can be found on the pages set out below:

Section	Information	Page
(1)	Interest capitalised	Not applicable
(2)	Publication of unaudited financial information	Not applicable
(4)	Details of long-term incentive schemes	51, 57, 58, 64 and 65
(5)	Waiver of emoluments by a director	Not applicable
(6)	Waiver of future emoluments by a director	56, 57, 64, 65, 69 and 70
(7)	Non pre-emptive issues of equity for cash	Not applicable
(8)	Non pre-emptive issue by major subsidiary undertakings	Not applicable
(9)	Listed subsidiary	Not applicable
(10)	Contracts of significance	48 and 49
(11)	Provision of services by a controlling shareholder	Not applicable
(12)	Shareholder waivers of dividends	See below
(13)	Shareholder waivers of future dividends	See below
(14)	Agreements with controlling shareholders	Not applicable

In respect of LR 9.8.4R (12) and (13) the trustee of the Imperial Tobacco Group PLC Employee and Executive Benefit Trust and the Imperial Tobacco Group PLC 2001 Employee Benefit Trust agrees to waive dividends payable on the Group's shares it holds for satisfying awards under various Imperial Brands PLC share plans. In accordance with Section 726 of the Act no dividends can be paid to the Company in respect of the shares it holds in treasury.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the Group and the parent Company 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 Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, and the parent Company financial statements in accordance with United Kingdom GAAP (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 Group and the parent Company and of the profit or loss of the Group for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether IFRSs as adopted by the European Union and applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Group and parent Company financial statements respectively; 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 the Group and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Act and, as regards the Group financial statements, Article 4 of the IAS Regulation.

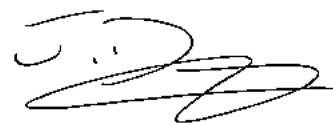
They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

Each of the Directors, whose names and functions are listed on pages 34 and 35, confirms that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Strategic Report and the Directors' Report include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

The Strategic Report and the Directors' Report were approved and signed by order of the Board.



John Downing

8 November 2016

Imperial Brands PLC

Incorporated and domiciled in England and Wales No: 3236483

DIRECTORS' REMUNERATION REPORT

REMUNERATION COMMITTEE



David Haines
Chairman

"Our remuneration policy incentivises management to deliver against our strategic objectives."

Members

David Haines *Chairman*
Ken Burnett (to 3 February 2016)
Therese Esperdy (from 1 July 2016)
Michael Herlihy
Steven Stanbrook (from 8 February 2016)

Karen Witts
Malcolm Wyman
Trevor Williams
Committee Secretary

Other regular attendees

Board Chairman¹
Chief Executive²
Group Company Secretary
Group Human Resources Director¹

Group Reward and Capability
Director
New Bridge Street, the
Committee's principal advisor²

1. Specifically excluded when their own remuneration or conditions of service are under discussion.
2. Appointed by the Committee.

Focus in 2016

- following the acquisition of assets in the USA, ongoing monitoring of performance conditions to ensure incentive pay-out levels appropriately reflect the intentions of the Committee and the remuneration policy at the time of grant
- use of discretion to increase revenue targets for in-flight LTIPs to mitigate the one off uplift from the acquisition of assets in the USA
- one off increase in EPS and revenue targets for the FY16 LTIP grant to mitigate the part year uplift from the acquisition of assets in the USA
- review of remuneration policy and positioning in light of the changed profile of the business following the successful USA acquisition, the Group's strategic objectives and to address real concern regarding the Group's ability to retain and attract executive talent

Focus for 2017

- consultation with major shareholders on proposed changes to the remuneration policy in order to address real concern regarding the Group's ability to retain and attract executive talent
- implementation of proposed changes
- ongoing monitoring of remuneration policy and performance conditions to ensure they appropriately support and incentivise delivery of the Group's strategic objectives

Remuneration Summary

The Committee's Aim

Our remuneration policy incentivises management to deliver our strategy, building on the Company's track record.

Our remuneration packages comprise:

Fixed elements	Variable elements
– salary	– annual bonus
– pension	– long-term incentive plan
– benefits	

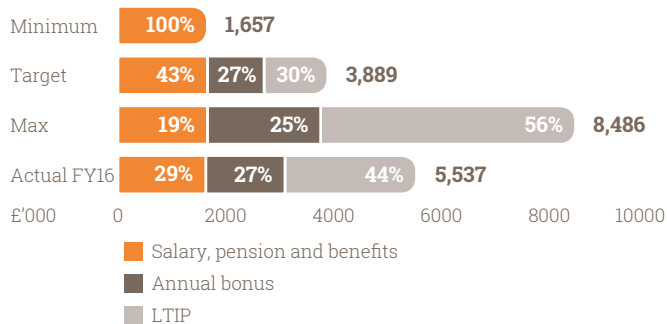


Turn to page 55

for further details of our remuneration policy

Remuneration is weighted towards performance related variable elements with targets aligned to the key performance indicators we use to measure the progress we make in delivering our strategy.

Under the proposed remuneration policy the potential reward opportunity for Alison Cooper, our Chief Executive, in the 2017 financial year is:



Summary of Total Remuneration for each Executive Director (2016)

£'000	Salary	Taxable benefits	Annual bonus	Share plans vesting	Share-save vesting	Pension benefits	Total
Executive Directors							
Alison Cooper	1,020	17	1,469	2,441	–	590	5,537
Oliver Tant	649	17	934	986	–	169	2,755
Matthew Phillips	541	24	779	757	4	434	2,539
	2,210	58	3,182	4,184	4	1,193	10,831



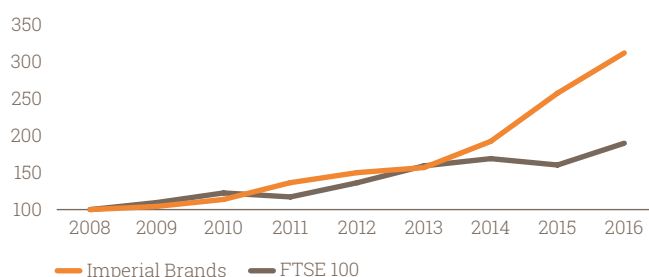
Turn to page 63

to read the full details in our Remuneration Report.

A Track Record of Out-performance

Execution of our strategy has resulted in Imperial Brands outperforming the FTSE and delivering a total shareholder return of 212%, as set out in the chart below.

Total Return Indices – Imperial Brands and FTSE 100



FTSE 100 Index for each of our financial year ends to 30 September 2016. We have chosen the FTSE 100 Index as it provides the most appropriate and widely recognised index for benchmarking our corporate performance over an eight-year period.

DEAR SHAREHOLDER

Our approach to remuneration aims to incentivise the delivery of our strategy and create strong alignment between the interests of shareholders and senior management over the long term.

We achieve this by ensuring:

- the Group is able to attract and motivate the high calibre of international executives required;
- members of our executive team have the opportunity to earn competitive levels of reward for delivery of strong performance in the context of the roles they perform;
- we have the appropriate performance measures to align executive and shareholder interests and expectations; and
- executive remuneration is not excessive but is fair and competitive; in particular, we guard against rewards for failure.

Our Performance Record

In the six years since we introduced our current strategy we have significantly outperformed the FTSE 100, delivering a Total Shareholder Return (TSR) of 174 per cent (compared to the index over the same period of 55 per cent).

I am pleased to say that this strong performance continued over the last year. We successfully integrated the \$7.2 billion acquisition of brands and assets from Reynolds American in the USA, enhancing our footprint in one of the world's most profitable tobacco markets. Our larger USA business, ITG Brands, made an excellent contribution to our results in the year. We also further improved the quality of our growth by increasing the contribution from our Growth and Specialist Brands, which now account for 60.1 per cent of the Group's tobacco net revenue. Our strong financial performance included adjusted earnings per share growth of 12 per cent, cash conversion of 95 per cent and dividend growth of 10 per cent.

Our performance resulted in an annual bonus pay-out for Executive Directors of 72 per cent of maximum opportunity. Our track record of success over the longer term started to be reflected in the outcome of the long-term plans, with vesting of approximately 59 per cent under the LTIP awards made in December 2013, and approximately 19 per cent vesting in respect of SMS awards made in February 2014.

The Issue We Face

Despite this strong performance, the pay of our executive team has been significantly below the average for companies of our size for some time. I am concerned that if we do not address the situation, we will be put at an unnecessary risk with regard to retaining our senior team, especially as we embark upon the next decade of our growth strategy.

Over the past three years we made a number of changes to our remuneration policy, which addressed part of the problem by bringing salaries into line with the market. At the same time we also strengthened governance through a shift towards long-term pay, the introduction of holding periods on vested shares and the strengthening of malus and claw back provisions.

However, when we look at overall levels of pay we continue to pay below competitive levels in the context of the very strong performance of the business. The underlying reason for this is that our variable pay opportunity falls short of that offered elsewhere.

Consultation

To address this we developed proposals to increase the opportunity within our variable compensation and consulted many of our largest investors. During this process I was very pleased to hear consistent strong support for our management team and their successful execution of our strategy; as well as a shared understanding of the issue we face on remuneration and support for addressing it.

There were divergent views on how this might best be achieved; many shareholders were supportive of the continued emphasis on long-term variable pay, while others suggested increases to fixed pay, either through higher base pay, or the use of restricted stock.

The use of restricted stock for Board executives in the UK remains at an early stage, and whilst we would not rule this out for the future, our current preference is to increase the LTIP opportunity as this will only increase pay if performance is delivered.

Some investors also considered that an increase in pay opportunity should be accompanied by higher performance targets. In our situation, a balanced approach is required since we are seeking to address a significant shortfall in opportunity and the resulting pay for performance, and to increase performance levels too far would risk undermining our original intent.

We therefore intend to raise the level of EPS performance required to achieve maximum pay-out under the LTIP. However, we would not wish to disguise the fact that our proposals allow us to pay more for the delivery of the levels of performance seen in recent years, and we believe this is entirely appropriate.

A number of shareholders raised a view that the weighting on EPS was quite high and could be replaced, in part, by operational measures. The possibility of increased shareholding requirements was also raised together with a post-exit shareholding requirement. Both these points were taken on board by the Committee.

I appreciate that we operate within a broader social context and recent years have seen a rise in concerns about executive pay in general. We are sympathetic to concerns about pay increases which do not reflect performance.

However, businesses such as ours are essential to the economy and it is in the interests of all our stakeholders that they should be managed as well as possible to produce optimal performance. To that end, we believe it is right and necessary that our executive team has the opportunity to earn competitive levels of reward for delivery of strong performance. This change also provides headroom for increases below executive level, where required, to attract and retain the talent necessary to drive the business forward.

Proposed Changes for 2017

Following consultation with shareholders our proposal is to:

- increase the opportunity under our LTIP by 100 per cent of base salary;
- increase the EPS target for maximum vesting from 8 per cent to 9 per cent growth per annum;
- introduce cash conversion as a performance measure into the LTIP;
- raise the shareholding requirement for the CEO from 300 per cent to 400 per cent of base salary; and
- introduce a post-exit shareholding requirement for the CEO of 100 per cent of base salary for two years.

As a result, our LTIP performance criteria reflect the key performance indicators aligned to our strategy: growth in revenue and earnings, the conversion of earnings to cash (supporting investment in our brands and our commitment to 10 per cent dividend growth) and the resulting creation of shareholder value.

In increasing the LTIP opportunity we are not seeking to address historic underpayment but are ensuring that our management team has the opportunity to earn competitive reward for continued high performance in future years.

The Committee will ensure that performance conditions remain stretching but realistic. Our recent history demonstrates that we have consistently upheld this principle; at the start of this year, the Committee used its discretion to increase revenue targets for all in-flight LTIPs to remove the positive impact of the USA acquisition to ensure only organic growth is rewarded and, for one grant, increased the earnings per share and revenue targets in the 2016 LTIP grant to reflect the partial year uplift from the same acquisition.

For our 2017 financial year, we have made salary increases in line with the Company as a whole to two of the three Executive Directors. The Committee made a higher increase to the CFO to reflect both his increased responsibilities in an expanded role incorporating Group Procurement and Group Information Systems, and the competitive CFO market. Our expectation is that future increases, for all Executive Directors, will all be broadly aligned with those across the Company.

As I have said in previous reports, I am confident that we have built strong links between our reward programmes and the key performance indicators used to measure the progress in delivering our strategy. The changes we are now proposing strengthen both these links and our competitive positioning, to ensure we are able to retain our successful management team and recruit the next generation when the time comes. As such, we believe the changes we are proposing to our policy are very much in the best interests of both the Company and shareholders, and I look forward to your support.



David Haines

Chairman of the Remuneration Committee

DIRECTORS' REMUNERATION REPORT

CONTINUED

GOVERNANCE

The Role of the Remuneration Committee

The Board recognises that it is ultimately accountable for executive remuneration but has delegated this responsibility to the Committee.

The Committee's principal function is to support the Group's strategy by ensuring its delivery is incentivised by the remuneration policy. It also determines the specific remuneration package, including service contracts and pension arrangements, for each Executive Director and our most senior executives.

The Committee held four meetings during the financial year.

The Committee's responsibilities include:

- ensuring remuneration arrangements support our strategy, align with our values and drive performance;
- maintaining a competitive remuneration policy appropriate to the business environment of the countries in which we operate, thereby ensuring we can attract and retain high calibre individuals;
- aligning senior executives' remuneration with the interests of long-term shareholders whilst ensuring that remuneration is fair but not excessive;
- assessing the output from the Board evaluation process insofar as it relates to the Committee;
- making recommendations to the Board in respect of our Chairman's fees;
- setting targets for performance related elements;
- oversight of our overall policy for senior management remuneration and of our employee share plans; and
- ensuring appropriate independent advisors are appointed to provide advice and guidance to the Committee.

The Committee's full terms of reference provide further details of the role and responsibilities of the Committee and are available on our website.

All members of the Committee are independent Non-Executive Directors which we consider fundamental in ensuring Executive Directors' and senior executives' remuneration is set by people who are independent and have no personal financial interest, other than as shareholders, in the matters discussed.

To reinforce this independence, a standing item at each Committee meeting allows the members to meet without any Executive Director or other manager being present.

This Report has been prepared in accordance with the provisions of the Companies Act 2006 (the Act) and The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 (the Regulations). It also meets the requirements of the UK Listing Authority's Listing Rules and the Disclosure and Transparency Rules. In this Report we describe how the principles of good governance relating to directors' remuneration, as set out in the UK Corporate Governance Code 2014 (the Code), are applied in practice. The Committee confirms that throughout the financial year the Company has complied with these governance rules and best practice provisions.

The Regulations require our auditors to report to shareholders on the audited information within this Report and to state whether, in their opinion, the relevant sections have been prepared in accordance with the Act. The auditors' opinion is set out on page 75 and we have clearly marked the audited sections of the Report.

Remuneration Committee Meetings Held in the 2016 Financial Year

Four Committee meetings were held in the 2016 financial year and included the following matters on the agenda:

Oct	Apr	Jun	Sept
– Directors' Remuneration Report – FY15 Bonus payments – FY16 Bonus target finalisation – LTIP – satisfaction of vesting criteria – LTIP 2016 grant and performance criteria – SMS – lapsing of Directors' award as vesting criteria not met – Approval of 2016 Sharesave grant	– Review of terms of reference – AGM voting and shareholder feedback – Update on remuneration governance – Review of remuneration policy	– Review of proposals for remuneration policy – Investor communications for proposed policy	– Market practice update – Potential outturn for FY16 bonus, LTIP and SMS – Update on policy proposals and FY17 salary and incentive structures – Review of Chairman's fees

Remuneration Policy for Executive Directors

Our strategy and business model drive our remuneration policy. Our policy is designed to offer competitive, but not excessive, base salary, with significant weighting towards performance-based elements, the measures of which incentivise and support the delivery of our strategy whilst also reflecting individual, functional and corporate performance. We aim to set and rigorously apply targets that are both stretching and achievable.

As stated earlier in this Report, we reviewed our remuneration policy in 2016. As a result of this review and shareholder feedback received during consultation, we have revised the remuneration policy. The changes to our policy are summarised in the table below and the rationale for these changes is set out in the letter from the Chairman of the Remuneration Committee on pages 52 and 53. Other elements of our remuneration policy have not changed.

Element	Previous policy	New policy
Maximum salary / Maximum increase in salary	No maximum for base salary.	Whilst there is no maximum salary or maximum increase in salary the Committee would only set a salary which exceeded the top quartile of salaries of the comparator group in unforeseen and exceptional circumstances.
Long-Term Incentive Plan maximum award sizes	Maximum award sizes: Chief Executive Officer: 350% of base salary. Other Executive Directors: 250% of base salary or such lower sum as determined by the Committee.	Maximum award sizes: Chief Executive Officer: 450% of base salary. Other Executive Directors: 350% of base salary or such lower sum as determined by the Committee.
Chief Executive shareholding guidelines	The Chief Executive is expected to build a holding broadly equivalent to 300 per cent of base salary over a period of five years from appointment.	The Chief Executive is expected to build a holding broadly equivalent to 400 per cent of base salary over a period of five years from appointment.
Post exit shareholding requirement	No requirement.	The CEO will have a post exit shareholding requirement of 100 per cent of salary for two years post exit.

It is intended that the remuneration policy set out in this Report will, if approved, for the purposes of section 226D(6)(b) of the Act, take effect immediately after the AGM on 1 February 2017.

DIRECTORS' REMUNERATION REPORT

CONTINUED

Remuneration Policy for Executive Directors

Element	Purpose and link to strategy	Operation	Maximum opportunity
Salary	Attract and retain high performing individuals, reflecting market value of role and the Executive Director's skills, experience and performance.	Reviewed, but not necessarily increased, annually by the Committee taking into account each Executive Director's performance together with changes in role and responsibility. Salary increases, if any, are generally effective from 1 October. The Committee considers pay data for UK listed companies closest to us by FTSE ranking (and excluding those in the financial services sector). These comparators serve to define a "playing field" within which an individual's reward needs to be positioned. In determining individual remuneration, the primary factors taken into account are individual performance, the scale of the challenges intrinsic to that individual's role, their ability and experience.	Whilst there is no maximum salary or maximum increase in salary, the Committee would only set a salary which exceeded the top quartile of salaries of the comparator group in unforeseen and exceptional circumstances. The Committee takes into account each Executive Director's performance, together with changes in role and responsibility and considers general increases for the UK wider management population.
Benefits	Competitive benefits taking into account market value of role and benefits offered to the wider UK management population.	Benefits include provision of company car, health insurance, life insurance and permanent health insurance which are provided directly or through the Company pension scheme. Opportunity to join the Sharesave Plan. Provision of relocation assistance upon appointment if/when applicable.	The level of benefit provision is fixed.
Annual Bonus Plan	Incentivise delivery of Group strategic objectives and enhance performance, including against the indicators we use to measure our performance as detailed on pages 6 and 7.	At least 60% of the annual bonus will be linked to key financial metrics and no more than 15% will be linked to individual measures. Performance below the threshold results in zero payment. Payments rise from 0% to 100% of the maximum opportunity for levels of performance between the threshold and maximum targets. Half of any annual bonus paid would be in deferred shares to be held for a minimum of three years, with the other half paid in cash. Malus provisions apply before payment and claw back provisions are in place for the three years following payment of annual bonus. The deferred shares are not subject to performance conditions.	200% of base salary or such lower sum as determined by the Committee.
Share Matching Scheme (no further awards to be made to Executive Directors)	Incentivise the delivery of Group strategic targets. Promote share ownership worldwide across the Imperial Brands management team.	The award granted in February 2014 was the last in which Executive Directors were eligible to participate. However, these outstanding awards will vest in February 2017 in line with the achievement of the relevant performance conditions. The three-year award had performance conditions based on financial measures with underpins. In respect of each element, performance below threshold target results in zero vesting. Vesting of each performance element starts at 25% and rises to 100% for levels of performance between threshold and maximum. There is no opportunity to retest and claw back provisions are in place. Dividends accrue on vested shares and will be paid on vesting in February 2017.	Maximum match is 1:1 on shares invested plus dividend equivalents.

Remuneration Policy for Executive Directors continued

Element	Purpose and link to strategy	Operation	Maximum opportunity
Long-Term Incentive Plan	Incentivise long-term Group financial performance in line with the Group's strategic objectives, including against the indicators we use to measure our performance as detailed on pages 6 and 7, and long-term shareholder returns. Align Executive Directors' interests with those of long-term shareholders.	Awards granted during or after January 2015 Awards have a performance period of three financial years starting at the beginning of the financial year in which the award is made and are based 20% on relative Total Shareholder Return (TSR) vs a peer group and 80% on financial measures. In respect of each performance element, performance below the threshold target results in zero vesting. Vesting of each performance element starts at 25% and rises to 100% for levels of performance between the threshold and maximum targets. There is no opportunity to re-test. Claw back and malus provisions are in place. Dividend equivalents accrued on vested shares are paid at the time of vesting. Any awards which vest will be subject to a further two-year holding requirement. Awards granted November 2013 Awards have a performance period of three financial years starting at the beginning of the financial year in which the award is made and are based 50% on TSR vs a peer group and 50% on financial measures with underpins. In respect of each performance element, performance below the threshold target results in zero vesting. Vesting of each performance element starts at 25% and rises to 100% for levels of performance between the threshold and maximum targets. There is no opportunity to re-test. Claw back provisions are in place. Dividends accrued on vested shares are paid at the time of vesting.	Chief Executive Officer: 450% of base salary. Other Executive Directors: 350% of base salary or such lower sum as determined by the Committee. Plus shares equivalent to the value of the dividend roll-up.
Pensions	Attract and retain high performing Executive Directors.	Pension provision for Executive Directors is provided in line with other employees through the Imperial Tobacco Pension Fund in the UK (the Fund). Executive Directors who joined the Fund prior to 1 October 2010 are members of the defined benefit section whereas Executive Directors joining the Fund on or after this date are offered membership of the defined contribution section. Executives have the option to receive a cash supplement in lieu of membership of the Fund, or in lieu of accrual on pensionable salary above the Fund's earnings cap, or in lieu of future service accrual. Members of the defined benefit section of the Fund accrue pension at a rate between 1/47th and 1/60th of pensionable salary. Further detail is provided in the Annual Report on Remuneration on pages 65 and 66. The rules of the Fund detail the pension benefits which members can receive on retirement, death or leaving service. The Committee may amend the form of any Executive Director's pension arrangements in response to changes in pensions' legislation or similar developments, so long as any amendment does not increase the cost to the Company of an Executive Director's pension provision.	Current policy is for a defined contribution and cash supplement limit of 26% of salary. Existing members of the defined benefit section have a cash in lieu of pension accrual limit of 35% of salary.

Note: Legacy awards – Subject to the achievement of applicable performance conditions, Executive Directors remain eligible to receive payments, and existing awards may vest, in accordance with the terms of any such award (including under the Share Matching Scheme, outlined on page 56) made prior to the approval and implementation of the remuneration policy.

DIRECTORS' REMUNERATION REPORT

CONTINUED

Committee Discretions Relating to Variable Pay Schemes

The Committee operates each of the Company's incentive plans for which it has responsibility according to their respective rules and, where relevant, in accordance with the Listing Rules. The Committee has discretion, consistent with market practice, in respect of, but not limited to:

- participants;
- the timing of grant of an award and/or payment;
- the size of an award (subject to the maxima set out in our policy);
- the performance measures and targets;
- the determination of vesting and confirmation that the calculation of performance is made in an appropriate manner, with due consideration of whether and, if so, how adjustments should be made (subject to the provision that any adjustments to targets set should result in the revised target being no less challenging than the original target);
- discretion required when dealing with a change of control and any adjustments required in special circumstances (e.g. rights issues, corporate restructuring events and special dividends); and
- determination of a good/bad leaver for plan purposes based on the rules of the plan and the appropriate treatment chosen.

In relation to the Annual Bonus, LTIP and legacy SMS awards, the Committee retains the ability to adjust the targets set if events occur which cause it to determine that the conditions are no longer appropriate and amendment is required so that the conditions achieve their original purpose and are not materially less difficult to satisfy than was intended. Adjustment may also be made for any changes to accounting policy over the performance period. Any use of discretion beyond the normal operation of the plan would be justified in the Annual Report on Remuneration and, if appropriate, be subject to consultation with the Company's major shareholders. The use of discretion in relation to the Company's Sharesave plan is as permitted under HMRC rules.

In the past two years the Committee has exercised its discretion on two occasions; both of these were to increase targets within the LTIP in order to reduce payments following the acquisition of USA assets, in order to ensure that the rewards received by the management team were in line with the Committee's original intentions when it set the performance criteria. The Committee will continue to review targets to ensure they reflect its original intentions, and this may include any discretion required due to the impact of the recently announced strategic investments.

Payments from Existing Awards

Subject to the achievement of applicable performance conditions, Executive Directors are eligible to receive payment, and existing awards may vest, in accordance with the terms of any such award made prior to the approval and implementation of the remuneration policy detailed in this Report.

Performance Measure Selection

The measures used under the annual bonus plan are selected annually to reflect the Group's key strategic initiatives for the year and reflect both financial and non-financial objectives.

The Committee reviews the performance measures annually and whilst it still considers adjusted EPS, net revenue and relative TSR to be appropriate measures of long-term performance for the Group, it has introduced a cash conversion measure to increase the focus on the financial discipline required to support our ongoing investment behind our growth strategy and our dividend commitment. TSR aligns with the Company's focus on shareholder value creation and rewards management for out-performance of sector peers. EPS provides strong line-of-sight for Executive Directors and supports the Group's long-term strategy. Net revenue supports the Company's focus on organic growth.

Performance measures are set to be stretching and achievable, taking into account the Company's strategic priorities and the economic environment.

Remuneration Policy for Other Employees

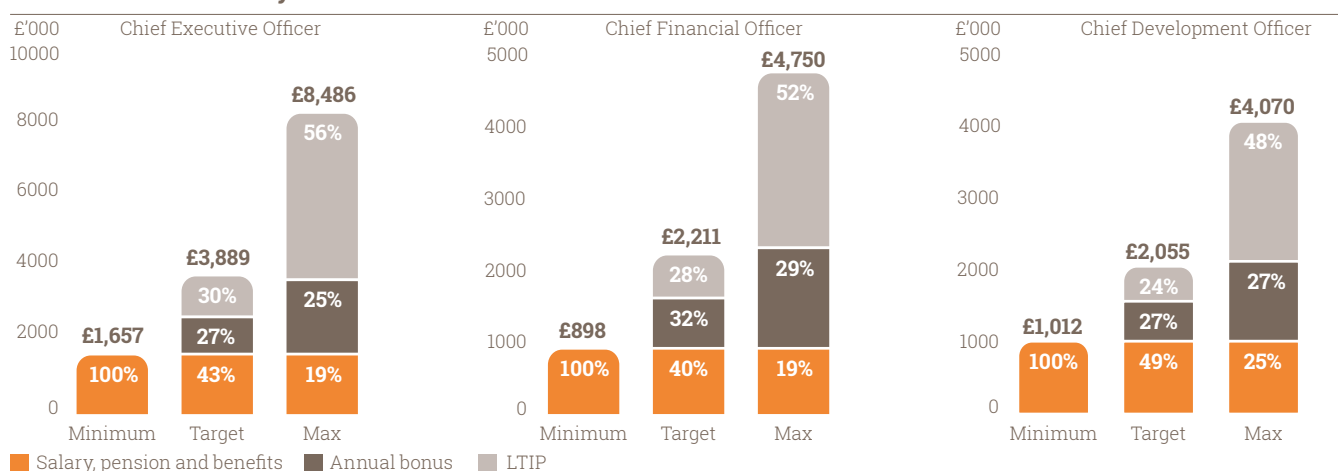
The Company's approach to annual salary reviews is consistent across the Group, with consideration given to the scope of the role, level of experience, responsibility, individual performance and pay levels in comparable companies.

All managers are eligible to participate in an annual bonus plan with similar metrics to those used for the Executive Directors. Other employees are eligible to participate in performance led annual bonus plans. Opportunities and specific performance conditions vary by organisational level with business area-specific metrics incorporated where appropriate.

Senior executives are eligible to participate in the LTIP (c.55 individuals) and the majority of members of the Corporate Management Group are eligible to participate in the SMS (c.1,000 individuals).

TOTAL REMUNERATION OF THE EXECUTIVE DIRECTORS FOR A MINIMUM, TARGET AND MAXIMUM PERFORMANCE

Total Remuneration by Performance Scenario for 2016/17 Financial Year



The charts are indicative as share price movement and dividend accrual have been excluded. Assumptions made for each scenario are as follows:

- Minimum: fixed remuneration only (i.e. salary, benefits and pension).
- Target: fixed remuneration plus half of maximum annual bonus opportunity plus 25 per cent vesting of LTIP awards. Note that Imperial Brands does not have a stated 'target' for either its financial measures or incentive pay-outs.
- Maximum: fixed remuneration plus maximum annual bonus opportunity plus 100 per cent vesting of LTIP awards.

Executive Directors' Service Agreements and Loss of Office Payments

The Company's policy is that Executive Directors' service agreements normally continue until their agreed retirement date or such other date as the parties agree, are terminable on no more than one year's notice and contain no liquidated damages provisions nor any other entitlement to the payment of a predetermined amount on termination of employment in any circumstances. In addition, in some limited cases career counselling may be provided after the cessation of employment for a defined period. Under the terms of our Articles of Association, all Executive Directors are subject to annual re-election by shareholders.

Executive Directors' service agreements contain provisions for payment in lieu of notice in respect of base salary, pension contributions and 5 per cent of base salary in respect of other benefits but these are at the Committee's sole discretion. The Company is unequivocally against rewards for failure. The circumstances of any termination (including performance) and an individual's duty and opportunity to mitigate losses would be taken into account in every case; our policy is to stop or reduce compensatory payments to former Executive Directors to the extent that they receive remuneration from other employment during the compensation period and any such payments would be paid monthly in arrears.

For Executive Directors leaving employment for specified reasons (including death, redundancy, retirement, ill health and disability, the business or company in which they are employed ceasing to be part of the Group or on a change of control) annual bonus awards will be based on performance, adjusted for time served, and paid at the same time as for other employees. The Committee has discretion to adjust the timing and pro-rating to take account of any prevailing exceptional circumstances.

Under the rules of both the LTIP and the legacy SMS, outstanding awards vest if a participant leaves for the specified reasons as detailed above. In these circumstances awards vest as the Committee determines having regard to the time the award has been held and the achievement of the performance criteria. Awards will vest either on termination of employment or, for awards granted under the policy approved by shareholders in 2014 and under the proposed policy, at the normal vesting date, as the Committee determines in its absolute discretion. If the termination of employment is not for one of the specified reasons and the Committee does not exercise its discretion to allow an award to vest, awards lapse entirely.

Executive Directors' Service Agreements

Executive Directors	Date of contract	Expiry date	Compensation on termination following a change of control
Alison Cooper	1 July 2007	Terminable on 12 months' notice	No provisions
Oliver Tant	1 October 2013	Terminable on 12 months' notice	No provisions
Matthew Phillips	31 May 2012	Terminable on 12 months' notice	No provisions

DIRECTORS' REMUNERATION REPORT

CONTINUED

Recruitment of Executive Directors

The remuneration package for a new Executive Director would be set in accordance with the terms of the approved remuneration policy in force at the time of appointment. The Committee may offer additional cash and/or share-based elements when it considers these to be in the best interests of the Company and, therefore, shareholders. Any such buyout awards would be based solely on remuneration lost when leaving the former employer and would reflect the delivery mechanism (i.e. cash, shares, options), time horizons and performance requirements attaching to that remuneration. Shareholders will be informed of any such awards at the time of appointment. The Committee may need to avail itself of the current Listing Rule 9.4.2 R if required in order to facilitate, in unusual circumstances, the recruitment or retention of the relevant individual. The Committee confirms that this provision would only be used to compensate for remuneration lost.

In the case of an internal appointment, any variable pay element awarded in respect of the prior role may be allowed to pay-out according to its terms on grant. In addition, any other ongoing remuneration obligations existing prior to appointment may continue, provided that they are put to shareholders for approval at the first AGM following their appointment.

For external and internal appointments, the Committee may agree that the Company will meet certain relocation expenses, as appropriate and within the limits set by the Committee.

Shareholding Guidelines

Whilst placing significant weight on annual performance, our policy aligns the interests of shareholders and other stakeholders with those of management by incentivising the growth in the value of the business over the long term. To support this alignment, we have share ownership guidelines as we believe Executive Directors and other senior managers should be encouraged to hold a substantial portion of their personal wealth in our shares.

Over a period of five years from appointment, Executive Directors are expected to build a holding in the Group's shares to a minimum value broadly equivalent to 400 per cent of salary (increased from 300 per cent) for the Chief Executive and 300 per cent for other Executive Directors. Other senior management are expected to invest at a level equivalent to between once and twice base salary, dependent upon grade. Failure to meet the minimum shareholding requirement is taken into account when determining eligibility for LTIP awards.

The Committee is also introducing a post-exit shareholding requirement for the Chief Executive of 100 per cent of salary for two years post-exit.

Non-Executive Directors do not have a shareholding requirement but are required to invest a minimum percentage of their fees in shares which they are required to retain for the duration of their appointment.

Consultation with Employees

Although the Committee does not consult directly with employees on the remuneration policy, the Committee does consider the general base salary increase, remuneration arrangements and employment conditions for the broader employee population when determining the remuneration policy for Executive Directors.

Differences in Remuneration Policy for Executive Directors Compared to Other Employees

The remuneration policy for Executive Directors is designed having regard to the remuneration policy for employees across the Group. However, there are some differences in the structure of the remuneration policy for the Executive Directors and other senior employees, which the Committee believes are necessary to reflect the different levels of responsibility. The key difference is the increased emphasis on long-term performance related pay for Executive Directors.

Consideration of Shareholder Views

The Committee considers shareholder feedback received in relation to the AGM each year at its first meeting following the AGM. This feedback, as well as any additional feedback received during any other meetings with shareholders, is considered as part of the Company's annual remuneration policy review.

The Committee notes that shareholders do not speak with a single voice, but we engage with our largest shareholders to ensure we understand the range of views which exist on remuneration issues. When any material changes are made to the remuneration policy the Committee chairman will inform major shareholders in advance, and will offer a meeting to discuss these.

In line with this policy, the Committee consulted with the Company's major shareholders on proposed changes to the remuneration policy between August and October 2016. During these consultations the Committee was pleased to hear of the strong support for the management team and the Group's strategy as well as the recognition of the current issue of low variable remuneration opportunity compared to peers. A variety of possible solutions were suggested including an increase to fixed remuneration, increases to existing incentive plans or the introduction of a restricted stock plan. As a result of the consultation the Committee proposes an increase to LTIP opportunity of 100 per cent of base salary, bringing remuneration opportunity more in line with peers but with additional rewards only paid for performance. By providing the management team with the opportunity to earn competitive rewards for high performance the Committee believes that the Company is better positioned to retain the existing successful management team and attract new talent as we enter the next phase of our growth strategy.

Policy in Respect of External Board Appointments

We recognise that external non-executive directorships are beneficial for both the Executive Director concerned and the Company. Each serving Executive Director is restricted to one external non-executive directorship and may not serve as the chairman of a FTSE 100 company. At the discretion of the Board, Executive Directors are permitted to retain fees received in respect of any such non-executive directorship.

Alison Cooper is a Non-Executive Director of Inchcape plc and was permitted to retain the £59,167 fee received from this position in the financial year.

Policy for Non-Executive Directors

Element	Purpose and link to strategy	Operation	Maximum opportunity
Fees	Attract and retain high performing individuals. Portion of fees applied to purchase of shares to align interests with those of shareholders.	Reviewed, but not necessarily increased, annually by the Board (after recommendation by the Committee in respect of the Chairman). Fee increases, if applicable, are normally effective from 1 October. The Board and, where appropriate, the Committee considers pay data at comparator companies of similar scale. The Senior Independent Director and the chairmen of the Audit and Remuneration Committees receive additional fees. It is proposed that from February 2017 additional fees will also be paid for Committee memberships. No eligibility for annual bonus, retirement benefits or to participate in the Group's employee share plans.	No prescribed maximum annual increase. Aggregate annual fees limited to £2.0 million by Articles of Association.
Benefits	Travel to the Company's registered office.	Travel to the Company's registered office is recognised as a taxable benefit.	Grossed-up costs of travel.

Non-Executive Directors' Letters of Appointment

The Chairman and Non-Executive Directors do not have service agreements but the terms of their appointment, including the time commitment expected, are recorded in letters of appointment which are available for viewing at our registered office during normal business hours and both prior to and at the AGM.

In line with our annual review policy, the Chairman's and Non-Executive Directors' terms of appointment were reviewed and confirmed by the Board on 2 February 2016. There are no provisions regarding notice periods in their letters of appointment which state that the Chairman and Non-Executive Directors will only receive payment until the date their appointment ends and, therefore, no compensation is payable on termination. Under the terms of our Articles of Association, all Non-Executive Directors are subject to annual re-election by shareholders.

ANNUAL REPORT ON REMUNERATION – HOW THE COMMITTEE IMPLEMENTED THE REMUNERATION POLICY FOR FINANCIAL YEAR ENDED 30 SEPTEMBER 2016

Implementing Executive Policy and Practice

In implementing the Company's remuneration policy (as detailed on pages 48 to 53 of the Company's Annual Report and Accounts 2014 available on our website), the Committee recognises that striking the right balance in finding a fair outcome in setting a competitive level of total remuneration is a matter of judgement. In forming this judgement, the Committee considered pay data at comparator companies of similar scale, primarily looking at a market capitalisation group made up of 10 companies above and 10 companies below Imperial Brands in the FTSE, excluding Financial Services. Comparisons with other companies, however, do not determine what remuneration the Company offers but, at most, serve to define a "playing field" within which an individual's reward needs to be positioned. In determining that positioning, the primary factors taken into account are the scale of the challenges intrinsic to that individual's role, their ability, experience and performance.

We align the interests of long-term shareholders and employees at all levels by, wherever possible, giving our employees the annual opportunity to build a shareholding in the Company through our employee share plans, with over 30 per cent of eligible employees participating in one or more plans.

During the year the Committee exercised its discretion to ensure that remuneration appropriately reflects management performance by increasing targets within long-term incentives. Revenue targets within all in-flight LTIPs were increased to reflect the impact of the one-off uplift from the acquisition of assets in the USA thereby only rewarding organic revenue growth.

For the same reason the Committee implemented a one off increase in EPS and revenue targets for the LTIP grant made during the year to mitigate the part year uplift from the acquisition of assets in the USA.

Linking Remuneration with Strategy

We focus on delivering high quality sustainable sales growth whilst effectively managing our costs and cash flows. Ensuring that our sales growth drivers and key enablers are supported and their delivery incentivised by our remuneration policy is key to maximising long-term returns to shareholders.

Alignment with our Strategy	Sustainable growth is at the heart of our strategy. This is supported by the inclusion of the drivers of growth within our variable remuneration – both the annual bonus and LTIP. Stretching performance targets incentivise the delivery of sales and the creation of shareholder value. Managing our costs and cash flows are the other elements of our strategic focus. Profitability, mainly in the form of earnings per share, forms a major part of the measurement in both the annual bonus and LTIP whilst cash conversion forms a measure for the annual bonus.
Alignment with our Shareholders	To align their interest with shareholders, employees at all levels are encouraged to have an interest in the Company's shares through both direct shareholdings (supported by shareholding requirements for senior executives) and through our share plans, with the value of the Corporate Management Group's overall remuneration being heavily influenced by the performance of our share price.
Attracting and Retaining the Right People	Our remuneration policy is designed to ensure a high quality pool of talented employees at all levels who are engaged and incentivised to deliver our strategy through clear links between reward and performance, without encouraging them to take undue risks. We believe it is important to ensure that management is competitively rewarded in relation to peers and the other opportunities available to them whilst ensuring we neither pay more than necessary nor reward failure. Our policy is, therefore, significantly weighted towards performance based elements.

Single Total Figure of Remuneration for each Director (Audited)

£'000	2016 Salary and fees	2015 Salary and fees	2016 Taxable benefits ¹	2015 Taxable benefits	2016 Annual bonus ²	2015 Annual bonus	2016 Share plans vesting ³	2015 Share plans vesting ³	2016 Share- save vesting ⁴	2015 Share- save vesting	2016 Pension benefits ⁵	2015 Pension benefits	2016 Total	2015 Total
Executive Directors														
Alison Cooper	1,020	965	17	16	1,469	1,544	2,441	626	–	6	590	480	5,537	3,637
Oliver Tant	649	630	17	16	934	1,008	986	–	–	–	169	163	2,755	1,817
Matthew Phillips	541	478	24	23	779	705	757	185	4	4	434	296	2,539	1,691
	2,210	2,073	58	55	3,182	3,257	4,184	811	4	10	1,193	939	10,831	7,145
Non-Executive Directors														
Mark Williamson	500	450	4	4	–	–	–	–	–	–	–	–	504	454
Ken Burnett ⁶	26	75	10	29	–	–	–	–	–	–	–	–	36	104
Therese Esperdy ⁷	19	–	7	–	–	–	–	–	–	–	–	–	26	–
David Haines ⁸	100	100	2	5	–	–	–	–	–	–	–	–	102	105
Michael Herlihy ⁸	100	100	2	4	–	–	–	–	–	–	–	–	102	104
Steven Stanbrook ⁹	49	–	10	–	–	–	–	–	–	–	–	–	59	–
Karen Witts	75	75	1	3	–	–	–	–	–	–	–	–	76	78
Malcolm Wyman ⁸	100	100	3	9	–	–	–	–	–	–	–	–	103	109
	969	900	39	54	–	–	–	–	–	–	–	–	1,008	954

1. Taxable benefits principally include an allowance (£15,000 in respect of Alison Cooper and Oliver Tant) in lieu of or the provision of a company car (£22,597 in respect of Matthew Phillips), fuel and health insurance. Benefits in kind for the Non-Executive Directors relate to the reimbursement of travelling expenses to meetings held at the Company's registered office.
2. Annual bonus earned for performance over the financial year ending 30 September 2016. In line with policy half of the net value is deferred in shares for three years; no further performance conditions apply.
3. Share plans vesting represent the value of SMS and LTIP awards where the performance period ends in the year and are based on a share price of £40.1689 being the three-month average to 30 September 2016. The 2015 estimated figure has been restated to reflect actual share price at the date of vesting.
4. Gains made on exercise are calculated as the difference between the option price and the market price on the date of exercise. These sharesave options were the only options exercised in the year; 195 shares in respect of Matthew Phillips.
5. Further details are contained in the Executive Directors' pension section on pages 65 and 66.
6. Ken Burnett retired from the Board on 3 February 2016.
7. Therese Esperdy was appointed to the Board on 1 July 2016.
8. Includes payment in respect of Senior Independent Director fees of £25,000 per annum and chairmanship of Remuneration and Audit Committees at an annual rate of £25,000.
9. Steven Stanbrook was appointed to the Board on 6 February 2016.

All expense payments made to Directors were made on the basis of reimbursement of expenses incurred grossed up for tax where expenses represent a taxable benefit. No payments were made by way of taxable expenses allowances. No Directors waived their fees. No payments were made to former directors nor were any payments made for loss of office during the year.

Additional Notes to the Single Total Figure of Remuneration (Audited)

This section sets out supporting information for the single total figure columns relating to annual bonus, share plans and pension benefits. In particular, it details the extent to which performance conditions have been satisfied for the annual bonus and for each share plan, namely the SMS and LTIP.

Determination of 2016 Annual Bonus

Management delivered a good performance in the year to 30 September 2016, strengthening our brands and market footprint and delivering strong cash conversion. As a result, we are a stronger business and continued to deliver a 10 per cent increase in annual dividend.

The annual bonus payment, determined with reference to performance over the financial year ending 30 September 2016, is 72 per cent of maximum opportunity (2015: 80 per cent). The Committee believes this to be an appropriate reflection of the performance and progress made through the year.

DIRECTORS' REMUNERATION REPORT

CONTINUED

Performance against individual measures is set out below:

Performance target	Assessment	Maximum percentage of bonus	Actual percentage of bonus
Adjusted EPS growth (constant currency) ^{KPI}	Performance is measured based on EPS growth at constant currency. Increases in top line revenues together with a strong focus on cost and cash opportunities provided growth in EPS of 12.0 per cent. This delivered an 83 per cent achievement against a cut in of 7.0 per cent and a maximum target of 13.0 per cent.	35	29
Cash conversion ^{KPI}	Performance is measured as cash flow as a percentage of adjusted operating profit. Instilling a more cost conscious culture, efficiently managing our cost base and our commitment to capital discipline enabled cash conversion of 95 per cent. This delivered a 100 per cent achievement against a cut in of 80.0 per cent and a maximum target of 92.0 per cent.	25	25
Volume growth in Growth Brands ^{KPI}	Performance is measured based on volume growth of our Growth Brands relative to the market. Consistent focus on developing our Growth Brands, through investments, migrations and choices in market, has enabled us to further optimise our brand portfolio and build the strength of our key brand assets. Growth Brand volumes increased by 5.1 per cent relative to the market. This delivered a 60 per cent achievement against a cut in of parity with the external market and a maximum target of 8.5 per cent out performance.	15	9
Non-financial	Non-financial measures consisted of a market share target. We showed strong results across a broad spread of markets, with resilience in Returns markets and positive performance across Growth markets. However, the threshold target was not met.	15	0
Individual objectives	Executive Directors have delivered strongly against their individual objectives, particularly in the successful integration of the acquired USA assets.	10	9
Achievement of bonus for 2016		100	72

KPI Key Performance Indicator used to measure the progress we make in delivering our strategy – see how we measure our performance on page 6 and 7.

No element of the annual bonus is guaranteed. Annual bonuses for Executive Directors and certain key executives are subject to malus provisions before payment and claw back during the three years following the end of the financial year in which they are earned. Claw back may be applied in the event of gross misconduct by the employee or misstatement of results where this had the effect of increasing the level of bonus that would otherwise have been paid.

Share Matching Scheme

The final SMS awards, at director level, were made to Alison Cooper and Matthew Phillips in February 2014 and will vest in February 2017 based on EPS and net revenue growth performance conditions measured over the three financial years to 30 September 2016, as set out below. Under the SMS Directors could invest up to their target bonus in shares which were, subject to the achievement of the performance conditions, matched at the end of a three-year period and dividend equivalents applied to any shares vesting.

	Performance target	Actual performance	Threshold vesting of award	Maximum percentage of award	Actual percentage vesting
Adjusted EPS ^{KPI}	5% – 10% average annual growth	5.8%	12.5%	50%	18.5%
Net revenue growth ^{KPI,1}	3% – 7% average annual growth	1.6%	12.5%	50%	0%
Achievement of SMS for 2016					18.5%

1. The target range of 3 to 7% includes the discretionary increase made by the Committee in consideration of the one off impact of the acquisition of US assets.

Long Term Incentive Plan

LTIP awards made to Alison Cooper, Oliver Tant and Matthew Phillips in November 2013 will vest in November 2016 based on performance conditions, measured over the three years, as set out below:

	Performance target	Actual performance	Threshold vesting of award	Maximum percentage of award	Actual percentage of award
TSR against comparator group ²	Threshold at median of peer group Pro rata between median and upper quartile Maximum above upper quartile	90% of companies exceeded	12.5%	50%	50%
Adjusted EPS ^{KPI}	5% – 10% average annual growth	5.8%	6.25%	25%	9.3%
Net revenue growth ^{KPI,1}	3% – 7% average annual growth	1.6%	6.25%	25%	0%
Achievement of LTIP for 2016					59.3%

1. The target range of 3 to 7% includes the discretionary increase made by the Committee in consideration of the one off impact of the acquisition of US assets.

2. The companies comprising the comparator group are:

Anheuser-Busch InBev NV	Altria Group Inc	Associated British Foods PLC	AstraZeneca PLC	British American Tobacco PLC
Burberry Group PLC	BT Group PLC	Capita PLC	Carlsberg A/S	Carnival PLC
Compass Group PLC	Diageo PLC	Experian Finance PLC	GlaxoSmithkline PLC	Heineken NV
International Consolidated Airlines Group SA	InterContinental Hotels Group PLC	ITV PLC	Japan Tobacco Inc.	Kingfisher PLC
Marks & Spencer Group PLC	Next PLC	Pearson PLC	Philip Morris International Inc	Pernod Ricard SA
Reckitt Benckiser Group PLC	Reed Elsevier PLC	Reynolds American	Rolls-Royce PLC	SAB Miller PLC
J Sainsbury PLC	Smith & Nephew PLC	Shire PLC	Tate & Lyle PLC	Tesco PLC
Unilever PLC	Vodafone Group PLC	Whitbread PLC	WM Morrison Supermarkets PLC	

KPI Key Performance Indicator used to measure the progress we make in delivering our strategy – see how we measure our performance on pages 6 and 7.

The TSR calculations, performed independently by Alithos Limited, use the share prices of each comparator group company, averaged over a period of three months, to determine the initial and closing prices. Dividend payments are recognised on the date shares are declared ex-dividend. The Committee considers this method gives a fairer and less volatile result as improved performance has to be sustained for several weeks before it effectively impacts on the TSR calculations. PwC performs agreed upon procedures in respect of the EPS and net revenue growth performance conditions for both the SMS and LTIP performance assessments.

Sharesave Plan

We believe that our Sharesave Plan is a valuable way of aligning the interests of a wide group of employees with those of our long-term shareholders. Annually we offer as many employees as practicable, together with our Executive Directors, the opportunity to join the Sharesave Plan. Options over shares are offered at a discount of up to 20 per cent of the closing mid-market price of our shares on the day prior to invitation. The Sharesave Plan allows participants to save up to £250 per month over a period of three years, and in the UK only three or, for grants in 2013 and earlier, five years, and then exercise their option over shares. In common with most plans of this type, no performance conditions are applied. In the financial year ending 30 September 2016, Matthew Phillips had a Sharesave plan vesting (2015: Alison Cooper and Matthew Phillips) and details are included in the single total figure table on page 63.

Total Pension Entitlements (Audited)

The Executive Directors who served during the financial year are all members of the Imperial Tobacco Pension Fund (the Fund), which is the principal retirement benefit scheme operated by the Group in the UK.

Members who joined before 1 October 2010 are included in the defined benefit section of the Fund. For members who joined prior to 1 April 2002 the Fund is largely non-contributory with a normal retirement age of 60. New members of the Fund after 30 September 2010 accrue pension benefits in the Fund on a defined contribution basis, in the defined contribution section of the Fund.

Alison Cooper and Matthew Phillips are members of the pre-April 2002 section of the defined benefit section of the Fund. Prior to 6 April 2006 they accrued a non-contributory pension at the rate of 1/47th of their pensionable salary limited by the effect of HMRC's earnings cap. Although HMRC removed this cap from 6 April 2006, the Fund did not dis-apply it in respect of past pensionable service and maintained its own earnings cap going forward. For pensionable service from 6 April 2006 onwards Alison Cooper and Matthew Phillips accrue an additional pension at a rate of 1/60th of their pensionable salary in excess of the Fund's earnings cap. They pay member contributions at the rate of 5 per cent on their pensionable salary in excess of the Fund's earnings cap. Both Alison Cooper and Matthew Phillips receive a salary supplement of 12 per cent of their pensionable salary in excess of the Fund's earnings cap.

Oliver Tant is also in receipt of a salary supplement equal to 12 per cent of his basic salary. He is a member of the defined contribution section of the Fund. In accordance with the Rules of the Fund he opted to limit his total contributions (member and Company) to a level which would not result in him incurring an Annual Allowance charge. Consequently, any Company contributions that otherwise would have been paid to the Fund on his behalf have instead been paid to him as a salary supplement. Oliver Tant registered for Fixed Protection 2016 and opted-out of contributory membership of the defined contribution section of the Fund with effect from 1 April 2016. No pension contributions have been paid to the Fund by or in respect of him since this date. Instead the Company has paid him an additional salary supplement of 14 per cent of his salary, increasing his total salary supplement from 1 April 2016 to 26 per cent.

The salary supplements have been calculated by the independent actuaries to reflect the value of the benefits of which they are in lieu and are discounted for early payment and for employer's national insurance contributions. The supplements are non-compensatory and non-pensionable.

DIRECTORS' REMUNERATION REPORT

CONTINUED

Matthew Phillips elected to use the Fund's scheme pays facility to settle his Annual Allowance charge for the 2011/12, 2012/13 and 2013/14 tax years. His accrued pension was reduced by £11,565.78 a year (including revaluation) to offset these Annual Allowance charge payments. This reduction to pension is reflected in the accrued pension figure as at 30 September 2016 (it is also reflected in the value of the benefits as at 30 September 2016).

The following table provides the information required by Schedule 8 of the Regulations and gives details for each Executive Director of:

- the annual accrued pension payable on retirement calculated as if he/she had left service at the year-end;
- the normal retirement ages;
- the value of the pension benefits at the start and end of the year, as calculated in accordance with the Regulations;
- the value of the pension benefits earned over the year, excluding any director's contributions and any increases for inflation, calculated in accordance with the Regulations; and
- any payments in lieu of retirement benefits.

None of the Executive Directors has made additional voluntary contributions.

Executive Directors' Pension Disclosures (Audited)

£'000	Age at 30/09/2016	Pensionable service at 30/09/2016	Accrued pension		Single figure numbers			Extra information to be disclosed under 2013 Directors' Remuneration Regulations		
			01/10/2015	30/9/2016	Payment in lieu of retirement benefits (i.e. pension supplement) £'000	Value x 20 over year (net of director's contributions) £'000	Total pension benefits £'000	Normal retirement age	Value x 20 at start of year £'000	Value x 20 at end of year £'000
Alison Cooper	50	17	192	219	98	492	590	60	3,840	4,380
Matthew Phillips	45	16	98	118	40	394	434	60	1,960	2,360
Oliver Tant ¹	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

1. Oliver Tant is a member of the defined contribution section of the Imperial Tobacco Pension Fund. He received a pension contribution into the defined contribution section of £30,000 (made up of £5,055.72 Company contribution plus £24,944.28 in respect of a salary sacrifice by Mr Tant in lieu of his personal contribution). In addition, a salary supplement of £77,868, representing 12 per cent of Mr Tant's basic salary, was paid to him together with an additional supplement of £85,790 in lieu of Company pension contributions which were not made to the Imperial Tobacco Pension Fund in order to maintain Mr Tant's total contributions within the Annual Allowance for pension savings). He registered for Fixed Protection 2016 and as a result opted-out of contributory membership of the Fund and ceased pension contributions with effect from 1 April 2016. Since this date Mr Tant has received an additional 14 per cent salary supplement in lieu of the Company contributions he would have received had he not registered for protection and opted out. The 14 per cent salary supplement is included in the total of £85,790.

Statement of Change in Pay of Chief Executive Compared With Other Employees

	Chief Executive to 30 September 2016	Percentage change (2016 vs 2015)	All Employees ¹ Percentage change (2016 vs 2015)
Salary	£1,020,000	5.7	3.9
Benefits	£16,635	0.9	4.5
Bonus	£1,468,800	(4.9)	(4.7)

1. Based on members of our Corporate Management Group. This group has been chosen as it represents a good proxy for employees across the Group but is not overly influenced by local custom, hyperinflation in some jurisdictions etc.

Relative Importance of Spend on Pay

The table below shows the expenditure and percentage change in overall spend on employee remuneration and dividends.

£million unless otherwise stated	2016	2015	Percentage change
Overall expenditure on pay ¹	826	811	1.8
Dividend paid in the year	1,386	1,259	10.1

1. Excludes employers' social security costs.

Share Interests and Incentives (Audited)

All Executive Directors who served in the financial year currently meet the Company's shareholding policy by either holding shares in excess of their requirement or being within five years of appointment. Current shareholdings are summarised in the following table:

	Shares held		Conditional awards and options held			Shareholding required (% salary)	Current shareholding (% salary) ¹	Requirement met ²
	Owned outright	Vested but subject to holding period	Unvested and subject to performance conditions	Unvested and subject to continued employment	Vested but not exercised			
Executive Directors								
Alison Cooper	162,111	18,341	329,362	354	–	300 ³	703	Yes
Oliver Tant	829	7,958	133,927	441	–	300	54	In role for less than five years
Matthew Phillips	43,960	5,397	108,532	212 ⁴	–	300	363	Yes
Non-Executive Directors								
Mark Williamson	10,055	–	–	–	–	–	–	N/A
Ken Burnett ⁵	2,772	–	–	–	–	–	–	N/A
Therese Esperdy	–	–	–	–	–	–	–	N/A
David Haines	1,029	–	–	–	–	–	–	N/A
Michael Herlihy	5,307	–	–	–	–	–	–	N/A
Steven Stanbrook ⁶	18,059	–	–	–	–	–	–	N/A
Karen Witts	471	–	–	–	–	–	–	N/A
Malcolm Wyman	3,951	–	–	–	–	–	–	N/A

1. Based on a share price of £39.735 being the closing price on 30 September 2016.

2. Non-Executive Directors do not have a shareholding requirement but are required to invest a minimum percentage of their fees in Imperial Brands PLC shares which they are required to retain for the duration of their appointment.

3. Under the proposed policy this is to be increased to 400 per cent.

4. During the year Matthew Phillips exercised 195 shares under the international sharesave plan at an option price of £18.40.

5. Ken Burnett retired from the Board on 3 February 2016.

6. Steven Stanbrook holds his shares in the form of American Depositary Receipts.

There have been no changes to the above holdings since the year end.

Variable Award Grants Made During the Year (Audited)

In line with our remuneration policy in force from 2014, no further awards to Executive Directors under the SMS will be made and the historic award levels have been consolidated into the Group's LTIP.

It is intended that LTIP awards will be made in February each year in order for any change in policy to be considered by shareholders immediately prior to grant.

The resulting number of LTIP shares and the associated performance conditions are set out below.

	Number of nil cost options	Face value ¹	Amount of base salary	End of performance period	Threshold vesting	Weighting (of award)	Performance condition ^{2,3}
Alison Cooper	100,464	£3,570,000	350%	30 September 2018	25%	50%	3 year adjusted EPS growth
					25%	30%	3 year net revenue growth
					25%	20%	TSR relative to bespoke comparator group
Oliver Tant	45,652	£1,622,250	250%	30 September 2018	25%	50%	3 year adjusted EPS growth
					25%	30%	3 year net revenue growth
					25%	20%	TSR relative to bespoke comparator group
Matthew Phillips	38,043	£1,351,875	250%	30 September 2018	25%	50%	3 year adjusted EPS growth
					25%	30%	3 year net revenue growth
					25%	20%	TSR relative to bespoke comparator group

1. Valued using the share price at the date of grant (15 February 2016) being £35.535 per share.

2. Vesting occurs as per the vesting schedule below.

3. Key performance indicators used to measure the progress we make in delivering our strategy – see how we measure our performance on page 12.

DIRECTORS' REMUNERATION REPORT

CONTINUED

Performance Criterion – EPS Element

This criterion is used for 50 per cent of the LTIP award. Vesting of awards on this element would occur as per the following vesting schedule.

Compound annual adjusted EPS growth ¹	Shares vesting (as a percentage of element)
Less than 5% per annum	nil
5% per annum	25%
5% to 10% per annum	Between 25% and 100% (pro rata)
10% per annum or higher	100%

1. The target range of 5 to 10% reflects the exceptional uplift to our normal range of 3 to 8% in consideration of the part-year impact of the acquisition of USA assets.

Performance Criterion – Net Revenue Growth Element

The net revenue growth criterion is used for 30 per cent of the LTIP award. Vesting of awards on this element would occur as per the following vesting schedule.

Compound annual growth in net revenue ¹	Shares vesting (as a percentage of element)
Less than 3% per annum	nil
3% per annum	25%
3% to 6% per annum	Between 25% and 100% (pro rata)
6% per annum or higher	100%

1. The target range of 3 to 6% reflects the exceptional uplift to our normal range of 1 to 4% in consideration of the part-year impact of the acquisition of USA assets.

Performance Criterion – TSR Element

The performance criterion for the TSR element is based on a single comparator group of companies across a broadly defined consumer goods sector and is applied to 20 per cent of the LTIP award.

The companies within the comparator group and the vesting schedule remain unchanged from the grant made in November 2013 detailed on page 65.

Under the rules of the LTIP, should the Company be acquired the performance period would end on the date of acquisition. Any outstanding awards would vest on a time pro rata basis subject to the achievement of the applicable performance criteria.

Awards With No Performance Conditions Made During the Year (Audited)

The deferred shares awarded during the year are set out below. No Executive Directors were granted Sharesave options during the year.

	Number of deferred shares	Face value ¹	Portion of net bonus	End of deferral period
Alison Cooper	11,594	£405,058	50%	30 September 2018
Oliver Tant	7,569	£264,437	50%	30 September 2018
Matthew Phillips	5,292	£184,886	50%	30 September 2018

1. Valued using the share price at the date of purchase (16 December 2015) being £34.93689 per share.

REMUNERATION DECISIONS TAKEN IN 2015/16

Salary

The Committee sets base salaries having regard to individual performance, changes to the individual's role and market data for each position based on several comparator groups which reflect the Company's size, sector and global reach. Consideration is given to the effect any amendment to an individual's base salary would have on their total remuneration package. Base salary is the only element of the package used to determine pensionable earnings.

An increase of 3 per cent, in line with other UK management, was awarded to Alison Cooper and Matthew Phillips.

An above inflation increase has been awarded to Oliver Tant to reflect both his increased responsibilities in an expanded role incorporating Group Procurement and Group Information Systems, and the competitive CFO market.

There was no increase in Non-Executive Directors' fees, with the exception of the Chairman whose fee was brought closer to market levels through an increase from £500,000 to £525,000, however, this will not be reviewed again for a period of two years.

	Salary 2015/16	Salary 2016/17	Percentage Change
Alison Cooper	£1,020,000	£1,051,000	3.0
Oliver Tant	£649,000	£700,000	7.9
Matthew Phillips	£541,000	£557,000	3.0

Annual Bonus

Our shareholders and other stakeholders place significant weight on our annual performance. We, therefore, think it is appropriate to have a major element of Executive Directors' remuneration targeted at incentivising delivery of the Group's annual objectives and enhancing performance against key financial and non-financial targets. The maximum bonus opportunity for all Executive Directors remains unchanged at 200 per cent.

Fifty per cent of net bonus paid will be in the form of the Group's shares deferred for a three-year period; the remaining 50 per cent will be paid in cash.

For the next financial year the performance measures have been set out in the table below:

	Performance target	Maximum of bonus
Adjusted EPS growth	Commercially confidential	25%
Cash conversion	Commercially confidential	25%
Market share	Share growth in core markets	20%
Revenue growth in Asset Brands	Commercially confidential	15%
Individual objectives	Commercially confidential	15%

These targets have been reweighted to reflect the Group's revised strategic focus for the year, with an increased weighting on market share and top line growth and a slightly reduced focus on EPS.

At this point, the above performance targets are considered commercially confidential but, to the extent that any bonuses are paid, further details will be provided retrospectively in the 2017 Annual Report. The Committee is not of the view that such targets will necessarily always be confidential but will review this on a year-by-year basis.

Share Plan Awards

Under the revised remuneration policy an increase in LTIP opportunity is proposed in order to ensure that the management team has the opportunity to earn comparative rewards for delivery of strong performance. This increase, equivalent to 100 per cent of salary, reduces the current gap in total remuneration opportunity between Imperial Brands and its peers.

	Revised maximum opportunity – percentage of salary	Former maximum opportunity – percentage of salary
Alison Cooper	450	350
Oliver Tant	350	250
Matthew Phillips	350	250

DIRECTORS' REMUNERATION REPORT

CONTINUED

February 2017 LTIP grant

Following feedback received during the consultation with shareholders the Committee has made changes to the structure of the 2017 LTIP.

These are:

- an increase to the maximum target relating to EPS growth, moving from a range of 3 to 8 per cent growth to a new range of 3 to 9 per cent; and
- introduction of a cash conversion measure with a weighting of 20 per cent (replacing part of the weighting on EPS).

A number of our investors indicated they regard Return on Invested Capital (ROIC) as a good measure of our performance. Whilst a ROIC measure has not been introduced, the Committee pays close attention to the level of return delivered and will take ROIC into account in confirming future vesting.

Performance criteria	Weighting in LTIP
Adjusted EPS growth	30%
Net revenue growth	30%
TSR	20%
Cash conversion	20%

When setting the performance criteria the Committee takes account of the Group's long-term plans and analysts' forecasts.

Performance Criterion – EPS Element

This criterion is used for 30 per cent of the LTIP awards. Vesting of awards on this element would occur in accordance with a vesting schedule agreed by the Committee on an annual basis. The proposed vesting schedule is:

Compound annual adjusted EPS growth	Shares vesting (as a percentage of element)
Less than 3% per annum	nil
3% per annum	25%
3% to 9% per annum	Between 25% and 100% (pro rata)
9% per annum or higher	100%

Performance Criterion – Net Revenue Growth Element

This criterion will be used for 30 per cent of the LTIP awards. Vesting of awards on this element would occur as per the vesting schedule below:

Compound annual net revenue growth	Shares vesting (as a percentage of element)
Less than 1% per annum	nil
1% per annum	25%
1% to 4% per annum	Between 25% and 100% (pro rata)
4% per annum or higher	100%

Performance Criterion – TSR Element

The performance criterion for the TSR element will be based on a single comparator group including 40 companies across a broadly defined consumer goods sector and will be applied to 20 per cent of the LTIP.

The companies within the comparator group remain unchanged, as detailed on page 65.

Vesting of awards on this element would occur as per the vesting schedule below:

Relative TSR performance	Shares vesting (as a percentage of element)
Below median of peer group	nil
At median of peer group	25%
Between median and upper quartile	Between 25% and 100% (pro rata)
Above upper quartile	100%

Performance Criterion – Cash Conversion Element

This criterion is used for 20 per cent of the LTIP awards. Vesting of awards on this element would occur in accordance with a vesting schedule agreed by the Committee on an annual basis. The proposed vesting schedule:

Average annual cash conversion	Shares vesting (as a percentage of element)
Less than 85% per annum	nil
85% per annum	25%
85% to 92% per annum	Between 25% and 100% (pro rata)
92% per annum or higher	100%

Under the rules of the LTIP, should the Company be acquired the performance period would end on the date of acquisition. Any outstanding awards would vest on a time pro rata basis subject to the achievement of the applicable performance criteria.

Voting on the Remuneration Report at the 2016 AGM

At the 2016 AGM we received a strong vote in favour of our remuneration report, with a small number of shareholders commenting on various aspects of our remuneration. We have sought to discuss these in more detail as part of the recent consultation with shareholders and where appropriate addressed their concerns within the proposed remuneration policy. We also received a strong vote in favour of our remuneration policy at our 2015 AGM although a small number of shareholders expressed concern in respect of various aspects including the expectation that incentive targets should be adjusted for our USA acquisition. These were addressed by the Committee using its discretion to increase in-flight LTIP targets.

Votes cast by proxy and at the meeting in respect of the Directors' remuneration were as follows:

Resolution	Votes for including discretionary votes	Percentage for	Votes against	Percentage against	Total votes cast excluding votes withheld	Votes withheld	Total votes cast including votes withheld
Directors' Remuneration Report (2016 AGM)	693,449,508	94.8	38,042,663	5.2	731,492,171	14,414,282	745,906,453
Directors' Remuneration Policy (2015 AGM)	704,892,593	93.6	48,447,661	6.4	753,340,254	9,328,030	762,668,284

Votes withheld are not included in the final figures as they are not recognised as a vote in law.

Advice Provided to the Committee

New Bridge Street (NBS) is retained, having been appointed following a tendering process, by the Committee as its principal, and only material, external advisor. NBS advises on all aspects of our remuneration policy and practice and reviews our structures against corporate governance best practice. NBS also presented a review of developments in UK corporate governance, remuneration developments and reporting regulations to keep Committee members up-to-date with new developments and evolving best practice.

NBS is a founder member of the Remuneration Consultants' Group and complies with its Code of Conduct which sets out guidelines to ensure that its advice is independent and free of undue influence. NBS' parent companies, Aon Hewitt Limited and Aon plc, provide other human resources and insurance services respectively to the Group. Having reviewed the structures in place to ensure the independence of NBS' advice to the Committee, it is satisfied that the other work provided by the wider Aon group does not impact on NBS' independence.

During the year NBS was paid time based fees of £145,000.

Other companies which provided advice to the Committee are as follows:

- Alithos Limited undertakes total shareholder return (TSR) calculations and provided advice on all TSR related matters. During the year it was paid a fixed fee of £19,500. Alithos Limited provided no other services to the Group;
- Allen & Overy LLP is available to provide legal advice to the Committee as and when required. It was not used for remuneration-related advice during the financial year. Allen & Overy LLP also provided other legal services to the Group;
- Pinsent Masons LLP provided legal advice in respect of the operation of the Group's employee share plans;
- PricewaterhouseCoopers LLP (PwC), our auditors, perform agreed upon procedures on earnings per share (EPS) and net revenue calculations used in relation to our employee share plans' performance criteria. During the financial year PwC was paid a fixed fee of £1,850 in respect of services to the Committee; and
- Towers Watson provided market pay data to ensure the consistent application of our remuneration policy for executives. During the year it was paid time based fees of £62,000 for these services. Towers Watson also provided actuarial services to the Group.

All of these advisors were appointed by the Committee which remains satisfied that the provision of those other services in no way compromises their independence. They are all paid on the basis of actual work performed rather than on a fixed fee.

The Group Human Resources Director and the Group Reward and Capability Director also attended and provided internal support and advice on market and regulatory developments in remuneration practice and on our employee share plans. Their attendance ensured the Committee was kept fully abreast of pay policies throughout the Group, which it then takes into account when determining the remuneration of the Executive Directors and our most senior executives.

DIRECTORS' REMUNERATION REPORT

CONTINUED

OTHER INFORMATION

Our middle market share price at the close of business on 30 September 2016, being the last trading day of the financial year, was £39.735 and the range of the middle market price during the year was £33.23 to £41.54.

Full details of the Directors' share interests are available for inspection in the Register of Directors' Interests at our registered office.

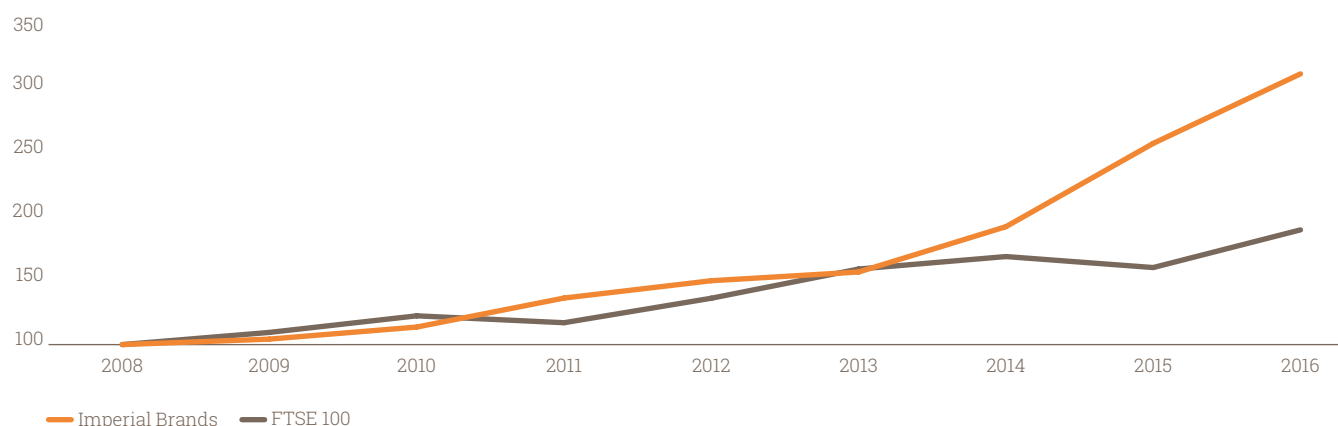
Award Dates

Our policy is to grant awards under all our employee share plans on predetermined dates based on an annual cycle.

Review of Past Performance

The chart below shows the value of £100 invested in the Company on 1 October 2008 compared with the value of £100 invested in the FTSE 100 Index for each of our financial year ends to 30 September 2016. We have chosen the FTSE 100 Index as it provides the most appropriate and widely recognised index for benchmarking our corporate performance over an eight-year period.

Total Return Indices – Imperial Brands and FTSE 100



Change in Chief Executive Remuneration

	2016 Alison Cooper	2015 Alison Cooper	2014 Alison Cooper	2013 Alison Cooper	2012 Alison Cooper ¹	2011 Alison Cooper ¹	2010 Alison Cooper ¹	2010 Gareth Davis ^{2,3}	2009 Gareth Davis
Total remuneration £'000	5,537	3,637	2,686	2,011	2,793	2,737	1,347	5,453	5,099
Annual Bonus as a percentage of maximum	72	80	69	34	51.2	33.1	84.7	84.7	85.2
Shares vesting as a percentage of maximum	45.7	15.8	5.8	nil	58.0	71.6	80.8	46.93	74.5

1. Total remuneration includes value of share plans vesting that were granted prior to appointment as Chief Executive.

2. Total remuneration includes value of share plans vesting on retirement.

3. Based on performance conditions applicable on date of retirement.

Operating Executive (excluding Executive Directors)

£'000	2016	2015
Base salary	2,402	2,221
Benefits	257	189
Pension salary supplement	263	261
Bonus	2,798	2,572
LTIP annual vesting ¹	1,838	402
SMS annual vesting ¹	266	nil
	7,824	5,645

1. Share plans vesting represent the value of SMS and LTIP awards where the performance period ends in the year and are based on a share price of £40.1689 being the three-month average to 30 September 2016.

Note: aggregate remuneration paid to or receivable by Executive Directors, Non-Executive Directors and members of the Operating Executive for qualifying services in accordance with IAS 24, which includes National Insurance and similar charges, was £20,959,617 (2015: £14,526,087).

KEY MANAGEMENT¹ COMPENSATION FOR THE YEAR ENDED 30 SEPTEMBER 2016 (AUDITED)

£'000	2016	2015
Short-term employee benefits	12,340	11,681
Post-employment benefits	1,313	1,182
Other long-term benefits	–	–
Termination benefits	–	–
Share-based payment (in accordance with IAS 24)	3,598	2,722
	17,251	15,585

1. Key management includes Directors, members of the OPEX and the Company Secretary.

Employee Benefit Trusts

Our policy remains to satisfy options and awards under our employee share plans from either market purchased ordinary shares or ordinary shares held in treasury, distributed through our employee benefit trusts: The Imperial Tobacco Group PLC Employee and Executive Benefit Trust (the Executive Trust) and the Imperial Tobacco Group PLC 2001 Employee Benefit Trust (the 2001 Trust) (together the Employee Benefit Trusts).

As at 30 September 2016, we held 77,289,137 ordinary shares in treasury which can be used to satisfy options and awards under our employee share plans either directly or by gifting them to the Employee Benefit Trusts.

Options and awards may also be satisfied by the issue of new ordinary shares.

Details of the ordinary shares held by the Employee Benefit Trusts are as follows:

	Balance at 01/10/2015	Acquired during year	Distributed during year	Balance at 30/09/2016	Ordinary shares under award at 30/09/2016	Surplus/ (shortfall)
Executive Trust	675,463	0	(37,647)	637,816	604,485	33,331
2001 Trust	2,489,892	1,620,000	(1,258,243)	2,851,649	3,833,972	(982,323)

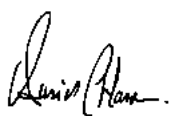
Share Plan Flow Rates

The Trust Deeds of the Employee Benefit Trusts and the rules of each of our employee share plans contain provisions limiting options and awards to 5 per cent of issued share capital in five years and 10 per cent in 10 years for all employee share plans, with an additional restriction to 5 per cent in 10 years for executive share plans. Currently, an aggregate total of 0.4 per cent of the Company's issued share capital (including shares held in treasury) is subject to options and awards under the Group's executive and all employee share plans.

Summary of Options and Awards Granted

Limit on awards	Cumulative options and awards granted as a percentage of issued share capital (including those held in treasury)	Options and awards granted during the year as a percentage of issued share capital (including those held in treasury)
10% in 10 years	1.8	0.1
5% in 5 years	0.8	0.1
5% in 10 years (executive plans)	1.3	0.1

For the Board



David Haines

Chairman of the Remuneration Committee

8 November 2016

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PARENT COMPANY FINANCIAL STATEMENTS

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REPORT ON THE GROUP FINANCIAL STATEMENTS

OUR OPINION

In our opinion, Imperial Brands PLC's group financial statements (the financial statements):

- give a true and fair view of the state of the Group's affairs as at 30 September 2016 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

WHAT WE HAVE AUDITED

The financial statements, included within the Annual Report and Accounts (the Annual Report), comprise:

- The Consolidated Balance Sheet as at 30 September 2016;
- The Consolidated Income Statement and Consolidated Statement of Comprehensive Income for the year then ended;
- The Consolidated Cash Flow Statement for the year then ended;
- The Consolidated Statement of Changes in Equity for the year then ended; and
- The notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is IFRSs as adopted by the European Union, and applicable law.

OUR AUDIT APPROACH

Context

The context for our audit was set by Imperial Brands PLC's major activities in 2016. The principal development which affected our audit was the full year impact of the prior year acquisition in the USA, as a result of which we consolidated our component team in the USA into a single location.

Overview



- Overall group materiality: £123 million which represents approximately 4 per cent of adjusted group profit before taxation.
- Following our assessment of the risk of material misstatement we selected 22 reporting entities for full scope audits which represent the principal business units.
- We conducted full scope audit work at 22 of these reporting entities which included significant operations in the UK, Germany, Netherlands, Spain, USA, Australia, France and five other locations. We also conducted specific audit procedures in Russia.
- In addition certain central reporting entities and group functions, including those covering treasury, taxation and retirement benefits, and the Parent Company were subject to a full scope audit.
- Goodwill and intangible assets impairment assessment.
- Accounting for restructuring provisions.
- Tax accounting and the level of tax provisions held against risks.

The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & Ireland)).

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls and fraud in revenue recognition, including evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as "areas of focus" in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

AREA OF FOCUS

Goodwill and intangible assets impairment assessment

We focused on this area because the determination of whether elements of goodwill and intangible assets are impaired involves complex and subjective judgements by the Directors about the future results of the relevant parts of the business.

At 30 September 2016 the Group had £12,098m of goodwill and £594m of intangible assets with indefinite lives and reasonable headroom in the majority of the Group's groupings of cash generating units (CGU's).

We focused on the valuation of the Growth Markets reporting segment (£2,269m of goodwill and intangible assets with indefinite lives). Growth Markets is made up of a number of operating segments and individual CGU's, including the Drive Growth CGU grouping and the Other Premium Cigar CGU grouping. For both of these goodwill is analysed separately and management's assessment indicated low headroom (£210m and £100m respectively).

For the Drive Growth CGU grouping we focused on the valuation of both the Russian and Italian businesses, which represent the most material parts of this CGU grouping. In particular we considered the robustness of short term growth included in the impairment models, together with discount rates and long term growth rates.

For the Other Premium Cigar CGU grouping the valuation is dependent on continuing steady profit growth. As such we focused on the assumptions the Directors made about the growth rates in the context of constraints which could reasonably impact their ability to meet forecast.

Accounting for restructuring provisions

The group has continued in its significant multi-year cost optimisation programme including factory closures, organisational rationalisation and the establishment of shared service centres. The group also continues to integrate its US businesses. Management has indicated they expect these programmes will require several years to complete.

In 2016 the charge in the Consolidated Income Statement relating to these programmes was £307m and there is a total restructuring provision held on the Consolidated Balance Sheet of £304m. The restructuring charge is separately identified on the face of the income statement and excluded from the non-GAAP earnings measure Adjusted Operating Profit.

The recognition of restructuring costs requires judgement to estimate the value and timing of net economic outflows and the extent to which the Group is externally committed. The presentation in the financial statements also requires consideration of whether the amounts included in the charge are fair and whether their separate presentation is helpful in understanding financial performance.

HOW OUR AUDIT ADDRESSED THE AREA OF FOCUS

We challenged the Directors' analysis around the key drivers of the cash flow forecasts including the ability to achieve sustained price increases, market size and market share. We also evaluated the appropriateness of the key assumptions including discount rates, short-term and long-term growth rates and performed sensitivities across the reporting segments.

For the Russian and Italian businesses we considered the impact of investment in marketing programmes over the medium-term forecast, together with the broader potential to grow profits in the longer term. We also considered the impact of current and expected legislative and duty changes on the business and considered the accuracy of management's current year forecasts.

For the Other Premium Cigar CGU, we evaluated the reasonableness of the Directors' forecast by challenging key assumptions about growth strategies including supply constraints, regulatory changes in key markets, opportunities in new markets and changes in the relationship between the USA and Cuba. We also considered the accuracy of management's current year forecasts.

As a result of our work we determined that the judgement by management that no impairment was required in respect of Drive Growth and Other Premium Cigar was reasonable. We note however that goodwill and intangibles held by these businesses remain sensitive to changes in key assumptions. In particular, for Drive Growth, a failure to achieve the growth objectives for planned market initiatives could give rise to an impairment. Given this management has disclosed relevant sensitivities (see note 11).

The cost optimisation programme operates predominantly through a series of distinct projects incorporating centralised governance and project management supporting local execution. This process gives rise to a series of specific restructuring charges being booked either at head office level or in individual component businesses. We conducted audit testing through our group team on centrally held charges and through local testing of charges at component businesses. Because the total restructuring cost also included some costs incurred at business units not included in our full scope audits the Group team tested these on a sample basis.

Using this approach we tested the valuation, accuracy and completeness of the individual restructuring costs. These primarily consisted of redundancies and related costs, consulting and professional fees and asset impairments. We found no material exceptions in our testing.

The principal areas of judgement underlying this work related to:

- the estimation of uncertain liabilities and impairment losses,
- the extent to which costs incurred on projects were sufficiently distinct and incremental to warrant inclusion in the restructuring charge and,
- projects which did not fit readily into the major elements of the programme but were considered by management to be appropriate for inclusion within the overall restructuring charge.

We challenged management over the basis for their judgements in these areas and determined that the amounts included in the charge were reasonable.

We also considered the merits of separate disclosure of the restructuring charge and discussed this with management and the audit committee. We concurred with their conclusion that the extensive scale and cost of the programme, its duration over several years and the level of centralised group wide control and board focus, indicated that separate disclosure was acceptable.

AREA OF FOCUS

Tax accounting and the level of tax provisions held against risks

There are a number of significant judgements involved in the determination of tax balances, specifically in relation to the recognition of tax losses and the assessment of deferred taxation liabilities in relation to the distribution of reserves held in overseas subsidiaries. The group also has a number of uncertain tax positions in relation to which management apply judgement in setting provisions.

Given the number of judgements involved and the complexities of dealing with tax rules and regulations in numerous jurisdictions, this was an area of focus for us.

HOW OUR AUDIT ADDRESSED THE AREA OF FOCUS

In the calculation of deferred taxes, we assessed the adequacy of tax loss recognition and the level of provision established in relation to a number of uncertain tax positions primarily in Europe including the challenge from the French tax authorities in relation to Altadis Distribution France. We determined that the position adopted in the financial statements was reasonable based on our consideration of management's assessment of risks combined with their use of experts in support of their provision for uncertain tax outcomes. We also considered the reasonability of the tax losses recognised.

We considered the overall clarity of disclosure in relation to tax provisioning and the discussion of contingent liabilities including Altadis Distribution France and a more general assessment of cross border transfer pricing and determined that they were fair and proportionate.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

The group is structured along two business lines being Tobacco and Logistics. The group financial statements are a consolidation of 278 legal entities represented by 224 reporting entities, comprising the Group's operating businesses and centralised functions.

The group's accounting process is structured around a local or regional finance function for each of the territories in which the Group operates. These functions maintain their own accounting records and controls and report to the head office finance team in Bristol through an integrated consolidation system. In our view, due to their significance and/or risk characteristics, 22 of the 224 reporting entities, including the Logistics sub-group, required an audit of their complete financial information and we used component auditors from other PwC network firms, and other firms operating under our instruction, who are familiar with the local laws and regulations in each of these territories to perform this audit work. We also conducted specific audit procedures in Russia based on our assessment of the risk of misstatement and the scale of operations at this business unit.

Where the work was performed by component auditors, we determined the level of involvement we needed to have in the audit work at those functions to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the Group financial statements as a whole.

The group engagement team visits the component teams on a rotational basis. In the current year the Group team visited the USA, Morocco, Germany, Sweden and Greece, as well as in-scope UK reporting locations. Video conferences were held at least once with the component auditors and management of every in-scope reporting entity and those undertaking specific procedures to discuss the results of the work performed. In addition the Group engagement team reviewed working papers of the auditors of the more significant components.

We also met the other auditors used on the logistics sub-group and reviewed their working papers during the year.

The group consolidation, financial statement disclosures and a number of complex items were audited by the Group engagement team at the head office. These included derivative financial instruments, net investment hedge accounting, treasury, taxation and retirement benefits. The Parent Company was also subject to a full scope audit.

Taken together, the reporting entities and group functions where we performed audit work accounted for approximately 82 per cent of group revenues and in excess of 90 per cent of both group profit before tax and group adjusted profit before tax.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall group materiality	£123 million (2015: £115 million).
How we determined it	Approximately 4 per cent of adjusted group profit before taxation.
Rationale for benchmark applied	We believe that adjusted profit before tax is the primary measure used by shareholders and other users in assessing the performance of the Group, and that by excluding items it provides a clearer view on the performance of the underlying business.
Component materiality	For each component in our audit scope, we allocated a materiality that is less than our overall group materiality. The range of materiality allocated across components was for each component in our audit scope, we allocated a materiality that was less than our overall group materiality. The range of materiality allocated across components was between £10 million and £40 million for the trading entities and £80 million for the financing and treasury entity.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £10 million (2015: £10 million) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Going concern

Under the Listing Rules we are required to review the Directors' Statement, set out on page 19, in relation to going concern. We have nothing to report having performed our review.

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the Directors' Statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to.

As noted in the Directors' Statement, the Directors have concluded that it is appropriate to adopt the going concern basis in preparing the financial statements. The going concern basis presumes that the Group has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Group's ability to continue as a going concern.

OTHER REQUIRED REPORTING

CONSISTENCY OF OTHER INFORMATION

Companies Act 2006 reporting

In our opinion, the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

ISAs (UK & Ireland) reporting

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

– information in the Annual Report is:	We have no exceptions to report.
– materially inconsistent with the information in the audited financial statements; or	
– apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or	
– otherwise misleading.	
– the statement given by the Directors on page 33, in accordance with provision C.1.1 of the UK Corporate Governance Code (the "Code"), that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Group's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group acquired in the course of performing our audit.	We have no exceptions to report.
– the section of the Annual Report on pages 39 to 43, as required by provision C.3.8 of the Code, describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.	We have no exceptions to report.

THE DIRECTORS' ASSESSMENT OF THE PROSPECTS OF THE GROUP AND OF THE PRINCIPAL RISKS THAT WOULD THREATEN THE SOLVENCY OR LIQUIDITY OF THE GROUP

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to:

– the Directors' confirmation on page 32 of the Annual Report, in accordance with provision C.2.1 of the Code, that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.	We have nothing material to add or to draw attention to.
– the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.	We have nothing material to add or to draw attention to.
– the Directors' explanation on page 32 of the Annual Report, in accordance with provision C.2.2 of the Code, as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	We have nothing material to add or to draw attention to.

Under the Listing Rules we are required to review the Directors' statement that they have carried out a robust assessment of the principal risks facing the Group and the Directors' statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

ADEQUACY OF INFORMATION AND EXPLANATIONS RECEIVED

Under the Companies Act 2006 we are required to report to you if, in our opinion, we have not received all the information and explanations we require for our audit. We have no exceptions to report arising from this responsibility.

DIRECTORS' REMUNERATION

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

CORPORATE GOVERNANCE STATEMENT

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS AND THE AUDIT OUR RESPONSIBILITIES AND THOSE OF THE DIRECTORS

As explained more fully in the Statement of Directors' Responsibilities, 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 ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Parent Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

WHAT AN AUDIT OF FINANCIAL STATEMENTS INVOLVES

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 Group'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.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OTHER MATTER

We have reported separately on the Parent Company financial statements of Imperial Brands PLC for the year ended 30 September 2016 and on the information in the Directors' Remuneration Report that is described as having been audited.



John Maitland (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors

Bristol

8 November 2016

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 30 SEPTEMBER

£ million unless otherwise indicated	Notes	2016	2015
Revenue	3	27,634	25,289
Duty and similar items		(13,535)	(12,585)
Other cost of sales		(8,143)	(7,533)
Cost of sales		(21,678)	(20,118)
Gross profit		5,956	5,171
Distribution, advertising and selling costs		(2,070)	(1,857)
Acquisition costs		–	(40)
Amortisation of acquired intangibles	11	(1,005)	(697)
Restructuring costs	5	(307)	(328)
Other expenses		(345)	(261)
Administrative and other expenses		(1,657)	(1,326)
Operating profit	3	2,229	1,988
Investment income		634	948
Finance costs		(1,984)	(1,209)
Net finance costs	7	(1,350)	(261)
Share of profit of investments accounted for using the equity method	13	28	29
Profit before tax	4	907	1,756
Tax	8	(238)	(33)
Profit for the year		669	1,723
Attributable to:			
Owners of the parent		631	1,691
Non-controlling interests		38	32
Earnings per ordinary share (pence)			
– Basic	10	66.1	177.4
– Diluted	10	66.0	176.9

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 SEPTEMBER

£ million	Notes	2016	2015
Profit for the year		669	1,723
Other comprehensive income			
Exchange movements		1,260	(198)
Items that may be reclassified to profit and loss		1,260	(198)
Net actuarial losses on retirement benefits	22	(604)	(28)
Deferred tax relating to net actuarial losses on retirement benefits	21	115	5
Items that will not be reclassified to profit and loss		(489)	(23)
Other comprehensive income/(expense) for the year, net of tax		771	(221)
Total comprehensive income for the year		1,440	1,502
Attributable to:			
Owners of the parent		1,336	1,489
Non-controlling interests		104	13
Total comprehensive income for the year		1,440	1,502

RECONCILIATION FROM OPERATING PROFIT TO ADJUSTED OPERATING PROFIT

£ million	Notes	2016	2015
Operating profit		2,229	1,988
Acquisition costs	29	–	40
Amortisation of acquired intangibles	11	1,005	697
Restructuring costs	5	307	328
Adjusted operating profit		3,541	3,053

RECONCILIATION FROM NET FINANCE COSTS TO ADJUSTED NET FINANCE COSTS

£ million	Notes	2016	2015
Net finance costs		(1,350)	(261)
Net fair value and exchange losses/(gains) on financial instruments	7	807	(226)
Post-employment benefits net financing cost	7	19	20
Adjusted net finance costs		(524)	(467)

CONSOLIDATED BALANCE SHEET

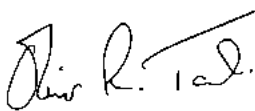
AT 30 SEPTEMBER

£ million	Notes	2016	2015
Non-current assets			
Intangible assets	11	20,704	18,690
Property, plant and equipment	12	1,959	1,768
Investments accounted for using the equity method	13	744	598
Retirement benefit assets	22	5	92
Trade and other receivables	15	89	84
Derivative financial instruments	20	1,063	901
Deferred tax assets	21	631	533
		25,195	22,666
Current assets			
Inventories	14	3,498	2,842
Trade and other receivables	15	2,671	2,454
Current tax assets	8	45	56
Cash and cash equivalents	16	1,274	2,042
Derivative financial instruments	20	46	74
		7,534	7,468
Total assets		32,729	30,134
Current liabilities			
Borrowings	18	(1,544)	(1,957)
Derivative financial instruments	20	(118)	(25)
Trade and other payables	17	(7,991)	(6,795)
Current tax liabilities	8	(284)	(167)
Provisions	23	(188)	(197)
		(10,125)	(9,141)
Non-current liabilities			
Borrowings	18	(12,394)	(12,250)
Derivative financial instruments	20	(1,646)	(735)
Trade and other payables	17	(17)	(13)
Deferred tax liabilities	21	(1,034)	(1,170)
Retirement benefit liabilities	22	(1,484)	(909)
Provisions	23	(287)	(220)
		(16,862)	(15,297)
Total liabilities		(26,987)	(24,438)
Net assets		5,742	5,696
Equity			
Share capital	24	104	104
Share premium and capital redemption		5,836	5,836
Retained earnings		(1,525)	(315)
Exchange translation reserve		896	(298)
Equity attributable to owners of the parent		5,311	5,327
Non-controlling interests	32	431	369
Total equity		5,742	5,696

The financial statements on pages 80 to 119 were approved by the Board of Directors on 8 November 2016 and signed on its behalf by:



Mark Williamson
Chairman



Oliver Tant
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 SEPTEMBER

£ million	Share capital	Share premium and capital redemption	Retained earnings	Exchange translation reserve	Equity attributable to owners of the parent	Non-controlling interests	Total equity
At 1 October 2015	104	5,836	(315)	(298)	5,327	369	5,696
Profit for the year	–	–	631	–	631	38	669
Exchange movements	–	–	–	1,194	1,194	66	1,260
Net actuarial losses on retirement benefits	–	–	(604)	–	(604)	–	(604)
Deferred tax relating to net actuarial losses on retirement benefits	–	–	115	–	115	–	115
Other comprehensive income	–	–	(489)	1,194	705	66	771
Total comprehensive income	–	–	142	1,194	1,336	104	1,440
Transactions with owners							
Cash from employees on maturity/exercise of share schemes	–	–	9	–	9	–	9
Purchase of shares by Employee Share Ownership Trusts	–	–	(7)	–	(7)	–	(7)
Costs of employees' services compensated by share schemes	–	–	26	–	26	–	26
Current tax on share-based payments	–	–	6	–	6	–	6
Dividends paid	–	–	(1,386)	–	(1,386)	(42)	(1,428)
At 30 September 2016	104	5,836	(1,525)	896	5,311	431	5,742
At 1 October 2014	104	5,836	(756)	(119)	5,065	398	5,463
Profit for the year	–	–	1,691	–	1,691	32	1,723
Exchange movements	–	–	–	(179)	(179)	(19)	(198)
Net actuarial losses on retirement benefits	–	–	(28)	–	(28)	–	(28)
Deferred tax relating to net actuarial losses on retirement benefits	–	–	5	–	5	–	5
Other comprehensive income	–	–	(23)	(179)	(202)	(19)	(221)
Total comprehensive income	–	–	1,668	(179)	1,489	13	1,502
Transactions with owners							
Cash from employees on maturity/exercise of share schemes	–	–	7	–	7	–	7
Costs of employees' services compensated by share schemes	–	–	22	–	22	–	22
Current tax on share-based payments	–	–	3	–	3	–	3
Dividends paid	–	–	(1,259)	–	(1,259)	(42)	(1,301)
At 30 September 2015	104	5,836	(315)	(298)	5,327	369	5,696

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 30 SEPTEMBER

£ million	2016	2015
Cash flows from operating activities		
Operating profit	2,229	1,988
Dividends received from investments accounted for under the equity method	19	24
Depreciation, amortisation and impairment	1,244	940
Loss/(profit) on disposal of property, plant and equipment and software	6	(2)
Profit on disposal of intellectual property	–	(31)
Post-employment benefits	(111)	(50)
Costs of employees' services compensated by share schemes	29	25
Movement in provisions	4	(67)
Operating cash flows before movement in working capital	3,420	2,827
(Increase)/decrease in inventories	(149)	21
Decrease in trade and other receivables	171	218
Increase in trade and other payables	116	89
Movement in working capital	138	328
Tax paid	(401)	(408)
Net cash generated from operating activities	3,157	2,747
Cash flows from investing activities		
Interest received	7	10
Purchase of property, plant and equipment	(164)	(194)
Proceeds from sale of property, plant and equipment	42	39
Proceeds from the sale of intellectual property	–	31
Purchase of intangible assets – software	(51)	(44)
Purchase of intangible assets – intellectual property rights	(14)	–
Internally generated intellectual property rights	(2)	(16)
Purchase of brands and operations	–	(4,613)
Net cash used in investing activities	(182)	(4,787)
Cash flows from financing activities		
Interest paid	(547)	(459)
Cash from employees on maturity/exercise of share schemes	9	7
Purchase of shares by Employee Share Ownership Trusts	(7)	–
Increase in borrowings	897	4,720
Repayment of borrowings	(2,637)	(380)
Loan to joint ventures	(9)	–
Cash flows relating to derivative financial instruments	(209)	139
Dividends paid to non-controlling interests	(42)	(42)
Dividends paid to owners of the parent	(1,386)	(1,259)
Net cash (used in)/generated from financing activities	(3,931)	2,726
Net (decrease)/increase in cash and cash equivalents	(956)	686
Cash and cash equivalents at start of year	2,042	1,413
Effect of foreign exchange rates on cash and cash equivalents	188	(57)
Cash and cash equivalents at end of year	1,274	2,042

1 ACCOUNTING POLICIES

BASIS OF PREPARATION

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the IFRS Interpretations Committee (IFRSIC) as published by the International Accounting Standards Board and adopted by the EU. In addition, the financial statements comply with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The financial statements have been prepared under the historical cost convention except where fair value measurement is required under IFRS as described below in the accounting policies on financial instruments.

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the period and of assets, liabilities and contingent liabilities at the balance sheet date. The key estimates and assumptions are set out in note 2 Critical Accounting Estimates and Judgements. Such estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable in the circumstances and constitute management's best judgement at the date of the financial statements. In the future, actual experience may deviate from these estimates and assumptions. This could affect future financial statements as the original estimates and assumptions are modified, as appropriate, in the year in which the circumstances change.

A summary of the more important accounting policies is set out below.

BASIS OF CONSOLIDATION

The consolidated financial statements comprise the results of Imperial Brands PLC (the Company) and its subsidiary undertakings, together with the Group's share of the results of its associates and joint arrangements.

Subsidiaries are those entities controlled by the Group. Control exists when the Group is exposed to, or has the rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Where necessary, accounting policies of subsidiaries are changed to ensure consistency with the policies adopted by the Group.

The acquisition method of accounting is used to account for the purchase of subsidiaries. The excess of the value transferred to the seller in return for control of the acquired business together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets is recorded as goodwill.

Intragroup transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless costs cannot be recovered.

JOINT VENTURES

The Group applies IFRS 11 to all joint arrangements. Under IFRS 11 investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. The Group has assessed the nature of its joint arrangements and determined them to be joint ventures. The financial statements of joint ventures are included in the Group financial statements using the equity accounting method, with the Group's share of net assets included as a single line item entitled

'Investments accounted for using the equity method'. In the same way, the Group's share of earnings is presented in the consolidated income statement below operating profit entitled 'Share of profit of investments accounted for using the equity method'.

FOREIGN CURRENCY

Items included in the financial statements of each Group company are measured using the currency of the primary economic environment in which the company operates (the functional currency).

The income and cash flow statements of Group companies using non-sterling functional currencies are translated to sterling (the Group's presentational currency) at average rates of exchange in each period. Assets and liabilities of these companies are translated at rates of exchange ruling at the balance sheet date. The differences between retained profits and losses translated at average and closing rates are taken to reserves, as are differences arising on the retranslation of the net assets at the beginning of the year.

Transactions in currencies other than a company's functional currency are initially recorded at the exchange rate ruling at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at exchange rates ruling at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement with exchange differences arising on trading transactions being reported in operating profit, and those arising on financing transactions being reported in net finance costs unless as a result of net investment hedging they are reported in other comprehensive income.

The Group designates as net investment hedges certain external borrowings and derivatives up to the value of the net assets of Group companies that use non-sterling functional currencies after deducting permanent intragroup loans. Gains or losses on these hedges that are regarded as highly effective are transferred to other comprehensive income, where they offset gains or losses on translation of the net investments that are recorded in equity, in the exchange translation reserve.

REVENUE RECOGNITION

For the Tobacco business, revenue comprises the invoiced value for the sale of goods and services net of sales taxes, rebates and discounts. Revenue from the sale of goods is recognised when a Group company has delivered products to the customer, the customer has accepted the products and collectability of the related receivables is reasonably assured. Sales of services, which include fees for distributing certain third party products, are recognised in the accounting period in which the services are rendered.

For the Logistics business, revenue comprises the invoiced value for the sale of goods and services net of sales taxes, rebates and discounts when goods have been delivered or services provided. The Logistics business only recognises commission revenue on purchase and sale transactions in which it acts as a commission agent. Distribution and marketing commissions are included in revenue. Revenue is recognised on products on consignment when these are sold by the consignee.

Customer rebates and discounts may be offered to promote sales. The calculated costs are accrued and accounted for as incurred and matched as a deduction from the associated revenues (i.e. excluded from revenues reported in the Group's consolidated income statement).

1 ACCOUNTING POLICIES CONTINUED

DUTY AND SIMILAR ITEMS

Duty and similar items includes duty and levies having the characteristics of duty. In countries where duty is a production tax, duty is included in revenue and in cost of sales in the consolidated income statement. Where duty is a sales tax, duty is excluded from revenue and cost of sales. Payments due in the USA under the Master Settlement Agreement are considered to be levies having the characteristics of duty and are treated as a production tax.

TAXES

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Management periodically evaluates positions taken in tax returns where the applicable tax regulation is subject to interpretation and establishes provisions on the basis of amounts expected to be paid to the tax authorities only where it is considered more likely than not that an amount will be paid or received. This test is applied to each individual uncertain position which is then measured on the single most likely outcome based on interpretation of legislation, management experience and professional advice.

Deferred tax is provided in full on temporary differences between the carrying amount of assets and liabilities in the financial statements and the tax base, except if it arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the assets can be realised. Deferred tax is determined using the tax rates that have been enacted or substantively enacted at the balance sheet date, and are expected to apply when the deferred tax liability is settled or the deferred tax asset is realised.

DIVIDENDS

Final dividends are recognised as a liability in the period in which the dividends are approved by shareholders, whereas interim dividends are recognised in the period in which the dividends are paid.

INTANGIBLE ASSETS – GOODWILL

Goodwill represents the excess of value transferred to the seller in return for control of the acquired business together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets.

Goodwill is tested at least annually for impairment and carried at cost less accumulated impairment losses. Any impairment is recognised immediately in the consolidated income statement and cannot be subsequently reversed. For the purpose of impairment testing, goodwill is allocated to groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

INTANGIBLE ASSETS – OTHER

Other intangible assets are initially recognised in the consolidated balance sheet at historical cost unless they are acquired as part of a business combination, in which case they are initially recognised at fair value. They are shown in the balance sheet at historical cost or

fair value (depending on how they are acquired) less accumulated amortisation and impairment.

These assets consist mainly of acquired trademarks, intellectual property, concessions and rights, acquired customer relationships and computer software. The Davidoff cigarette trademark and some premium cigar trademarks are considered by the Directors to have indefinite lives based on the fact that they are established international brands with global potential. Trademarks with indefinite lives are not amortised but are reviewed annually for impairment.

Intellectual property (including trademarks), supply agreements (including customer relationships) and computer software are amortised over their estimated useful lives as follows:

Intellectual property	5 – 30 years	straight line
Supply agreements	3 – 15 years	straight line
Software	3 – 10 years	straight line

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are shown in the consolidated balance sheet at historical cost or fair value (depending on how they are acquired), less accumulated depreciation and impairment. Costs incurred after initial recognition are included in the assets' carrying amounts or recognised as a separate asset as appropriate only when it is probable that future economic benefits associated with them will flow to the Group and the cost of the item can be measured reliably.

Land is not depreciated. Depreciation is provided on other property, plant and equipment so as to write down the initial cost of each asset to its residual value over its estimated useful life as follows:

Property	up to 50 years	straight line
Plant and equipment	2 – 20 years	straight line/reducing balance
Fixtures and motor vehicles	2 – 15 years	straight line

The assets' residual values and useful lives are reviewed and, if appropriate, adjusted at each balance sheet date.

FINANCIAL INSTRUMENTS AND HEDGING

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the relevant instrument. Financial assets are de-recognised when the rights to receive benefits have expired or been transferred, and the Group has transferred substantially all risks and rewards of ownership. Financial liabilities are de-recognised when the obligation is extinguished.

Non-derivative financial assets are classified as loans and receivables. Receivables are initially recognised at fair value and are subsequently stated at amortised cost using the effective interest method, subject to reduction for allowances for estimated irrecoverable amounts. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of those receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, and is recognised in the consolidated income statement. For interest-bearing assets, the carrying value includes accrued interest receivable.

Non-derivative financial liabilities are initially recognised at fair value and are subsequently stated at amortised cost using the effective interest method. For borrowings, the carrying value includes accrued interest payable, as well as unamortised transaction costs.

Cash and cash equivalents include cash in hand and deposits held on call, together with other short-term highly liquid investments.

The Group transacts derivative financial instruments to manage the underlying exposure to foreign exchange and interest rate risks. The Group does not transact derivative financial instruments for trading purposes. Derivative financial instruments are initially recorded at fair value plus any directly attributable transaction costs. Derivative financial assets and liabilities are included in the consolidated balance sheet at fair value, and include accrued interest receivable and payable where relevant. However, as the Group has decided (as permitted under IAS 39) not to cash flow or fair value hedge account for its derivative financial instruments, changes in fair values are recognised in the consolidated income statement in the period in which they arise unless the derivative qualifies and has been designated as a net investment hedging instrument in which case the changes in fair values, attributable to foreign exchange, are recognised in other comprehensive income.

Collateral transferred under the terms and conditions of credit support annex documents under International Swaps and Derivatives Association (ISDA) agreements in respect of certain derivatives are net-settled and are therefore netted off the carrying value of those derivatives in the consolidated balance sheet.

INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first in first out (FIFO) method. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

Leaf tobacco inventory which has an operating cycle that exceeds 12 months is classified as a current asset, consistent with recognised industry practice.

PROVISIONS

A provision is recognised in the consolidated balance sheet when the Group has a legal or constructive obligation as a result of a past event, it is more likely than not that an outflow of resources will be required to settle that obligation, and a reliable estimate of the amount can be made.

A provision for restructuring is recognised when the Group has approved a detailed formal restructuring plan, and the restructuring has either commenced or has been publicly announced, and it is more likely than not that the plan will be implemented, and the amount required to settle any obligations arising can be reliably estimated. Future operating losses are not provided for.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

RETIREMENT BENEFIT SCHEMES

For defined benefit schemes, the amount recognised in the consolidated balance sheet is the difference between the present value of the defined benefit obligation at the balance sheet date and the fair value of the scheme assets to the extent that they are demonstrably recoverable either by refund or a reduction in future contributions. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation.

The service cost of providing retirement benefits to employees during the year is charged to operating profit. Past service costs are recognised immediately in operating profit, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time.

All actuarial gains and losses, including differences between actual and expected returns on assets and differences that arise as a result of changes in actuarial assumptions, are recognised immediately in full in the statement of comprehensive income for the period in which they arise. An interest charge is made in the income statement by applying the rate used to discount the defined benefit obligations to the net defined benefit liability of the schemes.

For defined contribution schemes, contributions are recognised as an employee benefit expense when they are due.

SHARE-BASED PAYMENTS

The Group applies the requirements of IFRS 2 Share-Based Payment Transactions to both equity-settled and cash-settled share-based employee compensation schemes. The majority of the Group's schemes are equity-settled.

Equity-settled share-based payments are measured at fair value at the date of grant and are expensed over the vesting period, based on the number of instruments that are expected to vest. For plans where vesting conditions are based on total shareholder returns, the fair value at the date of grant reflects these conditions. Earnings per share and net revenue vesting conditions are reflected in the estimate of awards that will eventually vest. For cash-settled share-based payments, a liability equal to the portion of the services received is recognised at its current fair value at each balance sheet date. Where applicable the Group recognises the impact of revisions to original estimates in the consolidated income statement, with a corresponding adjustment to equity for equity-settled schemes and current liabilities for cash-settled schemes. Fair values are measured using appropriate valuation models, taking into account the terms and conditions of the awards.

The Group funds the purchase of shares to satisfy rights to shares arising under share-based employee compensation schemes. Shares acquired to satisfy those rights are held in Employee Share Ownership Trusts. On consolidation, these shares are accounted for as a deduction from equity attributable to owners of the parent. When the rights are exercised, equity is increased by the amount of any proceeds received by the Employee Share Ownership Trusts.

TREASURY SHARES

When the Company purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted on consolidation from equity attributable to owners of the parent until the shares are reissued or disposed of. When such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, increases equity attributable to owners of the parent. When such shares are cancelled they are transferred to the capital redemption reserve.

1 ACCOUNTING POLICIES CONTINUED

USE OF ADJUSTED MEASURES

Management believes that non-GAAP or adjusted measures provide a useful comparison of business performance and reflect the way in which the business is controlled. Accordingly, adjusted measures of operating profit, net finance costs, profit before tax, tax, attributable earnings and earnings per share exclude, where applicable, acquisition costs, amortisation and impairment of acquired intangibles, restructuring costs, post-employment benefits net financing cost, fair value and exchange gains and losses on financial instruments, and related tax effects and significant one-off tax provision charges or credits arising from the resolution of prior year tax matters. Reconciliations between adjusted and reported operating profit are included within note 3 to the financial statements, adjusted and reported net finance costs in note 7, adjusted and reported tax in note 8, and adjusted and reported earnings per share in note 10.

The adjusted measures in this report are not defined terms under IFRS and may not be comparable with similarly titled measures reported by other companies.

The items excluded from adjusted results are those which are one-off in nature or which arose due to acquisitions and are not influenced by the day to day operations of the Group, and the movements in the fair value of financial instruments which are marked to market and not naturally offset. Adjusted net finance costs also excludes all post-employment benefit net finance cost since pension assets and liabilities and redundancy and social plan provisions do not form part of adjusted net debt. This allows comparison of the Group's cost of debt with adjusted net debt. The adjusted measures are used by management to assess the Group's financial performance and aid comparability of results year on year.

The principal adjustments made to reported profits are as follows:

Acquisition Costs

Adjusted measures exclude costs associated with major acquisitions as they do not relate to the day to day operational performance of the Group.

Amortisation and Impairment of Acquired Intangibles

Acquired intangibles are amortised over their estimated useful economic lives where these are considered to be finite. Acquired intangibles considered to have an indefinite life are not amortised. We exclude from our adjusted measures the amortisation and impairment of acquired intangibles, other than software, and the deferred tax associated with amortisation of acquired intangibles and tax deductible goodwill. The deferred tax is excluded on the basis that it will only crystallise upon disposal of the intangibles and goodwill. The related current cash tax benefit is retained in the adjusted measure to reflect the ongoing tax benefit to the Group.

Fair Value Gains and Losses on Derivative Financial Instruments and Exchange Gains and Losses on Borrowings

IAS 39 requires that all derivative financial instruments are recognised in the consolidated balance sheet at fair value, with changes in the fair value being recognised in the consolidated income statement unless the instrument satisfies the hedge accounting rules under IFRS and the Group chooses to designate the derivative financial instrument as a hedge.

The Group hedges underlying exposures in an efficient, commercial and structured manner. However, the strict hedging requirements of IAS 39 may lead to some commercially effective hedge positions not qualifying for hedge accounting. As a result, and as permitted under IAS 39, the Group has decided not to apply cash flow or fair value hedge accounting for its derivative financial instruments. However, the Group does apply net investment hedging, designating certain borrowings and derivatives as hedges of the net investment in the

Group's foreign operations, as permitted by IAS 39, in order to minimise income statement volatility.

We exclude fair value gains and losses on derivative financial instruments and exchange gains and losses on borrowings from adjusted net finance costs. Fair value gains and losses on the interest element of derivative financial instruments are excluded as they will reverse over time or are matched in future periods by interest charges. Fair value gains and losses on the currency element of derivative financial instruments and exchange gains and losses on borrowings are excluded as the relevant foreign exchange gains and losses on the commercially hedged item are accumulated as a separate component of other comprehensive income in accordance with the Group's policy on foreign currency.

Restructuring Costs

Significant one-off costs incurred in integrating acquired businesses and in major rationalisation and optimisation initiatives together with their related tax effects are excluded from our adjusted earnings measures. These costs include the impairment of property, plant and equipment which are surplus to requirements due to restructuring activity.

Post-Employment Benefits Net Financing Cost

The net interest on defined benefit assets or liabilities, together with the unwind of discount on redundancy, social plans and other long term provisions are reported within net finance costs. These items together with their related tax effects are excluded from our adjusted earnings measures.

Tax Matters

Significant one-off tax charges or credits arising from the resolution of prior year tax matters (outside of changes in estimates in the normal course of business) are excluded from our adjusted tax charge to aid comparability and understanding of the Group's performance. The recognition and utilisation of deferred tax assets relating to losses not historically generated as a result of the underlying business performance are excluded on the same basis.

OTHER NON-GAAP MEASURES USED BY MANAGEMENT

Net Revenue

Tobacco net revenue comprises tobacco and Fontem Ventures revenue less duty and similar items, excluding peripheral products. Management considers this an important measure in assessing the performance of Tobacco operations.

Distribution Fees

Distribution fees comprises the Logistics segment revenue less the cost of distributed products. Management considers this an important measure in assessing the performance of Logistics operations.

Adjusted Net Debt

Management monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals and the fair value of derivative financial instruments providing commercial cash flow hedges.

NEW ACCOUNTING STANDARDS AND INTERPRETATIONS

There have been no new standards which became effective for the current reporting period, that have had a material effect on the Group.

Certain changes to IFRS will be applicable to the consolidated financial statements in future years. IFRS 15 Revenue from Contracts with Customers which is effective for the Group for its 2019 financial statements will result in some items currently classified as costs being netted against revenue. It is not expected to have material

effect on the Group's net asset or results. Management has yet to fully assess the impact of IFRS 9 Financial Instruments which is also effective for the Group for its 2019 financial statements. Our initial assessment of IFRS 16 Leases, effective for the Group for its 2020 financial statements, is that it will not have a material effect on the Group's net assets or results. There are no other standards or interpretations that are expected to have a material effect on the Group's net assets or results.

2 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Group makes estimates and assumptions regarding the future. Estimates and judgements are continually evaluated based on historical experience, and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

In the future, actual experience may deviate from these estimates and assumptions. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the current financial year are discussed below.

LEGAL PROCEEDINGS AND DISPUTES

The Group reviews outstanding legal cases following developments in the legal proceedings at each balance sheet date, considering the nature of the litigation, claim or assessment; the legal processes and potential level of damages in the jurisdiction in which the litigation, claim or assessment has been brought; the progress of the case (including progress after the date of the financial statements but before those statements are issued); the opinions or views of legal counsel and other advisers; experience of similar cases; and any decision of the Group's management as to how it will respond to the litigation, claim or assessment.

To the extent that the Group's assessments at any time do not reflect subsequent developments or the eventual outcome of any claim, its future financial statements may be materially affected, with a favourable or adverse impact upon the Group's operating profit, financial position and liquidity.

A summary of significant legal cases in which the Group is currently involved is disclosed in note 28.

INTANGIBLE ASSETS AND PROPERTY, PLANT AND EQUIPMENT

The Group allocates the purchase price of acquired businesses to their identifiable tangible and intangible assets. For major acquisitions we engage external consultants to assist in the valuation of identifiable intangible assets. The valuation process is based on discounted forecast cash flows and is dependent on assumptions about cash flows, economic factors and business strategy.

On acquisition intangible assets and property, plant and equipment are valued at fair value – intangible assets using the income method and property, plant and equipment using assessments of independent valuers. Goodwill represents the excess of value transferred to the seller in return for control of the acquired business together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets.

Intangible assets (other than goodwill, the Davidoff cigarette trademark and certain premium cigar trademarks) and property, plant and equipment are amortised or depreciated over their useful lives which are based on management's estimates of the period over

which the assets will generate revenue, and are periodically reviewed for continued appropriateness. Changes to the estimates used can result in significant variations in the carrying value.

The Group assesses the impairment of intangible assets and property, plant and equipment subject to amortisation or depreciation whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Additionally, goodwill arising on acquisitions and indefinite lived assets are subject to impairment review. The Group's management undertakes an impairment review annually or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable. Factors considered important that could trigger an impairment review of intangible assets and/or property, plant and equipment include the following:

- significant underperformance relative to historical or projected future operating results;
- significant changes in the manner of the use of the acquired assets or the strategy for the overall business; and
- significant negative industry or economic trends.

The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent in the application of the Group's accounting estimates in relation to intangible assets and property, plant and equipment affect the amounts reported in the financial statements, especially the estimates of the expected useful economic lives and the carrying values of those assets. If business conditions were different, or if different assumptions were used in the application of this and other accounting estimates, it is likely that materially different amounts could be reported in the Group's financial statements. Current and future levels of volatility and uncertainty over economic conditions are important factors in assessing the reasonableness of these estimates, assumptions and judgements. Further information on intangibles assets is given in note 11.

INCOME TAXES

The Group is subject to income tax in numerous jurisdictions and significant judgement is required in determining the provision for tax. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognises provisions for tax based on estimates of the taxes that are likely to become due. Where the final tax outcome is different from the amounts that were initially recorded, such differences will impact the current income tax and deferred tax provisions in the period in which such determination is made. Further information on income taxes is given in notes 8 and 21 to these financial statements.

PROVISIONS

The Group holds provisions where appropriate in respect of estimated future economic outflows, principally for restructuring activity, which arise due to past events. Estimates are based on management judgement and information available at the balance sheet date. Actual outflows may not occur as anticipated, and estimates may prove to be incorrect, leading to further charges or releases of provisions as circumstances dictate. Further information on provisions is given in notes 5 and 23.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

3 SEGMENT INFORMATION

Imperial Brands comprises two distinct businesses – Tobacco and Logistics. The Tobacco business comprises the manufacture, marketing and sale of tobacco and tobacco-related products, including sales to (but not by) the Logistics business. The Logistics business comprises the distribution of tobacco products for tobacco product manufacturers, including Imperial Brands, as well as a wide range of non-tobacco products and services. The Logistics business is run on an operationally neutral basis ensuring all customers are treated equally, and consequently transactions between the Tobacco and Logistics businesses are undertaken on an arm's length basis reflecting market prices for comparable goods and services.

The Tobacco business is managed based on the strategic role of groups of markets rather than their geographic proximity, with divisions focused on prioritising growth or returns. Returns Markets are typically mature markets where we have relatively large market shares and our objective is to maximise returns over the long-term by growing profits while actively managing market share. Growth Markets are mainly large profit or volume pools where we typically have market shares below 15 per cent and where our total tobacco approach provides many opportunities for share and profit growth both now and in the future. Following the 2015 acquisition, the USA has become a significant market and is therefore disclosed separately.

The function of Chief Operating Decision Maker (defined in IFRS 8), which is to review performance and allocate resources, is performed by the Board and the Chief Executive, who are regularly provided with information on our segments. This information is used as the basis of the segment revenue and profit disclosures provided below. The main profit measure used by the Board and the Chief Executive is adjusted operating profit. Segment balance sheet information is not provided to the Board or the Chief Executive. Our reportable segments are Growth Markets (which includes Premium Cigar and Fontem Ventures), USA, Returns Markets North, Returns Markets South and Logistics. Prevailing market characteristics such as maturity, excise structure and the breadth of the distribution networks determine the allocation of Returns Markets between Returns Markets North and Returns Markets South.

Operating segments are considered to be business markets. The main tobacco business markets within the Growth, Returns Markets North and Returns Markets South reportable segments are:

Growth Markets – Iraq, Norway, Russia, Saudi Arabia, Taiwan (also includes Premium Cigar and Fontem Ventures);

Returns Markets North – Australia, Belgium, Germany, Netherlands, Poland, United Kingdom; and

Returns Markets South – France, Spain and our African markets including Algeria, Ivory Coast, Morocco.

TOBACCO

£ million unless otherwise indicated

	2016	2015
Revenue	20,890	19,011
Net revenue	7,167	6,251
Operating profit	2,126	1,910
Adjusted operating profit	3,360	2,895
Adjusted operating margin %	46.9	46.3

LOGISTICS

£ million unless otherwise indicated

	2016	2015
Revenue	7,505	7,025
Distribution fees	809	749
Operating profit	98	74
Adjusted operating profit	176	154
Adjusted distribution margin %	21.8	20.6

REVENUE

£ million	2016		2015	
	Total revenue	External revenue	Total revenue	External revenue
Tobacco				
Growth Markets	3,137	3,085	3,019	2,970
USA	2,942	2,942	1,415	1,415
Returns Markets North	12,537	12,504	12,332	12,303
Returns Markets South	2,274	1,598	2,245	1,576
Total Tobacco	20,890	20,129	19,011	18,264
Logistics	7,505	7,505	7,025	7,025
Eliminations	(761)	–	(747)	–
Total Group	27,634	27,634	25,289	25,289

TOBACCO NET REVENUE

£ million	2016	2015
Growth Markets	1,568	1,449
USA	1,477	707
Returns Markets North	2,645	2,649
Returns Markets South	1,477	1,446
Total Tobacco	7,167	6,251

Tobacco net revenue excludes revenue from the sale of peripheral products of £190 million (2015: £175 million).

ADJUSTED OPERATING PROFIT AND RECONCILIATION TO PROFIT BEFORE TAX

£ million	2016	2015
Tobacco		
Growth Markets	443	409
USA	823	375
Returns Markets North	1,439	1,475
Returns Markets South	655	636
Total Tobacco	3,360	2,895
Logistics	176	154
Eliminations	5	4
Adjusted operating profit	3,541	3,053
Acquisition costs – Tobacco	–	(40)
Amortisation of acquired intangibles – Tobacco	(927)	(617)
Amortisation of acquired intangibles – Logistics	(78)	(80)
Restructuring costs – Tobacco	(307)	(328)
Operating profit	2,229	1,988
Net finance costs	(1,350)	(261)
Share of profit of investments accounted for using the equity method	28	29
Profit before tax	907	1,756

OTHER INFORMATION

	2016		2015	
£ million	Additions to property, plant and equipment	Depreciation and software amortisation	Additions to property, plant and equipment	Depreciation and software amortisation
Tobacco				
Growth Markets	32	33	32	31
USA	42	31	20	13
Returns Markets North	53	65	93	61
Returns Markets South	24	37	35	31
Total Tobacco	151	166	180	136
Logistics	13	31	14	29
Total Group	164	197	194	165

Additions to property, plant and equipment exclude those obtained as part of acquisitions (see note 12).

ADDITIONAL GEOGRAPHIC ANALYSIS

External revenue and non-current assets are presented for the UK and for individually significant countries. The Group's products are sold in over 160 countries.

	2016		2015	
£ million	External revenue	Non-current assets	External revenue	Non-current assets
UK	4,356	98	4,498	119
Germany	3,559	3,405	3,408	3,123
France	3,461	2,844	3,300	2,597
USA	3,065	8,057	1,536	7,308
Other	13,193	9,003	12,547	7,909
Total Group	27,634	23,407	25,289	21,056

Non-current assets comprise intangible assets, property, plant and equipment, and investments accounted for using the equity method.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

4 PROFIT BEFORE TAX

Profit before tax is stated after charging/(crediting):

£ million	2016	2015
Raw materials and consumables used ¹	899	868
Changes in inventories of finished goods – Tobacco ¹	1,765	1,802
Changes in inventories of finished goods – Logistics ¹	4,587	4,381
Operating lease charges	56	52
Net foreign exchange losses/(gains)	467	(122)
Write down of inventories	49	29
Loss/(profit) on disposal of property, plant and equipment and software	6	(2)
Impairment of trade receivables	5	3

1. 2015 restated to separately disclose the change in inventories of finished goods between the Tobacco and Logistics business.

ANALYSIS OF FEES PAYABLE TO PRICEWATERHOUSECOOPERS LLP AND ITS ASSOCIATES

£ million	2016	2015
Audit of Parent Company and consolidated financial statements	0.9	0.9
Audit of the Company's subsidiaries	3.4	3.6
Audit related assurance services	–	0.2
	4.3	4.7
Tax advisory services	1.1	1.0
Tax compliance services	0.3	0.1
Other services	0.3	3.0
	6.0	8.8

5 RESTRUCTURING COSTS

£ million	2016	2015
Employment related	144	100
Asset impairments	51	113
Other charges	112	115
	307	328

The charge for the year ending 30 September 2016 was £307 million (2015: £328 million) and relates mainly to our cost optimisation programme announced in 2013 (£188 million); this includes the closure of the Logrono (£108 million) and Mullingar (£21 million) factories, which were communicated earlier in the year. An additional £49 million was charged for integration costs relating to the assets acquired from Lorillard in 2015. The balance of £70 million covers all other restructuring activities across the Group.

The cost optimisation programme is expected to have a cash implementation cost in the region of £600 million and generate savings of £300 million by 2018. In 2016 the cash cost of the programme was £80 million (2015: £169 million), bringing the cumulative net cash cost of the programme to £420 million.

The total restructuring cash flow in the year was £268 million (2015: £256 million).

Restructuring costs are included within administrative and other expenses in the consolidated income statement.

6 DIRECTORS AND EMPLOYEES

EMPLOYMENT COSTS

£ million	2016	2015
Wages and salaries	826	811
Social security costs	172	161
Pension costs (note 22)	34	75
Share-based payments (note 25)	29	25
	1,061	1,072

Details of Directors' emoluments and interests, and of key management compensation which represent related party transactions requiring disclosure under IAS 24, are provided within the Directors' Remuneration Report. The Directors' Remuneration Report, on pages 51-73, includes details on salary, benefits, pension and share plans. These disclosures form part of the financial statements.

NUMBER OF PEOPLE EMPLOYED BY THE GROUP DURING THE YEAR

	2016		2015	
	At 30 September	Average	At 30 September	Average
Tobacco	27,900	28,700	30,500	29,300
Logistics	6,000	5,900	5,900	5,800
	33,900	34,600	36,400	35,100

NUMBER OF PEOPLE EMPLOYED BY THE GROUP BY LOCATION DURING THE YEAR

	2016		2015	
	At 30 September	Average	At 30 September	Average
European Union	15,800	16,000	16,500	16,600
Americas	8,500	8,800	9,800	8,300
Rest of the World	9,600	9,800	10,100	10,200
	33,900	34,600	36,400	35,100

7 NET FINANCE COSTS AND RECONCILIATION TO ADJUSTED NET FINANCE COSTS

RECONCILIATION FROM REPORTED NET FINANCE COSTS TO ADJUSTED NET FINANCE COSTS

£ million	2016	2015
Reported net finance costs	1,350	261
Fair value gains on derivative financial instruments	484	691
Fair value losses on derivative financial instruments	(825)	(578)
Exchange (losses)/gains on financing activities	(466)	113
Net fair value and exchange (losses)/gains on financial instruments	(807)	226
Interest income on net defined benefit assets (note 22)	143	138
Interest cost on net defined benefit liabilities (note 22)	(162)	(157)
Unwind of discount on redundancy and other long-term provisions	—	(1)
Post-employment benefits net financing cost	(19)	(20)
Adjusted net finance costs	524	467
Comprising		
Interest on bank deposits	(7)	(6)
Interest on bank and other loans	531	473
Adjusted net finance costs	524	467

8 TAXATION

ANALYSIS OF CHARGE IN THE YEAR

£ million	2016	2015
Current tax		
UK corporation tax	33	36
Overseas tax	467	449
Total current tax	500	485
Deferred tax movement	(262)	(452)
Total tax charged to the consolidated income statement	238	33

RECONCILIATION FROM REPORTED TAX TO ADJUSTED TAX

The table below shows the tax impact of the adjustments made to reported profit before tax in order to arrive at the adjusted measure of earnings disclosed in note 10.

£ million	2016	2015
Reported tax	238	33
Deferred tax on amortisation of acquired intangibles	261	149
Tax on net fair value and exchange movement on financial instruments	80	(11)
Tax on post-employment benefits net financing cost	7	6
Tax on restructuring costs	79	91
Tax on unrecognised losses	(56)	273
Adjusted tax charge	609	541

The use of adjusted measures is explained in note 1, Accounting Policies (Use of Adjusted Measures).

NOTES TO THE FINANCIAL STATEMENTS

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8 TAXATION CONTINUED

FACTORS AFFECTING THE TAX CHARGE FOR THE YEAR

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the average of the enacted UK corporation tax rates for the year of 20.0 per cent (2015: 20.5 per cent) as follows:

£ million	2016	2015
Profit before tax	907	1,756
Tax at the UK corporation tax rate	181	360
Tax effects of:		
Differences in effective tax rates on overseas earnings	(90)	(110)
Movement in provision for uncertain tax positions	43	44
Remeasurement of deferred tax balances	(101)	(310)
Remeasurement of deferred tax balances arising from changes in tax rates	–	(13)
Permanent differences	170	68
Adjustments in respect of prior years	35	(6)
Total tax charged to the consolidated income statement	238	33

Differences in effective tax rates on overseas earnings represents the impact of worldwide profits being taxed at rates different from 20 per cent. The effective tax rate benefits from internal financing arrangements between group subsidiaries in different countries which are subject to differing tax rates and legislation and the application of double taxation treaties. The movement between 2015 and 2016 is largely driven by increased earnings in the USA and other jurisdictions where the tax rate is higher than 20 per cent.

Remeasurement of deferred tax balances mainly represents the recognition of deferred tax assets previously not recognised. Of the £101 million (2015: £310 million) remeasurement, most of which relates to the Group's Spanish business, £89 million (2015: nil) relates to tax deductible amortisation and the balance of £12 million (2015: £310 million) relates to losses and other deferred tax assets. The 2015 remeasurement related to the recognition of deferred tax assets following the USA acquisition. The Group's assessment of the recoverability of deferred tax assets is based on a review of underlying performance of subsidiaries, changes in tax legislation and the interpretation thereof and changes in the group structure.

Permanent differences include £79 million in respect of non-deductible exchange losses (2015: £33 million gains) and £31 million (2015: £18 million) in respect of non-deductible interest expenses.

MOVEMENT ON CURRENT TAX ACCOUNT

£ million	2016	2015
At 1 October	(111)	(32)
Charged to the consolidated income statement	(500)	(485)
Charged to equity	(6)	(3)
Cash paid	401	408
Exchange movements	(24)	–
Other movements	1	1
At 30 September	(239)	(111)

The cash tax paid in the year is £99 million (2015: £77 million) less than the current tax charge. This arises as a result of timing differences between the accrual of income taxes and the actual payment of cash and the movement in the provision for uncertain tax positions.

ANALYSED AS:

£ million	2016	2015
Assets	45	56
Liabilities	(284)	(167)
	(239)	(111)

UNCERTAIN TAX POSITIONS

As an international business the Group is exposed to uncertain tax positions and changes in legislation in the jurisdictions in which it operates. The Group's uncertain tax positions principally include cross-border transfer pricing, interpretation of new or complex tax legislation and tax arising on the valuation of assets. The Group is also monitoring developments in relation to EU State Aid investigations but does not currently consider any provision is required. The assessment of uncertain tax positions is subjective and significant management judgement is required. This judgement is based on interpretation of legislation, management experience and professional advice.

Provisions arising from uncertain tax positions taken in the calculation of tax assets and liabilities are included within current tax liabilities. At 30 September 2016 the total value of these provisions, including foreign exchange movements, was £165 million (2015: £114 million). It is possible that amounts paid will be different from the amounts provided.

Management have assessed the Group's provision for uncertain tax positions and are comfortable that apart from the French matter referred to below, the provisions in place are not material individually or in aggregate, and that a reasonably possible change in the next financial year would not have a material impact on the results of the Group.

In November 2015 the Group received a challenge from the French tax authorities that could lead to additional tax liabilities of up to £253 million. The challenge concerns the valuation placed on the shares of Altadis Distribution France (now known as Logista France) following an intra group transfer of the shares in October 2012 and the tax consequences flowing from a potentially higher value that is argued for by the tax authorities. Based on professional advice, an amount of £41 million (2015: £23 million) is included in the provision for uncertain tax positions.

9 DIVIDENDS

DISTRIBUTIONS TO ORDINARY EQUITY HOLDERS

£ million	2016	2015	2014
Paid interim of 47.0 pence per share (2015: 91.9p, 2014: 38.8p)			
– Paid August 2014	–	–	370
– Paid June 2015	–	204	–
– Paid September 2015	–	204	–
– Paid December 2015	–	468	–
– Paid June 2016	225	–	–
– Paid September 2016	225	–	–
Interim dividend paid	450	876	370
Proposed interim of 54.1 pence per share (2015: nil, 2014: nil)			
– To be paid December 2016	516	–	–
Interim dividend proposed	516	–	–
Proposed final of 54.1 pence per share (2015: 49.1p, 2014: 89.3p)			
– Paid February 2015	–	–	851
– Paid March 2016	–	468	–
– To be paid March 2017	516	–	–
Final dividend	516	468	851
Total ordinary share dividends of 155.2 pence per share (2015: 141.0p, 2014: 128.1p)	1,482	1,344	1,221

The third interim dividend for the year ended 30 September 2016 of 54.1 pence per share amounts to a proposed dividend of £516 million, which will be paid in December 2016.

The proposed final dividend for the year ended 30 September 2016 of 54.1 pence per share amounts to a proposed dividend payment of £516 million in March 2017 based on the number of shares ranking for dividend at 30 September 2016, and is subject to shareholder approval. If approved, the total dividend paid in respect of 2016 will be £1,482 million (2015: £1,344 million). The dividend paid during 2016 is £1,386 million (2015: £1,259 million).

10 EARNINGS PER SHARE

Basic earnings per share is based on the profit for the year attributable to the owners of the parent and the weighted average number of ordinary shares in issue during the year excluding shares held to satisfy the Group's employee share schemes and shares purchased by the Company and held as treasury shares. Diluted earnings per share have been calculated by taking into account the weighted average number of shares that would be issued if rights held under the employee share schemes were exercised. No instruments have been excluded from the calculation for any period on the grounds that they are anti-dilutive.

£ million	2016	2015
Earnings: basic and diluted – attributable to owners of the Parent Company	631	1,691
Millions of shares		
Weighted average number of shares:		
Shares for basic earnings per share	954.0	953.4
Potentially dilutive share options	2.7	2.5
Shares for diluted earnings per share	956.7	955.9
Pence		
Basic earnings per share	66.1	177.4
Diluted earnings per share	66.0	176.9

NOTES TO THE FINANCIAL STATEMENTS

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10 EARNINGS PER SHARE CONTINUED

RECONCILIATION FROM REPORTED TO ADJUSTED EARNINGS AND EARNINGS PER SHARE

£ million unless otherwise indicated	2016		2015	
	Earnings per share (pence)	Earnings	Earnings per share (pence)	Earnings
Reported basic	66.1	631	177.4	1,691
Acquisition costs	–	–	4.2	40
Amortisation of acquired intangibles	78.0	744	57.5	548
Net fair value and exchange movements on financial instruments	76.2	727	(22.7)	(215)
Post-employment benefits net financing cost	1.3	12	1.5	14
Restructuring costs	23.9	228	24.9	237
Tax on unrecognised losses	5.9	56	(28.6)	(273)
Adjustments above attributable to non-controlling interests	(1.8)	(17)	(1.7)	(16)
Adjusted	249.6	2,381	212.5	2,026
Adjusted diluted	248.9	2,381	211.9	2,026

11 INTANGIBLE ASSETS

£ million	2016				
	Goodwill	Intellectual property	Supply agreements	Software	Total
Cost					
At 1 October 2015	11,698	10,672	1,179	244	23,793
Additions	3	16	–	51	70
Disposals	–	(7)	–	(14)	(21)
Exchange movements	1,930	1,789	179	28	3,926
At 30 September 2016	13,631	12,470	1,358	309	27,768
Amortisation and impairment					
At 1 October 2015	1,318	2,983	662	140	5,103
Amortisation charge for the year ¹	–	911	99	34	1,044
Disposals	–	(7)	–	(10)	(17)
Exchange movements	215	590	107	22	934
Accumulated amortisation	–	4,103	868	186	5,157
Accumulated impairment	1,533	374	–	–	1,907
At 30 September 2016	1,533	4,477	868	186	7,064
Net book value					
At 30 September 2016	12,098	7,993	490	123	20,704

1. Amortisation of acquired intangibles excluded from adjusted operating profit comprises amortisation on intellectual property of £906 million (2015: £603 million) and amortisation on supply agreements of £99 million (2015: £94 million). No adjustment is made for amortisation on internally generated intellectual property of £5 million (2015: nil).

	2015				
£ million	Goodwill	Intellectual property	Supply agreements	Software	Total
Cost					
At 1 October 2014	11,675	6,757	1,239	202	19,873
Additions	–	16	–	44	60
Acquisitions	381	4,053	–	8	4,442
Exchange movements	(358)	(154)	(60)	(10)	(582)
At 30 September 2015	11,698	10,672	1,179	244	23,793
Amortisation and impairment					
At 1 October 2014	1,386	2,432	597	124	4,539
Amortisation charge for the year	–	603	94	23	720
Impairment charge for the year	–	19	–	–	19
Exchange movements	(68)	(71)	(29)	(7)	(175)
Accumulated amortisation	–	2,609	662	140	3,411
Accumulated impairment	1,318	374	–	–	1,692
At 30 September 2015	1,318	2,983	662	140	5,103
Net book value					
At 30 September 2015	10,380	7,689	517	104	18,690

Intellectual property mainly comprises brands acquired in the USA in 2015 and through the purchases of Altadis in 2008 and Commonwealth Brands in 2007.

Supply agreements include Logistics customer relationships and exclusive supply arrangements in Cuba. All were acquired under the purchase of Altadis.

Intangible amortisation and impairment are included within administrative and other expenses in the consolidated income statement.

Amortisation and impairment in respect of intangible assets other than software and internally generated intellectual property are treated as reconciling items between reported operating profit and adjusted operating profit.

GOODWILL AND INTANGIBLE ASSET IMPAIRMENT REVIEW

Goodwill is allocated to groups of cash-generating units (CGUs) that are expected to benefit from the business combination in which the goodwill arose. For the Tobacco business CGUs are based on the markets where the business operates and are grouped in line with the divisional structure in operation during the year. The groupings represent the lowest level at which goodwill is monitored for internal management purposes. A summary of the carrying value of goodwill and intangible assets with indefinite lives is set out below.

	2016		2015	
£ million	Goodwill	Intangible assets with indefinite lives	Goodwill	Intangible assets with indefinite lives
Returns Markets North	4,360	196	3,745	168
Returns Markets South	1,648	103	1,415	88
Growth	1,974	295	1,700	253
USA	2,427	–	2,071	–
Tobacco	10,409	594	8,931	509
Logistics	1,689	–	1,449	–
	12,098	594	10,380	509

NOTES TO THE FINANCIAL STATEMENTS

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11 INTANGIBLE ASSETS CONTINUED

Goodwill has arisen principally on the acquisitions of Reemtsma in 2002 (all CGU groupings), Commonwealth Brands in 2007 (USA), Altadis in 2008 (all CGU groupings) and ITG Brands in 2015 (USA).

The Group tests goodwill and intangible assets with indefinite lives for impairment annually, or more frequently if there are any indications that impairment may have arisen. The value of a CGU, or group of CGUs as appropriate, is based on value-in-use calculations. These calculations use cash flow projections derived from three year financial plans which are approved by the Board annually and are based on detailed bottom-up market-by-market forecasts of projected sales volumes for each product line. These forecasts reflect, on an individual market basis, numerous assumptions and estimates regarding anticipated changes in market size, prices and duty regimes, consumer uptrading and downtrading, consumer preferences and other changes in product mix, based on long-term market trends, market data, anticipated regulatory developments, and management experience and expectations. We consider that pricing, market size, market shares and cost inflation are the key assumptions used in our plans.

GROWTH RATES AND DISCOUNT RATES USED

The compound annual growth rates implicit in these value-in-use calculations are shown below.

%	2016		
	Pre-tax discount rate	Initial growth rate	Long-term growth rate
Returns Markets North	9.0	1.1	1.8
Returns Markets South	11.3	(0.1)	1.8
Growth Markets	9.1-15.8	4.7-10.4	1.2-4.0
USA	10.1	4.3	2.5
Logistics	9.6	6.5	1.8

Cash flows from the three year plan period are extrapolated out to year five using the growth rate implicit in the three year plan, shown in the table above as the initial growth rate. Estimated long-term weighted average compound annual growth rates of between 1.2 per cent and 4.0 per cent per annum are used beyond year five.

Long-term growth rates are based on management's long-term expectations, taking account of industry specific factors such as the nature of our products, the role of excise in government fiscal policy, and relatively stable and predictable long-term macro trends in the Tobacco industry.

Discount rates used are based on the Group's weighted average cost of capital adjusted for the different risk profiles of the CGUs.

Our impairment projections are prepared under the basis set out in IAS 36 which can differ from our internal plans.

GROWTH MARKETS

Within our Growth Markets reporting segment, there are a number of CGU groupings based on our operating segments, including Drive Growth and Other Premium Cigar.

The Drive Growth CGU grouping includes our markets in Russia, Italy and Japan. Our impairment test for this CGU grouping indicated headroom of £210 million, and assumed an initial growth rate of 10.4 per cent. This growth rate reflects forecast benefits of increased investment behind growth brands and portfolio rationalisation, with significant investment in the earlier years forecast to deliver growth in the medium term. A reduction of around 50 per cent in the initial growth rate for these markets would cause the carrying value to equal the recoverable amount.

The impairment test for our Other Premium Cigar CGU grouping that includes our non-Cuban Premium Cigar business indicated headroom of £100 million. A reduction in overall forecast cash flows of 16 per cent, or a reduction in the initial growth rate of 370 basis points from 4.7 per cent, would cause the carrying value to equal the recoverable amount.

OTHER CGU GROUPINGS

For the rest of the Group, any reasonable movement in the assumptions used in the impairment tests would not result in an impairment.

12 PROPERTY, PLANT AND EQUIPMENT

	2016			
£ million	Property	Plant and equipment	Fixtures and motor vehicles	Total
Cost				
At 1 October 2015	926	1,816	366	3,108
Additions	6	137	21	164
Disposals	(79)	(121)	(25)	(225)
Reclassifications	30	(12)	(18)	–
Exchange movements	129	286	46	461
At 30 September 2016	1,012	2,106	390	3,508
Depreciation and impairment				
At 1 October 2015	169	955	216	1,340
Depreciation charge for the year	16	112	35	163
Impairment	15	22	–	37
Disposals	(52)	(106)	(23)	(181)
Reclassifications	3	(3)	–	–
Exchange movements	29	131	30	190
At 30 September 2016	180	1,111	258	1,549
Net book value				
At 30 September 2016	832	995	132	1,959

	2015			
£ million	Property	Plant and equipment	Fixtures and motor vehicles	Total
Cost				
At 1 October 2014	985	1,865	407	3,257
Additions	13	140	41	194
Acquisitions	34	58	14	106
Disposals	(77)	(80)	(69)	(226)
Reclassifications	12	(11)	(8)	(7)
Exchange movements	(41)	(156)	(19)	(216)
At 30 September 2015	926	1,816	366	3,108
Depreciation and impairment				
At 1 October 2014	214	923	266	1,403
Depreciation charge for the year	11	98	33	142
Impairment	–	58	1	59
Disposals	(42)	(64)	(63)	(169)
Reclassifications	–	3	(7)	(4)
Exchange movements	(14)	(63)	(14)	(91)
At 30 September 2015	169	955	216	1,340
Net book value				
At 30 September 2015	757	861	150	1,768

The impairment charges in 2016 were mainly due to the proposed closure of our Logrono manufacturing facility, as announced in 2016. The impairment charges in 2015 were mainly due to the proposed closure of our Nottingham and Nantes manufacturing facilities, as announced in 2014.

NOTES TO THE FINANCIAL STATEMENTS

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13 JOINT VENTURES

The principal joint ventures are Corporación Habanos SA, Cuba and Altabana SL, Spain. Summarised financial information for the Group's share of joint ventures, which are accounted for under the equity method, is shown below:

				2016
£ million	Corporación Habanos	Altabana	Others	Total
Revenue	53	122	34	209
Profit after tax	12	18	3	33
Non-current assets	211	7	11	229
Current assets	43	86	43	172
Total assets	254	93	54	401
Current liabilities	(51)	(25)	(35)	(111)
Non-current liabilities	(9)	(1)	(4)	(14)
Total liabilities	(60)	(26)	(39)	(125)
Net assets	194	67	15	276

				2015
£ million	Corporación Habanos	Altabana	Others	Total
Revenue	46	114	31	191
Profit after tax	14	16	4	34
Non-current assets	181	7	10	198
Current assets	35	69	36	140
Total assets	216	76	46	338
Current liabilities	(46)	(24)	(33)	(103)
Non-current liabilities	(6)	(2)	–	(8)
Total liabilities	(52)	(26)	(33)	(111)
Net assets	164	50	13	227

TRANSACTIONS AND BALANCES WITH JOINT VENTURES

£ million	2016	2015
Sales to	67	59
Purchases from	77	60
Accounts receivable from	14	8
Accounts payable to	(16)	(7)

MOVEMENT ON INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

£ million	2016	2015
At 1 October	598	561
Profit for the year from joint ventures	28	29
Increase/(decrease) in investment in associates	5	(3)
Foreign exchange	113	11
At 30 September	744	598

IFRS 11 Joint Arrangements came into effect for the Group from 1 October 2014. As a result of this standard the profit and loss items from joint ventures are shown in the consolidated income statement below net finance costs as "Share of investments accounted for using the equity method". Similarly, the asset and liability amounts are classified as "Investments accounted for using the equity method".

14 INVENTORIES

£ million	2016	2015
Raw materials	1,072	1,028
Work in progress	57	51
Finished inventories	2,215	1,609
Other inventories	154	154
	3,498	2,842

Other inventories mainly comprise duty-paid tax stamps.

It is generally recognised industry practice to classify leaf tobacco inventory as a current asset although part of such inventory, because of the duration of the processing cycle, ordinarily would not be consumed within one year. We estimate that around £280 million (2015: £358 million) of leaf tobacco held within raw materials will not be utilised within a year of the balance sheet date.

15 TRADE AND OTHER RECEIVABLES

£ million	2016		2015	
	Current	Non-current	Current	Non-current
Trade receivables	2,477	–	2,278	–
Less: provision for impairment of receivables	(59)	–	(54)	–
Net trade receivables	2,418	–	2,224	–
Other receivables	119	72	103	66
Prepayments and accrued income	134	17	127	18
	2,671	89	2,454	84

Trade receivables may be analysed as follows:

£ million	2016		2015	
	Current	Non-current	Current	Non-current
Within credit terms	2,357	–	2,137	–
Past due by less than 3 months	55	–	52	–
Past due by more than 3 months	6	–	35	–
Amounts that are impaired	59	–	54	–
	2,477	–	2,278	–

16 CASH AND CASH EQUIVALENTS

£ million	2016	2015
Cash at bank and in hand	1,266	2,018
Short-term deposits and other liquid assets	8	24
	1,274	2,042

£119 million (2015: £137 million) of total cash and cash equivalents is held in countries in which prior approval is required to transfer the funds abroad. Nevertheless, if the Group complies with these requirements, such liquid funds are at its disposition within a reasonable period of time.

17 TRADE AND OTHER PAYABLES

£ million	2016		2015	
	Current	Non-current	Current	Non-current
Trade payables	946	–	987	–
Other taxes, duties and social security contributions	6,124	–	5,075	–
Other payables	182	–	171	–
Accruals and deferred income	739	17	562	13
	7,991	17	6,795	13

NOTES TO THE FINANCIAL STATEMENTS

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18. BORROWINGS

The Group's borrowings are held at amortised cost, are as follows.

£ million	2016	2015
Current borrowings		
Bank loans and overdrafts	95	53
Capital market issuance:		
European commercial paper (ECP)	978	359
€500m 4.0% notes due December 2015	–	380
€1,500m 8.375% notes due February 2016	–	1,165
£450m 5.5% notes due November 2016	471	–
Total current borrowings	1,544	1,957
Non-current borrowings		
Bank loans	925	1,479
Capital market issuance:		
£450m 5.5% notes due November 2016	–	471
\$1,250m 2.05% notes due February 2018	966	825
€850m 4.5% notes due July 2018	739	634
\$500m 2.05% notes due July 2018	387	330
£200m 6.25% notes due December 2018	210	210
£500m 7.75% notes due June 2019	510	510
€750m 5.0% notes due December 2019	672	576
\$1,250m 2.95% notes due July 2020	968	826
€1,000m 2.25% notes due February 2021	869	745
£1,000m 9.0% notes due February 2022	1,055	1,054
\$1,250m 3.75% notes due July 2022	968	827
\$1,000m 3.5% notes due February 2023	773	660
£600m 8.125% notes due March 2024	626	626
\$1,500m 4.25% notes due July 2025	1,155	986
€650m 3.375% notes due February 2026	569	488
£500m 5.5% notes due September 2026	499	499
£500m 4.875% notes due June 2032	503	504
Total non-current borrowings	12,394	12,250
Total borrowings	13,938	14,207
Analysed as:		
Capital market issuance	12,918	12,675
Bank loans and overdrafts	1,020	1,532

Current and non-current borrowings include interest payable of £24 million (2015: £95 million) and £199 million (2015: £208 million) respectively as at the balance sheet date.

Interest payable on capital market issuances are at the fixed rates of interest and interest payable on bank loans and overdrafts are at floating rates of interest, including non-current bank loans which comprise committed USD term loan facilities due to mature between one and two years.

On 11 December 2015 €500 million 4.0 per cent notes were repaid and on 17 February 2016 €1,500 million 8.375 per cent notes were repaid. On 29 September 2016 \$300 million of bank term loans were repaid and cancelled.

All borrowings are unsecured and the Group has not defaulted on any borrowings during the year (2015: no defaults).

NON-CURRENT FINANCIAL LIABILITIES

The maturity profile of the carrying amount of the Group's non-current liabilities as at 30 September 2016 (including net derivative financial instruments detailed in note 20) is as follows:

	2016			2015		
£ million	Borrowings	Net derivative financial liabilities/ (assets)	Total	Borrowings	Net derivative financial liabilities/ (assets)	Total
Amounts maturing:						
Between one and two years	3,017	(39)	2,978	1,457	67	1,524
Between two and five years	3,229	9	3,238	4,405	(127)	4,278
In five years or more	6,148	613	6,761	6,388	(106)	6,282
	12,394	583	12,977	12,250	(166)	12,084

FAIR VALUE OF BORROWINGS

The fair value of borrowings as at 30 September 2016 is estimated to be £15,439 million (2015: £15,004 million). £14,419 million (2015: £13,472 million) relates to capital market issuance and has been determined by reference to market prices as at the balance sheet date. A comparison of the carrying amount and fair value of capital market issuance by currency is provided below. The fair value of all other borrowings is considered to equal their carrying amount.

£ million	2016		2015	
	Balance sheet amount	Fair value	Balance sheet amount	Fair value
GBP	3,874	4,835	3,874	4,518
EUR	3,827	4,122	4,347	4,493
USD	5,217	5,462	4,454	4,461
Total capital market issuance	12,918	14,419	12,675	13,472

UNDRAWN BORROWING FACILITIES

At 30 September the Group had the following undrawn committed facilities:

£ million	2016	2015
Amounts maturing:		
In less than one year	301	–
Between one and two years	–	739
Between two and five years	2,941	2,594
	3,242	3,333

During the year, the €1 billion facility maturing in July 2017 was reduced by €650 million, and the €2,835 million and £500 million facilities were extended by twelve months, both now maturing in July 2021.

19. FINANCIAL RISK FACTORS

FINANCIAL RISK MANAGEMENT

Overview

In the normal course of business, the Group is exposed to financial risks including, but not limited to, market, credit and liquidity risk. This note explains the Group's exposure to these risks, how they are measured and assessed, and summarises the policies and processes used to manage them, including those related to the management of capital.

The Group operates a centralised treasury function which is responsible for the management of the financial risks of the Group, together with its financing and liquidity requirements. Financial risks comprise exposures to funding and liquidity, interest rate, foreign exchange and counterparty credit risk. The treasury function is also responsible for the financial risk management of the Group's global pension schemes. The Group operates on a global basis and manages its capital to ensure that subsidiaries are able to operate as going concerns and to optimise returns to shareholders through an appropriate balance of debt and equity.

The Group's treasury activities are monitored by the Treasury Committee, which meets regularly throughout the year and comprises the Chief Financial Officer, the Company Secretary and other senior management from finance and treasury. The Treasury Committee operates in accordance with the terms of reference set out by the Board and a framework (the Treasury Committee framework) which sets out the expectations and boundaries to assist in the effective oversight of treasury activities. The Director of Treasury reports on a regular basis to the Treasury Committee.

The Board reviews and approves all major treasury decisions. The treasury function does not operate as a profit centre, nor does it enter into speculative transactions.

The Group's management of financial risks cover the following:

(A) MARKET RISK

Price risk

The Group is not exposed to equity securities price risk other than assets held by its pension funds disclosed in note 22. The Group is exposed to commodity price risk in that there may be fluctuations in the price of tobacco leaf. As with other agricultural commodities, the price of tobacco leaf tends to be cyclical as supply and demand considerations influence tobacco plantings in those countries where tobacco is grown. Also, different regions may experience variations in weather patterns that may affect crop quality or supply and so lead to changes in price. The Group seeks to reduce this price risk by sourcing tobacco leaf from a number of different countries and counterparties and by varying the levels of tobacco leaf held. Currently, these techniques reduce the expected exposure to this risk over the short to medium term to levels considered not material and accordingly, no sensitivity analysis has been presented.

Foreign exchange risk

The Group is exposed to movements in foreign exchange rates due to its commercial trading transactions and profits denominated in foreign currencies, as well as the translation of cash, borrowings and derivatives held in non-functional currencies.

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19. FINANCIAL RISK FACTORS CONTINUED

The Group's financial results are principally exposed to fluctuations in euro and US dollar exchange rates. Management of the Group's foreign exchange transaction and translation risk is addressed below.

Transaction risk

The Group's material transaction exposures arise on costs denominated in currencies other than the functional currencies of subsidiaries, including the purchase of tobacco leaf, which is sourced from various countries but purchased principally in US dollars, and packaging materials which are sourced from various countries and purchased in a number of currencies. The Group's sterling dividends to external shareholders are primarily sourced from foreign subsidiary earnings. Foreign currency flows are matched where possible and remaining foreign currency transaction exposures are not hedged.

Translation risk

The Group seeks to broadly match the currency of borrowings to the currency of its underlying investments in overseas subsidiaries, which are primarily euros and US dollars. The Group issues debt in the most appropriate market or markets at the time of raising new finance and has a policy of using derivative financial instruments, primarily cross-currency swaps, to change the currency of debt as required. Borrowings denominated in, or swapped into foreign currencies to match the Group's investments in overseas subsidiaries are treated as a hedge against the net investment where appropriate.

Foreign exchange sensitivity analysis

The Group's sensitivity to foreign exchange rates attributable to the translation of monetary items held by Group companies in currencies other than their functional currencies is illustrated on an indicative basis below. The sensitivity analysis has been prepared on the basis that net debt and the proportion of financial instruments in foreign currencies remain constant, and that there is no change to the net investment hedge designations in place at 30 September 2016. The sensitivity analysis does not reflect any change to revenue or non-finance costs that may result from changing exchange rates, and ignores any tax implications and offsetting effects of movements in the fair value of derivative financial instruments.

£ million	2016 Increase in income	2015 Increase in income
Income statement impact of non-functional currency foreign exchange exposures:		
10% appreciation of euro (2015: 10%)	458	60
10% appreciation of US dollar (2015: 10%)	46	13

An equivalent depreciation in the above currencies would cause a decrease in income of £560 million and £57 million for euro and US dollar exchange rates respectively (2015: £73 million and £16 million).

Movements in equity in the table below relate to hedging instruments designated as net investment hedges in hedging the Group's euro denominated assets.

£ million	2016 Change in equity	2015 Change in equity
Equity impact of non-functional currency foreign exchange exposures:		
10% appreciation of euro (2015: 10%)	494	751
10% appreciation of US dollar (2015: 10%)	83	101

An equivalent depreciation in the above currencies would result in a change in equity of -£604 million and -£102million for euro and US dollar exchange rates respectively (2015: -£918 million and -£124 million).

At 30 September 2016, after the effect of derivative financial instruments, approximately -1 per cent (2015: -2 per cent) of the Group's net debt was denominated in sterling, 58 per cent in euro (2015: 60 per cent), 43 per cent in US dollars (2015: 45 per cent), and nil per cent in other currencies (2015: -3 per cent).

Interest rate risk

The Group's interest rate risk arises from its borrowings net of cash and cash equivalents, with the primary exposures arising from fluctuations in euro, US dollar and sterling interest rates. Borrowings at variable rates expose the Group to cash flow interest rate risk. Borrowings at fixed rates expose the Group to fair value interest rate risk.

The Group manages its exposure to interest rate risk on its borrowings by entering into derivative financial instruments, principally interest rate swaps, to achieve an appropriate mix of fixed and floating interest rate debt in accordance with the Treasury Committee framework.

As at 30 September 2016, after adjusting for the effect of derivative financial instruments detailed in note 20, approximately 71 per cent (2015: 46 per cent) of net debt was at fixed rates of interest and 29 per cent (2015: 54 per cent) was at floating rates of interest.

Interest rate sensitivity analysis

The Group's sensitivity to interest rates on its euro, US dollar and sterling monetary items which are primarily external borrowings, cash and cash equivalents, is illustrated on an indicative basis below. The impact in the Group's Income Statement reflects the effect on net finance costs in respect of the Group's net debt and the fixed to floating rate debt ratio prevailing at 30 September 2016, ignoring any tax implications and offsetting effects of movements in the fair value of derivative financial instruments.

The sensitivity analysis has been prepared on the basis that net debt and the derivatives portfolio remain constant and that there is no net impact on other comprehensive income (2015: £nil).

The movement in interest rates is considered reasonable for the purpose of this analysis and the estimated effect assumes a lower limit of zero for interest rates where relevant.

£ million	2016	2015
	Change in income	Change in income
Income statement impact of interest rate movements:		
+/- 1% increase in euro interest rates (2015: 1%)	17	72
+/- 1% increase in US dollar interest rates (2015: 1%)	23	53
+/- 1% increase in sterling interest rates (2015: 1%)	–	3

(B) CREDIT RISK

The Group is primarily exposed to credit risk arising from trade receivables due from its customers, cash deposits and amounts due from external financial counterparties on financial instruments held with them. The maximum aggregate credit risk to these sources is considered to be £4,860 million at 30 September 2016 (2015: £5,296 million).

Trade and other receivables

The Group has some significant concentrations of customer credit risk. In order to manage its exposure to customer credit risk, policies have been implemented to ensure that sales of products are made to customers with an appropriate credit history and that credit support guarantees are obtained where appropriate. Analysis of trade and other receivables is provided in note 15.

Financial instruments

In order to manage its credit risk to any one counterparty, the Group places cash deposits and enters into derivative financial instruments with a diversified group of financial institutions carrying suitable credit ratings in line with the Treasury Committee framework. Utilisation of counterparty credit limits is regularly monitored by treasury and ISDA agreements are in place to permit the net settlement of assets and liabilities in certain circumstances. In a few historical cases, collateral has been deposited against derivative financial liabilities and supported by an ISDA Credit Support Annex.

The table below summarises the Group's largest exposures to financial counterparties as at 30 September 2016. At the balance sheet date management does not expect these counterparties to default on their current obligations. The impact of the Group's own credit risk on the fair value of derivatives and other obligations held at fair value is not considered to be material.

Counterparty exposure	2016		2015	
	S&P credit rating	Maximum exposure to credit risk £ million	S&P credit rating	Maximum exposure to credit risk £ million
Highest	AA-	150	AA-	153
2nd highest	AA-	125	AA-	131
3rd highest	AA-	87	AA-	114
4th highest	A+	85	A	114
5th highest	BBB+	52	A+	112

(C) LIQUIDITY RISK

The Group is exposed to liquidity risk, which represents the risk of having insufficient funds to meet its financing needs in any particular location when needed. To manage this risk the Group has a policy of actively maintaining a mixture of short, medium and long-term committed facilities that are designed to ensure that the Group has sufficient available funds to meet the forecast requirements of the Group over the short to medium term. To prevent over-reliance on individual sources of liquidity, funding is provided across a range of instruments including debt capital market issuance, bank term loans, bank revolving credit facilities and European commercial paper.

The Group primarily borrows centrally in order to meet forecast funding requirements, and the treasury function is in regular dialogue with subsidiary companies to ensure their liquidity needs are met. Subsidiary companies are funded by a combination of share capital and retained earnings, intercompany loans, and in very limited cases through external local borrowings. Cash pooling processes are used to centralise surplus cash held by subsidiaries where possible in order to minimise external borrowing requirements and interest costs. Treasury invests surplus cash in bank deposits and uses foreign exchange contracts to manage short-term liquidity requirements in line with cash flow forecasts. As at 30 September 2016, the Group held liquid assets of £1,274 million (2015: £2,042 million).

The table below summarises the Group's non-derivative financial liabilities by maturity based on their contractual cash flows as at 30 September 2016. The amounts disclosed are undiscounted cash flows calculated using spot rates of exchange prevailing at the relevant balance sheet date. Contractual cash flows in respect of the Group's derivative financial instruments are detailed in note 20.

£ million	2016					
	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	> 5 years
Non-derivative financial liabilities:						
Bank loans	1,020	1,038	105	933	–	–
Capital market issuance	12,918	15,767	1,947	2,576	4,303	6,941
Trade and other payables	946	946	946	–	–	–
Total non-derivative financial liabilities	14,884	17,751	2,998	3,509	4,303	6,941

19. FINANCIAL RISK FACTORS CONTINUED

	2015					
£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	> 5 years
Non-derivative financial liabilities:						
Bank loans	1,532	1,573	71	1,000	502	–
Capital market issuance	12,675	15,897	2,374	1,022	5,061	7,440
Trade and other payables	987	987	987	–	–	–
Total non-derivative financial liabilities	15,194	18,457	3,432	2,022	5,563	7,440

Capital management

The Group defines capital as adjusted net debt and equity and manages its capital structure through an appropriate balance of debt and equity in order to drive an efficient financing mix for the Group. Besides the minimum capitalisation rules that may apply to subsidiaries in different countries, the Group's only external imposed capital requirements are interest cover and gearing covenants contained within its core external bank debt facilities, with which the Group was fully compliant during the current and prior periods and expects to be so going forward.

The Group continues to target an investment grade credit rating which it monitors by reference to a number of key financial ratios, including ongoing consideration of the return of capital to shareholders via regular dividend payments and in ongoing discussions with the relevant ratings agencies.

As at 30 September 2016 the Group was rated Baa3/stable outlook by Moody's Investor Service Ltd, BBB/stable outlook by Standard and Poor's Credit Market Services Europe Limited and BBB/stable outlook by Fitch Ratings Limited.

HEDGE ACCOUNTING

The Group hedges its underlying exposures in an efficient, commercial and structured manner in line with the policies above, although the strict hedging requirements of IAS 39 may lead to some commercially effective hedge positions not qualifying for hedge accounting. As a result, and as permitted under IAS 39, the Group has decided not to apply cash flow or fair value hedge accounting in respect of these transactions.

The Group does apply hedge accounting in respect of certain net investments in foreign operations where appropriate. The hedge of a net investment in a foreign operation is a hedge of the translation foreign currency risk arising on the foreign operation. As at 30 September 2016 the Group had made net investment hedge designations in foreign operations in respect of external euro borrowings with a carrying value of €4,387 million (2015: €5,237 million), US dollar borrowings with a carrying value of \$7,950 million (2015: \$6,750 million), and cross-currency swaps with a notional value of €3,871 million (2015: €3,871 million).

The Group also treats certain permanent intragroup loans that meet relevant qualifying criteria under IAS 21 as part of its net investment in foreign operations where appropriate. Intragroup loans with a notional value of €1,943 million (2015: €2,077 million) and US dollar loans with a notional value of \$6,761 million (2015: \$5,077 million) were treated as part of the Group's net investment in foreign operations at the balance sheet date.

FAIR VALUE ESTIMATION AND HIERARCHY

All financial assets and liabilities are carried on the balance sheet at amortised cost, other than derivative financial instruments which are carried at fair value. Derivative financial instruments are valued using techniques based significantly on observable market data such as yield curves and foreign exchange rates as at the balance sheet date (Level 2 classification hierarchy per IFRS 7) as detailed in note 20. There were no changes to the valuation methods or transfers between hierarchies during the year. With the exception of capital market issuance, the fair value of all financial assets and financial liabilities is considered approximate to their carrying amount as outlined in note 18.

NETTING ARRANGEMENTS OF FINANCIAL INSTRUMENTS

The following tables set out the Group's financial assets and financial liabilities that are subject to netting and set-off arrangements. Financial assets and liabilities that are subject to set-off arrangements and disclosed on a net basis in the Group's Balance Sheet primarily relate to cash pooling arrangements and collateral in respect of derivative financial instruments under ISDA Credit Support Annex. Amounts which do not meet the criteria for offsetting on the balance sheet but could be settled net in certain circumstances principally relate to derivative transactions executed under ISDA agreements where each party has the option to settle amounts on a net basis in the event of default of the other party.

	2016				
£ million	Gross financial assets/liabilities	Gross financial assets/liabilities set-off	Net financial assets/liabilities per balance sheet	Related amounts not set-off in the balance sheet	Net
Assets					
Derivative financial instruments	1,243	(134)	1,109	(1,069)	40
Cash and cash equivalents	1,678	(404)	1,274	–	1,274
	2,921	(538)	2,383	(1,069)	1,314
Liabilities					
Derivative financial instruments	(1,898)	134	(1,764)	1,069	(695)
Bank loans and overdrafts	(499)	404	(95)	–	(95)
	(2,397)	538	(1,859)	1,069	(790)

	2015			
£ million	Gross financial assets/liabilities	Gross financial assets/liabilities set-off	Net financial assets/liabilities per balance sheet	Related amounts not set-off in the balance sheet
Assets				
Derivative financial instruments	1,016	(41)	975	(607)
Cash and cash equivalents	3,281	(1,239)	2,042	–
	4,297	(1,280)	3,017	(607)
Liabilities				
Derivative financial instruments	(801)	41	(760)	607
Bank loans and overdrafts	(1,292)	1,239	(53)	–
	(2,093)	1,280	(813)	607
Net				

20. DERIVATIVE FINANCIAL INSTRUMENTS

The Group's derivative financial instruments are held at fair value, are as follows.

	2016			2015		
£ million	Assets	Liabilities	Net Fair Value	Assets	Liabilities	Net Fair Value
Current derivative financial instruments						
Interest rate swaps	32	(60)	(28)	55	(20)	35
Foreign exchange contracts	9	(11)	(2)	13	(5)	8
Cross-currency swaps	5	(121)	(116)	6	–	6
Total current derivatives	46	(192)	(146)	74	(25)	49
Collateral ¹	–	74	74	–	–	–
	46	(118)	(72)	74	(25)	49
Non-current derivative financial instruments						
Interest rate swaps	1,063	(1,279)	(216)	666	(753)	(87)
Cross-currency swaps	–	(427)	(427)	235	(23)	212
Total non-current derivatives	1,063	(1,706)	(643)	901	(776)	125
Collateral ¹	–	60	60	–	41	41
	1,063	(1,646)	(583)	901	(735)	166
Total carrying value of derivative financial instruments	1,109	(1,764)	(655)	975	(760)	215
Analysed as:						
Interest rate swaps	1,095	(1,339)	(244)	721	(773)	(52)
Foreign exchange contracts	9	(11)	(2)	13	(5)	8
Cross-currency swaps	5	(548)	(543)	241	(23)	218
Collateral ¹	–	134	134	–	41	41
Total carrying value of derivative financial instruments	1,109	(1,764)	(655)	975	(760)	215

1. Collateral deposited against derivative financial liabilities under the terms and conditions of an ISDA Credit Support Annex

Fair values are determined based on observable market data such as yield curves and foreign exchange rates to calculate the present value of future cash flows associated with each derivative at the balance sheet date. The classification of these derivative assets and liabilities under the IFRS 7 fair value hierarchy is provided in note 19.

MATURITY OF OBLIGATIONS UNDER DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments have been classified in the balance sheet as current or non-current on an undiscounted contractual basis based on spot rates as at the balance sheet date. Some of the Group's derivative financial instruments contain early termination options. For the purposes of the above and following analysis, maturity dates have been based on the likelihood of an option being exercised with consideration to counterparty expectations and market conditions prevailing as at 30 September 2016. Any collateral transferred to counterparties in respect of derivative financial liabilities has been classified consistently with the related underlying derivative.

The table below summarises the Group's derivative financial instruments by maturity based on their remaining contractual cash flows as at 30 September 2016. The amounts disclosed are the undiscounted cash flows calculated using spot rates of exchange prevailing at the relevant balance sheet date. Contractual cash flows in respect of the Group's non-derivative financial instruments are detailed in note 19.

	2016					
£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	>5 years
Net settled derivatives	(205)	(374)	(23)	(6)	(136)	(209)
Gross settled derivatives	(450)					
– receipts		5,717	2,038	24	835	2,820
– payments		(5,906)	(1,990)	(107)	(975)	(2,834)
	(655)	(563)	25	(89)	(276)	(223)

NOTES TO THE FINANCIAL STATEMENTS

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20. DERIVATIVE FINANCIAL INSTRUMENTS CONTINUED

	2015					
£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	>5 years
Net settled derivatives	(20)	(183)	18	(7)	(13)	(181)
Gross settled derivatives	235					
– receipts		4,660	921	528	752	2,459
– payments		(5,405)	(976)	(550)	(974)	(2,905)
	215	(928)	(37)	(29)	(235)	(627)

DERIVATIVES AS HEDGING INSTRUMENTS

As outlined in note 19, the Group hedges its underlying interest rate exposure and foreign currency translation exposures in an efficient, commercial and structured manner, primarily using interest rate swaps and cross-currency swaps. Foreign exchange contracts are used to manage the Group's short-term liquidity requirements in line with cash flow forecasts as appropriate.

The Group does not apply cash flow or fair value hedge accounting, as permitted under IAS 39, which results in fair value gains and losses attributable to derivative financial instruments being recognised in net finance costs unless they are designated as hedges of a net investment in foreign operations, in which case they are recognised in other comprehensive income.

Interest rate swaps

To manage interest rate risk on its borrowings, the Group issues debt in the market or markets that are most appropriate at the time of raising new finance with regard to currency, interest denomination or duration and then uses interest rate swaps to re-base the debt into the appropriate proportions of fixed and floating interest rates where necessary. Interest rate swaps are also transacted to manage and re-profile the Group's interest rate risk over the short, medium and long-term in accordance with the Treasury Committee framework. Fair value movements are recognised in net finance costs in the relevant reporting period.

As at 30 September 2016, the notional amount of interest rate swaps outstanding that were entered into to convert fixed rate borrowings into floating rates of interest at the time of raising new finance were £11,676 million equivalent (2015: £11,667 million equivalent) with a fair value of £1,093 million asset (2015: £721 million asset). The fixed interest rates vary from 2.0 per cent to 8.7 per cent (2015: 2.0 per cent to 8.7 per cent), and the floating rates are EURIBOR, LIBOR and US LIBOR.

As at 30 September 2016, the notional amount of interest rate swaps outstanding that were entered into to convert floating rate debt into fixed rates of interest to manage and re-profile the Group's interest rate risk were £12,462 million equivalent (2015: £10,692 million equivalent) with a fair value of £1,298 million liability (2015: £741 million liability). The fixed interest rates vary from 0.8 per cent to 5.2 per cent (2015: 0.8 per cent to 5.2 per cent), and the floating rates are EURIBOR, LIBOR and US LIBOR. This includes forward starting interest rate swaps with a total notional amount of £2,459 million equivalent (2015: £4,990 million equivalent) with tenors extending for five years, starting between May 2017 and May 2022.

Cross-currency swaps

The Group enters into cross-currency swaps to convert the currency of debt into the appropriate currency with consideration to the underlying assets of the Group as appropriate. Fair value movements are recognised in net finance costs in the relevant reporting period unless they are designated as hedges of a net investment in foreign operations, in which case they are recognised in other comprehensive income.

As at 30 September 2016, the notional amount of cross-currency swaps entered into to convert issued fixed rate debt into the desired currency at floating rates of interest was £650 million (2015: £650 million) and the fair value of these swaps was £56 million net liability (2015: £5 million net liability).

As at 30 September 2016, the notional amount of cross-currency swaps entered into to convert floating rate sterling debt into the desired currency at floating rates of interest was £3,100 million (2015: £3,100 million) and the fair value of these swaps was £392 million net liability (2015: £232 million net asset).

HEDGES OF NET INVESTMENTS IN FOREIGN OPERATIONS

As at 30 September 2016, cross-currency swaps with a notional amount of €3,871 million (2015: €3,871 million) were designated as hedges of net investments in foreign operations. During the year, foreign exchange translation losses amounting to £474 million (2015: £202 million gains) were recognised in other comprehensive income in respect of cross-currency swaps that had been designated as hedges of a net investment in foreign operations.

FOREIGN EXCHANGE CONTRACTS

The Group enters into foreign exchange contracts to manage short-term liquidity requirements in line with cash flow forecasts. As at 30 September 2016 the notional amount of these contracts was £1,531 million equivalent (2015: £867 million equivalent) and the fair value of these contracts was a net liability of £2 million (2015: £8 million net asset).

21. DEFERRED TAX ASSETS AND LIABILITIES

Deferred tax assets and liabilities are offset only when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The following amounts, determined after appropriate offsetting, are shown in the consolidated balance sheet.

DEFERRED TAX ASSETS

	2016				
£ million	Accelerated depreciation and amortisation	Retirement benefits	Fair value movements	Other temporary differences	Total
At 1 October 2015	104	49	–	380	533
Charged /(credited) to consolidated income statement	(21)	8	–	41	28
Credited to other comprehensive income	–	108	–	–	108
Transfers	(221)	75	–	85	(61)
Exchange movements	(88)	29	–	82	23
At 30 September 2016	(226)	269	–	588	631

	2015				
£ million	Accelerated depreciation and amortisation	Retirement benefits	Fair value movements	Other temporary differences	Total
At 1 October 2014	1	101	1	138	241
Credited/(charged) to consolidated income statement	42	(3)	(1)	268	306
Charged to other comprehensive income	–	(7)	–	–	(7)
Transfers	43	(41)	–	(20)	(18)
Other movements	–	–	–	4	4
Exchange movements	18	(1)	–	(10)	7
At 30 September 2015	104	49	–	380	533

DEFERRED TAX LIABILITIES

	2016				
£ million	Accelerated depreciation and amortisation	Retirement benefits	Fair value movements	Other temporary differences	Total
At 1 October 2015	(1,334)	125	–	39	(1,170)
Credited/(charged) to consolidated income statement	159	(16)	–	91	234
Credited to other comprehensive income	–	7	–	–	7
Transfers	221	(75)	–	(85)	61
Exchange movements	(189)	6	–	17	(166)
At 30 September 2016	(1,143)	47	–	62	(1,034)

	2015				
£ million	Accelerated depreciation and amortisation	Retirement benefits	Fair value movements	Other temporary differences	Total
At 1 October 2014	(1,600)	52	–	118	(1,430)
Credited/(charged) to consolidated income statement	97	(4)	–	53	146
Credited to other comprehensive income	–	12	–	–	12
Acquisitions	–	26	–	10	36
Transfers	122	40	–	(144)	18
Exchange movements	47	(1)	–	2	48
At 30 September 2015	(1,334)	125	–	39	(1,170)

DEFERRED TAX EXPECTED TO BE RECOVERED WITHIN 12 MONTHS

£ million	2016	2015
Deferred tax assets	351	188
Deferred tax liabilities	(246)	(227)
	105	(39)

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21. DEFERRED TAX ASSETS AND LIABILITIES CONTINUED

DEFERRED TAX EXPECTED TO BE RECOVERED IN MORE THAN 12 MONTHS

£ million	2016	2015
Deferred tax assets	280	345
Deferred tax liabilities	(788)	(943)
	(508)	(598)

Within other temporary differences, deferred tax assets of £345 million (2015: £331 million) are recognised for tax losses carried forward to the extent that the realisation of the related tax benefit through future taxable profits is probable.

As at the balance sheet date, deferred tax assets of £125 million (2015: £78 million) have not been recognised due to the potential uncertainty of the utilisation of the underlying tax losses in certain jurisdictions. Of these unrecognised deferred tax assets £6 million are expected to expire in 2017, £9 million (2015: £15 million) are expected to expire within five years and nil (2015: £26 million) are expected to expire between 2022 and 2027.

Also within other temporary differences, deferred tax assets of £15 million (2015: £2 million) are recognised for tax credits carried forward to the extent that the realisation of the tax related benefit through future taxable profits is probable. Deferred tax assets of £159 million (2015: £143 million) have not been recognised due to the potential uncertainty of the utilisation of the credits. Of these unrecognised deferred tax assets £63 million are expected to expire between 2021 and 2027.

We have reviewed the recoverability of deferred tax assets in overseas territories in the light of forecast business performance, changes in tax legislation and the interpretation thereof. Consequently, we have increased deferred tax assets of £118 million (2015: £308 million increase) previously not recognised on the basis that it is more likely than not that these are recoverable. The increase principally relates to the Group's Spanish business.

The aggregate amount of temporary differences associated with undistributed earnings of subsidiaries for which deferred tax liabilities have not been recognised is £5 billion (2015: £5 billion). A provision of £50 million (2015: £50 million) has been made for taxation expected to arise on the planned future remittance of earnings totalling £1.6 billion (2015: £1.7 billion) from various subsidiaries. No liability has been recognised in respect of other differences because the Group is in a position to control the timing of the reversal of the temporary differences, and it is probable that such differences will not reverse in the foreseeable future.

Finance (No. 2) Act 2015 and the Finance Bill 2016 (which is substantively enacted at the balance sheet date) have reduced the UK corporation tax rate to 19% from 1 April 2017 and to 17% from 1 April 2020. These proposed changes are reflected in the deferred tax balances.

22. RETIREMENT BENEFIT SCHEMES

The Group operates a number of retirement benefit schemes for its employees, including both defined benefit and defined contribution schemes. The Group's three principal schemes are defined benefit schemes and are operated by Imperial Tobacco Limited in the UK, Reemtsma Cigarettenfabriken GmbH in Germany and ITG Brands in the USA; these schemes represent 65 per cent, 11 per cent and 7 per cent of the Group's total retirement benefit obligations and 44 per cent, 17 per cent and 11 per cent of the current service cost respectively.

IMPERIAL TOBACCO PENSION FUND

The UK scheme, the Imperial Tobacco Pension Fund or ITPF, is a voluntary final salary pension scheme with a normal retirement age of 60 for most members. The ITPF was offered to employees who joined the company before 1 October 2010 and has a weighted average maturity of 20 years. The population comprises 65 per cent in respect of pensioners, 33 per cent in respect of deferred members and 2 per cent in respect of current employees. New employees in the UK are now offered a defined contribution scheme. Should surplus funds arise in the defined benefit section they may be used to finance defined contribution section contributions on the Company's behalf with company contributions reduced accordingly.

The ITPF operates under trust law and is managed and administered by the Trustees on behalf of the members in accordance with the terms of the Trust Deed and Rules and relevant legislation. The ITPF's assets are held by the trust.

Annual increases in benefits in payment are dependent on inflation so the main uncertainties affecting the level of benefits payable under the ITPF are future inflation levels (including the impact of inflation on future salary increases and any salary increases above inflation) and the actual longevity of the membership.

The contributions paid to the ITPF are set by the ITPF Scheme Actuary every three years. The Scheme Actuary is an external consultant, appointed by the Trustees. Principal factors that the Scheme Actuary will have regard to include the covenant offered by the Group, the level of risk in the ITPF, the expected returns on the ITPF's assets, the results of the funding assessment on an ongoing basis and the expected cost of securing benefits if the fund were to be wound up.

The latest valuation of the ITPF was carried out as at 31 March 2013 when the market value of the invested assets was £2,957 million. Based on the ongoing funding target the total assets were sufficient to cover 100 per cent of the benefits that had accrued to members for past service, after allowing for expected future pay increases. The total assets were sufficient to cover 90 per cent of the total benefits that had accrued to members for past service and future service benefits for current members. In compliance with the Pensions Act 2004, Imperial Tobacco Limited and the Trustee agreed a scheme-specific funding target, a statement of funding principles and a schedule of contributions accordingly.

Following the valuation, the level of employer's contributions to the scheme was increased from £31 million per year. The Company paid £47.5 million on 31 March 2014, £52.5 million on 31 March 2015 and £57.5 million on 31 March 2016 and agreed to pay £65 million each year for the subsequent 12 years. Further contributions were agreed to be paid by the Company in the event of a downgrade of the Group's credit rating to non-investment grade by either Standard & Poor's or Moody's. In addition, surety guarantees with a total value of £400 million and a parental guarantee with Imperial Brands PLC have been put in place.

The Scheme Actuary prepares an annual update of the funding position as at 31 March each year. The latest actuarial valuation (31 March 2016) is currently being undertaken but the outcome of this valuation is not yet concluded. The previous annual update at 31 March 2015 showed a surplus of £329 million in relation to past service accrued benefits.

The main risk for the Group in respect of the ITPF is that additional contributions are required if the investment returns are not sufficient to pay for the benefits (which will be influenced by the factors noted above). The level of equity returns will be a key determinant of overall investment return. The investment portfolio is also subject to a range of other risks typical of the asset classes held, in particular exposure to equity markets, credit risk on bonds and exposure to the property market.

The IAS 19 liability measurement of the defined benefit obligation (DBO) and the current service cost are sensitive to the assumptions made about future inflation and salary growth levels, as well as the assumptions made about life expectation. They are also sensitive to the discount rate, which depends on market yields on sterling denominated AA corporate bonds. The main differences between the funding and IAS 19 assumptions are a more prudent longevity assumption for funding and a different approach to setting the discount rate. A consequence of the ITPF's investment strategy, with a significant proportion of the assets invested in equities and other return-seeking assets, is that the difference between the market value of the assets and the IAS 19 liabilities may be relatively volatile.

THE REEMTSMA CIGARETTENFABRIKEN PENSION PLAN

The German scheme, the Reemtsma Cigarettenfabriken Pension Plan (RCPP), is primarily a career average pension plan that is open to new entrants, though a small closed group of members has final salary benefits. It has a weighted average maturity of 19 years. The scheme population comprises 53 per cent in respect of pensioners, 16 per cent in respect of deferred members and 31 per cent in respect of current employees.

The plan is unfunded and the company pays benefits as they arise. The plan's obligations arise under a works council agreement and are subject to standard German legal requirements around such matters as the benefits to be provided to employees who leave service, and pension increases in payment. Over the next year Reemtsma Cigarettenfabriken GmbH expects to pay £22 million in respect of benefits.

Annual increases in benefits in payment are dependent on inflation so the main uncertainties affecting the level of benefits payable under the plan are future inflation levels and the actual longevity of the membership.

The IAS 19 liability measurement of the DBO and the current service cost are sensitive to the assumptions made about the above variables, as well as the discount rate, which depends on market yields on euro denominated AA corporate bonds.

ITG BRANDS HOURLY PENSION PLAN

The main USA pension scheme, the ITG Brands Hourly Pension Plan (ITGBH), is a defined benefit pension plan that is open to new entrants. It has a weighted average maturity of 11 years. The population comprises 68 per cent in respect of pensioners, 4 per cent in respect of deferred members and 28 per cent in respect of current employees.

The plan is funded and benefits are paid from the plan assets. Contributions to the plan are determined based on US regulatory requirements and ITG Brands is not expected to make any contributions in the next year.

Annual benefits in payment do not increase. The main uncertainty affecting the level of benefits payable under the plan is the actual longevity of the membership. Other key uncertainties impacting the plan include investment risk and potential past service benefit changes from future negotiations.

The IAS 19 liability measurement of the DBO and the service cost are sensitive to the assumptions made about the above variables, as well as the discount rate, which depends on market yields on US dollar denominated AA corporate bonds.

OTHER PLANS

Other plans of the Group include various pension plans, other post-employment and long-term employee benefit plans in several countries of operation. Many of the plans are funded, with assets backing the obligations held in separate legal vehicles such as trusts, others are operated on an unfunded basis. The benefits provided, the approach to funding and the legal basis of the plans reflect their local territories. IAS 19 requires that the discount rate for calculating the DBO and service cost is set according to the level of relevant market yields on corporate bonds where the market is considered "deep", or government bonds where it is not.

The results of the most recent available actuarial valuations for the various plans have been updated to 30 September 2016 in order to determine the amounts to be included in the Group's consolidated financial statements. The aggregate IAS 19 position is as follows:

NOTES TO THE FINANCIAL STATEMENTS

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22. RETIREMENT BENEFIT SCHEMES CONTINUED

DEFINED BENEFIT PLANS

£ million	2016			2015		
	DBO	Assets	Total	DBO	Assets	Total
At 1 October	(4,790)	3,973	(817)	(4,315)	3,535	(780)
Consolidated income statement expense						
Current service cost	(57)	–	(57)	(48)	–	(48)
Past service credit – Spanish free tobacco settlement	32	–	32	–	–	–
Past service credit – curtailment	16	–	16	2	–	2
Cost of termination benefits	(7)	–	(7)	(8)	–	(8)
Net interest (expense)/income on net defined benefit (liability)/asset	(162)	143	(19)	(157)	138	(19)
Administration costs paid from plan assets	–	(3)	(3)	–	(2)	(2)
Cost recognised in the income statement			(38)			(75)
Remeasurements						
Actuarial gain due to liability experience	52	–	52	37	–	37
Actuarial loss due to financial assumption changes	(1,160)	–	(1,160)	(121)	–	(121)
Actuarial gain/(loss) due to demographic assumption changes	10	–	10	(2)	–	(2)
Return on plan assets excluding amounts included in net interest (expense)/income above	–	494	494	–	58	58
Remeasurement effects recognised in OCI			(604)			(28)
Cash						
Employer contributions	–	127	127		101	101
Employee contributions	(1)	1	–	(2)	2	–
Benefits paid directly by the company	43	(43)	–	36	(36)	–
Benefits paid from plan assets	202	(202)	–	175	(175)	–
Net cash			127			101
Other						
Obligations and assets of acquired operations	–	–	–	(437)	367	(70)
Spanish free tobacco settlement ¹	27	(13)	14	–	–	–
Exchange movements	(304)	143	(161)	50	(15)	35
Total other			(147)			(35)
At 30 September	(6,099)	4,620	(1,479)	(4,790)	3,973	(817)

1. During the year ended 30 September 2016 we reached agreements in Spain with both current employees and a proportion of pensioners who would have received or had previously received payments in respect of former entitlements to free cigarettes to accept one-off cash payments in full settlement. Payments to current employees were disbursed during the year. The cash settlement to pensioners was paid in October 2016 and the liability was recognised in the balance sheet at 30 September 2016 in other liabilities.

Termination benefits in the year ended 30 September 2016 mainly relate to restructuring activity in Germany, the UK and the USA. The curtailment gain arises as a result of the closure of the Mullingar factory in Ireland and restructuring activity in the USA.

RETIREMENT BENEFIT SCHEME COSTS CHARGED TO OPERATING PROFIT

£ million	2016	2015
Defined benefit costs in operating profit	19	56
Defined contribution costs in operating profit	18	21
Total retirement benefit scheme costs in operating profit	37	77

Split as follows in the consolidated income statement:

£ million	2016	2015
Cost of sales	14	27
Distribution, advertising and selling costs	13	30
Administrative and other expenses	10	20
Total retirement benefit scheme costs in operating profit	37	77

ASSETS AND LIABILITIES RECOGNISED IN THE CONSOLIDATED BALANCE SHEET

£ million	2016	2015
Retirement benefit assets	5	92
Retirement benefit liabilities	(1,484)	(909)
Net retirement benefit liability	(1,479)	(817)

KEY FIGURES AND ASSUMPTIONS USED FOR MAJOR PLANS

£ million unless otherwise indicated	2016			2015		
	ITPF	RCPP	ITGBH	ITPF	RCPP	ITGBH
Defined benefit obligation (DBO)	3,979	658	437	3,093	482	361
Fair value of scheme assets	(3,632)	–	(419)	(3,178)	–	(355)
Net defined benefit liability/(asset)	347	658	18	(85)	482	6
Current service cost	25	10	6	26	9	2
Employer contributions	58	20	–	53	19	–
Principal actuarial assumptions used (% per annum)						
Discount rate	2.3	1.2	3.7	3.7	2.3	4.3
Future salary increases	3.5	2.7	n/a	3.5	2.9	n/a
Future pension increases	3.0	1.6	n/a	3.0	1.8	n/a
Inflation	3.0	1.6	n/a	3.0	1.8	n/a

	ITPF		RCPP		ITGBH	
	Male	Female	Male	Female	Male	Female
Life expectancy at age 65 years:						
Member currently aged 65	21.7	23.1	19.1	23.1	20.3	22.7
Member currently aged 50	23.0	24.6	21.1	25.1	21.5	24.0

	ITPF		RCPP		ITGBH	
	Male	Female	Male	Female	Male	Female
Life expectancy at age 65 years:						
Member currently aged 65	21.6	23.0	18.9	22.9	19.0	23.1
Member currently aged 50	22.9	24.5	20.9	24.8	21.0	25.0

Assumptions regarding future mortality experience are set based on advice that uses published statistics and experience in each territory. In particular for the ITPF, SAPS tables are used with various adjustments for different groups of members, reflecting observed experience. The largest group of members uses the SAPS All Pensioner Male Amounts table with a 109.8 per cent multiplier. An allowance for improvements in longevity is made using the CMI improvement rates with a long-term trend of 1.25 per cent per annum.

SENSITIVITY ANALYSIS FOR KEY ASSUMPTION AT THE END OF THE REPORTING PERIOD

Sensitivity analysis is illustrative only and is provided to demonstrate the degree of sensitivity of results to key assumptions. Generally, estimates are made by re-performing calculations with one assumption modified and all others held constant.

% increase in DBO	2016			2015		
	ITPF	RCPP	ITGBH	ITPF	RCPP	ITGBH
Discount rate: 0.5% decrease	10.3	10.1	5.8	8.1	9.1	5.7
Rate of inflation: 0.5% decrease	(8.1)	(7.1)	n/a	(6.6)	(6.3)	n/a
One year increase in longevity for a member currently age 65, corresponding changes at other ages	3.5	4.8	4.0	3.5	4.7	3.3

The sensitivity to the inflation assumption change includes corresponding changes to the future salary increases and future pension increases assumptions, but is assumed to be independent of any change to discount rate.

We estimate that a 0.5 per cent decrease/(increase) in the discount rate at the start of the reporting period would have increased/(decreased) the consolidated income statement pension expense by approximately £16 million.

An approximate split of the major categories of ITPF scheme assets is as follows:

£ million unless otherwise indicated	2016		2015	
	Fair value	Percentage of ITPF scheme assets	Fair value	Percentage of ITPF scheme assets
Equities	1,598	44	1,380	43
Bonds – index linked government	981	27	762	24
Bonds – corporate and other	581	16	536	17
Property	436	12	455	15
Other – including derivatives, commodities and cash	36	1	45	1
	3,632	100	3,178	100

The majority of the assets are quoted.

Excluding any self-investment through pooled fund holdings, the ITPF investments in financial instruments of Imperial Brands PLC amounted to £6 million (2015: £2 million).

22. RETIREMENT BENEFIT SCHEMES CONTINUED

An approximate split of the major categories of ITGBH scheme assets is as follows:

£ million unless otherwise indicated	2016		2015	
	Fair value	Percentage of ITGBH scheme assets	Fair value	Percentage of ITGBH scheme assets
Investment funds	276	66	312	88
Equities	–	–	6	2
Bonds – fixed government	61	15	23	6
Bonds – corporate and other	59	14	2	1
Other – including derivatives, commodities and cash	23	5	12	3
	419	100	355	100

The majority of the assets are non-quoted.

23. PROVISIONS

£ million	2016		
	Restructuring	Other	Total
At 1 October 2015	278	139	417
Additional provisions charged to the consolidated income statement	128	67	195
Amounts used	(137)	(19)	(156)
Unused amounts reversed	(2)	(39)	(41)
Exchange movements	37	23	60
At 30 September 2016	304	171	475

Analysed as:

£ million	2016	2015
Current	188	197
Non-current	287	220
	475	417

Restructuring provisions relate mainly to our cost optimisation programme (see note 5).

Other provisions principally relate to commercial legal claims and disputes and are expected to be used over a period of up to 10 years.

24. SHARE CAPITAL

£ million	2016	2015
Authorised, issued and fully paid		
1,036,000,000 ordinary shares of 10p each (2015: 1,036,000,000)	104	104

On 6 March 2014, 31,942,881 shares held in Treasury were cancelled creating the Capital Redemption reserve.

25. SHARE SCHEMES

The Group operates four types of share-based incentive programmes, designed to incentivise staff and to encourage them to build a stake in the Group.

SHARE MATCHING SCHEME

Awards are made to eligible employees who are invited to invest a proportion of their eligible bonus in shares for a period of three years, after which matching shares are awarded on a 1:1 ratio, plus dividend equivalents.

LONG TERM INCENTIVE PLAN (LTIP)

Awards of shares under the LTIP are made to the Executive Directors and senior executives at the discretion of the Remuneration Committee. They vest three years after grant and are subject to performance criteria. Dividend equivalents accrue on vested shares.

SHARESAVE PLAN

Options are granted to eligible employees who participate in a designated savings scheme for a three year period. Historically they were also granted for a five year period.

DISCRETIONARY SHARE AWARDS PLAN (DSAP)

Under the DSAP, one-off conditional awards are made to individuals to recognise exceptional contributions within the business. Awards, which are not subject to performance conditions and under which vested shares do not attract dividend roll-up, will normally vest on the third anniversary of the date of grant subject to the participant's continued employment. The limit of an award under the DSAP is capped at 25 per cent of the participant's salary at the date of grant. Shares used to settle awards under the DSAP will be market purchased.

Further details of the schemes including additional criteria applying to Directors and some senior executives are set out in the Directors' Remuneration Report.

ANALYSIS OF CHARGE TO THE CONSOLIDATED INCOME STATEMENT

£ million	2016	2015
Share Matching Scheme	21	19
Long Term Incentive Plan	5	3
Sharesave Plan	3	3
	29	25

The awards are predominantly equity settled. The balance sheet liability in respect of cash settled schemes at 30 September 2016 was £2.6 million (2015: £3.0 million).

RECONCILIATION OF MOVEMENTS IN AWARDS/OPTIONS

Thousands of shares unless otherwise indicated	Share matching scheme awards	LTIP awards	Sharesave options	DSAP awards	Sharesave weighted average exercise price £
Outstanding at 1 October 2015	2,730	959	1,519	–	21.05
Granted	730	409	329	19	25.40
Lapsed/cancelled	(313)	(209)	(287)	–	21.18
Exercised	(882)	(59)	(476)	–	18.57
Outstanding at 30 September 2016	2,265	1,100	1,085	19	24.73
Exercisable at 30 September 2016	–	–	23	–	18.66

Thousands of shares unless otherwise indicated	Share matching scheme awards	LTIP awards	Sharesave options	Sharesave weighted average exercise price £
Outstanding at 1 October 2014	2,708	769	1,578	19.36
Granted	827	404	442	25.40
Lapsed/cancelled	(170)	(197)	(94)	19.64
Exercised	(635)	(17)	(407)	19.72
Outstanding at 30 September 2015	2,730	959	1,519	21.05
Exercisable at 30 September 2015	–	–	47	17.66

The weighted average Imperial Brands PLC share price at the date of exercise of awards and options was £36.24 (2015: £29.71). The weighted average fair value of sharesave options granted during the year was £6.68 (2015: £5.84).

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25. SHARE SCHEMES CONTINUED

SUMMARY OF AWARDS/OPTIONS OUTSTANDING AT 30 SEPTEMBER 2016

Thousands of shares unless otherwise indicated	Number of awards/options outstanding	Vesting period remaining in months	Exercise price of options outstanding £
Share Matching Scheme			
2014	841	4	n/a
2015	706	16	n/a
2016	718	28	n/a
Total awards outstanding	2,265		
Long Term Incentive Plan			
2014	300	1	n/a
2015	391	17	n/a
2016	409	29	n/a
Total awards outstanding	1,100		
Sharesave Plan			
2012	28	–	20.45
2013	56	–	18.40
2014	319	10	20.40
2015	355	22	25.40
2016	327	34	29.68
Total options outstanding	1,085		
Discretionary Share Awards Plan			
2016	19	26	n/a
Total options outstanding	19		

The vesting period is the period between the grant of awards or options and the earliest date on which they are exercisable. The vesting period remaining and the exercise price of options outstanding are weighted averages. Participants in the Sharesave Plan have six months from the maturity date to exercise their option. Participants in the LTIP have seven years from the end of the vesting period to exercise their option. The exercise price of the options is fixed over the life of each option.

PRICING

For the purposes of valuing options to calculate the share-based payment charge, the Black-Scholes option pricing model has been used for the Share Matching Scheme and Sharesave Plan. A summary of the assumptions used in the Black-Scholes model for 2016 and 2015 is as follows.

	2016			2015	
	Share matching	Sharesave	DSAP	Share matching	Sharesave
Risk-free interest rate %	0.8	0.1-0.3	1.0	1.1	0.3-1.5
Volatility (based on 3 or 5 year history) %	23.0	22.8-23.8	23.4	22.0	22.5-23.0
Expected lives of options granted years	3	3	3	3	3
Dividend yield %	5.4	4.6-5.2	5.4	5.2	5.1-5.2
Fair value £	30.25	6.14-6.69	31.45	25.88	5.33-6.18
Share price used to determine exercise price £	35.54	37.10-37.51	36.54	30.25	31.75-32.63
Exercise price £	n/a	29.68	n/a	n/a	25.40

Market conditions were incorporated into the Monte Carlo method used in determining the fair value of LTIP awards at grant date. Assumptions in 2016 and 2015 are given in the following table.

%	2016	2015
Future Imperial Brands share price volatility	18.9-19.9	18.0
Future Imperial Brands dividend yield	3.6-3.9	5.2
Share price volatility of the tobacco and alcohol comparator group	16.0-35.0	14.0-32.0
Correlation between Imperial Tobacco and the alcohol and tobacco comparator group	37.0	30.0

EMPLOYEE SHARE OWNERSHIP TRUSTS

The Imperial Tobacco Group PLC Employee and Executive Benefit Trust and the Imperial Tobacco Group PLC 2001 Employee Benefit Trust (the Trusts) have been established to acquire ordinary shares in the Company to satisfy rights to shares arising on the exercise and vesting of options and awards. The purchase of shares by the Trusts has been financed by a gift of £19.2 million and an interest free loan of £181.9 million. In addition the Group has gifted treasury shares to the Trusts. None of the Trusts' shares has been allocated to employees or Executive Directors as at 30 September 2016. All finance costs and administration expenses connected with the Trusts are charged to the consolidated income statement as they accrue. The Trusts have waived their rights to dividends and the shares held by the Trusts are excluded from the calculation of basic earnings per share.

SHARES HELD BY EMPLOYEE SHARE OWNERSHIP TRUSTS

Millions of shares	2016	2015
At 1 October	3.2	4.2
Distribution of shares held by Employee Share Ownership Trusts	(1.3)	(1.0)
Gift of treasury shares	1.6	–
At 30 September	3.5	3.2

The shares in the Trusts are accounted for on a first in first out basis and comprise 0.5 million (2015: 0.4 million) shares acquired in the open market at a cost of £13.2 million (2015: £7.9 million) and 3.0 million (2015: 2.8 million) treasury shares gifted to the Trusts by the Group. There were £1.6 million (2015: nil) shares gifted in the financial year 2016.

26. TREASURY SHARES

Shares purchased under the Group's buyback programme are normally held in a separate treasury reserve and represent a deduction from equity shareholders' funds, and are only cancelled if the number of treasury shares approaches 10 percent of issued share capital. During the year the Group purchased no shares (2015: nil) and cancelled no shares (2015: nil).

Millions of shares	2016	2015
At 1 October	78.9	78.9
Gifted to Employee Share Ownership Trusts	(1.6)	–
At 30 September	77.3	78.9
Percentage of issued share capital	7.5	7.6

NOTES TO THE FINANCIAL STATEMENTS

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27. COMMITMENTS

CAPITAL COMMITMENTS

£ million	2016	2015
Contracted but not provided for:		
Property, plant and equipment and software	162	133

OPERATING LEASE COMMITMENTS

Total future minimum lease payments under non-cancellable operating leases consist of leases where payments fall due:

£ million	Property	Other	2016 Total	Property	Other	2015 Total
Within one year	42	15	57	36	10	46
Between one and five years	99	22	121	88	11	99
Beyond five years	32	–	32	32	–	32
	173	37	210	156	21	177

A review of operating leases has identified three leases with a total commitment greater than £10 million. A summary of these commitments is detailed below.

The French head office lease commenced on 1 January 2015 for a term of 10 years, due to terminate on 31 December 2024. Currently there is an annual commitment of €1.8 million. There is the option to terminate the lease on 30 June 2021, subject to six months notice, and an option to partially terminate the lease (1 floor and parking spaces) on 31 March 2018, subject to an indemnity of six months rent.

The German head office lease commenced on 1 January 2014 for a term of 10 years, due to terminate on 31 December 2024. Currently there is an annual commitment of €3.1 million which is price index graduated on an annual basis. There is the option to terminate up to 30 per cent of the remaining lease space from 31 December 2019 to 31 December 2023, subject to notice of 14 months and a pro-rata payment penalty. There is also the option to renew the lease for a period of five years, subject to this being agreed prior to 31 December 2016 otherwise the lease can be renewed on a year by year basis.

The Logista head office lease commenced on 1 January 2015 for a term of nine years, due to terminate on 31 December 2023. Currently there is an annual commitment of €1.8 million which is price index reviewed on an annual basis. There is the option to terminate the lease on 31 December 2021, subject to an indemnity of two months rent, and an option to extend the lease at expiry for a further nine years.

28. LEGAL PROCEEDINGS

The Group is currently involved in a number of legal cases in which claimants are seeking damages for alleged smoking and health related effects. In the opinion of the Group's lawyers, the Group has meritorious defences to these actions, all of which are being vigorously contested. Although it is not possible to predict the outcome of the pending litigation, the Directors believe that the pending actions will not have a material adverse effect upon the results of the operations, cash flow or financial condition of the Group. Consequently, the Group has not provided for any amounts in respect of these cases in the financial statements. For further details see page 49 of the Directors' Report.

29. ACQUISITIONS

There have been no acquisitions during the year ended 30 September 2016.

On 12 June 2015 the Group completed the purchase of the Winston, Salem, Kool and Maverick cigarette brands and the blu e-cigarette brand from Reynolds, together with the national sales force, office and production facilities previously owned by Lorillard for a cash consideration of \$7,056 million (£4,613 million). There have been no adjustments to provisional fair values of this acquisition in the year ended 30 September 2016.

30. NET DEBT

The movements in cash and cash equivalents, borrowings, and derivative financial instruments in the year were as follows:

£ million	Cash and cash equivalents	Current borrowings	Non-current borrowings	Derivative financial instruments	Total
At 1 October 2015	2,042	(1,957)	(12,250)	215	(11,950)
Reallocation of current borrowings from non-current borrowings	–	(471)	471	–	–
Cash flow	(956)	1,017	723	209	993
Accretion of interest	–	94	(13)	(23)	58
Change in fair values	–	–	–	(1,056)	(1,056)
Exchange movements	188	(227)	(1,325)	–	(1,364)
At 30 September 2016	1,274	(1,544)	(12,394)	(655)	(13,319)

ANALYSIS BY DENOMINATION CURRENCY

£ million					2016
	GBP	EUR	USD	Other	Total
Cash and cash equivalents	212	275	471	316	1,274
Total borrowings	(3,868)	(3,901)	(6,144)	(25)	(13,938)
	(3,656)	(3,626)	(5,673)	291	(12,664)
Effect of cross currency swaps	3,629	(4,172)	–	–	(543)
	(27)	(7,798)	(5,673)	291	(13,207)
Derivative financial instruments					(112)
Net debt					(13,319)

£ million					2015
	GBP	EUR	USD	Other	Total
Cash and cash equivalents	341	737	598	366	2,042
Total borrowings	(3,858)	(4,390)	(5,942)	(17)	(14,207)
	(3,517)	(3,653)	(5,344)	349	(12,165)
Effect of cross currency swaps	3,782	(3,570)	–	–	212
	265	(7,223)	(5,344)	349	(11,953)
Derivative financial instruments					3
Net debt					(11,950)

ADJUSTED NET DEBT

Management monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals and the fair value of derivative financial instruments providing commercial cash flow hedges.

£ million	2016	2015
Reported net debt	(13,319)	(11,950)
Accrued interest	221	279
Fair value of derivatives providing commercial hedges	216	25
Adjusted net debt	(12,882)	(11,646)

31. RECONCILIATION OF CASH FLOW TO MOVEMENT IN NET DEBT

£ million	2016	2015
(Decrease)/increase in cash and cash equivalents	(956)	686
Cash flows relating to derivative financial instruments	209	(139)
Increase in borrowings	(897)	(4,720)
Repayment of borrowings	2,637	380
Change in net debt resulting from cash flows	993	(3,793)
Other non-cash movements including revaluation of derivative financial instruments	(998)	389
Exchange movements	(1,364)	(20)
Movement in net debt during the year	(1,369)	(3,424)
Opening net debt	(11,950)	(8,526)
Closing net debt	(13,319)	(11,950)

32. CHANGES IN NON-CONTROLLING INTERESTS

There have been no changes in non-controlling interests in the current or prior year.

33. RELATED UNDERTAKINGS

In accordance with Section 409 of the Companies Act 2006 a full list of subsidiaries, partnerships, associates, and joint ventures, the principal activity, the country of incorporation and the effective percentage of equity owned by the Imperial Brands PLC, as at 30 September 2016, are provided in the entity financial statements of Imperial Brands PLC. There are no material related parties other than Group companies.

REPORT ON THE PARENT COMPANY FINANCIAL STATEMENTS OUR OPINION

In our opinion, Imperial Brands PLC's Parent Company financial statements (the financial statements):

- give a true and fair view of the state of the Parent Company's affairs as at 30 September 2016;
- 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.

WHAT WE HAVE AUDITED

The financial statements, included within the Annual Report and Accounts (the Annual Report), comprise:

- The Balance Sheet as at 30 September 2016;
- The Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law (United Kingdom Generally Accepted Accounting Practice).

OTHER REQUIRED REPORTING CONSISTENCY OF OTHER INFORMATION

Companies Act 2006 reporting

In our opinion, the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

ISAs (UK & Ireland) reporting

Under International Standards on Auditing (UK and Ireland) (ISAs (UK & Ireland)) we are required to report to you if, in our opinion, information in the Annual Report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Parent Company acquired in the course of performing our audit; or
- otherwise misleading.

We have no exceptions to report arising from this responsibility.

ADEQUACY OF ACCOUNTING RECORDS AND INFORMATION AND EXPLANATIONS RECEIVED

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

DIRECTORS' REMUNERATION

Directors' remuneration report – Companies Act 2006 opinion

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Other Companies Act 2006 reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS AND THE AUDIT OUR RESPONSIBILITIES AND THOSE OF THE DIRECTORS

As explained more fully in the Statement of Directors' Responsibilities, 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 ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Parent Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

WHAT AN AUDIT OF FINANCIAL STATEMENTS INVOLVES

We conducted our audit in accordance with ISAs (UK & Ireland). 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 Parent 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.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OTHER MATTER

We have reported separately on the Group financial statements of Imperial Brands PLC for the year ended 30 September 2016.



John Maitland (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors

Bristol

8 November 2016

IMPERIAL BRANDS PLC BALANCE SHEET

AT 30 SEPTEMBER

£ million	Notes	2016	2015
Fixed assets			
Investments	iii	7,968	7,968
Current Assets			
Debtors	iv	9,063	67
Creditors: amounts falling due within one year	v	(1)	(1)
Net current assets		9,062	66
Total assets less current assets		17,030	8,034
Net assets		17,030	8,034
Capital and reserves			
Called up share capital	vi	104	104
Capital redemption reserve		3	3
Share premium account		5,833	5,833
Profit and loss account		11,090	2,094
Total shareholders' funds		17,030	8,034

The financial statements on pages 122 to 133 were approved by the Board of Directors on 8 November 2016 and signed on its behalf by:

Mark Williamson
Chairman

Oliver Tant
Director

IMPERIAL BRANDS PLC STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 SEPTEMBER

£ million	Share capital	Share premium and capital redemption	Retained Earnings	Total Equity
At 1 October 2015	104	5,836	2,094	8,034
Operating profit	–	–	37	37
Dividends received	–	–	10,345	10,345
Total comprehensive income	–	–	10,382	10,382
Transactions with owners				
Dividends paid	–	–	(1,386)	(1,386)
At 30 September 2016	104	5,836	11,090	17,030
At 1 October 2014	104	5,836	1,864	7,804
Operating profit	–	–	(11)	(11)
Dividends received	–	–	1,500	1,500
Total comprehensive income	–	–	1,489	1,489
Transactions with owners				
Dividends paid	–	–	(1,259)	(1,259)
At 30 September 2015	104	5,836	2,094	8,034

I ACCOUNTING POLICIES

BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE WITH FRS 101

These financial statements were prepared in accordance with the Companies Act 2006, Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101) and applicable accounting standards.

The Company has undergone transition from reporting under UK GAAP to Financial Reporting Standard 101, 'Reduced Disclosure Framework' (FRS 101). The financial statements have therefore been prepared in accordance with FRS 101, as issued by the Financial Reporting Council.

The financial statements have been prepared on the historical cost basis. Historical cost is generally based on the fair value of the consideration given in exchange for the assets.

On transition the Company has applied IFRS 1 paragraphs 6-33 as adopted by the EU, as required under FRS 100 paragraph 11(b). As a result of the transition there has been no change to the result for the year or to total equity as at 30 September 2015.

As permitted by section 408(3) of the Companies Act 2006, no separate profit and loss account has been presented for the Company. As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available in the preparation of the financial statements, as detailed below:

- Paragraph 38 of IAS 1 'Presentation of financial statements' – comparative information requirements in respect of:
 - (i) paragraph 79(a)(iv) of IAS 1;
 - (ii) paragraph 118(e) of IAS 38 'Intangible assets' – reconciliations between the carrying amount at the beginning and end of the period;
- The following paragraphs of IAS 1 'Presentation of financial statements':
 - (i) 10(d) – statement of cash flows;
 - (ii) 10(f) – a statement of financial position as at the beginning of the preceding period when an entity applied an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statement;
 - (iii) 16 – statement of compliance with all IFRS;
 - (iv) 38A – requirement for minimum of two primary statements, including cash flow statements;
 - (v) 38B-D – additional comparative information;
 - (vi) 40A-D – requirements for a third statement of financial position;
 - (vii) 111 – cash flow information; and
 - (viii) 134-136 – capital management disclosures;
- IAS 7 'Statement of cash flows';
- Paragraph 30 and 31 of IAS 8 'Accounting Policies, changes in accounting estimates and errors' – requirement for the disclosure of information when an entity has not applied a new IFRS that has been issued but is not yet effective;
- Paragraph 17 of IAS 24 'Related party disclosures' – key management compensation;
- The requirements in IAS 24 'Related party disclosures' to disclose related party transactions entered into between two or more members of a group;
- IFRS 7 'Financial Instruments: Disclosures';
- Paragraphs 91 to 99 of IFRS 13 'Fair value measurement' – disclosure of valuation techniques and inputs used for fair value measurement of assets and liabilities; and
- The requirements of IFRS 1 'First-time adoption of International Financial Reporting Standards' to present a statement of financial position at the date of transition.

The principal accounting policies, which have been applied consistently, are set out below.

INVESTMENTS

Investments held as fixed assets comprise the Company's investment in subsidiaries and are shown at historic purchase cost less any provision for impairment. Investments are tested for impairment annually to ensure that the carrying value of the investment is supported by their recoverable amount.

DIVIDENDS

Final dividends are recognised as a liability in the period in which the dividends are approved by shareholders, whereas interim dividends are recognised in the period in which the dividends are paid. Dividends receivable are recognised as an asset when they are approved.

FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the relevant instrument. Financial assets are de-recognised when the rights to receive benefits have expired or been transferred, and the Company has transferred substantially all risks and rewards of ownership. Financial liabilities are de-recognised when the obligation is extinguished.

NOTES TO THE FINANCIAL STATEMENTS OF IMPERIAL BRANDS PLC

CONTINUED

I ACCOUNTING POLICIES CONTINUED

Non-derivative financial assets are classified as loans and receivables. Receivables are initially recognised at fair value and are subsequently stated at amortised cost using the effective interest method, subject to reduction for allowances for estimated irrecoverable amounts. A provision for impairment of receivables 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 those receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, and is recognised in the income statement. For interest-bearing assets, the carrying value includes accrued interest receivable.

Non-derivative financial liabilities are classified as loans and payables. Payables are initially recognised at fair value and are subsequently stated at amortised cost using the effective interest method. For borrowings, the carrying value includes accrued interest payable.

Cash and cash equivalents include cash in hand and deposits held on call, together with other short-term highly liquid investments.

TREASURY SHARES

When the Company purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity until the shares are reissued or disposed of. When such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, increases shareholders' funds. When such shares are cancelled they are transferred to the capital redemption reserve.

II DIVIDENDS

DISTRIBUTIONS TO ORDINARY EQUITY HOLDERS

£ million	2016	2015	2014
Paid interim of 47.0 pence per share (2015: 91.9p, 2014: 38.8p)			
– Paid August 2014	–	–	370
– Paid June 2015	–	204	–
– Paid September 2015	–	204	–
– Paid December 2015	–	468	–
– Paid June 2016	225	–	–
– Paid September 2016	225	–	–
Interim dividend paid	450	876	370
Proposed interim of 54.1 pence per share (2015: nil, 2014: nil)			
– To be paid December 2016	516	–	–
Interim dividend proposed	516	–	–
Proposed final of 54.1 pence per share (2015: 49.1p, 2014: 89.3p)			
– Paid February 2015	–	–	851
– Paid March 2016	–	468	–
– To be paid March 2017	516	–	–
Final dividend	516	468	851
Total ordinary share dividends of 155.2 pence per share (2015: 141.0p, 2014: 128.1p)	1,482	1,344	1,221

The third interim dividend for the year ended 30 September 2016 of 54.1 pence per share amounts to a proposed dividend of £516 million, which will be paid in December 2016.

The proposed final dividend for the year ended 30 September 2016 of 54.1 pence per share amounts to a proposed dividend payment of £516 million in March 2017 based on the number of shares ranking for dividend at 30 September 2016, and is subject to shareholder approval. If approved, the total dividend paid in respect of 2016 will be £1,482 million (2015: £1,344 million). The dividend paid during 2016 is £1,386 million (2015: £1,259 million).

III INVESTMENTS

COST OF SHARES IN IMPERIAL TOBACCO HOLDINGS (2007) LIMITED

£ million	2016	2015
At 1 October	7,968	7,968
At 30 September	7,968	7,968

The Directors believe that the carrying value of the investments is supported by their underlying net assets.

A list of the subsidiaries of the Company is shown on pages 126 to 133.

IV DEBTORS

£ million	2016	2015
Amounts owed from Group undertakings	9,063	67

Amounts owed from Group undertakings are unsecured, interest bearing, have no fixed date for repayment and are repayable on demand.

V CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

£ million	2016	2015
Cash at bank and in hand	1	1

VI CALLED UP SHARE CAPITAL

£ million	2016	2015
Authorised, issued and fully paid		
1,036,000,000 ordinary shares of 10p each (2015: 1,036,000,000)	104	104

VII RESERVES

As permitted by section 408(3) of the Companies Act 2006, the profit and loss account of the Company is not presented. The profit attributable to shareholders, dealt with in the financial statements of the Company, is £10,382 million (2015: £1,489 million). This is after charging an audit fee of £0.9 million (2015: £0.9 million).

TREASURY SHARES

Shares purchased under the Group's buyback programme are normally held in a separate treasury reserve and represent a deduction from equity shareholders' funds, and are only cancelled if the number of treasury shares approaches 10 percent of issued share capital. During the year the Group purchased no shares (2015: nil) and cancelled no shares (2015: nil).

Millions of shares	2016	2015
At 1 October	78.9	78.9
Gifted to Employee Share Ownership Trusts	(1.6)	–
At 30 September	77.3	78.9
Percentage of issued share capital	7.5	7.6

VIII GUARANTEES

Imperial Brands PLC has guaranteed various borrowings and liabilities of certain UK and overseas subsidiary undertakings, including various Dutch and Irish subsidiaries. At 30 September 2016, the contingent liability totalled £18,138 million (2015: £14,123 million).

The guarantees include the Dutch subsidiaries, all of which are included in the consolidated financial statements as at 30 September 2016 and which, in accordance with Book 2, Article 403 of The Netherlands Civil Code, do not file separate financial statements with the Chamber of Commerce. Under the same article, Imperial Brands PLC has issued declarations to assume any and all liabilities for any and all debts of the Dutch subsidiaries.

The guarantees also cover the Irish subsidiaries, all of which are included in the consolidated financial statements as at 30 September 2016. The Irish companies, namely John Player & Sons Limited and Imperial Tobacco Mullingar, have therefore availed themselves of the exemption provided by section 17 of the Irish Companies (Amendment) Act 1986 in respect of documents required to be attached to the annual returns for such companies.

The Directors have assessed the fair value of the above guarantees and do not consider them to be material. They have therefore not been recognised on the balance sheet.

IX RELATED PARTY DISCLOSURES

Details of Directors' emoluments and interests are provided within the Directors' Remuneration Report. The Directors Remuneration Report, on pages 51-73 includes details on salary, benefits, pension and share plans. These disclosures form part of the financial statements.

X FIRST-TIME ADOPTION OF FRS 101

This is the first year in respect of which the Company has prepared its financial statements under FRS 101. The previous financial statements for the year ended 30 September 2015 were prepared under 'old UK GAAP'. The date of transition to FRS 101 for the Company is 1 October 2014. Set out below are descriptions of the various implementation options applied by the Company in preparing the financial statements for the year ending 30 September 2016, as well as reconciliations from 'old UK GAAP' to FRS 101 for both total comprehensive income for the year ended 30 September 2015 and total equity as at 1 October 2014 and 30 September 2015.

MANDATORY EXCEPTIONS TO RETROSPECTIVE APPLICATION

Mandatory exceptions to retrospective application in IFRS 1 applied in converting from 'old UK GAAP' to FRS 101 are in respect of exception for estimates – estimates made as at 1 October 2014 under FRS 101 are consistent with those made previously under 'old UK GAAP'.

RECONCILIATION OF TOTAL COMPREHENSIVE INCOME FOR THE YEAR ENDED 30 SEPTEMBER 2015, AND TOTAL EQUITY AT 1 OCTOBER 2014 AND 30 SEPTEMBER 2015

The transition from 'old UK GAAP' to FRS 101 has resulted in no change to the reported total comprehensive income for the year ended 30 September 2015, nor to total equity as at 1 October 2014 or 30 September 2015.

RELATED UNDERTAKINGS

In accordance with Section 409 of the Companies Act 2006 a full list of subsidiaries, partnerships, associates, and joint ventures, the principal activity, the country of incorporation and the effective percentage of equity owned, as at 30 September 2016 are disclosed below. With the exception of Imperial Tobacco Holdings (2007) Limited, which is wholly owned by the Company, none of the shares in the subsidiaries is held directly by the Company.

SUBSIDIARIES: REGISTERED IN ENGLAND AND WALES, WHOLLY OWNED

Name	Principal activity
Attendfriend Limited	Dormant
British Tobacco Company Limited	Dormant
Congar International UK Limited	Dormant
Fontem UK Limited	In liquidation
Imperial Brands Enterprise Finance Limited	Provision of treasury services to other Group companies
Imperial Brands Finance PLC	Provision of treasury services to other Group companies
Imperial Investments Limited	Dormant
Imperial Tobacco Altadis Limited	Provision of finance to other Group companies
Imperial Tobacco Capital Assets (1)	Provision of finance to other Group companies
Imperial Tobacco Capital Assets (2)	Provision of finance to other Group companies
Imperial Tobacco Capital Assets (3)	Provision of finance to other Group companies
Imperial Tobacco Capital Assets (4)	Provision of finance to other Group companies
Imperial Tobacco Group Limited	Dormant
Imperial Tobacco Holdings (1) Limited ^(iv)	Holding investments in subsidiary companies
Imperial Tobacco Holdings (2007) Limited ^(iv)	Holding investments in subsidiary companies
Imperial Tobacco Holdings Limited	Holding investments in subsidiary companies
Imperial Tobacco Initiatives	Provision of finance to other Group companies
Imperial Tobacco International Limited	Export and marketing of tobacco products
Imperial Tobacco Lacroix Limited	Provision of finance to other Group companies
Imperial Tobacco Limited	Manufacture, marketing and sale of tobacco products in the UK
Imperial Tobacco Overseas (Polska) Limited	Holding investments in subsidiary companies
Imperial Tobacco Overseas Holdings (1) Limited ^(viii)	Holding investments in subsidiary companies
Imperial Tobacco Overseas Holdings (2) Limited	Holding investments in subsidiary companies
Imperial Tobacco Overseas Holdings (3) Limited	Holding investments in subsidiary companies
Imperial Tobacco Overseas Holdings Limited	Holding investments in subsidiary companies
Imperial Tobacco Overseas Limited ^(x)	Holding investments in subsidiary companies
Imperial Tobacco Pension Trustees (Burlington House) Limited	Dormant
Imperial Tobacco Pension Trustees Limited ^(iv)	Dormant
ITG Brands Limited	Holding investments in subsidiary companies
Joseph & Henry Wilson Limited	Licencing rights for the manufacture and sale of tobacco products
La Flor de Copan UK Limited	Holding investments in subsidiary companies
Park Lane Tobacco Company Limited	Dormant
Rizla UK Limited	Entity ceased trading
Sinclair Collis Limited ^(iv)	Distributor of tobacco products in England, Scotland and Wales
Tabacalera de Garcia UK Limited	Holding investments in subsidiary companies

SUBSIDIARIES: INCORPORATED OVERSEAS, WHOLLY OWNED

Name	Country of incorporation	Principal activity
800 JR Cigar Inc	United States of America	Holding investments in subsidiary companies
Altadis Canarias SAU ⁽ⁱⁱ⁾	Spain	Marketing and sale of tobacco products in the Canary Islands
Altadis Emisiones Financieras SAU	Spain	Provision of finance to Altadis SA and its subsidiaries
Altadis Holdings USA Inc	United States of America	Holding investments in subsidiary companies
Altadis Luxembourg SA	Luxembourg	Holding investments in subsidiary companies
Altadis Management Services Corporation	United States of America	Trademark service company
Altadis Mayotte SAS	France, Mayotte Island	Sales and distribution of tobacco products in Mayotte Island
Altadis Middle East FZCO	United Arab Emirates	Sales and marketing of tobacco products in the Middle East
Altadis Ocean Indien SAS	France (La Reunion Island)	Sales and distribution of tobacco products in la Reunion Island
Altadis Retail Corporation	United States of America	Trademark owner
Altadis S.A.U.	Spain	Manufacture, sales and distribution of tobacco products in Spain
Altadis Shade Company LLC	United States of America	Manufacture and sale of tobacco products in the USA
Altadis USA Inc	United States of America	Manufacture and sale of cigars in the USA
Association pour la Recherche sur les Nicotianées (ARN)	France	Research and development
Athena IP Vermögensverwaltungs GmbH	Germany	Davidoff cigarette trademark owner
Badische Tabakmanufaktur Roth-Händle GmbH	Germany	Trademark owner
Cacique, SA – Comércio, Importação e Exportação	Brazil	Dormant
Casa Blanca Inc	United States of America	Restaurant
Casa de Montecristo Inc	United States of America	Retail
Casa de Montecristo TN LLC	United States of America	Retail
Casa de Montecristo TX LLC	United States of America	Retail
CBHC Inc	United States of America	Dormant
Cigar Savor Enterprises LLC	United States of America	Manufacture of tobacco products
Commonwealth Brands Inc	United States of America	Manufacture and sale of tobacco products in the USA
Commonwealth-Altadis, Inc	United States of America	Sales and distribution of tobacco products in the USA
Congar International Corp (Delaware)	United States of America	Manufacturing and distribution of mass market cigars
Conneticut Shade Corporation	United States of America	Holding investments in subsidiary companies
Consolidated Cigar Holdings Inc ^(vii)	United States of America	Holding investments in subsidiary companies
Coralma International SAS	France	Holding investments in subsidiary companies
Cuban Cigar Brands BV ^(v)	Netherlands Antilles	Trademark owner
Direct Products Inc (Inactive)	United States of America	Holding investments in subsidiary companies
Dunkerquoise des Blends SAS	France	Tobacco processing
East Side Cigar, Inc	United States of America	Production and distribution of cigars
Ets L Lacroix Fils NV/SA	Belgium	Manufacture and sale of tobacco products in Belgium
Fontem (Beijing) Technology Solutions Limited ⁽ⁱ⁾	People's Republic of China	Research and development
Fontem Holdings 1 B.V.	The Netherlands	Holding investments in subsidiary companies
Fontem Holdings 2 B.V.	The Netherlands	Holding investments in subsidiary companies
Fontem Holdings 3 B.V.	The Netherlands	Holding investments in subsidiary companies
Fontem Holdings 4 B.V.	The Netherlands	Holding investments in subsidiary companies
Fontem Holdings B.V.	The Netherlands	Holding investments in subsidiary companies
Fontem International GmbH	Germany	Holding investments in subsidiary companies
Fontem US, Inc.	United States of America	Sales and marketing of tobacco products in the US
Fontem Ventures B.V.	The Netherlands	Holding investments in subsidiary companies
Gauloises Inc.	United States of America	In liquidation
Huotraco International Limited	Cambodia	Production and marketing of tobacco products
Imperial Brands Finance France SAS	France	Provision of finance to other Group companies
Imperial Nominees Limited ⁽ⁱⁱⁱ⁾	New Zealand	Trustee Company
Imperial Tobacco (Asia) Pte. Ltd.,	Singapore	Trading of tobacco related products
Imperial Tobacco (Beijing) Limited ⁽ⁱ⁾	People's Republic of China	In liquidation
Imperial Tobacco Australia Holdings B.V.	The Netherlands	Holding investments in subsidiary companies
Imperial Tobacco Australia Limited	Australia	Sales and marketing of tobacco products in Australia
Imperial Tobacco Austria Marketing Service GmbH	Austria	Marketing of tobacco products in Austria
Imperial Tobacco BH doo ⁽ⁱ⁾	Bosnia-Herzegovina	Marketing and distribution of tobacco products in Bosnia
Imperial Tobacco Brasil Comércio de Produtos de Tabaco Ltda.	Brazil	Co-ordinating and monitoring of WEST license productions and distribution of tobacco products
Imperial Tobacco Bulgaria EOOD ⁽ⁱ⁾	Bulgaria	Manufacture and sale of tobacco products in Bulgaria

RELATED UNDERTAKINGS

CONTINUED

SUBSIDIARIES: INCORPORATED OVERSEAS, WHOLLY OWNED CONTINUED

Name	Country of incorporation	Principal activity
Imperial Tobacco China Limited ⁽ⁱ⁾	People's Republic of China	In liquidation
Imperial Tobacco CR s.r.o.	Czech Republic	Sales and marketing of tobacco products in the Czech Republic
Imperial Tobacco Denmark ApS	Denmark	Distribution of tobacco products in Denmark and Greenland
Imperial Tobacco Distribution EOOD ⁽ⁱ⁾	Bulgaria	Marketing and distribution of tobacco products in Bulgaria
Imperial Tobacco Distribution Romania srl	Romania	Marketing and distribution of tobacco products in Romania
Imperial Tobacco EFKA Management GmbH	Germany	Manufacture of tobacco products in Germany
Imperial Tobacco España, S.L.U.	Spain	Holding investments in subsidiary companies
Imperial Tobacco Estonia OÜ	Estonia	Sales of tobacco products
Imperial Tobacco Finland Oy	Finland	Sales and marketing of tobacco products in Finland
Imperial Tobacco Germany Finance GmbH	Germany	Holding investments in subsidiary companies
Imperial Tobacco Hellas S.A.	Greece	Sales and marketing of tobacco products in Greece
Imperial Tobacco Holdings (Netherlands) B.V.	The Netherlands	Provision of finance to other Group companies
Imperial Tobacco Holdings International B.V.	The Netherlands	Provision of finance to other Group companies
Imperial Tobacco Ireland Unlimited Company ^(v)	Ireland	Provision of finance to other Group companies
Imperial Tobacco Italia S.r.l.	Italy	Sales and marketing of tobacco products in Italy
Imperial Tobacco Italy S.r.l.	Italy	Holding investments in subsidiary companies
Imperial Tobacco Japan Kabushiki Kaisha	Japan	Sales and marketing of tobacco products in Japan
Imperial Tobacco Kyrgyzstan LLC ⁽ⁱ⁾	Kyrgyzstan	Marketing and distribution of tobacco products in Kyrgyzstan
Imperial Tobacco Magyarország Dohányforgalmazó Kft (Imperial Tobacco Hungary)	Hungary	Sales and marketing of tobacco products in Hungary
Imperial Tobacco Management (1) Limited	Guernsey	Holding investments in subsidiary companies
Imperial Tobacco Management (2) Limited	Guernsey	Holding investments in subsidiary companies
Imperial Tobacco Management Luxembourg (3) sarl	Luxembourg	Holding investments in subsidiary companies
Imperial Tobacco Marketing Sdn Bhd	Malaysia	Trading of tobacco products
Imperial Tobacco Mullingar Unlimited Company	Ireland	Manufacture of fine cut tobacco in the Republic of Ireland
Imperial Tobacco New Zealand Limited	New Zealand	Manufacture and sale of tobacco products in New Zealand
Imperial Tobacco Norway AS	Norway	Sales and marketing of tobacco products in Norway
Imperial Tobacco Polska Manufacturing SA	Poland	Manufacture of tobacco products in Poland
Imperial Tobacco Polska S.A.	Poland	Manufacture and sale of tobacco products in Poland
Imperial Tobacco Portugal SSPLC	Portugal	Advertising and support management
Imperial Tobacco Sales & Marketing LLC	Russia	Sales and marketing of tobacco products in Russia
Imperial Tobacco SCG doo Beograd ⁽ⁱ⁾	Serbia	Marketing and distribution of tobacco products in Serbia
Imperial Tobacco Sigara ve Tutunculuk Sanayi Ve Ticaret A.S.	Turkey	Manufacture of tobacco products in Turkey
Imperial Tobacco Slovakia a.s.	Slovak Republic	Sales and marketing of tobacco products in the Slovak Republic
Imperial Tobacco South Africa S.A.	Panama	Provision of services to other Group companies
Imperial Tobacco Taiwan Co Limited	Taiwan	Sales and marketing of tobacco products in Taiwan
Imperial Tobacco Taiwan Manufacturing Company Limited	Taiwan	Manufacture of tobacco products in Taiwan
Imperial Tobacco Tutun Urunleri Satis Ve Pazarlama A.S.	Turkey	Sales and marketing of tobacco products in Turkey
Imperial Tobacco Ukraine ⁽ⁱ⁾	Ukraine	Sales and marketing of tobacco products un Ukraine
Imperial Tobacco US Holdings BV	The Netherlands	Holding investments in subsidiary companies
Imperial Tobacco Volga LLC ⁽ⁱ⁾	Russia	Manufacture of tobacco products in Russia
Imperial Tobacco West Africa SAS ⁽ⁱ⁾	Cote D'Ivoire	Holding investments in subsidiary companies
Imperial Tobacco Yaroslavl CJSC ⁽ⁱ⁾	Russia	Manufacture of tobacco products in Russia
Imperial Tobacco Zagreb doo ⁽ⁱ⁾	Croatia	Marketing and distribution of tobacco related products in Croatia
IMPTOB South Africa (Pty) Limited	South Africa	Manufacture of tobacco products in South Africa
International Marketing Promotional Services Limited	Nigeria	Sales and marketing and of tobacco products in Nigeria
ITB Corporation Limited	Bahamas	Trademark owner
ITG Brands Holdco LLC	United States of America	Holding investments in subsidiary companies
ITG Brands, LLC	United States of America	Marketing and distribution of tobacco products in the USA
ITG Holdings USA Inc ^(ix)	United States of America	Holding investments in subsidiary companies
ITI Cigars SL	Spain	Holding investments in subsidiary companies
ITL Pacific (HK) Limited	Hong Kong	Manufacture and sale of tobacco and tobacco related products
J & R Tobacco (New Jersey) Corp	United States of America	Sales of tobacco and tobacco related products
JAW-Invest Oy	Finland	Trademark owner
John Player & Sons Limited	Ireland	Sales and marketing of tobacco products in the Republic of Ireland
John Player Ireland Pension Trustee Limited	Ireland	Trustee Company

SUBSIDIARIES: INCORPORATED OVERSEAS, WHOLLY OWNED

Name	Country of incorporation	Principal activity
JR Cigar (DC) Inc	United States of America	Sales of tobacco and tobacco related products
JR Cigars.com, Inc.	United States of America	Sales of tobacco and tobacco related products
JR Mooresville, Inc	United States of America	Sales of tobacco and tobacco related products
JR Tobacco NC, Inc	United States of America	Sales of tobacco and tobacco related products
JR Tobacco of America Inc	United States of America	Sales of tobacco and tobacco related products
JR Tobacco of Burlington Inc	United States of America	Sales of tobacco and tobacco related products
JR Tobacco of Michigan Inc	United States of America	Sales of tobacco and tobacco related products
JR Tobacco Outlet Inc	United States of America	Sales of tobacco and tobacco related products
JSNM SARL	France	Trademark owner
La Flor de Copan SAS	France	Manufacture of cigars in Honduras
Los Olvidados SRL	Dominican Republic	Manufacture and distribution of cigars
Max Rohr, Inc	United States of America	Trademark owner
MC Management, Inc.	United States of America	Provision of services to other Group companies
Meccarillos France, SA	Luxembourg	Holding investments in subsidiary companies
Meccarillos International, SA	Luxembourg	Holding investments in subsidiary companies
Meccarillos Suisse, SA	Luxembourg	Holding investments in subsidiary companies
Midtown Cigar, Inc.	United States of America	Sales of tobacco and tobacco related products
Millennium Tobacco	Ireland	Provision of finance to other Group companies
Newglade International Unlimited Company	Ireland	Provision of finance to other Group companies
Phillippine Bobbin Corporation	Philippines	Manufacture of tobacco related products
PT Reemtsma Indonesia	Indonesia	In liquidation
Real Club de Golf la Herrería S.A.	Spain	Management of golf course
REEMARK Gesellschaft für Markenkooperation mbH	Germany	Dormant
Reemtsma Cigarettenfabriken GmbH	Germany	Manufacture and sale of tobacco products in Germany
Reemtsma Mexico SA de CV IL	Mexico	In liquidation
Rizla International B.V.	The Netherlands	Holding investments in subsidiary companies
Robert Burton Associates Limited	United States of America	Marketing of papers in the US
Santa Clara Inc	United States of America	Distribution of cigars
Seita Participations SAS	France	Holding investments in subsidiary companies
Seita Senegal Sarl	Senegal	Dormant
Skruf Snus AB	Sweden	Manufacture, marketing, sales of tobacco products in Sweden
Société Centrafricaine de Cigarettes SA ⁽ⁱ⁾	Central African Republic	Manufacture and distribution of cigarettes in Central African Republic
Société Centrafricaine de Distribution Sarl ⁽ⁱ⁾	Central African Republic	Dormant
Société du Mont Nimba Sarl ⁽ⁱ⁾	Guinee Conakry	Dormant
Société Nationale d'Exploitation Industrielle des Tabacs et Allumettes SAS (SEITA)	France	Manufacture and sale of tobacco products in France, and export of tobacco products
Société pour le Développement du Tabac en Afrique SAS	France	Purchasing company
System Designed to Africa Sarl	Morocco	Distribution of tobacco products
Tabacalera Brands Inc	United States of America	Trademark owner
Tabacalera Brands SLU	Spain	Holding investments in subsidiary companies
Tabacalera de Garcia Limited	Bermuda	Holding investments in subsidiary companies
Tabacalera de Garcia SAS	France	Manufacture of cigars in the Dominican Republic
Tabacalera SLU	Spain	Holding investments in subsidiary companies
Tabacalera USA Inc	United States of America	Holding investments in subsidiary companies
Tahiti Tabacs SASU	France, Papeete (Tahiti)	Distribution of tobacco products in Denmark and Greenland
Tobacco Products Fulfillment, Inc.	United States of America	Fulfilment services
Tobaccoor SAS ^(v)	France	Holding investments in subsidiary companies
Tobačna 3DVA, trgovsko podjetje, d.o.o.	Slovenia	Retail of products in Slovenia
Tobačna Grosist d.o.o.	Slovenia	Marketing and distribution in Slovenia
Tobačna Ljubljana d.o.o. ^(v)	Slovenia	Sales and marketing tobacco products in Slovenia
Tobamark International SA	France	Trademark owner
Urex Inversiones SA	Spain	Holding investments in subsidiary companies
Van Nelle Canada Limited ^(vii)	Canada	Import and distribution of tobacco and tobacco related products in Canada
Van Nelle Tabak Nederland B.V. ^(x)	The Netherlands	Manufacture and sale of tobacco products in the Netherlands
Van Nelle Tobacco International Holdings B.V.	The Netherlands	Sale of tobacco and tobacco related products
West Park Tobacco Inc.	United States of America	Purchase company for USA tobaccos

RELATED UNDERTAKINGS

CONTINUED

SUBSIDIARIES: INCORPORATED OVERSEAS, PARTLY OWNED CONTINUED

Name	Country of incorporation	Principal activity	Percentage owned
Be To Be Pharma, S.L	Spain	Distribution of pharmaceuticals	70.0
Caribbean Investment Corporation, SA ⁽ⁱ⁾	Switzerland	Dormant	50.0
CDM Tampa, LLC	United States of America	Retail	50.0
Comercial Iberoamericana SA ⁽ⁱ⁾	Spain	Wholesale and distribution of tobacco products	50.0
Compagnie Agricole et Industrielle des Tabacs Africains SAS	France	Management company	99.9
Compagnie Agricole et Industrielle des Tabacs de Cote D'Ivoire SA, IL ⁽ⁱ⁾	Cote D'Ivoire	In liquidation	74.6
Compagnie Réunionnais des Tabacs SAS	France, St Pierre (La Reunion Island)	Manufacture of cigarettes	98.6
Compañía de Distribución Integral de Publicaciones Logista SLU ^(iv)	Spain	Distribution of published materials and other products	70.0
Compañía de Distribución Integral Logista Holdings, S.A. ⁽ⁱⁱⁱ⁾	Spain	Holding investments in subsidiary companies	70.0
Compañía de Distribución Integral Logista Polska, sp. Z o.o. (SL)	Poland	Distribution of tobacco products in Poland	70.0
Compañía de Distribución Integral Logista S.A.U.	Spain	Distribution of tobacco products in Spain	70.0
Coprova SAS ⁽ⁱ⁾	France	Distribution of Cuban cigars in the Caribbean	50.0
Cuba Cigar, S.L. ⁽ⁱ⁾	Spain	Distribution of Cuban cigars in the Canary Islands	50.0
Cubacigar (Benelux) N.V. ⁽ⁱ⁾	Belgium	Distribution of cigars in Belgium	50.0
Cyberpoint, S.L.U.	Spain	Distribution of POS software	70.0
Dalso, S.R.L. ⁽ⁱ⁾	Dominican Republic	Distribution of Cuban cigars in Republic Dominican	50.0
Distribérica SA	Spain	Holding investments in subsidiary companies	70.0
Distribución de Publicaciones Siglo XXI, Guadalajara	Spain	Distribution of published materials and other products in Spain	56.0
Distribuidora de Ediciones SADE, SAU	Spain	Distribution of published materials and other products in Spain	70.0
Distribuidora de las Rias SA	Spain	Distribution of published materials and other products in Spain	70.0
Distribuidora del Este S.A.U.	Spain	Distribution of published materials and other products in Spain	70.0
Distribuidora del Noroeste SL	Spain	Distribution of published materials and other products in Spain	70.0
Dronas 2002, SLU	Spain	Industrial parcel and express delivery service	70.0
Empor – Importação e exportação, SA ⁽ⁱ⁾	Portugal	Distribution of tobacco products in Portugal	50.0
Gauloises (Pty) Limited IL	South Africa	In liquidation	50.0
Habanos Nordic AB ⁽ⁱ⁾	Sweden	Distribution of Cuban cigars in Scandinavia	50.0
Imperial Tobacco Production Ukraine ⁽ⁱ⁾	Ukraine	Manufacture of tobacco products in Ukraine	99.9
Imperial Tobacco TKS a.d ⁽ⁱ⁾	Macedonia	Manufacture, marketing and distribution of tobacco products in Macedonia	99.1
Imperial Tobacco TKS a.d. – Dege Kosove	Kosovo	Manufacture, marketing and distribution of tobacco products in Kosovo	99.1
Imprimerie Industrielle Ivoirienne SA ⁽ⁱ⁾	Cote D'Ivoire	Printing company	72.8
Infifon APS ⁽ⁱ⁾	Denmark	Holding investments in subsidiary companies	50.0
Infifon Hong Kong Limited ⁽ⁱ⁾	China	Distribution of Cuban cigars in China	50.0
Infifon I, BV ⁽ⁱ⁾	The Netherlands	Holding investments in subsidiary companies	50.0
Infifon II NV ⁽ⁱ⁾	Netherlands Antilles	Distribution of Cuban cigars in Russia	50.0
ITB Corporation y Cia., S.R.C.	Spain	Trademark owner	86.7
La Mancha 2000, S.A., Sociedad Unipersonal	Spain	Logistics services	70.0
Lao Tobacco Limited ⁽ⁱ⁾	Laos	Manufacture and distribution of cigarettes in Laos	53.0
Logesta Deutschland GmbH, Sociedad Unipersonal	Germany	Long haul transportation in Germany	70.0
Logesta France SARL	France	Long haul transportation in France	70.0
Logesta Gestión de Transporte SAU	Spain	Long haul transportation services in Spain	70.0
Logesta Italia, S.R.L., Sociedad Unipersonal	Italy	Long haul transportation in Italy	70.0
Logesta Lusa LDA	Portugal	Long haul transportation in Portugal	70.0
Logesta Maroc SA IL	Morocco	In liquidation	89.8
Logesta Polska Sp Zoo	Poland	Long haul transportation in Poland	70.0
Logista France Holding SA	France	Holding investments in subsidiary companies	70.0
Logista France SAS	France	Holding investments in subsidiary companies	70.0
Logista Italia Spa	Italy	Long haul transportation in Italy	70.0
Logista Pharma SA	Spain	Distribution of pharmaceuticals	70.0
Logista Promotion et Transport SAS	France	Marketing and distribution of tobacco products in France	70.0
Logista, Transportes, Transitários e Pharma, Lda., Sociedad Unipersonal	Portugal	Industrial parcel delivery and pharmaceutical logistics in Portugal	70.0
Logista-Dis SAU	Spain	Sale of tobacco products in Spain	70.0

SUBSIDIARIES: INCORPORATED OVERSEAS, PARTLY OWNED

Name	Country of incorporation	Principal activity	Percentage owned
MABUCIG (Manufacture Burkinabe de Cigarette)	Burkina Faso	Manufacture of cigarettes in Burkina Faso	72.7
Macotab SAS (Manufacture Corse des Tabacs)	France, Bastia	Manufacture and sales of cigarettes	99.9
Manufacture de Cigarettes du Tchad SA	Tchad	Manufacture and distribution of cigarettes in Chad	95.0
Midsid – Sociedade Portuguesa de Distribuição, S.A., Sociedad Unipersonal	Portugal	Wholesale of tobacco and other products	70.0
MTOA SA ⁽ⁱ⁾	Senegal	Manufacture and sales of cigarettes in Senegal	97.3
NITAF Limited, IL ⁽ⁱ⁾	Nigeria	In liquidation	50.0
Promotora Vascongada de Distribuciones SA	Spain	Distribution of published materials and other products in Biscay and Santander	70.0
Publicaciones y Libros SA	Spain	Publishing company	70.0
Puro Tabaco SA ⁽ⁱ⁾	Argentina	Distribution of Cuban cigars in Argentina and Chile	50.0
Reemtsma Kyrgyzstan OJSC ⁽ⁱ⁾	Kyrgyzstan	Manufacture and sale of tobacco products in Kyrgyzstan	98.6
S3T Pte Ltd ⁽ⁱ⁾	Singapore	Holding investments in subsidiary companies	51.0
SACIMEM SA ⁽ⁱ⁾	Madagascar	Manufacture of cigarettes in Madagascar	65.4
SITAB Industries SA ⁽ⁱ⁾	Cote D'Ivoire	Manufacture of cigarettes in Cote D'Ivoire	80.5
SITAR Holding SAS	France (La Reunion Island)	Holding investments in subsidiary companies	98.6
Société Africaine d'Impression Industrielle SA ⁽ⁱ⁾	Senegal	Manufacture and distribution of cigarettes in Senegal	99.8
Société Allumettiere Française SAS	France	Manufacture and distribution of cigarettes	70.0
Société de Distribution Sénégalaise SA ⁽ⁱ⁾	Senegal	In liquidation	97.5
Société des Cigarettes Gabonaises SA ⁽ⁱ⁾	Gabon	In liquidation	87.8
Société Industrielle et Agricole du Tabac Tropical SA ⁽ⁱ⁾	Congo	Manufacture and distribution of cigarettes in Congo	89.7
Société Ivoirienne des Tabacs SA ⁽ⁱ⁾⁽ⁱⁱⁱ⁾	Cote D'Ivoire	Manufacture and distribution of cigarettes in Ivory Coast	74.1
Société Marocaine des Tabacs SA	Morocco	Manufacture and distribution of cigarettes in Morocco	99.9
SOCTAM SA ⁽ⁱ⁾	Madagascar	Manufacture and distribution of cigarettes in Mali	50.5
Supergroup SAS	France	Wholesale of tobacco products	70.0
T2 Gran Canaria SA	Spain	Pharmaceutical products logistics in Canary Islands	70.0
Top Cigars Corporation LLC ⁽ⁱ⁾	Russia	Distributor of Habanos in Russia	50.0
Universal Brands, S.A.	Spain	Trademark owner	86.7
Xinet SA ⁽ⁱ⁾	Uruguay	Distribution of Cuban cigars in Uruguay	50.0

ASSOCIATES: REGISTERED IN ENGLAND AND WALES

Name	Principal activity	Percentage owned
C H (Downton) Limited ^(ix)	Dormant	25.0
F J (Downton) Limited	Dormant	25.0
Hunters & Frankau Limited	Dormant	25.0
Incentive Marketing Services (UK) Limited	Dormant	25.0
Jacon Financial Services Limited ^(ix)	Dormant	25.0
Joseph Samuel & Son Limited	Dormant	25.0
Knight Brothers Cigar Shippers Limited	Dormant	25.0
Lancha House Limited	Dormant	25.0
Melbourne Hart & Company Limited	Dormant	25.0
Melbourne Hart Holdings Limited ^(ix)	Dormant	25.0
Morris & Morris Limited	Dormant	25.0
Tabaco Torcido Traders Limited	Dormant	25.0
The English Import Company Limited	Dormant	25.0
Tropic Tobacco Company Limited	Dormant	25.0

RELATED UNDERTAKINGS

CONTINUED

ASSOCIATES: INCORPORATED OVERSEAS

Name	Country of incorporation	Principal activity	Percentage owned
5th Avenue Products Trading GmbH ⁽ⁱ⁾ ^(iv)	Germany	Distribution of Cuban cigars in Germany	27.5
Avanza Libros S.L.U., Sociedad Unipersonal, I.L.	Spain	In liquidation	35.0
Azur Finances SA	Cameroon	Holding investments in subsidiary companies	20.0
Caribbean Cigars Corporation NV ⁽ⁱ⁾	Curacao	Distribution of Cuban cigars in the Caribbean	25.0
Compañía Española de Tabaco en Rama SA (Cetarsa) ⁽ⁱ⁾	Spain	Production and sale of raw tobacco	20.8
Diadema Spa ⁽ⁱ⁾	Italy	Distribution of Cuban cigars in Italy	30.0
Distribuidora de Publicaciones del Sur, S.A.	Spain	Distribution of published materials and other products	35.0
Distribuidora Valenciana de Ediciones S.A.	Spain	Distribution of published materials and other products in Valencia	35.0
Entreprises des Tabacs en Guinée ⁽ⁱ⁾	Guinée Conakry	Dormant	34.0
Havana House Cuban Products Specialist Limited ⁽ⁱ⁾	New Zealand	Distribution of Cuban cigars in New Zealand	25.0
Havana House Limited ⁽ⁱ⁾	Canada	Distribution of Cuban cigars in Canada	25.0
Importadora y Exportadora de Puros y Tabacos SA DE CV (IEPT) ⁽ⁱ⁾	Mexico	Marketing and distribution of Cuban cigars in Mexico	25.0
Intertabak AG ⁽ⁱ⁾	Switzerland	Distribution of Cuban cigars in Switzerland and Liechtenstein	25.0
Lippoe Tobacco Corporation International NV	Netherlands Antilles	Distributor of Cuban leaf	27.5
Logista Libros SL	Spain	Distribution of books	35.0
Manufacture Mauritanienne des Tabacs	Mauritanie	Manufacture and import of tobacco products	34.6
Maori Tabacs, S.A. ⁽ⁱ⁾	Andorra	Distribution of Cuban cigars in Andorra	25.0
Marfany I Mas Industria Tobacco SA (Mitsa) (MARFANY MAS INDUSTRIA TABAQUERA, S.A.)	Andorra	Manufacture of Cuban cigars in Andorra	24.0
New Mentality Limited ⁽ⁱ⁾	British Virgin Islands	Dormant	25.0
Pacific Holding (Thailand) Company Limited ⁽ⁱ⁾ ^(vi)	Thailand	Holding investments in subsidiary companies	25.0
Phoenicia Beirut SAL ⁽ⁱ⁾	Lebanon	Retail in Lebanon	25.0
Phoenicia TAA Cyprus Ltd ⁽ⁱ⁾	Cyprus	Distribution of Cuban cigars in the Middle East and Africa	25.0
Pit Stop Limited ⁽ⁱ⁾	British Virgin Islands	Dormant	25.0
Promotion et Distribution a Madagascar ⁽ⁱ⁾	Madagascar	Distribution of cigarettes in Madagascar	33.4
SITABAC S.A.	Cameroon	Manufacture and distribution of tobacco products in Cameroon	34.5
Société Internationale des Tabacs Malgaches ⁽ⁱ⁾	Madagascar	Leaf processing	47.9
Société Nationale des Tabacs et Allumettes du Mali SA ⁽ⁱ⁾	Mali	Manufacture and distribution of cigarettes in Mali	28.0
Terzia SPA	Italy	Wholesale to tobacconists in Italy	47.6
The Pacific Cigar (Thailand) Co Limited ⁽ⁱ⁾ ^(vii)	Thailand	Distribution of Cuban cigars in Thailand	25.0
The Pacific Cigar Co. (Singapore) Pte Limited ⁽ⁱ⁾	Singapore Australia	Distribution of Cuban cigars in Singapore	25.0
The Pacific Cigar Company (Australia) Pty Limited ⁽ⁱ⁾	Australia	Distribution of Cuban cigars in Australia	25.0
The Pacific Cigar Company (Macau) Limited ⁽ⁱ⁾	Macau	Distribution of Cuban cigars in Macau	25.0
The Pacific Cigar Company (Malaysia) SDN BHD ⁽ⁱ⁾	Malaysia	Dormant	25.0
The Pacific Cigar Company (New Zealand) Limited ⁽ⁱ⁾	New Zealand	Distribution of Cuban cigars in New Zealand	25.0
The Pacific Cigar Company Limited ⁽ⁱ⁾	China	Distribution of Cuban cigars in Asia	25.0
The Pacific Cigar International Co Limited ⁽ⁱ⁾	Taiwan	Distribution of Cuban cigars in Asia	25.0

JOINT VENTURES: INCORPORATED OVERSEAS

Name	Country of incorporation	Principal activity	Percentage owned
Altabana SL ⁽ⁱ⁾	Spain	Holding investments in subsidiary companies involved in the marketing and sale of Cuban cigars	50.0
Corporación Habanos SA ⁽ⁱ⁾	Cuba	Export of cigars manufactured in Cuba	50.0
International Cubana de Tabaco SA ⁽ⁱ⁾	Cuba	Manufacture of cigarillos in Cuba	50.0
Intertab SA ⁽ⁱ⁾	Switzerland	Holding investments in subsidiary companies	50.0
NITAF Holding BV, IL ^(iv)	The Netherlands	In liquidation	50.0
Promotora de Cigarros SL ⁽ⁱ⁾	Spain	Sales and marketing of cigars manufactured in Cuba	50.0
West Tobacco Pte Ltd ⁽ⁱ⁾	Singapore	Dormant	50.0
Compañía de Distribución Integral Logista S.A.U. y GTECH Global Lottery, S.L.U., U.T.E.	Spain	Services and distribution	35.0

PARTNERSHIPS

The Group also owns the following partnerships:

Name	Country	Principal activity
Fabrica de Tabacos La Flor de Copan S de R.L. de CV	Honduras	Holding investments in subsidiary companies Principal place of business: Apartado Postal 209, Colonia Mejia-Garcia, Santa Rosa de Copán, Honduras
Imperial Tobacco (Efka) GmbH & Co. KG	Germany	Manufacture of tubs in Germany Principal place of business: Industriestrasse 6, Postfach 1257, D-78636 Trossingen, Germany
Imperial Tobacco Kazakhstan LLP ⁽ⁱ⁾	Kazakhstan	Marketing and distribution of tobacco products in Kazakhstan Principal place of business: 3rd Floor, Prime Business Park, 100/2 Furmanov Str, Medeuskiy District, Almaty, 050000, Kazakhstan
ITG Brands Holdpartner LP	United States of America	Marketing and sale of tobacco products in United States of America Principal place of business: 714 Green Valley Road, Greensboro, NC27408, United States of America

The subsidiaries listed were held throughout the year and the consolidated Group financial statements include all the subsidiary undertakings identified. All dormant UK entities have taken the exemption available to not have an audit of their financial statements.

Unless otherwise stated the entities are unlisted, have 1 type of ordinary share capital and a reporting period ending on 30 September each year.

- (i) December year end
- (ii) March year end
- (iii) Listed entity
- (iv) Holding of one type of ordinary share only (where more than one type of share is authorised / in issue). Only applicable to partly owned entities – percentage ownership is shown in the tables above.
- (v) Holding of two types of ordinary share (where more than one type of ordinary share is authorised / in issue). Only applicable to 100% owned subsidiaries.
- (vi) Holding of preference shares only
- (vii) Holding of ordinary and preference shares
- (viii) Holding of ordinary and redeemable shares
- (ix) Holding of ordinary and deferred shares
- (x) Holding of two types of ordinary share and redeemable shares

The percentage of issued share capital held by the immediate parent and the effective voting rights of the Group are the same except for Imperial Tobacco Italia Srl where the entire share capital, and therefore 100 per cent of the voting rights, are held by a number of Group companies, and Compañía de Distribución Integral Logista SAU, Logista France SAS, and Logista Italia SpA are 100 per cent owned subsidiaries of Compañía de Distribución Integral Logista Holdings SA, which is itself 70 per cent owned by Altadis SAU.

SHAREHOLDER INFORMATION

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Financial Calendar and Dividends

Half-year results are expected to be announced in May 2017 and the full year's results in November 2017.

The Annual General Meeting of the Company will be held on Wednesday 1 February 2017 at the Bristol Marriott Hotel City Centre. The Notice of Meeting and explanatory notes about the resolutions to be proposed are set out in the circular enclosed with this report.

Dividends are generally paid at the end of March, June, September and December. Payment of the 2016 final dividend, if approved, will be on 31 March 2017 to shareholders on the Register of Members at the close of business on 17 February 2017. The associated ex dividend date will be 16 February 2017.

Shareholders who do not currently mandate their dividends and who wish to do so should complete a mandate instruction form obtainable from our Registrars, Equiniti Limited, at the address shown.

Share Dealing Service

Our Registrars offer Shareview Dealing, a service which allows you to buy or sell Imperial Brands PLC ordinary shares if you are a UK resident. You can deal on the internet or by phone. Log on to www.shareview.co.uk/dealing or call them on 03456 037 037 between 8.00am and 4.30pm Monday to Friday for more information about this service. If you wish to sell your Imperial Brands PLC ordinary shares, you will need your shareholder reference number which you can find on your share certificate.

Individual Savings Account

Investors in Imperial Brands PLC ordinary shares may take advantage of a low cost Individual Savings Account (ISA) and Investment Account where they can hold their Imperial Brands PLC ordinary shares electronically. The ISA and Investment Account are operated by Equiniti Financial Services Limited. Commission starts from £12.50 and £1.75 respectively for the sale and purchase of shares.

For a brochure or to apply for an ISA or Investment Account go online to www.shareview.co.uk/dealing or call Equiniti on 0345 300 0430.

Dividend Reinvestment Plan

Imperial Brands PLC has set up a dividend reinvestment plan (DRIP) to enable shareholders to use their cash dividend to buy further Imperial Brands PLC ordinary shares in the market. Further information can be obtained from Equiniti on 0371 384 2268 (+44 (0)121 415 7173) or online at www.shareview.co.uk.

American Depositary Receipt Facility

Imperial Brands PLC ordinary shares are traded on the OTCQX International Premier platform in the form of American Depositary Shares (ADSs) using the symbol 'IMBBY'. The ADS facility is administered by Citibank, N.A. and enquiries should be directed to them at the address shown.

Website

Information on Imperial Brands PLC is available on our website: www.imperialbrandspc.com

Equiniti also offers a range of shareholder information online. You can access information on your holdings, indicative share prices and dividend details and find practical help on transferring shares or updating your details at www.shareview.co.uk



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